Global oil and gas tax guide

2018

Building a better working world

Preface

The *Global oil and gas tax guide* summarizes the oil and gas corporate tax regimes in 86 countries and also provides a directory of EY oil and gas tax and legal contacts. The content is based on information current to 1 January 2018, unless otherwise indicated in the text of the chapter.

Tax information

This publication should not be regarded as offering a complete explanation of the tax matters referred to and is subject to changes in the law and other applicable rules. Local publications of a more detailed nature are frequently available, and readers are advised to consult their local EY professionals for more information.

EY Global oil and gas tax guide is part of a suite of tax guides, including the *Worldwide Corporate Tax Guide*, the *Worldwide Personal Tax Guide*, the *Worldwide VAT, GST and Sales Tax Guide*, the *International Estate and Inheritance Tax Guide*, the *Transfer Pricing Global Reference Guide*, the *Worldwide R&D Incentives Reference Guide* and the *Worldwide Cloud Computing Tax Guide*.

Each represents thousands of hours of tax research. They are available free online along with timely *Global Tax Alerts* and other great publications on ey.com or in our EY Global Tax Guides app for tablets. Further information concerning EY oil and gas services may be found at **ey.com/oilandgas**.

EY Law

EY Law has the necessary capabilities to assist companies throughout the industry value chain based on a cross-discipline approach and the culture of client service.

We advise on all legal and regulatory, risk management, enforcement and compliance issues across multiple jurisdictions.

Directory

Office addresses, telephone numbers and fax numbers, as well as names and email addresses of oil and gas tax contacts, are provided for the EY member firms in each country. The listing for each tax contact includes a direct-dial office telephone number, if available.

Oil and gas law contacts for the EY member firms are also included at the back of this publication.

The international telephone country code is listed in each country heading. Telephone and fax numbers are presented with the city or area code and without the domestic prefix (1, 9 or 0) sometimes used within a country.

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Concession

Under a concession, an oil and gas company is granted exclusive rights to exploration and production of the concession area and owns all oil and gas production. Under concession an oil and gas company typically pays royalties and corporate income tax. Other payments to the government may be applicable, such as bonuses, rentals, resource taxes, special petroleum or windfall profit taxes, export duties, state participation and others.

Production sharing contract (PSC)/production sharing agreement (PSA)

Under a PSC/PSA, a national oil company (NOC) or a host government enters into a contract directly with an oil and gas company. A company finances and carries out all E&P operations and receives a certain amount of oil or gas for the recovery of its costs along with a share of the profits. Sometimes PSC/PSA requires other payments to the host government, such as royalties, corporate income tax, windfall profit taxes, etc.

Service contracts

Under a service or risk service contract, an oil and gas company finances and carries out petroleum projects and receives a fee for this service, which can be in cash or in kind. The fees typically permit the recovery of all or part of the oil and gas company's costs and some type of profit component.

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Depending on the date on which the petroleum contract was signed, the Algerian fiscal regime applicable to the oil and gas upstream industry is governed by one of the following:

- Law No. 86-14 dated 19 August 1986
- Law No. 05-07 dated 28 April 2005 (as amended by Ordinance No. 06-10 dated 19 July 2006 and Law No. 13-01 dated 20 February 2013)

These laws govern production sharing contracts (PSCs) or other similar contracts concluded between the Algerian authorities and the contractor.

The main taxes applicable in this sector are the following:

- Under Law No. 86-14:
  - Royalties
  - Income tax
  - Tax on extraordinary profits (TEP) or windfall tax
- Under Law No. 05-07:
  - Royalties
  - Petroleum income tax (PIT)
  - Additional profits tax (APT)
  - Surface tax

Legal regime

- Law No. 86-14 governs the appraisal, exploration, exploitation and transportation of hydrocarbons, as well as the construction and installation of sites enabling these activities.
- Law No. 05-07 is broader in application, as it also provides for the refining of hydrocarbons; the commercialization, storage and distribution of petroleum products; and the construction and installation sites enabling these activities.

The latter also provides for the transfer of some rights and duties from the national oil company (NOC), Sonatrach, back to the Algerian state through the newly created national agency for hydrocarbons (ALNAFT). For instance, ALNAFT is the sole holder of the permit for the exploration and exploitation of hydrocarbons.

ALNAFT may enter into contracts with third parties to perform exploration or exploitation activities.

However, the NOC maintains a key role, as invitations to tender for the award of an exploration and exploitation contract must contain a clause that awards the NOC a 51% interest in the contract. Law No. 05-07 as amended by Law No. 13-01 provides that oil and gas pipeline transport activities are performed by the NOC or its subsidiaries.

Under Law No. 05-07, the period combining exploration (7 years) and exploitation (25 years) is 32 years and follows a two-period approach. The exploitation period has been extended by five years for natural gas deposits, according to Law No. 13-01.

Exploration period

The exploration period lasts a maximum of seven years (consisting of an initial exploration phase of three years, followed by two phases of two years each). The exploration area is reduced by 30% at the end of the initial exploration phase and by another 30% after the second exploration phase.

Once a field has been discovered, a declaration of commerciality (déclaration de commercialité) and a draft of the development plan must be sent to ALNAFT for approval. Expected costs of development and a description of the exploitation area must be attached to the project development plan, and a budget must be delivered annually. The draft of the development plan must specify the agreed location as a basis for the royalties' calculation.

If the development plan includes the use of water, the contracting party will have to pay for the water at a rate of DZD80 per cubic meter.

Exploitation period

The exploitation period lasts a maximum of 32 years less the duration of the exploration period (7 years). For dry gas fields, there is an additional five-year exploitation period.

Specific periods apply for unconventional oil and gas. For the exploration and exploitation of liquid unconventional oil and gas, the exploration period is fixed at 11 years from the date of commencement of the agreement and is followed by an exploitation period of:

- 30 years in the case of exploitation of liquid unconventional oil and gas
- 40 years in the case of exploitation of gaseous unconventional oil and gas (i.e., up to 51 years as compared to 32 years for conventional oil and gas)

The production period may be extended for an initial period of five years upon request by the contracting party. This additional period may be followed by a second optional extension of five years upon request by the contracting party and after agreement by ALNAFT.

For unconventional oil and gas, the contractor may, within the scope of the performance of the pilot project, benefit from an anticipated production authorization of up to four years. This anticipated production is subject to the tax regime provided for by law.

B. Fiscal regime

Main taxes under the former regime (Law No. 86-14) that remain applicable for certain contracts

Royalties

Royalties are due on the gross income and are paid by the NOC at a rate of 20%. The royalty rate can be reduced to 16.25% for Zone A and 12.5% for Zone B (different zones of the Algerian territory). The Ministry of Finance can reduce the royalty rate further to a limit of 10%.

Income tax

Income tax at the rate of 38% applies to the profit made by a foreign partner and is paid by the NOC on its behalf.

In practice, the income tax is included in the profit oil received by the NOC.

This profit is calculated by subtracting the royalties paid, transportation costs, amortization costs and exploitation costs from the gross income.

TEP or windfall tax

TEP was introduced by Ordinance No. 06-10 dated 29 July 2006 and applies only to contracts signed under Law No. 86-14.

TEP applies to the output share of foreign partners of the NOC when the arithmetic average price of oil exceeds US$30 per barrel and applies at rates ranging from 5% to 50%.

The decree provides for different rates depending on the type of contract signed with the foreign partner, including:

- Contracts in which there is production sharing, without distinction between hydrocarbons for reimbursement and hydrocarbons as a profit for the foreign partner and without a "price cap" mechanism
- Contracts in which there is production sharing, with a clause containing a specific formula for calculating the compensation of the foreign partner without a "price cap" mechanism
- Contracts in which there is production sharing, with a clause containing a specific formula for calculating the compensation of the foreign partner with a "price cap" mechanism

Main taxes applicable under Law No. 05-07, as amended

Surface fee

The surface fee is an annual tax that is not deductible. The amount of this tax payable depends on the territorial zone in which the operations are carried out and the surface perimeter.

The rates of the surface fee per square kilometer (in Algerian dinars) are given in the table below.

	Exploration period				
	Years 1–3 (inclusive)	Years 4–5	Years 6–7	Retention period and exceptional period	Production period
Area A	4,000	6,000	8,000	400,000	16,000
Area B	4,800	8,000	12,000	560,000	24,000
Area C	6,000	10,000	14,000	720,000	28,000
Area D	8,000	12,000	16,000	800,000	32,000

Zones A, B, C and D correspond to areas in the territory of Algeria.

Please note that the surface fee is indexed annually to the US dollar.

According to Law No. 13-01, the rates for Area A are applied for the site perimeters of unconventional oil and gas exploration and production.

Royalties

Royalties are calculated on the amount of hydrocarbons extracted from each perimeter of exploitation multiplied by the average monthly fixed price, and paid monthly to ALNAFT.

Royalties are established on the basis of the quantity of hydrocarbon production at the agreed spot (point de measure), the location at which the measurement of the hydrocarbons production will take place (Art 5 and 26 L. 2005).

The fixed price is calculated by reference to published indexes, depending on the nature of the hydrocarbons.

The rate of royalties is determined under the terms of each contract. Nevertheless, the Law has fixed a minimum rate for each area of production:

Production (barrels of oil equivalent, BOE) | Area	A	B	C	D
0–20,000 BOE/day	5.5%	8.0%	11.0%	12.5%
20,001–50,000 BOE/day	10.5%	13.0%	16.0%	20.0%
50,001–100,000 BOE/day	15.5%	18.0%	20.0%	23.0%
> 100,000 BOE/day	12.0%	14.5%	17.0%	20.0%

The royalty is deductible for APT purposes.

According to Law No. 13-01, a reduced rate of 5% applies for unconventional oil and gas reservoirs, site perimeters located in underexplored areas, and those that have complex geography and/or that lack infrastructure (the list of which is set by regulation).

PIT

The taxable basis corresponds to the value of the production of each perimeter of exploitation during the year, less deductible expenses.

PIT is deductible for APT purposes and must be paid monthly by the operator.

The following taxes and expenses are deductible:

- Royalties
- Annual investments for exploration and development
- Reserves for abandonment or restoration costs
- Training costs

According to the changes provided by Law No. 13-01, a distinction must be made for contracts entered into for an exploitation period before 20 February 2013.

The tax rate is calculated by taking into consideration the volume of production since production started (accrued production) (PV)and is determined as follows:

Accrued production in 10 DZD 10^9	First accrued production point (S1)	70
	Second accrued production point (S2)	385
PIT rate	First level	30%
	Second level	70%
	Level when PV is between S1 and S2	40 ÷ (S2-S1) × (PV-S1) + 30

Example:

If the accrued production since the beginning of exploitation (PV) is 200 * DZD 10^9, the PIT rate would be:

40 ÷ (385-70) × (200-70) + 30 = 40 ÷ 315 × 130 + 30 = 46.5%

Law No. 13-01 amends the method for calculating the rate of the PIT, which will now range from 20% to 70% on the basis of the profitability of the project and which will be updated annually (coefficient R1 and R2 according to the scope under consideration), instead of the previous thresholds (S1 and S2) fixing the application of the rate at 30% or 70% depending solely on the cumulative value of production (VP) or turnover.

For a given calendar year, the coefficient (R1) is the ratio of accumulated gross profit (updated at a rate of 10%), from the year of entry into force of the contract up to the year preceding the year determining the rate of PIT, to cumulative investment expenses (updated at the rate of 10%), since the year of entry into force of the contract until the year preceding the determination of the rate of PIT.

For a given calendar year, the coefficient (R2) is the ratio of accumulated gross profit (updated at the rate of 20%), from the year of entry into force of the contract until the year preceding the year in determining the rate of PIT, to cumulative investment expenses (updated at the rate of 20%), since the year of entry into force of the contract until the year preceding the year determining the rate of PIT.

The following table is applied to the values of R1 and R2:

		Case 1	Case 2	Case 3
PIT rate	R1 ≤ 1	20%	30%	20%
	R1 > 1 and R2 < 1	20% + 50% x R2	30% + 40% x R2	20% + 50% x R2
	R2 ≥ 1	70%	70%	70%

Case 1 includes all exploitation perimeters except the perimeters included in Case 3 where the daily production is less than 50,000 BOE.

Case 2 includes all exploitation perimeters excluding the perimeters included in Case 3 where the daily production is more than 50,000 BOE.

Case 3 includes small deposits and underexplored perimeters that have complex geology and/or that lack infrastructure.

For contracts mentioned above, "uplift" rules apply to the annual research and development investments as follows:

Zones	Uplift rate	Depreciation rate
A and B	15%	20% (5 years)
C and D	20%	12.5% (8 years)

Additional profits tax

This tax is due by all entities involved in an exploration or production contract, based on the annual profits after PIT.

The following expenses are deductible for the calculation of the taxable basis:

- Royalties
- PIT
- Depreciation
- Reserves for abandonment or restoration costs

There are two applicable rates:

- 30%
- 15% (for profits that are reinvested)

This tax must be paid by the day that the annual income tax return is filed.

For calculation of this tax, legal persons who participate in research and/or exploitation agreements can consolidate their activities in Algeria under some conditions.

According to Law No. 13-01, for unconventional oil and gas, small deposits and underexplored areas that have complex geology and/or that lack infrastructure, each company that is party to the agreement is subject to a reduced rate set at 19% (instead of 30%), under the terms and conditions in force at the date of payment and pursuant to the depreciation rates provided for in the appendices to this Law. The said rate is applicable so long as the coefficient P2 is less than 1. If it is equal to or greater than 1, the applicable rate is 80%.

As a reminder, the Additional Tax on Income is still applicable at the reduced rate of 15% in the case of investments — notably in gas pipeline transport and in upstream petroleum activities (as Article 88 of Law was not amended).

Ancillary taxes

Gas flaring tax

Gas flaring is forbidden; however, ALNAFT can give exceptional authorization for a period not exceeding 90 days. The contractor is liable for a tax of DZD 8,000 per thousand normal cubic meters (nm^3).

This tax is not deductible for tax purposes.

Unconventional oil and gas

Law No. 13-01 has provided a legislative framework for unconventional oil and gas. Unconventional oil and gas that exist and are produced from a reservoir or geological formation that presents at least one of the following characteristics or conditions:

- Compact reservoirs whose average matrix permeabilities are equal to or less than 0.1 millidarcy and/or that can be produced by using only horizontal wells and tiered fracking
- Impermeable formations such as, clay with low permeability, or schist geological formations that can only be exploited using horizontal wells and tiered fracking
- Geological formations containing oil and gas that present viscosities higher than 1,000 centipoises or densities lower than 15° API (American Petroleum Institute)
- High-pressure and high-temperature reservoirs

There is little environmental specificity within the framework of the production of unconventional oil and gas, but the following apply:

- Authorization or concession granted by the administration in charge of water resources in coordination with ALNAFT for the use of abstracted water
- Rational use of water with no further specifications
- A general obligation for all exploration and exploitation activities to comply with the laws and rules in force for the protection of the environment and the use of chemical products, notably for operations concerning unconventional oil and gas

Any contracting party to an exploration and production agreement entered into with ALNAFT may benefit, within the scope of an amendment to the agreement, from the conditions applied to unconventional oil and gas in the event that the hydrocarbons to be exploited are primarily characterized by one of the situations provided for in the definition of the term "unconventional oil and gas."

The carrying out of the activities relating to the exploitation of clay and/or shale or impermeable geological formations with very low permeability (shale gas and shale oil) using the techniques of hydraulic fracturing are subject to approval by the Council of Ministers.

Other tax or legal requirements are as mentioned above.

C. Capital allowances

Under Law No. 05-07, the depreciation rates of investments in exploration and development are subject to an increased uplift mechanism, depending on the nature of the works and the zone in which the works were performed:

	Research and development	
Zone	A and B	C and D
Rate of depreciation	20%	12.5%
Rate of uplift	15%	20%

D. Incentives

As a general rule, operations conducted under the former law regime (1986) and the 2005 regime are exempt from:

- Value-added tax (VAT)
- Customs duties
- Social contributions (foreign employees of petroleum companies are not subject to social security contributions in Algeria if they remain subject to social security protection in their home country)

An exemption from the tax on professional activity applies to contracts signed under Law No. 86-14.

Moreover, as mentioned in the sections above, several incentives are provided by Algerian law in order to enhance the exploration and production of unconventional hydrocarbons.

E. Withholding taxes

Withholding taxes (WHT) are not dealt with under the Hydrocarbons Law.

F. Financing considerations

There are no specific issues or limitations concerning the financing of hydrocarbon activities in Algeria.

G. Transactions

The transfer of an interest in a PSC governed by Law No. 05-07 is subject to a 1% tax on the value of the transaction. This tax is also applicable to the transfer of a PSC signed under Law No. 86-14.

H. Indirect taxes

Facilities and services that are directly allocated to research and exploitation activities are exempt from VAT and customs duties.

I. Other

Foreign exchange controls

If exploration expenses were paid with imported convertible currency, nonresidents are authorized to:

- Keep abroad the product of hydrocarbon exportations acquired according to the contract
- Freely use the proceeds from sales of hydrocarbons on the national market, acquired according to the contract, and transfer them abroad

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - □ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ■ **Service contract**

A. At a glance

Fiscal regime

There are three types of contracts, each with different tax regimes:

1. Production sharing agreement (PSA) — the most common form of arrangement
2. Partnership — applicable only to certain partnerships set up in the 1960s and 1970s, such as Block 0 and FS/FST
3. Risk service contract (RSC)

Taxes applicable to all oil tax regimes:

- Petroleum income tax (PIT) — 50% (PSA) and 65.75% (partnership and RSC)
- Surface fee (SF) — US$300 per square kilometer (km^2)
- Training tax contribution (TTC) — US$0.15 per barrel/US$100,000 to US$300,000[1]

1 *Annual contribution of US$100,000 to US$300,000 only applicable before production phase.*

Taxes applicable exclusively to partnerships and RSC:

- Petroleum production tax (PPT) — 20%[2]
- Petroleum transaction tax (PTT) — 70%
- Investment incentives — U[3]

Legislation changes[4] enacted in 2012 envisage a tax reduction for Angolan national oil and gas companies.

Consumption tax rules for oil and gas companies.

B. Fiscal regime

The tax regime applies to all entities, whether Angolan or foreign, within the Angolan tax jurisdiction that perform exploration, development, production, storage, sale, exportation, processing and transportation of not only crude oil and natural gas but also naphtha, paraffin, sulfur, helium, carbon dioxide and saline substances from petroleum operations.

The current oil and gas taxation regime applies to concessions granted on or after 1 January 2005, as well as to profits or capital gains from assignment of an interest in an earlier concession.

A PSA is a contract between a contracting group and the state concessionaire under which the contracting group bears all expenditures for exploration and extraction of substances in the contract area, together with related losses and risks.

The state concessionaire is a distinct department of Sonangol (the Angolan national oil company (NOC)), through which the Government manages its oil and gas properties and its contractual relationships with other oil companies.

Profit oil, under a PSA, is the difference between the total oil produced and oil for cost recovery (cost oil). Cost oil is the share of oil produced that is allocated for recovery of exploration, development, production, and administration and service expenditures.

Profit oil is shared between the state concessionaire and its partners based on the accumulated production or on the contracting group rate of return (preferred method).

The computation of tax charges for each petroleum concession is carried out on a completely independent basis.

In a PSA, the assessment of taxable income is independent for each area covered by the PSA, except for the expenses provided for in Article 23, subparagraph 2 (b) of Law No. 13/04, dated 24 December 2004, to which the rules in the preceding paragraph apply (generally, exploration expenditure).

Common revenues and costs associated with distinct development areas and concessions are allocated proportionally based on the annual production.

For the purposes of assessing taxable income, crude oil is valued at the market price calculated on the free-on-board (FOB) price for an arm's-length sale to third parties.

Bonuses may be due from the contracting group to the state concessionaire in compliance with the Petroleum Activities Law and cannot be recovered or amortized. Furthermore, a price cap excess fee may also be payable under a PSA whenever the market price per oil barrel exceeds the price fixed by the Minister of Oil. In both cases, the amounts are ultimately due to the Angolan state.

A contracting group may also be requested to make contributions for social projects to improve community living conditions (such as hospitals, schools and social housing), which also cannot be recovered or amortized.

2 *May be reduced to 10%.*
3 *U: uplift on development expenditure under investment allowance.*
4 *Presidential Legal Decree No. 3/12, of 16 March 2012.*

Entities engaged in business activities in Angola and not subject to the oil and gas taxation regime are subject to industrial tax on business profits. This tax is not dealt with in this guide. Moreover, this guide does not cover the specific tax regimes that apply to mining activities or the incentives available under private investment law, such as exemptions from customs duties, industrial tax, dividends withholding tax (WHT) and property transfer tax. Since a special regime is in force for the liquefied natural gas (LNG) project, we also outline below the main features of the said regime.

Petroleum income tax

PIT is levied on the taxable income assessed in accordance with the tax law from any of the following activities:

- Exploration, development, production, storage, sale, exportation, processing and transportation of petroleum
- Wholesale trading of any other products resulting from the above operations
- Other activities of entities primarily engaged in carrying out the above operations, resulting from occasional or incidental activity, provided that such activities do not represent a business

PIT does not apply to the receipts of the state concessionaire, premiums, bonuses and the price cap excess fee received by the state concessionaire under the terms of the contracts and is computed on accounting net income adjusted in accordance with the tax law. Tax law provides detailed guidelines on taxable revenues, deductible costs and nondeductible costs.

PSAs

Under a PSA, tax-deductible costs should comply with the following general rules:

- Cost oil is limited to a maximum percentage of the total amount of oil produced in each development area, in accordance with the respective PSA (generally 50%, but may be increased up to 65% if development expenditures are not recovered within four or five years from the beginning of commercial production or from the year costs are incurred, whichever occurs later).
- Exploration expenditures are capitalized and are recognized up to the amount of cost oil (limited as above) not utilized in the recovery of direct production and development expenses as well as indirect administration and service expenses.
- Development expenditures are capitalized, and the amount is increased by the investment allowance (uplift) defined in the respective PSA and amortized at an annual rate of 25% up to the cost oil amount, from the year incurred or upon commencement of oil exportation, whichever occurs later.
- Production expenditures are expensed up to the cost oil amount.
- Administration and service expenditures are either capitalized and amortized (similar to development expenses) or immediately expensed up to the cost oil amount being allocated to exploration, development and production expenses.
- Inventory is allocated to exploration, development, production, and administration and service activities in proportion to its utilization or consumption within oil operations.
- Strategic spare parts are allocated to exploration, development, production, and administration and service expenses in accordance with the respective PSA.
- Costs incurred in assignment of a participating interest (the difference between acquisition price and recoverable costs plus the net value of remaining assets — goodwill) are considered development expenses (but do not benefit from uplift), provided such difference has been taxed at the level of the transferor.
- Should the cost oil amount not be enough to recover allowable expenses, the balance can be carried forward within the same concession.

Taxable income is fixed by an assessment committee on the basis of the tax return submitted. The committee validates the amounts reported and determines the taxable income. The taxpayer may challenge the amount determined by the committee.

If the company operates under a PSA, the tax rate is 50%; otherwise, the tax rate is 65.75%.

Partnerships and RSCs

For partnerships and RSCs, tax-deductible costs should comply with the following general rules:

- Costs incurred in exploration operations, drilling costs of development wells, costs incurred for production, transportation and storage facilities, as well as costs incurred with the assignment of a participating interest (the difference between the acquisition price and the capitalized costs plus the net value of remaining assets — goodwill, provided this difference has been taxed at the level of the transferor), are recognized at an annual rate of 16.666% as of the beginning of the year in which they are incurred, or the year in which oil is first commercially produced, whichever occurs later.
- Costs that are incurred before production are capitalized and recognized over a four-year period (25% per year) from the first year of production.
- If the costs exceed the revenues in a given year, the excess can be carried forward up to five years.

Petroleum production tax

PPT is computed on the quantity of crude oil and natural gas measured at the wellhead and on other substances, less the oil used in production as approved by the state concessionaire.

The tax rate is 20%. This rate may be reduced by up to 10% by the Government and upon petition by the state concessionaire in specific situations, such as oil exploration in marginal fields, offshore depths exceeding 750 meters or onshore areas that the Government has previously defined as difficult to reach. This tax is deductible for the computation of PIT.

PPT is not imposed under a PSA.

Petroleum transaction tax

PTT is computed on taxable income, which takes into account several adjustments in accordance with the tax law. The tax rate is 70%. This tax is deductible for the computation of PIT.

Deduction of a production allowance and an investment allowance is possible on the basis of the concession agreement. PPT, SF, TTC and financing costs are not deductible to compute the taxable basis.

PTT is not imposed under a PSA.

Surface fee

SF is computed on the concession area or on the development areas whenever provided for in the application agreement of Decree-Law No. 13/04.

The surcharge is equivalent to US$300 per km² and is due from partners of the state concessionaire. This surcharge is deductible for PIT purposes.

Training tax

This levy is imposed on oil and gas exploration companies as well as production companies, as follows:

- US$0.15 per barrel — for production companies as well as companies engaged in refinery and processing of petroleum
- US$100,000 a year — for companies owning a prospecting license
- US$300,000 a year — for companies engaged in exploration.

The levy is also imposed on service companies that contract with the above entities for more than one year.

The levy for service companies is computed on the gross revenue from any type of contract at the rate of 0.5%. If a clear distinction exists between goods and services, it may be possible to exempt the portion relating to the goods, and in some circumstances, it may also be possible to exempt part of the services for work entirely performed abroad.

The same 0.5% also applies to the revenue obtained by entities engaged in the storage, transport, distribution and trading of petroleum.

Angolan companies with capital more than 50% owned by Angolan nationals are not subject to this levy. Also excluded from this levy are:

- Foreign companies that supply materials, equipment and any other products
- Services providers and entities engaged in the construction of structures (or similar), which execute all or most of the work outside Angola
- Entities engaged in a business not strictly connected with the oil industry

Unconventional oil and gas

No special terms apply: there are no specific rules applicable to unconventional oil or unconventional gas.

C. Capital allowances

Investment allowances (uplift on development expenses) may be granted by the Government upon request made to the ministers of oil and finance. The amount and conditions are described in the concession agreement. Uplift may range between 30% and 40%, based on the profitability of the block.

Production allowances exist for certain blocks, which allow for the tax deduction of a fixed US dollar amount per barrel produced in all development areas in commercial production from a predefined date. This deduction is available up to the unused balance of cost oil.

D. Incentives

The Government may grant an exemption from oil industry-related taxes, a reduction of the tax rate or any other modifications to the applicable rules, whenever justified by economic conditions. This provision may also be extended to customs duties and other taxes.

In this regard, a law was enacted granting tax incentives to Angolan national oil and gas companies, i.e., all public companies owned by the state and/or Angolan public companies or privately owned companies wholly owned by Angolan nationals.

The incentives granted include the PIT reduction from 50% (PSA) and 65.75% (partnership and RSC) to the equivalent of the industrial tax standard rate, which is 30%.

Moreover, Angolan national oil and gas companies are exempt from the signature bonus and from making contributions to social projects that may be due under the respective PSA.

The PSA entered into between the Government and the oil company may override the general taxation regime and may set forth specific taxation rules and rates.

E. Withholding taxes

For companies operating in the oil and gas industry, no WHT is levied on dividends.

Interest is normally subject to 10% (shareholder loans) or 15% investment income WHT.

Royalties are subject to 10% investment income WHT.

Industrial WHT applies to service payments at a general rate of 6.5%.

No branch profits remittance tax applies in Angola for oil and gas entities.

F. Financing considerations

There are no thin capitalization rules in Angola. However, finance expenses are not deductible for PIT, except for borrowings with banks located in Angola upon authorization by the ministers of finance and oil.

G. Transactions

Profits or capital gains, whether accounted for or not, on the sale of oil and gas interests are included in the calculation of taxable profit.

No tax is levied on the share capital of oil and gas companies.

Other income is generally included in the taxable basis for the PIT computation.

H. Indirect taxes

Consumption tax

Consumption tax is currently levied on the production and importation of goods, at rates that vary between 2% and 80%, as well as on the provision of the following services:

Services	Rate
Telecommunication and electronic communication services Other companies, such as	5%
Water consumption	5%
Energy consumption	5%
Rental of areas specifically used for storage or collective parking of vehicles	5%
Lease of machinery and other equipment, except when such lease gives rise to income subject to taxation under the scope of the Investment Income Tax Code	5%
Rental of areas prepared for conferences, lectures, exhibitions, advertising or other events	5%
Consulting services, namely legal, tax, financial, accounting, IT, engineering, architecture, economics, real estate and audit services	5%
Photography, film processing, image editing, IT and web-design services	5%
Private security services	5%
Tourism and travel services promoted by travel agencies or equivalent tour operators	5%
Management of commercial establishments, canteens, dormitories, real estate and condominiums	5%
Hotel and similar services	10%

Consumption tax must be paid by the goods supplier or service provider. If certain services are rendered by a nonresident entity, a reverse charge mechanism applies in which an Angolan acquirer must assess and pay the respective consumption tax.

Any consumption tax benefit or advantage granted to importation of certain types of goods must also be extended to its production.

Consumption tax — specific rules for oil and gas upstream companies

All entities providing services (subject to consumption tax) to oil and gas upstream companies should assess the consumption tax due in the respective invoices or equivalent documents.

This taxation regime derives from the fact that there are no subjective exemptions foreseen in the Consumption Tax Law (except the ones mentioned below) and, therefore, although subject to a special tax regime, oil and gas upstream companies are not entitled to consumption tax exemption.

Consequently, oil and gas upstream companies, when paying the services related to those invoices or equivalent documents, must pay only the amount due as consideration for the services rendered (except with respect to water and electricity supplies, communications and telecommunications, lodging, touristic or similar services) and should hold the consumption tax amount therein included since they are liable for delivering such tax amount at the respective tax office.

A consumption tax exemption has been established for oil and gas companies at the exploration or development stage (up to the start of commercial production), and at the production phase (in cases where consumption tax could result in an economic and contractual misbalance) under the following conditions:

- An oil and gas company formally submits a request to its respective request to the National Tax Office seeking a tax exemption.
- An oil and gas company acquires services subject to consumption tax (other than the water, electricity supplies, communications and telecommunications, and lodging, touristic or similar services).
- An oil and gas company could seek exemption only for those services that are directly connected with and provided for in the concession areas.
- An oil and gas company should obtain a tax exemption certificate from the National Tax Office, without which such an exemption is not valid.
- An oil and gas company at production stage should obtain authorization from the National Concessionary and a joint ruling from the Minister of Finance and the Minister of Petroleum.

Customs duties

Under the Customs Tariff applicable as from year 2014, customs duties are levied on imported goods, including equipment. The rates vary between 2% and 50%, according to the goods tariff classification.

The oil and gas industry has a special customs regime that provides an exemption from customs duties, consumption tax and general levies and taxes on the importation of goods to be used exclusively in oil and gas operations (although stamp tax at 1% and statistical tax at the general rate of 0.1% still apply). The list of goods may be added to upon a petition to the Minister of Finance. The importer should present to the customs authorities a declaration stating that the goods are to be exclusively used in such operations.

A temporary import regime granting an exemption from customs duties and consumption tax is also available for goods that are exported within one year (general regime) or two years (oil and gas industry regime); this may be extended upon petition. A temporary exportation regime is also available for goods shipped abroad for repairs, provided the goods are re-imported within a one-year period.

The exportation of oil produced in each concession before or after processing is exempt from duties, except from stamp duty on customs clearance documents, the statistical tax of 0.1% ad valorem and other fees for services rendered.

Stamp duty

Stamp duty is levied on a wide range of operations, including:

- Acquisition and financial leasing of real estate at 0.3%
- Collection of payments as a result of transactions at 1%
- Real estate lease at 0.4%
- Lease of equipment at 0.4%
- Importation of goods and equipment at 1%
- Bank guarantees between 0.1% and 0.3%

- Insurance premiums between 0.1% and 0.4%
- Funding arrangements between 0.1% and 0.5%

The transfer of shares in an oil company should not be subject to stamp duty; however, the transfer of oil and gas assets may be deductible.

The rates vary between 0.1% and 1% but may also be a nominal amount, depending on the operation.

Some of the stamp duty rates apply starting from 1 April 2012.[5]

Emoluments

General customs emoluments at the rate of 2% of the customs value of the goods are also chargeable on the importation of goods.

Transport expenses also apply and may vary, depending on the means of transport used and the weight of the goods.

I. LNG Project

The Angola LNG Project (the Project) — meaning all activities and installations aimed at receiving and processing associated gas in Angola, production in Angola of LNG and natural gas liquids (NGL), as well as respective commercialization — has been considered to be of public interest; hence, special incentives for tax, customs and exchange controls have been granted under Decree-Law No. 10/07.

The Project is subject to the laws applicable to petroleum activities, namely, the Petroleum Activities Law, the Petroleum Activities Taxation Law and the Customs Regime law applicable to the oil sector, as complemented and amended by the Decree-Law.

Angola LNG Limited is the main entity responsible for executing the Project, through which the promoting companies hold their investment and rights. Other companies, such as *Sociedade Operacional Angola LNG and Sociedade Operadora dos Gasodutos de Angola*, act in representation of Angola LNG Limited. Promoting companies, which are the original shareholders of Angola LNG Limited, include Cabinda Gulf Oil Company Limited, Sonangol — Gas Natural Limitada, BP Exploration (Angola) Limited and Total Angola LNG Limited.

Petroleum income tax

Taxable profit of Angola LNG Limited is subject to PIT computed in accordance with the rules stated in Decree-Law No. 10/07 and other related legislation. Tax losses can be carried forward for five years.

Taxable profit is imputed to the promoting companies under a sort of tax transparency regime. The applicable PIT rate is 35%.

Promoting companies enjoy a tax credit for 144 months from the commercial production date, against the PIT liability, determined as per Decree-Law No. 10/07.

An exemption from PIT applies to interest and dividends obtained by affiliates (of promoting companies) that hold a participating interest in a block through which a production contract is entered into with Sonangol.

Training tax contribution

Angola LNG Limited is subject to TTC of US$0.15 per LNG barrel, increased by US$0.02 per each mmbtu of LNG sold.

Gas surcharge

Angola LNG Limited is subject to the payment of a gas surcharge, on a quarterly basis, as from the first LNG export.

5 *The Stamp Duty code has been revised and republished by Presidential Legislative Decree No. 3/14, of 21 October, in force since that date. In this context, other tax rates have been modified; namely, some customs exportation operations are now subject to a 0.5% rate.*

Industrial tax

Any income that is obtained by Angola LNG Limited, the promoting companies, and their affiliates, and is related to the commercial activities and transactions realized under the Project can benefit from an industrial tax exemption.

Profits obtained by *Sociedade Operacional Angola LNG* and *Sociedade Operadora dos Gasodutos de Angola* are subject to industrial tax, although specific rules apply.

Payments made by Angola LNG Limited to *Sociedade Operacional Angola LNG* and *Sociedade Operadora dos Gasodutos de Angola*, as well as the payments between *Sociedade Operacional Angola LNG* and *Sociedade Operadora dos Gasodutos de Angola*, concerning the execution of any service contract, are not subject to industrial tax withholdings.

Concerning service contracts (including the supply of materials) entered into by Angola LNG Limited, *Sociedade Operacional Angola LNG* and *Sociedade Operadora dos Gasodutos de Angola*, these companies are not required to perform industrial tax withholdings. This exemption applies during only a specific time frame. This is also applicable to the entities contracted and subcontracted and to the subcontracts aimed at the rendering of services or works (including the supply of materials) for the Project.

Investment income tax

Interest income derived from shareholder loans or other loans made by the promoting companies, respective affiliates, and third parties, for the benefit of Angola LNG Limited, *Sociedade Operacional Angola LNG, Sociedade Operadora dos Gasodutos de Angola* or other companies they have incorporated, will be exempt from investment income tax. A similar exemption, under certain conditions, may apply on interest derived from loans made between the promoting companies.

Promoting companies and their affiliates are exempt from investment income tax on dividends received from Angola LNG Limited, *Sociedade Operacional Angola LNG* and *Sociedade Operadora dos Gasodutos de Angola*.

Angola LNG Limited, *Sociedade Operacional Angola LNG, Sociedade Operadora dos Gasodutos de Angola* or any other company incorporated by them are not required to withhold investment income tax in relation to payments under certain lease contracts, transfer of know-how, and intellectual and industrial property rights. This exemption applies during only a specific time frame.

Other tax exemptions

Income obtained by Sonangol from payments for the use of the associated gas pipelines network, made by Angola LNG Limited under the investment contract, is exempt from all taxes and levies. Angola LNG Limited should not perform any withholdings on such payments.

Angola LNG Limited, *Sociedade Operacional Angola LNG, Sociedade Operadora dos Gasodutos de Angola*, promoting companies, and their affiliates are exempt from all other taxes and levies that are not specified in Decree-Law No. 10/07, namely, PPT, PTT, urban property tax, property transfer tax, investment income tax and stamp duty (under certain conditions). These companies are subject to the standard administrative surcharges or contributions due in relation to commercial activities and transactions associated with the Project, provided such surcharges and contributions are generically applicable to the remaining economic agents operating in Angola.

The transfer of shares in Angola LNG Limited, *Sociedade Operacional Angola LNG* and *Sociedade Operadora dos Gasodutos de Angola*, without a gain, should be exempt from all taxes and levies. Moreover, no taxes or levies are imposed on the shares of the mentioned companies, including increases and decreases of capital and stock splits.

No taxes or levies are imposed on the transfers or remittances of funds to make any payment to the promoting companies, their affiliates or third parties making loans that are exempt from income tax or WHT, as per Decree-Law No.

10/07, including the reimbursement of capital and payment of interest in relation to shareholder loans and other loans, as well as the distribution of dividends in accordance with the above decree-law.

Customs regime

In accordance with the Project's regime, the customs procedure applicable to the operations and activities is that established for companies in the customs regime law applicable to the oil industry, with the changes and adjustments stated in Decree-Law No. 10/07.

This customs regime is applicable to Angola LNG Limited, *Sociedade Operacional Angola LNG, Sociedade Operadora dos Gasodutos de Angola* and other entities that carry out operations or activities related to the Project on behalf of Angola LNG Limited, *Sociedade Operacional Angola LNG* or *Sociedade Operadora dos Gasodutos de Angola*.

In addition to the goods listed in the customs regime law applicable to the oil industry, various other products that are exclusively used for the purposes of the Project are also exempted from customs duties.

Angola LNG Limited, *Sociedade Operacional Angola LNG* and *Sociedade Operadora dos Gasodutos de Angola* are subject to surcharges on all acts of importation and exportation (up to the limit of 0.1%), a statistical surcharge on all acts of importation and exportation (0.1% ad valorem) and stamp duty on all acts of importation and exportation (0.5%).

J. Other

Environmental rules

Angolan Decree No. 59/07, of 13 July, foresees the requirements, criteria and procedures to be adopted, namely by the oil and gas industry, to obtain the respective environmental license. Under this decree, a fee is due, which should be jointly established by an executive decree issued by the Ministry of Finance and by the entity responsible for the environmental policy.

In view of the above, considering the high risk, operational characteristics and volume of investments required to carry out oil and gas activities, the Angolan competent authorities considered justifiable the adoption of a specific fee regime for this industry.

Thus, on 3 May 2013, the Government issued Executive Decree No. 140/13, which approves the calculation basis of the rate applicable to environmental projects within the oil and gas industry.

Under this executive decree, the rate/fee in question is determined based on the "total environmental impact" (TEI) quantified by its coverage, its severity and its duration. The quantification formula is also foreseen in the executive decree under analysis.

Therefore, and since the taxable basis varies according to the different stages of the oil and gas project, the basis for calculating the value of the environmental fee is based on the following formulas:

- Installation license rate (TI):

  TI = 3 (corresponding to the number of years of duration of the installation license) × TEI × AOA220,000.
- Operation license fee (TO):

  TO = 5 (corresponding to the number of years of duration of the installation license) × TEI × AOA220,000.
- License renewal fee:

  The license renewal fee should amount to a maximum of 20% of the original installation license fee or the operating license fee.
- License fee in case of projects aiming to increase the production and/or improve the quality of the project (TA):

  TA = remaining period for operating license termination × TEI × AOA220,000.

Personal income tax

Employees working in Angola are subject to personal income tax, which is charged under a progressive rate system up to 17%. Personal income tax is paid through the WHT mechanism operated by employers (PAYE system).

Social security

Nationals or foreign individuals working in Angola are subject to the local social security regime. Contributions are paid by the employer and are due at the rates of 8% for employers and 3% for employees. Individuals temporarily working in the country may be exempt from local contributions if they remain affiliated to a similar regime abroad.

Petroleum activities law — main features

Concession rights and mineral rights are attributed to the NOC. Foreign or local entities may contract with the NOC as investors. Any company that wants to conduct oil and gas operations in Angola must do so in partnership with the NOC — except for operations within the scope of an exploration license.

Partnership with the NOC may take one of the following forms: a company, a consortium agreement or a PSA. The NOC is also permitted to carry out oil and gas activities under RSCs. In some cases, an incorporated joint venture may also be put into place. As a general rule, if the joint venture takes the form of a company or a consortium agreement in which the NOC has an interest, the state interest should be greater than 50% (although the percentage may be lower upon receiving government authorization).

The partnership must be preapproved by the Government. The operator, which may or may not be a partner, must be stated in the concession agreement following a proposal by the NOC. The operator or the partner must be a commercial company.

The investment risk during the exploration phase is taken by the parties that have contracted with the NOC; such parties are unable to recover their investment if no economic discovery is made.

Borrowings for investments from third parties by the NOC or its partners must be authorized by the Government if oil production is used as security.

An exploration license or an oil concession is required to carry out the activity.

Hiring of contractors by oil and gas companies

Local regulations provide for the following three regimes:

1. Limited free-trade regime — certain services should be provided by only local companies (foreign contractors are excluded).
2. Semi-free-trade regime — certain services may be provided only by local companies or by foreign contractors when associated with local partners.
3. Free-trade regime — all services related to oil and gas activity (onshore and offshore) that are not within either of the two previous regimes and that require a high level of industry expertise may be freely provided by local companies or by foreign contractors, although joint ventures with local partners are possible.

A company is considered to be a local company if the majority of its share capital is owned by Angolan investors and if the company is registered with the Ministry of Petroleum or the Angolan Chamber of Commerce and Industry.

Licensed entities, the state concessionaire and its partners, and all entities that participate in oil operations must:

- Acquire materials, equipment, machinery and consumption goods produced locally, provided they are of equivalent quality and are available in reasonable time, at prices no more than 10% above the cost of imported items (including transportation, insurance and customs costs)

- Contract with local service providers if the services rendered are identical to those available in the international market and if the price, when liable to the same level of tax, does not exceed the price charged by foreign service providers for similar services by more than 10%
- Recruit local nationals, unless there are no locals with the required qualifications and experience

Foreign-exchange controls

Legislation was approved in January 2012 to introduce foreign-exchange control regulations applicable only to the oil and gas sector.

These rules aim primarily to establish a uniform treatment in this sector by replacing the multiple exchange regimes that have been applied to the oil and gas upstream companies operating in Angola, providing fair treatment to all investors.

These foreign-exchange control rules cover the trade of goods and services and capital movements arising from the prospecting, exploration, evaluation, development and production of crude oil and natural gas.

For the purpose of the rules, exchange operations encompass (i) the purchase and sale of foreign currency; (ii) the opening of foreign currency bank accounts in Angola by resident or nonresident entities and the transactions carried out through these bank accounts; (iii) the opening of national currency bank accounts in Angola by nonresident entities and the transactions carried out through these bank accounts; and (iv) the settlement of all transactions of goods, services and capital movements.

The NOC and corporate investors, domestic or foreign, must carry out the settlement of foreign-exchange transactions through bank institutions domiciled in the country and authorized to conduct foreign-exchange business. This must be done by opening bank accounts, in the foreign currency, and depositing sufficient funds for tax payments and other mandatory payments for the settlement of goods and services provided by residents or nonresident entities.

In general terms, these rules imposed on oil and gas upstream companies foresee that (i) all foreign-exchange transactions must be carried out through Angolan banks and (ii) the bank accounts opened in Angolan banks must be funded sufficiently to satisfy tax obligations and the purchase of all goods and services from local and foreign companies.

Other

The NOC and its partners must adopt an accounting system in accordance with the rules and methods of the General Accounting Plan. The Ministry of Finance may issue rules to adjust the accounts if the currency devalues, using the US dollar as a benchmark. Accounting records must be maintained in Angola, and book entries should be made within 90 days.

Oil and gas upstream entities (which are now classified as large taxpayers) must prepare local statutory accounts under the local generally accepted accounting principles (GAAP), which need to be certified by a statutory auditor duly registered at the local professional association — *Ordem dos Contabilistas e Peritos Contabilistas de Angola*.

The fiscal year is the calendar year. The time allowed in Article 179 of the Commercial Companies Code for the approval of the balance sheet and the report of the board of auditors is reduced to two months.

Documents must be submitted in Portuguese, using Angolan kwanza, and these documents must be signed and stamped to indicate approval by a director. Oil tax returns are filed in thousand Angolan kwanza and US dollars.

The Angolan Central Bank BNA approved Ruling No. 7/14, of 8 October, in force since 8 November 2014, which established rules concerning the Foreign Exchange Transactions Regime applicable to oil and gas companies[6] (including

6 *This regulation was first covered by Law No. 2/12, of 13 January 2012, in force since 13 April 2012.*

LNG companies), namely the sale of foreign currency to BNA, under the following terms:

- Except for receivables and bonuses obtained by NOC, all oil and gas companies should sell to BNA the foreign currency for tax payment purposes, and BNA should credit such amount in the national currency (Angolan kwanza) to the national Treasury account.
- Oil and gas companies (including those undertaking exploration for oil and gas) should sell to BNA the correspondent foreign currencies needed to proceed with the payments for services rendered and supply of goods to resident entities, and BNA should credit such amounts to the oil and gas companies' bank account domiciled in Angola.

Certain deadlines and specific rules apply.

Argentina

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Argentina is organized into federal, provincial and municipal governments. The fiscal regime that applies to the oil and gas industry principally consists of federal and provincial taxes:

- Corporate income tax (CIT) — 30% (a)
- Withholding tax (WHT):
  - Dividends — 7%/0%/35% (b)
  - Interest — 15.05%/35%
  - Royalties — 21%/28%/31.5%
- Minimum presumed income tax (MPIT) — 1%
- Value-added tax (VAT) — 21% (general rate)
- Stamp tax — 1.3% (general rate)
- Turnover tax — 3.4% (average rate)
- Customs duties — importation taxes (rates on cost, insurance and freight (CIF)), importation duty 0%/35%, statistical rate 0.5%, VAT 10.5%/21% and withholding on income tax 0%/6%/11%, VAT 0%/10%/20% and turnover tax 0%/2.5%
- Export taxes — income tax withholding on exports: 0%/0.5%/2% on certain cases; export duties applicable to only certain products (see Section D)
- Royalties — 12%
- Tax on debits and credits in checking accounts — 0.6%
- Personal assets tax — equity interest on local entities 0.25%
- Social security tax — employer 23.5% or 26.7%, employee 17%

a. The corporate income tax rate is 30% for fiscal years starting 1 January 2018 to 31 December 2019, and 25% for fiscal years starting 1 January 2020 and onward.

b. A 7% dividend withholding tax rate is applicable for profits accrued during fiscal years starting from 1 January 2018 to 31 December 2019. The rate will be 13% for profits accrued in fiscal years starting from 1 January 2020 and onward. The abovementioned rates apply to distributions made to resident individuals or foreign investors, while distributions to resident corporate taxpayers are not subject to withholding. A 0% dividend withholding tax rate is generally applicable for profits accrued during fiscal years that started prior to 1 January 2018; however, in these cases, a 35% withholding tax (known as "equalization tax") is triggered if the distribution exceeds the after-tax accumulated taxable income of the taxpayer.

B. Fiscal regime

Argentina is organized into federal, provincial and municipal governments. The main taxes imposed on the oil and gas industry by the national government include income tax, VAT, minimum presumed income tax, personal assets tax, tax on debits and credits in checking accounts, custom duties, export taxes and social security taxes.

Provincial taxes imposed on the petroleum industry are turnover tax, stamp tax and (for upstream companies only) royalties. Municipalities may impose taxes within their jurisdictions.

Taxation powers are jointly exercised by the national and provincial governments within the provincial territories. However, the national government has also exclusive taxation power on all the Argentine exclusive economic zone.

Corporate income tax (CIT)

Argentine resident corporations and branches are subject to income tax on their non-exempt, worldwide income at a rate of 30% (for fiscal years starting 1 January 2020 and onward, the rate will be 25%).

Capital gains obtained by tax-resident companies are included in taxable income and taxed at the regular corporate tax rate. Capital gains on the sale, exchange, barter or disposal of Argentine non-listed shares, quotas, participation in entities, titles, bonds and other Argentine securities held by foreign residents are subject to a 15% tax (which may be calculated on actual net income, or by applying a 90% presumed income, thus resulting in an effective 13.5% tax on sale price).

Capital gains derived by foreign residents from the transfer of listed shares are covered by an exemption, to the extent the investor is not resident in, and the funds do not arise from, "non-cooperating" jurisdictions.

Dividends

The dividend withholding tax rate is 7% for profits accrued during fiscal years starting from 1 January 2018 to 31 December 2019, and 13% for profits accrued in fiscal years starting from 1 January 2020 and onward. The abovementioned rates apply to distributions made to resident individuals or foreign investors, while distributions to resident corporate taxpayers are not subject to withholding. A 0% dividend withholding tax rate is generally applicable for profits accrued during fiscal years that started prior to 1 January 2018; however, in these cases, a 35% withholding tax (known as "equalization tax") is triggered if the distribution exceeds the after-tax accumulated taxable income of the taxpayer.

Consolidation

No system of group taxation applies in Argentina. Members of a group must file separate tax returns. There are no provisions to offset the losses of group members against the profits of another group member.

Tax losses

Net operating losses arising from the transfer of shares or equity interests — including shares of mutual funds and financial trusts and any other right on trusts and similar products — digital currencies, public or corporate bonds and other securities may offset income of only the same origin. The same applies to losses from activities that are not sourced in Argentina and from transactions under derivative agreements (except for hedging transactions). Losses from exploration and exploitation of living and non-living natural resources performed in the Argentine continental shelf and in the economic exclusive area, including artificial islands, facilities and other structures established in such area may offset income of only Argentine sources. All tax losses generated in a tax period may be carried forward to the five periods following the period when the losses were incurred.

Thin capitalization

Under general principles, transactions between related parties must be made on an arm's-length basis.

The Argentine income tax law establishes a limit for the deduction of interest arising from financial loans granted by related parties. The limit equals 30% of earnings before interest, taxes, depreciation and amortization (EBITDA) or a certain amount to be determined by the Executive Power, whichever is higher. The limit each year will be increased by the amount unused (if applicable) in the prior three years. In addition, if certain interest was not deductible in a given year due to the application of the limitation, it can be carried forward for five fiscal years. "Interest" includes foreign exchange differences.

The law provides exemptions from the deduction limit for certain situations (e.g., interest derived on loans obtained by Argentine banks and financial trusts or when the beneficiary of the interest has been subject to tax on such income, in accordance with the Argentine income tax law). In addition, the limitation will not apply to situations in which it is proved that the ratio of interest to EBITDA of the Argentine borrower is equal to or lower than the same ratio for its economic group — regarding debt with unrelated lenders — for the same fiscal year.

Transfer pricing

Transfer pricing rules follow the Organisation for Economic Co-operation and Development (OECD) guidelines (the arm's-length principle).

Depreciation

The following depreciation principles apply:

- Intangible assets related to the oil and gas concession — depreciation based on units of production
- Wells, machinery, equipment and productive assets — depreciation based on units of production
- Other tangible assets (vehicles, computers) — straight-line, considering the useful lives of the assets

Minimum presumed income tax (MPIT)

MPIT is assessed at a rate of 1% on the value of the taxpayer's assets at the end of the taxpayer's accounting period. Value in this case excludes shares in Argentine companies. In addition, value excludes investments in new movable assets or infrastructure for the initial year of investment and the succeeding year.

MPIT is due to the extent that a taxpayer's MPIT liability exceeds its CIT. This excess is then treated as a tax credit that may be carried forward for the 10 years following the year the tax was paid. To the extent that the taxpayer's CIT exceeds MPIT during this 10-year period, the credit may be used to reduce the CIT payable, up to the amount of this excess.

Under Law 27,260, MPIT will be eliminated for fiscal years beginning on or after 1 January 2019.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

Inflationary adjustment

Adjustment for inflation is allowed in accordance with the following rules: (i) inflation adjustment of new acquisitions and investments carried out from 1 January 2018 and onward; and (ii) the application of an integral inflation adjustment mechanism when the variation of the Internal Wholesale Price Index supplied by the National Institute of Statistics and Censuses is higher than 100% for the 36-month period before the end of the fiscal period.

Revaluation option

Argentine-resident individuals and companies have the option to revaluate for tax purposes their assets located in Argentina that generate taxable income. The revaluation option is applicable for the first fiscal period that ends after 30 December 2017 (for example, for fiscal periods ending on 31 December, the revaluation option would be applicable to the year-end of 31 December 2017).

The new tax value of the assets will be determined by applying a "revaluation factor" to the tax value originally determined in each year or period of the asset's acquisition or construction. In the case of immovable or movable property qualifying as fixed assets, the value may be determined by an independent appraiser under certain conditions.

In addition, the Law imposes a one-time special tax on the amount of the revaluation. The applicable rate will vary depending on the assets revaluated:

- Real estate (regarded as capital assets): 8%
- Real estate (regarded as inventories): 15%
- Shares, quotas and other participations in Argentine companies owned by resident individuals: 5%
- All other assets (except inventories and cars, which may not be revaluated): 10%

Assets subject to an accelerated tax depreciation regime cannot be included in this revaluation option.

C. Withholding taxes on interest and royalties

A WHT rate of 15.05% applies on interest payments related to the following types of loans:

- Loans granted by foreign financial entities that are located in the following jurisdictions:
  - Jurisdictions not considered as low- or no-tax jurisdictions as per Argentine rules

  Or

  - Jurisdictions that have signed exchange-of-information agreements with Argentina and have internal rules providing that no banking, stock market or other secrecy regulations can be applied to requests for information by the Argentine tax authorities
- Loans for the importation of movable assets, except automobiles, if the loan is granted by the supplier of the goods

In general, the WHT rate for all other interest payments to nonresidents is 35%.

The general WHT rate for royalties is 31.5%. If certain requirements are met, a 21%/28% rate may apply to technical assistance payments, and a 28% rate may apply to certain royalties (e.g., trademarks).

The above withholding tax rates may be altered by a double tax agreement (where relevant). As noted in Section E, Argentina has entered into numerous double tax agreements.

D. Indirect taxes

VAT

VAT is levied on the delivery of goods and the provision of services derived from an economic activity, on the import of goods, and on the import of services to be used or exploited in Argentina.

The standard VAT rate is 21%. This rate is reduced for certain taxable events (e.g., sales, manufacturing, fabrication or construction, and definitive imports of goods that qualify as "capital assets" according to a list included in the VAT law and on interest, commissions and fees on loans granted by financial institutions, subject to certain conditions).

Exports are exempt from VAT. Taxpayers may claim a refund from the Government for VAT paid relating to exports.

The VAT that a company charges on sales or service provisions is known as "output VAT." The VAT paid by companies for goods or services purchases is called "input VAT." In general, companies deduct input VAT from output VAT every month and pay the difference (if any). VAT returns are filed monthly.

If, in a given month, the input VAT exceeds the output VAT, the difference may be added to the input VAT for the next month. A taxpayer is not entitled to a refund unless the accumulated input VAT is related to:

- Exports
  Or
- Investments in fixed assets (except cars) after six months of the purchase, construction, fabrication or import of such assets, if the accumulated VAT could not be offset with output VAT

Stamp tax

Stamp tax is a provincial tax levied on acts formalized in Argentina through public or private instruments. It is also levied on instruments formalized abroad when they produce effects in Argentina.

In general, effects are produced in Argentina when the following activities occur in its territory: acceptance, protest, execution, demand on compliance and payment. This list is not exhaustive.

Each province has its own stamp tax law, which is enforced within its territory.

The documents subject to stamp tax include agreements of any kind, deeds, acknowledged invoices, promissory notes and securities.

The general rate is approximately 1.3%, but in certain cases — for example, when real estate is sold — the rate may reach 4%. However, rates vary according to the jurisdiction.

Royalties

Royalties in Argentina amount to 12% of the wellhead value of the product. Under certain particular circumstances, the rate may vary. Royalties may be treated as an immediate deduction for CIT purposes.

Turnover tax

Provincial governments apply a tax on the gross revenues (or turnover) of businesses. The rates are applied to the total gross receipts accrued in the calendar year. The average rate is 3.4% (for upstream companies). The rate could be higher for service companies in the oil and gas industry.

Exports are exempt for turnover tax purposes for all activities without any formal procedure.

Customs duties

Argentina is a member of the World Trade Organization (WTO), the Latin American Integration Association (ALADI) and MERCOSUR (South American trade block).

As a member of the WTO, Argentina has adopted, among other basic principles, the General Agreement on Tariffs and Trade (GATT) Value Code, which establishes the value guidelines for importing goods.

ALADI is an intergovernmental agency that promotes the expansion of regional integration to ensure economic and social development, and its ultimate goal is to establish a common market. Its 13 member countries are Argentina, Bolivia, Brazil, Chile, Colombia, Cuba, Ecuador, Mexico, Panamá, Paraguay, Peru, Uruguay and Venezuela.

MERCOSUR was created in 1991, when Argentina, Brazil, Uruguay and Paraguay signed the Treaty of Asunción. Bolivia is also in the process of being appointed as member. The basic purpose of the treaty is to integrate the four member countries through the free circulation of goods, services and productive factors and establish a common external tariff.

Venezuela was incorporated as a full member of MERCOSUR on 31 July 2012, but due to internal sanctions, it is currently suspended and cannot exercise the rights granted by this Treaty. It should also be noted that Chile, Colombia, Ecuador, Guyana, Peru and Surinam are associated with MERCOSUR as acceding countries.

The import of goods originating in any of the member countries is subject to a 0% import duty.

Import taxes

In Argentina, importation duties are calculated on the CIF value of goods, valued using GATT valuation standards. The duty rate ranges from 0% to 35%, according to the category of goods, which should be identified for duty purposes using common MERCOSUR nomenclature tariffs.

Additionally, the importation of goods is subject to the payment of a statistical rate, which is 0.5% of the CIF value of goods with a US$500 cap, and VAT (10.5%/21%, depending on the goods). VAT payable at importation may be treated as input VAT by the importer.

The definitive importation of goods is subject to an additional income tax withholding of 6% or 11% (depending on whether the imported assets are to be marketed or to be used by the company), VAT withholding (10% or 20%) and turnover tax withholding (2.5%). These tax withholdings constitute an advance tax payment for registered taxpayers of tax calculated in the tax return for the relevant tax period. In the case of imports of capital assets, property, plant and equipment, no withholdings would apply.

Export taxes

The definitive exportation of goods is subject to an additional withholding tax when such goods are invoiced to a country different from the one where the foreign importer is located. Rate is 0.5% (or 2% when the invoices are issued to entities located in non-cooperative countries regarding fiscal transparency) of the free-on-board (FOB) value of the goods.

Export duty is levied on the export of goods for consumption, i.e., the definitive extraction of merchandise from Argentina. Most export duties were eliminated in 2016/2017 — in particular, export duties on crude oil and liquid gas.

Other taxes

Tax on debits and credits in checking accounts

The tax on debits and credits in checking accounts is assessed at a 0.6% rate, based on the amount of the credit or debit made in the checking account. The tax is determined and collected by the bank.

Additionally, 34% of the tax paid for bank account credits may be offset against income tax or MPIT returns and related tax advances.

A new Decree issued on May 7, 2018 established that 33% of the tax paid for both "credits" and "debits" can offset income tax and MPIT obligations (including obligations arising from annual tax returns or the respective advance payments) for fiscal years starting 1 January 2018, and thereafter. The new creditability percentage is effective for the tax on debits and credits derived from taxable events occurring 1 January 2018, and thereafter.

Personal assets tax

Personal assets tax applies to individuals with assets owned as at 31 December each year. For resident individuals, the tax applies on assets owned in Argentina and abroad. For nonresident individuals, the tax applies on assets owned only in Argentina.

The law presumes (without admitting evidence to rebut the presumption) that shares, quotas and other participation interests held in the capital of Argentine companies by nonresident entities are indirectly owned by foreign individuals; thus, the tax applies to this type of ownership. The tax amounts to 0.25% annually (based on the equity value according to the financial statements), which must be paid by the Argentine companies as substitute taxpayers. The substitute taxpayer is consequently entitled to ask for a refund of the tax from its shareholders or partners.

Social security taxes

Salaries paid to employees are subject to employer and employee contributions to the social security system.

The percentages for employers and employees are 23.5% and 17.0%, respectively. The employee's tax must be withheld from the salary payment by the employer.

Additionally, if a company's main activity is commerce or the provision of services and its average sales for the last three fiscal years exceed ARS48 million (about US$2 million), the social security taxes borne by the company rise from 23.5% to 26.7%.

E. Other

Business presence

In Argentina, forms of "business presence" typically include corporations, limited liability companies, foreign branches and joint ventures (incorporated and unincorporated). In addition to commercial issues, the tax consequences of each form are important considerations when setting up a business in Argentina. Unincorporated joint ventures are commonly used by companies in the exploration and development of oil and gas projects.

Foreign exchange controls

The Central Bank of Argentina has implemented regulations aimed at relaxing the control measures on the foreign exchange market. Foreign currency obtained from export of goods and services will not be subject to the obligation to bring and settle in the Exchange Market. Financial loans are not required to be settled into Argentina. However, regardless of whether the funds are entered and settle or not, it is mandatory to register the debt on Central Bank's Communique "A" 6401. Payments abroad of dividends, loans, interest and principal, as well as imports of goods, are allowed.

Promotion program for incremental gas production

In January 2013, a resolution established a promotion program for additional gas production sold on the domestic market over a determined base. Beneficiaries will receive a governmental compensation to reach US$7.5 per million BTU.

Promotion system for investments in hydrocarbon operations

There is a promotion system for hydrocarbon investors. If certain conditions are met, the following benefits are provided:

- Investors will be able to trade a portion of liquid and gaseous hydrocarbon production from the project freely on the foreign market after the fifth year of the project, without having to pay export duties.
- Investors would have free availability of the foreign currency obtained as a result of the sale of that portion (although there are certain conditions that must be satisfied), without the obligation of entering that money into Argentina.
- When domestic demand prevents the producer from exporting the abovementioned portion, those producers will be guaranteed a local price that is equivalent to the export benchmark (without the effect of withholdings, which would not apply in this case), and they will have privileged rights to obtain freely available foreign currency on the official exchange market up to the amounts equaling the abovementioned percentage.

Province of Tierra del Fuego

A special tax regime currently applies to certain activities carried out in the Province of Tierra del Fuego. Law No. 19640 establishes that individuals, undivided estates and legal persons are exempt from any national tax that may apply to events, activities or transactions performed in the Province of Tierra del Fuego, Antarctica and the South Atlantic Islands, or that relate to assets located in Tierra del Fuego. As a result, activities carried out in the Province of Tierra del Fuego are exempt from CIT, VAT and MPIT. Furthermore, employees working in this province are exempt from income tax.

Despite this, the Argentine Government enacted Decree No. 751/2012, which abolishes all fiscal and custom benefits created by Law No. 19640 in respect of activities related to oil and gas production, including services to the oil and gas industry. Decree No. 751/2012 applies to taxable events and income accrued since 17 May 2012.

However, Decree No. 520/2017 partially reverted such abolition, establishing that oil and gas produced in Tierra del Fuego will not be subject to VAT when sold to consumers located in such jurisdiction. It applies to taxable events since 18 July 2017.

Treaties to avoid international double taxation

Argentina has numerous treaties in effect to avoid double international taxation and thus promote reciprocal investment and trade. International treaties entered into with the following countries are currently in place: Australia, Belgium, Bolivia, Brazil, Canada, Chile, Denmark, Finland, France, Germany, Italy, Mexico, Netherlands, Norway, Russia, Spain, Sweden, Switzerland and United Kingdom.

Also, Argentina has entered into specific international transportation treaties with several nations.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- □ **Production sharing contracts**
- □ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies in Australia to the petroleum industry consists of a combination of corporate income tax (CIT), a petroleum resource rent tax (PRRT) and royalty-based taxation.

- Royalties[1] – 10% to 12.50%
- Income tax – CIT rate 30%[2]
- Resource rent tax – 40%[3]
- Capital allowances – D, E, O[4]
- Investment incentives – L, RD[5]

B. Fiscal regime

The current fiscal regime that applies in Australia to the petroleum industry consists of a combination of CIT, a PRRT and royalty-based taxation.

1 *Generally applicable to onshore projects, royalties paid are creditable for PRRT and deductible for income tax purposes. A 5% royalty applies for tight gas in Western Australia (WA). Different rates may apply for geothermal energy.*

2 *The corporate tax rate for small businesses (with an aggregated turnover of less than AU$2 million) has been reduced to 27.5%.*

3 *PRRT paid is deductible for income tax purposes. From 1 July 2012, PRRT also applies to all onshore projects and the North West Shelf.*

4 *D: accelerated depreciation; E: immediate write-off for exploration costs; O: PRRT expenditure uplift.*

5 *L: losses can be carried forward indefinitely; RD: R&D incentive.*

Corporate income tax

Australian resident corporations are subject to income tax on their nonexempt, worldwide taxable income at a rate of 30%.

From 1 July 2017, a 27.5% company tax rate applies to "small business" companies with less than AU$25 million of turnover. The corporate income tax rate will progressively decrease to 25% by 2026 for companies with less than AU$50 million of turnover.

Small business companies benefiting from the reduced CIT rate must determine whether they frank at 27.5% or 30%, based on the prior year's turnover.

The taxable income of nonresident corporations from Australian sources that is not subject to final withholding tax or treaty protection is also subject to tax at the applicable CIT rate. The CIT applies to income from Australian oil and gas activities.

Australia does not apply project ring fencing in the determination of corporate income tax liability. Profits from one project can be offset against the losses from another project held by the same tax entity, and profits and losses from upstream activities can be offset against downstream activities undertaken by the same entity.

Australia has tax consolidation rules whereby different Australian resident wholly owned legal entities may form a tax-consolidated group and be treated as a single tax entity.

CIT is levied on taxable income. Taxable income equals assessable income less allowable deductions. Assessable income includes ordinary income (determined under common law) and statutory income (amounts specifically included under the Income Tax Act). Deductions include expenses, to the extent that they are incurred in producing assessable income or are necessarily incurred in carrying on a business for the purpose of producing assessable income.

Deductions for expenditures of a capital nature may be available under the "Uniform Capital Allowance" regime. The most common being in the form of a capital allowance for depreciating assets (see "Capital allowances" in Section C). However, there may be deductions available for other types of capital expenditures (e.g., an expenditure incurred to establish an initial business structure is deductible over five years).

Profits from oil and gas activities undertaken by an Australian resident company in a foreign country are generally exempt from tax in Australia, provided they are undertaken through a foreign permanent establishment (PE).

Capital gains

Gains resulting from a capital gains tax (CGT) event may be subject to income tax. Gains arising from assets acquired prior to 20 September 1985 can be disregarded subject to the satisfaction of integrity measures. Capital gains or losses are determined by deducting the cost base of an asset from the proceeds (money received or receivable, or the market value of property received or receivable). For corporate taxpayers, the net capital gain is included in taxable income and taxed at the applicable CIT rate.

Capital losses are deductible against capital gains and not against other taxable income. However, trading losses are deductible against net taxable capital gains, which are included in taxable income. Net capital losses can be carried forward indefinitely for use in subsequent years, subject to meeting loss carryforward rules.

Capital gains and losses on disposals of plant and depreciating assets acquired on or after 21 September 1999 are not subject to the CGT provisions. Instead, these amounts are treated as a balancing adjustment under the depreciation rules and are taxed on revenue account (see "Asset disposals" in Section G).

Oil and gas exploration permits, retention leases and production licenses acquired after 30 June 2001 are treated as depreciating assets and are therefore not subject to CGT. Permits, leases and licenses acquired on or before 30 June 2001 are subject to the CGT provisions.

For interests in foreign companies of 10% or more, capital gains or losses derived by an Australian resident company on the disposal of shares in a foreign company are reduced according to the proportion of active versus passive assets held by the foreign company. Foreign companies with at least 90% active assets can generally be disposed of free of CGT.

Australian companies with foreign branch active businesses (which will generally include oil and gas producing assets) can also generally dispose of foreign branch assets free of CGT.

Nonresidents are subject to CGT on only taxable Australian property (TAP). TAP includes:

- Taxable Australian real property (e.g., real property or land in Australia and mining, quarrying or prospecting rights if the underlying minerals or materials are in Australia)
- Indirect Australian real property, comprising a membership interest in an entity in which, broadly speaking, the interest in the company is equal to or greater than 10% and more than 50% of the market value of the company's assets can be traced to taxable Australian real property; the residency of the entity is irrelevant, and this measure can apply to chains of entities (see Section G for an explanation of how this principle is applied in the context of nonresidents selling shares in an Australian company)
- Assets of a business conducted through a PE in Australia
- Rights or options to acquire the abovementioned assets

A 12.5% non-final withholding tax applies to the disposal of TAP by nonresidents from 1 July 2017 (previously 10% from 1 July 2016) (see Section E).

Functional currency

Provided certain requirements are met, taxpayers may elect to calculate their taxable income by reference to a functional currency (i.e., a particular foreign currency) if their accounts are solely or predominantly kept in that currency.

Transfer pricing and global base erosion and profit shifting (BEPS)

Australia's transfer pricing laws, amended in 2012 and 2013, ensure that international related-party transactions are priced at arm's length. Taxpayers are required to self-assess the impact of any differences between actual and arm's-length conditions. The legislation requires taxpayers to demonstrate that the actual commercial or financial dealings between themselves and offshore related parties accord with those that might be expected to be agreed between independent parties. If this is not to be the case, arm's-length conditions should be assessed on arrangements that would reasonably be expected to exist between independent third parties (this may involve a reconstruction of transactions in certain circumstances, setting aside actual contractual terms).

The Australian Taxation Office (ATO) issued guidance in 2014 on the new transfer pricing specific documentation requirements for compliance purposes. In addition to preparing transfer pricing documentation in accordance with ATO requirements, taxpayers are subject to certain mandatory record-keeping requirements in order to support their self-assessment position. Failure by taxpayers to prepare documentation for income years commencing on or after 1 July 2013, which meets the ATO minimum requirements outlined in the legislation, results in those taxpayers not being able to establish that they have a Reasonably Arguable Position (RAP) with respect to their transfer prices.

In the event of an ATO audit, this automatically elevates the taxpayer to a higher penalty position. The ATO has released simplified documentation requirements for certain categories of taxpayers/related-party dealings, which may be used by taxpayers to minimize some of their record-keeping and compliance costs.

Specific disclosures in relation to international related-party transactions and their underlying pricing (including methodologies adopted and supporting documentation maintained) are required to be made as part of the income tax return process.

Australia is actively involved in the global BEPS debate. Effective for income years commencing on or after 1 January 2016, domestic legislation has been implemented in respect of Action 7 (preventing the artificial avoidance of PE status) in the form of the Multinational Anti-Avoidance Law (MAAL) and Action 13 (transfer pricing and country-by-country (CbC) documentation). This legislation applies only to taxpayers that are a "significant global entity" (SGE) for the year (i.e., it is a global parent entity or a member of a consolidated accounting group that has annual global income exceeding AU$1 billion). All Australian entities and Australian PEs of nonresidents are required to lodge a CbC report, a master file and a local file (subject to certain exemptions). The local file is not wholly consistent with the Organisation for Economic Co-operation and Development (OECD) recommendations, and the ATO will still expect taxpayers to prepare separate Australian-specific transfer pricing documentation.

This legislation also doubles the amount of any penalty imposed on an SGE for entering into any tax-avoidance or profit-shifting schemes in which the taxpayer does not have a RAP.

On 27 March 2017, the Australian Parliament passed legislation to implement a Diverted Profits Tax (DPT). The DPT allows the Australian Commissioner of Taxation to impose a penalty DPT rate of 40% on Australian and foreign owned SGEs in respect of certain profits "diverted" out of Australia. The DPT applies for income years commencing on or after 1 July 2017. The DPT is designed to complement other existing anti-avoidance rules contained in Part IVA of the *Income Tax Assessment Act 1936*. Very broadly, it will apply to arrangements or "schemes" where:

- A taxpayer ("the relevant taxpayer" has obtained a tax benefit in connection with the scheme in an income year
- A foreign entity, that is an associate of the relevant taxpayer, entered into or carried out the scheme or is otherwise connected with the scheme
- The principal purpose, or one of the principal purposes of the scheme, is to obtain an Australian tax benefit or to obtain both an Australian and foreign tax benefit
- None of the statutory exemptions apply

As part of this package of legislation, the revised OECD transfer pricing guidelines will also be incorporated into Australia's tax law from 1 July 2016. These arose from BEPS Actions 8 to 10 and are intended to ensure that transfer pricing outcomes better reflect value creation in global supply chains. Accompanying the introduction of the DPT were increased penalties for noncompliance with tax document requirements for SGEs with, by way of example, "failure to lodge" penalties for SGEs being as high as AU$525,000. These changes will apply from 1 July 2017.

On 7 June 2017, Australia signed the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (the Multilateral Instrument). The Multilateral Instrument (OECD BEPS Action 15) was developed to efficiently modify jurisdictions' double tax agreements to prevent their exploitation and to improve international dispute resolution mechanisms. Exposure draft legislation released for consultation in February 2018 would give the Multilateral Instrument force of law in Australia. Pending the ratification of the Multilateral Instrument by Australia's double tax agreement partners, it will modify the majority of Australia's double tax agreements to comply with relevant BEPS initiatives, including changes to double tax agreement outcomes relating to hybrid mismatches, PEs, treaty abuse and dispute resolutions.

In March 2018, the Australian Treasury released a revised exposure draft of Australia's hybrid mismatch rules, which were originally released for consultation in November 2017. These rules address BEPS Action 2 (neutralizing the effects of hybrid mismatch arrangements) and are aimed at eliminating double tax benefits arising from arrangements that exploit differences in the tax treatment of an entity or an instrument under the tax laws of two or more tax jurisdictions. Contained within these rules is an integrity measure that targets related-party cross-border financing where the tax outcome is "in substance" a hybrid outcome by virtue of the creditor being resident in a no- or low-tax cost jurisdiction. The anticipated start date of the rules is 1 January 2019.

In 2016, the ATO also published two documents relevant to various lease-in, lease-out (LILO) arrangements (e.g., charter structures that involve bringing vessels/rigs, etc., into Australian waters) and foreign residents operating vessels/other assets in Australia. Consultation with advisors is currently underway and ongoing ATO compliance activity is expected across the industry. The ATO published both a taxpayer alert (TA 2016/4), summarizing the ATO's concerns regarding LILO arrangements and, in December 2016, circulated an updated draft guidance paper on *Transfer pricing and profit attribution guidance in relation to foreign resident vessels operating in Australia and cross border vessel leasing*. The latter has been designed to provide practical guidance on transfer pricing and profit attribution issues in relation to the operation of vessels in Australia.

The ATO has issued Taxpayer Alert TA 2016/4 explaining its concerns in relation to certain LILO arrangements around transfer pricing, PE attribution, Part IVA and withholding taxes.

International related-party financing arrangements (IRPFAs) have been a high-priority area for the ATO for some time. Within the 2017 year, a high-profile case and subsequent Practical Compliance Guideline (PCG) 2017/4 on IRPFAs have provided insight into the ATO's view on the pricing and conditions of these transactions. The PCG risk assessment, although not a mandatory exercise, provides the ATO's expectation that taxpayers self-assess each of their IRPFAs on, at a minimum, an annual basis against a number of specified criteria. These criteria then assign the IRPFA a risk zone based on the outcomes of the self-assessment. A taxpayer is deemed to fall in the risk zone of its highest-risk IRPFA.

Dividends

Dividends paid by Australian resident companies can be franked with a franking credit to the extent that Australian income tax has been paid by the company at the full corporate tax rate on the income being distributed.

For resident corporate shareholders, to the extent the dividend has been franked, the amount of the dividend is grossed up by the amount of the franking credit and included in assessable income. The company is then entitled to:

- A nonrefundable credit or offset of an amount equal to the franking credit
- Conversion of excess franking credits into carryforward trading losses
- A franking credit in its own franking account that can in turn be distributed to its shareholders

For resident individual shareholders, the shareholder includes the dividend received plus the franking credit in assessable income. The franking credit can be offset against personal income tax assessed in that year, and excess franking credits are refundable.

Dividends paid or credited to nonresident shareholders are subject to a final 30% withholding tax (the rate is generally reduced by any applicable tax treaty) on the unfranked portion of a dividend. No dividend withholding tax applies to franked dividends. Subject to double tax treaty relief, the withholding tax is deducted at source on the gross amount of the unfranked dividend.

Dividends paid by a foreign company to an Australian resident company are not taxable if the Australian company has a 10% or more participation interest in the foreign company. This exemption is limited to equity interests from 16 October 2014 and aligns with the debt/equity classification of financial instruments for income tax purposes.

Special rules exempt withholding tax on dividends paid to foreign residents that are classed as "conduit foreign income." This term broadly means foreign-sourced income earned by an Australian company that is not subject to tax in Australia. In practice, this means non-Australian exploration and production companies may consider using Australia as a regional holding company because:

- Profits from foreign operations (or foreign subsidiaries) can be passed through Australia free of tax.
- CGT is not generally levied on the disposal of foreign subsidiaries or branch operations (provided they hold predominantly active assets).

Tax year

A company's tax year runs from 1 July to 30 June of each year. It is, however, possible to apply for a different accounting period to align a taxpayer's tax year with the financial accounting year of the taxpayer or the worldwide corporate group.

PRRT

PRRT is a federal tax that applies to petroleum projects. PRRT applies at the rate of 40%. PRRT has historically applied only to projects in most offshore areas under the jurisdiction of the Commonwealth of Australia. However, from 1 July 2012, PRRT also applies to onshore projects and the North West Shelf project. PRRT does not apply to projects within the Australia-East Timor Joint Petroleum Development Area (JPDA) (see Section I for further details).

PRRT returns are due annually, for each year ending 30 June, if assessable receipts are derived in relation to a petroleum project. It is not possible to change the PRRT year-end to a date other than 30 June. Quarterly installments of PRRT must also be calculated and paid.

PRRT applies to the taxable profit of a project generated from a project's upstream activities. The taxable profit is calculated by reference to the following formula:

Taxable profit = assessable receipts − deductible expenditures

Generally, because PRRT is imposed on a project basis, the deductibility of expenditure is limited to expenditures incurred for that project, and such expenditures cannot be deducted against other projects of the same entity. However, exploration expenditures may be transferred between projects in which the taxpayer or its wholly owned group of companies has an interest, subject to certain conditions.

A liability to pay PRRT exists where assessable receipts exceed deductible expenditures.

PRRT is levied before income tax and is deductible for income tax purposes. A PRRT refund received is assessable for income tax purposes. A grossed-up deduction against the PRRT liability is available for royalties and excise paid (on onshore projects and the North West Shelf project). Taxpayers can elect to calculate their PRRT liability by reference to a functional currency other than Australian dollars, provided certain requirements are met.

Assessable receipts include most receipts, whether of a capital or revenue nature, related to a petroleum project — e.g., petroleum receipts, tolling receipts, exploration recovery receipts, property receipts, miscellaneous compensation receipts, employee amenity receipts and incidental production receipts.

For projects involving the conversion of gas to liquids, special regulations apply to govern the calculation of the deemed sale price of the sales gas at the point at which it is capable of conversion. It is necessary to calculate a deemed price in terms of the regulations in which no independent sale occurs at the gas-to-liquid conversion point. This price is then applied to determine the assessable receipts subject to PRRT.

Deductible expenditures include expenses of a capital or revenue nature. There are six categories of deductible expenditures:

- Exploration expenditures (e.g., exploration drilling costs, seismic survey)
- General project expenditures (e.g., development expenditures, costs of production)
- Closing-down expenditures (e.g., environmental restoration, removal of production platforms)
- Resource tax expenditure (e.g., state royalties and excise)
- Acquired exploration expenditure
- Starting base expenditure

Acquired exploration expenditure and starting base expenditure are applicable to only onshore projects and the North West Shelf, which transitioned into the PRRT regime from 1 July 2012.

Certain expenditures are not deductible for PRRT purposes — for example, financing-type costs (principal, interest and borrowing costs); dividends; share issue costs; repayment of equity capital; private override royalties; payments to acquire an interest in permits, retention leases and licenses; payments of income tax or good and services tax (GST); indirect administrative or accounting-type costs incurred in carrying on or providing operations or facilities; and hedge expenses. A number of these items are contentious and have been subject to review and recent legislative amendments. With respect to indirect costs, the ATO has released two Practical Compliance Guidelines (PCGs) that deal specifically with the PRRT treatment of:

- PCG 2016/12 — deductibility of general project expenditure relating to the overhead component of time written costs
- PCG 2016/13 — deductibility of general project expenditure

These PCGs apply in relation to expenditure incurred on or after 1 July 2015.

Excess deductible expenditures can be carried forward to be offset against future assessable receipts. Excess deductible expenditures are compounded using one of a number of set rates ranging from a nominal inflation rate (based on GDP) to the long-term bond rate plus 15%, depending on the nature of the expenditure (exploration, general, resource tax, acquired exploration or starting base expenditure) and the year the expenditure was incurred (or deemed to be incurred for projects transitioning to PRRT from 1 July 2012). Such a compounded expenditure is referred to as an "augmented" expenditure.

Where closing-down expenditures and any other deductible expenditures incurred in a financial year exceed the assessable receipts, a taxpayer is entitled to a refundable credit for the closing-down expenditure, which is capped at the amount of PRRT paid by the taxpayer in relation to the project. The amount of this credit or PRRT refund is calculated in terms of specific rules.

As discussed above, onshore projects and the North West Shelf project transitioned into the PRRT from 1 July 2012. Those projects that existed on 2 May 2010 had the option of electing a "starting base" or taking into account expenditures incurred prior to 1 July 2012.

A consolidation regime has also been introduced for PRRT purposes from 1 July 2012. This applies to onshore project interests only.

On 30 November 2016, the government announced a review of the current PRRT system with numerous submissions being provided from both Treasury and Industry since that time. Following his, treasury is continuing to review the PRRT system and is seeking additional consultation on matters raised.

Royalty regimes

For onshore projects, wellhead royalties are applied and administered at the state government level. Wellhead royalties are generally levied at a rate of between 10% and 12.5%[6] of either the gross or net wellhead value of all the petroleum produced.

6 *A 5% royalty rate applies for onshore tight gas in Western Australia (WA). Different rates may apply for geothermal energy.*

Each state has its own rules for determining wellhead value; however, the calculation generally involves subtracting deductible costs from the gross value of the petroleum recovered. Deductible costs are generally limited to the costs involved in processing, storing and transporting the petroleum recovered to the point of sale (i.e., a legislative net back).

For most offshore projects, federally administered PRRT is applied rather than a royalty and excise regime. Royalties continue to apply to onshore projects subject to the PRRT.

Unconventional oil and gas

No special taxes apply to unconventional oil or unconventional gas. However, as discussed above, special regulations apply to the conversion of gas to liquids for PRRT purposes.

C. Capital allowances

In calculating a company's CIT liability, tax depreciation deductions may be available.

Depreciating assets include assets that have a limited effective life and that decline in value over time. Examples of depreciating assets include plant and equipment, certain items of intellectual property (IP), in-house software, and acquisitions of exploration permits, retention leases, production licenses, and mining or petroleum information after 30 June 2001.

A capital allowance deduction equal to the decline in the value of the asset may be determined on a diminishing-value (DV) or a prime-cost (PC) method. The DV method allows a taxpayer to claim a higher decline in value earlier in the effective life of a depreciating asset.

The formula under each method is as follows:

- DV = base value × (days held/365 days) × 200%/asset's effective life.
- PC = asset's cost × (days held/365 days) × 100%/asset's effective life.

A taxpayer can elect to use either the effective life determined by the ATO or to independently determine (self-assess) the effective life of an asset.

A specific concession under the capital allowance provisions relevant to the oil and gas industry is the immediate write-off available for costs incurred in undertaking exploration activities.

From 14 May 2013, the acquisition cost of acquiring a petroleum right that is first used for exploration is immediately deductible only if the right is acquired directly from an issuing authority of the Commonwealth, state or territory. The acquisition cost of petroleum rights otherwise acquired from 14 May 2013 is treated as follows:

- If the right is first used for exploration, the cost will be claimed as a capital allowance over the lesser of 15 years or the effective life.
- If the right is first used for development drilling for petroleum or for operations in the course of working a petroleum field, the cost may be claimed as a capital allowance over the effective life.

However, concessional treatment in the form of a rollover relief is available for exploration "farm-in, farmout" arrangements and interest realignments (see "Farm-in and farmout" in Section G).

The effective life of certain tangible assets used in petroleum refining, oil and gas extraction, and the gas supply industry is capped at between 15 and 20 years, with taxpayers able to self-assess a lower effective life. The ATO is also currently reviewing the effective life of assets used in the oil and gas industry, specifically relating to mining support services. Draft assets lists are expected to be realized during 2018.

D. Incentives

Exploration

Expenditure on exploration is immediately deductible for income tax purposes.

Tax losses

Income tax losses can be carried forward indefinitely; however, the utilization of a carried-forward loss is subject to meeting detailed "continuity of ownership" requirements (broadly, continuity in more than 50% of the voting, dividend and capital rights traced to ultimate shareholders) or "same business test" requirements.

The company tax-loss carryback rules, which applied to tax losses incurred in the 30 June 2013 income year, have been repealed, and therefore tax losses are no longer able to be carried back to previous income years.

Research and development (R&D)

The R&D Tax Incentive provides a nonrefundable 38.5% tax credit or offset to eligible entities that have a turnover greater than AU$20 million and perform R&D activities. The 38.5% tax credit can be used to offset the company's income tax liability to reduce the amount of tax payable. If the company is in a tax-loss position, the tax credit can be carried forward indefinitely, subject to the satisfaction of the ownership and same business tests as required. Smaller companies with annual group turnover of less than AU$20 million (globally) can obtain a refundable 43.5% tax credit, provided they are not controlled by tax-exempt entities. A AU$100 million threshold applies to the R&D expenditure for which companies can claim a concessional tax offset under the R&D Tax Incentive. For any R&D expenditure amounts above AU$100 million, companies will still be able to claim a tax offset at the normal corporate tax rate.

Eligible R&D activities are categorized as either "core" or "supporting" R&D activities. Core R&D activities are broadly defined as experimental activities whose outcome cannot be known in advance and which generate new knowledge. Supporting activities may also qualify if they are undertaken for the purpose of directly supporting the core R&D activities (certain specific exclusions can apply).

Eligible expenditure is defined as expenditure incurred by an eligible company during an income year, including contracted expenditure, salary expenditure and other expenditure directly related to R&D. Generally, only R&D activities undertaken in Australia qualify for the R&D Tax Incentive with some limited scope to claim overseas R&D activities that have a scientific link to Australia.

Eligible companies are companies incorporated in Australia or foreign branches that have a PE in Australia.

To claim the R&D Tax Incentive, claimants must complete an annual registration with AusIndustry (the government body that looks after the technical aspects of the R&D Tax Incentive) and must retain appropriate substantiation of its R&D activities. The annual registration needs to be lodged within 10 months of the end of the income tax year-end.

Foreign-owned R&D

Where IP formally resides in a foreign jurisdiction of an Australian R&D entity (e.g., an overseas parent company), the Australian-based R&D activities may qualify for the 38.5% R&D Tax Incentive, provided that an approved-format R&D contract exists and is undertaken with a country with which Australia has a double tax treaty.

E. Withholding taxes

Interest, dividends and royalties

Interest, dividends and royalties paid to nonresidents are subject to a final Australian withholding tax of 10%, 30% (on the unfranked portion of the dividend to the extent it does not comprise conduit foreign income — see Section B for a discussion on dividends) and 30%, respectively, unless altered by a relevant double tax treaty or a specific exemption applies.

Australia has a comprehensive double tax treaty network that can significantly reduce these taxes. In addition, some recent double tax treaties specifically exclude payments for the use of substantial equipment from the definition of royalty.

Natural resource payments made to nonresidents are subject to a non-final withholding tax. Natural resource payments are payments calculated by reference to the value or quantity of natural resources produced or recovered in Australia. Entities receiving natural resource payments are required to lodge an income tax return in Australia, which includes the non-final withholding tax paid.

Branch remittance tax

Branch remittance tax does not generally apply in Australia; however, care should be taken if dividends are paid from such Australian sourced profits, especially if the shareholder is not a tax resident in a jurisdiction that has a double tax treaty with Australia.

Foreign resident withholding tax and foreign contractor withholding tax

Foreign resident withholding tax and foreign contractor withholding tax (FRWT) of 5% must be withheld from payments made to foreign residents for certain "works" and for related activities in connection with such works in Australia.

Works include the construction, installation and upgrade of buildings, plant and fixtures, and include such works where they relate to natural gas field development and oil field development and pipelines. Related activities cover associated activities, such as administration, installation, supply of equipment and project management.

A variation of, or exemption from, the FRWT rate of 5% may be sought from the ATO in certain circumstances — for example, if the relevant income is not assessable in Australia, or if the rate of 5% is excessive in comparison to the amount of tax that would ultimately be payable, or if the foreign entity has an established history of tax compliance in Australia.

Examples of payments that are not subject to FRWT include:

- Payments that constitute a royalty (a royalty withholding tax may apply depending on the circumstances)
- Payments for activities relating purely to exploration-related activities
- Payments for services performed entirely outside of Australia

Withholding tax from clients of nonresidents doing business in Australia without an Australian Business Number

An entity is required to withhold 47% from a payment it makes to another entity if the payment is for a supply made in the course or furtherance of an enterprise carried on in Australia and the other entity does not correctly quote its Australian Business Number (ABN).

The 47% need not be withheld if the ABN is correctly quoted or if the taxpayer has evidence that the payment is being made to a nonresident for a supply that is not made in carrying on an enterprise in Australia, or if it will be exempt from income tax.

Withholding tax on transactions involving taxable Australian property (TAP)

For contracts entered into on or after 1 July 2017, Australian domestic legislation imposes a 12.5%[7] non-final withholding tax obligation on the purchase of certain TAP assets from foreign residents (see "Capital gains" in Section B for assets that are TAP). The 12.5% withholding tax is on the proceeds payable in relation to the sale (not the profit from the sale). There are a number of exceptions, including real property transactions with a market value less than AU$750,000 (previously AU$2 million). The measures place additional compliance obligations upon purchasers and sellers, both resident and nonresident. Australian resident vendors will need to apply to the ATO for a

7 *A withholding tax rate of 10% applies to contracts that are entered into between 1 July 2016 and before 1 July 2017.*

clearance certificate confirming they are not foreign residents if the value of the property is AU$750,000 or greater (residential property transactions under AU$750,000 are exempt). Other exemptions and variations may apply.

F. Financing considerations

Australia's income tax system contains significant rules regarding the classification of debt and equity instruments and, depending on the level of funding, rules that have an impact on the deductibility of interest.

Thin capitalization measures apply to the total debt of Australian operations of multinational groups (including foreign and domestic related-party debt and third-party debt). The measures apply to the following entities:

- Australian entities that are under foreign control (inward investors).
- Foreign entities that either invest directly into Australia or operate a business through an Australian branch (inward investors).
- Australian entities that control foreign entities or operate a business through an overseas branch (outward investors).

From 1 July 2014, the thin capitalization rules provide for a safe harbor based on 60% of assets (assets less non-debt liabilities, plus or minus some adjustments). This largely approximates to a debt-to-equity ratio of 1.5:1. Interest deductions are denied for interest payments on the portion of the company's debt that exceeds the safe harbor ratio. The thin capitalization rules do not apply to an entity whose debt deductions (and those of its associates) do not exceed AU$2 million. Separate rules apply to financial institutions.

If the entity's debt-to-equity ratio exceeds the safe harbor ratio, interest is still fully deductible, provided the entity can satisfy the arm's-length test. Under this test, the company must establish that the level of debt could be obtained under arm's-length arrangements, taking into account industry practice and specific assumptions required under the tax law.

The maximum allowable debt of an Australian entity may alternatively be determined by reference to a worldwide gearing test of the entity and its associates. The rate for the worldwide gearing test is 100% from 1 July 2014.

The debt/equity classification of financial instruments for tax purposes is subject to prescribed tests under law. These measures focus on economic substance rather than on legal form. If the debt test is satisfied, a financing arrangement is generally treated as debt even if the arrangement could also satisfy the test for equity.

The debt/equity measures are relevant to the taxation of dividends (including imputation requirements), the characterization of payments to and from nonresident entities, the thin capitalization regime, and the dividend and interest withholding taxes and related measures.

Australia does not currently impose interest quarantining. Generally, corporate-level debt deductions may be used to offset all assessable income derived by the borrowing entity, regardless of the source or type of assessable income. However, interest deductions may be disallowed if the related borrowing is directly related to the derivation of certain exempt income (e.g., foreign income derived by a foreign branch).

G. Transactions

Asset disposals

The disposal of an exploration permit, retention lease or production license acquired on or after 1 July 2001 may result in an assessable or deductible balancing adjustment under the Uniform Capital Allowance provisions for income tax purposes. Any gain is assessable and included in taxable income — not just the depreciation previously claimed (i.e., sales proceeds less the written-down tax value). If the sales proceeds are less than the written-down tax value, a deductible balancing adjustment is allowed.

The transfer or disposal of an interest in an exploration permit does not in itself trigger PRRT consequences; a transferor is not subject to PRRT on any consideration received, and the transferee is not entitled to any deduction for PRRT purposes for any consideration given. However, generally the purchaser inherits the vendor's PRRT profile, including undeducted expenditure.

Farm-in and farmout

It is common in the Australian oil and gas industry for entities to enter into farm-in arrangements.

Under an immediate transfer arrangement, the farmer will typically transfer a percentage interest in a permit or license on entry into the agreement, in return for a commitment from the farmee to undertake exploration or other commitments for a period of time or up to a specified amount. A cash payment may also be made to the farmer by the farmee on entering into the arrangement.

Under a deferred transfer arrangement, the farmer will typically transfer a percentage interest in a permit or license after the farmee meets its commitment to undertake exploration (or other commitments) for a period of time or up to a specified amount. A cash payment may also be made to the farmer by the farmee on entering into the arrangement.

The income tax implications for a farmee who enters into a farm-in arrangement on or after 1 July 2001 are determined under the Uniform Capital Allowance provisions. A farmee is deemed to hold a depreciating asset, being the interest in the petroleum permit, from the time the interest is acquired (this can be up front or deferred, depending on the terms of the particular arrangement).

The income tax consequences of farm-in and farmout arrangements can be complex. The ATO has previously expressed its views in two tax rulings (MT 2012/1 and MT 2012/2). In addition, concessional treatment in the form of a rollover relief is available for exploration "farm-in, farmout" arrangements and interest realignments that were adversely impacted by the enacted changes to immediate deductions for exploration (refer to Section C above).

Acquisition costs of a farmee are not deductible for PRRT purposes and, similarly, consideration received by a farmer for a farmout is not assessable for PRRT purposes.

Selling shares in a company (consequences for resident and nonresident shareholders)

A share disposal is generally subject to the CGT regime. Nonresidents who dispose of shares in an Australian or nonresident company are subject to tax in Australia only if the shares are considered to be taxable Australian property (TAP) (see Section B for a discussion of CGT and TAP and Section E for a discussion on withholding tax). Entities that hold, directly or indirectly (via interposed subsidiaries), assets comprising primarily Australian oil and gas exploration permits and production licenses are generally classed as having TAP. However, exceptions to this provision may apply, depending on the company's asset mix.

H. Indirect taxes

Goods and services tax

Introduction

A GST regime applies in Australia. Most transactions that take place within the Indirect Tax Zone (ITZ) (and some from offshore) are subject to GST. This tax, which was introduced in July 2000, is a multistaged value-added tax (VAT) that applies at each point of the supply chain. It is applied at a standard rate of 10%, with GST-free status (zero rated) for qualifying exported products and services and some other specified transactions; and input taxed treatment (exempt) generally applies to financial services and residential housing.

Both Australian resident and nonresident entities engaged in the oil and gas industry may be subject to GST on services and products supplied. Most commercial transactions have a GST impact, and this should be considered prior to entering into any negotiation or arrangement.

Imports and exports

The importation of most goods into the ITZ for home consumption is subject to GST (irrespective of the Australian GST registration status of the importer). GST is typically payable at the time the goods are entered for home consumption in a similar manner to customs import duty (see below). Goods may not be released by the customs authorities until such time as the GST and import duty have been paid. The importation of low- value goods (i.e., less than AU$1,000) into the ITZ is currently not subject to GST. GST will apply to such low-value imports by consumers, in certain situations, from 1 July 2018.

Under certain conditions, importers may register to participate in the GST deferral scheme. This scheme allows the payment of GST on imports to be deferred until lodgment of the entity's Business Activity Statement (BAS) for the tax period in which the import is made. It is at this time that the entity would typically claim input tax credits for the GST payable on the imported goods. The deferral scheme therefore alleviates the cash flow impacts that may otherwise occur if the GST is paid at the time the goods are entered for home consumption. GST is calculated on the *value of the taxable importation*, which includes the value of the goods, the import duty, and the international transport and insurance.

If goods are exported, GST-free status may be obtained. To qualify as GST-free, goods must generally be exported within 60 days of the earlier of consideration being provided or a tax invoice being issued, although this period can be extended by the ATO in certain circumstances. Evidence that indicates the goods have left the ITZ within the required time frame must be retained by exporters.

Registration

The compulsory GST registration threshold is AU$75,000; however, entities below this threshold can choose to voluntarily register for GST.

Nonresident entities are able to register for GST, and GST will apply to taxable supplies made by them. A nonresident may appoint a tax or fiscal representative in Australia (but is not required to do so).

As of 1 July 2016, nonresident entities may be able to access revised administrative concessions regarding the requirement to register for GST in the ITZ. Whether the concessions will apply depends on a nonresident's proposed activities in the ITZ; however, as a guide, a nonresident may not be required to register if it:

- Does not carry on its enterprise through a fixed place in the ITZ
  Or
- Does not carry on, or intend to carry on, its activities for more than 183 days in a 12-month period

A registered entity may recover input tax on "creditable acquisitions," that is, the GST charged on goods and services that a registered entity acquires for creditable purposes. Input tax is claimed through the BAS.

There are both voluntary and compulsory reverse-charge provisions that may apply to both resident and nonresident entities.

Disposal of assets or shares

The disposal of an asset, such as an exploration permit, retention lease or production license, will ordinarily be a taxable supply upon which GST is payable. However, an entity can usually claim input tax credits for acquisitions made in connection with the sale and/or acquisition of the asset(s). Such transactions can also be treated as GST-free going concerns in qualifying circumstances.

A share disposal is ordinarily treated as an input-taxed supply under the Australian GST regime. Thus, although no GST will be payable on the sale of the shares, an entity may be restricted from claiming input tax credits on acquisitions made in connection with the disposal or acquisition of those shares.

Farm-in and farmout

The GST consequences of farm-in and farmout arrangements can also be complex and MT 2012/1 and MT 2012/2 (See "farm-in" discussion in Section G above) include the ATO's views on the GST interactions.

Various supplies are made by the farmer and farmee and depend on whether the arrangement is an immediate or deferred transfer farm-in and farmout. Once these supplies have been identified by all parties, the supplies will be either taxable or GST-free (as a going concern).

Common GST-related issues arising in farm-in and farmout arrangements include:

- Economic mismatch of supplies between the farmer and farmee (on the basis of GST-free and taxable supplies being made by the parties)
- Non-cash consideration
- The valuation of supplies involving non-cash consideration
- GST registration of the parties involved in the arrangement

Import duty

All goods imported into Australia are subject to classification and have the potential to attract customs import duty. Rates of duty are determined by the specific tariff classification of the goods being imported. Import duty for goods other than "excise-equivalent goods" will typically be levied at a rate of either 0% or 5%. The rate of duty is applied to the customs value of the goods, which generally reflects a free-on-board (FOB) value.

Any import duty payable must be paid at the time goods are entered for home consumption.

If duty is payable, opportunities may exist to reduce or remove the tariff imposed. Preferential treatment may be available if goods originate from countries with which Australia has a trade agreement. Alternatively, concessional treatment may be available if substitutable goods are not produced in Australia. Importers should assess import duty implications and opportunities to benefit from treatments well before goods are shipped to Australia.

Subject to limited exceptions, importers are required to lodge an import declaration for all goods being entered into Australia. All goods arriving in Australia from overseas are subject to customs controls, and importers may be required to hold permits or licenses before certain restricted goods can be imported.

Excise-equivalent goods (EEGs), such as petroleum products, alcohol and tobacco, attract excise-equivalent customs duty upon importation into Australia. That is, the import duty reflects the excise duty payable on such goods when produced in Australia. Import duty for EEGs is calculated on quantity rather than value, although in some cases there may be an ad valorum amount of duty payable as well. Most tariff classifications for petroleum products attract a "cents per liter" rate of duty only. Preferential or concessional duty treatments are not applicable to EEGs; however, opportunities to recover amounts paid may exist through duty drawback (where duty-paid goods are subsequently exported) or through a claim for fuel tax credits.

Export duty

There are no duties applied to goods exported from Australia.

Excise duty

Excise duty is applied to some goods manufactured in Australia, including petroleum products, alcohol and tobacco. Excise does not generally apply to exported goods. In the case of crude oil and condensate production from coastal waters, onshore areas, and the North West Shelf project area, the rate of excise duty can range from 0% to 55%, depending on annual production and whether oil is considered old, intermediate or new. The maximum rate for new oil (discovered after 1975) is 30%. In all cases, an excise liability is worked out by applying the relevant crude oil excise rate to the volume weighted average of the realized FOB price. The first 30 million barrels of crude oil and concentrate from a field are excise-free, and for projects that have a PRRT liability, any excise payable is effectively creditable through a grossed-up deduction.

Excise duty on most refined liquid petroleum products is (as of March 2018) AU$0.409 per liter and is subject to biannual indexation, occurring in February and August each year. If excise duty is already paid on goods exported from Australia, it may be recovered through an application for drawback or, if the exported product is fuel, through a claim for fuel tax credits.

Fuel tax credits

"Fuel tax" is the term given to excise duty payable on fuel manufactured or purchased in Australia, or the excise-equivalent customs duty payable on imported fuel. In Australia, entities that acquire fuel for use in a business activity may be entitled to claim fuel tax credits (FTCs) to recover amounts of fuel tax paid.

Before claiming FTCs, it must be established that the fuel for which credits are to be claimed is eligible fuel (i.e., duty-paid). It must also be confirmed that the business activity in which the fuel is to be consumed is an eligible activity and that credits are being claimed at the appropriate rates. In some instances, it may also be necessary to confirm that fuel has been effectively acquired before making a claim for FTCs, particularly where fuel and/or services are supplied under contract.

Importantly, a claim for FTCs can be made based on intended use. FTC entitlements are claimed through the BAS, and entities (or agents) seeking to make a claim must be registered with the ATO for GST. Where actual use of the fuel differs from any claim based on intended use, amendments are made in subsequent BAS submissions.

FTC calculations must be based on the rate of fuel tax applicable at the time fuel was acquired. Various FTC calculation methodologies are available to claimants and should be given due consideration based on individual circumstances.

Stamp duty

Introduction

Stamp duty is a state- and territory-based tax that is generally imposed on specified transactions. Each state and territory has its own stamp duty legislation, which can vary in relation to the types of instrument or transaction on which duty is imposed, the rates of duty, the parties liable to pay duty and the timing for lodgment and payment of duty.

Below, we explain the stamp duty that may be payable with respect to the transfer of petroleum assets.

Stamp duty — transfer of dutiable property

The stamp duty payable on the conveyance or transfer of dutiable property is based on the higher of the consideration paid (including GST and liabilities assumed) and the market value of the dutiable property being transferred at rates that range from 4.5% up to 5.95%.

The definition of dutiable property varies in each Australian jurisdiction, but generally includes land, chattels/goods, certain rights in respect of dutiable property and business assets. Queensland (Qld), Western Australia (WA) and the Northern Territory (NT) are the only Australian jurisdictions that continue to impose stamp duty on the transfer of business assets. The definition of business assets generally includes goodwill, intellectual property, business names, business licenses and supply rights (WA and Qld only). In Qld, business assets also include the debts of a business (if the debtor resides in Qld) and personal property, such as stock/inventory. Chattels (i.e., moveable items of plant and equipment) are subject to duty only if transferred with other dutiable items of property.

The definition of "land" generally includes freehold or leasehold interests in land, mining tenements, fixtures (New South Wales (NSW), WA and the Australian Capital Territory (ACT)) or anything fixed to the land by more than its own weight (Qld, Victoria (Vic), Tasmania (Tas), NT and South Australia (SA)). In WA and Qld, the definition of "land" also includes a pipeline (WA only) and a pipeline license that is administered or issued under the Petroleum Pipelines Act 1969 (WA) or the Petroleum and Gas (Production and Safety) Act 2004 (Qld).

Qld and SA are the only Australian jurisdictions that treat certain petroleum titles as dutiable items of property (not Commonwealth petroleum titles situated in Commonwealth waters). A farm-in concession may be available with respect to farm-in agreements involving exploration tenements (SA) or exploration authorities (Qld).

A liability to pay stamp duty with respect to the transfer of dutiable property may arise at the time of entering into an agreement to transfer dutiable property (NSW, Qld, WA and SA) or at the time the dutiable property is transferred (Vic, Tas, ACT and NT).

Share or unit transfers

Landholder duty may be payable on the acquisition of a 50% or greater interest in a private company or unit trust (the acquisition threshold for a private unit trust in Vic is 20% or more), or the acquisition of a 90% or greater interest in a listed company or unit trust, if the entity directly or indirectly (i.e., through its linked entities/subsidiaries) holds an interest in "land" (as previously defined above) situated within an Australian jurisdiction and the unencumbered value of the land exceeds certain value thresholds. The land value thresholds differ between the Australian jurisdictions: in NSW, Qld and WA, the land value threshold is AU$2 million; in Vic and SA, it is AU$1 million; in NT and Tas, it is AU$500,000; and in the ACT, there is no value threshold. The acquisition of a listed company would not have any stamp duty implications in the ACT. In Qld, landholder duty does not apply to acquisitions of units in private unit trusts, as duty is separately chargeable with respect to trust acquisitions, which are discussed below.

In SA and Qld, the acquisition of units in private unit trust schemes that hold land in SA or any Qld property may still be subject to transfer duty at rates of up to 5.5% in SA, or up to 5.75% in Qld (there are certain exceptions for public unit trust schemes in Queensland and registered managed investment schemes, approved deposit funds and pooled superannuation trusts in South Australia).

Landholder duty is payable at rates that range from 4.5% up to 5.95% based on the unencumbered value of the Australian land (including items fixed to the land) held by the entity that is acquired and its linked entities/subsidiaries, but only to the extent of the interest that has been acquired. In certain Australian jurisdictions, such as WA, NSW and Tas, the landholder duty payable would be based on the gross value of the Australian land and chattels (moveable items of plant and equipment) held by the company and its subsidiaries.

In NSW, Vic, SA, Qld and Tas, there is a stamp duty concession for the acquisition of a 90% or greater interest in a listed landholder. The landholder duty payable in these jurisdictions is limited to 10% of the total duty that would otherwise be payable.

We note that:

- SA will be abolishing the stamp duty payable with respect to the transfer of nonresidential or non-primary production real property situated in SA as from 30 June 2018. There is currently a two-thirds (i.e., 66.66%) stamp duty reduction in respect of the transfer of nonresidential or non-primary real property situated in SA. This would also apply to the transfer of interests in landholding entities that hold nonresidential and non-primary production real property situated in SA. The phasing out of duty on transfers of nonresidential and non-primary production real property would also apply to the transfer of petroleum titles issued under the Petroleum and Geothermal Energy Act 2000 (SA) or transfers of interests in landholding entities that hold such petroleum titles.

Exemptions from stamp duty — transfers between related entities

A corporate reconstruction exemption (CRE) (also known as a Connected Entity Exemption in WA) may be available to exempt the stamp duty payable on the transfer of dutiable property between the members of a corporate group. An exemption from landholder duty may also be available for the transfer of landholding entities within a corporate group.

The members of a corporate group generally include companies and unit trusts (not discretionary trusts), and there is a requirement that the parties to the transaction have at least 90% common ownership and control (either directly or through a common parent entity). In addition, certain pre- and post association requirements may need to be satisfied in order to qualify for an exemption and to ensure that the duty that has been exempted (if a CRE has been approved) is not clawed back.

A CRE may also be available in order to interpose a new holding company or unit trust between the shareholders/unitholders and the members of a corporate group.

An advance ruling may be sought as to whether a CRE would be approved prior to undertaking a transaction.

Stamp duty and registration fees — transfers or dealings in petroleum titles (onshore and offshore)

The stamp duty treatment of transfers or dealings in Australian onshore petroleum titles (i.e., petroleum titles situated within an Australian state or territory or within three nautical miles of the coastline of the state or territory) varies among the Australian states and territories.

Transfers or dealings in onshore petroleum titles may be subject to stamp duty or a registration fee, depending on the relevant jurisdiction. For example, WA exempts from stamp duty any transfers or dealings in onshore petroleum titles. However, WA imposes a registration fee on the transfer or dealings in onshore petroleum titles, calculated at 1.5% of the greater of the consideration and the value of the petroleum title. WA is the only Australian jurisdiction that imposes a registration fee on the transfer or dealings in onshore petroleum titles, while Qld and SA are the only Australian jurisdictions that impose stamp duty on the transfer or dealings in onshore petroleum titles.

Transfers or dealings in offshore petroleum tenements (i.e., tenements situated outside three nautical miles of the coastline of a state or territory, but within Australian Commonwealth waters) are subject to a fixed application fee. The application fee is intended to reflect the administrative costs incurred in undertaking the assessment of the applications by the National Offshore Petroleum Title Administrator (NOPTA).

The application fee for the approval of a transfer of an offshore petroleum title (i.e., a petroleum title situated in Commonwealth waters) is currently set at AU$7,500, and the approval of dealing relating to an offshore petroleum title is also currently set at AU$7,500.

Employment taxes

Employers have an obligation to comply with various employment taxes, including Pay As You Go Withholding from payments of remuneration to residents of Australia, or for work done in Australia by nonresidents. Other significant taxes include fringe benefits tax payable on noncash employee benefits at a rate of 47% and payroll taxes (paid by employers) of 4.75% to 6.85%, in which the rates vary by state.

A statutory employer contribution of 9.5% is not a tax in itself, but it is important to note that it applies to superannuation. This contribution rate will remain at 9.5% until 30 June 2021 and then increase by 0.5 percentage points each year until it reaches 12%. From 1 July 2015, superannuation may be required for nonresident employees working offshore Australia up to 200 nautical miles from Australia's territorial sea baseline. Australia also has compulsory workers' insurance requirements.

I. Other

Timor-Leste and the Joint petroleum development area (JPDA)

Historically, the taxing rights for operations in the JPDA have been split between Timor-Leste and Australia on a 90:10 basis (i.e., 90% is taxed in Timor-Leste, and 10% in Australia). On 6 March 2018, Australia's Minister for Foreign Affairs, the Hon Julie Bishop MP, and Timor-Leste's Minister Assisting the Prime Minister on Boundary Delimitation, His Excellency Mr. Hermenegildo Pereira, signed the Treaty between Australia and the Democratic Republic of Timor-Leste Establishing Their Maritime Boundaries in the Timor Sea (the Treaty). The Treaty has been negotiated between the two governments as a result of the termination and subsequent cessation of the Treaty of Certain Maritime Agreements in the Timor Sea (CMATS) under which the historical 90:10 split was determined.

The Treaty now delineates a permanent maritime boundary between the two countries, as well as addressing the legal status of oil and gas reserves located in the Timor Sea, in particular the Greater Sunrise gas fields.

In summary, the Treaty:

- Establishes a permanent maritime boundary between Australia and Timor-Leste, resulting in a number of offshore petroleum operations transferring from an area of shared Australia and Timor-Leste jurisdiction (i.e., the JPDA) to Timor-Leste's exclusive jurisdiction
- Provides for the cessation of both the Timor Sea Treaty (the TST) and International Unitisation Agreement (the IUA) upon its entry into force
- Creates a special regime for the joint development, exploitation and management of the Greater Sunrise Gas Fields by Australia and Timor-Leste
- Establishes procedures with respect to arbitration
- Sets out transitional measures to provide regulatory certainty and continuity for affected investors with oil and gas interests in the Timor Sea

As part of these transitional measures, the Timor-Leste government has agreed that its arrangements for contractors provisions will provide for "the continuance of the fiscal regime on conditions equivalent to the fiscal regime in place."

This guide does not deal with the tax implications of operating in the JPDA or Timor-Leste.

Foreign Investment Review Board

The federal Government monitors investment into Australia through the Foreign Investment Review Board (FIRB). Government policy generally is to encourage foreign investment, although there are strict controls regarding the purchase of real estate. There are notification and approval requirements depending on the level of investment and the assets in which the investment is made.

Acquisitions of greater than 15% of a company's share capital are also subject to review.

Effective from 1 December 2015, various changes to Australia's foreign investment regime came into force, including changes to thresholds for FIRB approval; new application fees for FIRB applications; higher and wider penalties for nonresidents for breaches of investment approval requirements and third parties, such as agents for their involvement in causing the breach; and new ATO registration requirements for nonresidents holding agricultural land.

Domestic production requirements

There has been significant discussion regarding minimum domestic production requirements, particularly in the context of domestic gas. This landscape is continuing to evolve, and companies that seek to invest in Australia should be aware that there is increasing speculation that a minimum domestic production commitment may be imposed, depending on the location of the project. This has been subject to intense political debate in 2017/2018 with some limited domestic gas reservation policies already in place in certain states.

Foreign exchange controls

There are no active exchange control restrictions on the flow of funds. However, the Financial Transaction Reports Act of 1988 requires each currency transaction involving the physical transfer of notes and coins in excess of AU$10,000 (or the foreign currency equivalent) between Australian residents and overseas residents, as well as all international telegraphic and electronic fund transfers, to be reported to the Australian Transaction Reports and Analysis Centre (AUSTRAC). This information is then available to the ATO, Federal Police, Australian Customs Service and other prescribed law enforcement agencies.

Business presence

Forms of "business presence" in Australia that are typical for the petroleum industry include companies, foreign branches and joint ventures (incorporated and unincorporated). In addition to commercial considerations, the tax consequences of each business are important to consider when setting up a business in Australia. Unincorporated joint ventures are commonly used by companies in the exploration and development of oil and gas projects.

Visas

Australia has very strict immigration rules, and it is critical that anyone moving to Australia, whether for a short-term or long-term stay, enter and remain in Australia holding the correct visa. The appropriate visa will depend on the nature, location and duration of the proposed work and whether an employment relationship exists between the foreign worker and an Australian entity. In the oil and gas context, special consideration must also be given to the type of offshore resources installation or vessel upon which the work will be performed. Sanctions, including fines as well as criminal and civil penalties, may be imposed on employers, and foreign workers may have their visas canceled and subject to exclusion periods if there has been inadequate compliance with Australian immigration rules.

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Azerbaijan's fiscal regime consists of a combination of production sharing agreements (PSAs) and host government agreements (HGAs). In addition, the Law on Application of Special Economic Regime for Export-Oriented Oil and Gas Operations (the Law) came into force on 17 April 2009. The Law applies to export-oriented oil and gas operations carried out by contractors, as well as by subcontractors, as defined in the Law. The Law will be effective for 15 years but may be further extended once this period is over.

- Bonuses — Negotiated bonuses and acreage fees are applicable to PSAs.
- PSA — PSA partner contractors are subject to a profit tax (at a negotiated rate that varies from 20% to 32%) and social fund contributions for local employees. Other potential major payments include bonuses, acreage fees and social fund payments. The PSA partners are exempt from all other taxes, including royalties.

  PSA subcontractors are deemed to earn taxable profit of 20% to 25%, depending on the particular PSA, of the payments received for transactions performed in Azerbaijan. These subcontractors are subject to tax on such profit at the rate of 20% to 32%, resulting in a total withholding tax (WHT) obligation at rates between 5% and 8%. Subcontractors are also liable for social fund payments.
- HGA — Participants are subject only to a profit tax of 27% and social fund contributions for local employees. The participants are exempt from all other taxes. Registered contractors (subcontractors in common terms) are exempt from all types of taxes, except for social fund payments.
- Income tax rate — Tax rates range from 14% (up to AZN2,500) to 25% (above AZN2,500) — the same as in domestic legislation.
- Capital allowances — Capital allowances are calculated in accordance with the tax rules prescribed under the applicable tax regime of PSAs and HGAs and in accordance with the Tax Code of the Republic of Azerbaijan (TCA) for contractors and subcontractors falling under the Law.

B. Fiscal regime

Azerbaijan's fiscal regime consists of a combination of PSAs and HGAs. To become entitled to a special economic regime introduced by the Law, contractors and subcontractors, except for foreign subcontractors that do not have a permanent taxable presence (i.e., a permanent establishment) in Azerbaijan, should obtain a special certificate that will be issued for each contract separately. The certificate will be granted by the respective state authority, generally for a period specified in the contractor's or subcontractor's contract (or an alternative document). However, the period may not be longer than the validity period of the Law. The legislation in Azerbaijan applies to ownership of all petroleum resources existing in a natural state in underground and surface strata, including the portion of the Caspian Sea within the jurisdiction of the state that vested with Azerbaijan.

The State Oil Company of the Azerbaijan Republic (SOCAR) has been given the authority to control and manage the country's petroleum resources. Several oil consortia, with participation from a number of major oil companies, are engaged in exploration and production activities in the Azerbaijani sector of the Caspian Sea and in onshore exploration. All consortia were created on the basis of PSAs.

Currently, HGAs apply to oil and gas pipeline projects. The Main Export Pipeline (Baku-Tbilisi-Ceyhan) (MEP) and the South Caucasus Pipeline (SCP) activities are governed by the respective HGAs.

There are substantial differences between the general tax legislation and the tax regimes of the existing PSAs, HGAs and the Law. Generally speaking, PSAs, HGAs and the Law have negotiated taxes that provide for substantial relief to investors, while those operating outside the abovementioned agreements must pay the whole range of standard Azerbaijani taxes under the statutory tax regime.

Production sharing agreements

A range of taxes, duties and bonuses are applicable to PSAs. The taxation of contractor parties and subcontractors are considered separately below.

Contractor parties

Oil and gas contractors (PSA partners) are subject to profit tax and social fund contributions for local employees. Other major payments include bonuses and acreage fees. The PSA parties are exempt from all other taxes, including royalties.

Profit tax

Under the PSAs currently in effect, contractor parties carrying out business in Azerbaijan in connection with petroleum operations are subject to tax on profit. The profit tax rate is negotiated and varies from 20% to 32%.

Taxable income is calculated in accordance with internationally accepted accounting practices in the petroleum industry, rather than in accordance with Azerbaijani statutory accounting procedures. In calculating taxable income, contractors get a capital allowance for capital expenditure based on the tax depreciation rules prescribed by PSAs.

Losses incurred by contractor parties to PSAs during the period of exploration are deductible once production starts. Loss carryforward provisions (including how long losses may be carried forward) vary between different PSAs.

Activities that are not connected with hydrocarbon activities in Azerbaijan or relevant contract areas are deemed to be outside the scope of PSAs and the related protocol tax regimes. If a company is engaged in both hydrocarbon and non-hydrocarbon activities, separate accounting books in accordance with statutory rules must be maintained to reflect income and losses generated from the non-hydrocarbon activities. The operating companies under the PSAs are not taxable and allocate income and expenses to contractor parties in proportion to their participating interests in the PSAs.

Social charges

Under the PSAs, contractor parties are permitted to employ personnel as required for the purpose of carrying out their operations. There may be requirements to give preferences, as far as they are consistent with the operations, to employ citizens of Azerbaijan within the framework of the overall quotas.

Contractor parties are required to make contributions to the Social Insurance Fund of 22% of the gross local payroll. These contributions are made at the expense of the employer. A further 3% of employees' salaries is withheld from local employees and paid to the same Social Insurance Fund.

Bonus payment and acreage fees

The terms of the bonus payment and the size of the bonus are negotiated and vary for each individual PSA. Existing PSAs call for the bonus to be paid in three installments, connected with the stages of the agreements.

Starting with the second consortium agreement signed, an acreage fee is payable for the contract area during the exploration period and an additional exploration period. For some PSAs, the range of the acreage fee is US$1,200 to US$2,000 per square kilometer (km^2).

Royalties

Under the existing PSAs, the contractor parties are not subject to royalties for extraction of hydrocarbon resources in Azerbaijan.

Subcontractors

Both Azerbaijani legal entities and foreign legal entities are treated as subcontractors to PSAs. Azerbaijani legal entities are subject to tax in accordance with the general taxation rules. Registered foreign subcontractors, on the other hand, are generally subject to WHT (as described below), as well as social fund payments in the same manner as contracting parties. The sale of goods or equipment to which title is transferred outside Azerbaijan, and the provision of services outside of Azerbaijan, should not be subject to the WHT.

Withholding taxes

Foreign subcontractors that carry on business in Azerbaijan in connection with hydrocarbon activities are deemed to earn a taxable profit of 20% to 25% of the payments received in respect of transactions performed in Azerbaijan (depending on the particular PSA). These subcontractors are subject to tax on profits at a rate of 20% to 32%, resulting in a total WHT obligation at the rates of 5%, 6.25%, 7.5% or 8% (depending on the particular PSA) of the gross contractual payment.

Some of the existing PSAs envisage that every person making a payment to foreign subcontractor carrying on business in Azerbaijan and not registered for tax purposes in Azerbaijan shall withhold tax at a rate of 10% from such payments and shall pay such tax to the State budget.

WHT on foreign subcontractors that sell goods should apply to only a markup charged on such goods. Under certain PSAs, in which no markup is indicated, the tax may apply to the gross sales price.

However, under some of the existing PSAs, certain foreign subcontractors are subject to profit taxation under the domestic law. Such foreign subcontractors include those registered in Azerbaijan for tax purposes, the ones working after approval of the development and production stage of the agreement, or those selling goods without indicating a markup on their sales.

Social charges

Just as contracting parties may do, subcontractors are allowed to employ personnel as required for the purpose of carrying out their operations. There may be requirements to give preferences, as far as they are consistent with the operations, to employ citizens of Azerbaijan within the framework of the overall quotas.

Subcontractors are required to make contributions to the Social Insurance Fund of 22% of the gross local payroll. These contributions are made at the expense of the employer. A further 3% of employees' salaries is withheld from local employees and paid to the same Social Insurance Fund.

Other benefits

Export and import regulations

Each contractor or subcontractor is entitled to import and re-export (free of any taxes) machinery, equipment, fixed assets, goods, works and services for use in petroleum operations. However, customs processing fees are payable. A customs duty exemption certificate must be obtained from the customs authority in connection with the PSA.

VAT

Contractors and subcontractors are "exempt with credit" from value-added tax (VAT) (i.e., a 0% rate is applied) in connection with petroleum activities on all:

- Goods, works and services supplied to or by them
- Exports of petroleum
- Imports of goods, works and services

Any supplier of works and services (including subcontractors) to each contractor may treat these supplies as being exempt from VAT with credit. A VAT exemption certificate must be obtained from the relevant tax authority in connection with the PSA.

Tax residency rules for individuals

Local employees are generally subject to taxation under the Azerbaijani domestic tax regime, whereas most existing PSAs separately address the issue of expatriate taxation.

Normally, an expatriate employee of an operating company, a contractor party, an affiliate of a contractor party or a foreign subcontractor who is present in Azerbaijan on "ordinary business" becomes a tax resident in the event that they spend more than 30 consecutive days in Azerbaijan in a calendar year. Income earned after the 30th day is taxable in Azerbaijan. Individuals spending fewer than 30 consecutive days but more than 90 cumulative days in Azerbaijan in a calendar year are also treated as tax residents, and income earned after the 90th day becomes taxable. Rotating employees and foreign employees who have a primary place of employment in Azerbaijan qualify as tax residents if they spend more than 90 cumulative days in Azerbaijan in a calendar year, and they are taxable from the first day of their presence in Azerbaijan.

Penalties

In general, penalties applicable to contractor parties and subcontractors under the PSAs tend to be less strict than those provided for by the general domestic legislation. One of the typical penalties applied is interest for late tax payments at the London Interbank Offered Rate (LIBOR) plus 4%.

Host government agreements

Currently, HGAs apply exclusively to oil and gas pipeline projects. MEP and SCP activities are governed by the respective HGAs. A range of taxes and duties is applicable to HGAs. The taxation of participants and contractors is considered separately below and on the next page.

Participants

Participants (the HGAs' partners) are subject to a profit tax at 27% and social fund contributions for local employees. The participants are exempt from all other taxes.

Profit tax

Profit tax may apply to all participants (i.e., companies investing in the pipelines), although actual or deemed tax treaty relief may protect the parties from taxation in Azerbaijan. Profit tax applies individually to each participant.

The profit tax rate is fixed at 27% in the Azerbaijan HGA and is based on the prevailing statutory rate in effect on the date of signature of the agreement.

Tax depreciation is available for expenditure of a capital nature. In addition, tax losses of a MEP and SCP participant may be carried forward without limitation to the subsequent years of assessment.

Social charges

Participants (HGA partners) are allowed to employ personnel as required for the purpose of carrying out their operations. Participants are required to make contributions to the Social Insurance Fund of 22% of the gross local payroll. These contributions are made at the expense of the employer. A further 3% of the employees' salaries is withheld from local employees and paid to the same Social Insurance Fund.

Both Azerbaijani legal entities and foreign legal entities are considered as contractors (subcontractors) to the HGAs. Registered contractors are allowed to employ personnel as required for the purpose of carrying out their operations, and they are exempt from all types of taxes except for social fund payments (which apply in a similar manner as for the participants).

Contractors are required to make contributions to the Social Insurance Fund of 22% of the gross local payroll. These contributions are made at the expense of the employer. A further 3% of the employees' salaries is withheld from local employees and paid to the same Social Insurance Fund.

Other benefits

Export and import regulations

The HGAs allow for import and re-export (free of any taxes) of machinery, equipment, fixed assets, goods, works and services for use in HGAs' operations. However, customs processing fees are payable. A customs duty exemption certificate must be obtained from the customs authority in connection with the HGAs' operations.

VAT

Participants and contractors are exempt with credit from VAT (i.e., a 0% rate is applied) in connection with the HGAs' activities on all:

- Goods, works and services supplied to or by them
- Imports of goods, works and services

Additionally, any supplier of works and services (including contractors) to each participant may treat those supplies as being exempt with credit from VAT. A VAT exemption certificate must be obtained from the relevant tax authority in connection with the HGA operations.

Tax residency rules for individuals

Special residency rules apply for expatriate employees of the participants and contractors. Specifically, a foreign individual who spends more than 182 days in a calendar year in Azerbaijan is considered to be a tax resident. Residents are liable to pay personal income tax exclusively on income received from Azerbaijani sources.

The Law

The privileges set out next are envisaged under the special economic regime established by the Law.

Profit tax

Contractors have an option of paying profit tax at 5% of total payments (without any expense deductions) received from the qualifying activity. Alternatively, contractors may choose to be subject to profit tax on such activity under the basic rules established by the TCA. If a contractor chooses to pay profit tax specified by the TCA, any future increases in the tax rate will have no effect on the contractor, because it will continue paying the tax at the rate valid on the date when the aforesaid certificate was issued.

All payments made to foreign subcontractors (legal entities only) by contractors or other subcontractors will be subject to WHT at a rate of 5%. Payments made to foreign subcontractors that are physical persons are subject to WHT in the manner specified by the TCA. Local subcontractors (both legal entities and individuals) shall also pay their respective taxes in accordance with the TCA.

Withholding tax

No WHT applies to the payments made by contractors and foreign subcontractors for dividends and interests.

Nonresident subcontractors are not subject to the net profit repatriation tax at the source of payment by their permanent establishments.

VAT

Goods (works and services) exported by contractors from Azerbaijan are subject to VAT at a 0% rate.

Income tax

Regarding contractors' and subcontractors' employees, foreign and stateless persons directly employed in Azerbaijan, as well as Azerbaijani citizens, shall be subject to income tax in accordance with the TCA.

Property tax and land tax

Contractors are exempted from both property tax and land tax.

Any other taxes envisaged by the TCA but not covered by the Law should be applied in the manner specified by the TCA.

Customs regime

Contractors and subcontractors are exempt from customs duties and VAT on goods (works and services) imported to, or exported from, Azerbaijan. Irrespective of the value of imported or exported equipment and materials, contractors and subcontractors shall pay AZN275 of customs collections for each customs declaration.

Currency regulation regime

Contractors and subcontractors may open, keep and use AZN and foreign currency accounts at banks within as well as outside Azerbaijan. Contractors must inform the relevant Azerbaijani authorities about the opening and closing of bank accounts outside Azerbaijan. Moreover, contractors and subcontractors may convert funds received in AZN into foreign currency, and, as such, freely transfer these funds outside Azerbaijan, subject to making tax and other mandatory payments.

The Law also imposes the following "local content" type requirement:

Use of local manpower regime

Unless export-oriented oil and gas operations are to last for less than six months, within one year from the day of obtaining the certificate, at least 80% of contractors' and subcontractors' employees represented at all organizational hierarchies and management bodies shall be Azerbaijani citizens. However, in certain cases, a relevant state authority shall grant permission to contractors and subcontractors to employ Azerbaijani citizens in different proportions.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Capital allowances are available to contractors (PSAs) and participants (HGAs). Allowances are calculated in accordance with the tax rules prescribed by the relevant agreements.

D. Incentives

Not applicable.

E. Withholding taxes

WHTs are specific to PSAs. The details are given in Section B.

F. Financing considerations

There are no specific issues related to financing.

G. Transactions

Participation interests in PSAs and HGAs, and shares in companies that hold an interest in PSAs and HGAs, may be sold. The transaction mechanisms and the tax consequences of any sales depend on the provisions of the particular PSA or HGA.

H. Indirect taxes

Import duties and export duties

Each contractor or subcontractor under a PSA or participant or contractor under an HGA is entitled to import and re-export (free of any taxes) machinery, equipment, fixed assets, goods, works and services for use in respect of petroleum operations. A customs duty exemption certificate must be obtained from the customs authority.

VAT

Contractors and subcontractors are exempt with credit from VAT (i.e., a 0% rate is applied) in connection with petroleum activities on all:

- Goods, works and services supplied to or by them
- Exports of petroleum
- Imports of goods, works and services

Additionally, any supplier of works and services (including subcontractors) to each contractor may treat those supplies as being exempt with credit from VAT. A VAT exemption certificate must be obtained from the relevant tax authority in connection with the PSA.

I. Other

Issues relevant to PSAs, HGAs and the Law are discussed in Section B.

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

- Corporate income tax (CIT) rate – 46%[1]
- Capital gains tax (CGT) rate – n/a
- Branch tax rate – n/a

Withholding tax (WHT):

- Dividends – n/a
- Interest – n/a
- Royalties – n/a
- Management fees – n/a
- Branch remittance tax – n/a

Net operating losses (years):

- Carryback – n/a
- Carryforward – indefinitely[2]

Bahrain provides a free, open and transparent environment for businesses and has a globally competitive, value creation story that focuses on sustainability, skills and good governance.

Although major industries, such as oil, gas, aluminum and others connected with the infrastructure, are usually majority-owned by the Government, there is an increasing trend toward privatization, and no industry is closed to foreign investors.

To carry out any commercial activity in the Kingdom of Bahrain, a legal vehicle should be established in accordance with the Bahrain Commercial Companies Law No. 21 of 2001.

Foreign investors are able to establish a 100% foreign-owned entity in Bahrain under certain conditions. However, for some business activities (e.g., trading), there is a limitation on foreign ownership, so a local partner would be required.

1 *Only applicable only to hydrocarbon companies obliged to pay tax in Bahrain.*
2 *Only applicable to hydrocarbon companies obliged to pay tax in Bahrain.*

B. Fiscal system

Corporate tax

There are no corporate taxes in Bahrain except for the levy of income tax on the profits of companies engaged in the exploration, production or refining of crude oil and other natural hydrocarbons in Bahrain, which is levied at a rate of 46%.

Taxable income for oil companies is net profits, consisting of business income less business expenses.

Reasonable business expenses are deductible for tax purposes. This includes administrative, overhead and establishment expenses, interest, royalties, rental, contributions, remunerations, rewards for services rendered by others, and pension or other plans established for the benefit of the persons rendering the services.

Trading losses of oil companies may be carried forward indefinitely. Loss carryback is not permitted.

Personal income tax

There are no personal income taxes in Bahrain.

Capital gains tax

There is no capital gains tax in Bahrain.

VAT, excise duties and other indirect taxes

Currently, there is no value-added tax (VAT) or goods and services tax (GST) in Bahrain except for the following:

- Hotel, short-term lease apartment rents and certain restaurants are subject to a 10% tourism levy on the gross income
- 12% sales tax on gasoline included in the price

However, Bahrain has signed the Gulf Cooperation Council (GCC) VAT framework agreement in relation to the implementation of VAT in the GCC region (including Bahrain) starting in 2018. The standard VAT rate is to be 5%. While VAT has already been introduced in the Kingdom of Saudi Arabia and the United Arab Emirates from 1 January 2018, Bahrain is expected to introduce VAT in the second half of 2018.

Further, Bahrain has implemented excise tax on 30 December 2017 pursuant to the GCC's unified law on selective excise taxes. The following goods are subject to excise tax in Bahrain at the noted tax rate:

- Soft drinks are subject to 50%.
- Cigarettes and energy drinks are subject to 100%.

Withholding tax

There are no withholding taxes in Bahrain.

Zakat (religious wealth tax)

Zakat is not levied in Bahrain.

Land registration fee

There is generally[3] a 2% land registration fee payable to the Government of Bahrain on the transfer of real property. If relevant registrations are completed at the Bahraini Survey and Land Registration Bureau (SLRB) within the first two months following the transaction finalization with the notary public, a discount applies, lowering the overall registration fee to 1.7%.

3 *Subject to certain specific exemptions, e.g., where title to property is transferred by donation, where the title to property is transferred to the Government of Bahrain, where the purchase of a residential property by an individual is subject to a mortgage from Eskan Bank and the value of the property does not exceed the mortgaged amount, and other exemptions similar to these.*

Payroll tax

There is no payroll tax in Bahrain.

Advance tax ruling

Advance tax rulings are not available in Bahrain.

Transfer pricing

Bahrain does not have any transfer pricing rules. However, in principle, transactions between related parties should be at arm's length.

Customs duties

The GCC countries (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates) announced the unification of customs duties, effective from 1 January 2003.

There are no customs tariffs on financial transactions or trade in locally manufactured goods between GCC Member States where the products have at least 40% local value-added content. A certificate of origin may be issued by the Bahrain Chamber of Commerce and Industry as proof of the goods' origin.

Bahrain has been a member of the World Trade Organization (WTO) since January 1995 and signed General Agreement on Tariffs and Trade (GATT) in December 1993. Bahrain applies its customs tariff according to the codes issued by the World Customs Organization (WCO). The following are the broad categories applicable to customs duty:

- 0% duty — basic food items (e.g., rice, vegetable, fruits, fresh fish, meat), books and magazines
- 5% duty — all other imported items, such as clothes, cars, electronics and perfumes and frozen food items
- 20% duty — some paper and aluminium products
- 100% duty — tobacco and tobacco-related products:
  - These are also evaluated based on the quantity or weight, and the higher value is taken into consideration for duty.
- 125% duty — alcoholic beverages

Municipality tax

A municipality tax is payable by individuals or companies renting property in Bahrain. The rate of the tax varies for unfurnished, furnished residential property and commercial property; rates vary from 7% to 10% depending on the type of rental agreement:

- Rented commercial building — 10% of rent
- Rented unfurnished residential building — 10% of rent
- Rented furnished residential building:
  - Owner pays electricity, water and municipal tax — 7% of rent
  - Tenant pays electricity, water and municipal tax — 7.5% of rent

Some landlords include the tax and utility costs when quoting the rental amounts.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Social insurance

The social insurance scheme is governed by the Social Insurance Organization (SIO). It is mandatory to register all employees, once employed by a Bahraini entity, with the SIO and pay social contributions.

Every January, an employer is required to update salary records for employees registered with the SIO.

Whenever an employee joins or leaves an entity, the entity must update its SIO records. The SIO will calculate the amount to be remitted monthly, and the employer is required to remit the same by the stipulated date.

The deduction is made from basic wages and recurring constant allowances as a percentage, and this is then appropriated for social insurance and pension.

The basis for the calculation of social insurance contributions cannot exceed BHD4,000 per month (i.e., if the salary exceeds BHD4,000 per month, the contributions will be calculated only on BHD4,000).

Set out next is an overview of social security contributions and benefits applicable in Bahrain.

Contribution	Rate (%)
For Bahrainis	
Social insurance contributions (pension fund)	
Employer's contribution	9%
Employee's contribution	6%
Insurance against employment injuries	
Employer's contribution	3%
Unemployment insurance	
Employee's contribution	1%
For expatriates	
Insurance against employment injuries	
Employer's contribution	3%
Unemployment insurance	
Employee's contribution	1%

End-of-service benefit

At the completion of their employment contract in Bahrain, expatriate employees are entitled to an end-of-service benefit that is calculated on the following basis:

- Half a month's salary for every year of service for the first three years
- One month's salary for each subsequent year

D. Other levies

Foreign workers levy

Employers have to pay fees in order to obtain employment visas for their employees. Currently, the fee for a two-year employment visa is BHD200. All private and public companies are required to pay a monthly levy with respect to each expatriate that is employed. The levy is charged at a rate of BHD5 per employee for the first five expatriate employees and BHD10 for each expatriate employee thereafter. Further, since January 2015, an additional fee of BHD72 for health insurance when issuing/renewing a visa for an expat has been introduced. This fee may not be applicable if the employer provides compulsory health insurance for the employee.

E. Foreign-exchange controls

There are no exchange control restrictions on converting or transferring funds. Furthermore, Bahrain has no withholding or thin capitalization rules in relation to the financing arrangements in Bahrain.

F. Double tax treaties

To date, Bahrain has signed double tax treaties with 44 jurisdictions, 42 of which are in force. In addition, Bahrain has initialed agreements with Guernsey, Spain, Switzerland and Liechtenstein and is currently in negotiations with Hong Kong, Jersey, Latvia and Kyrgyzstan.

Bahrain double tax treaties

Bahrain has entered into double tax treaties with many jurisdictions, namely Algeria, Austria, Barbados, Belarus, Belgium, Bermuda, Brunei Darussalam, Bulgaria, China (mainland), Cyprus, the Czech Republic, Egypt, Estonia, France, Georgia, Hungary, Iran, Ireland, the Isle of Man, Jordan, Korea (South), Lebanon, Luxembourg, Malaysia, Malta, Mexico, Morocco, the Netherlands, Pakistan, the Philippines, Portugal, Seychelles, Singapore, Sri Lanka, Syria, Sudan, Tajikistan, Thailand, Turkey, Turkmenistan, the United Kingdom, Uzbekistan and Yemen.

Furthermore, Bahrain has signed a tax treaty with Bangladesh, but this treaty is not yet in force.

Bahrain has also initiated discussions on entering tax treaties with Guernsey, Hong Kong, Jersey, Kyrgyzstan, Latvia, Liechtenstein, Spain and Switzerland.

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Tax regime applied to this country

☐ **Concession** ☐ Royalties ☐ Profit-based special taxes ☐ Corporate income tax	■ **Production sharing contracts** ☐ **Service contract**

A. At a glance

The tax and legal regime applicable to oil companies operating in Benin depends on the date on which the petroleum contract was signed. Petroleum contracts signed with the Beninese Authorities before 17 October 2006 are governed by the Petroleum Code dated 13 April 1973 (Order No. 73-33).

This Code only provides for a concession regime. Oil companies operating under the 1973 regime had the opportunity to opt into the new 2006 regime (this option expired in November 2007).

On 17 October 2006, a new Petroleum Code was issued by the Beninese Authorities (Law No. 2006-18). In addition to the existing 1973 concession regime, this new Petroleum Code introduced production sharing contracts (PSCs) and other types of contracts used in the petroleum sector.

Fiscal regime

The fiscal regime applicable to the petroleum industry is provided for by the Beninese Tax Code, the 2006 Petroleum Code or the 1973 Petroleum Code (as applicable) and the agreement concluded between the hydrocarbons contractor and the Beninese Authorities.

The main taxes applicable in the petroleum sector are:

- Under the Petroleum Code of 1973:
  - Fixed fees depending on the type of agreement concluded with the Beninese Authorities
  - Royalty
  - Surface fees
  - Income tax on gross profit at a rate between 50% and 55%
- Under the Petroleum Code of 2006:
  - Fixed fees depending on the type of agreement concluded with the Beninese Authorities
  - Royalty
  - Surface fees
  - Income tax with a cap of 45%, with the tax rate depending on the categories of hydrocarbon and operating conditions

Legal regime

Under the Petroleum Code of 1973, hydrocarbon contractors are required to set up a Benin subsidiary in order to hold a petroleum title.

The Petroleum Code also provides that the exploitation of hydrocarbons is based on a concession regime. Under this regime, the Beninese Authorities grant to a hydrocarbon contractor or a consortium the exclusive right to prospect or research for a maximum of nine years. Where there is a discovery, the Beninese Authorities may grant an exploitation permit for production. In return, the hydrocarbon contractor or the consortium pays royalties and taxes to the state of Benin.

Three types of permits are provided for under the Petroleum Code of 1973:

- A prospecting authorization: This allows its owner to perform investigations from the surface with potential use of geophysical and geochemical methods to obtain evidence of hydrocarbons. The prospecting period is nine years, with an initial period of three years and two renewals of three years each.
- A permit for research (also called an "H permit"): This allows its owner to perform surface or deep work to obtain further evidence regarding the operating conditions and industrial use and to conclude on the existence of exploitable deposits. The permit for research has a maximum term of nine years, with an initial period of three years and two renewals of three years each.
- A concession for hydrocarbon exploitation: Only the holder of a valid research permit can obtain this. It allows its owner to extract hydrocarbons. The concession period is 25 years, which may be extended for an additional 10-year period.

The Petroleum Code of 2006 has introduced the possibility of using PSCs. The Code also provides that the state of Benin can conclude all kinds of contracts in use in the international oil industry.

The 2006 Code supersedes the 1973 Code provisions concerning prospecting, research and exploitation of hydrocarbons, but prospecting authorization is now limited to three years.

The obligation to establish a Beninese subsidiary to hold the petroleum title is enforced by the new Code.

B. Fiscal regime

Hydrocarbon contracts signed before the publication of the Petroleum Code of 2006 remain governed by the Petroleum Code of 1973. Until November 2007, oil companies under the 1973 regime could opt for the new regime provided by the Petroleum Code of 2006.

Main taxes under the Petroleum Code of 1973

Fixed fees

The following table indicates the fixed fees due, depending on the petroleum license required:

Hydrocarbons prospecting authorization	XOF2.5m
Issuance of an H permit	XOF4m
Renewal of an H permit	XOF4m
Provisional authorization for exploiting hydrocarbons	XOF5m
Issuance or renewal of petroleum concession	XOF10m
Authorization of hydrocarbon pipeline transportation	XOF2m

Surface fees

The surface fee is an annual tax based on the surface allocated to perform petroleum activities. The following table summarizes the surface fees applicable:

H permit	XOF12.5 per hectare during the first period XOF25 per hectare for the following periods
Concession for hydrocarbons exploitation	XOF375 per hectare during the first three years XOF750 per hectare for the following years

The surface fee for temporary exploitation of an oil field is XOF300 per hectare.

Proportional royalty on hydrocarbons

This royalty is proportional to the initial value of the hydrocarbon fields and is determined as follows:

- 12.5% for liquid hydrocarbons
- 10% for gas hydrocarbons

The value used is the price set at oil wells, after their cleaning out. Oil used by the producing company, gas flaring and reinjected gas are not subject to this royalty charge.

Income tax

Hydrocarbon contractors are subject to income tax on research and exploitation activities. The income tax rate is negotiated in the convention concluded between the contractor and Beninese Authorities. However, for the holders of a concession for hydrocarbon exploitation, the income tax rate must be between 50% and 55% of the gross profit.

The Benin Financial Act of 1999 has fixed the income tax rate at 55% for research, exploitation, production and sale of hydrocarbons. In principle, the taxable gross profit is defined as total revenues less total expenses. In the case where special conditions on the determination of the taxable gross profit and its basis are specified in the petroleum concession agreement (PCA), the provisions of the Tax Code should be applied only if these provisions are not changed by the PCA. Moreover, the Petroleum Code of 1973 obligates the hydrocarbon contractor to provide annually two certified copies of its balance sheet, profit and loss account, auditor's report and board meeting report to the director of mines, geology and hydrocarbons.

Main taxes under the Petroleum Code of 2006

The Petroleum Code of 2006 has modified the tax legislation of petroleum contracts, as set out next.

Fixed fees

Fixed fees are due on the following:

- Granting of a prospecting authorization
- Issuance and renewal of an H permit
- Issuance and renewal of an exploitation permit
- Provisional authorization for exploiting hydrocarbons
- Authorization of hydrocarbon pipeline transportation

Annual surface fees

A fixed surface fee is due for research and exploitation permits.

Royalty *ad valorem*

This royalty is proportional to the value of the hydrocarbons at the wellhead. The rate of this royalty is negotiated in the petroleum contract and will depend on the nature of hydrocarbons and the operating conditions. However, the minimum rate is 8%.

Oil and gas that are either consumed for direct production needs or reinjected into the field or lost, together with related substances, are excluded from the calculation of the taxable basis for the ad valorem royalty.

Income tax

Hydrocarbon contractors are subject to income tax on research and exploitation activities. The income tax rate is negotiated in the convention concluded between the contractor and Beninese Authorities. However, this rate is capped at 45%.

For the holders of concessions of hydrocarbon exploitation, the income tax rate is between 35% and 45%.

In the case of a PSC, the income tax due by the contractor is deemed to be included in the profit oil received by the state (which will then pay the income tax).

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Incentives

Tax incentives

Article 106 of the Petroleum Code of 2006 provides that the permit holders and their subcontractors are exempt from all duties and taxes during:

- The research period, except for property taxes on residential premises, surface fees, road tax and the fixed fees on granting authorizations and permits
- The exploitation period, except for the ad valorem royalty and income tax

Moreover, hydrocarbon contractors are exempted from paying the "patente," a specific business tax for which the value depends on the location and the activities of the taxpayer.

Customs incentives

Pursuant to Article 7 of Order No. 73-34 and Article 108 of the Petroleum Code of 2006, mineral substances subject to concessions are exempt from customs duties (export duties). The petroleum agreement provides that hydrocarbon contractors and their subcontractors may benefit from exemptions from duties and taxes on imported equipment, exploitation materials and machines.

These exemptions are negotiated by the hydrocarbon contractor while concluding the agreement with the Beninese Authorities.

VAT

Value-added tax (VAT) is not included in the Petroleum Code of 2006. However, in practice, hydrocarbon contractors may benefit from VAT exemptions on activities strictly related to petroleum operations. This exemption is negotiated by the hydrocarbon contractor while concluding the petroleum agreement with the Beninese Authorities.

D. Withholding taxes

Withholding taxes (WHT) are not dealt with under the Petroleum Code. According to the provisions of the General Tax Code, amounts paid to nonresident companies as compensation for services of any kind provided or used in Benin are nonetheless subject to WHT at a rate of 12% — but PSCs may be exempt from WHT from certain types of subcontractors.

E. Registration duties

The Petroleum Codes do not provide for specific rules on registration duties.

F. Capital allowances

The Petroleum Codes do not include capital allowances. These are taken into account while negotiating the petroleum agreement with the Beninese Authorities.

G. Financing considerations

There is no specific issue or limitation concerning the financing of hydrocarbon activities.

H. Transactions

The Petroleum Codes do not include any specific taxation on the transfer of an interest in petroleum contracts. However, registration duties may apply.

I. Foreign exchange controls

According to Article 109 of the Petroleum Code of 2006, permit holders and their subcontractors are allowed to:

- Pay in foreign currency, in full or in part, wages, reimbursements and other indemnities
- Open, keep and use bank accounts in foreign currencies in Benin and abroad, and accounts in local currency in Benin
- Directly pay abroad, in foreign currency, foreign subcontractors for the acquisition of equipment and supplies of services related to the petroleum operations
- Receive, transfer and keep abroad and freely dispose of all funds, including but not limited to, all payments received for the exportation of hydrocarbons and any payments received from the government
- Obtain from abroad all financing required for the petroleum operations
- Buy local currencies required for the petroleum operations and convert into foreign currency all local currencies in excess of the immediate domestic needs in accredited banks or exchange offices

Compliance requirements

- The holder of a petroleum title is required to keep, in French and in conformity with local legislation, accounting information separated from any other activity not covered by the petroleum contract.

Brazil

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- □ **Service contract**

A. At a glance

Fiscal regime

The Brazilian fiscal regime that applies to the oil and gas industry consists of corporate income tax (CIT) and Government and third-party takes. Government and third-party takes vary depending on the type of contract.

In Brazil, there are two main types of contract:

- Concession contract (CC) — under this contract, the assessment is done through the allocation of scores and weights, considering the signature bonus, the minimum exploratory program and the national content.
- Production sharing contract (PSC) — under this contract, the winner of the bid is the entity that offers the greater volume of oil to the Government. Introduced in 2010, this model is applicable for exploitation of pre-salt and other strategic areas. On 21 October 2013, the first bidding round for the Libra block (pre-salt area) took place. Both second and third bidding rounds occurred on 27 September 2017, and the fourth bidding round is schedule to take place in June 2018 (see Section I).

According to Article 20, paragraph 1 of the Brazilian Constitution, the states, Federal Districts, municipalities, as well as the direct administration entities of the federal Government, are entitled to the participation in the results or financial compensation for the exploration of the following: oil, natural gas, water resources for purposes of electricity generation and other mineral resources on their territory, continental platform, territorial sea or exclusive economic zone.

Government and third-party takes include:

- Signature bonus — a one-time amount (not less than the minimum price established by the ANP (the Brazilian National Agency of Petroleum, Natural Gas and Biofuels) paid by the winning bidder in the proposal for the CC or the PSC to explore and produce crude oil and natural gas. The minimum amount to be offered as signature bonus is set out in the bidding documents and may vary a lot depending on a field.

- Royalty percentage — under the CC, it varies from 5% to 10% of the oil and gas production reference price. Under the PSC, it corresponds to 15% of the volume of produced oil.

  Profit Oil: Under the PSC, the recovery of the costs incurred and investments made in the exploration and development phases, by receiving a fixed percentage of the production, is usually denominated "cost oil." The remaining oil, referred to as "profit oil," corresponds to the share of production that will be shared between the producing country and the Oil Company, in accordance with the terms previously established in the production.
- Special participation percentage — applies only under the CC, as a percentage that varies from 10% to 40% for large production volumes, based on progressive tables relating to net production revenues adjusted for royalties, exploration investments, operating costs, depreciation and taxes.
- Fee for occupation or retention of an area — the activities of exploration, development and production of oil and natural gas, carried out through concession contracts, are subject to the payment of the area retention fee for the occupation/retention of the area. The collection of the area retention fee aims to discourage the retention of concessions without the purpose of exploration, and its value is set by the tender notice and the concession agreement. Such value is determined for each calendar year, based on the number of days of the contract and per square kilometer or fraction of the concession area (from BRL10 to BRL5,000 per km², depending on the phase and based on a progressive table).
- Landlord cost percentage — under a CC, it varies from 0.5% to 1% of the oil and gas production reference price. Under a PSC, it applies only to onshore oilfields and corresponds to a percentage up to 1% of the value of the oil and gas production.

Other fiscal arrangements primarily include:

- Income tax rate — 34%
- Resource rent tax — none
- Capital allowances — D[1], U[2]
- Investment incentives – L[3], RD[4]

B. Fiscal regime

Corporate income tax

Brazilian resident legal entities are subject to income tax on their worldwide income at a rate of 15%, with a surtax of 10% for profits exceeding BRL240,000 a year. In addition, Brazil imposes a social contribution tax on corporate net profits at a rate of 9%. Therefore, the combined corporate income tax (CIT) rate used is 34%. Taxation is the same for entities bearing CC or PSC contracts or both.

Brazil does not apply ring fencing in the determination of the CIT liability with respect to projects held under the same legal entity. Therefore, profits from one project can be offset against losses from another project conducted by the same legal entity, and, similarly, profits and losses from upstream activities can be offset against profits and losses from other activities undertaken by the same legal entity. Brazil has no tax consolidation rules; each legal entity is subject to its own CIT, and losses from one entity cannot be offset with gains from another entity even within the same group.

1 *D: accelerated depreciation.*

2 *U: capital uplift.*

3 *L: tax losses can be carried forward indefinitely.*

4 *RD: research and development (R&D) incentives.*

Brazilian resident legal entities may elect to pay CIT based on taxable profits determined as:

- A percentage of gross revenues (presumed profit method — PPM)

Or

- A proportion of their actual income under accounting records (actual profit method — APM)

Such election is made annually, and it is usually driven by the company's profitability and future investment plans. In general, the PPM taxation regime, due on a quarterly basis, is limited to companies with annual gross revenues that do not exceed BRL78 million (or BRL6.5 million per month of activity) during the prior year. Accordingly, upstream companies that operate in Brazil generally pay CIT based on taxable profits determined according to their actual income according to their accounting records.

Under the APM, the tax is charged on the company's accounting profit and adjusted for nondeductible expenses and nontaxable revenues. CIT may be calculated and paid on a quarterly or annual basis (with prepayments during the calendar year). In general, operating expenses are deductible for CIT purposes, provided they are "necessary and usual" to the company's activity.

Royalties on oil and gas production are fully tax-deductible. Other types of royalties, in general, may be deducted from taxable income limited to 1% to 5% of the net sales derived from the activity on which royalties are paid, depending on the business activities of the payer entity. For trademark royalties, the limit is 1%. For royalty payments to be treated as tax-deductible expenses, the underlying contracts must be approved by the Brazilian Intellectual Property Agency (the INPI), and they must be registered with the Brazilian Central Bank (BACEN) to allow foreign remittances.

Expenditures incurred in the exploration and production activities are immediately deductible. For the development phase, specific rules apply for exhaustion and depreciation expenses. Depreciation and amortization criteria, as well as specific rules related to the oil and gas industry, are described in Section C.

Foreign profits taxation

Brazilian legislation has implemented a worldwide system that has a rigorous foreign profits taxation (controlled foreign corporation (CFC)) regime. Under the CFC regime, any type of corporate investment abroad, be it direct or through a branch or subsidiary, is subject to corporation tax on a current basis (at 31 December of each year), regardless of a foreign local tax burden, local substance of the foreign group company, and the active or passive nature of the operations carried out abroad.

Currently, Brazil utilizes the CFC rules, such as the following:

- Individual taxation is a general rule but with a temporary option to allow consolidation, until 2022, of the results of certain companies directly or indirectly controlled by the Brazilian company for Brazilian tax purposes.
- The temporary provision allows the payment of tax on foreign profits in installments.
- Tax deferral is allowed for profits earned through affiliates (generally, minority interests).
- A carve-out from the CFC regime to foreign subsidiaries and affiliates that earn profits directly related to oil and gas operations in Brazil, The Brazilian parent or investor of such a foreign subsidiary or affiliate is exempt from tax in Brazil on those profits.
  - Law No. 12,973 of 2014 provides a tax exemption applicable until 2019 up to the limit of the profits earned through subsidiaries corresponding to oil upstream.[5]

5 *According to Law No. 13,586 of 2017.*

Carryforward tax losses

Tax losses may be carried forward indefinitely. No carryback or inflation adjustments are permitted. Tax losses that are carried forward may be used to offset up to 30% of a company's taxable income in a tax period. Restrictions on the offsetting of carried forward tax losses may be imposed if there is a change of ownership control and a change of the business activity between the period when the losses were generated and the period when the losses will be effectively used.

Foreign losses

The losses of a direct or indirect foreign subsidiary that have been accrued in calendar years preceding the period in which Law 12,973/14 comes into force may be used to offset future profits of the same entity, considering the proportion of interest in each subsidiary. In order to offset the losses, the taxpayer should report the amounts in the Demonstrative of Foreign Losses by 31 July 2015 within Brazilian tax authorities' electronic system (the "SPED" system), considering the following conditions determined in Normative Instruction SRF 1,520/14, Article 10:

- The accumulated foreign losses subject to offset with future profits should be proportional to the Brazilian parent participation in each of the foreign subsidiaries.
- The offset should be performed before its conversion into reals (BRL).
- The amount to be offset is not limited to 30% of the entity's net income.

Losses after 2015 should be reported electronically, by 31 July of the subsequent years, on a stand-alone basis.

The legislation determines that taxpayers will lose their right to offset the accumulated losses if the losses are not duly reported in the electronic Demonstrative for Foreign Accumulated Losses.

Regarding the entities that may opt to consolidate, the positive result of the consolidation should be included in the Brazilian parent entity's taxable basis, taking into account any relevant losses. The new rules have maintained the prohibition to use losses to offset Brazilian parent profits in consolidated. These rules, only allow current losses to offset future profits of the same entity. When the law does not permit the consolidation, or if the taxpayer has opted not to consolidate, the current loss can only be used to offset future profits of the same entity.

Capital gains

Capital gains recognized by Brazilian resident entities are included as ordinary income and taxed at CIT standard rates. In general, capital losses incurred in a calendar year may offset operating profits or capital gains generated in the same year. Excess capital losses may be carried forward indefinitely but are limited to 30% of future capital gains only.

Until 2016, capital gains derived by nonresidents on shares and other assets located in Brazil were subject to capital gains tax at a rate of 15%.

Normative Instruction 1,732 of 2017 expressly provides the capital gains tax rate for Brazilian Companies as a progressive rate system with rates ranging from 15% to 22.5%.

A 25% rate applies to nonresidents located in low-tax jurisdictions.

Transfer pricing

Brazilian transfer pricing regulations deviate from the arm's-length principle adopted under the Organisation for Economic Co-operation and Development (OECD) guidelines and from the majority of the countries with transfer pricing regulations. There are no profit-based methods, and a functional/risk analysis is not necessary. Profit margins are determined by law, which may not provide consistency with an arm's-length result; an exception applies to the methods for commodities transactions.

The legislation contains a very broad definition of "related parties," involving concepts of direct and indirect control and utilizing voting power and business control criteria. The legislation also includes joint ventures, consortia and other forms of joint ownership (as related parties). There are also rules whereby exclusive distributors and interposed parties are also considered related parties for the purposes of Brazilian transfer pricing regulations.

The Brazilian transfer pricing rules also apply to residents located in low-tax jurisdictions (LTJs) or privileged tax regimes (PTRs), regardless of any equity relationship with the Brazilian company, as defined under Brazilian tax legislation. The legislation that provides guidance on the list of LTJ and PTR jurisdictions is revised frequently. Relevant recent amendments to the oil and gas industry were introduced in regard to Austrian holding companies that had no substantive economic activity and certain types of Singaporean entities that should be considered as privileged tax regimes. The inclusion of Ireland, Curacao and Saint Martin in the list of low-tax jurisdictions should also be noted, as well as the exclusion of Netherlands Antilles, Costa Rica, Madeira Island, Saint Kitts and Nevis and Switzerland from the aforementioned list (see the complete list on taxation on universal bases).

From January 2013, the transfer pricing legislation counted on an updated version. The main changes included the following: (i) the gross profit margin for the calculation of the "resale minus profit" method for imports would be determined by the taxpayer's sector of economic activity — including 40% gross profit for companies that work in the extraction of crude oil, natural gas and petroleum products;[6] (ii) mandatory transfer pricing methods for the calculation of export or import of products deemed as commodities; and (iii) changes to the calculation of interest associated with finance operations.

Prices on the importation and exportation of goods, services and rights are generally based on the following transfer pricing methods:

- Use of uncontrolled, similar transactions (PIC and PVex)
- Resale minus (PRL and PVA/PVV)
- Cost plus (CPL and CAP)
- Market price quotation, in the case of commodities (PCI and Pecex)

With the exception of commodity pricing, no "best method/most appropriate" rule applies. Instead, a Brazilian taxpayer may demonstrate compliance with the transfer pricing rules by choosing the method that is the most favorable to the taxpayer, provided that the necessary documentation can be established. In the case of products considered commodities, the application of the "market price quotation" is mandatory.

Regarding exportation, transfer pricing rules apply to transactions entered into with related parties or parties located in LTJs or PTRs only if the average price charged in the transaction is less than 90% of the average price for identical or similar goods, services or rights traded in Brazil during the same period and under similar payment terms with unrelated parties (the "absolute safe harbor" provision). Operations with commodities do not apply for the absolute safe harbor provisions.

Brazilian transfer pricing regulations also provide for two additional safe-harbor provisions on exports, which allow the Brazilian entity to demonstrate the adequacy of the adopted export price by disclosing regular commercial documents that support the export transaction. Under such provisions, no additional transfer price calculation is required. The safe-harbor provisions are not applicable to the export of products classified as commodities or exports to LTJs or PTRs. The safe-harbor provisions apply in the following situations:

- The taxpayer's net export revenues do not exceed 5% of the total net revenues during the calendar year.

6 *The 40% gross profit could be reduced to 20% if a taxpayer committed with only the associated service/supply for the oil and gas sector, according to Law 9,430/96, Article 18,12,III.*

- The taxpayer demonstrates a minimum pretax net profit of 10% on the export transaction (for the analyzed calendar year and the two preceding years). This safe harbor applies only if the exports to related parties do not represent more than 20% of the company's total export revenues.

Inbound and outbound transactions involving commodities must be tested by calculating the benchmark data as the daily average price of goods or rights as traded on international future or commodity exchanges or markets or as published by internationally recognized institutions modified by certain price adjustments to reflect market conditions on the day of the transaction. Price adjustments include quality and volume corrections as well as freight, logistics, payment terms and others.

The legislation states that for commodities with public prices disclosed by government agencies in the Brazilian *Official Gazette* (DOU), the data might be used for the purpose of comparing the covered transactions export prices. As is the case of crude oil prices provided on a monthly basis by the National Petroleum Agency (ANP). It is worth mentioning that the calculation methodology of the reference prices was amended by ANP in 2017 to include additional elements such as sulfur, nitrogen and acidity de-escalators.

The intercompany leasing of equipment and the chartering of vessels — typical operations within the oil and gas industry — are not clearly covered by the legislative framework and thus should be deeply and carefully analyzed. Additionally, the Brazilian Revenue Service amended the provisions for qualifying for the special customs regime — Repetro — which affected intercompany transactions, e.g., prohibiting some cases of related-party chartering of vessels.

Interest paid to or received by related parties abroad associated with loan agreements is also subject to Brazilian transfer pricing rules. The calculation of the maximum amount of deductible expenses or the minimal revenue arising from interest subject to transfer pricing regulations should observe the following:

- In a case of transactions in US dollars (USD) at a fixed rate, the parameter rate is the market rate of the sovereign bonds issued by the Brazilian Government on the external market, indexed in USD.
- In a case of transactions in Brazilian reals (BRL) at a fixed rate, the parameter rate is the market rate of the sovereign bonds issued by the Brazilian Government on the external market, indexed in BRL.
- In all other cases, the parameter rate is the London Interbank Offered Rate (LIBOR).

The subsequently obtained parameter rate can still be increased by an annual spread to be established by Brazil's Ministry of Finance. From 2013 onward, the annual spread was fixed by the Brazilian Ministry of Finance with 3.5% for interest expenses and 2.5% for interest income.

The Brazilian transfer pricing rules do not apply to royalty payments associated with agreements duly registered with the INPI, to the extent that the deductibility of these payments for CIT in Brazil is subject to limitations based on domestic legislation.

Transactions involving cost sharing, cost contribution and management fees might be considered deductible for purposes of calculating income tax and social contribution on net income, when assessed according to article 299 of the Income Tax Regulation. According to private ruling No. 8/2012, costs and expenses shared among group companies could be considered deductible when:

- They are relating to goods and services actually paid and received
- They are considered to be necessary, usual and normal to the business activities of the payer
- They are apportioned based on a reasonable and objective criterion, agreed up front and properly formalized by an instrument signed by the parties

- The apportionment criterion is consistent with the effective cost of each company, and the total price paid for goods and services is in compliance with the general accounting principles
- The company that centralizes the acquisition of goods and services appropriates solely the portion that relates to it under the apportionment criterion adopted

It is worth mentioning that other private rulings address this matter.

Brazilian membership to the OECD

On 30 May 2017, Brazilian Finance and Foreign Affairs ministers sent an intention letter to the Secretary-General of the OECD, asking to begin the process of becoming a member in the organization. Once the OECD accepts the application, an adjustment of the Brazilian legal framework to meet the OECD requirements will become mandatory. After Brazil's application is accepted, the entire membership process is expected to occur in three years.

Brazil's membership will affect its transfer pricing legislation. The OECD, the Brazilian revenue service and the taxpayers shall enter into a discussion to identify the most appropriate way to transition from the current transfer pricing legislation to the OECD guidelines. The discussion may begin as early as March 2018 and extend over a 15-month period.

Dividends and interest on net equity

No currency exchange restrictions are imposed on dividends distributed to shareholders domiciled abroad, provided the foreign investment into Brazil is properly registered with the BACEN.

A Brazilian entity may also calculate notional interest on the net equity value (adjusted by the deduction of certain accounts) payable to both resident and nonresident shareholders. Notional interest on equity is a hybrid mechanism to remunerate the capital of shareholders and create a deductible expense for purposes of Brazilian CIT.

Currently, interest on equity is calculated by applying the official long-term interest rate (TJLP) on net equity, but it is limited to 50% of the greater of the current earnings or accumulated profits. Interest on equity paid to a foreign beneficiary is subject to withholding tax (WHT) in Brazil charged at a general rate of 15% (25% if payment is made to an LTJ).

Interest on equity payments tends to be advantageous to profitable Brazilian subsidiaries, to the extent that the interest generates tax-deductible expenses at 34% with the cost of the 15% WHT, although the overall tax benefit should be evaluated in light of the country of residence of the foreign shareholder. Interest on net equity received by a Brazilian company is also subject to social contribution taxes, PIS (Programa de Integração Social) and COFINS (Contribuição para o Financiamento da Seguraridade Social) at a combined rate of 9.25%.

Transactions with companies located in a low-tax jurisdiction or under a privileged tax regime

Since 2010[7], Brazil has had LTJ and PTR lists, producing the following tax consequences when relations with companies from such listed countries occur.

Transfer pricing

Transactions with individuals resident in an LTJ or subject to a PTR are considered as transactions between related parties and subject to control of transfer prices, even if they are not effectively related (see further details on transfer pricing in Section B).

Thin capitalization rules

Interest due to companies resident in an LTJ or subject to a PTR are subject to a maximum debt-to-equity ratio of 0.3:1, instead of the general ratio of 2:1 (see Section F).

7 *Normative Instruction 1.037 of 2010.*

Deductions of payments to an individual or company resident in a low-tax jurisdiction or under a privileged tax regime

Any payment made, directly or indirectly, to an individual or company resident in an LTJ or under a PTR is not deductible for income tax purposes unless the following requirements are met:

- Identification of the effective beneficiary of the income
- Evidence of the operating capacity of the recipient
- Supporting documentation regarding the price paid for rights, goods and services

Furthermore, it is also established that the effective beneficiaries will be deemed to be those entities to which the income can be attributable, not any created with the sole purpose of avoiding taxes.

Increased WHT rate

Remittances to a resident of an LTJ are generally subject to a 25% withholding income tax rate for Brazilian tax purposes, instead of the general rate of 15% (an increase that, to date, does not apply to remittances made to beneficiaries subject to a PTR). (See Section E.)

Taxation on universal bases

The presence of a legal entity resident in an LTJ or subject to a PTR may affect the taxation in Brazil of the profits earned through subsidiaries, affiliates and affiliates abroad (for the so-called "contamination" effect).

Apart from the special treatment described above, for the purpose of holding companies located in Denmark, the Netherlands and Austria,[8] Brazilian tax authorities have adopted a concept of substantial economic activity.[9] That is, such holding companies must comply with several substance aspects, such as qualified employee presence and physical facilities suitable for management and effective decision-making in order to no longer be qualified as a PTR under Brazilian law (see further details in "Foreign profits taxation" section).

Normative Instruction SRF No. 1.773/2017 introduced changes in the Black and Grey lists. Brazilian tax authorities have excluded Costa Rica, Singapore and Madeira Island of the Black list and included Portugal, Costa Rica and Singapore in the Grey List.[10]

Black list (LTJ)	
American Samoa	Labuan
American Virgin Islands	Liberia
Andorra	Liechtenstein
Anguilla	Macau
Antigua and Barbuda	
Aruba	Maldives
Ascension Islands	Marshall Islands
Bahamas Community	Mauritius Island
Barbados	Monaco
Belize	Nation of Brunei
Bermuda Islands	Nauru
British Virgin Islands	Niue
Campione d'Italia	Norfolk Island
Cayman Islands	Oman

8 *Normative Instruction 1.658 of 2016.*

9 *Declaratory Act No. 3 of 2015.*

10 *Normative Instruction 1,773 of 2017.*

Channel Islands	Panama
Cook Islands	Pitcairn Island
	Qeshm
Curaçao	Republic of Kiribati
Cyprus	Republic of Seychelles
Djibouti	Saint Helena
Dominica	Saint Lucia
Fed. of St. Christopher and Nevis	Saint Martin
French Polynesia	Saint Pierre and Miquelon
Gibraltar	St. Vincent. and the Grenadines
Granada	Samoa
Hong Kong	San Marino
Ireland	
Island of Man	Solomon Islands
Kingdom of Bahrain	Tristan da Cunha
Kingdom of Swaziland	Turks and Caicos Islands
Kingdom of Tonga	United Arab Emirates
Lebanon	Vanuatu

Gray list (PTR)

Country	PTR
Uruguay	Sociedad Financera de Inversion (Safis) until 31 December 2010
Denmark	Holding companies without economic substance
The Netherlands	Holding companies without economic substance
Iceland	ITC
USA	State Limited Liability Company (LLC), with nonresident participants
Spain	Entidad de Tenencia de Valores Extranjeros (E.T.V.Es.)
Malta	ITC and International Holding Company
Switzerland	Holding companies taxed with a CIT rate lower than 20%
Austria	Holding companies without economic substance
Costa Rica	Free Zone's regime (RZF)
Portugal	Centro Internacional de Negócios da Madeira's regime (CINM)
Singapore	Specific regimes of differentiated aliquots

Government and third-party takes

Government and third-party takes vary depending on the contractual regime to which the Brazilian entity is subject.

Concession participant or PSC consortium member

Foreign companies may participate in the block concession or PSC bidding rounds held by the ANP. However, a foreign company must commit to incorporating a company in Brazil under Brazilian law, with its headquarters and administration in Brazil, to hold the concession rights or to be a partner in the PSC if it wins the bid.

Concession contracts

In 1997, with the end of the monopoly of Petróleo Brasileiro S/A (Petrobras) in the Brazilian oil and gas sector, a concession regime was introduced into Brazilian legislation to grant licenses to private players to perform oil and gas activities in Brazil. Under the concession regime, the concessionaire is authorized to explore oil and gas activities within a certain area, at its own cost and risk, and must compensate the Brazilian Government for this right.

More than one company may exploit a concession. Partners on a joint venture should organize themselves under a consortium agreement. Specific provisions between the partners can be set up through a joint operation agreement (JOA) for each concession granted.

In this context, upstream concession holders are subject to the payment of four government and one third-party takes, as described next.

Signature bonus (government)

The signature bonus reflects the amount offered by the winning bidder in the proposal for the concession to explore and produce crude oil and natural gas. It is a one-time payment, and it may not be less than the minimum price established by the ANP in the bid notice. It must be paid in full at the date of the signature of the respective concession agreement.

Royalties (government)

The amount of petroleum royalties to be paid monthly for a field is equivalent to 10% of the total production volume of crude oil and natural gas of the field during that month, multiplied by the relevant reference prices (determined by the ANP), beginning in the month of the relevant production startup date, with no deductions allowed. Royalty payments are due on the last working day of the month following the month of their computation.

The ANP may, in the bid notice for a given block, reduce the percentage of 10% to a minimum of 5% of the total production volume, considering geological risks, production expectations and other factors pertaining to the block. In the 14 bidding rounds conducted by the ANP (note that round 8 was canceled in February 2013), only some of the auctioned blocks — blocks classified as inactive marginal fields for evaluation, rehabilitation and production of oil and natural gas — had their royalties reduced from 10% to 5%.

Special participation payment (government)

The special participation payment represents an extraordinary financial compensation payable due to crude oil and natural gas exploration and production concessionaires for large volumes of production or high earnings. It must be paid in relation to each field in a given concession area from the quarter when the relevant production startup date occurs. Special participation payments are due on the last working day of the month following the quarter of computation.

Computation of special participation is based on net production revenues adjusted for royalties, exploration investments, operating costs, depreciation and taxes. In general, the special participation rates are based on progressive tables that range from 10% to 40%[11] and consider:

- Reservoir location (onshore, lakes, rivers, river islands, lake islands and continental shelf within bathymetric depths of up to and more than 400 meters)
- Years of production (1, 2, 3 and more than 3 years)
- The inspected quarterly production volume, measured in thousands of cubic meters of equivalent oil, for each field

11 *Note, however, that Decree 2705/98, article 22 provides for some exemptions depending on the field location and the production volume.*

The current standard CC provides that, in fields where the special participation is due, concessionaires must invest an amount equivalent to 1% of the gross revenue of the oilfield in expenses that qualify as R&D.

Fee for occupation or retention of areas (government)

Both the bid notice and the concession agreement include payment provisions for the occupation or retention of the area. The amount is to be computed each calendar year, beginning from the date of execution of the concession agreement. It is payable on 15 January of the following year.

The amount due for the occupation or retention of an area is set by the ANP, which considers the block location and other pertinent factors. The calculation is based on a progressive table that ranges from BRL10 to BRL5,000 per square kilometer.

Landlord cost (third party)

Landlord cost is not a governmental take, because it is due to the owner of the land as a monthly rental payment for access to and use of the land. For onshore blocks, the ANP sets the amount from 0.5% to 1% of the oil and gas production reference price. In the 12 bidding rounds conducted by the ANP (note that round 8 was canceled), only some of auctioned blocks — blocks auctioned that were classified as inactive marginal fields for evaluation, rehabilitation and production of oil and natural gas — had their landlord cost reduced from 1% to 0.5%.

Production sharing contracts

After significant debate, Law 12,351 was published on 23 December 2010, introducing a production sharing regime for the pre-salt area and other strategic areas, which include regions of interest for national development, characterized by low exploration risk and high production potential. The first pre-salt bidding round occurred on 21 October 2013. In summary, a PSC is a regime in which the contracted company will execute, at its own cost and risk, exploration, development and production activities and, in the case of commercial discovery, will have the right to recover, in oil, operational costs incurred during the exploration and development stages (cost of oil) and receive the volume corresponding to the oil surplus (the difference between the total oil produced and royalties paid plus recovered costs) relating to its participation in the venture. Signature bonuses and production royalties will not be allowed in the computation of the cost oil. Details about allowed expenses in the cost oil are duly provided by ANP.

Decree 9,041/2017 published on 3 May 2017, regulated Law 12.351/2010, regarding Petrobras' right of first refusal to act as operator in the consortium exploring oil blocks in the pre-salt contracted under the production sharing contracts. The measure aims to give more transparency to the auctions of pre-salt areas planned by the government later this year.

Petrobras should express its interest in participating as operator in the consortiums formed to explore blocks under the production sharing contracts within 30 days, as of the date of publication, by the National Council of Energy Policy (CNPE), of the technical parameters of each auction. In the case of the third round of pre-salt bids, for example, this CNPE publication occurred even before the regulation of Petrobras' participation rules.

The decree establishes that the state must manifest itself by specifying the blocks in which it has interest and the percentage of participation that it intends, never below 30%.

However, it will be for the CNPE to establish the percentage of Petrobras' participation, considering the percentages between the minimum of 30% and that indicated in the manifestation of the company.

According to the decree, if Petrobras does not exercise its first right of refusal, the blocks will be the subject of a bidding process, from which Petrobras will be able to participate on an equal basis with the other bidders.

The consortium to explore and produce oil and gas in these strategic areas must be set up by:

- The Government-owned company Empresa Brasileira de Administração de Petróleo e Gás Natural S.A. – Pré-Sal Petróleo S.A. (PPSA), to be incorporated with the specific purpose of managing the PSC:
  - PPSA will not bear any risks or cost associated with the exploration, development and production activities.
- Petrobras
- The bid winner, if applicable, which shall have joint liability for the execution of the contract with Petrobras

Under Brazilian oil and gas legislation, upstream PSC holders are subject to the payment of two government and one third-party takes, as described next.

C. Capital allowances

As a general rule, fixed assets may be depreciated according to their "useful life." Documentation is required to support the useful life when it differs from the useful life provided by the Brazilian Internal Revenue Service (the RFB). If RFB's understanding differs from the taxpayer's study, the asset's useful life should be subject to a final opinion to be issued by the Brazilian National Institute of Technology or other similar institute.

Examples of rates ordinarily used by the RFB include:

- Buildings — 25 years
- Machinery and equipment — 10 years
- Vehicles, computer hardware and software — five years

A company that operates two shifts per day may depreciate machinery and equipment at 1.5 times the normal rate. If it operates three shifts, it may double the normal rate.

Oil and gas upstream companies may depreciate fixed assets directly connected with upstream operations based on the rates published periodically by the Federal Revenue Office of Brazil (RFB) for each type of asset. The taxpayer shall be entitled to compute the quota effectively adequate to the depreciation conditions of the company's machines, equipment and facilitation instruments applied in the development activities of the production, provided that the taxpayer proves this adequacy when adopting a different rate from that published by the RFB.

Exhaustion expenses from assets generated in preparation for production are deductible for IPRJ and CSLL purposes. Until 31 December 2022, an accelerated exhaustion rate for such assets is available. In such instance, the exhaustion rate is calculated according to the units-of-production method and multiplied by a factor of 2.5.

Currently, some tax incentives apply to specific industries and also to companies located in developing areas, such as the north and northeast regions of Brazil. An R&D incentive was enacted in 2006 that introduced an accelerated depreciation program and capital uplifts. For further information, see Section D below.

Capital expenditures for the acquisition of rights, which are expected to exist or be exercised within a limited period, may be amortized. This amortization can be calculated based on the remaining life of the right, or on the number of accrual periods for which the legal entity expects to enjoy the benefits originating from the expenses registered as deferred charges.

According to article 1 of Law No. 13.586/2017, the expenditures for the depletion of assets generated by expenses incurred in the development phase to enable production are deductible for CIT purposes. Accelerated depletion rates for these assets are applicable; the exhaust rate is calculated according to the units-produced method multiplied by 2.5. The accelerated exhaustion quota shall be excluded from net profit, and the total accumulated exhaustion, including normal and accelerated exhaustion, shall not exceed the cost of the asset.

Rehabilitation or decommissioning

Brazilian rules on rehabilitation or decommissioning for tax purposes[12] determines that the expenditures rehabilitation or decommissioning shall only be tax deductible when actually incurred. Thus, before the rehabilitation or decommissioning is actually performed, the costs accrued under financial statements shall be added back for CIT purposes and controlled under the CIT computation book as a temporary difference.

There are no loss carryback rules in Brazil.

D. Incentives

Tax holiday

Brazil does not have a tax holiday regime.

Regional incentives

Apart from some special customs regimes (see comments about the special bonded warehouse for oil and gas platforms and about the Repetro regime in Section H below), REPENEC (Regime especial de incentivos para o desenvolvimento de infraestrutura da indústria petrolífera nas regiões Norte, Nordeste e Centro-Oeste) is the only specific tax incentive for the oil and gas industry.

REPENEC

On 14 June 2010, Law 12,249/2010 (a conversion of Provisional Measure 472/09) was published in Brazil's *Official Gazette*. Among other measures, the law introduced a new special regime for the oil and gas industry (REPENEC). REPENEC relates to infrastructure projects in the oil and gas industry approved by the federal Government by 31 December 2010 for applicants established in the north, northeastern or midwestern regions of Brazil.

In summary, in the event of local sales or importation of new machinery, instruments and equipment, and of construction materials for use or integration into infrastructure projects classified as fixed assets, REPENEC provides for the suspension of social contribution taxes PIS and COFINS, federal value-added taxes (VAT) (IPI) and import duty (II) that would otherwise apply (please see Section H for further explanations on these taxes).

Other regional tax incentives

Besides REPENEC, Brazil offers a variety of more general tax incentives intended to attract businesses of particular importance and foster the development of certain underdeveloped regions in the country.

The following incentives are offered to entities located in the area of the Agency for the Development of the Northeastern States (Superintendência de Desenvolvimento o Nordeste, or the SUDENE) and the Agency for the Development of the Amazon (Superintendência de Desenvolvimento da Amazônia, or the SUDAM):

- A reduction of 75% on the 25% CIT due, calculated on profits from activities covered by the incentive tax treatment (lucro da exploração) for projects considered to be vital for development of the SUDAM and SUDENE regions, or for modernization, expansion or diversification of existing projects considered to be vital for the development of the SUDAM and SUDENE regions:
    - This incentive is granted until 31 December 2018. Companies may benefit from this incentive for a maximum period of 10 years.
    - Historically, this deadline is postponed, but so far, no new rule has been enacted.
- From 1 January 2009 to 31 December 2013, a reduction of 12.5% on the 25% CIT due, calculated on profits from activities covered by the incentive

12 *Article 45 of Law No.12,973/15 and article 45 of Brazilian IRS Normative Instruction No.1,700/17.*

tax treatment (lucro da exploração) for new ventures considered to be a priority for the development of the regions covered by the SUDAM and the SUDENE

Until 2018, companies that undertake projects of particular importance for the development of the region are entitled to reinvest up to 30% of the income tax due at 15% on their SUDENE and SUDAM projects.

Research and development

Companies that invest in technological innovation are entitled to a R&D federal tax incentive under Law 11,196/05 of 2005. The definition of "technological innovation" is "the design of a new product or manufacturing process, as well as new functionalities or characteristics added to products or to processes, which results in incremental improvements and an actual gain in quality or productivity, thus leading to increased market competitiveness."

Based on the qualifying conditions, the application of this tax incentive is associated with the design of new manufacturing processes or products, or with new functionalities or characteristics being added to existing processes or products.

In summary, the tax incentives offered include:

- Deduction of total expenditures made during the computation period in connection with technological R&D of technological innovation, which are classifiable as operating expenses pursuant to Brazilian tax legislation
- Deduction for the purposes of CIT of 60% to 100% of total expenditures made during the computation period in connection with R&D of technological innovation, which are classifiable as operating expenses by Brazilian tax legislation
- Reduction by 50% of IPI levied on equipment, machinery, devices and instruments, as well as on their related spare accessories and accompanying tools, that were intended for use in technological R&D
- Accelerated depreciation by deduction, in the acquisition year, of the total cost of new machinery, equipment, devices and instruments intended for use in activities regarding R&D of technological innovation
- Accelerated amortization by deduction (only for CIT purposes) in the computation year in which they are incurred, of the expenditures classifiable as deferred assets relating to the acquisition of intangible assets associated exclusively with R&D of technological innovation activities
- Reduction to zero of the WHT rate applicable to foreign remittances for the purposes of registration and retention of trademarks, patents and cultivars (variety of cultivated plants)

No prior approval is necessary to take advantage of this tax incentive. However, the taxpayer is required to provide information to Brazil's Science, Technology, Innovation and Communication Ministry (Ministério da Ciência, Tecnologia, Inovações e Comunicações) on its technological research programs by 31 July of each subsequent year and must have a regular status update, in both semesters of the year, regarding its federal tax liabilities.

After receiving the taxpayer's report, the Ministry will assess if the R&D initiatives are in accordance with the definitions established by the Brazilian laws. If the report is not approved, the taxpayer may appeal and provide further information in order to prove the eligibility of R&D initiatives to the tax incentives.

Under Brazilian tax legislation, all documentation related to the use of these tax incentives must be available for tax inspectors during the open period under the statute of limitations.

Exportation incentives

Another incentive for exporters that can be used by the oil and gas industry in Brazil is the Regime Especial de Aquisição de Bens de Capital para Empresas Exportadoras (RECAP), which is a special tax regime for the acquisition of capital goods by companies qualified as exporting companies, created by Law 11,196/2005 and regulated by Decree 5,649/2005. To benefit from the RECAP, a company must have recognized gross revenues derived from exports in the prior year of at least 50% of its total annual gross income, and it must maintain this minimum of export revenues for the following two calendar years (or the following three years if the company does not comply with the first requirement).

The RECAP regime applies to certain equipment, instruments and machinery imported directly by the RECAP beneficiary to be used as fixed assets. Under the RECAP regime, the social contribution taxes on gross revenues triggered upon the importation, namely PIS and COFINS, are suspended and converted into a zero tax rate after the incentive conditions are complied with. The regime also provides for the suspension of PIS and COFINS on local acquisitions made by the beneficiary of the RECAP regime.

In addition to the conditions outlined above, to benefit from the RECAP regime, a Brazilian legal entity must not have any overdue federal tax liabilities. Benefits are also canceled if the legal entity does not comply with the minimum export revenues requirement of 50% and if the beneficiary does not comply with the other requirements of the RECAP regime or at the beneficiary's own request.

A legal entity excluded from the RECAP regime must pay interest and penalties on the taxes suspended, calculated from the date of acquisition of the imported assets and services or the registration of the import transaction with the electronic customs system (SISCOMEX).

The RECAP tax incentive is not available to Brazilian companies subject to PIS and COFINS under the cumulative tax regime.

Apart from the RECAP tax incentive, Brazilian legal entities may also qualify for the IPI, PIS and COFINS suspension upon a local purchase or importation of raw materials, intermediary products and package materials if they meet, among other conditions, the 70% of export revenue outlined above. Some Brazilian states provide a similar tax incentive for state VAT (ICMS) tax purposes.

E. WHT and other taxes on imported services

Royalties and technical services

Royalties and technical assistance fees remitted abroad are generally subject to WHT at a rate of 15% (unless a tax treaty provides otherwise) as well as CIDE, IOF, the federal tax on financial operations (Imposto sobre Operações de Crédito, Câmbio E Seguro, ou Relativas A Valores, Mobiliários), municipal tax on services (ISS) and PIS/COFINS mentioned below. Royalties and technical assistance fees paid to residents of LTJs are subject to WHT at a rate of 25%.

There has been much debate in Brazil on whether technical services should or should not qualify as royalties. In summary, according to Declaratory Interpretative Act 5/2014 of the Federal Revenue Service, the tax treatment for technical services regarding WHT should be the following:

- Royalties (art. 12): when the treaty or treaty's protocol gives technical services and royalties equal treatment
- Independent professions (art. 14): when there is technical qualification of a person or group of people

Or

- Business profits (art. 7): other cases (Austria, Finland, France, Japan and Sweden)

Administrative and similar services

Administrative and similar service fees remitted abroad are generally subject to WHT at a rate of 15% (unless a tax treaty provides otherwise) when the CIDE tax is due on this remittance (see below). Administrative service fees paid to residents of LTJs are subject to WHT at a rate of 25%.

Other services

For the remittance of fees for other services, the WHT rate is 25%, even if the payment is not made to an LTJ. This rate applies because CIDE tax is not due on these remittances. In case CIDE is due and the remittance is not made to an LTJ, a 15% rate applies.

Rental

Rental payments made to a nonresident are generally subject to WHT at a rate of 15%. Rental payments made to residents of LTJs are subject to WHT at a rate of 25%.

Payments for the charter of vessels with no service components are subject to WHT at a rate of 0%, provided that the entry of the vessel into Brazilian waters is approved by the competent authority. This reduced rate does not apply if the beneficiary is domiciled in an LTJ, in which case taxation will be at the rate of 25%.

Provisional Measure No. 795/2017 (MP 795/2017) converted into Law No. 13.586/2017 introduced significant changes in the conditions to apply 0% WHT tax rates over certain charter remittances to vessel owners located overseas. Upon 1 January 2018, the new percentages to be adopted under the split contract must be as follows:

- 70% for vessels with floating production systems and/or storage and discharge
- 65% for vessels with a drilling, completion or workover/wellwork systems

Or

- 50% for other types of vessels

For offshore support vessels, MP 795/2017 expressly mentions that this type of vessel is not included on the abovementioned limits.

Remittances abroad will be subject to WHT at a rate of 15% on the portion of the charter contract exceeding those thresholds, or a rate of 25% when the beneficiary is located in an LTJ or a PTR, as defined by Brazilian tax legislation.

The new legislation provides a specific definition of related party for the application of the restrictions, which departs from that generally adopted for Brazilian tax purposes. The foreign owner of the vessel and the service provider will be considered related parties when they are partners directly or indirectly in the entity owning the chartered assets.

CIDE tax

The CIDE tax is charged at a rate of 10% on royalty payments, including fees for technical assistance, technical services, administrative services and similar services. The Brazilian payer that makes the remittance to the foreign beneficiary is considered to be the taxpayer for purposes of the CIDE tax.

Social contribution taxes on importation

As a general rule, PIS and COFINS are both social contribution taxes charged on the importation of services and are usually charged at a rate of 1.65% and 7.6%, respectively (a combined nominal rate of 9.25%). The Brazilian importer under the noncumulative PIS and COFINS regime may compute a PIS and COFINS tax credit for certain services acquired (for more details, see Section H). As the right for tax credits has been strongly debated within the oil and gas industry, and it is not under a mature legislative consensus, it should be deeply and carefully analyzed by taxpayers.

Service tax on importation

The ISS is charged on the importation of services. ISS applies at rates that vary from 2% to 5%, depending on the nature of the service and the municipality where the Brazilian taxpayer is domiciled.

Tax on financial operations on import of services

The federal tax on financial operations, or IOF, is currently charged at 0.38% on the amount of Brazilian currency exchanged into foreign currency for the payment of imported services. Most currency exchange transactions are subject to IOF at a rate of 0.38%. This tax may be altered by the executive branch with immediate effect.

F. Financing considerations

Thin capitalization

Thin capitalization rules were introduced in Brazil to apply to inbound and outbound transactions performed either with related parties or with unrelated parties resident in LTJs or under a PTR.

Under the applicable rules, irrespective of whether the intercompany loans are compliant with the general rules governing the deduction of expenses and Brazilian transfer pricing rules, interest expenses are deductible only if the related Brazilian borrower does not have a debt-to-equity ratio greater than 2:1. Any excess interest is not deductible for the purposes of Brazilian CIT.

Additionally, interest expenses deriving from financing arrangements executed with a contracting party established in an LTJ or under a PTR, irrespective of whether related or not to the Brazilian borrower, are deductible only if the debt-to-equity ratio of the Brazilian borrower does not exceed 0.3:1.

Debt versus equity

Brazilian operations can be financed by debt, equity or a combination of both. By capitalizing a Brazilian entity with equity, a parent company bears the risk of currency exchange fluctuation. Alternatively, if the Brazilian entity is financed through debt, the exchange risk is shifted to the Brazilian subsidiary, which may accrue a currency exchange loss or gain for book and tax purposes, even if unrealized. At the election of the Brazilian payer, currency exchange gains or losses may be recognized on a cash or on an accrual basis for Brazilian tax purposes. Debt may also be interest-bearing, which triggers a deductible interest expense for Brazilian tax purposes. Usually, Brazilian corporate borrowers cannot lend funds to others on conditions that are more favorable when compared with their own debt liabilities — otherwise, the difference in interest rates may be deemed not deductible.

With the recent introduction of thin capitalization and transfer pricing rules on loans in Brazil, restrictions are applicable to interest deduction on loans (see above).

To foster Brazilian exports, the Government has reduced the WHT on export financing loans to 0%. Therefore, if an upstream company intends to export its production, either totally or partially, this instrument may be tax-efficient because it triggers a local tax deduction at the rate of 34% with the cost of 0% WHT.

IOF on loans

Under certain circumstances, IOF is imposed by the federal Government at rates varying from 0% to 25%. Indeed, domestic loans between legal entities, including related parties, are subject to IOF, on the credit transaction, at a maximum rate of 1.88% per year.

Foreign loans are subject to IOF on the foreign currency exchange transaction, but not on the lending (foreign credit) transaction itself. As a general rule, a 0% rate applies, but foreign loans with average maturity terms of up to 180 days are subject to IOF at a rate of 6%. The rates can be modified by a Decree issued by the Brazilian government with immediate effects.

G. Transactions

Under Brazilian oil and gas legislation, it is possible to transfer concession agreements to third parties, provided that the transfer is preapproved by the ANP.

Asset disposals

Concession costs, including exploration and development costs, are classified as permanent assets. Disposals of permanent assets are treated as nonoperating transactions, which trigger capital gains or losses. Capital gains are taxed at the same CIT rates as ordinary income (see Section B).

Farm-in and farmout

Brazilian tax legislation does not have a special tax treatment for farm-in and farmout transactions. Accordingly, general Brazilian tax rules apply to asset disposals.

Selling shares in a Brazilian company

Investments not for sale in subsidiaries either in Brazil or abroad are classified as permanent assets. Disposals of permanent assets by Brazilian legal entities are treated as nonoperating transactions, which trigger capital gains or losses. Capital gains are taxed at the same CIT rates as ordinary income (see Section B above).

The gain on a sale of a Brazilian asset by a nonresident shareholder is taxable in Brazil at a progressive rate of 15% to 22.5%. If the beneficiary of the capital gain is resident in an LTJ, the WHT rate is increased to 25%. Indirect dispositions of Brazilian assets are not taxable, but transactions with lack of substance can be challenged by Brazilian tax authorities in Brazil (see Section B).

Exportation of oil

Oil export transactions are exempt from ICMS, IPI, PIS and COFINS.

H. Indirect taxes

State VAT (ICMS)

ICMS is due on the local sale of oil and gas, based on the sale price, including the ICMS itself (built-in calculation). For intrastate operations (carried out by a seller and buyer located in the same Brazilian state, or imports), the ICMS rate is determined by the legislation of the state where the sale is made and generally varies from 17% to 20%.

Interstate transactions (carried out between a seller and buyer located in different Brazilian states) are subject to reduced rates of 7% or 12%, depending on the states involved. One exception is that, because of immunity established by the Brazilian Federal Constitution, ICMS is not due on interstate oil operations. On the other hand, in the case of consumables or fixed assets, the buyer must pay to the state where the buyer is located, the ICMS DIFAL, which is calculated based on the difference between the interstate rate and the buyer's own internal ICMS rate.

From January 2013 onward, interstate transactions with imported products have been subject to an ICMS rate of 4%. To apply this rate, some requirements should be observed, like the non-submission of the product to a manufacturing process or, in the case of further manufacturing, the resulting product should have a minimum imported content of 40%.

Federal VAT

As a general rule, federal VAT (IPI) is charged on transactions involving manufactured goods by a manufacturing plant, or on the first sale in Brazil of an imported asset, as defined in the legislation in force (Decree No. 7,212/2010). According to the Brazilian Federal Constitution, local sales, intrastate sales or the importation of oil products, including crude oil and its by products, are not subject to the IPI tax.

IPI rates vary from 0% to 365%.

Social contribution taxes on gross revenue

PIS and COFINS are social contribution taxes charged on gross revenues earned by a Brazilian legal entity under one of two different regimes of calculation: noncumulative and cumulative.

Under the noncumulative regime, PIS and COFINS are generally charged at a combined nominal rate of 9.25% (1.65% PIS and 7.6% COFINS) on revenues earned by a legal entity. Certain business costs result in tax credits to offset PIS and COFINS liabilities (e.g., depreciation of machinery, equipment and other fixed assets acquired to be directly used in the manufacturing of a product or rendering of a service). PIS and COFINS paid upon importation of certain assets and services are also creditable. Upstream companies are generally subject to this regime, but in practice there is some disagreement on the availability of such credits depending on the phase of the area/field.

Brazilian taxpayers subject to the cumulative regime must calculate PIS and COFINS at a combined rate of 3.65% (0.65% PIS and 3% COFINS). No tax credits are provided under this regime. The regime applies to some industries (not including oil and gas) and also to companies that compute taxable profits as a percentage of gross sales. For further information, please see Section B above.

From 1 July 2015, taxpayers subject to the noncumulative regime must calculate PIS and COFINS over certain financial revenues, applying the rates of 0.65% and 4%, respectively. Until this date, these types of revenue were taxed at the rate of 0%. The exception for that rule is the revenue derived from export operations of goods and services or/and contracted obligations, including loans and financing. In this respect, financial expenses are not taken into consideration in the calculation of the PIS and COFINS credits to be offset over such revenue.

Importation of equipment and other items

In Brazil, companies that intend to operate with foreign trade transactions must be registered within the SISCOMEX electronic system, an integrated computerized system through which all international trade transactions are electronically processed. Through this system, an import declaration (Declaração de Importação, or DI) is issued and registered for each import operation.

In a few cases, the importation of goods, including machinery and equipment, also requires an import license (Licença de Importação, or LI), which is a type of preauthorization for the import procedure. The need for a prior import license is determined based on the tariff classification of the goods to be imported and some other specific conditions.

The licensing procedure may be automatic or non-automatic, depending on the product. In most cases, the import license is obtained automatically during the filing of the DI in the SISCOMEX system. Certain products, however, are subject to the non-automatic licensing process, which means that it is important to check whether the import license must be obtained before shipment of goods to Brazil. In some other listed circumstances, the import license may be obtained after the shipment of the goods but before the registration of the DI (at the beginning of the customs clearance process).

The importation of certain goods, such as petrochemicals, crude oil and natural gas, requires authorization from special regulatory agencies as a condition for the issuance of the import license.

The import duty (Imposto de Importação, or II) is due on the customs value of imported goods, consisting of the cost of the product, plus the international insurance and freight (i.e., the cost, insurance and freight (CIF) value). The customs value may vary depending on specified price elements, as defined by the customs valuation rules.

II is a non-recoverable tax, which means that no credits are available against it, and it always represents a cost to the importer (as II is not a creditable tax, and consequently, II paid upon importation cannot be deducted from any subsequent import transaction taxed by the II).

The II rate varies depending on the tariff classification of the imported goods, as per Mercosur's tariff code system, which is based on the Harmonized System. The average rate for machinery and equipment is 14%.

Capital goods, data processing and telecommunications goods may benefit from an II reduction of up to 0% if the importer is able to attest and demonstrate that no similar goods are manufactured in Brazil (ex-tarifario benefit).

In addition to being subject to II, import transactions are also subject to IPI, PI, COFINS and ICMS.

For import transactions, the IPI is calculated on the customs value of the imported item, plus the II. The rate also depends on the respective tariff classification. The average IPI rate ranges between 10% and 20%. However, for machinery and equipment, the rate can range from 0% to 20%. IPI is a recoverable tax, which means that, in principle, the amount paid on the import transaction may be offset in the future, provided some requirements are met. On the importation of equipment and other assets to be incorporated to the importer's fixed asset, however, no credits can be offset, and the IPI becomes a cost.

ICMS is charged on the customs value of the imported goods, plus II, IPI, ICMS itself, PIS and COFINS and other smaller customs charges. ICMS rates vary depending on the state where the importer is located, which means that, unlike II and IPI, the ICMS applicable rate does not relate to the product itself but to the state where the importation takes place. The ICMS rates range from 17% to 20% and may be lower in some cases, depending on:

- The nature of the goods being imported
- Eventual application of state tax benefits

Freight surcharge for renovation of the merchant marine fleet

Maritime transportation is subject to a freight surcharge for renovation of the merchant marine fleet (Adicional ao Frete para Renovação da Marinha Mercante, or AFRMM), which is an extra freight charge levied through Brazilian and foreign shipping companies unloading cargo in Brazilian ports. AFRMM is charged at a rate of 25% on ocean navigation freight, at 10% on coastal navigation freight and at 40% on the inland navigation of liquid bulk cargos carried within the north and northeast regions of Brazil (based on the bill of lading and the cargo manifest).

The AFRMM does not apply to the transportation of goods in connection with exploration activities of hydrocarbons and other underwater minerals in the Brazilian Exclusive Economic Zone, such as those carried out by Petrobras. In addition, goods imported by autarchies and other entities directly connected to federal, state and municipal governments, are not subject to the AFRMM.

Similarly, AFRMM is suspended for assets imported under a special customs regime granted by the Brazilian Revenue Services (Receita Federal do Brasil), such as under the drawback or the temporary admission regime with suspension of taxes, up to the date of registration of the import declaration (DI) in the event of nationalization.

The main fees applicable to the customs clearance of imported equipment or goods are storage fees, demurrage, terminal handling charges (capatazias), unstuffing and cargo handling fees, and deconsolidation of bill-of-lading fees. Rates and amounts vary.

Special customs regimes related to oil and gas activities

A number of special regimes relate to oil and gas activities, as described next.

Special bonded warehouse for oil and gas platforms

The special bonded warehouse for oil and gas platforms is a customs regime specifically targeted to cover bonded areas located in oil and gas platforms contracted by companies located abroad for research and drilling purposes. This special bonded warehouse may be operated and located in construction or conversion platforms, shipyards or other manufacturing establishments located by the sea and destined for the construction of marine structures, oil platforms and modules for such platforms.

This regime applies to materials, parts, pieces and components to be used in the construction or conversion of such facilities and allows manufacturing processes and testing activities to be performed inside the bonded facility.

The arrangement grants full suspension of federal taxes otherwise due on imports (II, IPI, PIS and COFINS) and full suspension of federal taxes otherwise due on local purchases (IPI, PIS and COFINS). Some states also extend the benefits to ICMS.

Temporary admission

The temporary admission is a special customs regime that grants total or partial suspension of federal import taxes (II, IPI, PIS, and COFINS) on the importation of equipment and general products, provided that the imported items are re-exported within a stipulated period. Failure to re-export the products results in a tax liability for the previously suspended taxes, increased by fines and interest.

Under the total suspension, the temporary admission is generally granted for a maximum period of six months, with a possible extension by the same amount of time.

Equipment and products imported for economic applications, such as those imported to be used or applied on the provision of services or production of other goods, fall under the temporary admission regime with partial suspension of the import taxes. In this case, they may remain in the country for the duration of the underlying contract (operational lease, rental, loan, etc.). Goods under financial lease agreements may not be received in under the temporary admission regime, or for the total duration of the contract supporting the operation, limited to five years.

Under the current calculation rules, II, IPI, PIS and COFINS will be partially paid and calculated at 1% per month of permanency of the imported goods in Brazil, calculated on the total amount of taxes that otherwise would be due upon nationalization. Due to recent precedents from the Brazilian Supreme Court, no ICMS is due on the importation of goods under the temporary admission regime, even when federal taxes are proportionally due, as previously explained.

Drawback

The Brazilian customs legislation provides for different types of drawback regimes; the following are the two most relevant ones.

Integrated drawback suspension

Regulated by the Foreign Trade Operations Department (DECEX), the integrated drawback suspension (Drawback Integrado Suspensão) is a special customs regime that allows the importation and local acquisition of goods to be applied or consumed in the manufacturing process for export purposes, with total suspension of federal taxes (i.e., II, IPI and PIS/COFINS-Import). These items must be subject to at least a certain manufacturing level and be composed of, or be consumed in the industrialization of, a product to be further exported. The regime also provides for the suspension of the AFRMM freight surcharge, when applicable.

As a general rule, integrated drawback suspension allows the suspension of ICMS on only imported items; there is no similar benefit for goods purchased locally under the regime. For goods purchased locally, the local invoice issued by the local supplier must be registered by the beneficiary company within the SISCOMEX system.

Internal and strict controls over the inventory of goods imported and locally acquired for industrialization and exportation under the drawback regime are required.

A Brazilian company that requests drawback suspension must comply with certain requirements to obtain approval. As a general rule, taxes may be suspended on regular imports for one year, extendable for another year. With long production cycles, the suspension may reach five years.

Integrated drawback exemption

The integrated drawback exemption (Drawback Integrado Isenção) (IDE) is a variation of the drawback regime. The main difference from the suspension framework consists in exempting imported or locally purchased items from regular taxation when similar and fully taxed items were already used in the process of manufacturing exported final goods.

IDE is a type of retroactive applicability of the drawback rules. It works as a replacement for benefited items that could have been covered by integrated drawback suspension in the past two years, but were not.

The IDE regime involves an exemption from II, IPI, PIS, COFINS. IDE applies to the importation of raw materials and goods in equal quantity and quality as the ones once used in the prior manufacturing process in Brazil of a final product that was already exported. The company benefiting from the drawback exemption must prove that the goods have been exported to obtain the tax exemption.

Certified bonded warehouse

The certified bonded warehouse (DAC) system is a special export system under which goods are deemed exported but physically remain within a bonded warehouse in Brazil. Goods remitted to a DAC facility are subject to certain export customs clearance procedures and are considered as legally exported for all fiscal, administrative and foreign-exchange purposes.

Remittances to DAC are exempted from all federal taxes (IPI and PIS/COFINS). As ICMS is a state tax, each Brazilian state establishes its own legislation and decides whether ICMS should be levied.

Goods may remain stored in this special regime for no longer than one year.

Repetro

Repetro is the most relevant tax incentive for the oil and gas industry. Repetro is a special customs regime available in Brazil for the importation, local acquisition and exportation of equipment and other qualifying assets for the oil and gas industry.

With the recent advent of Law 13,586/2017 and Normative Instruction 1,781/2017, in addition to the regular framework of Repetro valid until 2020 (for goods admitted until the end of 2018), a new version of the special regime was introduced, namely Repetro-SPED, valid until 2040. Both modalities are applicable to companies and consortiums that hold an authorization or concession to exploit oil and gas in Brazil and to its subcontractors.

In general terms, there are different types of agreements that may support the importation under Repetro, such as operational leasing, rent, loan and free loan. Note that goods covered by financial leasing agreements are not allowed under the temporary import modality of such regime, since the regime's main requirements are that the ownership of the referred goods remain with a legal entity established abroad and that such goods be imported without exchange coverage and on a temporary basis, being obliged to be re-exported once the contract terms have been fulfilled.

In summary, the Repetro-SPED provides for:

i. Fictitious exportation and subsequent importation (definitive or temporary) of main goods, as well as spare parts destined for these goods
ii. Definitive importation with full suspension of federal taxes for items listed in Annex I and II of the Normative Instruction mentioned above
iii. Temporary admission for economic use with total suspension of federal taxes for items listed in Annex II of the Normative Instruction mentioned above
iv. Definitive importation or local acquisition of raw material, intermediate products and packaging material with suspension of federal taxes

Note that the regime applies to qualifying equipment and parts with a unitary import value of US$25,000 or more.

Regarding the state VAT (ICMS) within the Repetro, there are also some relevant new considerations. Through ICMS Agreement 03/2018, signed by the National Council of Finance Policy (CONFAZ), the Brazilian States may apply the following benefits:

i. ICMS tax basis reduction on definitive importation or local acquisition under Repetro-SPED, in order that the tax burden be 3%
ii. ICMS exemption on temporary admission under Repetro-SPED
iii. ICMS exemption on exportation, even if fictitious or local sales of national products that will be later acquired under Repetro-SPED

Rio de Janeiro and São Paulo State have already internalized the provisions of ICMS Agreement 03/2018, adhering to all benefits provided.

It is important to highlight that, as the changes to the special regime are still recent, the industry is still expecting changes in the legal framework and regulations for Repetro. For example, certain parties in Rio de Janeiro are trying to revoke the rate reduction for production activities, maintaining the benefit only for exploration activities. If the state moves forward in this sense, those imports could be taxed at 18%, which is the regular import rate in Rio de Janeiro.

I. Other

International Financial Reporting Standards and Law 11638/07

Effective 1 January 2008, Law 11,638/07 prescribed, among other accounting changes, that accounting standards issued by the Brazilian Securities Commission (CVM) must all be aligned with international financial reporting standards (IFRS) adopted in the main security markets — i.e., standards issued by the International Accounting Standards Board (the IASB), which is currently considered the international reference for accounting standards.

Functional currency

Companies that adopt, for statutory purposes, a functional currency other than Brazilian reals (BRL) need to maintain a parallel accounting system totally in historical BRL (it is not the one translated in BRL for publication purposes) for all taxes calculation purposes. As a consequence, for companies that adopt different functional currency, the existence of two balances will remain.

National content

The national content rule was created to promote national industry. Under this rule, a certain percentage of goods, equipment and services must be purchased from Brazilian suppliers.

Up to ANP round 4, there were no minimum national content requirements. As from ANP round 5, the ANP has established minimum national content requirements for the exploration and development phases.

Currently, the federal government reduced the demand for national content on the new hiring of equipment used by the oil industry in exploring new areas by an average of 50%.

The modified methodology will already be valid for the next auctions of the ANP. The reduction will be implemented by changing the way the national content is calculated on the equipment. Instead of a complicated system, like the previous one, which had more than 90 items and descended to details like the type of tube used in certain equipment, the calculation will now be global. In onshore exploration fields, the percentage will be calculated in the two stages of the exploratory process: exploration and production.

With the new rules, the third round of the pre-salt and the 14th round of concessions will have fewer requirements than in recent years, with the obligation to contract in Brazil only: 18% in the exploration phase; 25% in the activities related to construction of wells; 40% for collection and disposal systems; and 25% for stationary production units (platforms). In the case of onshore blocks (for the 14th round), the requirements are 50% both in the operation phase and in the production phase.

As for rounds of marginal areas, there will be no requirement for national content, while for the second pre-salt auction, which will offer areas subject to unitization (reserves that extend beyond the limits of blocks already in operation) and will apply the same index defined in the contracts of the contiguous areas, was already expected.

Minimum national content on the oil and gas production, in %		old rule	New rules
Onshore	Exploration phase	70	50
	Development phase	77	50
Offshore (above 100 meters)	Exploration phase	37	18
	Well construction	55	25
	Oil collection and disposal system	55	40
	Platforms	55	25

Next rounds

In June 2018, the fourth round of bidding for blocks under the pre-salt auction regime will offer five new areas in the pre-salt polygon. The areas named Itaimbezinho, Três Marias, Dois Irmãos, Saturno and Uirapuru will be offered in the Campos and Santos basins.

The 15th round of bidding under the concession regime is scheduled for 29 March 2018. The round will be offer 70 blocks, 49 in the maritime basins of Ceará, Potiguar, Sergipe-Alagoas, Campos and Santos, including two blocks adjacent to Saturn. In addition, 21 blocks will be offered in the terrestrial basins of Paraná and Parnaíba.

Next BID rounds:

- R154 (concession) — March 2018 (288 blocks)
- Pre-salt 4 new areas (sharing) — 2018
- Pre-salt 5 new areas (sharing) — 2019

Repatriation of capital

Repatriation of share capital is generally not restricted if the foreign investor has registered its foreign direct original investment and subsequent capital increases or capitalization of earnings with BACEN.

Repatriation of capital may be accomplished by the sale of Brazilian shares to a local resident by a capital reduction, redemption of shares or liquidation of the Brazilian company. Commercial law contains specific rules on the redemption of shares and on companies repurchasing their own shares.

ICMS taxation over oil extraction — Rio de Janeiro State

At the end of 2015, Rio de Janeiro State published Law 7,183/15 establishing a tax event for ICMS taxation purposes post-extraction of oil and when the product passes through the Production Measure Station. In the past, specifically in 2003 (Law 4,117/03 — "Noel Law"), the Rio de Janeiro State tried to start charging ICMS in a similar situation; however, the State decided to suspend the effects of such law due to several arguments in favor of considering such law unconstitutional.

The new law, published at the end of 2015, has similar issues and constitutional gaps in comparison to the Noel Law. This recent topic has generated a lot of discussion in the oil and gas industry about considering, again, whether such legal disposition is unconstitutional. In 2016, the Brazilian Association of Oil Exploitation Companies (ABEP) filed a lawsuit against the Rio de Janeiro State in order to declare the unconstitutionality of Law 7,183/15. Although the Brazilian Supreme Court has not yet decided on this, the Attorney General of the Republic (PGR) has already positioned preliminarily in favor of the unconstitutionality of New Noel Law; nevertheless, it is important to follow the Supreme Court's final position.

Creation of fee payment to control and monitor environmental inspection related to research, exploration and production of oil and gas (TFPG) — Rio de Janeiro State

Following the ICMS taxation over oil extraction in the end of 2015, the Rio de Janeiro State enacted State Law No. 7.182 (of 29 December 2015), creating a new fee (TFPG) based on the regular environment inspections by the Rio de Janeiro Institute of Environment (INEA) on the activities related to the oil and gas industry. The TFPG fee would be charged on the fixed price of 1 UFIR-RJ (an annual state index that represents in 2018 3,29396BRL) per oil barrel produced.

For various reasons, the TFPG fee has also been discussed by the oil and gas industry, since some elements would classify this fee, too, as unconstitutional. Similar to following developments of the ICMS charge, it is important to follow discussions of the TFPG fee during the year, because the current scenario may change if the Brazilian courts find such fee to be unconstitutional.

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Tax regime applied to this country

- ■ **Concession**
  - □ Royalties
  - □ Profit-based special taxes
  - ■ Corporate income tax
- □ **Production sharing contracts**
- □ **Service contract**

A. At a glance

Fiscal regime

In Cambodia, the oil and gas fiscal regime is classified as the Real Regime System of Taxation (a self-assessment system). The principal taxes that apply are as follows:

- Tax on Income (TOI)/Corporate Income Tax (CIT) — 30% plus additional tax on exceed income ratio
- Investment incentives — Exemption from "minimum tax" (see Section B below); and import duty exemption under investment incentives
- Withholding taxes
- Indirect taxes

An additional tax on excess income also applies and this tax is based on an excess accumulated income to accumulated expense ratio which applies at the following progressive rates:

Excess income ratio	Rate
0 – 1.3	0%
More than 1.3 – 1.6	10%
More than 1.6 – 2.0	20%
More than 2.0 – upwards	30%

B. Fiscal regime/Real Regime System

Corporate income tax

Under the Law on Financial Management (LOFM) for 2018, taxpayers are taxed at a rate of 30% on the income realized from petroleum and mining operations. The TOI/CIT liability is calculated by multiplying the rate of tax with the taxable income.

The taxable income usually differs from the taxpayer's accounting profits due to certain tax deductions while certain deductible expenses for accounting purposes need to be added back in the tax calculation. For the calculation of taxable income for a tax year, taxpayers should use the accounting profit before tax to which adjustments for deductible and nondeductible expenses should be applied.

In addition to the above TOI, taxpayers are subject to additional tax based on an excess income ratio, which applies at progressive rates as follows:

Exceed income ratio	Rate
0 – 1.3	0%
More than 1.3 – 1.6	10%
More than 1.6 – 2.0	20%
More than 2.0 — Upwards	30%

"*Excess income ratio*" is a division of accumulated income to accumulated expenses which have been derived and incurred from petroleum or mining operations during current tax year.

"*Taxpayers*" under this provision refers to:

- Contractor: a person with whom the Cambodian government has concluded a petroleum agreement
- Licensee: a person who has been issued or granted mining rights

Operating expenses in petroleum and mining exploitation

Under the LOFM 2018, operating expenses incurred in petroleum and mining exploitation (i.e. an operating licensed block) are deductible from the current tax year's gross income for TOI calculation purposes.

Interest expense deduction

Taxpayers are allowed to claim interest expense deductions based on a debt-to-equity ratio of 3:1.

Provision for environmental restoration costs

Taxpayers are allowed to claim deductions on environmental restoration costs in relation to petroleum and mining operations in the tax year in which the provision is made and approved by the authorized authorities.

However, if the actual environmental restoration costs are more/less than the provision, the difference is either deductible or taxable for the TOI purposes in the tax year in which the environmental restoration is completed.

Depreciation and amortization

Petroleum and mining operation:

For both petroleum and mining operations, research and exploration expenditure should be amortized on a straight-line basis over the expected life of the commercial production under the development plan or five years, whichever is sooner.

For petroleum operations, development expenditure should be amortized on a straight-line basis over the expected life of the commercial production under a development plan or 10 years (seven years for mining operations).

Where the development plan is less than one year, the development expenditure can be included with the research and exploration expenditure and amortized as above.

Tangible and intangible assets other than research and exploration, or development expenditure:

Under the tax regulations, tangible assets are categorized into four classes and are depreciated at the following rates:

Classes	Assets	Method	Rate (%)
1	Building and structures	Straight-line	5
2	Computers, electronic information systems, software, and data-handling equipment	Declining-balance	50
3	Automobiles, trucks, and office furniture and equipment	Declining-balance	25
4	Other tangible property	Declining-balance	20

Intangible assets with a limited useful life, such as patents, copyrights, drawings, models and franchises, can be amortized over their useful life on a straight-line basis. If the life of intangible assets cannot be determined, the assets are amortized using the straight-line method at a rate of 10%.

Losses carried forward

For petroleum operations, taxpayers can carry forward taxable losses up to 10 years, while for mining operation taxpayers can only carry forward taxable losses up to 5 years. Tax losses carry forward shall be unutilized on a "first-in, first-out" basis and it must be utilized in the same licensed block only.

Minimum tax

Minimum tax is exempted.

TOI/CIT returns and payments

Resident taxpayers must file annual TOI/CIT return within three months after the end of the tax year.

Investment incentives

Investment incentives may be applicable for the "qualified investment projects" (QIP), which is a tax deferral incentive. Once the QIP is granted the taxpayer is entitled to certain investment incentives and the contractor will need to register their investment with the Council for the Development of Cambodia.

Exploration of gas, oil and all kinds of mining activities, including supply bases for gas and oil activities are eligible for customs duty exemption although this exemption does not apply to TOI/CIT.

C. Withholding tax

Payments to resident taxpayers

Resident taxpayers carrying on a business in Cambodia must withhold tax from payments made to other resident taxpayers at the following rates:

Description	Rate (%)
Interest paid to recipients other than domestic banks and saving institutions	15
Royalties	15
Payments to individuals or non-registered taxpayers for services, including management, consulting and similar services	15
Rent paid for movable and immovable property	10

Payments to nonresident taxpayers

Under the LOFM for 2017, WHT of 14% applies to all the payments of Cambodian sourced income by a resident or permanent establishment of a non-resident to a non-resident.

In general, the above withholding taxes are considered to be final taxes. However, the withholding tax on rent paid to registered resident taxpayers may be offset against any liability for the TOI.

If withholding tax is not withheld from the recipient, it is borne by the payer. Accordingly, the withholding tax is not deductible for TOI/CIT purposes.

In addition, interest free loans are allowable as of 2014 and in this regard the tax authority will not deem an interest expense on loans in order to impose withholding tax. Cambodian taxpayers in receipt of zero interest loans need to register the loan with the tax authority within 30 days of the loan agreement being entered into and a copy of the loan agreement should be provided to the tax authority.

Withholding tax returns and payments

Resident taxpayers must submit withholding tax returns and remit withholding taxes to the tax authorities by the 20th day of the following month.

D. Indirect taxes

Export duties

The export of crude oil is subject to export duty at the rate of 0% up export.

Import duties

Import duties are levied on a wide range of products, with rates varying from 0% to 35%. For details of the exemption, see the subsection on investment incentives in Section B above.

Specific Tax on Certain Merchandises and Services (STCMS)

STCMS is a form of excise tax that applies to the import or domestic production of petroleum products. The rates on the import of petroleum products range from 4.35% to 25%. Crude oil is not subject to STCMS.

Value-added tax

Cambodia's VAT applies to the business activities of Real Regime taxpayers making taxable supplies. Such businesses must charge VAT on the value of the goods or services supplied. VAT also applies on the duty-paid value of imported goods.

The standard rate of VAT is 10%. A 0% rate of VAT applies for goods exported from Cambodia and services consumed outside Cambodia. A 0% rate also applies to enterprises in supporting industries and subcontractors that supply certain goods and services to exporters.

A resident taxpayer must complete the VAT registration within 30 days after the date on which the taxpayer becomes a taxable person. The filing of VAT returns and the payment of VAT due for a particular month must be made by the 20th day of the following month.

E. Financing consideration

According to Cambodia's tax regulations, a limitation of interest rates on loans obtained from banks and other enterprises should be determined as follows:

- For loans from third parties, the interest rate should not exceed 120% of the market rate at the time of the loan transaction;
- For loans from related parties, the interest rate should not exceed the market rate at the time of loan transaction.

The term "market rate" in this context is the average interest rate on loans from at least five of the largest commercial banks in Cambodia to their customers. The "market rate" is published annually by the General Department of Taxation (GDT) in January or February for the preceding year. Interest costs relating to an interest rate higher than the rate quoted by the GDT will not be deductible for TOI purposes.

The 2017 market interest rate for USD denominated loans was 9.31%, and this is an annual rate. Furthermore, the market interest rate for loans denominated in Khmer Riel (KHR) for 2017 was 12.12% per annum. This rate is also an average of interest rate for KRH denominated loans from three commercial banks in Cambodia.

In addition, deductions for interest are limited to 50% of taxable profits plus interest income earned during the tax year, if any, and interest expenses and other expenses are excluded from this calculation. The disallowed interest may be carried forward and a deduction claimed in subsequent years, subject to the same limitations.

Furthermore, for loans as stated above, the taxpayer should notify and submit the agreements and other supporting documentation to the tax authority within 30 days of the loan transaction being entered into. If the taxpayer fails to notify the tax authority by providing it with the supporting documents, the loan amount will be added to the taxpayer's taxable income for that year.

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Cameroon's fiscal regime applicable to the upstream petroleum industry consists of Cameroon's General Tax Code, the Cameroon Petroleum Code and the production sharing contracts (PSCs) or concession agreements (CAs) concluded between the state of Cameroon and a "holder," which under the Cameroon Petroleum Code is a petroleum company or a consortium of commercial companies at least one of which is a petroleum company that is linked with the state by a petroleum contract. The main taxes applicable in this sector are:

- Corporate income tax
- Annual surface rental tax
- Royalties on the production
- Additional petroleum tax
- Bonuses
- Stamp and registration duties

Once negotiations on a PSC or CA are concluded between the contractor and the state of Cameroon, the agreement is signed by the minister in charge of petroleum activities following approval of the Minister of Finance. Each PSC and CA is presented for approval to the President of Cameroon and, once approved, published in the *Official Journal* and registered in accordance with the conditions provided by the law.

The state has an option to participate directly or indirectly through a public entity in the joint venture agreement with the consortium. Usually, this participation will range from 5% to 25%. The state's share should equal a percentage of output as reduced by petroleum costs incurred by the contractor — i.e., a percentage of oil production profit. The share will vary in accordance with the daily average of total available production.

Corporate income tax

The corporate income tax rate is provided for in the PSC. It may vary from 33% up to a maximum of 50%.

Bonuses

There are typically two sorts of bonuses: signature and production.

A "signature bonus" is one that a holder pays to the state for the conclusion of a petroleum contract. A lump sum in US dollars is to be paid on the effective date of signature.

A "production bonus" is one that a holder pays to the state depending on the quantities of hydrocarbons produced. In this case, a lump sum in US dollars is to be paid at the start of production of hydrocarbon output, and a further lump sum in US dollars is to be paid when the cumulative amount of production since the start of the exploitation phase reaches a certain level specified in the PSC.

Royalties (applicable only to CA holders)

The tax base and royalty rate are provided for in the CA. Royalties are payable on a monthly basis.

Surface rental tax (applicable only to PSC holders)

An annual surface rental tax is levied in Cameroon. This tax is payable in cash each calendar year before 31 January, based on the surface area on 1 January each year or, for the first year, on the surface area on the effective date.

The relevant rates are:

- The first year — XAF1,750/km²
- The second year — XAF2,000/km²
- The third year — XAF3,500/km²
- The following years — XAF5,500/km²

Other allowances and incentives

See Sections C and D below for further details.

B. Fiscal regime

Corporate income tax

Corporate income tax (CIT) is levied on the taxable profits of the contractor. "Taxable profits" amount to net profits arising from all upstream activities performed in Cameroon during the taxable period. "Net profits" represent the difference between the opening and closing value of net assets for the relevant year of assessment, less extra contributions, plus any amounts taken by associated companies during this period. Net profits are computed after deduction of all expenses that are necessary to perform upstream operations (as supported by relevant invoices), depreciation, reserves and losses, as applicable.

CIT is payable in cash, except where the state expressly requests settlement by means of a corresponding quantity of hydrocarbons. Except as otherwise provided for by the PSC, up-front CIT is due monthly. The monthly amount is 2.2% of the turnover of the previous month, and any remaining balance due for the fiscal year has to be paid before 15 March.

The Cameroon's General Tax Code does not provide for profits from one project to be offset against losses from another project held by the same tax entity. Accordingly, each petroleum project should be accounted for separately.

Cost oil

The "cost oil" (or "reimbursement oil") is the portion of the available production applied for reimbursement of petroleum costs. "Petroleum costs" are all expenses borne by the contractor within the framework of the PSC and determined in accordance with accounting principles.

Government share of profit oil

After the deduction of cost oil, remaining production volumes are shared between the state and the contractor according to the value of the ratio *R* as defined in the table below. *R* represents the ratio of "net cumulated revenue" to "cumulated investments," which are determined in accordance with the cumulated amounts from the effective date until the end of the calendar year. "Net cumulated revenue" is the cumulative value of the benefit after assessment of the corporation tax. "Cumulated investments" are the cumulative value of expenditure on research, evaluation and development.

Non-recoverable expenditures

Non-recoverable expenditures are those considered by the PSC to be non-recoverable. They notably include payments made for the settlement of fees, charges or expenses not directly related to the petroleum operations or not necessary for the undertaking of these operations.

They include, for instance, payments made for:

- Signature bonuses
- Costs relating to the period prior to the effective date
- External auditing costs paid by the contractor within the framework of the particular relationship between the companies constituting the contractor
- Penalties

Surface rental tax

The payment of a surface rental tax is due annually as of the signature of the PSC or service contract. Based on a typical PSC, the annual surface rental tax is determined as follows:

- The first year — XAF1,750/km^2
- The second year — XAF2,000/km^2
- The third year — XAF3,500/km^2
- The following years — XAF5,500/km^2

This tax is payable in cash each calendar year on or before 31 January, based on the surface area on 1 January each year or, for the first year, on the surface area on the effective date.

Royalty regime and additional petroleum tax

Contractors under a CA are subject to payment of a monthly royalty on the free-on-board (FOB) value of hydrocarbons produced, to be paid in cash or in kind at the state's option. The rate, basis of calculation, declaration, settlement and recovery of this royalty are specified in the CA.

Contractors can be subject to an additional petroleum tax that is based on the profitability of the petroleum operations. The rate, basis of calculation, declaration, settlement and recovery of this additional tax are again specified in the CA.

Bookkeeping

Holders of petroleum contracts or businesses are required to establish a separate account for their petroleum operations for each fiscal year. This bookkeeping will enable the establishment of accounting for production and profits as well as a balance sheet highlighting the profits, assets and liabilities directly allocated to hydrocarbon operations.

Holders of petroleum contracts undertaking petroleum operations in Cameroon are permitted to carry out bookkeeping and accounting records in US dollars and to record their registered capital in this currency. The method for such accounting in US dollars will be detailed in the petroleum contract between the holder of the contract and the state of Cameroon.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Land and intangible assets are not depreciable for tax purposes. Other fixed assets may be depreciated on a straight-line basis at rates provided for under the PSC and the General Tax Code. The following are some of the applicable straight-line rates.

Asset	Rate (%)
Buildings	5 to 20
Plant and machinery and transport equipment	7.5 to 33
Office equipment	10 to 20

D. Incentives

Ability to carryforward losses

Under the General Tax Code, losses arising from petroleum operations may be carried forward for up to four income tax years; but the PSC may provide for a longer period. Losses may not be carried back.

VAT incentives

The supply of goods and services of any kind that are directly linked to petroleum operations are exempt from value-added tax (VAT).

Contractors' suppliers, subcontractors, services providers and affiliates are also exempt from VAT otherwise due on account of sales made, services rendered or work performed in connection with the contract.

E. Withholding taxes

Dividends

Dividends paid by a company incorporated in Cameroon to a nonresident are exempt from the tax on dividends, as provided for by the Petroleum Code.

Interest

A 16.5% withholding tax (WHT) is imposed on interest paid on debt claims, bank deposits and guarantees to corporations that do not have their head office in Cameroon or to nonresident individuals.

However, the following interests are exempted: (i) interests paid in consideration for foreign loans of a maturity period of at least seven years and (ii) interests paid to nonresident lenders in consideration for funds related to the development phase.

Royalties

WHT will be levied on remuneration paid to foreign companies or individuals providing services to the local company if the services are used in Cameroon and if the foreign entities have no professional installation in Cameroon.

The rate of WHT is in principle 15% of the gross amount. However, the specific cases below shall be considered:

On one hand, remuneration of all types of services provided to oil companies during the research and development phases are subject to a reduced WHT rate of 5%.

On the other hand, companies engaged in drilling, research or assistance work on behalf of oil companies, whose activity is deemed to constitute a permanent establishment, may opt for a 15% deemed-profit tax. In this respect, they must formally renounce the common taxation regime and declare that they opt for the application of the withholding tax regime. They are still subject to withholding requirements with regard to their local and foreign subcontractors and reporting obligations of the related transactions. Related invoices for foreign subcontractors must indicate the gross amount paid and the 15% WHT applied.

However, remuneration paid for assistance services, equipment and material rentals and any other services provided by affiliated companies, not having a permanent establishment in Cameroon, at actual costs during the exploration and development phases shall be exempted from the WHT on royalties.

Branch remittance tax

Except as otherwise provided for by international tax treaties, profits made by companies that do not have their head office in Cameroon are deemed to be distributed to foreign entities (individual or corporate) that are not resident or do not have their head office in Cameroon. However, under the Petroleum Code, contractors are exempt from any tax on profits or income distributed.

Capital gains in relation to the assignment of interests

Capital gains deriving from the sale of participating interests in the PSC (farm-ins and farmouts) and shares of companies that own exploration or exploitation authorizations are subject to the capital gains tax at the rate of 16.5%. This also applies to indirect transfers.

The capital gains tax is withheld by the assignor. In case the transaction is done abroad, the resident company (i.e., the assignor) and the nonresident entity are jointly liable for the payment of the tax.

This tax is levied on the difference between the sale price of the assets and the cost price, or capital, if the cost price cannot be determined.

F. Financing considerations

Thin capitalization limits

Interests on funds made available to the company by shareholders in addition to their capital contributions, regardless of the form of the company, are deductible within the limit of those calculated at the rate of the Central Bank increased by two percentage points. However, with respect to shareholders who directly or indirectly own at least 25% of the share capital or corporate voting rights, such deduction shall be possible only if:

- The sums made available by all the partners do not exceed two and half times the amount of the equity; otherwise, interests on the excess amount shall not be deductible.
- The interests paid to the shareholders do not exceed 25% of profit before the application of the corporate tax and before deduction of the said interests and amortizations taken into account in determining such profit; otherwise, the excess amount of interests shall not be deductible

G. Transactions

Asset disposals

Income realized through the transfer of certain classes of asset of the holder is offset against the balance of petroleum costs to be recovered.

Capital gains are taxed at the regular corporate rate, which may vary from 33% up to a maximum of 50%. However, the tax due can be deferred in the event of a merger. Capital gains deriving from the sale of a petroleum permit or an authorization, or a participating interest in a permit or authorization, are also subject to income tax on securities at the rate of 16.5%. Given that the seller is normally subject to CIT in Cameroon, the income tax on securities withheld at source by the buyer (as required by the law) will be considered as a tax credit for the seller with respect to the said CIT.

If the business is totally or partially transferred or discontinued, only one half of the net capital gain is taxable, provided the event occurs less than five years after the startup or purchase of the business, and only one third of the gain is taxable when the event occurs five years or more after the business is begun or purchased.

The registration fees to be paid for asset disposals are:

- Transfer of exploration permit — XAF6 million
- Transfer of production permit — XAF250 million

A PSC may be terminated if all the assets are transferred.

H. Indirect taxes

Import duties

Provisions relating to customs duties are identical for most contracts (PSC or CA). They usually provide that the designated contractor and its subcontractors are allowed to import into Cameroon any goods, materials, machinery, equipment and consumer goods that are necessary to carry out qualifying operations, in its own name or in the name of its subcontractors, as follows:

- The contractor or third parties acting on its behalf or its subcontractors may import without restriction all materials, products, machinery, equipment and tools under the regulations relating to temporary admission (AT) or temporary imports (IT), either normal or special, on condition that these goods are to be used exclusively for qualifying operations and that they can be re-exported at the end of their use.
- The contractor or third parties acting on its behalf or its subcontractors are allowed to import, without payment of duty, materials, products, machinery, equipment and tools to be used exclusively for oil prospecting and exploration in the specified area, provided these are listed in the Annex to Act No. 2/92-UDEAC-556 dated 30 April 1992.
- The contractor or third parties acting on its behalf or its subcontractors may be granted permission by the Ministry of Economy and Finance to import, at a reduced rate of duty of 5%, materials, products, machinery, tools and equipment that, although they do not meet the criteria In the first two bullet points, are necessary and required for production, storage, treatment, transport, shipment and transformation of hydrocarbons.

Export duties

There is no export duty applicable.

VAT

The supply of goods and services of all kinds that are directly linked to petroleum operations are exempt from VAT.

Ancillary activities that are not linked to petroleum operations will be subject to VAT at a rate of 19.25%.

Stamp duties

Stamp duties may be payable on the registration of various contracts concluded by an oil company.

Registration fees

Registration fees depend on the type of agreement concluded.

I. Other

Exchange controls

The Economic and Monetary Community of Central Africa Countries (CEMAC) Act, dated 29 April 2000, provides exchange control regulations that apply to financial transfers outside the "franc zone," which is a monetary zone including France and mostly French-speaking African countries. However, for the duration of the PSC, Cameroon Authorities provide certain guarantees to the contractor for operations carried out within the framework of the PSC or CA, especially:

- The right to open a local or foreign bank account in local or foreign currencies
- The right to collect, and maintain offshore, all funds acquired or borrowed abroad, including sales receipts, and to freely dispose thereof, to the extent these exceed the requirements of its operations in Cameroon
- The right to repatriate capital invested under a PSC and to transfer proceeds relating to the capital — in particular, interest and dividends
- The right to provide offshore payments to nonresident suppliers

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies to the oil and gas industry in Canada consists of a combination of royalties and income taxation:

- Corporate income tax — federal corporate tax rate at 15% in 2018 and provincial corporate tax rates that vary from 11.5% to 16%, depending on the province
- Royalties — Crown royalties applicable to Government-owned lands, at a rate of up to 45%; separate regime for oil sands and offshore production; freehold royalties vary from lease to lease
- Investment – IC – R&D[1] 15%

B. Fiscal regime

Corporate income tax

For Canadian income tax purposes, a corporation's worldwide taxable income is computed in accordance with the common principles of business (or accounting) practice, modified by certain statutory provisions in the Canadian Income Tax Act. In general, there is not a special tax regime for oil and gas producers.

Depreciation, depletion or amortization recorded for financial statement purposes is not deductible; rather, tax-deductible capital allowances specified in the Income Tax Act are allowed.

Oil and gas corporations are taxed at the same rate as other corporations. Corporations are taxed by the federal Government and by one or more provinces or territories. The basic rate of federal corporate tax is 25%, but it is reduced to 15% by an abatement of 10% on a corporation's taxable income earned in a province or territory. Provincial or territorial tax rates are added to the federal tax, and they generally vary between 11.5% and 16% of taxable income, depending on the province.

1 *IC: investment credit; R&D: research and development.*

No tax consolidation, group relief or profit transfer system applies in Canada. Each corporation computes and pays tax on a separate legal entity basis. Business losses referred to as non-capital losses may be carried back 3 years and carried forward 20 years.

Gains resulting from a disposal of capital property are subject to tax. Capital gains or losses are determined by deducting the adjusted cost base of an asset from the proceeds of disposition. One-half of the capital gain (the taxable capital gain) is subject to tax at regular income tax rates.

Capital losses are exclusively deductible against capital gains and not against any other income. However, non-capital losses are deductible against taxable capital gains, which are included in taxable income. Capital losses can be carried back three years and forward indefinitely for use in future years. When a corporation is acquired, its unused capital losses expire.

Oil and gas rights are Canadian resource properties or foreign resource properties, which are not capital properties.

Royalties

Oil and gas producers are required to make royalty payments to the holder of the mineral rights. In Canada, the majority of the mineral rights are owned by the provincial, territorial or federal governments (the Government) or by First Nations.

Royalty payments to the Government are referred to as "Crown royalties." The computation of Crown royalties is fairly complex and varies from province to province, because each province or territory has its own royalty regime. In general, computations are based on a function of well productivity and the wellhead price. Crown royalty rates typically range up to 45%. Separate tax and royalty regimes may apply to oil sands, the Arctic and Atlantic offshore production.

Indian Oil & Gas Canada (IOGC) is a regulatory agency responsible for managing and administering the exploration and development of crude oil and natural gas on First Nations reserve lands. IOGC assists First Nations with all stages of resource management. Subsurface rights are part of an Indian reserve; however, the title to subsurface rights, including oil and gas, is held by the Crown in trust for the First Nations. As a result, a producer must obtain the necessary licenses and permits from IOGC when exploring and developing resources on First Nations land. First nations reserve lands and the resources on them are a separate entity in Canada and are governed by the Indian Oil & Gas Act. Indian royalties are also unique and are negotiated between the lessee and the Native bands on a well-by-well basis. Unlike Canada, IOGC does not take oil in kind, and all royalties are paid in cash.

Royalties paid on mineral rights that are privately owned are called "freehold royalties." These royalties are typically based on production, and the royalty percentage varies according to the freehold lease. Because the Crown does not receive royalties on freehold leases, "freehold mineral taxes" are levied by the Crown on freehold leases, and the tax is based on production.

Royalties are deductible in determining income for tax purposes.

Unconventional oil and gas

There are no special provisions or rules with respect to unconventional gas. For unconventional oil, see Section D.

C. Capital allowances

Oil and gas rights

The cost of oil and gas rights is accumulated in a pool called Canadian Oil and Gas Property Expense (COGPE). Each year, the pool is increased by the cost of new acquisitions and reduced by the proceeds from disposition of oil and gas rights and by deductions claimed from the pool. COGPE does not include the cost of any tangible or depreciable property, such as oil and gas machinery or equipment.

Deductions in computing income for income tax purposes for a taxation year may be claimed up to a maximum amount of 10% of the unclaimed COGPE balance. The deduction is discretionary, and unclaimed COGPE may be carried forward indefinitely in order to be claimed in future years.

Oil and gas exploration

The costs incurred to determine the existence, extent and location of oil and gas (such as seismic, geological, geophysical and geochemical expenses) and the cost of drilling a well that is unsuccessful and abandoned within a short time after drilling is completed are accumulated in a pool called Canadian Exploration Expense (CEE). Each year, the CEE pool is increased by new expenditures and reduced by the amount claimed from the pool. CEE does not include the cost of any tangible or depreciable property, such as oil and gas well machinery or equipment.

A deduction for a taxation year may be claimed up to a maximum amount of 100% of the unclaimed CEE balance. The deduction is discretionary, and unclaimed CEE may be carried forward indefinitely, to be deducted in future years. A corporation that carries on an oil and gas business cannot claim a CEE deduction in a taxation year if the deduction would create or increase a loss for tax purposes for that year.

Oil and gas development

The costs incurred to drill and complete an oil or gas well for the production of oil and gas are accumulated in a pool called Canadian Development Expense (CDE). Each year, the CDE pool is increased by new drilling and completion expenditures, and reduced by the amount claimed from the pool. The CDE does not include the cost of any tangible or depreciable property, such as oil and gas well machinery or equipment.

A deduction for a taxation year may be claimed to a maximum amount of 30% of the unclaimed CDE balance. The deduction is discretionary, and the unclaimed CDE may be carried forward indefinitely in order to be deducted in future years, subject to the 30% limitation.

Foreign exploration and development

The costs incurred to acquire foreign oil and gas rights and the expenses incurred to explore or develop a foreign oil and gas property are accumulated in a pool called Foreign Resource Expense (FRE). A separate FRE pool must be maintained for all FRE expenditures for each particular country. FRE does not include the cost of any tangible or depreciable property, such as oil and gas well machinery or equipment.

A corporation that carries on an oil and gas business is permitted to claim a minimum 10% FRE deduction in a taxation year, regardless of whether it has any income from the foreign resource property for the year. The deduction for a particular taxation year may be increased to the lesser of 30% of the FRE pool for a particular country or the income for the year from the foreign resource property in that country. Unclaimed FRE may be carried forward indefinitely in order to be claimed in future years.

Well equipment

The acquisition cost for oil and gas well equipment used for the exploration, development and production of oil and gas is accumulated in a pool called Class 41. Each year, the Class 41 pool is increased by the cost of oil and gas well equipment acquired in the year. It is reduced by deductions claimed from the pool (capital cost allowances) and by the proceeds of disposition (up to the original cost) of the oil and gas equipment that was previously added to the pool.

A deduction may be claimed up to a maximum amount of 25% on the unclaimed Class 41 pool balance. The deduction is discretionary, and the unclaimed Class 41 pool may be carried forward indefinitely in order to be claimed in future years. Only one-half of the normal 25% deduction is allowed in respect of the additions in the year. Special available-for-use rules determine when the cost of oil and gas equipment is first available for the purposes of claiming a deduction.

D. Oil sands operations

The Canadian tax rules do not have a specific section that covers the taxation of oil sands operations. The tax treatment of oil sands project expenditures depends on a number of determinations, which are affected by factors such as the material being extracted and the types of operations involved.

The two most common types of oil sands operations are open-pit mining and in situ projects. In situ operations involve oil wells that can generally be compared with the oil wells used for conventional oil production. Open-pit mining is used to remove and process oil sands (to extract bitumen) at surface level, whereas in situ techniques are used when the oil sands are located at depths that are not economical to reach through surface mining.

The acquisition cost of an oil sands lease or other oil sands resource property is treated as COGPE.

Expenses incurred for performing geological, geophysical or geochemical activities and for trenching, prospecting, digging test pits and preliminary sampling for an oil sands project may be eligible for treatment as CEE.

Costs incurred during oil sands development using an open-pit mine or an in situ project for production may be claimed as capital cost allowance (CCA) deductions which are generally available for equipment acquired for oil sands operations at 25% on a declining-balance basis or CDE for drilling and completion expenditures.

E. LNG operations

While Canada does not have current liquid natural gas (LNG) exports, there has been a significant increase in activity in this area, and a number of LNG projects are proposed. With the expected growth in LNG exports, particularly from the west coast, the province of British Columbia (BC) enacted a new tax on LNG activities (the LNG Tax).

However, the current BC New Democratic Party (NDP) government has revised the fiscal framework in BC to put natural gas development on a level playing field with other industrial sectors. The new framework provides for the elimination of the LNG Tax that had required LNG-specific tax rates (discussed in more detail below).

By way of background, the LNG Tax is a BC provincial tax separate from the BC income tax. LNG Tax applies for taxation years beginning on or after 1 January 2017 to profits from an "LNG source," which is defined as liquefaction activities carried out at or in respect of a particular LNG facility in BC. The LNG Act distinguishes not only between an LNG source and a non-LNG source, but also between each particular LNG source. Thus, if a person has an LNG source and a non-LNG source, LNG Tax applies only to income from the LNG source, and if the person has more than one LNG source (i.e., the person undertakes liquefaction activities at or in respect of more than one LNG facility), LNG Tax applies separately on a non-consolidated basis to each LNG source.

Conceptually, LNG Tax applies only to a ring-fenced set of activities, from the input of feed gas to an LNG facility to the sale of LNG from the BC coast. If there is no actual transaction at these boundaries, sales or purchases (as applicable) are deemed to occur at amounts determined in accordance with specific transfer pricing rules.

The LNG Tax is a two-tier tax. A tier one tax of 1.5% applies to an LNG taxpayer's net operating income. A tier two tax of 3.5% (5% for taxation years beginning on or after 1 January 2037) applies to an LNG taxpayer's net income. Computations of "net operating income" and "net income" generally begin with the computation of net income for tax purposes but exclude significant items, such as interest and depreciation. Tier one tax is creditable against tier two tax, such that the maximum aggregate LNG Tax payable will be at the tier two rate. LNG Tax is not deductible for federal or provincial income tax purposes under current legislation. A natural gas income tax credit (3% of gas purchased for LNG operations) is available from 1 January 2017 to reduce corporate income tax in BC. Unused credits can be carried forward indefinitely as long as there is income from liquefaction activities and a permanent establishment in BC.

In March 2018, the BC NDP Government announced that it would repeal the LNG Tax, if a positive final investment decision was made to build an export facility in Kitimat located in northern BC.

F. Incentives

Scientific research and experimental development

Scientific research and experimental development (SR&ED) is a federal incentive tax credit (ITC) program to encourage innovation, economic development and job creation in Canada. SR&ED is defined as the systematic investigation or research carried out in a field of science or technology by means of experiment or analysis.

Eligible SR&ED work is classified into the following categories: (a) basic research, (b) applied research, (c) experimental development and (d) specific support work.

Expenditures must be claimed in the fiscal year in which SR&ED activities were performed. Eligible expenditures are classified into the following categories: (a) salaries and wages, (b) materials, (c) Canadian contractors and (d) overhead expenses incremental and directly attributable to the prosecution of SR&ED.

SR&ED expenditures are eligible for federal ITC of 15%. In addition, most provinces offer similar incentives on eligible expenditures, with ITC rates varying from 10% to 20%. In some cases, the ITCs that are not required to offset taxes otherwise payable are refundable.

The treatment of SR&ED expenditures has the following special features:

- Generally, SR&ED ITCs are used to offset taxes otherwise payable. Unused SR&ED ITCs may be carried back for up to three years and forward for up to 20 years.
- Current expenditures are accumulated in a special pool that can be deducted at a rate of 100% in the current year or in any subsequent year. No time limit applies for deducting these amounts.
- If these expenditures are carried out in the course of carrying on an oil and gas business in Canada, they are deductible when computing the income from that oil and gas business for income tax purposes.

G. Withholding taxes

Under the Income Tax Act, withholding tax (WHT) is imposed at a rate of 25% on interest, dividends, royalties and certain other payments; however, the rate may be reduced under an applicable tax treaty.

Interest

Interest paid to arm's-length nonresident persons is exempt from WHT (other than in respect of participating debt). Interest paid to non-arm's-length nonresident persons is subject to 25% WHT, unless the rate is reduced by an applicable treaty. Generally, the reduced treaty rate is either 10% or 15%; however, the Canada–US Income Tax Convention provides for a 0% WHT rate for interest paid to non-arm's-length US residents that qualify for benefits under the Canada-US Income Tax Convention.

Dividends

Dividends paid to nonresidents are subject to 25% WHT, unless the rate is reduced by an applicable treaty. Generally, the reduced treaty rate is 15%. If the nonresident shareholder is a corporation that has a substantial interest in the payer (usually defined as 10% of the votes and value), the dividend WHT rate is typically reduced to either 5% or 10%, depending on the applicable treaty.

Oil and gas royalties

Oil and gas royalties paid to nonresidents are generally subject to 25% WHT, and this rate is not usually reduced under tax treaties.

Branch remittance tax

In general, repatriated branch profits (i.e., after-tax income, subject to an allowance for investment in Canadian property) are subject to an additional 25% tax. If a nonresident corporation that carries on business in Canada is resident in a treaty country, in most cases, the branch profits tax rate is reduced by the applicable treaty to either 5% or 10%.

H. Financing considerations

Interest expense is generally deductible, provided that the interest is a reasonable amount and that it is incurred pursuant to a legal obligation to pay interest on borrowed money or on an amount payable for property and that it is used for the purpose of earning income from a business or property. Canadian transfer pricing rules apply to the interest rate on a debt owed to a non-arm's-length nonresident.

Thin capitalization restrictions

Canada has thin capitalization rules that can disallow a deduction for interest payable by a Canadian corporation on debts owed to "specified nonresidents." These rules generally disallow a deduction for interest on the portion of the affected debt that exceeds one and a half times the Canadian corporation's equity. The calculation is determined using the monthly average of the greatest amount of the debts outstanding at any time in each calendar month in the relevant taxation year. A corporation's equity for this purpose is basically the aggregate of its retained earnings (deficits are ignored) at the beginning of the year and the monthly average of each of its contributed surplus and paid-up capital in respect of shares owned by specified nonresidents at the beginning of each calendar month. Certain amounts may also be included in the computation in which a corporation is a member of a partnership. The thin capitalization rules also apply to Canadian resident trusts and to nonresident trusts and corporations that carry on business in Canada or are otherwise treated as a Canadian resident.

Any disallowed interest under the thin capitalization rules will be deemed to be a dividend and subject to WHT applicable to dividends.

Back-to-back loans

There is an anti-avoidance provision that applies to back-to-back loan arrangements aimed at financing transactions in which a third party (e.g., a bank) is interposed between a Canadian borrower and a specified nonresident of the Canadian borrower to circumvent either or both the Canadian thin capitalization restrictions and Canadian WHT. If the anti-avoidance provision applies, the applicable loan will be subject to the thin capitalization rules, and the withholding rate on the interest payments will be subject to the higher of the actual withholding rate and the withholding rate that would apply if the loan were made by the specified nonresident.

The back-to-back loan rules have been expanded to apply to back-to-back arrangements in respect of rents, royalties or similar payments (herein referred to as "royalties"), and to "character substitution" transactions.

The "character substitution" rules were introduced to prevent the avoidance of the back-to-back loan rules through the use of "economically similar arrangements" between the intermediary and a nonresident person. Specifically, a back-to-back loan arrangement may exist in circumstances where either interest or royalties are paid by a Canadian-resident person to an intermediary, and the intermediary has obligations to pay amounts of a different character to a nonresident person in such manner that the back-to-back loan rules may not technically apply. Where a back-to-back arrangement exists under these character substitution rules, an additional payment of the same character as that paid by the Canadian resident (i.e., interest or royalty, as the case may be) to the intermediary will be deemed to have been made by the Canadian resident directly to the other nonresident person.

The back-to-back loan rules have also been extended to apply to shareholder loans; such rules are aimed at preventing taxpayers from circumventing the shareholder loan rules by lending indirectly through an intermediary.

I. Transactions

Many transactions in Canada involve the acquisition of shares of a corporation or interests in a partnership, as opposed to a direct acquisition of operating assets. This trend is generally driven by the differing tax consequences of each type of transaction for the vendor. On the sale of a capital property (such as shares or partnership interests to taxable Canadian residents), only one-half of the capital gain is included in taxable income in Canada. However, the sale of operating assets can give rise to income, 100% of which is included in taxable income in Canada, and capital gains (as discussed in further detail below). Having a mix of income and capital gains on a sale of assets generally results in a higher effective tax rate on an asset sale vs. a sale of shares, which are capital property.

Share acquisitions

There are no stamp duties or similar taxes payable in Canada on the acquisition of shares.

Since there are no tax consolidation rules in Canada, most share acquisitions are completed using a special-purpose Canadian acquisition corporation, which is formed by the purchaser to acquire the shares of the target corporation. The purchaser capitalizes the acquisition corporation with debt (subject to the thin capitalization restrictions noted) and equity. Subsequent to the acquisition of the shares of the target corporation, the acquisition corporation and the target corporation are amalgamated. The purpose of the amalgamation is to ensure that the interest expense paid on the debt incurred by the acquisition corporation is deductible against the income of the target corporation. Since there are no tax consolidation rules in Canada, if the amalgamation is not completed, the interest expense incurred by the acquisition corporation would not be available to offset the income of the target corporation. Using a special-purpose Canadian acquisition corporation and capitalizing with equity also facilitates repatriation whereby capital may be returned to a nonresident shareholder free of WHT.

Generally, no rules allow for a step-up of the inside-tax basis of the assets of the target corporation upon acquisition of the target corporation's shares. However, when the acquisition corporation and the target corporation amalgamate, an opportunity arises to step up to fair market value the tax cost of non-depreciable capital property owned by the target corporation at the date of the acquisition (usually shares of subsidiaries or partnership interests), provided that certain qualifying conditions are met.

Shares in a private corporation and any other shares not listed on a designated stock exchange (including shares of nonresident corporations) are taxable Canadian property if more than 50% of their value is attributable directly or indirectly to Canadian oil and gas properties and other Canadian real property at any time in the 60-month period preceding the sale. The sale of this type of share can give rise to a Canadian income tax liability for a nonresident vendor. To ensure that nonresidents pay tax due in respect of a sale of taxable Canadian property, the nonresident vendor must provide the purchaser with a certificate issued by the tax authorities. The certificate is granted when appropriate arrangements are made to ensure payment of any tax liability. If the certificate is not provided, the purchaser must withhold and remit to the tax authorities 25% of the purchase price, whether or not any tax would be payable by the vendor on the sale. It is not necessary to obtain a certificate with respect to shares that are listed on a recognized stock exchange.

If a share purchase results in an acquisition of control, certain tax consequences apply for the acquired corporation, including a deemed tax year-end and restrictions on the availability of tax losses and the deductibility of FRE, CEE, CDE and COGPE.

Asset acquisitions

Generally, no land transfer taxes are imposed on the purchase of oil and gas assets.

The allocation of the purchase price among the various assets acquired has Canadian tax implications for both the vendor and the purchaser. For the vendor, the manner in which the purchase price is allocated may result in the recapture of CCA claimed in prior years, the realization of income upon the sale of intangible oil and gas rights (see above) and, in some cases, capital gains on the sale of capital property. For the purchaser, the value attributed to the various assets forms the cost of such assets. Therefore, to accelerate deductions from the taxable income that will be generated from the business in future years, the purchaser may wish to allocate as much of the purchase price as possible to depreciable property (in most cases, eligible for Class 41, which is a 25% declining-balance pool) rather than to oil and gas rights (in most cases, classified as COGPE, a 10% declining-balance pool). The allocation is a matter of negotiation between the parties, and the values attributed to the assets should generally form part of the purchase agreement.

Most assets used by a nonresident vendor in a Canadian oil and gas business are taxable Canadian property and are usually not treaty-protected property. In these circumstances, the purchaser is therefore generally required to withhold and remit to the tax authorities 50% of the purchase price if the nonresident vendor does not have a certificate from the tax authorities authorizing a lesser withholding rate.

J. Indirect taxes

Goods and services tax and harmonized sales tax

The goods and services tax (GST) (harmonized sales tax (HST) in certain provinces) is a federal value-added tax (VAT) that applies to the supply of property and services made in Canada and certain imports into Canada.

Taxable supplies made in the provinces of Newfoundland, New Brunswick, Nova Scotia and Prince Edward Island are subject to HST at a rate of 15%. Taxable supplies made in the province of Ontario are subject to HST at a rate of 13%. Supplies made in all other provinces and territories of Canada are subject to GST at a rate of 5%.

The importation of goods (e.g., products and equipment) into Canada is subject to GST, which is payable by the importer to the Canada Border Services Agency.

Certain supplies, such as goods sold for subsequent export and certain services provided to nonresidents of Canada, are zero-rated. This means that GST/HST applies to the transaction, but at a rate of 0%. Documentation that evidences the export, and in some situations a declaration letter provided by a GST-registered exporter, is required to support the zero-rating.

Certain goods and services are exempt from GST, such as most supplies made by charities and financial institutions. Oil and gas businesses are not typically involved in making exempt supplies.

GST/HST paid on purchases and imports is recoverable by a registrant that purchases the goods or services for use in commercial activities. "Commercial activities" include business carried on by a registrant other than the business involved in making exempt supplies. Oil and gas businesses are typically engaged in commercial activities.

A nonresident is required to register for GST/HST if it makes taxable supplies in Canada in the course of a business carried on in Canada. The term "carrying on business" is not defined under the Excise Tax Act.[2] Several factors are considered in determining whether a nonresident carries on business in Canada. Generally, a nonresident must have a significant presence in Canada to be considered to be carrying on business in Canada. Even if a nonresident does not carry on business in Canada, it may choose to register voluntarily if it expects to pay a significant amount of GST/HST to its suppliers or on importation (although it should be noted that the nonresident must meet

2 *The Excise Tax Act is the statute that governs GST/HST.*

certain conditions to register voluntarily). A voluntary registration will allow a nonresident to recover the GST/HST paid on purchases that are acquired for consumption, use or supply in the course of its commercial activities.

If a nonresident does not have a permanent establishment in Canada through which it makes supplies, it will be required to post security with the Canada Revenue Agency in order to register for GST/HST. The security ranges from CAD$5,000 to CAD$1 million. The security is based on 50% of the absolute value of the expected net GST/HST payable or recoverable over the course of the first year of registration.

Except for rights supplied to consumers[3] and to non-registrants that acquire the right in the course of the business of supplying these rights to consumers, the supply of natural resources property rights is deemed not to be a supply. Therefore, any consideration paid or due, or any fee or royalty charged or reserved in respect of these rights, is deemed not to be consideration for GST/HST purposes and thus does not attract GST/HST. This provision applies to most (but not all) property interests that form the legal basis of Canada's major resource industries (i.e., oil and gas, mining, forestry). This treatment generally results in no GST/HST payable in respect of the rights covered by this provision, which include:

- A right to explore for or exploit: a mineral deposit (including oil and gas); a peat bog or deposit of peat; or a forestry, water or fishery resource
- A right of entry or use relating to the right to explore
- A right to an amount computed by reference to the production (including profit) from, or to the value of production from, any such deposit, bog or resource

Oil and gas businesses often explore for and operate oil and gas resource properties as joint ventures with other oil and gas companies. If a written joint venture agreement exists between the joint venture participants and if the participants complete an election, the operator can account for the GST/HST collected on the sales and claim an input tax credit for the GST/HST paid on purchases on its own GST/HST return. Furthermore, if the election is in place, the operator does not need to charge GST/HST to the other participants on the joint venture interest billings.

Provincial sales taxes

Saskatchewan, Manitoba and British Columbia each impose a provincial sales tax (PST) on sales and imports of tangible goods, software and some services acquired for consumption or use in those provinces unless specifically exempt. The PST rates for 2017 are as follows: Saskatchewan at 6%, Manitoba at 8% and British Columbia at 7%. In those provinces, PST will apply in addition to the federal GST of 5%. Alberta does not have a provincial sales tax, so only GST at the rate of 5% applies to supplies made in that province.

In general, persons are required to register for PST if they make regular supplies of taxable goods or services in a province to the end users and they carry on business in the province. Once registered, persons must collect PST on all taxable goods and services they deliver in that province.

PST is imposed on the purchaser. Thus, even if PST is not charged by the vendor, it must be self-assessed by the purchaser on any taxable purchases. PST is non-recoverable unless it is paid in error.

Goods acquired for the purpose of resale are not subject to PST.

Each province also provides various exemptions in respect of certain goods and services. For example, BC and Manitoba provide exemptions or rebates for certain oil and gas exploration and production equipment, certain processing materials and certain services in respect of oil and gas exploration and well servicing.

3 *"Consumer" is defined by the Excise Tax Act as a "particular individual who acquires or imports the property or service for the particular individual's personal consumption, use or enjoyment or the personal consumption, use or enjoyment of any other individual at the particular individual's expense."*

Some goods are conditionally exempt (e.g., if exemption is based on the person's use, status or intent to resupply the goods rather than the nature of the goods themselves). In these circumstances, the vendor is required to obtain certain documents or information from the purchaser. The documents and information required to satisfy this condition vary by province.

Other indirect taxes

If a business imports, refines or sells refined fuel products, it may be required to register for and remit federal excise tax and provincial fuel taxes. In many provinces, businesses that use natural gas they produce to power their own compressors are required to self-assess fuel tax on their consumption of natural gas.

British Columbia, Alberta and Manitoba impose a carbon tax on various fossil fuels consumed in the province, including natural gas that is flared or used to power compressors. A federal carbon tax is applicable in provinces that have not implemented a carbon tax or a green-house gas cap and trade system (as has been implemented in Ontario and Quebec). The carbon tax rate varies, based on the type of fossil fuel used. In Alberta, the oil and gas industry is largely exempt from the carbon tax until 2023.

There may also be customs duties on the import of certain types of goods and equipment into Canada. The duties are payable to the Canada Border and Services Agency, together with the import GST by the importer of record.

The federal Government and many provinces levy a tax on the payment of insurance premiums to nonresident insurers with respect to risk that is located in Canada or the respective province.

Chad

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Chad's fiscal regime applicable to the upstream petroleum industry consists of:

- The Chadian Petroleum Code (Law No. 006/PR/2007) dated 2 May 2007 pertaining to hydrocarbons
- Ordinance No. 001/PR/2010 dated 30 September 2010 (the Ordinance), which approved the standard production sharing contracts (PSCs) and modified and completed the provisions of the abovementioned law regarding petroleum operations
- The standard production contract (hereafter referred to as the Model PSC)
- The PSC and concession agreements (CA) concluded between the state of Chad and contractors (the oil companies)
- The Chadian Tax Code

Fiscal regime under a PSC

- Corporate income tax (CIT) — not applicable
- Royalties on crude oil — rate set by the PSC, provided that it is not less than 14.25% nor greater than 16.5%
- Royalties on natural gas production — rate set by the PSC, provided that it is not less than 5% nor greater than 10%
- Cost stop (as defined below) — 70%
- Cost recovery principles — ring fence according to the Model PSC (negotiable) and the principle of LIFO (last-in, first-out)
- Tax oil (as defined below) — cannot be less than 40% and varies according to a profitability ratio (the R-factor)
- Surface rent tax — annual contribution as agreed in the PSC (non-recoverable cost)
- Exceptional tax on capital gains resulting from assets assignments — 25%
- Withholding tax (WHT) — on payments made to nonresidents for services provided in the country as described below
- Dividends — exempt
- Interest — exemption for interest paid to nonresident lenders
- L[1] — value-added tax (VAT) exemption
- Signature bonus — as agreed in the PSC
- Bonus for the awarding of an exclusive exploitation authorization — as agreed in the PSC

1 *L: Ability to carry forward losses.*

Fiscal regime under a CA

In practice, such contracts are no longer concluded.

Legal regime

The Chadian Petroleum Code provides for two types of regimes: the concession regime and the PSC regime. However, since the issuance of Ordinance, all of the conventions and agreements concluded between the State and contractors have followed the PSC regime, based on the Model PSC approved by this Ordinance.

Under this regime, the contractor undertakes petroleum activities on behalf of the State but at the contractor's sole and full risk. The contractor is not entitled to be granted a mining title. Exploration operations are undertaken pursuant to an exclusive exploration authorization granted to the contractor for a maximum period of five years, renewable once for three years. The exclusive exploration authorization provides exclusive rights to undertake exploration activities within the contractual zone. In a case of a commercial discovery, the State grants to the contractor or the consortium (as appropriate) an exclusive exploitation authorization for a maximum period of 25 years that is renewable once for 10 years.

Upon the award of any exclusive exploitation authorization, the State is entitled to require the assignment of a stake up to a maximum of 25% of the rights and obligations attached to the exclusive exploitation authorization. Pursuant to Article 16 of the Ordinance, the participation of the State is fully carried by the oil company for a threshold of 10% of the participation. The State is co-owner of the exclusive exploitation authorization to the extent of its participation.

The contractor is responsible for financing all petroleum costs. In return, as from the date of production startup, the contractor is entitled to recover these petroleum costs by receiving a quantity of hydrocarbons known as "cost oil," which cannot exceed 70% of production per year. The remaining production, known as "profit oil," is shared between the State and the contractor. The share for the State in the profit oil, referred to as "tax oil," cannot be less than 40% of the profit oil and varies according to a profitability ratio (the R-factor).

The ownership of any property purchased or acquired by the contractor for the purpose of carrying out petroleum operations is transferred to the State free of charges. However, the contractor is reimbursed through the cost recovery mechanism discussed below.

PSCs are negotiated with reference to the Model PSC approved by law. They are signed by the minister in charge of petroleum activities, approved by an Act of Parliament and published in the *Official Gazette*.

B. Fiscal regime (under a PSC)

Corporate income tax

Chadian CIT is charged at a rate of 35%.

Pursuant to Article 15 of the Ordinance, a contractor is not subject to any other taxation other than the taxation that is provided by the Ordinance and the Model PSC.

According to Article 47.1.2.d of the Model PSC, the contractor (the oil company or the consortium that jointly holds the exclusive exploitation authorization) is exempt from CIT. Article 47.2.1 of the Model PSC provides that the share for the State via the tax oil mechanism is the equivalent of CIT. A tax clearance is delivered to the contractor upon payment of the tax oil to certify that this tax oil is the equivalent of the CIT and that there is no need for the contractor to pay any additional CIT or direct tax on profits.

The contractor must nevertheless file a yearly tax return for its petroleum operations within three months following the end of the tax year (i.e., before 1 April).

Net profits arising from the operations carried out by the contractor in Chad that do not form part of petroleum operations are subject to CIT in accordance with the common law and shall be held in separate accounting from the petroleum operations accounting.

Royalty regime

Contractors are subject to a monthly royalty on production at a rate agreed in the PSC. The Model PSC provides that the rate ranges from 14.25% to 16.5% for crude oil and from 5% to 10% for natural gas.

The royalty on crude hydrocarbons shall be payable at the State's option, either in cash or in kind.

Contractors must file a monthly production statement, together with supporting documents, that sums up the total production of the previous month, including, but not limited to:

- The net hydrocarbon production (total hydrocarbon production minus water, sediment and the quantities of hydrocarbons used for petroleum operations)
- The quantity of hydrocarbons allocated to the payment of the royalty, as measured at the measurement point, regardless of whether such royalty is paid in cash or in kind
- The quantity of hydrocarbons allocated for the reimbursement of the petroleum costs
- The quantity of hydrocarbons delivered at the delivery point, which is the quantity of hydrocarbons to be exported

The summary should mention separately the quantity of crude hydrocarbons and the quantity of natural gas.

Each royalty is required to be paid by the 15th day of the month following the relevant month. When the royalty is paid in cash, the amount is assessed based on the ex-field market price.

Royalty is not a recoverable cost under the PSC.

Cost recovery

Contractors are entitled to receive a part of the net production (after deduction of the royalty) for the purpose of recovery of their petroleum costs. The production to be allocated to the recovery or reimbursement of the petroleum costs cannot exceed 70% of net production (after deduction of the royalty).

The petroleum costs shall be reimbursed in the following order of priority:

- Exploitation costs (opex)
- Development costs
- Exploration costs
- Provisions that are determined to cover abandonment operations

Non-recoverable expenditures

Some expenditures or costs are not recoverable. Examples include:

- Expenses relating to the marketing and transportation of the hydrocarbons beyond the delivery point
- Gifts, donations and subsidies, except those approved by the Chadian State
- Gifts and discounts granted to suppliers, as well as gifts and discounts granted to intermediaries used in the frame of supplies or services contracts
- Fines, confiscations and penalties of all kinds arising from consortium transactions in contravention of the legal, economic or fiscal provisions of the convention
- Any other expenses that are not necessary for the performance of petroleum operations or are considered indirect, unreasonable or excessive
- Surface rent tax
- Signature bonus and the bonus for the award of an exclusive exploitation authorization (although in certain contracts these are recoverable)

Surface rent tax

Contractors are liable to the payment of an annual surface rent tax on the basis of the surface area as provided for in the PSC.

The surface rent tax is payable annually and in advance, based on the situation as of January of the current year, and must be paid to the Public Treasury by 31 March of the relevant year.

Exceptional tax on capital gains relating to assignment of interests

Pursuant to Article 17 of the Ordinance, capital gains resulting from any assignment by a contractor of any authorization to undertake petroleum operations under the PSC and related assets shall be subject to a special 25% tax, which shall be payable by the assignor pursuant to the terms and conditions set forth in the Model PSC. In practice, however, the special tax applies only to assignments of exclusive exploration authorizations or assets and interests deriving from such authorizations. Under PSCs, there is an exemption for capital gains resulting from the transfer of assets under an exclusive exploitation authorization (farm-in and farmout during the exploitation period). Interaffiliated companies' assignments are also exempt from this tax.

This special tax is levied on the difference between the sale price of the assets and the cost price of the relevant assets. The tax is payable within 30 days from the issuance of the assignment authorization by the State.

Flat amount on prospecting, exploration and exploitation of oil and gas

Pursuant to Article 68 of Law No. 006/PR/2007 dated 2 May 2007 pertaining to hydrocarbons, the request for attribution, renewal, transfer and renouncement to a petroleum authorization or permit should be subject to the approval of the Minister of Energy and Petroleum. Such approval is granted after the payment of a lump sum set as follows:

- US$50,000 for the issuance and the renewal of the prospecting authorization
- US$50,000 for the issuance, renewal, prorogation and division of an exclusive exploration authorization or an exploration permit
- US$1 million for the transfer of an exclusive exploration authorization or an exploration permit
- US$500,000 for the issuance and renewal of an exclusive exploitation authorization or an exploitation permit
- US$3 million for the transfer of an exclusive exploitation authorization or an exploitation permit

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Incentives

VAT incentives

The supply of goods and services of all kinds that are directly linked to petroleum operations are exempt from VAT. A list of exempted goods and services is included in the PSC.

D. Withholding taxes

Dividends

Dividends paid by a company incorporated in Chad to a nonresident are exempt from taxation as provided by the Petroleum Code.

Interest

Any interest paid to lenders that are nonresident, from a Chadian fiscal point of view, shall be exempt from any WHT.

Payments made abroad

WHT applies to the following types of services provided in Chad but only insofar as such withholding is prescribed by the Chadian General Tax Code:

- Technical, financial and accounting services
- A share of general and administrative expenses relating to operations carried out in Chad
- Equipment or material rental

- Supplying information of an industrial, commercial, scientific or technical nature
- Any services provided to a contractor by any other contractor, subcontractor or affiliate

For the purposes of the application of the relevant withholding rules, "technical, financial and accounting services," as well as "general and administrative expenses," shall have their respective common law meanings.

E. Financing considerations

Thin capitalization limits

Interest paid to shareholders for funds made available to the company in addition to their capital contributions, regardless of the type of the company, is fully deductible to the extent that:

1. The rate applied does not exceed the Chadian Central Bank's rate plus two points.
2. The interest is calculated on the portion of loan no higher than half of the share capital.

However, intercompany interest-bearing loans (loans granted by sister companies) are not tax deductible as from 1 January 2015.

International tax treaties signed with the Chadian State could provide for specific provisions related to the deductibility of interest on loans.

F. Indirect taxes

Import duties

Provisions regarding customs duties are identical for most contracts. They usually provide that the person designated as the "contractor," as well as the subcontractors, is allowed to import into Chad any goods, materials, machinery, equipment or consumer goods that are necessary to carry out qualifying operations in the contractor's own name or in the name of the subcontractors. The following rules apply:

- The material intended exclusively for petroleum exploration and exploitation will be exempt from all taxes and customs duties.
- Equipment, merchandise and appliances intended for the petroleum exploration and exploitation work sites will be placed under the normal temporary admission regime.
- Work site vehicles, specialized or not, will be placed under the temporary admission regime; company vehicles and vehicles for personal use will be subject to the general legal regime without exemption; airplanes and their spare parts and consumable materials required for petroleum exploration and exploitation, as listed in an appendix of the PSC, will be exempt from all taxes and customs duties.

Export duties

The Chadian Petroleum Code provides that contractors will be exempt from any taxes and duties while exporting.

VAT

As noted above, the supply of goods and services of all kinds that are directly linked to petroleum operations is exempt from VAT. A list of exempted goods and services is usually enclosed with the CA. Ancillary activities that are not linked to petroleum operations will be subject to VAT at a rate of 18%.

No separate registration process is necessary for VAT purposes. VAT registration will be included in the registration for tax purposes with the Chadian tax administration. There is no threshold minimum value of supplies; registration for tax purposes will be required for all resident entities.

Registration fees

Registration fees depend on the type of the agreement concluded. Contractors are exempt from registration fees relating to the incorporation of any company in Chad and from any capital increase.

G. Other

Exchange control

The Economic and Monetary Community of Central Africa Countries (CEMAC) Act (Act No. 02/00/CEMAC/UMAC/CM), dated 29 April 2000, provides for exchange control regulation that applies to financial transfers outside the franc zone, which is a monetary zone including France and mostly French-speaking African countries. However, for the duration of the CA, Chadian authorities provide certain guarantees to the contractor for the operations carried out within the framework of the CA, notably:

- The right to obtain financing from abroad necessary for the conduct of the petroleum operations; to receive and to maintain abroad all funds acquired or borrowed abroad, including income from sales; and to dispose of them freely insofar as funds exceed the requirements of their operations in Chad and of their fiscal and contractual obligations
- Free movement of funds belonging to it, free of all taxes and duties, between Chad and any other countries
- The right to repatriate the capital invested within the framework of the CA and to transfer income from such capital — particularly interest and dividends — although the state shall have no obligation to provide foreign currency
- Free transfer of amounts payable, as well as the right to receive amounts of any nature that are payable to them, subject to making the necessary declarations required by the regulations
- The right to direct payments abroad to foreign suppliers and services required for the petroleum operations

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Tax regime applied to this country

■ **Concession** ☐ Royalties ☐ Profit-based special taxes ■ Corporate income tax	☐ **Production sharing contracts** ☐ **Service contract**

A. At a glance

Fiscal regime

As a general rule, the oil and gas industry is subject to the same general tax regime and tax regulations as any other industry in Chile. However, pursuant to Article 19, No. 24, Subsection 10 of Chile's Political Constitution, the exploration, exploitation or benefits arising from deposits or oil fields that contain substances that are not freely traded may be carried out by means of administrative concessions or through special operating contracts or agreements. According to the foregoing, there is a special regime applicable to the exploitation of hydrocarbons, being an exception to the abovementioned general rule.

This special regime is contained in Decree Law No. 1.089 of 1975, which regulates the granting, subscription, rights, obligations and tax treatment of the operating agreements (*Contrato Especial de Operaciones para la Exploración y Explotación de Hidrocarburos,* or special operating agreements for the exploration and exploitation of hydrocarbons, also known as CEOP) by means of which private contractors may carry out the exploitation of hydrocarbons:

- Corporate income tax (CIT) rate (standard regime):
  - 2018 onward: attributed regime (14A) — 25%, or semi-integrated regime (14B) — 27%
- Special taxation regime applicable to CEOP contractors — 50% tax on gross revenues:
  - The President of Chile can grant discounts and/or allow for taxation under the general regime (overall burden is 35% on net taxable income).
- Tax on capital gains 35%
- Withholding tax (WHT):
  - Dividends — 35%
  - Interests — 35%; reduced to 4% for certain operations (e.g., government bonds, inbound loans from foreign banks or foreign financial institutions and other operations) subject to thin-cap limitations if paid to related parties abroad
  - Royalties (patents, trademarks, formulas and similar items) — 30%, 15%, 0%
  - Technical services and professional services — 15%–20%
  - Other fees and compensation for services rendered abroad — 35%
- Under certain circumstances, the WTH may be reduced or eliminated under a Double Taxation Treaty

- Net operating losses (years):
  - Carryback — ceased to exist from 1 January 2017
  - Carryforward — unlimited
- Value-added tax (VAT) — 19%

B. Fiscal regime

Special operating agreements for the exploration and exploitation of hydrocarbons (CEOP)

These agreements are subject to a special regime under which a 50% tax is assessed on gross revenues for the relevant CEOP. The President of Chile can determine that the CEOP contractor is taxed under the general income tax regime (overall burden of 35% on net taxable income) and can also grant reductions of the tax of the special regime or of all or some of the taxes contained in the Income Tax Law, equivalent to 10%, 20%, 30%, 40%, 50%, 60%, 70%, 80%, 90% or 100% if the exploration or exploitation areas are difficult to access, if there are no double taxation agreements in force between Chile and the country from which the investment comes, or when other terms of the CEOP are too burdensome for the contractor.

When hydrocarbons are transferred as payment to the contractor under the respective CEOP, these payments are exempt from all taxes and duties, including export taxes.

The remuneration of foreign subcontractors that are domiciled abroad and that have entered into a CEOP will be subject to a 20% tax rate, applied to the total amount of the remuneration, and will substitute any other direct or indirect tax that may be levied upon the remuneration of the subcontractor. The President of Chile may grant a reduction of the abovementioned tax equivalent to 10%, 20%, 30%, 40%, 50%, 60%, 70% or 75% of the same.

Under the provisions of Decree Law No. 1.089, companies engaged in oil exploration or exploitation activities are eligible for VAT and customs reductions ranging from 10% to 100% on certain items, including imported machines, materials and spare parts. These reductions are granted by the President of Chile by means of enacting a supreme decree. Alternatively, Decree Law No. 1.089 allows VAT-free and customs-free temporary entry of CEOP-related equipment for up to five years, with the possibility of extending the period on a yearly basis through the National Customs Director.

Notwithstanding the foregoing, in practice, almost all of the companies acting as contractors or subcontractors in a CEOP are subject to the standard tax regime.

Specific oil and gas tax

According to Law No. 18.502, a specific tax is applied to natural compressed gas and liquefied gas used in vehicular consumption, automotive gasoline and diesel.

With respect to natural compressed gas and liquefied gas, this tax will be levied upon its sale in Chilean territory. The same tax will be applicable when the distributor, producer or importer of these gases sells them directly for vehicular consumption or in order to supply fuels to vehicles exploited by them.

With regard to automotive gasoline and diesel, the tax will be accrued when they are sold for the first time or when imported into the country, and levied upon the producer or the importer.

This tax applies on the basis of a fixed component and a variable component.

- Fixed component: under Articles 1 and 6 of Law 18.502, the following amounts are levied on each type of fuel, on the basis of the volume sold:
  - Automotive gasoline: 6.0 UTM per m^3
  - Diesel: 1.5 UTM per m^3
  - Compressed natural gas: 1.93 UTM per 1.000 m^3
  - Liquefied gas: 1.40 UTM per m^3

- Variable component: the fixed component is then adjusted (increased or decreased) with the purpose of mitigating the fluctuations in the price of fuels for the consumers.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Corporate tax

General considerations

Chilean resident companies are subject to CIT (first-category tax) on their net taxable income of local and foreign sources. Local source income is taxed on an accrual basis while foreign source income is generally taxed on a cash basis (unless controlled foreign corporations rules apply). Companies incorporated in Chile are considered tax residents in Chile.

The income of local companies is assessed in two stages: first, with CIT, when the income is accrued; and second, when the profits are distributed to or withdrawn by its owners (branches are taxed in a similar way). The corporate tax is credited against the tax on profits withdrawn by or distributed to business owners.

Tax rates

The current CIT rate for profits generated in the calendar year 2018 is 25% for the attributed regime or 27% for the semi-integrated regime.

D. Tax payments and income tax return

Financial statements must be prepared as of 31 December of each year for income tax purposes. Income tax returns must be filed in April of the following year.

Provisional monthly payments (PPM) with respect to the final annual income tax liability must be made on a monthly basis. The amount payable is determined as a percentage of gross receipts accumulated during the corresponding month. If the company has losses in a given year, PPM can be suspended during the following quarter. PPM will continue to be suspended if losses continue in the quarters thereafter.

E. Foreign tax relief

Income tax paid in other countries for most types of income can be credited against Chilean CIT liabilities. In the case of dividends, the foreign tax credit is the lower of:

- The taxes paid abroad
- 32% of the net foreign source income divided by 0.68 (35% and divided by 0.65 if sourced from a country that has a tax treaty with Chile)

There is also an annual cap on foreign tax credits (32% of net annual foreign source income or 35% if sourced from a treaty country).

Foreign tax relief may also be available under double tax treaties currently in force in Chile with the following countries: Argentina, Australia, Austria, Belgium, Brazil, Canada, China, Colombia, Korea, Croatia, Denmark, Ecuador, Spain, France, Ireland, Italy, Japan, Malaysia, Mexico, Norway, New Zealand, Paraguay, Peru, Poland, Portugal, United Kingdom, Czech Republic, Russia, South Africa, Sweden, Switzerland and Thailand.

Chile has signed tax treaties with Uruguay and the United States, which are not currently enforceable but will be once they are ratified by the congress of the respective states.

F. Determination of taxable income

Taxable income, determined in accordance with accounting records based on International Financial Reporting Standards (IFRS), includes all profits, with the exception of specified items that are not considered income for tax purposes. Dividends received by resident companies from other resident companies are exempt from tax.

Taxable income is determined on the basis of profits or losses disclosed in the financial statements prepared at the company's year-end.

Inventories

For inventory valuation, the first-in, first-out (FIFO) method and the weighted-average cost method are accepted by law.

Expenses

As a general rule, all necessary expenses for producing income, duly proven and justified, may be deducted in determining taxable income.

Likewise, Chilean taxes, except for those contained in the Income Tax Law, are deductible. Foreign taxes that are not creditable in Chile are not treated as deductible expenses. In the case of VAT, whenever VAT cannot be reclaimed, it is a deductible cost or expense.

Depreciation and amortization allowances

Depreciation of tangible fixed assets is tax deductible. Depreciation is calculated using the straight-line method on the estimated useful life of the assets, without considering a residual value.

The tax authority has established the following normal periods of depreciation:

Assets	Years
Solid buildings	40–80
Semi-solid buildings	20–40
Buildings of light materials	10
General installations	10
Machinery and equipment	15
Cars, pickups, station wagons and buses	7
Trucks	7

Taxpayers may apply the accelerated-depreciation method. This allows the calculation of depreciation as straight-line depreciation based on a useful life for an asset equivalent to one-third of the normal useful life established by the Chilean tax authorities. Accelerated depreciation can be applied to new goods acquired locally or imported goods, provided that the useful life exceeds three years.

The difference between normal and accelerated depreciation must be recaptured on any profits distributed to nonresidents.

Goods that become unusable before the end of their expected useful life may be depreciated at twice the rate that was originally expected.

Research and development (R&D) expenses may be deducted entirely in the year they are owed or paid, or they can be amortized over six consecutive years.

Annual depreciation rates must be applied after the revaluation of fixed assets according to the monetary restatement rules (see below).

Monetary restatement

The Income Tax Law contains provisions designed to prevent the taxation of profits created by inflation. These provisions, known as "monetary restatement," require taxpayers to revalue certain assets and liabilities annually based on changes reflected in the consumer price index (CPI)[1] and the foreign-exchange rates.

In order to make an inflation adjustment, a distinction is made between monetary and non-monetary assets and liabilities. Only non-monetary assets and liabilities in existence at the balance sheet date are adjustable by inflation.

1 *The National Statistics Institute sets Chile's monthly CPI.*

Equity is considered non-monetary.

Relief for losses

Losses may be carried forward indefinitely. The carryback ceased to exist from 2017.

Certain limitations apply to the possibility to use accumulated net operating losses (NOLs) after a change of ownership (these limitations essentially aim at preventing the purchase of companies with the purpose of using NOLs and not developing its main line of business).

G. Issues related to foreign companies

International loans and thin capitalization rules

Foreign investors frequently use debt financing for their Chilean projects to benefit from a reduced 4% WHT on qualifying interest payments (provided that the interest is paid to a foreign bank or to a foreign financial institution). However, a penalty tax for the difference between the WHT paid and 35% (generally giving 31%) is collected from the debtor if the beneficiary of the payment is a related party and the debtor is in an "excess indebtedness" position in the year of payment. The penalty tax is assessed on the interest in the portion of the excess.

A company is in an "excess indebtedness" position when its overall debt is greater than three times its equity (a 3:1 ratio).

The penalty tax applies to any interest paid to related parties abroad if it benefited from a reduced WHT rate (i.e., below 35%) either by disposition of law or by application of a tax treaty, if such interest is paid in a year of "excess indebtedness." The penalty tax is assessed only on the portion of the excess.

Services, duties, patents and technical assistance

In general, payments for services provided abroad made to entities not domiciled in Chile are subject to a 35% WHT. Also, a 15% rate applies for technical assistance, engineering and professional services, whether provided in Chile or abroad, unless the payment is made to a resident of a low-tax jurisdiction — in which case, the rate is 20%.

The payment of royalties for intellectual property (IP) is subject to a 15% or 30% WHT, depending on the specific nature of the intangible. However, the 15% rate is only available if the payment is not made to a resident of a low-tax jurisdiction — in which case, the rate is 30%. Payments for non-customized software in which the buyer is the end user are generally exempt from WHT.

The tax treaties subscribed to by Chile under the OECD Model establish reduced rates for services and royalties provided by a resident of a contracting state, or even exemption if the income qualifies as a business profit.

Capital gains

From 1 January 2017, capital gains are no longer taxed solely with the corporate tax and are subject to the general regime, with a rate of 35% in the case of nonresident beneficiaries.

Sales of shares of companies listed on the stock exchange are exempt from income tax under certain conditions. In addition, under certain double tax treaties, the general rate may be reduced.

A 35% tax also applies to the gain obtained in the transfer of shares/rights in a foreign company if it directly or indirectly holds Chilean assets, depending on the magnitude of the underlying Chilean assets in the total price of the transfer. However, not all gains are taxed, as the rules of calculation of the gain try to diminish the impact of foreign assets in the calculation. The 35% rate can be replaced with the rate that would have applied if the underlying Chilean assets were directly sold by their owners.

Under certain conditions, tax treaties can limit (or even exempt) the taxation of capital gains.

H. Transfer pricing

Chile has a robust transfer pricing regulation based on OECD principles and standards. In this regard, the arm's-length principle must be complied with when there are transactions between related parties. The tax law now defines what should be understood as "related" parties, and it contains and individualizes the methods that may be applied by taxpayers within the "best method rule." Transfer pricing studies are not mandatory but are advisable. Advanced pricing agreements (APAs) with the tax authority are also allowed; they last for three years if concluded and can be renewed for another three years.

Taxpayers must file a sworn statement every year in order to inform the Chilean tax authorities of all transactions carried out with its related parties. The differences determined by the Chilean tax authorities in related transactions are taxed with a 40% tax, plus penalties.

I. Taxation on payments to persons or entities not domiciled in Chile

Profit distributions out of Chile are subject to taxation, as indicated in Section A above. Other payments to nonresident entities are subject to Chilean taxes, to the extent that they are Chilean source income. Exceptional services rendered abroad are also subject to Chilean taxation. Applicable rates are listed below in Section J.

J. Special withholding tax rates

- Payments of interests: 35%
  - A reduced 4% rate applies if interest accrued from specific operations, such as government and Central Bank bonds, or loans borrowed from foreign banks or foreign financial institutions, among others; 4% thin-cap limitations apply if beneficiary is a related party abroad
- Payments for the use of trademarks, patents, formulas and IP in general: 15%/30%/0%
- Payments for engineering services, technical assistance and professional services rendered in Chile or abroad: 15%/20%
- Fees paid for ocean freight to or from Chilean ports: 5%
- Payments for leases of foreign ships used in or intended for transport services: 20% (exempt if reputed Chilean)
- Payments of insurance premium: 22% (2% for reinsurance)
- Payments for leases, with or without purchase rights, of imported equipment eligible for deferred payment of customs mechanism: 1.75%

Under certain conditions, withholding tax rates can be reduced or disabled by existing enforceable double taxation agreements (a list is provided in section E of this guide).

K. Withholding tax on dividends and profit distributions or withdrawals

Foreign taxpayers are subject to a 35% WHT on profits and dividends obtained from Chilean businesses. The WHT is the second tier of taxation of business profits. The corporate tax paid on income withdrawn, distributed or remitted can be credited against the WHT. This credit must be added in the calculation of the tax base for the WHT.

The following example illustrates the above:

Chilean company's income	100
Corporate tax (first-category tax)	(25)
Income distributed to foreign parent company	75
WHT base (additional tax)	100
WHT determined	(35)
Corporate tax credit	25
WHT payable	(10)
Available to foreign parent company	65

From 1 January 2017, certain taxpayers are no longer able to use all the corporate tax paid as credit against the WHT. Instead, they are allowed to use only 65% of the corporate tax credit. In this sense, under the Partially Integrated Regime, shareholders or partners will be taxed only on the actual distribution of dividends or profits by the company. Companies will be subject to 27%, effective from 2018 onward. Under this regime, only 65% of the paid CIT may be used as a credit against final taxes (except tax treaty resident shareholders). As a result, in the Partially Integrated Regime, the overall tax burden applied to nonresident shareholders will be 35% if the residents are in a treaty country, or 44%, 45% otherwise.

L. Indirect taxes

VAT

VAT applies to sales and other transactions regarding tangible movable property, as well as to payments for certain services. It also applies to certain real estate transactions. The standard VAT rate is 19%. VAT is imposed under a debit-credit system. Exports of goods and certain services are exempt from VAT, and input-VAT credits can be recovered by the exporter.[2]

2 *For example, in March 2018, one UTM is equivalent to approximately CLP47,301; with an exchange rate of CLP605.65 per USD, one UTM is approximately US$78.*

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies to the petroleum industry in China mainly consists of production sharing contracts (PSCs), special oil gain levies, value-added tax (VAT), consumption tax (CT), resource tax, environmental protection tax (EPT) and corporate income tax (CIT):

- Special oil gain levy — calculated in accordance with a formula in circumstances in which the monthly average weighted price per barrel of crude oil sold is greater than US$40 per barrel before 1 November 2011, US$55 per barrel before 1 January 2015 and US$65 per barrel from 1 January 2015
- Royalties — 0% to 12.5%, not applicable to PSCs concluded after 1 November 2011
- Bonuses — defined in the PSC and take into account the volume of petroleum resources and the economic value of the field
- Production sharing — based on production volumes
- Income tax rate — 25%
- VAT — 17% (general rate)
- CT — based on the volumes and categories of the taxable petroleum products
- Resource tax — 6% of the sales price, where sales revenue is collected from 1 December 2014
- Mineral resources compensation fee — 0% of the sales revenue from oil and gas production from 1 December 2014
- EPT — based on the volumes of the pollutants discharged and the specific items of the pollutants
- Investment incentives — qualified research and development (R&D) expenditure, which can be deducted at 150% of the actual expenses

B. Fiscal regime

Foreign petroleum companies are permitted to participate in and operate the exploration, development and production of petroleum resources in China by entering into PSCs with the Chinese Government or its designated Chinese national petroleum companies.

Special oil gain levy

As of 26 March 2006, a revenue windfall levy is charged on all oil production enterprises (both domestic and foreign) that sell crude oil produced in China. According to the Ministry of Finance, the revenue windfall levy applies regardless of whether the crude oil is sold within or outside China. The revenue windfall levy is charged whenever the weighted average price of crude oil sold in any month exceeds US$40 per barrel for months before 1 November 2011, US$55 per barrel for months before 1 January 2015 and US$65 per barrel for months after 1 January 2015.

The revenue windfall levy, if applicable, is paid monthly and filed quarterly. The amount of revenue windfall levy payable per barrel is calculated according to the formula:

Special oil gain levy = (monthly weighted average price per barrel of crude oil sold – US$65) × rate of levy – quick calculation deduction

The progressive rates and quick calculation deduction amounts are as follows:

US$65 per barrel for months ending after 1 January 2015

Crude oil price (US$/barrel)	Rate of levy	Quick calculation deduction (US$/barrel)
65–70 (inclusive)	20%	0.00
70–75 (inclusive)	25%	0.25

Crude oil price (US$/barrel)	Rate of levy	Quick calculation deduction (US$/barrel)
75–80 (inclusive)	30%	0.75
80–85 (inclusive)	35%	1.50
Above 85	40%	2.50

Petroleum royalties

Petroleum royalties are administered and collected by the tax authorities under the relevant rules produced by the Ministry of Finance. Payments are made in-kind with the crude oil and natural gas produced.

Sino-foreign[1] PSC onshore petroleum operations in the Qinghai, Tibet and Xinjiang provinces and sino-foreign PSC offshore petroleum operations are subject to petroleum royalties, as shown below:

Annual gross output of crude oil (thousand metric tons)	Royalty rate
Portion not exceeding 1,000	0.0%
Portion between 1,000 and 1,500	4.0%
Portion between 1,500 and 2,000	6.0%
Portion between 2,000 and 3,000	8.0%
Portion between 3,000 and 4,000	10.0%
Portion exceeding 4,000	12.5%

Annual gross output of natural gas (cubic meters)	Royalty rate
Portion not exceeding 2 billion	0%
Portion between 2 billion and 3.5 billion	1%
Portion between 3.5 billion and 5 billion	2%
Portion exceeding 5 billion	3%

Sino-foreign PSC onshore petroleum operations other than those located in the Qinghai, Tibet and Xinjiang provinces are subject to a different set of petroleum royalties, as shown below:

Annual gross output of crude oil (thousand metric tons)	Royalty rate
Portion not exceeding 500	0.0%
Portion between 500 and 1,000	2.0%
Portion between 1,000 and 1,500	4.0%
Portion between 1,500 and 2,000	6.0%
Portion between 2,000 and 3,000	8.0%
Portion between 3,000 and 4,000	10.0%
Portion exceeding 4,000	12.5%

1 *Involving collaboration between a Chinese state-owned oil company and a foreign oil company.*

Annual gross output of natural gas (cubic meters)	Royalty rate
Portion not exceeding 1 billion	0%
Portion between 1 billion and 2.5 billion	1%
Portion between 2.5 billion and 5 billion	2%
Portion exceeding 5 billion	3%

Pursuant to the resource tax regulations issued in 2011, Chinese and foreign parties to onshore/offshore PSCs are required to pay resource tax instead of royalties. Where a PSC for oil and gas exploitation was concluded before 1 November 2011, taxpayers follow the old petroleum royalties regime during the effective period of the PSC. Taxpayers, who are mainly Chinese and foreign parties on cooperative upstream oil and gas projects, are required to pay resource tax (instead of royalties) upon expiry of the PSC.

Signature bonus

A signature bonus is a lump-sum payment made by a petroleum entity to the Government for the right to exploit the petroleum resource. The amount may be defined by the Government based on the volume of petroleum resources and economic value of the field. The signature bonus is payable upon signing a PSC.

Chinese national petroleum companies that receive a signature bonus from foreign petroleum companies may treat it as an increase of capital reserve.

Resource tax

According to the regulations on resource tax issued by the State Council on 30 September 2011, companies engaged in the exploitation of natural resources in China are liable to pay resource tax. The tax rate for crude oil and natural gas is 5% before 1 December 2014 and 6% from 1 December 2014, based on the sales price. The sales price shall be determined on the same basis as for VAT purposes, i.e., the total consideration plus any other charges. However, the sales price shall not include the output VAT collected.

Oil and gas used by taxpayers in the continuous production of oil and gas are not subject to resource tax. Tax exemptions and reductions are also available in the following situations, subject to the approval of the tax authorities:

- Full exemption for oil and gas extracted and used for heating required to transport heavy oil in-field
- 40% exemption for the extraction of heavy oil, high pour point oil and high sulfur gas
- 30% exemption for tertiary recovery
- 20% exemption for oil and gas extracted from low abundance oil (gas) field
- 30% exemption for deepwater oil (gas) field

Mineral resources compensation fee

According to the newly issued notice " Adjustment of Certain Resource Tax Policies on Crude Oil and Natural Gas by the State Administration of Taxation and Ministry of Finance," effective from 1 December 2014, the mineral resources compensation fee levied on oil and gas is reduced to zero.

Environmental Protection Tax

To promote environmental protection in China, the Standing Committee of the National People's Congress (NPC Standing Committee) finally passed and promulgated the "EPT Law of the People's Republic of China" with the Chairman Order [2016] No. 61 on 25 December 2016 to replace the previous Pollutant Discharge Fees. This EPT Law constitutes the fifth tax law in China and took effect from 1 January 2018.

According to the EPT Law, EPT taxpayers include enterprises, public institutions and other producers and business operators directly discharging taxable pollutants within the territory (land and coastline) of the PRC. EPT shall be imposed on pollutants that are generated from urban sewage and household waste treatment plants and exceed the State's or local disposal standards. In addition, the storage or disposal systems regarding solid waste by enterprises, public institutions and other operators failing to meet the relevant State or local standards shall be subject to EPT. Under the EPT Law, taxable pollutants are divided into four categories: air pollutants, water pollutants, solid waste and noise.

The EPT Law provides a tax rate range in its annexed "EPT Taxable Items and Tax Amounts." EPT shall be calculated based on the volume of the pollutants discharged. For air and water pollutants, the tax basis shall be determined according to their pollution equivalent weights respectively. For solid waste and noise pollutants, the taxation basis shall be determined according to the quantity discharged and the decibel level. Local governments are allowed to adjust the tax rates within a range, provided that the adjustments are approved by the standing committee of the local NPC at the same level and are submitted to the NPC Standing Committee and the State Council for record filing purposes.

An EPT obligation arises on the date when a taxpayer discharges taxable pollutants. The EPT shall normally be calculated monthly and filed on a quarterly or transaction-by-transaction basis.

Production sharing

Production sharing is based on the production volume that is termed "annual gross production." A PSC defines the percentage of total production to be used for cost recovery and the sharing of the Government and the PSC participants in the "profit production."

Annual gross production net of all revenue levies and revenue taxes (such as special oil gain levy, resource tax and VAT) is used for calculating "cost recovery" and profit production. In general, cost recovery for offshore PSCs and onshore PSCs is from 50% to 62.5% and 60%, respectively (with deemed interest cost recovery on development costs).

The cost recovery mainly involves the recovery of the following expenses and expenditure in the sequence below:

- Petroleum royalties (replaced by resource tax for PSCs concluded after 1 November 2011)
- Production and operating expenses
- Exploration expenditure
- Development expenditure
- Deemed interest cost recovery on development costs, currently 9%

The remainder is automatically added to the pool for profit production.

Profit production is shared between the government and the PSC participants based on the allocation factor stipulated in the PSC.

Ring fencing

In China, there is no clear definition of "ring fencing" for PSC participants — meaning that PSC participants do not need to determine the tax base or the amount of tax separately for each PSC activity.

According to China's income tax law, if the taxpayer is conducting activities in multiple provinces, the head office is generally responsible for calculating the total amount of taxable income and tax payable on a consolidated basis. The head office and its branches are required to file tax returns and prepay tax, respectively, with the local tax authorities based on the prescribed allocation method on a monthly or quarterly basis. After the end of the year, the head office must conduct the annual tax filing on a consolidated basis. The CIT should also be settled by the head office and its branches with the local tax authorities based on the prescribed allocation method.

If the contractor has more than one contract, it can offset the tax losses generated by one or more contracts against the profits resulting from other contracts.

Corporate income tax

Petroleum companies are taxed at the rate of 25% on their taxable income according to the Enterprise Income Tax Law. Taxable income equals assessable income less deductions. Net operating tax losses may be carried forward for five years to offset future taxable income. Carryback of losses is not allowed.

Taxable income is defined as total revenues less nontaxable income, tax-exempt income, deductible expenses and tax losses. For PSC petroleum operations in China, deductions may typically include payments of revenue-based taxes and levies (including special oil gain levies and VAT levied at a rate of 5%), petroleum royalties or resource tax, deductible production and operating expenses, tax amortization of exploration expenditure and tax amortization of development expenditure.

All necessary and reasonable expenses incurred in carrying on a business are deductible for tax purposes, except for advertisement and sales promotion expenses, entertainment expenses, union fees, employee welfare costs and employee education expenses, which are subject to specified deduction thresholds. Qualified R&D expenditure may be deducted at 150% of the actual expenses. Charitable donations within 12% of the total annual profit are deductible.

The allocated management fee by a parent company to its subsidiaries is not deductible for CIT purpose under the prevailing China income tax regulations. However, a management fee allocated by head office to its branches may be deductible provided sufficient supporting documents can substantiate its reasonableness. In general, a reasonable service fee incurred by the head office can be deductible provided that such expenses are actually incurred and supported by proper documents, and the price follows the arm's-length principle. Reasonable and related expenses actually incurred by an enterprise, including costs, expenses, taxes, losses and other expenses, are deductible in calculating taxable income for CIT purposes. Provisions are in general not deductible, such as various provisions and allowances for asset impairment and risk reserves.

The regulation of Shuizonghan (2015) No. 494 has specified that if a foreign party enters into an agreement with a Chinese party for cooperative exploitation of oil and gas but does not set up an independent enterprise in China, the foreign and Chinese parties must both pay CIT. The foreign party is regarded as a nonresident enterprise having an establishment or place engaged in production or operation activities in China, and the income derived by it from cooperative exploitation of oil and gas shall pay CIT on its China-sourced income derived by such establishment or place, and on its foreign-sourced income which is effectively connected with such establishment or place of business. The after-tax profits obtained by foreign parties are exempt from CIT.

If a foreign party and a Chinese party jointly establish a Sino-foreign cooperative joint venture to carry out the exploitation of oil and gas, the joint venture shall be regarded as a resident enterprise regardless of its legal status and pay CIT on its income from exploitation of oil and gas and other income. The after-tax profits derived by the foreign party as the investor from the Sino-foreign cooperative joint venture shall pay CIT on its China-sourced income.

Foreign tax credit

Before 1 January 2017, a foreign tax credit (FTC) is allowed for foreign income taxes paid, or indirectly borne, by China resident enterprises, but the credit is generally limited to the amount of China CIT payable on the foreign-sourced portion of an enterprise's worldwide taxable income and must be calculated on a country-by-country basis. For dividend income derived from overseas subsidiaries, FTCs would be allowed within three tiers, provided the qualified shareholding percentage requirement is met.

Special FTC treatment has been granted to Chinese oil companies under Caishui (2011) No. 23, which extends the FTCs from dividend income derived by Chinese oil companies up to five tiers (for foreign-sourced income derived from the investment activities, construction service and technical service of oil and gas exploration projects overseas). In addition, Chinese oil companies are able to select either the country-by-country method or general deduction method. The general deduction method (or combined method) applies to only a specific class of worldwide income, i.e., foreign-sourced income relating to the exploration of crude oil and relevant technical services (upstream-related activities).

Once a calculation method is adopted, no changes can be made for five years. The balance of creditable foreign tax and FTC limit calculated for prior years can be carried forward and credited in the remaining years, according to the China CIT Law.

On 28 December 2017, the Ministry of Finance and State Administration of Taxation jointly released Caishui [2017] No. 84 ("Circular 84") which took retroactive effect from 1 January 2017 to improve the current FTC policies for all industries. According to Circular 84, a PRC resident enterprise is allowed to calculate its FTC limit either on a country-by-country method or a general deduction method. Once a PRC resident enterprise elects to apply a method, the basis should not be changed for five years. In addition, according to Circular 84, in addition to Chinese oil companies, for dividend income derived from overseas subsidiaries, FTCs are expanded to five tiers for all industries.

Abandonment expenses

The actual incurred abandonment expense is deductible for China CIT purposes, but it should be netted against the provision made. The regulation of SAT Announcement (2011) No. 22 (Notice 22), issued by the State Administration of Taxation, provides the following detailed regulations, which were effective from 21 April 2011.

Registration of abandonment plan

Expenses incurred on abandonment of offshore oil and gas production facilities cover expenditure on disposal, removal and environment restoration of offshore oilfields and the related preparatory works. According to Notice 22, an operator of the oilfield should prepare and register the detailed provisional abandonment plan for offshore oil and gas production facilities with its competent tax bureau before it starts deducting the provision for abandonment expenses.[2] The provisional abandonment plan should cover an estimation of abandonment costs, funding arrangements and methods to dispose of the facilities.

Before the company implements the abandonment of the oilfield, the implementation plan for the abandonment should be registered with the competent tax bureau.

Provision for abandonment expenses and tax treatment

Provision for abandonment expenses should be made on a monthly basis in the month after the relevant oilfield enters into commercial production. The provision should be made based on the "production method" or "straight-line method" in accordance with the proposed abandonment plan. Such provisions would be managed as a special fund and would be deductible for CIT purposes.

Under the straight-line method, the formula would be:

Monthly provision for abandonment expenses = (total estimated abandonment expenses — accumulated provision for abandonment expenses)/PSC contract production period (in months) — gain or losses of designated account for abandonment expenses for current month

2 *According to Circular [2010] No. 1305, jointly issued by the Ministry of Finance and other authorities, provision for abandonment expenses should start to be made in the month following the month in which the oilfield commenced commercial production.*

Under the production method, the formula would be:

Monthly provision for abandonment expenses = (total estimated abandonment expenses — accumulated provision for abandonment expenses) x current month's provision ratio — gain or losses of designated account for abandonment expenses for current month

Current month's provision ratio = current month's actual production/ (current month's actual production + closing proved exploitation reserves) where "gain or losses of designated account for abandonment expenses" includes interest income and foreign-exchange gain or loss in relation to the designated account

Use of abandonment expenses provision

Upon implementation of the abandonment plan, the actual incurred abandonment expenses would be netted against the provision made. If there is any unused provision after completion of the abandonment plan, the provision balance should be added back to the taxable income of that year. However, any abandonment expenses incurred in excess of the provision made would be deductible from the taxable income of that year.

Management of abandonment expenses provision

The provision and use of abandonment expenses should be accounted for in RMB. Any foreign-exchange gain or loss should be taken into account in calculating the provision to be made.

The provision for abandonment expenses should not be used for other purposes. Otherwise, the amount used for other purposes in which a tax deduction has been claimed should be added back for income tax purposes.

Service contracts

Foreign contractors that provide services to a petroleum company in China are liable to pay Chinese taxes, including CIT, VAT and some other local levies.

CIT is payable at the standard tax rate of 25% of actual profits derived by a foreign contractor or on the imputed profits agreed upon between a foreign contractor and the tax authorities.

VAT at 11% or 6% generally applies to provision of oil and gas field services. Foreign companies that provide oilfield services in China should pay VAT in accordance with relevant rules and regulations.

The petroleum company that receives the services is deemed to be the tax-withholding agent.

Tax on engineering, procurement and construction contract in China

Under the China turnover tax regime, an engineering, procurement and construction (EPC) contract is not administered as one single contract. The EPC parts of the contract will be charged with VAT at the rates of 6%, 17% and 11%, respectively, allowing the input VAT to be offset against the output VAT. In terms of CIT, the cost/expense incurred for the implementation of the EPC contract is an allowable deduction for CIT purposes.

Unconventional oil and gas

The Chinese Government issued a shale gas industry policy in October 2013, which states that the Government will continue to increase financial support for shale gas exploration and extraction. The policy includes five items, such as designating shale gas as one of the nation's strategic emerging industries, providing subsidies for shale gas producers, encouraging provincial governments to subsidize local producers, tax reductions or exemptions for producers and customs tariff exemptions for imported equipment.

Upon approval by the Ministry of Finance and the National Energy Administration, unconventional oil and gas projects can be entitled to a specific national financial subsidy.

C. Capital allowances

Amortization of expenditure on acquisition of oil (gas) field interests and exploration expenditure

Under Circular Caishui (2009) No. 49 (Circular 49), qualified expenditure on the acquisition of oil (gas) field interests and exploration expenditure incurred by a petroleum company can either be expensed against production income generated from other oil (gas) fields that the company owns in China or be capitalized and amortized on a straight-line basis against production income generated from the oil (gas) field for which the expenditure was incurred. The minimum amortization period of the exploration expenditure is three years, starting from the month during which commercial production commenced.

Expenditure on the acquisition of an oil (gas) field (oilfield acquisition expenditure) includes all necessary expenditures incurred in obtaining the exploration right.

Exploration expenditure may include the drilling of appraisal wells, feasibility studies, the preparation of an overall petroleum development program, and other work to identify petroleum reserves and to determine whether the reserves have commercial value. Exploration expenditure may also include expenses incurred for scientific research and training for the development of petroleum resources in China.

Any remaining oilfield acquisition expenditure and exploration expenditure balance that is not yet amortized can be expensed if the operations cease as a result of a failure to discover any commercial oil (gas) structure. Net operating tax losses may be carried forward for five years to offset against future taxable income. Carryback of losses is not allowed.

If the exploration drilling expenses incurred result in fixed assets and the relevant oilfield enters into commercial production, the unamortized exploration drilling expenses should be reclassified as development expenditures for depreciation purposes.

Depreciation of development expenditure

Under Circular 49, qualified development expenditures may be depreciated on a straight-line basis against production income generated from the oil (gas) field for which the expenditure was incurred, subject to a minimum period of not less than eight years starting from the month during which commercial production commenced. If the operation of an oil (gas) field is terminated, the residual value of the development assets would be recognized as a loss and be deductible for CIT purposes in the year of termination. Net operating tax losses may be carried forward for five years to offset against future taxable income. Carryback of losses is not allowed.

Development expenditure includes activities such as design, construction, installation, drilling and the corresponding research work, performed during the period starting from the approval date for the overall petroleum development program up until the commencement date for commercial production. Expenditures, including all investments — either tangible or intangible (and including fixed assets acquired) — that have been made during the period of development operations should be capitalized, based on each individual oil (gas) field.

D. Investment incentives

In an effort to support oil and gas drilling, the Chinese Government has issued tax exemption incentives for drilling programs in China. During China's 12th five-year period, which started on 1 January 2011 and ended on 31 December 2015, oil and gas drilling projects on specially appointed land and sea areas were exempt from import duties and import VAT on equipment, instruments, accessories and special-purpose tools that domestic companies are unable to manufacture and that are directly used in exploration and exploitation. The exemptions are valid within quotas for free imports.

Tax-exempt drilling programs include projects on deserts and barren beaches in Chinese territory, land blocks jointly exploited by Chinese and foreign companies under the permission of the Chinese Government, inland seas, territorial waters, continental shelves and other maritime resources under China's jurisdiction.

According to circulars Caiguanshui (2016) No. 68 and Caiguanshui (2016) No. 69, this policy is extended to the 13th five-year period, which started on 1 January 2016 and ends on 31 December 2020.

According to the regulation of Caishui (2015) No.76, the urban land use tax exemption incentive will be given to oil and natural gas (including shale gas and coal bed methane) production enterprises temporarily for certain land for production and construction of oil and natural gas (including land temporarily used for geological exploration, drilling, borehole operation, oil or gas field surface engineering and other construction, land used for special railway line, highway and oil, gas, or water pipeline outside the factory of an enterprise, and land used for pipelines for long-distance transportation of oil and gas) and land used for fire protection, flood prevention and drainage, wind protection and sand protection facilities in industrial and mining areas outside a city, county and designated town.

E. Withholding taxes and double tax treaties

Remittance of dividends, interest, royalties and rental income is subject to withholding tax (WHT) at a rate of 10%. WHT is due at the time the remittance is made or at the time the relevant transaction and costs are recorded in the accounting books of the Chinese payer, whichever is the earlier.

The treaty WHT rates for dividends, interest and royalties vary depending on the particular country. Generally speaking, dividend, interest and royalty WHT rates vary between 5% and 10%.

F. Financing considerations

According to relevant CIT regulations, interest expenses paid on bank loans used to finance taxable operations are generally deductible. Interest expenses paid on loans from related parties other than a financial institution are also deductible. The deduction is subject to the arm's-length principle and generally should be subject to a debt-to-equity ratio of two to one. Please note that PSCs are not subject to the thin capitalization regime (i.e., the deductibility of interest is not subject to a two-to-one debt-to-equity ratio).

Deemed interest cost recovery on development costs is not deductible for income tax purposes.

G. Transactions

Disposal of PSC interest

Gains, if any, derived from the disposal of an interest in a PSC are taxable in China. Taxable gains are equal to the disposal proceeds less the remaining balance of exploration and development expenditure that has yet to be amortized for tax purposes. Costs incurred for acquiring an interest in a PSC may be claimed as qualified exploration and development expenditure and are eligible for tax amortization according to the relevant tax rules.

According to the announcement (2015) No. 7 issued by the State Administration of Taxation, if a nonresident enterprise indirectly transfers equities and other properties (China taxable assets) of a Chinese resident enterprise to avoid its obligation to pay CIT by implementing arrangements lacking reasonable commercial purposes, such indirect transfer shall be re-characterized as a direct transfer of China taxable assets and shall be subject to CIT. The assessment factors for the reasonable commercial purpose test include whether the income is of a China source, economic substance assessment and tax purpose test. All relevant arrangements related to an indirect transfer of China taxable assets are considered in totality when assessing "reasonable commercial purposes" under the rule of "substance over form."

The buyers (whether resident enterprises or not) who are obliged to pay relevant consideration are withholding agents of CIT with respect to the capital gain derived from an indirect transfer of China taxable assets.

Generally, an interest in a PSC qualifies as China taxable assets. However, currently it is still unclear whether the indirect transfer of a PSC interest should be assessed as a return on investment or as a capital gain for CIT purposes.

H. Indirect taxes

Customs duties

The importation of tangible goods (including equipment and materials) into China for the purpose of petroleum exploration, development and production is subject to customs duties. However, this arrangement is subject to the availability of special import incentives, as discussed in Section D.

VAT

VAT is payable at a rate of 5% on the crude oil and natural gas produced from an oil (gas) field operated under a Sino-foreign PSC.

The purchase of goods (including equipment and materials) supplied in China is subject to VAT, generally at the standard rate of 17%. After the full implementation of VAT reform on 1 January 2009, input VAT associated with the purchase of fixed assets is deductible against output VAT unless the taxpayer is subject to the special VAT exemption regime as discussed in Section D.

Consumption tax

CT is payable on the production and importation of certain luxury items, such as cigarettes, gasoline, alcoholic beverages, jewelry, high-end cosmetics (including high-end beauty and makeup cosmetics, high-end skin care cosmetics and cosmetics sets), motor vehicles, motor vehicle tires, golf balls and equipment, luxury watches and yachts.

For petroleum products, the CT shall be calculated based on the volume of the sales and its related fixed tax rate, as shown below:

Petroleum products	Tax rate*
1. Petrol	RMB1.52/liter
2. Diesel	RMB1.2/liter
3. Aviation kerosene	RMB1.2/liter (CT collection to be deferred)
4. Naphtha	RMB1.52/liter
5. Solvent oil	RMB1.52/liter
6. Lubricant	RMB1.52/liter
7. Fuel oil	RMB1.2/liter

* The CT rate for petroleum products described above took effect since 13 January 2015.

Local levies

To unify the city construction tax (CCT) and education surcharge (ES) treatments applicable to foreign enterprises (FEs), foreign investment enterprises (FIEs), domestic enterprises and individuals, on 18 October 2010, the State Council announced circular Guofa (2010) No. 35 to resume from 1 December 2010 the collection of CCT and ES from FEs, FIEs and foreign individuals who had been exempted from these local levies for more than 20 years. On 7 November 2010, the Ministry of Finance released another circular, Caizong (2010) No. 98, regarding the unification of the local education surcharge (LES) on all parties subject to turnover tax in China. LES is a separate local levy from CCT and ES, but these three levies share the same tax base, i.e., the turnover taxes (VAT and consumption tax) actually paid by taxpayers.

The applicable rates of the local levies:

- CCT — 7% of China turnover taxes for a taxpayer in a city; 5% of China turnover taxes for a taxpayer in a country town or town; 1% of China turnover taxes for a taxpayer in a place other than a city, country town or town
- ES — standardized as 3% of China turnover taxes
- LES — standardized as 2% of China turnover taxes

SAT issued a special tax circular (SAT Circular (2010) No. 31) on 30 December 2010 to reconfirm that foreign oil companies participating in upstream petroleum production are liable to pay CCT as well as ES. CCT and ES are levied at their respective applicable rates on the 5% flat rate VAT payment made by the foreign oil company. The applicable CCT rate is 1% for a foreign oil company participating in an offshore oil production project.

Circular No. 31 does not clarify whether a foreign oil company would also be liable to pay LES. Assuming that LES would also be payable, extra indirect tax costs to an offshore oil production project would be equivalent to 6% of the VAT payments, adding CCT, ES and LES together, whereas the extra indirect tax costs to an onshore oil production project could be equivalent to 12% of the VAT payments should the project be located in a city.

I. Other

Transfer pricing

China has introduced transfer pricing rules that require all fees paid or charged in business transactions between related parties to be determined based on an arm's-length standard. If the parties fail to meet this requirement, the tax bureau may make reasonable adjustments by using one of the following methods:

- Comparable uncontrolled price (CUP)
- Resale price method (RPM)
- Cost plus method (CPM)
- Transactional net margin method (TNMM)
- Profit split method (PSM)
- Other methods that are consistent with the arm's-length principle

The new income tax regime recognizes the concept of cost-sharing arrangements. Taxpayers may also apply for advance pricing agreements (APAs) in China.

General anti-avoidance rules

The CIT regime introduced general anti-avoidance rules that require any tax planning to have a "business purpose."

The controlled foreign corporation (CFC) rules have also been introduced to counter planning based on income deferral. Under the rules, a CFC's retained earnings are subject to current Chinese taxation if the earnings are retained overseas without a reasonable business purpose.

Colombia

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- □ **Production sharing contracts**
- □ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies to the oil industry consists of a combination of corporate income tax (CIT) and royalty-based taxation.

Royalties[1]

New oil and gas discoveries after Law 756 issued in 2002: field daily production (Monthly average in barrels of crude per day)	Percentage (%)
Up to 5,000	8%
5,001 to 125,000	8% + ([production – 5,000] × 0.10)
125,001 to 400,000	20%
400,001 to 600,000	20% + ([production – 400,000] × 0.025)
More than 600,000	25

Royalties for gas exploitation are obtained by applying the following percentages on oil royalties:

Location	Percentage
Onshore and offshore below 1,000 ft. depth	80%
Offshore more than 1,000 ft. depth	60%

Royalties on unconventional hydrocarbons — shale gas, shale oil, tar sands and tight sands — are equivalent to 60% of those on conventional oil.[2]

1 *Law 756 entered into force on 25 July 2002 (Official Diary No. 44,878). Law 1530, issued on 17 May 2012, modified some aspects of Law 756.*

2 *Decree 4923 of 26 December 2011.*

Bonuses

Economic rights to be paid to the National Hydrocarbon Agency (ANH)[3] are applicable[4] as set out in the table below. Further details are included in the section on "Royalty regimes."

Rights for the use of the subsoil (exploration phase)	An amount in US dollars per hectare, depending on the location and area of the block and the duration of the phase
Rights for the use of the subsoil exploration and production (E&P)	An amount in US dollars per barrel
Participation rights	A percentage of the production (after royalties) to the extent agreed in the contract
Rights for high prices	Agreed in the contract as explained below, with regard to the level of production paid in-kind or in cash set by the ANH
Rights of participation relating to the extension of production phase	If the production phase is extended, the contracting party pays the ANH a sum depending on the nature of the hydrocarbon (10% or 5% as explained below)
Technology transfer rights	An amount set in relation to the number of hectares and the fraction of the contracted area, and rights for the use of the subsoil fixed

Production sharing contract

It is no longer possible to execute new production sharing contracts (PSCs) in Colombia. PSCs were used until Decree 1760 of 2003 came into effect.

PSCs executed before Decree 1760 of 2003 may still be in force. Therefore, it is possible to become an associate of a PSC if an associate of one of the contracts in force assigns the economic rights in the contract, either totally or partially.

Exploration and production

The oil and gas contract model was changed, from PSC to an exploration and production (E&P) contract — which is a type of contract similar to a concession contract (royalty and tax system) — entered by the ANH. The contractor autonomously explores and produces at its own risk and cost. The length of time in each phase of the E&P contract is as follows[5]:

- Phase 0 — up to 24 months, with extensions allowed to identify special zones and consult with local communities (i.e., indigenous territories)
- Exploration — six years, with extensions allowed under certain conditions
- Evaluation — up to two years
- Exploitation — up to 24 years (plus extensions no longer than 10-year periods until final depletion).

3 *Agencia Nacional de Hidrocarburos (ANH).*

4 *In development of Resolution 502 of 2017 on the Opening of the Competitive Procedure Sinú San Jacinto 2017.*

5 *Under 2017 version of the E&P contract, extensions can be granted under certain conditions.*

The contractor has all the production rights, after a sliding-scale royalty payment, and makes conditional payments to the ANH to share surplus income in case of high crude prices. Natural gas and heavy crude have these general tax considerations and special incentives:

- Income tax rate — CIT rate: 34% for FY 2017 and 33% from 2018
- Income tax surcharge — 6% for 2017, 4% for 2018 and 0% from 2019
- Wealth tax
- Return to report assets held abroad (foreseeable depending on the operation of each companies; but not applicable to Colombian branches)
- Resource rent tax — not applicable
- Capital allowances — D, A[6]
- Investment incentives —Don, Env, R&D, CERT, heavy machinery and capital goods[7]

B. Tax regime

Corporate tax

"Domestic corporations" are corporations organized under Colombian law. "National corporations" are corporations with their principal domicile within the Colombian territory, organized under Colombian law, or that during the respective taxable year or period have their effective place of management in the Colombian territory (simply holding board meetings in Colombia is not enough to qualify as a national corporation). National corporations are taxed on worldwide income and capital gains.

Permanent establishment

The permanent establishment (PE) concept was introduced into domestic tax legislation[8] from 2013. The PE definition maintains the main characteristics of the Organisation for Economic Co-operation and Development (OECD) model definition, with some exceptions (paragraphs 3 and 7 of Article 5 of the OECD model). The PE will be subject to tax on income and capital gains sourced only in Colombia, and attribution will be based on domestic "tax accounting" records, which should be supported mainly by an analysis of functions, assets, risks and personnel. Oil and gas fields are expressly considered as a PE by local law.[9]

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6 *D: depreciation; A: amortization. A special 30% capital allowance for investment in real productive fixed assets was granted, except for free-trade-zone taxpayers, up to FY2010. As of FY2011, 30% applies only for taxpayers with legal stability agreements filed before 1 November 2010 who have been granted the application of the tax benefit up to three years since its stabilization; from 2017, taxpayers can deduct all value-added tax (VAT) paid on the acquisition or importation of capital goods taxed at the general rate.*

7 *Don: donations; Env: tax credit of 25% of investments in the environment; R&D: special deduction for donations and investments in research, technological development and innovation or/and tax credit of 25% of investments made in research, technological development or innovation; CERT: the investments in the hydrocarbons sector that will give rise to the granting of CERT will be exclusively those that aim at the discovery of new hydrocarbon reserves, an increase in proven reserves or establishment of new recoverable reserves; Heavy machinery: tax credit of VAT paid on the acquisition and importation of heavy machinery for basic industries; capital goods: special deduction of all VAT paid on the acquisition or importation of capital goods taxed at the general rate.*

8 *Law 1607 of 2012.*

9 *According to Decree 3026 of 2013, for the purpose of its definition in Colombia, PE is included in the concept of a foreign company, not only for companies and foreign entities but also for foreign individuals who develop any business or activity. The decree expressly considered business or activity, the activities of the professions, the provision of personal services and activities of an independent character. The definition of PE includes the fixed place for business as a place for business within Colombian territory.*

Corporate income tax

As the result of the recent tax reform (Law 1819 of 2016), the income tax and the income tax for equality (CREE) have been combined into one single tax, CIT.

The general rate is 34% for 2017 and 33% for 2018 and onward.

In addition, a surtax of 6% and 4% is applicable for 2017 and 2018, respectively; this surtax applies to taxpayers with taxable income greater than COP800 million (approx. US$266,000). This surtax is subject to an advance payment equal to 100% of its estimated value.

In summary, CIT rates are:

Concept	FY 2017	FY 2018	From FY 2019
CIT	34%	33%	33%
Surtax	6%	4%	0%
Total rate	40%	37%	33%

The free trade zone (FTZ) income tax rate is 20% for legal entities that perform activities in the industrial FTZs and that qualify as "manufacturing users"[10] or "users that provide services."[11] The reduced income tax rate does not apply to commercial users.[12]

Previously, the businesses involving exploration, exploitation or extraction of nonrenewable natural resources could not obtain an FTZ status. However, according to the Decree 2147, 2016, offshore FTZs for development of oil and gas activities are allowed subject to certain conditions.

Offshore free trade zones

By means of the Decree 2147 of 2016, the national Government introduced the requirements for establishing an offshore FTZ. This incentive is aimed at developing offshore exploration and production projects in a form of FTZs, which would provide tax and customs benefits.

The application for a certificate establishing a FTZ should be filed for the considered activities (technical evaluation activities, exploration and production of hydrocarbons offshore and related activities) with the ANH, which will also approve the entity that will act as an operator of a project.

The certificate of an offshore FTZ shall comprise continental or insular areas for the development of logistic, compression, transformation, gas liquefaction and other activities directly related to the offshore hydrocarbons sector.

According to Article 43 of Decree 2147 of 2016, within six years following the authorization of an offshore FTZ, the operator of the agreement signed with the ANH shall:

- Perform an investment in an amount equal to or greater than the remaining value of the agreement as of the application for the declaration of a FTZ in each contract signed with the ANH comprising the offshore FTZ
- Creation of at least 30 new direct jobs

10 *"Manufacturing user" is an entity authorized to produce, transform or assemble goods through the processing of raw materials or semi-manufactured products, exclusively in one or more free trade zones.*

11 *"Users that provide services" are entities authorized to develop the following activities exclusively in one or more free trade zones: (i) logistics, transportation, handling, distribution, shipping, labeling and classification of goods; (ii) communications and data processing; (iii) science and technological research; (iv) medical assistance and health services; (v) tourism; (vi) maintenance of goods; (vii) technical support maintenance of aircraft and related equipment; and (viii) auditing, administration, consulting and others.*

12 *"Commercial user" is an entity authorized to develop marketing activities, merchandising, storing or preservation of goods.*

Tax year and due dates for corporations

The tax year is the calendar year for the CIT return. The Colombian Government sets the due dates for filing tax returns and making tax payments annually. Income tax is paid in three installments by large taxpayers and in two installments by all other corporate taxpayers. Each year, the tax authorities identify and list the companies they will consider to be large taxpayers as of that year, as well as companies that will be removed from the list.

Taxable income for CIT purposes

The tax basis for calculation of annual CIT payments is the higher of ordinary taxable income and presumptive income.

Ordinary taxable income

Ordinary taxable income is calculated by subtracting deductible costs and expenses from net revenues (taxed revenues minus rebates and discounts). If this calculation results in a net operating loss (NOL), the loss may be carried forward in the following 12 taxable periods.

Additional restrictions apply to the transfer of tax losses in mergers or spin-offs (which may be tax-free events for Colombia tax purposes if certain requirements are met). The transfer of tax losses in mergers and spin-offs is applied only where the economic activity of the companies involved (which generates the losses) remains the same after the merger or spin-off occurs.

The amount of income tax payable after tax credits may not be less than 75% of the income determined under the presumptive income rules before taking the tax credits into account.

Presumptive income

Presumptive income is calculated as 3.5%[13] of the taxpayer's prior year tax equity ("net tax equity" is tax assets minus tax liabilities). Liabilities held with related parties abroad can be regarded as debt for local tax purposes (if transfer pricing requirements are met).

Some assets may be excluded from the taxable basis — for example, the net equity value of assets during nonproductive periods of an enterprise and associated with the same unproductive contract.[14] The excess of presumptive income may be carried forward as a compensation for five years.

Costs and expenses

Costs and expenses may generally be deducted from income tax, provided that they are necessary and related to the generation of taxable income, and the expenditure is not limited or forbidden by law.

Payments abroad

In general, taxpayers may deduct expenses incurred abroad if they are related to national source income and if:

- Where applicable, the relevant withholding tax is made on the payments
- The amounts charged comply with the transfer pricing rules
- Exchange regulations are fulfilled[15]

If tax withholdings are not required, deductibility of costs and expenses abroad is limited to 15% of the net taxable income before such payment. Compliance with transfer pricing rules is mandatory, where applicable.[16]

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13 *The new presumptive income rate only applies from 2017. The previous rate was 3%.*

14 *On 5 May 2011, a decision issued by a law tax court (Council of State) confirmed that reference to "enterprise" must be taken based on a contract (not an individual well), when establishing the productivity of assets in the determination of presumptive income tax.*

15 *Sections 123 and 419 of the Colombian Tax Code.*

16 *Sections 121 and 122 of the Colombian Tax Code include some exceptions to this 15% limitation; also Sections 124 and 260-7.*

Accounting and tax interaction

For the purposes of determination of the taxable basis and valuation of assets, liabilities, income, costs and expenses, taxpayers must use systems and principles currently effective for the recognition and measure, whenever the tax legal framework makes a reference to International Financial Reporting Standards (IFRS) for when a differential treatment is not provided for.

Accounting rules of accrual and accumulation should be used for the registration of assets, liabilities, income, costs and expenses.

A series of exemptions to the general rule of accrual or accumulation of income, costs and expenses are accepted, including those relating to interest, impairment and others. Transactions that may have an impact on other comprehensive income (OCI) will have tax effects only in the moment; they must be presented as year-end results or reclassified to an account different from OCI generating a taxable income.

Capital gains tax

Gains on the sale of assets considered fixed assets[17] and owned for more than two years are subject to capital gains tax (CGT) at a rate of 10%. Capital losses may be offset against capital gains generated in the same taxable year. The portion of the capital gains that corresponds to previous depreciation/amortization deductions must be treated as a deduction recapture, which means that the amount is treated as ordinary income. In the case of payment in favor of foreign entities on the basis of capital gains, a withholding tax must be paid at a 10% rate.

Functional currency

For tax purposes, financial and accounting information, as well as assets, liabilities, equity, revenues, costs and expenses, shall be carried out and presented in Colombian pesos (COP) from the moment of initial recognition and thereafter.

Transfer pricing

Income tax payers that (i) carry out transactions with foreign related parties, (ii) are domiciled in the national customs territory (*Territorio Aduanero Nacional* — TAN in Spanish) and carry out transactions with related parties located in free trade zones or (iii) carry out transactions with individuals, partnerships, entities or companies located, resident or domiciled in tax havens or benefiting from harmful preferential tax regimes, are required to comply with the transfer pricing regime.

In addition, permanent establishments of nonresident individuals or legal entities or of foreign entities as well as branches and agencies of foreign partnerships, subject to income tax in Colombia, that carry out transactions with (i) related parties domiciled abroad, (ii) related parties in free trade zones or (iii) people, partnerships, entities or companies located, resident or domiciled in tax havens or benefiting from harmful preferential regimes, are also required to comply with the transfer pricing regime.

As a consequence, taxpayers obliged to fulfil the transfer pricing regime must determine their income, costs, deductions, assets and liabilities considering the conditions that would have been agreed in comparable transactions with, or between, independent parties (i.e., their transactions should comply with the arm's-length principle).

For income tax purposes, and particularly for the application of transfer pricing rules, the law considers that a party is related to another under the following scenarios: (i) subsidiaries, (ii) branches, (iii) agencies, (iv) permanent establishments and (v) other situations, including cases in which transactions

17 *Section 60 of the Colombian Tax Code defines "fixed assets" as "those assets which are not sold or changed in the regular course of business." Additionally, "Movable assets correspond to inventories. Fixed assets correspond to all assets other than inventories and will be classified in accordance with new regulatory technical frameworks, such as property, plant and equipment, investment property, non-current assets held for sale."*

are carried out between related parties through third parties, whenever more than 50% of the gross revenues arise individually or jointly from their partners or shareholders, or when consortiums, temporary unions, participation agreements and other association models that do not give rise to the establishment of legal entities exist, among others.

The Colombian regime includes several of the methods contained in the transfer pricing guidelines published by the Organisation for Economic Co-operation and Development (OECD). However, as a result of rulings of the Constitutional Court of Colombia, the OECD Guidelines may not be directly referred to for purposes of interpretation of the Colombian transfer pricing rules and are considered auxiliary criteria for interpretation.

Significant aspects of the transfer pricing system in Colombia include the following:

I. Transfer pricing obligations

a. **Transfer pricing return, local file and master file**

Income taxpayers, including individuals, legal entities and permanent establishments that on the last day of the taxable year register either (i) gross equity (assets) equal to or higher than 100,000 tax value units (*Unidades de Valor Tributario* — UVT in Spanish) (approximately US$1,096,000 for taxable year 2017) or (ii) gross revenues equal to or higher than 61,000 UVT (approximately US$668,000 for taxable year 2017) are required to present a transfer pricing return.

On the other hand, a transfer pricing report must be prepared and filed, and such document must contain a master file including relevant information of the multinational group, and a local file, containing information related to the specific transactions carried out by the Colombian entity. The transfer pricing report must be prepared by companies that perform transactions that exceed 45,000 UVT (approx. US$493,000 for taxable year 2017), per transaction type.

If taxpayers register transactions with individuals, partnerships, entities or companies located, resident or domiciled in tax havens or benefiting from harmful preferential regimes, the transfer pricing report should solely be prepared for those transactions that surpass 10,000 UVT (approx. US$110,000 for taxable year 2017).

The transfer pricing documentation (local file and master file) shall be kept (i) during five years, which will be counted starting on 1 January of the following taxable year or (ii) for as long as the tax return's statute of limitations is open — whichever covers the longest span of time.

b. **Country-by-country report**

As of taxable year 2016, taxpayers of the income tax who fulfill any of the following conditions shall present a country -by-country report, containing information related to the global multinational group's allocation of income and taxes. The conditions are as follows:

- Controlling entities of multinational groups that fulfill the following:
    i. Are considered residents in Colombia
    ii. Own subsidiaries, branches or permanent establishments, residing or located abroad, accordingly
    iii. Are not subsidiaries of other companies domiciled abroad
    iv. Are required to prepare, present and disclose consolidated financial statements
    v. Registered consolidated revenues, for accounting purposes, equal to or greater than 81,000,000 UVT (approx. US$887,407,000 for taxable year 2017)
- Entities residing in the national customs territory or residing abroad that possess permanent establishments in Colombia, and that have been designated by the controlling entity of the multinational group, domiciled abroad, as the responsible entity to file the country-by-country report

- One or more entities or permanent establishments domiciled in the national customs territory that belong to the same multinational group, whose ultimate parent company is located abroad, and that fulfill the following conditions:

  i. When assessed as a whole, the Colombian entities contribute 20% or more of the consolidated revenues of the multinational group

  ii. The ultimate parent company has not filed the country-by-country report in its jurisdiction

  iii. The consolidated revenue of the multinational group is equal to or greater than 81,000,000 UVT (approx. US$887,407,000 for taxable year 2017)

Entities that belong to multinational groups and are tax residents in Colombia must notify the tax authorities about the identity and tax jurisdiction of the reporting entity of the group, in the means, formats, terms and conditions established by the National Government.

II. Other transfer pricing considerations

- Colombian law establishes that the application of the comparable uncontrolled price method in order to assess purchases of used assets must be carried out using the invoice issued by the third party when the asset was first purchased and the calculation should consider the depreciation up until the date of the transaction. The calculation shall take into account the accounting principles generally accepted in Colombia. In cases where the invoice is not available, and under the assumption that it is an asset being disposed of in a different state from the one that was originally purchased, a technical valuation performed by an independent expert might be presented.
- In transactions involving the purchase or sale of shares that are not quoted on stock exchange markets or transactions involving other assets that impose restrictions in terms of their comparability, the Colombian legislation establishes that common valuation methods shall be used, especially those that calculate market values based on the present value of future incomes. It is forbidden to use equity values as appropriate valuation methods.
- Beginning in 2017, the most appropriate method to analyze transactions involving commodities has been the comparable uncontrolled price method, and some criteria have been defined for its application. Transactions carried out between independent parties or prices quoted in national or international sources shall be used, taking into account essential elements such as the date or quoting period agreed between the parties. The date used to agree the price must be supported with documents such as agreements, offers and acceptance or any other related proofs, and their terms must be consistent with the actual behavior of independent parties under similar circumstances. These documents shall be registered in the electronic services provided by the tax authorities. If the taxpayer does not provide such proof or if the date used is not consistent with the market behavior, the tax authorities might consider the date set in the bill of lading as the most appropriate pricing date.
- To determine the level of comparability between controlled and uncontrolled transactions that allows the application of the transfer pricing methods, the following attributes must be taken into consideration:
  - Characteristics of the transactions
  - Economic activities or functions
  - Contractual terms
  - Market and economic circumstances
  - Business strategies

  Nevertheless, Colombian legislation has established further requirements regarding transfer pricing analysis for specific transaction types.

- For financing transactions, the law has established that the following comparability elements shall be taken into account: principal amount, term, credit rating of the debtor, collaterals, solvency and interest rate. In addition, the law establishes that, regardless of the interest rate set, interest payments shall not be deducted if the comparability elements are not met. If the terms and conditions of the financing transactions are not similar to market behaviors, the transactions might not be considered as loans but rather as capital contributions, and thus, interest payments shall be treated as dividends.
- It is important to mention that the Colombian legislation establishes that taxpayers shall give priority to internal comparables whenever they exist.
- With regard to costs or expenses for intragroup services, Colombian taxpayers must demonstrate that the services were in fact received, and an analysis of the benefits perceived shall be performed, considering main aspects such as (i) cost of the service, (ii) amount that a third party would be willing to pay, (iii) costs registered by the service provider and (iv) identification of the agreements, forms or methods used to support the invoices.
- Segmented financial information used for the preparation of the local file must be certified by a public accountant or independent auditor.
- Business restructuring in which functions, assets or risks of the Colombian entity are assigned or transferred to a foreign related party must comply with the arm's-length principle.
- Advanced pricing agreements (APAs) may be signed with the tax authorities and will have a five-year term (including one-year rollback).
- Penalties are imposed for failing to meet filing deadlines and requirements and for submitting erroneous or incomplete reports.

Preferential tax regimes (tax haven jurisdictions)

Colombian law establishes that for legal purposes the term "tax haven" means a noncooperative jurisdiction or a jurisdiction with a low-tax or no-tax burden. The national Government has published a list of the countries, jurisdictions, domains, associated states or territories that are considered tax havens for tax purposes.[18] Taxpayers that do business with a company located, domiciled or resident in a tax haven and want to deduct income tax payments must document and show detail of the functions performed, assets used, risks assumed, and all costs and expenses incurred by the beneficiary company in the tax haven.

Additionally, to constitute a cost or deduction, the taxpayer must have withheld tax (except for financial transactions registered with Colombia's Central Bank). If the payments constitute taxable income to the beneficiary company, the applicable tax rate is 34% for FY 2017 and 33% for FY 2018, regardless of the nature of the payments. The Colombian tax authorities have provided diverse interpretations of this point, which should be reviewed on a case-by-case basis.

Transactions with individuals, companies, firms or entities located, residing or domiciled in tax havens will be subject to the transfer pricing regime, requiring supporting documentation and an informative tax return to be filed.

Dividends

For Colombian tax purposes, the remittance of profits by a branch or PE to its parent entity is considered as a dividend (constructed dividend). Law 1819 of 2016 re-established taxation over dividends distributed to resident individuals and to nonresident legal entities and individuals. The dividend tax would apply to profits obtained from 2017.

Dividends paid to nonresidents are subject to CIT at the rate of 5%. If the dividends paid were taxed at a corporate (paying resulting CIT), PE or branch level, no additional tax would be applicable. Dividends paid to foreign legal entities arising from profits that were not subject to taxes at the level of the

18 *Decree 1625 of 2016.*

company distributing them would be first subject to a 35% withholding tax and then subject to a 5% withholding tax on the amount to be distributed, net of the 35% withholding tax.

If the nontaxable dividends in a given year are higher than the commercial profits of that year, the difference can be carried back for two years or carried forward for five years to offset the profits of such periods.

Please note that before the tax reform,[19] Regulation No. 3026 of 27 December 2013 provided guidance for profit distribution of branches that belongs to the special exchange law regime.

Such regulation provides that for income tax purposes, a branch that belongs to the special exchange law regime[20] must transfer profits to its home office when either of these facts arise:

- The equity account called "supplementary investment to assigned capital account" (ISCA by its initials in Spanish) results in a "debit balance" or negative balance. The Executive Order states that the value of the dividend shall be the same as the "debit balance" at the end of the year.

  Or
- When the debit balance at the beginning of the year increases during the year, the dividend value will correspond to the increase in the debit balance during the year.

Royalty regimes

Royalties for use of the production field

In Colombia, ownership of minerals found beneath the surface, including oil and gas, is vested in the national Government. Therefore, companies engaged in the exploration and extraction of nonrenewable resources (i.e., oil and gas) must pay the ANH (which represents the Government) a royalty at the production field, determined by the Ministry of Mining as follows:

- New oil discoveries following the introduction of Law 756 issued in 2002 (E&P contracts), as per the following table:

Field daily production (monthly average in barrels of crude per day)	Percentage (%)
Up to 5,000	8%
5,001 to 125,000	8% + (production – 5,000) × 0.10
125,001 to 400,000	20%
400,001 to 600,000	20% + (production – 400,000) × 0.025
More than 600,000	25%

- Prior to the introduction of Law 756 issued in 2002, two other royalty regimes applied: 20% and a sliding scale (5% to 25%).

19 *Law 1819 of 29 December 2016.*

20 *As a general rule, all business entities undertaking business operations in Colombia are subject to Colombia's exchange control regime provisions. Colombian incorporated legal entities are considered as "residents" for exchange control purposes and are subject to what is referred to as the "ordinary exchange control regime." Colombian registered branches of foreign legal entities also qualify as residents and are therefore subject to this same regime; however, if the sole business purpose of such a branch is to enter into oil and gas, coal, ferronickel, uranium exploration, and exploitation activities (qualified branch), the same may apply and validly qualify for "special exchange control regime" treatment.*

Royalties for gas exploitation are obtained by applying the following percentages to oil royalties:

Location	Percentage (%)
Onshore and offshore below 1,000 ft. depth	80
Offshore more than 1,000 ft. depth	60

Royalties on unconventional hydrocarbons — shale gas, shale oil, tar sands and tight sands — are equivalent to 60% of those on conventional oil.[21]

Currently, royalties are allowed to be collected in kind, and in certain cases, cash payment is also allowed.

Economic rights of the ANH[22]

Standard contracts for the exploration and exploitation of oil and gas set out various economic rights related to use of the subsoil and subsurface of an area, as described next.[23]

Right for use of the subsoil and subsurface during the exploration phase

Beginning with the second exploration phase, the contracting party pays a fee in US dollars as set out in the table below.[24]

By means of Circular 05 of 12 February 2018, the ANH updated the values of formulas for 2018 to determine economic rights corresponding to rights for the use of subsoil and rights for high prices.

For the purpose of economic rights assessments, the annual Producer Price Index (PPI) for 2018 is 0.4550%:

Monthly amount per phase in US$/hectares on exploration areas				
Size of contract area	First 100,000 hectares		Each hectare in addition to first 100,000	
Duration of the phase	<= 18	>18	< = 18	>18
Within polygons A and B	2.68	3.58	3.58	5.35
Outside polygons A and B	1.79	2.68	2.68	3.58
Offshore	0.90			

Terms applicable for Colombia rounds 2012 and 2014:

Size of contract area	First 100,000 hectares		Each hectare in addition to first 100,000	
Duration of the phase	<= 18 months	>18 months	< = 18 months	>18 months
Onshore	2.68	3.58	3.58	5.35
Offshore	0.90			

Please note that values can change depending on the negotiation of the contract.

21 *Decree 4923 of 26 December 2011.*

22 *The latest contract model appears on the ANH website: www.anh.gov.co (latest version for contracts entered into from 2017). The figures have been established by the Administrative Act Circular 05 of 12 February 2018*

23 *Established within the E&P contract (2017 model contract for E&P).*

24 *Annex C of the latest version of the E&P contract (2017 model contract for E&P).*

Right for the use of the subsoil and subsurface during the E&P phase

The contracting party pays ANH the resulting value of multiplying US$0.1353 by the number of barrels of liquid hydrocarbon owned by the contracting party and US$0.1353 per thousand cubic feet of natural gas.[25] This amount increases annually, based on the terms of the contract.

Rights for high prices

The production levy may be payable in cash or in kind and is linked to international prices for hydrocarbons. The rates vary depending on the quality of produced hydrocarbons and projects' logistics.

From the time when the accumulated production of the exploitation area, including the volume of royalties, exceeds five million barrels of liquid hydrocarbon (not applicable for extra-heavy hydrocarbons), and if the international oil reference price (West Texas Intermediate (WTI)) is higher than the price determined in the contract (Po), the contracting party shall pay an amount Q, at an agreed delivery point, for participation within the production, net of royalties, according to the following formula:

$$Q = [(P-Po)/P] \times S$$

Notes:

1. For gas, the rule applies five years after commencement of the exploitation field, instead of on the basis of accumulated production.
2. ANH may ask to receive this right in cash rather than in kind, according to certain rules set up in the E&P contract.
3. Q: Economic right to pay the ANH.
4. P: for liquid hydrocarbon, P is the average benchmark of the WTI index in US dollars per barrel. For natural gas, P is the average sale price of the gas sold in the contract in US dollars per million British thermal units (BTUs).
5. PO: for liquid hydrocarbon, PO is the base price of benchmark crude oil expressed in US dollars per barrel; and for natural gas, it is the average natural gas price in US dollars per million BTU, according to a table included in the contract. The table varies depending on one of the following: (i) the American Petroleum Institute (API) gravity of crude oil (starting from 15° API); for heavy crude oil, the rights for high prices are triggered if API gravity is higher than 10°; or (ii) discoveries more than 300 meters offshore; or (iii) the amount of natural gas produced and exported. However, if the API gravity is 10° or less, the rights for high prices are not triggered. Unconventional liquid hydrocarbons are included.
6. S: Participation percentage according to table B established within the E&P contract (2014 model contract for E&P).

WTI Price (P)	Percentage of participation (S)
Po ≤ P < 2Po	30%
2Po ≤ P < 3Po	35%
3Po ≤ P < 4Po	40%
4Po ≤ P < 5Po	45%
5Po ≤ P	50%

7. Almost all the amounts are subject to a readjustment formula already set up in the E&P model contract.

25 *Ibid.*

Rights of participation due to extension of production phase

If the production phase of an exploration area is extended from the initial exploitation phase subscribed in the E&P contract, the contracting party pays the ANH a sum equivalent to 10% of the production for light hydrocarbon, or 5% in the case of heavy hydrocarbon.[26]

Technology transfer rights

Technology transfer rights lead to a royalty payment to perform investigation, education and scholarships programs, from 25% of the amount resulting from multiplying the number of hectares and fraction of the contracted area to the value assessed on rights for the subsoil and subsurface.[27]

Other participation rights

The E&P model contract applicable for contracts submitted since 2009[28] allows the ANH to agree a percentage of the production with the contractor in other circumstances, subject to negotiation.

Unconventional oil and gas

Royalties on unconventional hydrocarbons — shale gas, shale oil, tar sands and tight sands — are equivalent to 60% of those on conventional oil.

C. Capital allowances

Depreciation

For income tax purposes, taxpayers are entitled to deduct reasonable amounts for the depreciation of goods used in business or income-producing activities, provided those have rendered service in the taxable year or period.

For income tax purposes, a taxpayer will depreciate the tax basis of depreciable assets, less its residual value over its useful life.

Depreciation basis is the acquisition price plus the directly attributable costs until the asset is available for use.

The useful life is determined according to the accounting technique according to IFRS.

The depreciation methods should be those established in the accounting technique of IFRS.

The annual depreciation rates should be those established in accordance with the accounting technique, provided those rates do not exceed the maximum rates determined by the national Government.

Maximum annual depreciation rates will vary between 2.22% and 20.00%.

In the absence of regulations,[29] in selected items, the maximum value should be as follows:

Type of asset	Annual tax depreciation rate (%)
Constructions and buildings	2.22%
Aqueduct, plant and networks	2.50%
Electric equipment	10.00%
Machinery, equipment	10.00%
Furniture and movable goods	10.00%
Computer equipment	20.00%

26 *E&P contract (2017 model contract for E&P).*

27 *Ibid.*

28 *The E&P contract used for 2013 onward corresponds to the 2009 E&P model issued by the ANH.*

29 *At the time of the issuance of this guide, such regulation has not been issued. Taxpayers should seek professional advice in this respect.*

Accelerated depreciation: the depreciation rate can be increased by 25% if the depreciable good is used daily for 16 hours and proportionally in higher fractions, provided this can be properly documented by the taxpayer.

The depreciable and amortizable assets held by the end of 2016 are subject to special provisions.

Amortization of investments in exploration, development and construction of deposits of mines, oil and gas for tax purposes

The following expenses incurred for the exploration of natural resources should be amortized:

- Acquisition of exploration rights
- Seismic, topographic, geological, geochemical and geophysical studies, as long as they are linked to a finding of the nonrenewable natural resource
- Exploratory drilling
- Excavations of ditches, trenches, pikes, exploratory tunnels, quarries, scaffolds and the like
- Sampling
- Activities related to the assessment of the commercial viability of the extraction of a natural resource
- Other costs, expenses and acquisitions necessary in this stage of evaluation and exploration of nonrenewable natural resources that are likely to be capitalized in accordance with accounting technique

The recent legislative changes introduced amortization and deduction rules of investments on evaluation, exploration, development and construction of mines and oil and gas fields, along with some transition rules for existing balances as of 31 December 2016.

Tax reform (Law 1819 of 19 December 2017) changes amortization rules in the oil and gas sector:

Exploration outcome	Amortization rules
Successful reservoir	Units of operation (UOP) = (Units produced in the year/proved reserves developed remnants or proven recoverable reserves at the end of the previous year) * balance to be amortized at the end of the previous year
Unprofitable reservoir	In the year in which it is determined or, at the latest, in the following two years

Investments made between 1 January 2017 and 31 December 2027 will be amortized by the straight-line method over a period of five years.

If the production is depleted earlier than provided for in the corresponding contract, the outstanding balance may be amortized in the taxable year or period in which that production status is verified or, in any case, at the latest, within two years of the testing.

Costs incurred in the process of improvement in the exploitation of a nonrenewable natural resource will be capitalized and amortized.

Until 2016, investments made in the mines and oil fields for the purpose of amortization could include disbursements made in areas in operation as in non-production areas. This is no longer permitted from 2017.

D. Incentives

Exploration

During a nonproductive period, an exploration company is required to calculate income tax under the presumptive income tax system. An exemption excludes nonproductive assets being affected by this tax assessment (explained in section B).

Temporary incentives incorporated as a response to the drop of oil price

The following measures,[30] among others, were incorporated as a response to the drop of oil price:

- It is permitted to extend the phases of exploration, evaluation programs and statements of commerciality up to nine months, with only one extension of six additional months. The terms and periods must be due within 12 months following the date of filing of the corresponding request.
- It is permitted to apply the E&P terms to the duration of the exploration agreement over offshore areas entered into before 2014, with agreements that were granted in the course licensing rounds in that year.

Tax holiday

Colombia does not have a tax holiday regime.

Incentives for the use of nonconventional and renewable energy

Law 1715 of 2014 was issued to promote the development and use of nonconventional and renewable energy sources. By Decree 2143 of 2014, the Government regulated those incentives with the following tax benefits.

Tax deductions: A deduction of 50% of the investment made for R&D related to the production and use of nonconventional and renewable energy is available for five years from the moment on which the investment was made.

This deduction cannot exceed 50% of the net income of the taxpayer calculated before deducting the amount of investment.

The taxpayer must obtain an environmental assessment certification issued by the Colombian Ministry of Environment.

Value-added tax (VAT) exemption: National and imported goods and services destined for pre-investment and investment in nonconventional and renewable energy are exempt from VAT.

The Ministry of Environment will certify the equipment and service covered by this exemption.

The Colombian Mining and Energy Planning Unit issues the list of goods and services covered with the VAT exemption.

Customs duty incentive: An exemption from customs duties on the importation of goods for pre-investment and investment in nonconventional and renewable energy is available.

This benefit applies only to goods that are not produced in the country, and any request for duty exemption should be filed by an applicant in advance of importation.

It is necessary to obtain a certification issued by Ministry of Mines and Energy through Colombian Mining and Energy Planning Unit.

Accelerated depreciation: Necessary goods for pre-investment and investment (acquired or built) of nonconventional and renewable energy will be able to apply for this regime.

The depreciation rate cannot exceed 20%.

Tax losses

Taxpayers can offset tax losses[31] against ordinary net income obtained in the following taxable period without prejudice to the presumptive income for the year. A tax loss may be carried forward for the following 12 taxable periods.

30 Decisions 02 and 04 of 16 March and 8 September 2015 issued by ANH.

31 Tax losses arising from nontaxable income and from costs and deductions that do not have relationship with the generation of taxable income, in no case may be offset against net income of the taxpayer.

CIT returns from which tax losses arise or in which prior year tax losses are claimed are open for review by the tax authorities for a longer period than the standard period.

If the tax loss is offset in any of the last two years, the statute of limitations will be extended from said offset for a further three years in relation to the return in which said loss was offset.

Offsetting tax losses and presumptive income excess that originated before 2017 (for income tax and income tax for equality purposes) will follow applicable rules at the time they originated. However, the value to be offset should be determined in accordance with the formula provided for in article 290 of Law 1819 of 2016.

Additional restrictions apply to the transfer of losses in mergers or spin-offs (which are tax-free events for Colombian tax purposes, under certain circumstances). In mergers, the surviving entity may offset losses originating in the merged entities, limited to the percentage of its equity participation in the merged entity's equity. In spin-offs, the new company (or companies) or the resulting companies may offset losses originating in the spun-off entity, limited to the participation percentage of the new companies in the equity of the spun-off company. Tax losses generated do not affect the entity's presumptive income for the relevant tax year. To have the right to offset tax losses, companies involved in mergers or spin-offs are required to carry on the same economic activity as they did before the merger or spin-off process.[32]

Regional incentives

Section 16 of Decree 1056 of 1953 (the Oil Code) states that "oil exploration and exploitation, the extracted crude oil, its derivatives and its transportation, machines and elements used for its benefit, and in the construction and maintenance of refineries and pipelines" are exempt from departmental or municipal taxes. In these circumstances, the taxpayer may be required to file a local tax return with assessment of no taxes.

Another incentive that exists for oil and gas activities is one under the industrial and commercial activities (ICA) tax regime.[33] The ICA regime does not assess tax for the exploitation of oil and gas if the amount received by the municipality as royalties and contributions is equal to or greater than the amount it would have received otherwise as a tax under the ICA.[34] In these circumstances, the taxpayer is not required to file an ICA return (but the case must be analyzed when the taxpayer obtains financial revenues).

Tax credit for donations

Donations made to nonprofit entities that have been qualified as part of the income tax special regime and to the non-taxpayers of Sections 22 and 23 of the Colombian Tax Code will grant a discount for income tax purposes of 25% of the value donated in the year or taxable period. In these cases, these donations may not be used as a deduction. This treatment will be regulated for its application.

This treatment is subject to regulation for its application.

Tax credit for investment in control and improvement of the environment

Legal entities that directly make investments in the control, conservation and improvement of the environment shall be entitled to a tax credit of 25% of the investments they have made in the relevant tax year from their income. The

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32 Section 147 of the Colombian Tax Code.

33 The triggering event is the exercise or undertaking, directly or indirectly, of commercial, industrial or service activities within the jurisdiction of a municipality or district, either permanently or occasionally, in a certain property, with or without a commercial establishment.

34 Section 39 of Law 14 of 1983.

investments that have been demanded by the environmental authorities are not acceptable for the benefit.

Research, technological development and innovation

Investments in research, technological development and innovation give arise to:

- A special deduction for donations and investments in research, technological development and innovation: taxpayers may deduct 100% of the investment made in research, technological development or innovation.
- Tax credit for investments made in research, technological development or innovation: taxpayers are entitled to a credit of 25% of the value invested in the taxable year or period. Investments can be made through researchers, groups or research centers, among others. The project qualification must comply with environmental impact criteria as a requirement for the credit.

These should be projects qualified by the National Tax Benefits Council (CNBT) in accordance with the criteria and conditions defined by National Council on Economic and Social Policy (*Consejo Nacional de Política Económica y Social*, CONPES).

The CNBT will define a maximum annual amount of deduction and a maximum annual amount when simultaneously requesting deductions and tax credits.

Income tax credit for VAT paid on heavy machinery for basic industries

The VAT paid on the importation of heavy machinery for use by basic industries may be used as a tax credit (discount) for income tax purposes. The mining industry, the sectors of hydrocarbons and transmission and generation of energy are considered a basic industry for these purposes.[35] The benefit is carried forward with no limitation in time.

Special deduction of VAT paid on the acquisition or importation of capital goods

VAT at the general rate for the acquisition or importation of capital goods may be taken as a deduction for the income tax in the period of acquisition or importation, provided that such benefit is not used concurrently with the tax credit for heavy machinery. It also applies to the assets acquired under the financial leasing, which envisages a purchase option at the end of a contract.

CERT (tax refund certificate)[36]

The investments in the hydrocarbons sector that will give rise to the granting of CERT will be exclusively those that aim at the discovery of new hydrocarbon reserves, the increase in proven reserves or the establishment of new recoverable reserves.

CERT value shall constitute neither a nontaxable income nor capital gains for the person who receives or acquires it and may be used for the payment of national taxes administered by DIAN (*Dirección de Impuestos y Aduanas Nacionales de Colombia*).

Temporary imports

"Temporary importation" is defined as the importation of certain goods that must be exported under the same conditions as they entered the national customs territory within a specific period of time — that is, without having undergone any modifications, except for the normal depreciation resulting from use.

Temporary imports can obtain some deferrals in payments of import duties (customs duty and VAT). However, the sale of goods will be restricted while they remain within the national customs territory.

35 *Section 258-2, Colombian Tax Code*

36 *This benefit was regulated by Decree 2253 of 207.*

The temporary imports can be of two subtypes: short-term and long-term. Temporary imports are classed as short-term when they are imported to meet specific needs. The maximum import term will be six months, extendable for up to three additional months and, in exceptional situations, for up to yet another three months with prior authorization from the DIAN customs authorities, for a total of one year.

VAT or customs duties are not meant to be paid on this type of temporary import. Once the short-term duration has expired, the importer must re-export or modify the import declaration to the long-term subtype (with a deferral of payment) or to an ordinary import.

Temporary imports are classed as long-term when they are imports of capital goods and any accessory or spare parts, as long as they constitute one single shipment. The maximum term for these imports is five years. Extensions are not expressly authorized but are possible if the request is filed with the customs authorities before the entry of the goods into the country. Import duties have to be paid in biannual installments every six months within the five years.

On 7 March 2016 the Colombian Government issued Decree 390 of 2016, by means of which the customs regulation was modified. However, some articles of the new regulation will come into force once they are regulated by the DIAN and the adjustments required by the information system of the DIAN comes into operation. Therefore, the regulation regarding temporary import modalities corresponds to that in force at the date of preparation of this document, that is, Decree 2685 of 1999, and it would be required to observe the new regulation once it is issued.

Authorized economic operators

By means of Decree 3568 of 27 September 2011 (amended by Decree 1894 of 2015), the DIAN incorporated the concept of an authorized economic operator (AEO). Exporters and importers in the oil and gas industry may request this authorization. The main benefits of the AEO are the following:

- Recognition as a secure and reliable operator
- Use of special and simplified procedures for inspection or recognition procedures
- Non-intrusive inspection
- Consolidated payment of import duties (customs duty and VAT), penalties, and interest
- VAT exclusion on imports of industrial machinery not produced in the country
- Use of special channels and mechanisms for conducting foreign trade operations
- Cash flow benefits on the return of credit balances of VAT

To be recognized as an AEO, the request must be presented to the DIAN, which will grant it subject to compliance with the conditions set forth in the regime.

Free trade agreements

Colombia has various free trade agreements (FTAs) in force allowing the importation of goods and raw materials, in most cases with a 0% customs duty rate. The most significant are those involving the following:

- Colombia and the United States
- Colombia and the European Union
- Colombia and Canada
- Colombia and Mexico
- Colombia and Chile
- Colombia and Guatemala, Honduras and El Salvador
- The Andean Community (Peru, Bolivia, Ecuador and Colombia)
- Colombia and the Economic Complementary Agreement (Mercosur)
- Argentina, Brazil, Uruguay, Paraguay, Colombia and the European Free Trade Association (EFTA) which includes Switzerland, Liechtenstein, Norway and Iceland

- The Pacific Alliance (Chile, Mexico, Peru and Colombia)
- Colombia and the Republic of Korea

Import duties

Goods imported on a permanent basis by companies in the oil and gas sector are generally subject to import duties (customs duties and VAT).

Special terms apply to imports and exports of oil and gasoline by pipeline.

Regarding customs duty tariffs, Colombia has different types of rates that, in general, range between 0%, 5%, 10% and 15%. The applicable customs duty tariff was partially amended, among others, by means of Decree 1625 of 14 August of 2015, which provides for a zero customs duty tariff rate for the importation of certain raw materials and capital goods not produced locally. This decree was modified by Decrees 1084, 1230, 1287 of 2016; Decrees 420 and 1343 of 2017; and Decree 272 of 2018 including or excluding goods under the mentioned benefit.

Export duties

No duties apply to goods on export from Colombia.

E. Withholding taxes

Colombia has a withholding tax (WHT) regime that is intended to secure the collection of taxes and make the system more efficient by providing for the advance collection of tax. The most important taxes subject to this procedure are income tax, VAT and ICA.

Self-withholding of income tax for exports of hydrocarbons

Exportation of hydrocarbons is subject to “self-income tax withholding” by the exporter, the withheld amount being paid to the authorities through the corresponding WHT return. The rate of the self-income tax withholding is 1.5% on the exportation amount. This income tax withholding is creditable against the year-end income tax due.

Note that the rate of 1.5% may vary if another regulatory decree regarding the self-withholding is established. The maximum withholding rate authorized by law cannot exceed 10%.

New self-withholding for income tax purposes (an additional self-withholding)

As of 1 January 2017, taxpayers have the status of self-withholding agents for purposes of income tax, provided they meet the following conditions:

- They are a national company, foreign company or PE.
- They are exempt from the payment of social security contributions and payroll taxes with respect to their workers who earn a wage less than 10 minimum monthly legal wage (SMMLV as defined in Spanish).

This self-withholding must be settled on each payment or credit entry to income tax taxpayers, and the rate may range from 0.4% to 1.6%, depending on a type of economic activity.

Those responsible for self-withholding must file and pay self-withholdings performed each month, within the deadlines set for the effect by the national Government.

The self-withholding will be applied regardless of the traditional tax withholding.

Payments made abroad

Generally, services rendered abroad generate foreign source income, and therefore no Colombian WHT applies. This provision does not apply to services rendered abroad that are, by legal provision, considered to be generators of national source income. For example, this service includes payments or credits to accounts related to consulting, technical services and technical assistance services, which are subject to WHT at the rate of 15% irrespective of whether they are rendered in the country or abroad.

Unless modified by a treaty,[37] the following table contains a list of the most relevant items subject to WHT, together with the relevant withholding rates on payments made to beneficiaries abroad. The list is not exhaustive.

Items	Income tax withholding	Deductibility (income tax)	VAT***
Payment for technical assistance services and consulting (rendered in Colombia or abroad)*	15%	15% limit does not apply	19%******
Payment for technical services or technical assistance (rendered in Colombia)***	15%	15% limit does not apply	19%
Overhead expenses for administrative services rendered abroad and charged to related entities	15%	15% limit does not apply	19%
Royalties for acquisition and exploitation of intangibles	15%	100%**	19%
Royalties in acquisition and exploitation of software	33% over a special taxable base (80% of the value of the contract)	100%	19%
Construction services *****	1%	15% limit not does	19%
Payments for services rendered in Colombia (other than those mentioned above); tax references on these cases will be analyzed on a case-by-case basis	15%	15% limit does not apply	19%
Payments for services rendered abroad as a general rule (other than those mentioned above)	0%	Limitation of 15% of net taxable income	19%
Payments to tax havens	34% for FY 2017 33% from FY 2018	100% (****)	19%

37 *Treaty to prevent double taxation with Spain is applicable as of 2009. Treaty with Chile is applicable as of 2010. Treaty with Switzerland is applicable as of 2012. Treaty with Canada is applicable as of 2013. Treaty with Mexico is applicable as of 2014. Treaties with South Korea and India are applicable as of 2015. Treaties with Czech Republic and Portugal are applicable as of 2016. Treaties with United States, France, Belgium, United Kingdom, Germany, Netherlands, Japan, United Arab Emirates and Italy are pending to enter into force.*

Notes:

* For these types of service, the supplier must be a nonresident in Colombia.[38]

** Payments are deductible if the transaction is structured as a service and pursuant to the arm's-length principle, supported by a transfer pricing study, regardless of whether it is subject to WHT, provided it complies with general tax deduction requirements. The 15% limitation applies if no WHT applies. In some cases, the deduction is granted if compliance with the registration of the service contracts is met (i.e., general licensing, technical services and technical assistance services).

*** Colombian residents receiving services in Colombia from nonresident providers must apply a reverse charge mechanism. In this case, a special withholding method is applied whereby the Colombian resident who requests the service must withhold the total VAT generated. If the VAT paid is creditable, the resident computes the self-accounted VAT amount from its bimonthly VAT return for the period when the payment was made.

**** A transfer pricing study is also required to allow the deduction of expenses incurred with a third-party resident in a tax haven jurisdiction.

***** Obligation to file a tax return by the nonresident.

****** May be subject to further regulation. Changes may be expected.

Interest on credit obtained abroad

Generally, payments or credits to accounts made by legal entities relating to interest are subject to WHT, at the rates of 15%, from 2017 onward (unless modified by a treaty[39]). Nevertheless, the following credits obtained abroad (among others) are not considered as national source income,[40] so they are not subject to WHT:

- Short-term credits originating from imports of goods and banks overseas
- Credits for foreign trade operations obtained through financial corporations and banks incorporated pursuant to the Colombian laws in effect

Note that foreign indebtedness is not allowed for branches belonging to the special exchange regime.

F. Financing considerations

Effective from 1 January 2013, thin capitalization rules are applicable in which any interest paid on loans (with third parties or related parties) that on average exceeds a 3:1 debt-to-equity ratio is not deductible. For this purpose, the equity that should be taken into account is the taxpayer's previous year's net equity as well as any debt that accrued interest.

G. Transactions

Farm-in and farmout

Farm-in arrangements are commonly used in Colombia in the oil and gas industry. A farm-in typically involves the transfer of part of an oil and gas interest in consideration of an agreement by the transferee (the farmee) to make certain expenditures that would otherwise have to be undertaken by the owner (the farmer). For tax purposes, the local selling price cannot be lower

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38 Paragraph 2, Section 408 of the Tax Code.

39 Treaty to prevent double taxation with Spain is applicable as of 2009. Treaty with Chile is applicable as of 2010. Treaty with Switzerland is applicable as of 2012. Treaty with Canada is applicable as of 2013. Treaty with Mexico is applicable as of 2014. Treaties with South Korea and India are applicable as of 2015. Treaties with Czech Republic and Portugal are applicable as of 2016. Treaties with United States, France, Belgium, Germany, Netherlands, Japan, United Arab Emirates and Italy are pending its entry into force.

40 Section 25 of the Tax Code.

than 75% of the fair market value of the rights. Transactions with foreign-related parties must comply with transfer pricing provisions.

Selling shares in a company

A share disposal is generally subject to the CGT or income tax regime. The taxable capital gain or taxable net income is equal to the positive difference between the sale price of the asset and its tax basis (fiscal cost). Sales to foreign related parties must comply with transfer pricing provisions. Unrelated sales or sales between Colombia-resident related parties cannot be performed for less than 75% of the fair market value of the assets sold.

The tax reform includes a presumption that the market value of the shares not listed on the stock exchange market cannot be lower than the equity value plus 15%. The same treatment will apply to the sale of rights on investment vehicles, such as trusts and collective investment funds that hold shares or interests.

Nonresidents that dispose of shares held directly in a Colombian company are subject to tax in Colombia. Indirect sales may be levied in Colombia. Assets owned in Colombia for two years or more are liable to tax as capital gains on sales. Assets owned for less than two years are liable to income tax upon the sale under the ordinary regime.

H. Indirect taxes

VAT and GST

Colombian VAT is triggered by the following transactions[41]:

- Sales of movable and immovable tangible goods that have not been expressly excluded
- Sale or transfer of rights in intangible assets solely associated with industrial property
- Render of services in Colombia or abroad, unless expressly excluded
- The import of movable tangible goods that have not been expressly excluded

It is important to note that the services provided from abroad are taxed with VAT, when the recipient and/or beneficiary is in the national territory. There are specific rules to determine when the beneficiary is in the national territory.

Liquefied natural gas, natural gas in the gaseous state, electric energy, and crude oil received by the ANH for the payment of royalties are excluded from VAT under Section 424 of the Colombian Tax Code, modified by Law 1819 of 2016. Other VAT-excluded products include goods that are basic necessities and services, such as health, transportation, education and public services. Excluded supplies are not subject to VAT, and the VAT paid to suppliers of goods and services cannot therefore be credited in the VAT return and should be accounted for as an increase in the cost or expense of the goods or services. If a company exclusively makes excluded supplies, the VAT paid on its supplies cannot be recovered through the VAT credit system; thus, VAT paid becomes an additional cost or expense for the company.

In Colombia, the term "exempt supplies" is used for supplies of goods and services that are liable to VAT but have a zero rate (taxed at 0%). Exported goods and services are included within this category. In this case, the VAT paid to suppliers of goods and services may be recovered through the VAT credit system. If, as a result of making exempt supplies, the taxpayer has paid more VAT to its suppliers than it has charged, the credit balance may be requested as a refund from the tax authorities (subject to compliance with certain requirements and conditions).

To improve the tax collection system, the Colombian Government has introduced a VAT withholding mechanism and designated certain entities as VAT withholding agents (including government entities, large taxpayers and taxpayers of the common system to contract with persons or entities without

41 *Section 420 of the Tax Code.*

residence in Colombia). These agents are responsible for withholding 15% of the VAT on any payment or accounting accrual related to taxable goods or services. In the case of transactions with nonresidents (both entities and individuals), the withholding rate is 100% of the VAT.

From 2017, the general VAT rate is 19%. This rate applies to all goods and services, unless specific provision allows a reduced rate.

The VAT rate on imported goods for the oil and gas sector is generally 19%. However, the Colombian Tax Code offers the following VAT benefits for imported goods:

- Subsection 428(e) of the Colombian Tax Code establishes a VAT exclusion for the temporary importation of heavy machinery for use by basic industries (the hydrocarbon sector is regarded as a basic industry) to the extent that those goods are not produced in the country (subject to the opinion given by the Ministry of Commerce, Industry and Tourism). Any request for VAT exclusion must be submitted at the time of the importation.
- Subsection 428(f) of the Colombian Tax Code establishes a VAT exclusion for importation of machinery or equipment for treatment of residues when this machinery is not produced in Colombia.
- Subsection 428(g) of the Colombian Tax Code establishes a VAT exclusion for ordinary imports of industrial machinery made by so-called "high export users" to the extent that the machinery is used to transform raw materials and does not have local production (according to the opinion given by the Ministry of Commerce, Industry and Tourism). Any such request for exclusion should be submitted at the time of the importation.
- VAT will be accrued on mergers and spin-offs if the tax event does not qualify as tax neutral.

Sale tax on the sale of oil derivatives

Producers, importers, its economic associates of each other, wholesale distributors and/or industrial traders are taxpayers of VAT on the sale of oil derivatives.

VAT invoiced on the acquisition of oil derivatives may be creditable as input VAT by the acquirer, when (1) the acquirer is responsible for the sales tax, (2) the goods acquired are computable as cost or expense of the company and (3) the oil derivatives are destined to be used in taxable or tax-exempt transactions.

Refund of VAT on offshore investments

Regardless of whether the relevant taxpayer has income or not, it will have the right to:

- File a VAT return from the moment in which exploratory activities start
- Treat as deductible the VAT paid on the acquisition or importation of goods or services used in the exploration and development stages to conform the cost of their fixed assets or amortizable investments
- Request that the VAT receivable balance be refunded in the year following its generation

The VAT refund cannot be used concurrently with the VAT discount on heavy machinery, nor can these values be used as a cost, deduction or credit on income tax.

National tax on gasoline and diesel oil

A taxable event, according to the National Tax on Gasoline and ACPM (the term for diesel in Colombia), is the sale, withdrawal or import for own consumption or import for the sale of gasoline and ACPM. The tax is levied on the sales made by the producers on the date of issue of the invoice; for withdrawals for the producers' consumption it is levied on the date of withdrawal, and for imports, it is levied on the date on which the gasoline or the ACPM is nationalized.

Taxpayers are those who purchase gasoline or ACPM from a producer or importer, when the producer or importer have made withdrawals for their own consumption.

The national tax on gasoline is set at a rate of COP490 (approx. US$0.16) per gallon, that of extra gas at a rate of COP930 (approx. US$0.31) per gallon; and the national tax on ACPM is set at a rate of COP469 (approx. US$0.16) per gallon. The national tax on other products defined as gasoline and ACPM in accordance with this law, other than extra gasoline, is set at a rate of COP490 (approx. US$0.16).

Excise duties

Excise duties do not apply to upstream oil and gas.

Registration tax

A registration tax is levied on documents or contracts that must be registered with the Chamber of Commerce or with the public instrument office.

As explained below, a branch is the most common and convenient legal structure for oil and gas companies. Companies that operate using other legal structures must register with the authorities (e.g., a notary) if they decide to increase their patrimony by funding, and they must pay registration taxes, whereas branches do not have these obligations. Instead, a branch maintains a special account called a "supplementary investment to the assigned capital," in which it registers capital differences after funding, as if the account were a current account held with the head office.

I. Other

Wealth tax

The tax was introduced by Law 1739 of 2014. The tax was assessed on 1 January 2015 by companies that met the requirements at that time. These companies have to pay the wealth tax during fiscal years 2015, 2016 and 2017. The taxable basis is the adjusted[42] gross equity minus debts as of each year (on 1 January 2015, 2016 and 2017).

Tax on financial transactions

The tax on financial transactions (TFT) applies to any financial debit transactions involving a withdrawal of deposited resources in checking or savings bank accounts opened in financial entities. Exemptions apply, but none apply specifically to the oil and gas sector.

The current tax rate is 0.4%, applied to the total amount of the transaction. In general, the withholding agents of TFT are financial entities and the Colombian Central Bank.

Fifty percent of the amount paid will be a deductible allowance.

Mergers and spin-offs

Acquisition mergers and spin-offs

The acquisition merger and spin-off rules apply to domestic companies that are not deemed to be related parties under the definitions contained in the transfer pricing rules. The merger and spin-off rules are neutral for income tax and VAT purposes, as no disposal of property is deemed to occur. No disposal of shares is deemed to take place for the shareholders of the participating companies, provided that certain conditions are met, such as (i) owners of 75% of the shares of the existing companies participate in the resulting company and (ii) shareholders receive a participation equivalent to no less than 90% of the resulting capital as measured by application of the valuation methods and the share exchange method used. A two-year minimum holding period is required; otherwise, a special fine may be imposed, with certain exceptions. Other restrictions apply.

42 *The reform protects the taxable basis from potential fluctuations in the equity (increase/decrease). The reform includes a limitation that assumes a formula with reference to the taxable basis as of 1 January 2015, bearing in mind the adjusted inflation with a 25% variation.*

When foreign and domestic companies participate in a merger or spin-off, the same consequences apply as are set out in the preceding paragraph, to the extent that the absorbing company (in mergers) or resulting company (in spin-offs) is a domestic entity.

Reorganization mergers and spin-offs

The reorganization merger and spin-off rules apply to domestic companies that are deemed to be related parties under the definitions contained in the transfer pricing rules. The merger or spin-off is tax-free for income tax and VAT purposes. The requirements that apply to acquisition mergers or spin-offs also apply to reorganization mergers and spin-offs, except that certain thresholds increase. For example, (i) ownership of interest in shares is increased to 85%, and (ii) shareholders must receive a participation equivalent of no less than 99% of the resulting capital as measured by the application of the valuation methods and share exchange method used. Other restrictions apply.

Mergers and spin-offs of foreign entities owning Colombian property

Foreign mergers or spin-offs of companies holding Colombian interests are taxed in Colombia when through these mechanisms direct ownership of Colombian companies or assets is transferred, provided the value of the assets exceeds 20% of the total assets of the group to which the participating companies in the merger or spin-off belong, according to the consolidated balance sheet of the ultimate parent company.

Foreign exchange regime

As a general rule, all business entities that undertake business operations in Colombia are subject to Colombia's exchange control regime. Colombian incorporated legal entities qualify as "residents" for exchange control purposes and are subject to the "general foreign exchange control regime." Colombian registered branches of foreign legal entities also qualify as residents and are subject to this same regime; however, if the purpose of the business of a branch of a foreign entity is to enter into hydrocarbon exploration and exploitation activities, or to provide exclusive services to the hydrocarbon sector in accordance with Decree 2058 of 1991 (as a "qualified branch in which case they will require an exclusivity certificate issued by the Ministry of Mining and Energy"), the branch will belong to the special foreign exchange control regime.

The most notable differences between the two regimes are related to the way that the entities may handle their foreign currency resources and deal with "exchange operations" as set out next.

General regime	Special regime
Scope	
Applies to all Colombian residents (persons, public entities and incorporated legal vehicles, including companies undertaking exploration and exploitation of oil and gas and non-qualifying branches of foreign legal entities).	Applies to branches of foreign companies operating in the exploration and exploitation of oil, gas, coal, ferronickel or uranium, as well as to branches with the exclusive provision of services to the hydrocarbon sector (qualifying branches). To apply for the special regime, branches devoted to providing exclusive services will require a certification issued by the Ministry of Mining and Energy that has to be renewed every year.

General regime	Special regime
Regime election	
Applies by default to the residents referenced above.	Branches of foreign companies that comply with the abovementioned requirements and that do not wish to follow the special provisions stipulated in the special foreign exchange control regime must report their decision to the Central Bank, and they will resign to the special regime for a minimum period of 10 years as from the date of submitting the respective communication. By resigning, all foreign exchange operations carried out shall be subject to the common regulations provided for in the general foreign exchange control regime (Section 50 of Resolution 8 of 2000), as explained below.

General regime	Special regime
Characteristics	
It is mandatory to repatriate and channel through the exchange market all foreign currency received from sales abroad (i.e., it is mandatory to bring it into Colombia and convert it into local currency through an intermediary of the foreign exchange market). However, Colombian regulations also allow for residents to wire the money under the general regime through a foreign currency-based bank account registered at the Central Bank as a compensation account.	It is not mandatory to repatriate foreign currency received from sales (i.e., to bring it into Colombia and convert it into local currency). Branches are only required to repatriate into the Colombian foreign exchange market the foreign currency needed to cover expenses in Colombian currency.

General regime	Special regime
Characteristics	
Acquisition of foreign currency from the Colombian regulated foreign currency market is permitted. An entity covered by this regime should undertaken all its exchange control mandatory operations through Colombian-qualified foreign exchange intermediaries or their compensation accounts.	In general, branches belonging to the special exchange regime do not have access to the regulated foreign exchange market. As a result, these branches are not allowed to purchase foreign currency from the Colombian foreign currency market. Therefore, the execution of determined exchange operations is limited, and most business must be attended directly by the main office. By way of exception, qualifying branches may remit abroad through the exchange market (with the certification of the entity's statutory auditor external auditor) any proceeds received in Colombian pesos derived from internal sales of oil, natural gas or services related to the hydrocarbon sector, as well as the foreign capital amount to be reimbursed to the main office in the event of the liquidation of the branch in Colombia.
Residents that belong to the general foreign exchange regime are obliged to carry out the payment of internal operations between them in Colombian legal currency (COP). Exceptionally, they are allowed to carry out these payments in foreign currency through duly registered compensation accounts. Both the payer and the receiver should wire through these accounts. Furthermore, there are some specific operations that are permitted to be undertaken in foreign currency between residents (duty free payments, international transportation tickets and freights, personal expenses on international credit cards, insurance premium and reinsurance). It is important to consider that companies belonging to the hydrocarbons sector but that do not qualify for the special regime (as they are not branches or branches that resigned to the regime) may make payment in a foreign currency between them and special regime branches.	All expenses incurred by a branch in Colombia should be paid in Colombian legal currency (COP), except for payments between companies in the same business sector, which may be performed in foreign currency. These are the national entities with foreign investment (companies and branches of foreign companies) that carry out activities of exploration and exploitation of oil, natural gas, coal, ferronickel or uranium, and national companies with foreign investment that provide exclusive services to the hydrocarbon sector in accordance with Decree 2058 of 1991 (as a "qualified branch in which case they will require an exclusivity certificate issued by the Ministry of Mining and Energy").

General regime	Special regime
Characteristics	
Import and export of goods, international investments, foreign indebtedness, financial derivatives and guarantees are operations that residents must mandatorily wire through the foreign exchange market, either through an intermediary of that market or through compensation accounts. All other operations may be voluntarily channeled through the foreign exchange market.	Due to the restriction to acquire foreign currency, all imports of goods must be paid in full by the main office or directly by the branch through their free-market account opened above. The import of goods by these types of branches must be filed for customs purposes as nonreimbursable imports. Payment for services (which is a free-market operation not mandatory to be channeled through the foreign exchange market) must be made abroad by the main office on behalf of the branch or through a free-market account of the branch. These payments are considered to be contributions as supplementary investment to the assigned capital when made abroad by the main office. Payments made by the main office must be managed as supplementary investments to the assigned capital.
Colombian-incorporated legal entities may receive investments in cash or in kind from foreign shareholders (whereas non-qualifying branches may receive only cash contributions as supplementary investment to the assigned capital).	For example, a branch that has assigned capital and supplementary investment to the assigned capital (ISCA). The receipt by a branch of an investment in cash or in kind is accounted for either as assigned capital or more commonly as ISCA. The ISCA is a special equity account that, even though it forms an integral part of the equity accounts of the branch, is a separate account from the assigned capital account. This allows the flow of investment funds into the branch's equity account without entailing a change to the assigned capital account, thus allowing the branch to increase or reduce the ISCA balance without requiring the formality of a corporate resolution, or prior authorization by Colombian supervisory entities (e.g., Superintendency of Corporations). Therefore, the ISCA can be managed, in effect, as a "current account" of the branch with its main office. The branches pertaining to the special exchange regime may receive contributions in cash or in kind as ISCA.

<table>
<tr><th>General regime</th><th>Special regime</th></tr>
<tr><th colspan="2">Foreign currency movements</th></tr>
<tr><td>These entities may carry out all operations that are typical of the foreign exchange market. Some of the exchange control operations as mentioned above are:
Foreign investments in Colombia and related yields
Colombian capital investments abroad and related yields
Financial investments in securities issued abroad, investments in assets located abroad and related yields, unless the investment is made with foreign currency from transactions that are not required to be wired through the exchange market
Endorsements and warranty bonds in foreign currency
Financial derivatives transactions
Foreign indebtedness</td><td>These entities may:
Receive foreign investments into their assigned capital or ISCA
Be allowed to remit abroad only the proceeds of the branch's final liquidation and the proceeds received in Colombian pesos for internal sales of oil, natural gas or services
Considering that the main office receives the proceeds abroad, and carries out directly most of the payments on behalf of the branch, it may not:
Carry out operations of the exchange market
Remit profits
Carry out foreign indebtedness operations
Purchase foreign currency for the payment of obligations
Pay for imports of goods</td></tr>
</table>

<table>
<tr><th>General regime</th><th>Special regime</th></tr>
<tr><th colspan="2">Registration of foreign investment</th></tr>
<tr><td>In general terms, registration of a foreign investment is an automatic process at the time of channeling funds through the foreign exchange market, via the filing of Foreign Exchange Declaration for International Investments.

Some specific investments, such as contributions in kind, intangibles and tangibles, participation in contracts that do not imply participation in the capital and the capitalization of sums "with right of remittance," such as payable interest or dividends, are registered using Form 11.

Substitution of foreign direct investments derived from corporate restructuring operations should be registered using Form 11A.

The cancelation of the registry of the foreign investment should be made using Form 12.

For the special registries (Forms 11 and 11A) as well as the cancellation (Form 12), the filing of the required form has a deadline of six months as from the time of the operation.</td><td>Registration of a foreign investment is automatic at the time of channeling the funds through the foreign exchange market, via presentation of Foreign Exchange Declaration for International Investments.

Registration of ISCA has to be completed and updated by 30 June of the year following the investment, using Form 13.</td></tr>
</table>

General regime	Special regime
Annual foreign investment update	
Form 15, "Equity reconciliation – companies and branches of the general regime," is used for providing a foreign investment update. This annual update is not mandatory to entities subject to surveillance, control or inspection by the Superintendency of Corporations, when such entities are obliged to submit their annual financial statements to this authority. It is not mandatory as well for companies or branches in process of liquidation and for those who do not have any changes in their capital distribution during the year. An entity submitting an annual update must do so by 30 July if its identification number ends in an even number, and by 15 August if it ends in an odd number.	Form 13 is used for providing a foreign investment update. The deadline for submitting the form is six months from the financial closing on 31 December every year.

General regime	Special regime
Foreign trade operations	
Payment of imports must be channeled through the Colombian foreign exchange market. The proceeds of exports must be brought into the Colombian foreign exchange market.	Imports coming from their home office or from third parties must not be paid in foreign currency; therefore, all goods entering the country should come in as a contribution from their main office. Imports therefore qualify as nonreimbursable imports, so there is no access to foreign currency to pay for them. Exports are carried out by the branch but are paid directly to the main office abroad or to a free-market account of the branch outside Colombia.

General regime	Special regime
Foreign indebtedness	
Entities may enter into passive or active foreign debt transactions. Also, active indebtedness can be undertaken with any nonresident, and passive indebtedness with any legal entity abroad (persons only for some specific purposes). Payment of foreign indebtedness operations (passive or active), together with its financial costs, must be wired through the Colombian foreign exchange market.	These entities may not enter into passive or active foreign indebtedness operations for any concept — i.e., all foreign indebtedness (including any international leasing) must be undertaken by the main office, as opposed to the branch.

General regime	Special regime
Foreign currency accounts	
Entities may have checking or savings accounts in foreign currency with foreign financial entities, and they are not required to report or register them with the Central Bank. These accounts may only be used for handling operations not required to be channeled through Colombia's foreign exchange market (Section 55 of Resolution 8 of 2000).	Entities may have current or savings accounts in foreign currency with foreign financial entities, and they are not required to report or register them with the Central Bank (Section 55 of Resolution 8 of 2000).
Entities may have foreign currency compensation accounts registered with the Central Bank for handling operations that are mandatory to be wired through the Colombian foreign exchange market (Section 56 of Resolution 8 of 2000).	Entities cannot have compensation accounts due to the fact that accessing the Colombian foreign exchange market is proscribed.

J. Other tax compliance

The Colombian Tax Code states that taxpayers are required to provide certain specified information to the tax authorities. Based on that, the tax authorities (at national and municipal levels) request every year from some taxpayers detailed information (known colloquially as "MM") to support the figures reported in their income tax returns, using a specific format provided by the tax authorities.

Individuals or corporations acting as "operator" in E&P oil and gas contracts are obliged to provide MM to the tax authorities, comprising a full set of information from their own operations and those of any partners engaged in the same E&P contract.

K. Anti-abuse rules

An operation or series of operations constitutes tax abuse when it meets the following requirements:

- Involves the use or implementation of one or more artificial acts or legal transactions without apparent economic and/or commercial purpose
- In order to obtain a tax benefit, regardless of any additional subjective intent

Tax authorities are empowered to take the following actions against tax abuse:

1. To characterize (determine the "true" nature) the whole operation that constitutes abuse and, consequently, to ignore its effects
2. Issue administrative acts in which it proposes and settles taxes, interests and penalties

L. Green tax/carbon national tax

The tax is levied of sale, withdrawal, import for own consumption or importation for the sale of fossil fuels (including all oil derivatives and all kinds of fossil gas) that are used with energy purposes, provided that they are used for combustion.

The rate is determined depending on the emission factor of carbon dioxide (CO_2) for each given fuel, expressed in unit volume (kilogram of CO_2) per unit of energy (terajoules) according to the volume or weight of the fuel:

Fossil fuel	Unit of measure	Rate/unity
Natural gas	Cubic meter	COP29 (approx. US$0.01)
Oil liquefied gas	Gallon	COP95 (approx. US$0.03)
Gasoline	Gallon	COP135 (approx. US$0.16)
Kerosene and jet fuel	Gallon	COP148 (approx. US$0.05)
Diesel	Gallon	COP152 (approx. US$0.05)
Fuel oil	Gallon	COP177 (approx. US$0.06)

Côte d'Ivoire

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ■ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime applicable to the oil and gas industry in Côte d'Ivoire is governed by the General Tax Code, the Petroleum Code and any production sharing contracts (PSCs) or contract of service concluded between the Ivorian Government and the contractor (hereafter referred to as the holder). The most recent PSCs are those where the tax is paid on behalf of the holder (a "tax-paid PSC"), rather than those when the tax is paid by the holder (a "taxpaying PSC").

The principal taxes and duties applicable to the oil and gas industry are:

- Corporate Income tax (CIT) — 25%
- Surface rent tax — no specific legislated rate and depends on the terms of the PSC
- Bonuses — amount depends on the terms of the PSC
- Royalties on production — rate depends on the terms of the PSC[1]
- Capital allowances – D, E[2]
- Incentives – L, RD[3]

B. Fiscal regime

There are two groups of petroleum companies in Côte d'Ivoire. The first consists of exploration and production (E&P) companies specializing in the exploration and the production of oil and gas (hereafter referred to as E&P companies or holder). The second group consists of petroleum services providers that specialize in the supply of petroleum services and are subcontracted by the holder (see Section I below).

The fiscal regime that applies to E&P companies differs from the one applying to petroleum service providers.

Corporate tax

E&P companies in Côte d'Ivoire are subject in principle to CIT on their nonexempt income at the rate of 25%. Some holders are exempt from corporate tax, and such exemptions are specified in their PSCs.

CIT could be paid in cash or in kind (in which case, the CIT is considered as already included in the profit oil of the state). In the latter case, the national oil company (PETROCI) must deliver a tax payment certificate to the holder.

1 *Royalties are applicable to the holder of the PSC.*
2 *D: accelerated depreciation; E: immediate write-off of exploration costs.*
3 *L: ability to carryforward losses; RD: R&D incentive.*

The CIT is calculated on the net taxable income of the holder. The net profit is the difference between the value of the opening and closing balances of the net assets in the relevant year of assessment, less extra contributions, plus any amounts taken by associated companies during the said period. Exploration and development costs are taken into account in determining the company's income.

The profit is calculated after deduction of all charges that meet the following conditions:

- Are incurred in the direct interest of the company or are related to the normal course of the company's business
- Correspond to actual charges and are supported by sufficient evidence
- Are reflected by a decrease in the net assets of the company
- Are included in the charges of the fiscal year during which they were incurred

However, the PSCs signed over the last few years are tax-paid PSCs. The holders are receiving their profit oil share net of taxes (including CIT). The Ivorian Government is supposed to settle the holder's taxes on its behalf out of its own share of profit oil. The holder will still receive tax payment certificates.

Characteristics of the PSC

A PSC is concluded between the holder and the Ivorian Government and is signed by both the Minister of Petroleum and the Minister of Finance. It is one of the most common contracts used by the Government. The PSC is in principle published in the *Official Journal,* but this has never been done in practice.

As in most PSCs, an E&P company finances all exploration and development costs and bears all costs and risks of this operation in the event that no oil and gas is found.

The production is allocated as follows: one part of the production will be used to recover the exploration and development costs incurred by the company ("cost oil"); the remaining part ("profit oil") is shared between the Government and the holder. Production sharing is calculated with reference to the production volume, and cash can be payable in lieu of oil under certain circumstances.

Government share of profit oil

The government share of profit oil is determined in each PSC or the service contract and is based on the outcome of the negotiation between the Government and the E&P company; there is no sharing ratio required by law. It should be equal to a percentage of the production after the deduction of cost oil.

As an illustrative example of a PSC, the Government share of profit oil could be as follows:

Daily oil production (barrels)	Government share of profit oil	Holder share of profit oil
From 0 to 100,000	45%	55%
From 100,001 to 200,000	47%	53%
From 200,001 to 300,000	55%	45%
Over 300,000	60%	40%

Cost oil

Recoverable expenditures

Exploration and development costs are recoverable by the holder in the form of cost oil.

Non-recoverable expenditures

The following expenditures are not recoverable:

- Expenditures relating to the period before the effective date of the contract
- Expenses relating to the operations carried out beyond the point of delivery, such as marketing and transportation charges
- Bonuses
- Financing costs (under certain conditions).

Determination of cost oil

Cost oil is all expenses borne by the holder in the performance of the PSC and determined in accordance with relevant accounting processes. Cost oil and profit oil are determined for each contract; there is no standard rate, and each holder agrees its share of cost oil with the Government. Cost oil recovery is usually capped between 70% and 80% of the total production.

Uplift

Before 2018 Finance law, the companies to benefit from this exemption were determined by joint order of the Minister in charge of the Budget and the Minister in charge of oil and gas.

However, the implementation of this provision could be detrimental to new oil companies, as they may not be on the list for the period following their establishment.

This is why the condition of the list has been removed.

Since 2018 Finance law (article 7), oil companies and their subcontractors benefit directly from the annual exemption by way of certification.

Some PSCs allow the holder to claim an uplift (i.e., additional cost oil) on expenditures incurred for deep- and ultra-deep water operations. The uplift rate is negotiated for each PSC.

VAT

According to article 2 of 2018 Finance Law, the catering on offshore oil platforms is covered by this exemption. Also, the same article adds that repair and maintenance services of the company vehicles allocated to the executives of the oil companies, the security of their homes as well as the various service provided to the consultants to whom the oil companies have recourse, are not covered by the VAT exemption.

The holder is exempt from value-added tax (VAT) and tax on financial operations in Côte d'Ivoire for the purchase of goods and services related to its petroleum activities. The availability of the exemption is subject to compliance with VAT exemption procedures established by the Ivorian tax authorities.

The holder is liable for VAT at the rate of 18% on the purchase of certain goods and services not connected with petroleum operations.

It is not necessary to register for VAT separately. As soon as a company is registered in Côte d'Ivoire (as a branch or company), a taxpayer number is allocated to the holder, and it covers all taxes, including VAT.

The VAT exemption procedure has been simplified by the 2016 Finance Law by making it an annual process instead of an invoice by invoice process.

Bonuses

Each petroleum or gas agreement specifies the bonus payable to the Government. The amount is negotiated with the Government when the agreement is signed, and therefore, the amount of any bonus payable generally differs in each contract. There are two kinds of bonus:

- Signature bonus, payable 30 days after the signing of a gas or petroleum agreement
- Production bonus, payable 30 days after the last day of the test production

Bonuses vary according to the total cumulated oil production. Based on an example, the bonus might be due as follows:

- US$3m when the net cumulated oil production reaches 50m barrels
- US$6m when the net cumulated oil production reaches 75m barrels
- US$8m when the net cumulated oil production reaches 100m barrels
- US$12m when the net cumulated oil production reaches 200m barrels

Annual surface rent

The payment of an annual surface rent or other surface rent can be due according to the PSC or service contract. In this case, the payment must be made in the first 10 days of the year. In the case of annual surface rent tax, the amount due will be paid for the entire year, based on the area of the permit.

Unconventional oil and gas

No special terms apply for unconventional oil or gas.

C. Capital allowances

Holders are subject to local generally accepted accounting principles (GAAP) known as SYSCOHADA.

In practice, each holder, whether resident or not, must adopt two accounting systems: one for general activities and the other for petroleum costs. In the second system, the relevant company must have a special account each year where the production level, results and balance sheet of the company are set out.

Immediate write-off for exploration costs

The exploration expenses incurred by the holder in the territory of Côte d'Ivoire — including the cost of geological and geophysical surveys, and the cost of exploration wells — will be regarded as expenses fully deductible as of the year during which they are incurred. Alternatively, these costs may be capitalized under certain conditions and depreciated once production starts.

D. Incentives

Tax exemptions

Holders of PSCs are exempt from certain taxes, duties and fees as soon as they sign the PSC and up to the end of their activities in Côte d'Ivoire or at the end of the PSC. The main taxes exempted are:

- Tax on banking operations
- VAT
- Taxes and duties applicable to petroleum products supplied to permanent facilities and drilling facilities.

During this period, equipment intended directly and exclusively for petroleum operations is exempt from any duties and taxes on its importation into Côte d'Ivoire by the holder or by companies working on its behalf.

Ability to carry forward losses

In a taxpaying PSC, the unverified amount of the loss is deductible from the taxable profits until the fifth fiscal year following the period in which the loss arose, unless the PSC or service contract authorizes the holder to carry these losses forward beyond the five-year period.

Losses relating to asset depreciation can be carried forward indefinitely.

E. Withholding taxes

Dividends

Dividends distributed by the holder are exempt from taxation.

Interest

Loan interest related to petroleum activities paid by the holder to its affiliates is not subject to any withholding tax (WHT).

Technical services

Nonresident service providers are subject to taxation on the payment they receive from a holder based in Côte d'Ivoire at a common rate of 20%. In the presence of a double tax treaty, services having the characteristics of royalties are subject to 10% tax.

However, some PSCs can exempt the holder and its service providers or suppliers from this tax.

Branch remittance tax

Branch remittance tax applies in general, but not to PSC holders.

F. Thin capitalization limits

There are no thin capitalization tax rules.

G. Transactions

Asset disposals

The income that results from asset disposals is included in the corporate income of the holder and is subject to CIT and registration fees.

Capital gains

In principle, capital gains are taxed at the corporate income tax rate of 25% (capital gains arising from transfer of assets, or from a PSC participating interest between affiliated companies, could be exempt from CIT under certain conditions).

H. Indirect taxes

Import duties

All goods and materials entering Côte d'Ivoire from overseas are subject to customs import duties.

However, personal and domestic goods of nonresident workers of E&P companies are exempt from any customs duties. Also, all materials required to carry out petroleum or gas operations are exempt.

VAT

See Section B above.

Export duties

Holders that export petroleum products are not subject to export duties.

Stamp duties

Stamp duties are due on transactions made by a holder. These stamp duties are the same for all companies.

Registration tax

Upon company registration, holders become taxable entities and must register with the tax authorities in order to obtain a tax identification number.

The registration tax for the creation of a subsidiary is:

- Up to US$10m share capital — 0.3%
- More than US$10m share capital — 0.1%

I. Petroleum services provider tax regime

Petroleum services providers are eligible to the Simplified Tax Regime if all of the following conditions are met:

- The provider is a foreign entity.
- The provider signed a service contract with an E&P company or a direct contractor of an E&P company.
- The provider uses expensive equipment and machinery, i.e., the drilling rig.
- The provider is registered with the Trade Register of Côte d'Ivoire as an agency or branch.
- The provider files a request with the Head of Tax Office within three months after the start of operations in Côte d'Ivoire.

The taxpayer must opt to be taxed under this regime if it wishes to operate under the Simplified Tax Regime; this election is definitive and is subject to the approval of the Head of Tax Office.

The Simplified Tax Regime (STR) covers corporate income tax, dividend withholding tax, tax on insurance premiums and payroll taxes (as described in the table below). A single STR rate is applied to turnover realized by the providers in Côte d'Ivoire.

Ivorian Tax administration has recently implemented the online portal "e-impôts" through which all companies should mandatory filed and paid relevant tax returns.

Taxes	Taxable basis	Rate	Effective rate (on gross turnover)
Corporate income tax	10% of turnover	25%	2.5%
Withholding tax on dividends	50% of profit (i.e., 5% of turnover)	15%	0.75%
Payroll taxes			
‣ For expatriate employees	8% of turnover	12%	0.96%
‣ For local employees	2% of turnover	2.8%	0.056%
Tax on salaries (due by employees)			
‣ Salary tax	8% of turnover	1.5%	0.12%
‣ National contribution tax	10% of turnover	5%	0.5%
‣ General income tax	8% of turnover	10%	0.8%
Tax on insurance premium	10% of turnover	0.1%	0.1%
Overall tax rate			5.786%

Providers that have elected to use the STR do not need to keep local books under local GAAP.

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

The fiscal system applied in Croatia to upstream operations is based on production sharing contracts (PSCs). The fiscal terms are defined both in the PSCs and in applicable legislation. Croatia has a model PSC for both onshore and offshore blocks, prepared in time for the first international bidding round launched in 2014. Some provisions addressing the specifics of petroleum operations are still evolving.

A. At a glance

- Income tax rate — 12%/18%
- Signature bonus — biddable
- Production bonus — applies
- Surface rental fees — apply
- Administration fee — applies
- Royalties — 10%
- Cost recovery — applies
- Profit production — linked to the so-called "R-factor"
- Customs duties – apply

Note that at the end of 2017, the Croatian Government introduced a new Act on Exploration and Production of Hydrocarbons into the Croatian Parliament, where it is currently subject to debate. Since the European Union has launched two EU Pilot dialogues for noncompliance with EU directives, the new Act is expected to be adopted during 2018. Consequently, the currently applicable Regulation on Fees for Exploration and Production of Hydrocarbons that was issued by the Croatian Government on the basis of the Act on Exploration and Production of Hydrocarbons and which is still in force, regulating signature bonus, production bonus, surface rental fees, administration fee, royalties and profit production, may also be amended.

B. Fiscal regime

Corporate income tax regime

Resident companies are subject to tax on their worldwide income. A company is deemed resident in Croatia if its legal seat or its place of management and supervision is located there. Branches of foreign companies are subject to tax on their profits derived only from Croatia.

The rate of corporate income tax depends on realized revenue in a fiscal period, whereby for revenues up to HRK3 million, a tax rate of 12% applies, and for revenues equal to or exceeding HRK3 million, a tax rate of 18% applies.

Generally, lower tax rates or other tax benefits may be available based on size and location of investment. There is no branch remittance tax in Croatia.

Some provisions addressing specifics of petroleum operations are yet to be introduced to the general tax regime (for example, depreciation rates for exploration and development costs, and the treatment of unsuccessful exploration). Until then, companies should apply the general income tax rules.

Signature bonus

A signature bonus is biddable. The minimum bonus is HRK1.4 million. The signature bonus is tax-deductible, but not cost-recoverable.

Production bonus

A production bonus is linked to accumulated production and distinguished for oil fields and gas fields. Bonuses are payable upon commencement of production and also after certain production thresholds are reached. There is no distinction for onshore and offshore blocks. Production bonuses are tax-deductible, but not cost-recoverable.

Oil fields	
Cumulative production thresholds (barrels of oil equivalent)	Production bonus (HRK)
Start of commercial production	1,400,000
50,000	1,400,000
100,000	1,400,000
150,000	1,400,000
200,000	1,400,000

Gas fields	
Cumulative production (barrels of oil equivalent)	Production bonus (HRK)
Start of commercial production	900,000
25,000	900,000
50,000	900,000
75,000	900,000
100,000	900,000

Surface rental fees

Surface rental fees apply at the following annual rates:

- HRK400 per square kilometer are specified in the PSC agreement
- HRK4,000 per square kilometer of exploitation area for each such area

Surface rentals are tax-deductible, but not cost-recoverable.

Administration fee

An annual administration fee applies. The rate for the first year of the contract is HRK600,000, increasing annually by 4% until the expiration of the contract and license. The administration fee is tax-deductible, but not cost-recoverable.

Royalties

The royalty rate is 10% of market value of gross production. Royalties are tax-deductible.

Cost recovery

In line with the draft PSCs for onshore and offshore licensing, the cost recovery ceiling for crude oil is set for offshore blocks at 50% of production net of any royalty payment, and for onshore blocks at 70% of production net of royalty payments. Costs allowed for recovery can be recovered at a rate of 100%, subject to a specified recovery ceiling. Unrecovered costs can be carried forward within the duration of the contract.

Profit production

The production remaining after royalty payments and cost recovery is treated as profit production, to be further split between the State and the contractor.

Profit split is based on the so-called "R-factor" as set out in the table below. Both the R-factor's sliding scale and the production split rates are predetermined. The R-factor is defined thus:

R = cumulative net revenues ÷ cumulative capital expenditures

R-factor	Contractor's share of profit production	State's share of profit production
$R \leq 1$	90%	10%
$1 < R \leq 1.5$	80%	20%
$1.5 < R \leq 2$	70%	30%
$R > 2$	60%	40%

Royalties, the cost recovery ceiling and the profit production split are not distinguished for oil and for natural gas.

Customs duties

Both contractors and subcontractors engaged in carrying out operations under a PSC with respect to the importation of equipment and materials are not exempt from customs duties and are subject to both European Union legislation and the laws and regulations of the Republic of Croatia effective at the time.

Unconventional oil and gas

Currently, no special terms exist for unconventional oil or unconventional gas.

Cyprus

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies in Cyprus to the oil and gas industry consists of a combination of corporate income tax (CIT), capital gains tax (CGT), value-added tax (VAT) and excise duty, whereby upstream oil and gas exploration and exploitation activities are to be undertaken under a production sharing contract (PSC).

- CIT rate — 12.5%
- CGT rate — 20%
- Branch tax rate — 12.5%
- VAT standard rate — 19%
- VAT reduced rate — 0% (applicable for certain exploration activities)
- Royalties — none
- Bonuses — yes
- Surface rental fees — yes
- PSC — yes

B. Fiscal regime

There are currently no specific tax laws on hydrocarbon exploration and exploitation activities in Cyprus, and the general (corporate) tax laws in force are applicable. The definition of the terms "Cyprus Republic" and "permanent establishment" includes all activities relating to the exploration and exploitation within Cyprus territorial sea as well as within any area outside the territorial sea, including the contiguous zone, the exclusive economic zone and the continental shelf.

As per the model exploration and production sharing contract (MEPSC), published as part of the third licensing round for offshore Cyprus concerning the authorization for hydrocarbons exploration, the intention of the Cyprus Government is to enter into a PSC with operators and contractors under which the Republic of Cyprus shall be entitled to a certain percentage of the profit hydrocarbons resulting from the hydrocarbon operations to be undertaken by the operator or contractor in Cyprus at its sole risk, cost and expense. Under the MEPSC, the applicable CIT shall be deemed to be included in the Republic's share of profit oil and profit gas, and therefore, the portion of the available hydrocarbons that the operator or contractor is entitled to shall be net of CIT.

Corporate income tax

Companies resident in Cyprus are subject to CIT on their worldwide income from business activities and certain other selected types of income. A company is deemed "resident" in Cyprus if its management and control are exercised from Cyprus. Nonresident companies are taxed only on income derived from a permanent establishment in Cyprus and on rental income from property located in Cyprus and on certain other types of income (please refer to Section E, Withholding taxes).

Ring fencing

Cyprus does not apply ring fencing in determining an entity's corporate tax liability in relation to its oil and gas activities. Losses from one project (where, if such losses were profits, they would be subject to CIT) can be offset against profits of the same company from another project; similarly, profits and losses from upstream activities can potentially be offset against downstream activities undertaken by the same taxpayer. New oil and gas industry taxation rules in this respect may be introduced by regulations envisaged by the Government.

CIT is levied on taxable income

Taxable income is the difference between taxable revenues and tax-deductible expenses for the year of assessment. Expenses (including interest expenditure) are deductible for CIT purposes if they are incurred wholly and exclusively for the production of (taxable) income.

The determination of taxable income is generally based on accounts prepared in accordance with International Financial Reporting Standards (IFRS), subject to certain adjustments and provisions.

Tax losses

Losses can be carried forward for five years from the end of the year of assessment in which the tax losses are incurred. This means in practice that tax losses incurred in tax year 2018 cannot be set off after the tax year 2023, and so on. Loss carrybacks are not allowed.

Groups of companies

Group loss relief for a tax loss incurred in an income year is allowed between resident group companies that meet certain conditions.

The group loss relief applies to cases in which the surrendering company is registered in and is a tax resident of another European Union (EU) Member State on the proviso that it has exhausted all possibilities available for using the losses in its respective country of tax residency or in the country where its intermediary holding company has its legal seat. In such instance, the tax losses should be calculated based on the provisions of the Cypriot tax laws.

Capital gains tax

Cypriot CGT is levied at a rate of 20% with respect only to profits realized upon a disposal of immovable property situated in Cyprus, as well as on the (direct and indirect) sale of shares of companies whose property consists partly or wholly of immovable property situated in Cyprus. Gains realized upon the disposal of shares in companies that do not own Cypriot-based immovable property are not subject to CGT. Moreover, the disposal of a lease registered in accordance with the Immovable Property (Tenure, Registration and Valuation) Law constitutes a taxable event for Cypriot CGT purposes.

Although not explicitly provided in the legislation, the term "immovable property" should be confined to include only immovable property physically situated on the mainland of Cyprus, as well as leases registered in accordance with the provisions of the Immovable Property Law, and should include neither the sea blocks or sea beds falling within the exclusive economic zone of the Republic of Cyprus nor a right to a fixed or variable payment for the working of mineral deposits and other natural resources (e.g., rights under the PSC).

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Depreciation and amortization allowances

The general depreciation and amortization allowances rules are as follows:

- *Plant and machinery:* A straight-line allowance of 10% a year is given on capital expenditures for plant and machinery (20% for assets acquired in 2012–18).
- *Industrial buildings:* A straight-line allowance of 4% a year is available for industrial buildings (7% for assets acquired in 2012–18).
- *Commercial buildings:* A straight-line allowance of 3% a year is available for commercial buildings.
- *Office equipment:* A straight-line allowance of 20% a year is available for computers. Other office equipment is depreciated under the straight-line method at an annual rate of 10% (20% for assets acquired in 2012–18).
- *Motor vehicles:* In general, a straight-line allowance of 20% a year is available for motor vehicles (except for private saloon cars).
- *Sales of depreciable assets:* On disposal of an asset, if sale proceeds are less than the remaining depreciable base, a further allowance is granted, up to the difference between the two. If sale proceeds exceed the depreciable base, the excess (up to the amount of allowances received) is included in taxable income. This is done on an asset-by-asset basis.

New oil and gas industry depreciation and amortization allowance rules may be introduced by regulations envisaged by the Government.

D. Incentives/tax holidays

There are no specific incentives or tax holiday facilities in Cyprus.

E. Withholding taxes

Cyprus does not impose any withholding taxes (WHT) on payments of dividends and interest to nonresident shareholders or lenders.

A 5% or 10% WHT rate applies (subject to double tax treaty relief or the absence of WHT, based on the EU Interest and Royalties Directive) to royalty payments for the economic utilization of licensing rights and the provision of technical assistance services within Cyprus.

A 5% WHT applies (subject to double tax treaty relief) on the gross income derived by a nonresident person (having no permanent establishment in Cyprus) in relation to services performed in Cyprus for activities connected with the exploration or exploitation of the seabed or subsoil or their natural resources, as well as in connection with activities relating to the installation and exploitation of pipelines and other installations on the soil, seabed or on the sea surface.

F. Financing considerations

Thin capitalization and transfer pricing

Currently, there are no thin capitalization rules or debt-to-equity ratios in Cyprus. However, EBITDA-based interest expense limitation rules are to be introduced in Cyprus as of 1 January 2019 following implementation of the EU Anti-Tax Avoidance Directive.

The arm's-length principle is codified in the CIT law in wording similar to that of Article 9 of the Organisation for Economic Co-operation and Development (OECD) Model Tax Convention. Consequently, all transactions entered into with related parties should be concluded on an arm's-length basis in order to avoid adjustments of the taxable profit by the Cypriot tax authorities. However, there are no specific rules regarding transfer pricing or transfer pricing documentation requirements in Cyprus (apart from back-to-back intragroup financing transactions).

It is expected that transfer pricing guidelines and transfer pricing documentation requirements will be introduced by the end of 2018.

In terms of intragroup loans (not back-to-back), this means that the interest rate applicable on such loan(s) should be based on market terms and conditions (irrespective of the tax-residency status of the related counterparty of the Cypriot tax-resident company). It may be good to have such market interest rate supported by a transfer pricing study.

As of 1 July 2017, the minimum margin scheme was withdrawn and intra-group loans financed out of debt instruments should be documented based on a transfer pricing study to be prepared by an independent transfer pricing advisor based on the Circular requirements and the OECD TP guidelines.

G. Transactions

Asset disposals

The MEPSC provides for assignment of the PSC (subject to conditions) as well as a change of control of the contractor.

If the contractor (Cyprus tax-resident company) is to realize a gain from disposal of assets, such gain is not subject to CIT in Cyprus if not realized in the course of conducting the business and being capital in nature (i.e., if such transactions are not of a repetitive character) and is not subject to CGT in Cyprus (unless Cyprus-based immovable property is disposed of).

Farm-in and farmout

No specific provision applies for the tax treatment of farm-in and farmout consideration, and its treatment is determined on the basis of the general taxation principles and provisions of the PSC.

No specific provisions exist from a VAT perspective on such transactions; however, potential cash outflows may arise if such transactions are considered as sale of rights on property. Opportunities exist, however, under certain conditions, to avoid such costs if such exit transactions can qualify as a VAT-free transfer of a business (or part of it) as a going concern.

Joint operations

There are currently no specific rules in Cyprus on the allocation of profits (i.e., revenues and costs) applicable to joint undertakings.

No specific provisions exist from a VAT perspective on Joint Operations. Arguably, from a VAT perspective, Cypriot VAT concerns and reporting obligations can relate only to the Operator under the PSC agreement.

H. Indirect taxes

VAT

In Cyprus, the following VAT rates currently apply: the standard rate at 19%, the reduced rates of 5% and 9%, and the zero rate (0%). The standard rate of VAT applies to all supplies of goods or services, unless a specific provision allows a reduced rate, zero rate or exemption.

Specifically for the oil and gas industry, certain exemptions may be enjoyed through the application of the zero rate. Zero rate can be applied for example with regard to:

- Goods acquired to be incorporated on drilling rigs for the purpose of construction, repair, maintenance, alteration or fitting-out of such platforms, or to link such drilling or production platforms to the mainland, as well as goods and services for the fueling and provisioning of such drilling or production platforms

- The supply, modification, repair, maintenance, chartering and hiring of self-propelled drilling rigs, provided that such rigs meet the definition of "qualifying vessels" (i.e., used for the navigation of the high seas for the purpose of commercial, industrial or fishing activities)

Excise duties

In accordance with the EU Acquis, Cyprus has adopted special excise duty rates in the following categories of products known as "harmonized," irrespective of whether they are produced in Cyprus, imported from other EU Member States or imported from non-EU countries:

- Energy products and electricity, e.g., petroleum oil, gas oil, kerosene, natural gas, coal and coke

Transfer tax

There are no specific transfer taxes in Cyprus other than Land Registry Office fees when transferring immovable property situated in Cyprus.

Stamp duties

Cyprus levies stamp duty on every instrument (i.e., agreement or contract) if it relates to any property situated in Cyprus or if it relates to any matter or thing that is performed or carried out in Cyprus (e.g., a sale or purchase of Cyprus-based assets, such as immovable property and shares in a Cypriot company; agreement/contract in relation to oil and gas operations in Cyprus). There are instruments (e.g., agreements without consideration) that are subject to Cypriot stamp duty at a fixed fee ranging from €0.07 to €35, and instruments that are subject to stamp duty based on the value of the instrument at the following rates:

For sums €1–€5,000	Nil
For sums €5,001–€170,000	€1.50 per €1,000 or part thereof
For sums above €170,000	€2 per €1,000 or part thereof

The maximum stamp duty payable is capped at €20,000 per instrument/agreement.

Registration fees

Registration fees are payable to the Registrar of Companies upon incorporation of a Cypriot company (fixed fee of €105 and an additional fee of 0.6% on every euro of registered nominal or authorized capital), upon every further increase of registered nominal or authorized capital (fee of 0.6% on every euro of registered nominal or authorized capital), and upon every further issue of shares (fixed fee of €20).

Other significant taxes

The following table summarizes other significant taxes.

Nature of tax	Rate (%)
Special contribution for the Defense Fund of the Republic	
On 75% of rents received	3%
On interest received or credited (except for interest earned in the ordinary course of business)	30%
On dividends received or deemed to be received from a nonresident company (if exemption under the Cyprus domestic tax laws does not apply)	17%

Payroll taxes

Nature of tax	Rate (%)
Social insurance contribution, levied on each employee's gross salary, up to €4,533 per month, payable by both employer and employee	7.8%
Special Cohesion Fund, levied on gross salary, payable by employer	2%
Human Resource Development Authority and Redundancy Fund, levied on gross salary, up to €4,533 a month, paid by employer	1.7%
Leave Fund, levied on gross salary, up to €4,533 a month, paid by employer in lieu of holiday pay (employer may obtain exemption from contribution to this fund)	8%

I. Other

Foreign-exchange controls

Cyprus does not impose foreign-exchange controls.

Gas to liquids

There is no special regime for gas-to-liquids conversion.

Mergers and demergers

No taxes arise on mergers and demergers with respect to transfers of businesses, assets or shares provided they qualify as company reorganization transactions.

Country-by-country reporting requirements

Per the Cypriot country-by-country (CbC) reporting requirements, a CbC report must be prepared and submitted to the Tax Department by multinational enterprise (MNE) groups if the annual consolidated group revenue exceeds €750 million during a fiscal year. The deadline to file the CbC report with the Tax Department is 12 months from the end of the relevant accounting period (e.g., for MNE group with year-end 31 December 2017, the reporting deadline would be by 31 December 2018).

Notification requirement

Each Cypriot constituent entity of an MNE group that has a CbC reporting obligation should file an annual notification with the Tax Department by the last day of the fiscal year to which the CbC report relates. Noncompliance with the CbC reporting legislation may result in penalties of up to €20,000 per entity.

Implementation of EU Anti-Tax Avoidance Directive

Cyprus, along with the other EU Member States, is required to adopt the EU Anti-Tax Avoidance Directive (ATAD) by 1 January 2019. ATAD combats abusive tax practices in the field of corporate taxation and contains rules aimed at addressing some of the practices most commonly used by large companies to reduce their tax liability, including:

- A controlled foreign company (CFC) rule to deter profit shifting to low-tax jurisdictions
- An exit tax to prevent tax avoidance
- An interest expense limitation
- A broadly worded anti-avoidance rule
- A rule targeting hybrid mismatches among Member States

The new provisions for the tax system should be in effect beginning 1 January 2019, with the exception of exit taxation and anti-hybrid articles, which should be in effect beginning 1 January 2020, and will bring substantial changes on how international groups operate.

Democratic Republic of the Congo

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ■ **Service contract**

A. At a glance

Fiscal regime

The law provides a tax difference in tax treatments following the stage of the hydrocarbon activity and the nature of the contract.

Hydrocarbon Law No. 15/012 dated 1 August 2015 provides for two types of petroleum contracts: production sharing contract (PSC) or service contract. Services agreements are submitted to the tax regime provided in the agreement.

Petroleum conventions regularly acquired before the enforcement of the aforementioned Hydrocarbon Law remain valid until they expire and will be submitted to the new law to their renewal.

The rules for taxation, rate, control, sanctions, prescription and litigation in relation to bonuses, royalties, profit oil contribution, etc., are contained in the Hydrocarbon Law and its Decree, the Income Tax Code dated March 2003 and amended to date, and petroleum contracts.

While the tax regime for services agreements is defined in the agreement itself, PSCs are subject to a tax regime defined by the Hydrocarbon Law and the contract itself. For the latter, four tax zones have been set up according to their geological and environmental characteristics: tax zones A, B, C and D. The Hydrocarbon Decree provides rules on classification of companies.

The main PSC taxes applicable are:

- Surface rent
- Bonuses — various amounts applicable depending on the tax zone and provided by the Hydrocarbon Decree and the contract
- Royalties — various amounts applicable depending on the tax zone and provided by the Hydrocarbon Decree and the contract
- Cost oil and excess oil — payment rules provided by the Hydrocarbon Law and Decree and the contract
- Profit and super profit oil — various amounts applicable depending on the tax zone and provided by the Hydrocarbon Decree and the contract

No corporate income tax applies under this regime, and only listed taxes in the Hydrocarbon Law are applicable (i.e., there are exemptions for all others).

B. Fiscal regime

Petroleum contracts

The petroleum contract is the agreement under which the DRC Hydrocarbon Ministry gives to a local or a foreign entity, after being selected after a call for tender, in association with the National Company, the right of exploration and exploitation in the form of a production sharing contract or a service contract.

The tax regime of these contracts is set as follows:

Production sharing contract

Usually, under the terms of a PSC and to the extent that oil is discovered by a company undertaking exploration and development activities in the DRC, the exploitation is made in the name of the DRC Government. If oil is not discovered, all the costs of exploration are assumed by the company.

The interest of the state is granted to the National Hydrocarbon Company (SONAHYDROC), which manages the DRC Government stake.

The tax regime of the PSC is mainly defined in the Hydrocarbon Law and Decree but also in the PSC itself.

- Royalty rates are set up in the PSC but must not be less than the following:
  - For tax zone A: 12.5%
  - For tax zone B: 11%
  - For tax zone C: 9.5%
  - For tax zone D: 8%

Royalties are calculated on net oil production (production excluding any water, mud, sediment, etc.) exclusive of any warehouse and transportation costs. The royalty is payable either in kind or in cash.

- Surface rentals are payable annually and calculated on the surface of the block on the exploration phase or on the exploitation phase.
- Cost oil and costs stop: the order of priority of the recoverable cost is set out in the Hydrocarbon Decree and the PSC. There is also a costs stop, which is a cost cap on net production and varies from 55% to 65% depending on the tax zone. Any excess oil (i.e., recoverable costs for a given period that exceed the cost stop) is equally shared by the company and the state.
- Profit oil: the Hydrocarbon Law prescribes for a minimum rate as follows while the Hydrocarbon Decree and PSC set out the detailed mechanism:
  - For tax zone A: 45%
  - For tax zone B: 40%
  - For tax zone C: 40%
  - For tax zone D: 35%

There is also in certain cases a super profit oil that entirely goes to the state when the oil price reaches the high-end price as defined by the Hydrocarbon Decree and PSC.

Bonuses

Bonuses are usually paid to the DRC Government for grant or renewal of an exploration or exploitation permit (in which case it is known as a "signature bonus"), or upon start of production.

Unconventional oil and gas

No special tax terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Not applicable because there is no corporate income tax due in a PSC.

D. Incentives

There are various tax incentives provided in the Hydrocarbon Law. The General Tax Direction and the General Customs and Excise Direction should provide to contractors or service providers, subsidiaries, consultants or subcontractors the certificates of non-taxation covering all these taxations incentives. These incentives are listed below.

Exemption from all taxes below:

Income taxes, taxes relating to companies, customs duties and withholding taxes

E. Withholding taxes

Branch remittance tax

There is no concept of branch remittance tax for overseas tax-resident companies performing activities in the oil and gas sector in the DRC.

F. Indirect taxes

VAT

The VAT law provides that the import of materials, equipment, and chemical goods and services related to petroleum activities is exempt from VAT during exploration, development and construction, as well as during the exploitation phase.

Import duties

In general, common law is applied.

Goods specifically intended for hydrocarbon operations are imported totally exempt.

The temporary importation of goods specifically intended for petroleum operations is subject to the standard temporary admission with a surety exemption.

Export duties

Export duties depend on the nature of the equipment. Exportation of hydrocarbon products in the DRC is free of customs duties and taxes.

Stamp duties

Stamp duties are not applicable.

Registration fees

Registration fees are not applicable.

However, registration fees at the rate of 1% of the amount of the capital are due for the incorporation of a public limited liability company or for an increase of its capital. Also, a 3% of registration fees is also due on transfer of shares of a company.

Exchange rules

Specific exchange rules should be provided by the Central Bank of Congo (DRC).

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The tax regime that applies to hydrocarbon exploration and production (E&P) companies in Denmark consists of a combination of corporate income tax (CIT) and hydrocarbon tax. As of 1 January 2014, all licenses are covered by Chapter 3A of the Hydrocarbon Tax Act. Certain transition rules apply to licensees, which, prior to 2014, were taxed according to the so-called "Chapter 3" under the previous hydrocarbon tax regime (hydrocarbon tax rules applicable to licenses granted before 1 January 2004).

The principal aspects of the fiscal regime for the oil and gas sector are as follows:

- Royalties – none
- Bonuses – none
- Production sharing contract (PSC) – none[1]
- Income tax rate:
  - Ordinary CIT rate – 22%
  - Chapter 2 CIT rate – 25%
  - Chapter 3A hydrocarbon tax rate – 52%
- Resource rent tax – none
- Capital allowances – D, U, E[2]
- Investment incentives – L[3]

B. Fiscal regime

Danish resident companies are subject to tax in accordance with a modified territoriality principle, which means that income and expenses from foreign permanent establishments (PEs) and real estate outside Denmark are not included in the income of a Danish resident company. As a general rule, branches of foreign companies located in Denmark are taxed exclusively on trading income and on chargeable capital gains derived from the disposal of trading assets that are located in Denmark and related to a PE.

1 *Denmark does not have a PSC regime, except for the fact that the Danish Government holds a 20% interest in the 1962 Sole Concession.*

2 *D: depreciation; U: capital uplift; E: immediate write-off for exploration costs.*

3 *L: losses can be carried forward indefinitely.*

The Danish hydrocarbon tax rules, however, contain a broader definition of when a Danish tax limited liability is created for a foreign company or person, compared with the ordinary PE test. Foreign persons and companies that engage in hydrocarbon feasibility studies, exploration activities, production of hydrocarbons and related business, including the construction of pipelines, supply services and transportation of hydrocarbons by ship or pipeline, are subject to taxation in Denmark on the income from the time the activity commences in Denmark. If Denmark has entered into a double tax treaty with the country where the foreign company is a tax resident, the treaty may modify the Danish tax liability.

With effect from income year 2015, the Hydrocarbon Tax Act establishes a tax liability for state institutions and entities, including the simultaneously created Nordsøenheden (an independent state company whose task is to administer Nordsøfonden, the state oil and gas company), even though they are tax-exempt under the Danish Corporation Tax Act. The amendment widens the tax liability to cover not merely extraction but also related activity.

The Danish hydrocarbon tax system that applies to hydrocarbon E&P companies and state institutions is a two-string system combining CIT at a rate of 25% (Chapter 2 income) and a special hydrocarbon tax at a rate of 52% (Chapter 3A income). Effective as of 1 January 2014, all licenses are taxed according to Chapter 3A. Certain transition rules apply to licensees that, prior to 2014, were taxed according to Chapter 3 under a former hydrocarbon tax regime. The overall combined tax rate for Chapters 2 and 3A is 64% as Chapter 2 taxes paid are deductible against the Chapter 3A income. The income covered by Chapters 2 and 3A includes first-time sales of hydrocarbons, gains and losses from disposal of licenses, exploration rights, gains and losses from the disposal of assets used in E&P activities and financial income directly related to the hydrocarbon activities.

Income related to conducting hydrocarbon feasibility studies, providing services to E&P companies, constructing pipelines, providing supply services and transporting hydrocarbons by ship or pipeline is not covered by Chapter 2 or Chapter 3A, but is subject to ordinary CIT at 22%. This also applies for state institutions and entities that normally are tax-exempt under the Danish Corporation Act.

The income taxed under Chapters 2 and 3A is calculated according to the ordinary tax rules that apply to Danish companies and branches, with the adjustments provided in the Danish Hydrocarbon Tax Act. In general, as a result of the hydrocarbon tax uplift (see the subsection on capital uplift in Section C below), hydrocarbon tax is levied exclusively on profitable oil field production. Chapter 2 taxes paid are allowed as a deduction against the tax basis for hydrocarbon tax (Chapter 3A).

Separate tax returns must be filed each year for each income stream (i.e., for Chapter 2 and Chapter 3A income), and all companies involved in oil and gas exploration in Denmark are required to file a Danish tax return from the year when they commence their exploration activities. The filing deadline is 1 May of the following year. The financial period must follow the calendar year.

Besides its hydrocarbon income, the company may have ordinary corporate income (income not covered by the hydrocarbon tax rules). Such income is taxed at the ordinary CIT rate. The filing deadline for this tax return is 30 June of the following year.

Ring fencing and losses

As a general principle, expenses and tax losses on transactions not related to Danish oil and gas E&P may not be offset against oil- and gas-related taxable income, either for company tax purposes (Chapter 2) or for hydrocarbon tax purposes (Chapter 3A). For example, financing expenses are deductible against the oil- and gas-related income only to the extent that the loan proceeds have been used in an oil and gas business. Chapter 2 tax losses may, however, be offset against ordinary corporate income (income not covered by the hydrocarbon tax act), but this does not apply the other way around.

As of 1 January 2014, no field ring fence exists. This means that tax losses from one field may be offset against a profitable field. All fields are jointly taxed, and the taxable income is constructed on an aggregated basis. This applies under both Chapter 2 and Chapter 3A.

Dismantlement costs

Expenses related to closing down a field are tax-deductible under Chapters 2 and 3A. Companies and persons taxed according to Chapter 3A may receive a tax refund equal to the tax value of the tax losses remaining at the time of closing a Danish hydrocarbon business. The refund is limited to the hydrocarbon taxes paid (52% tax).

The expenses are deductible when they have been incurred. Provisions for dismantlement costs are not deductible.

Mandatory joint taxation

Danish companies, branches of foreign companies and real property in Denmark that belong to the same corporate group are subject to mandatory joint taxation. The mandatory joint taxation also applies if a group has two entities in Denmark involved with hydrocarbon activities.

Functional currency

Provided that certain requirements are met, taxpayers may calculate their taxable income by reference to a functional currency (i.e., a currency other than the Danish krone). The election must be made before the beginning of the income year.

Transfer pricing

Transactions between affiliated entities must be determined on an arm's-length basis. In addition, Danish companies and Danish PEs must report summary information about transactions with affiliated companies when filing their tax returns.

Danish tax law requires entities to prepare and maintain written transfer pricing documentation for transactions that are not considered insignificant. The documentation does not routinely need to be filed with the tax authorities, but on request it must be filed within 60 days. For income years beginning on or after 2 April 2006, enterprises can be fined if they have not prepared any transfer pricing documentation or if the documentation prepared is considered to be insufficient as a result of gross negligence or deliberate omission.

The fine for failure to prepare satisfactory transfer pricing documentation is a maximum amount of DKK250,000 per year per entity for up to five years, plus 10% of the income rise carried through by the tax authorities. The basic amount may be reduced to DKK125,000 if adequate transfer pricing documentation is subsequently filed.

Fines may be imposed for every single income year for which satisfactory transfer pricing documentation is not filed. In addition, companies may be fined if they disclose incorrect or misleading information to be used in the tax authorities' assessment of whether the company is subject to the documentation duty.

The documentation requirements for small and medium-sized enterprises apply exclusively to transactions with affiliated entities in non-treaty countries that are not members of the European Union (EU) or the European Economic Area (EEA). To qualify as a small or medium-sized enterprise, companies must satisfy the following conditions:

- They must have fewer than 250 employees.
- They must have an annual balance sheet total of less than DKK125 million or annual revenues of less than DKK250 million.

The amounts above are calculated on a consolidated basis (i.e., all group companies must be taken into account).

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Capital uplift

To enable companies engaged in oil and gas E&P activities to earn an attractive rate of return after taxes, the hydrocarbon tax relief (uplift) was introduced to ensure that the 52% Chapter 3A hydrocarbon tax is levied exclusively when production from a field is extraordinarily profitable. No uplift is available under Chapter 2. The Chapter 3A hydrocarbon tax relief is an uplift of 30% on qualifying expenditures, which includes capitalized exploration costs and investments made in drilling rigs, ships, pipelines and other production plant and equipment. The relief is available for the tax basis for hydrocarbon tax only. The uplift is allowed as a 5% deduction per year over a six-year period and is granted in addition to the normal tax depreciation of plant and machinery and amortization of capitalized exploration costs over a five-year period. The uplift is not available for lease payments, interest, and production and administration expenses.

Certain transition rules are applicable to licensees that, prior to 2014, were taxed according to Chapter 3 of the previous hydrocarbon tax regime. An uplift of 25% per year over a 10-year period was granted under the old hydrocarbon tax regime; however, according to the transition rules, the uplift is reduced to 10% per year over the remaining 10-year depreciation period.

A tax incentive was passed in the Danish Parliament on 28 November 2017 introducing a tax incentive scheme that can be elected by oil and gas companies involved with the exploration and exploitation of hydrocarbons on the Danish continental shelf.

The incentive scheme introduces the following main features:

- Introduction of an investment window covering the period 2017–2025, where oil producers can elect an investment scheme according to which the rates for tax depreciations of platforms, operating equipment, etc., is increased from 15% declining balance to 20% declining balance. Also, the special hydrocarbon allowance on certain investments increased from 5% per year for a total of six years to 6.5% per year for a total of six years. Furthermore, the time from when the tax depreciation and hydrocarbon allowance on such investments can be taken will be moved to the time of payment to the supplier instead of to the date where the assets are delivered, final and ready for use.
- A supplementary tax is introduced in case the oil/gas price exceeds certain price levels; the purpose of the supplementary tax is to ensure that the incentive is paid back by the oil producers in case of increases in the prices of hydrocarbons. The basis of the supplementary tax is the corporate taxable income before financial income and financial expenses. The supplementary tax amounts to 5% in case the yearly average oil price exceeds US$75 per barrel and 10% in case the yearly average oil price exceeds US$85 per barrel. The supplementary tax is tax-deductible in the hydrocarbon income statement.
- The incentive scheme is voluntary and can be elected during the period 2017–2025; however, once the incentive scheme has been elected the scheme becomes mandatory.
- When the investment window closes in 2025, the incentive scheme stops.

Depreciation

An acquired oil license right may be amortized at an equal rate per year over the term of the license.

The main rule is that fixed assets (machinery, production equipment, etc.) may be depreciated according to the reducing-balance method by up to 25% a year. However, a number of large assets with a long economic life are depreciated on a separate balance by up to 15% annually, according to the reducing-balance method. This group of assets includes, for example, fixed plants such as drilling rigs.

Exploration costs

All costs related to oil and gas exploration in Denmark are allowed as a deduction for the purposes of Chapters 2 and 3A when they are incurred.

As an alternative to expensing the costs when they are incurred, exploration costs may be capitalized and then deferred for amortization over five years when the oil production is commenced or for write-off if the exploration is stopped altogether. No time limits apply to capitalized exploration costs.

A company may choose to expense costs when they are incurred for the purposes of Chapter 2 while, at the same time, capitalizing them for the purposes of hydrocarbon tax (Chapter 3A). Capitalization of exploration costs is particularly advantageous in relation to the 52% hydrocarbon tax and, unlike non-capitalized costs, capitalized exploration costs qualify for an uplift of 30% by way of hydrocarbon tax relief (see above).

No capitalization of exploration expenses can be made by a company from the time the company has classified one field as "commercial." To the extent the company has some costs that do not relate to the oil and gas business in Denmark, these costs are deductible only against ordinary business income.

D. Incentives

Tax losses

Chapters 2 and 3A tax losses may be carried forward indefinitely, except that hydrocarbon tax losses realized before the 2002 income year may be carried forward for only 15 years.

According to the transition rules applicable to licensees that, prior to 2014, were taxed according to the old Chapter 3, only 71% of any field tax losses accumulated but not utilized before the transition to the new tax regime can in general be utilized against future income generated under the new tax regime effective from 1 January 2014. The accumulated tax losses can be utilized by 2.5% in the income years 2014–15 and by 6% in the income years 2016–26. The remaining 29% cannot be deducted and is therefore forfeited.

If a change of control of an entity occurs, certain tax loss carryforward restrictions may apply for ordinary tax losses. It is likely that the change of ownership rules do not apply to Chapters 2 and 3A tax losses, but this issue has not yet been specifically dealt with in law or in practice.

E. Withholding taxes

Classification of shares

"Subsidiary shares" can generally be defined as shares in a company in which the shareholder directly owns at least 10% of the share capital (although other conditions also apply).

"Group shares" are shares in a company that are subject to mandatory joint taxation under Danish rules with the shareholder, or are eligible to be subject to international joint taxation under Danish rules with the shareholder.[4]

"Portfolio shares" are shares that are not subsidiary shares or group shares.

Dividends paid

In general, dividends paid are subject to withholding taxes (WHTs) at a rate of 27%, except for portfolio shares for which the rate is 15.4%. However, no WHT is imposed on dividends paid to companies if the Danish shares qualify as subsidiary shares, provided that the WHT has to be reduced or eliminated as a result of the EU Parent-Subsidiary Directive or a double tax treaty, and provided that the rights under the EU Parent-Subsidiary Directive or a double tax treaty

4 *See Section C on "Group of companies" in the* EY Worldwide Corporate Tax Guide.

are not revoked under Danish general anti-avoidance rules. For a company owning Danish shares that are not subsidiary shares but group shares, it is a requirement that the WHT should be reduced or eliminated as a result of the EU Parent-Subsidiary Directive or a double tax treaty if the shares were subsidiary shares. Furthermore, in both cases, under the Danish tax authority's current practice, the recipient of the dividends must be the beneficial owner of them and thus must be entitled to benefits under the EU Parent-Subsidiary Directive or a double tax treaty.

A Danish company declaring a dividend to a foreign company must withhold dividend tax at a rate of 27% on the declared dividend, if the recipient is subject to Danish tax on the dividend.

The rate of 27% on such dividend distributions has been deemed to infringe the freedom of establishment under EU law, as the WHT levied on dividend distributions to Danish companies/PEs is 22% (follows the general CIT rate). In order to remedy this conflict with EU law, the final dividend WHT rate is lowered to 22%. However, 27% still have to be withheld by the Danish company distributing the dividends and the foreign recipient must subsequently apply for a refund of the differential (5%-point for 2017).

Special anti-avoidance rules may in specific situations trigger withholding tax, e.g., certain intragroup transfers.

Dividends received

Dividends from group shares or subsidiary shares are tax-exempt if the dividend has to be reduced or eliminated according to the EU Parent-Subsidiary Directive or a double tax treaty. Dividends for which the dividend-paying company has made a tax deduction in its taxable income are not tax-exempt for the Danish dividend-receiving company unless taxation in the source country is reduced or eliminated according to the EU Parent–Subsidiary Directive.

Dividends received by a Danish PE may also be tax-exempt if the PE is owned by a foreign company that is tax resident within the EU, EEA or in a country that has concluded a double tax treaty with Denmark.

Dividends received on a company's own shares are tax-exempt.

WHT on dividends from a Danish subsidiary to a foreign company will apply in the case of redistribution of dividends if the Danish company itself has received dividends from a more-than-10%-owned company in another foreign country and if the Danish company cannot be regarded as the beneficial owner of the dividends received. Correspondingly, it will apply if the Danish company has received dividends from abroad through one or more other Danish companies. Such dividends will generally be subject to WHT at a rate of 27%, unless the rate is reduced under a double tax treaty with Denmark, or the recipient is covered by the EU Parent-Subsidiary Directive. As mentioned above, the rate of 27% has been lowered to 22% with effect from 1 July 2016.

Dividends from non-listed portfolio shares must be included in the taxable income of the dividend-receiving company with 70% of the dividends received. This amount is taxed at a rate of 22%. The effective rate of taxation on received dividends is consequently 15.4%. A tax credit may be available for the dividend-receiving company for foreign WHT paid by the dividend-distributing company.

Capital gains derived from the disposal of non-listed portfolio shares should not trigger any taxation, provided the shares disposed of relate to a Danish limited liability company (or similar foreign company), the shares are not publicly listed, a maximum of 85% of the book value of the portfolio company is placed in publicly listed shares and the company disposing of the shares does not buy new portfolio shares in the same company within six months after the disposal.

Interest

In general, interest paid to foreign group companies is subject to WHT at a rate of 22%.

The WHT is eliminated if any of the following requirements are satisfied:

- The interest is either exempted from taxation or is taxed at a reduced rate under the provisions of a double tax treaty. For example, if WHT on interest is reduced to 10% under a double tax treaty, the WHT is eliminated completely. Further, the double tax treaty must not be disapplied under general anti-avoidance provisions.
- The interest is exempted from taxation in accordance with the EU Interest and Royalties Directive (2003/49/EC). Further, the directive must not be disapplied under general anti-avoidance provisions. Under the directive, interest is not subject to tax if both of the following conditions are satisfied:
  - The debtor company and the creditor company fall within the definition of a company under Article 3 in the EU Interest and Royalties Directive.
  - The companies have been associated as stated in the directive for a period of at least 12 months.
- The interest accrues to a foreign company's PE in Denmark.
- The interest accrues to a foreign company in which the Danish company, indirectly or directly, is able to exercise control (for example, by holding more than 50% of the voting rights).
- The interest is paid to a recipient that is controlled by a foreign parent company resident in a country that has entered into a double tax treaty with Denmark and has controlled foreign corporation (CFC) rules and, if under these foreign CFC rules, the recipient may be subject to CFC taxation.
- The recipient company can prove that the foreign taxation of the interest income amounts to at least three-quarters of the Danish CIT and that it will not in turn pay the interest to another foreign company that is subject to CIT, amounting to less than three-quarters of the Danish CIT.

In cases covered by the two first bullet points above, the recipient of the interest must be the beneficial owner of the interest and thus must be entitled to benefits under the EU Interest and Royalties Directive or a double tax treaty.

The abovementioned measures and exceptions also apply to noninterest-bearing loans that must be repaid with a premium by the Danish debtor company.

Royalties

Royalty payments are subject to a 22% WHT.

The WHT rate may be reduced under a double tax treaty or taxed in accordance with the EU Interest and Royalties Directive. Royalty payments are subject to WHT if the payments are remunerated for the use of, or the right to use, any patent, trademark, brand, brand name, design, model, pattern, drawing, secret formula or manufacturing or production method, or for information on industrial, commercial or scientific experiences (know-how). The rules apply both to lump-sum payments and to ongoing payments. Under Danish tax law, the qualification of royalty income is based on the substance of the agreement between the parties rather than on how the payments are "named" (form).

As a general rule, payments to technical service providers and nonresident contractors are not subject to WHT, unless the payment falls within the definition of royalty as defined above. These services may, however, be subject to taxation under Chapter 2 (corporate taxation of hydrocarbon income).

Branch remittance tax

Branch remittance tax is not applicable in Denmark.

Income tax withholding and reporting obligations

A foreign company that is engaged in oil and gas exploration or production activities in Denmark is required to withhold a 30% flat-rate income tax from salaries paid to nonresident employees working in Denmark. If Denmark has entered into a double tax treaty with the country where the foreign employee is a tax resident, the treaty may modify the Danish tax liability.

From a double taxation treaty viewpoint, triangular situations may occur in which the employees are resident in a different country than the foreign company (the employer), i.e., the tax assessment should be performed based on the treaty between Denmark and the employee's country of residence.

The withholding and the payment of withheld taxes are required on a monthly basis, and reports must be filed with the Danish tax administration on an annual basis.

F. Financing considerations

Interest expenses

Interest expenses and capital losses (e.g., due to foreign exchange) on debts incurred for financing oil and gas E&P in Denmark are allowed as a deduction against both tax bases (Chapters 2 and 3A). The interest or loss must be related to the Danish oil and gas activity.

However, a branch of a foreign company cannot deduct interest on loans from its principal (i.e., its head office); there must be an "outside" lender (which can be a sister company).

Capital losses are generally deductible according to the realization principle, but it is possible to opt for the mark-to-market principle on currency fluctuations.

Debt to equity and other interest limitation rules

Under the thin capitalization rules, interest paid and capital losses realized by a Danish company, or by a branch of a foreign group company, are partly deductible to the extent that the Danish company's debt-to-equity ratio exceeds 4:1 at the end of the debtor's income year and the amount of controlled debt exceeds DKK10 million.

Denied deductibility applies exclusively to interest expenses related to the part of the controlled debt that needs to be converted to equity in order to satisfy the debt-to-equity rate of 4:1 (a minimum of 20% equity). The thin capitalization rules also apply to third-party debt if the third party has received guarantees or similar assistance from a foreign group company.

The Danish thin capitalization rules have been supplemented by an "interest ceiling" rule and an "earnings before income tax" (EBIT) rule. These rules cover both controlled and non-controlled debt. Only companies with net financial expenses exceeding DKK21.3 million are affected by these supplementary rules. For jointly taxed companies, the DKK21.3 million threshold applies to all group companies together.

As a result of the interest ceiling, deduction for net financial expenses is restricted to 3.2% (2017 level) of the taxable value of certain qualified assets. Any net financial expenses that exceed this amount are lost, except for capital and exchange losses, which may be carried forward for three years.

Under the EBIT rule, a company may reduce its taxable income (due to financial expenses) by only 80% of the EBIT. Net financial expenses in excess of this amount are nondeductible, but, in contrast with the net financial expenses restricted under the interest ceiling rule, these amounts can be carried forward to be used in future years (if they are not restricted once again by the EBIT rule in that year). The EBIT calculation must be made after a possible restriction due to the interest ceiling.

If a company establishes that it could obtain third-party financing on similar terms, it might be permitted to deduct the interest that would normally be disallowed under the ordinary thin capitalization rules described above. But no arm's-length principle can be applied to help the company avoid the interest ceiling or the EBIT rule.

G. Transactions

Asset disposals

The disposal of assets is a taxable event; gains and losses are generally taxable or deductible. As a rule, sales proceeds from fixed assets are deducted from the depreciation pool.

As an alternative, it is also possible to take the loss deduction directly in the taxable income computation. However, this requires that the written-down tax value of the asset be deducted from the depreciation pool and that no depreciation on the asset be available in the year of sale. Further, the depreciation pool must not become a negative amount as a result of deducting the written-down tax value of the asset from the pool.

Farm-in and farmout

It is common in the Danish hydrocarbon production industry for entities to enter into farm-in arrangements. However, the tax consequences of farm-in and farmout arrangements must be considered on a case-by-case basis, depending on how the agreement is structured.

The farmee (the party entering into a farm-in arrangement) is subject to taxation according to the hydrocarbon taxation rules. A farmee is deemed to hold a depreciating asset, the interest in the hydrocarbon license, from the time the interest is acquired (which can be up front or deferred, depending on the terms of the particular arrangement). The farmee can deduct the cost of the depreciating asset. The "cost" is the amount that the farmee is considered to have paid for the interest, and it can include the value of noncash benefits. Future commitments incurred by the farmee in respect of interest are generally deductible for the farmee (either outright or over the asset's effective life) if the farmee holds an interest in the permit.

The farmer (i.e., the person farming out) is deemed to have disposed of an interest in the license, production equipment, etc. The tax treatment of the farmer is described in the subsection above on asset disposals.

Selling shares in a company

Taxation of a company's dividends received, and realized capital gains on the sale of shares, will depend solely on whether the shares qualify as subsidiary shares, group shares, own shares or portfolio shares.

H. Indirect taxes

VAT

Since Denmark is part of the EU, the EU common system of value-added tax (VAT) has been implemented. VAT is a general value-added tax on consumption, which is based on transactions. VAT applies to all supplies of goods and services at every stage of the supply chain, up to and including the retail stage. A deduction is granted for VAT on purchases for use in a business subject to VAT, making the VAT neutral to the business and industrial structure. The place of taxation depends on the place of supply. However, specific rules exist concerning the place of supply where a distinction between the supply of goods and of services must be made. Gas, water, electricity and heat are considered as goods in this context.

The VAT system was introduced in Denmark in July 1967. Danish VAT is now applied at a standard rate of 25%; however, some transactions are zero-rated, and other transactions and entities are exempt from VAT.

Danish VAT applies exclusively within Danish territory, which is made up of landmasses, internal territorial waters, up to 12 nautical miles into the outer territorial waters from the shore or base line and the airspace above. The territory does not include the Faroe Islands or Greenland.

VAT applies to the following: the supply of goods or services made in Denmark by a taxable person; the acquisition of goods from another EU Member State (intra-community acquisition) by a taxable person; reverse-charge services received by a taxable person; and the importation of goods from outside the EU, regardless of the status of the importer. A "taxable person" is anyone who independently carries out an economic activity. Furthermore, a prerequisite for applying VAT is that the supply of goods or services be made for a consideration.

From 1 July 2014 whereby the supply between Danish companies (business-to-business sales) of, for example, mobile phones, tablets and laptops is no longer subject to sales VAT. Instead, a national reverse-charge mechanism applies, and the business company must calculate and apply the sales VAT, and subsequently deduct this VAT according to the VAT-deduction right on purchases. This does not include purchases from retailers.

Examples of common transactions and arrangements are given in the following (non-exhaustive) list:

Subject to VAT	Zero-rated	Exemption
Selling goods and services	Exports	Letting of real estate
Leasing goods	Intra-community trade	Financial transactions
Importing goods	–	Conveyance of passengers

If goods are exported or sold to a VAT-registered entity in another EU Member State, (intra-community supply), the supplies may qualify as free of VAT if they are supported by evidence that the goods have left Denmark.

Non-established businesses must also register for VAT in Denmark if any of the following apply:

- Goods are located in Denmark at the time of supply
- The business acquires goods into Denmark from other EU countries
- The business acquires mobile phones, laptops, etc., from Danish business suppliers of these goods
- Goods are imported from outside the EU
- If performing activities in Denmark that are subject to VAT
- Distance sales exceed the annual threshold for services taxable in Denmark, and to which the reverse-charge mechanism is not applicable

The VAT registration threshold is DKK50,000 (approximately €6,700); however, entities trading below this threshold can choose to register voluntarily for VAT. There is no registration threshold for foreign businesses.

A registered entity must include the output VAT it has charged on its sales in its periodic VAT returns (monthly, quarterly or biannually, depending on the taxable person's total annual turnover). From the output VAT, the registered entity may deduct input VAT on purchases and costs related to its activities subject to VAT. Non-established businesses may apply for reimbursement on costs incurred in Denmark.

Import duties

Denmark is part of the EU, which is a customs union with a common market; goods that circulate within the EU are deemed to be "in free circulation," and the transfer of goods between EU Member States is exempt from customs duty. The EU is considered one country from a customs point of view.

The importation of goods from outside the EU may be subject to customs duty (depending on the nature of the goods). The EU, therefore, is considered one country from a customs point of view. The duty rate on imported goods is regulated by the customs tariff, which is based on information from the World Customs Organization (WCO). Furthermore, the EU has entered into several agreements with developing countries. According to these agreements, goods from the developing countries may be subject to a reduced or zero customs duty rate under certain circumstances.

Goods are reported to the Danish tax authorities on importation into Denmark and, thus, to the EU Customs Union. In general, all duties (including customs duty, excise duties and VAT) must be paid to the authorities before the goods are in free circulation in Denmark and the EU. However, most companies are granted a credit.

Export duties

The export of goods or services is not subject to any duties.

Excise duties

Excise duties are levied on a number of goods manufactured in Denmark or imported into Denmark. Excisable goods include mineral oil products, natural gas, coal and electricity. All these energy products are covered by an energy tax, a carbon dioxide tax and a sulfur tax. The rates for the most common products in 2017 are as follows (where €1 is approximately DKK7.50):

Energy product	Energy tax	Carbon dioxide tax	Sulfur tax(es)	Nitrogen oxide tax
Gasoline	€0.57/liter	€0.061/liter	€3.1/kg content of sulfur	€0.0012/liter
Diesel oil	€0.40/liter	€0.061/liter	€3.1/kg content of sulfur	€0.0012/liter
Heating oil	€0.26/liter	€0.061/liter	€3.1/kg content of sulfur	€0.012/liter
Heavy fuel oil	€0.30/kg	€0.073/kg	€3.1/kg content of sulfur	€0.037/kg
Natural gas	€0.29/m³	€0.052/m³	nil	€0.0011/m³
Coal	€7.37/GJ	€2.17/GJ	€3.1/kg content of sulfur	€0.67/GJ
Electricity	€0.12/ kWh	nil	nil	nil

For certain purposes, companies that are registered for VAT can get a refund on energy taxes and carbon dioxide taxes.

The energy tax on electricity for oil and gas drilling purposes in Danish territory is refundable. The carbon dioxide tax on electricity is also refundable if it is used for refining. If certain conditions are met, the energy tax, carbon dioxide tax and sulfur tax on heating oil, heavy fuel oil, natural gas and coal for oil and gas drilling and refining purposes are refundable. Taxes on gasoline and diesel oil (for engines) are not refundable.

Offshore oil and gas drilling takes place outside Danish territory and is therefore outside the scope of energy taxation. However, offshore oil and gas drilling activities are liable for the nitrogen oxide tax.

Stamp duty and registration fee

The Stamp Duty Act was amended in 1999, and again in 2013. As a result, only "insurance against loss or damage" is subject to what is now called a "casualty insurance fee." This fee constitutes 1.1% of the collected insurance premiums.

The other parts of the Stamp Duty Act are implemented in the Registration Fee Act. This registration fee should not be confused with the registration fee on cars (commonly known as "car tax"). The main items subject to the registration fee arising from the Registration Fee Act are the registrations of ownership of immovable property, boats and aircraft (generally, when ownership changes).

The registration fee is fixed. However, the basis of the fee calculation is subject to specific regulations. As a general rule, the fee on immovable property is DKK1,660 plus 0.6% of the amount payable for the change in ownership. It should be noted that it is possible to avoid the 0.6% registration fee on immovable property in connection with an ownership change as a result of certain transactions (such as mergers, demergers and the conveyance of assets).

I. Other

Business presence

Forms of business presence in Denmark typically include companies, foreign branches and joint ventures (incorporated and unincorporated). In addition to commercial considerations, it is important to consider the tax consequences of each form when setting up a business in Denmark. Unincorporated joint ventures are commonly used by companies in the exploration and development of oil and gas projects.

Tax treaty protection

In general, oil and gas production constitutes a PE under most tax treaties; therefore, treaty protection cannot generally be expected for a foreign company. For individual income tax liability, tax treaty provisions vary from country to country, and protection against Danish taxation may be available in specific cases.

Other reporting obligations

Entities involved in E&P that engage foreign (non-Danish) contractors to provide services have a reporting obligation to the Danish tax authorities. The Danish tax authorities use this information to determine whether the contractor has a Danish limited tax liability arising from the services provided.

Ecuador

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Tax regime applied to this country

☐ **Concession**	■ **Production sharing contracts**
☐ Royalties	■ **Service contract**
☐ Profit-based special taxes	
☐ Corporate income tax	

A. At a glance

Fiscal regime

The principal elements of Ecuador's fiscal regime that relate to the oil and gas sector are as follows:

- Corporate income tax (CIT) rate – 25%[1]
- Royalties – 12.5% to 18.5%[2]
- Bonuses – none
- Exploration and exploitation service fee — 1% of the services fee amount after determination of profit sharing and income tax
- Sovereignty margin — 25% of gross income of the field production
- Exploration and exploitation service contract — contracting structure currently applied

Capital allowances

Immediate write-off for exploration costs is not a common practice. However, these costs can be subject to write-off when the operation is finished. See the description of the amortization of exploration costs in the following sections.

Investment incentives

Net operating losses may be carried forward and offset against profits in the following five years, provided that the amount offset does not exceed 25% of the year's profits. Loss carrybacks are not permitted.

Depreciation and amortization expenses can be deducted on a double base (twice the expense), to the extent they are related to the acquisition of machinery, equipment and technologies for the implementation of cleaner production mechanisms, energy generation projects from renewable sources or reduction of environmental impact of productive activities, and greenhouse gas emission reduction.

Reinvestment of profits results in a 10% reduction to the CIT rate.

1 *A 44.4% income tax rate applies for companies whose concession contracts in force were agreed in accordance with previous legislation, but this is no longer used by the current Government.*

2 *Royalties paid to the Government for petroleum exploitation might range from 12.5% to 18.5%, depending on the barrels produced, and calculated upon the gross monthly income. For gas exploitation, there is a minimum rate of 16% over the monthly income.*

B. Fiscal regime

Corporate income tax

The Ecuadorian tax system is based on the "worldwide principle," whereby all income, both foreign and Ecuadorian-sourced, is subject to income tax.

Oil and gas companies are subject to the general rules that apply to all industries. Oil and gas entities that operate through a locally incorporated company, a branch or a consortium are obligated to file and pay annual CIT for the net profit of the year. Income tax has to be paid on an annual basis, in April, for the preceding calendar year.

The CIT rate is 25% beginning in 2018. However, companies that reinvest their profits are entitled to a 10% reduction in the income tax rate, provided that they use those profits for the acquisition of new machinery or equipment to be used in production activities or for the purchase of goods related to research and technology applied to production. Likewise these companies must be considered as regular exporters in order to obtain the benefit. The reinvested profits are taxed at a 15% rate, provided that the reinvested amount has been used for the acquisition of machinery for purposes of the business.

For Ecuadorian companies whose shareholders, beneficiaries or similar are resident or established in tax havens or lower tax jurisdictions, representing 50% or more of its corporate capital (direct or indirect participation), the CIT rate is 28%. If the tax haven participation is lower than 50%, the 28% CIT rate applies only over the portion of taxable base related to this participation.

Also, the 28% CIT rate applies when the company fails to comply with the obligation to provide its shareholders' annex (which includes the information on shareholders, partners, and members) to the Ecuadorian Internal Revenue Service (IRS).

Incomes derived from the sale of stocks, shares, capital representative rights or any other that allows exploration, exploitation, concession or similar, are considered as income from an Ecuadorian source subject to CIT. These transactions should be reported to the IRS. Failure to comply with this obligation will result in a fine of 5% based on the market price of the shares.

General deductibility rules

Resident taxpayers are taxed on their net income: taxable income less deductible costs and expenses.

In this manner, all the expenses that are directly related to the main course of the business, and necessary to obtain, maintain or improve taxable income, might be considered as deductible expenses on production of duly supported valid invoices and receipts.

- Indirect expenses allocated from abroad to companies domiciled in Ecuador by their related parties, will be deductible up to 5% of the income tax basis plus the amount of those expenses.
- Any expenses incurred directly by a foreign member of the same group of companies who assigns the expense to the Ecuadorian taxpayer are considered indirect expenses.
- If the expenses are remitted to a tax haven, lower tax jurisdiction or special tax regime, a 35% withholding income tax is applicable.
- Despite the aforementioned, regarding contracts for the exploration and exploitation of nonrenewable natural resources, technical/administrative services will be considered directly as indirect expenses assigned from abroad to Ecuadorian entities by its related parties. Therefore, these services will consider the 5% limitation.

Royalties in the exploration and exploitation of oil and gas are subject to a 1% deductibility limitation of the corporate income taxable basis plus such expenses.

Withholding taxes

According to the local legislation, withholding taxes (WHT) are triggered upon payment or crediting on account, whether directly or through any other intermediary, to the extent it constitutes taxable income for the receiver. In this sense, remittances of Ecuadorian-sourced income to nonresidents are subject to WHT. The tax is withheld on the gross amounts remitted with no deductions allowed. The taxpayer of this WHT is the nonresident beneficiary of the Ecuadorian-sourced income. However, the local payer is considered a withholding agent and, as such, is jointly and severally liable.

It is noteworthy that all incomes are deemed taxable except those expressly listed as exempt. The list of exemptions does not include items, such as royalties, renderings of service, expenses reimbursement, payments made to nonresidents or the importation of goods. Generally, almost all types of cross-border payments are subject to income tax withholding, at a rate of 25% beginning in 2018. However, this percentage can be reduced under the application of double taxation treaty benefits.

Income generated from non-monetary investments, performed by companies that have contracts with the Ecuadorian Government for the rendering of oil and gas exploration and exploitation services, is considered as exempt, provided that such investments:

- Have been charged to these companies by their related companies as a cost in order to render services for the execution of the said contracts
- Have been registered before the Ecuadorian Central Bank as non-monetary investments to be reimbursed

A 2% WHT applies on payments made to local beneficiaries for the provision of services, and a 1% WHT is applied to the acquisition of goods.

Dividends

Dividends paid after determination and payment of annual income tax are also exempt, provided that the beneficiary is a company non-domiciled in a tax haven (in accordance with the Ecuadorian Blacklist issued by the tax administration authority), preferential tax regime or low-tax jurisdiction. Dividend recipients domiciled in a tax haven, preferential tax regime or low-tax jurisdiction have been subject to an additional income tax withholding of 7%[3] since 2018.

Dividends received by Ecuadorian corporations from foreign corporations are considered to be tax-exempt income, provided that those foreign-sourced incomes have already been subject to taxation in the country of origin and provided that such country is not deemed to be a tax haven or lower tax jurisdiction for Ecuadorian tax purposes — in which case, the tax paid overseas (if any) could be used as a tax credit for local purposes, up to the level of income tax liability in Ecuador.

Dividends paid to individuals who are tax residents are subject to an income tax withholding at a rate that varies from 0% to 35% depending on the amount distributed.

Noncommercial loans granted to shareholders and related parties should be considered as dividend prepayments and subject to WHT assumed by the Ecuadorian taxpayer. This WHT is considered as a tax credit for the Ecuadorian entity.

Interest

Interest payments and financial fees are generally subject to 25% income tax withholding (0% locally in some specific cases); however, if the loan has been granted by a foreign financial institution, specialized nonfinancial institutions[4] or an international organization (e.g., the World Bank), no income tax withholding should apply on such interest payments.

3 *If the company paid 28% of CIT before to distribute the dividends.*

4 *Qualified by the Superintendence of Banks.*

In addition, for interest expenses on foreign loans to be deductible the following conditions should be met:

- The economic "substance over form" condition should be met.
- The loan must be registered with the Central Bank of Ecuador.
- The interest rate should not exceed the maximum rate set up by the Central Bank of Ecuador at the date of registration of the loan.
- The income tax withholding on the payment should be made if applies. (When the interest rate exceeds the maximum rate set up by the Central Bank of Ecuador, the 25% income tax withholding should be made over the excess).
- When the transaction is performed between related parties, a three-to-one debt-to-equity ratio is applied.

Excess on sale price

With respect to the units sold, the Government is entitled to at least 70% of the difference between the sale price and the base price established in the contract. If the base price has not been established in the contract, it is determined by the president of Ecuador through a decree. In no case will the decreed price be less than the international price in force at the contract subscription date. For the PSCs signed by Petroecuador before August 1, 2008, the applicable rate on the excess sales price shall be 99%.

Foreign tax relief

Ecuador does not grant relief from foreign taxes for companies domiciled in Ecuador. However, apart from countries considered to be tax havens, income sourced from other countries received by Ecuadorian corporations is considered to be tax-exempt, provided that the income was subject to tax in that foreign country. This exemption does not apply when the foreign income comes from a tax haven jurisdiction.

Prepayment of Income tax

Companies that have signed an oil and gas exploration and exploitation services contract with the Ecuadorian Government are required to make a prepayment of income tax. This prepayment consists of an amount equal to 50% of the CIT amount triggered and paid in the previous fiscal year, less the amounts paid by the company via income tax withholdings. The prepayment of income tax is made in two installments: one in July and the other in September of the corresponding fiscal year.

If the triggered CIT for the current fiscal year, payable in April of the following year, is lower than the prepayment of income tax, the latter constitutes a minimum tax amount payable, and no refund is available.

Other

There is no branch remittance tax in Ecuador.

Exploitation companies might be granted one or more fields in Ecuador, which could be negotiated in one or more exploitation service contracts. Ecuadorian laws state that the party to each contract must be considered as a single and separate business unit, and the consolidation of financial statements of contract units is therefore not permitted.

C. Contracts

In Ecuador, a variety of contracts can be signed with the government in order to invest and produce in the oil and gas sector: joint contracts, shared management contracts, specific services provision or specific goods acquisition contracts and participation contracts. However, due to changes made by the last government, participation contracts are no longer being signed; instead, the oil and gas exploration and exploitation service contract is now being strictly enforced.

In order to sign an oil and gas exploration and exploitation service contract, companies must be domiciled in Ecuador through a local branch or a subsidiary company, and must participate in a public open bidding process.

In addition, companies that have signed an oil exploration and exploitation service contract may sign an additional contract in order to explore and exploit natural gas within the same field.

Exploration phase

The oil and gas exploration phase can last four years and can be extended for two years with prior approval by the hydrocarbons secretary.

Production sharing contracts

The participation of the contractor is based on production volume. It is calculated using the terms and parameters offered and agreed upon in the contract, in accordance with the following formula:

$$\mathbf{PC = X \times Q}$$

where:

PC = Participation of the contractor

X = Average factor, in decimals, corresponding to the participation of the contractor

Q = Audited annual production in the area of the contract

Gross proceeds

In a PSC, income corresponds to the participation of the contractor based whether on the sales price or on the references price; however, the sales price cannot be less than the reference price set by the government petroleum entity (EP PETROECUADOR).

According to the regulations applicable to hydrocarbons, the reference price is the average price for the previous month's external sales of hydrocarbons made by EP PETROECUADOR of equivalent quality, based on the contractual bases. If there are no external sales by EP PETROECUADOR, the reference price is calculated based on the crude proportion negotiated by the parties, obtained from specialized and recognized publications.

For natural gas, the reference price is the same as for renewable energy. In PSCs, the reference price is calculated as follows:

- For free natural gas: the reference price for each unit is calculated by multiplying the calorific power (in BTU) by the BTU price of fuel oil No. 6.
- For condensed gas: the reference price of a metric ton is the same for the average volume price of liquefied petroleum gas sold by *EP PETROECUADOR* under cost, insurance and freight (CIF) conditions.

Therefore, the reference prices may be verified with the production companies to analyze new conditions regarding this issue.

Preproduction costs

Generally, preproduction costs include exploration costs, development costs and associated financial costs. If reserves are found, these costs are amortized equally over a five-year period starting from the date that production begins. If no reserves are found, these costs may be deducted in the year that this is recognized.

Payments to related parties that exceed 5% of the taxable basis are not deductible for CIT purposes. Amortization of preproduction costs attributable to administrative expenses is not permitted to exceed 15% of the total amount of such costs.

Funding from a company's headquarters must be registered as a long-term liability. No income statements need be presented.

Exploration costs

For PSCs, exploration costs may be assigned within the duration of the exploration period, which might range from four to six years starting from the date that the contract is registered in the Hydrocarbons Control and Regulation Agency (Agencia de Regulación y Control Hidrocarburífero).

Exploration costs generally include depreciation of fixed assets (support equipment). Excluded from exploration costs are those that are incurred by the contractor before the date of registration of the contract in the Hydrocarbons Directory, and interest from financing.

Furthermore, in order to initiate exploration activities, the company must give a 20% guarantee to EP PETROECUADOR.

Development costs

These costs can be registered from the date on which the development plan is approved.

Production costs

These costs should be registered from the date on which the first barrel is available for commercialization or industrialization and should be amortized based on the units of production. During this period, funding from a company's headquarters is registered as a short-term liability and income statements are presented.

Depreciation, depletion and amortization (DDA) calculation

Preproduction costs are amortized on a straight-line basis over a five-year period, starting from the production phase.

Production costs are amortized over the life of the contract using the units-of-production method based on proven crude oil reserves. The amortization period begins the following year from the one in which the investment is capitalized. See formula below:

DDA = (unamortized cost at beginning of period/proven reserves at beginning of period) × production during period.

If the proven reserves change during the fiscal year, the applicable formula is as follows:

DDA = (unamortized cost at beginning of period/proven reserves at beginning of period) × production during period.

Transportation and storage costs are amortized on a straight-line basis over a 10-year period beginning with operations.

Support equipment is depreciated using the straight-line method, according to general percentages of annual depreciation as follows:

- Buildings, aircraft and ships — 5%
- Facilities, machinery, equipment and furniture — 10%
- Vehicles and other transportation equipment — 20%
- Electronic hardware and software — 33.33%

Transport and storage costs

Amortization of transport and storage costs will be carried out in 10 years from the moment the transport system enters in operation, duly authorized by the National Agency for Control and Regulation of Hydrocarbons.

Oil production

To determine oil production, it is necessary to measure the crude oil kept in the warehouse tanks at the collecting centers, after separating water and ware materials. The resulting oil is measured in barrels.

Fiscal uncertainty

Oil and gas companies must adapt to the fiscal regime in force. However, fiscal uncertainty clauses are included in oil and gas transportation contracts.

Marginal field contracts

With low operational and economic priority, marginal field contracts are intended for low-quality crude. They represent less than 1% of the national production.

Under these contracts, all production belongs to the estate. Exploration costs under these contracts are capitalized annually. The tax basis for these costs (adjusted for amortization) is considered an asset of the contractor.

For the development of the contract, the contractor receives reimbursement for operational costs for the base curve of production, in dollars, and participation in the volume of crude oil resulting from any increase over base production. The base curve is estimated on future production from developed, proven reserves using mathematical simulation and studies of the wells; the base curve is specifically detailed in the contract.

Service contracts for the exploration and exploitation of hydrocarbons

In service contracts for the exploration and exploitation of hydrocarbons, the contractor commits to EP PETROECUADOR to provide exploration and exploitation services in the areas previously determined. The contractor uses its own economic resources. Accordingly, the contractor has to invest the necessary capital and use the equipment, machinery and technology required for such contracts.

Transportation, commercialization and production costs (including reimbursements and payments made by EP PETROECUADOR in favor of the contractor) are deducted from income. Furthermore, the contractor secures the right to a refund of its investments, costs and expenses, as well as the payment for services provided, when it finds hydrocarbons that may be commercialized.

Farm-in and farmout

Farm-in and farmout are both permissible; however, before any agreement is entered into, it is mandatory that the contractor obtain the written authorization of EP PETROECUADOR and the Ministry of Non-Renewable Natural Resources. If the authorization is not duly obtained, any agreement is invalid, resulting in the termination of the contract with the Government. The Government is in charge of not only authorizing this type of agreement but also qualifying the entity entitled to the rights through the corresponding transfer. Transfer fees apply, and vary depending on the type of transfer.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

D. Royalties

As a general rule, royalties to be paid to the Ecuadorian Government range from 12.5% to 18.5%. To determine the amount of royalties, oil production has to be efficiently determined once water and ware have been separated from the oil. A measurement will then be taken in the collection tank centers. The corresponding royalties will be paid on a monthly basis.

Royalties for PSCs are generally calculated as follows:

Production (P) in barrels per day	Monthly maximum contractor sharing	Monthly minimum estate sharing
P < 30,000	87.5%	12.5%
30,000 ≤ P < 60,000	86.0%	14.0%
P ≥ 60,000	81.5%	18.5%

E. Financing considerations

Effective from 1 January 2008, thin capitalization rules are in force, establishing a ratio of three to one foreign debt to equity.

F. Transactions

Capital gains

There is no capital gains tax in Ecuador, but the profit generated from the sale of stocks, shares and rights that allow exploration, exploitation, concession or similar is considered as income from an Ecuadorian source subject to CIT. Losses on sales between related parties are not deductible.

Asset disposals

All assets are generally the property of the Government, except for those acquired under specific service contracts.

With respect to all contracts, assets from foreign investments can enter the country under a special customs regime known as "temporary importation with re-exportation." Under this regime, there is no income tax effect or value-added tax (VAT) effect (provided the goods are not "nationalized").

Outflow tax

All Ecuadorian taxpayers that remit currency abroad are subject to a 5% tax on the amount of the transfer, regardless of whether the transaction is made through a financial institution.

All payments made abroad by Ecuadorian tax-resident companies shall pay outflow tax independently, if the financial resources are not located in Ecuador.

Additionally, exportation cash in amounts (incomes) also trigger currency exportation tax, regardless of whether the corresponding payments were made in Ecuador. In this case, the value of outflow tax payments that were generated abroad may be deducted.

Dividends distributed to foreign residents shall be exempt from outflow tax to the extent that the recipients of the dividends are not domiciled in a tax haven or lower tax jurisdictions. Outflow tax payments can be considered as CIT tax credit for five fiscal years in some cases.

G. Indirect taxes

Import taxes

Import taxes are paid based on the customs return (generally based on the description of goods, including origin, cost and quantity) on "auto-liquidation" (generally, the self-assessment of taxes) performed by the taxpayer. The taxable base for customs taxes is the CIF value.

The direct importation of machinery, tools and other materials for the exploitation and exploration of hydrocarbons, by companies that have entered into exploration and exploitation contracts with the Ecuadorian Government, is not subject to import taxes during the period of exploration or in the first 10 years of exploitation, provided that the imported machines are not made in Ecuador. Similarly, the importation of equipment, machinery, implements and other materials are exonerated from customs taxes within the exploration phase and within 10 years of the exploitation phase, provided that such products are not, and could not, be produced in Ecuador.

VAT

VAT is based on the value of imported goods, the acquisition of goods and the provision of services. The VAT rate is 12%; however, certain transfers of goods or services are specifically zero-rated. Imported services are taxed with 12% VAT.

Local taxpayers must file monthly VAT returns. VAT amounts paid in the local acquisition of goods or services, importation of goods or services, and acquisition of intellectual property rights could be offset with the VAT amounts levied on sales, to the extent sales are taxed with 12% VAT.

VAT paid on the purchase of goods or services for the production of exported goods may be recovered (this benefit is not applicable in the case of the oil and gas industry). In addition, companies may receive tax credits regarding all VAT payments for the purchase of goods or services, when those purchases have been in order to render services levied with 12% VAT.

Export duties

The tax basis for customs duties is the freight-on-board (FOB) value. Export duties depend on this item.

H. Other considerations

Employee profit sharing

In general, all employers must distribute 15% of their annual profits to their employees. In the hydrocarbon industry, the employees receive only 3% of the 15%, and the remaining 12% is provided on behalf of the Government.

Other specific requirements

For all contracts:

- Compensation for public construction — the contractor is required to compensate public construction at the beginning of the production period in accordance with government plans, the size of the contracted area and the proximity of the findings. The amount of this compensation is determined by the Government.
- Water and materials contribution — this is an annual fixed contribution of at least US$60,000.
- Provinces contribution — it is necessary to make a monthly auto-liquidation; the amount is based on the transported barrels through the SOTE (state pipeline for export of oil), except for any that are not destined for sale.
- Fund for the development of Amazon provinces — the taxable base is the value of the EP PETROECUADOR bill for the services performed.
- Fund for the development of the ecosystem of the Amazon region — the taxable base is the commercialization value of the petroleum.
- Environmental warranties — the amount depends on the basis for contracting.

For specific services provision or specific goods acquisition contracts:

- Honor of offer warranty — a minimum of 2% of the amount of the offer. This warranty is recoverable once the contract is signed.
- Proper compliance warranty — 5% of the amount of the contract. This warranty is recoverable once the documentation of termination or delivery is registered.
- Proper performance of work — 5% of the amount of the contract. This warranty is recoverable once there is evidence of the quality of the well's materials and whether the development work is considered highly effective.
- Investment warranty — before the signing of the contract, the contractor or its associate must pay a guarantee in a quantity equivalent to 20% of the compromised investments detailed for the contractor during the exploration period. This guarantee may be paid in cash or government bonds. This warranty is recoverable once the exploitation period concludes and all exploration obligations have been accomplished.

Egypt

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Egypt's fiscal regime applying to the oil and gas exploration and production industry is a combination of concession agreements and production sharing contracts.

The concession agreement must be formalized between the following three parties:

1. The Arab Republic of Egypt, as the owner of the resource
2. A public sector company representing the Ministry of Petroleum:
   - Egyptian General Petroleum Company (EGPC)
   - Egyptian Natural Gas Holding Company (EGAS)
   - Ganoub El Wadi Petroleum Holding Company (GANOPE)
3. Foreign holding companies and local private sector companies (contractors)

The public sector company will be the last bearer of the corporate tax due, as it pays the corporate tax due on behalf of the contractor.

The concession agreement will envisage a specific cost recovery mechanism.

B. Fiscal regime

Oil and gas exploration and production companies operating in Egypt will be subject to the provisions of the Egyptian income tax law, except as otherwise provided in the concession agreement.

Corporate tax

As per the provisions of the Egyptian Income Tax Law No. 91 of 2005, the corporate tax applies to:

- Companies that are resident in Egypt, on profits generated inside or outside Egypt
- Companies that are not resident in Egypt, on profits generated only inside Egypt

Based on the provisions of the Egyptian income tax law, the profits of oil and gas exploration and production companies should be subject to corporate tax at a rate of 40.55%.

The concession agreement provides that the contractor should be obliged to adhere to the Egyptian income tax provisions in connection with the filing of the corporate tax return, the assessment of tax and the keeping of required legal books.

The contractor is obliged to prepare the corporate tax return and submit it to the public sector partner 25 days prior to the filing due date. EGPC/EGAS/GANOPE should have the right to review the tax return in order to confirm the tax-due calculations.

As per the provisions of the Egyptian Income Tax Law, the tax return should be filed before 1 May each year, or within four months following the closing date of each financial year.

The contractor's annual income for Egyptian income tax purposes under the concession agreement should be calculated as follows:

- The total sum received by the contractor from the sale and/or any other disposition of all petroleum/gas acquired by the contractor pursuant to the provisions of the concession agreements, reduced by:
  - The costs and expenses of the contractor
  - The value of the excess cost recovery oil/gas as determined by the concession agreement

The public sector partner of the concession agreement shall pay the tax in the name of, and on behalf of, the contractor.

Because it is considered as additional income to the contractor, the corporate tax paid by the public sector partner will be subject to corporate tax. The contractor must add an amount to its taxable profit equal to the corporate tax amount paid by the public sector partner on its behalf.

Egypt applies ring fencing in the determination of corporate tax liability. Profits of certain concession agreements cannot be offset against the losses of another concession agreement, even if both concessions are cascaded by the same taxable entity.

The public sector partner of the concession must review, confirm and approve in its own corporate tax return the contractor's calculations of corporate tax due.

An exploration entity is generally entitled to sell its share of the oil to whomever it chooses, subject to approval by the EGPC (and in some circumstances, the EGPC may elect to purchase the oil itself). The sales income from its share of the oil and deductible expenses (which may be recoverable and non-recoverable expenses) is included as part of the entity's tax return and is subject to tax.

Capital gains tax

Gains resulting from a capital gains tax (CGT) event may be subject to tax. The Income Tax Law provides for CGT events, including the disposal of assets. Capital gains or losses are determined by deducting the net book value of an asset from its proceeds (money received or receivable, or the market value of property received or receivable).

For oil and gas exploration and production companies, the concession agreement typically provides that any assignment, sale, transfer or any other such conveyance done in accordance with the concession agreement provisions shall be exempted from any transfer/capital gain tax and any other taxes, including, without limitation, income tax, sales tax, stamp duty tax, or any similar taxes.

Functional currency

Provided certain requirements are met under Egypt's Income Tax Law, taxpayers may calculate their taxable income by reference to a functional currency (i.e., a particular foreign currency) if their accounts are solely or predominantly kept in that currency.

The corporate tax due amount shall be translated to Egyptian pounds in the company's corporate tax return based on the exchange rate declared by the EGPC.

Transfer pricing

Egyptian tax law includes measures to ensure that the Egyptian taxable income base associated with cross-border transactions is based on arm's-length prices. Several methods for determining the arm's-length price are available, and strict documentation requirements apply to support the method chosen and the prices reached. This is particularly relevant to the sale of commodities, intercompany services, intercompany funding arrangements, and bareboat and time charter leases.

Dividends

The concession agreement provides that, except for corporate income tax, the contractor shall be exempted from all taxes that might be imposed on dividends.

Bonuses

Signature bonuses and production bonuses are generally considered deductible according to the concession agreement.

Direct instructions were issued by EGPC in this regard, stressing the deductibility of such bonuses for corporate tax purposes. However, having such bonuses as deductible costs in a corporate tax return is still debatable and challenged within the Egyptian Tax Authority — which, in return, issued instructions contradicting the EGPC instructions and stressing the fact that such costs should not be considered deductible.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Capital allowances are based on the provisions of the concession agreement.

D. Incentives

Exploration

Expenditures on exploration are capitalized and are deductible for income tax purposes. Based on the provisions of the concession agreement and pending approval of the EGPC, capitalized exploration expenses are amortized over the lifetime of the concession agreement.

Tax losses

Income tax losses may be carried forward for five years.

Research and development

R&D incentives are based on the provisions of the concession agreement.

E. Withholding taxes

Generally, the Egyptian Income Tax Law imposes a withholding tax on all payments made by an Egyptian resident entity to nonresident entities, such as interest, dividends or royalties.

However, some concession agreements provide an exemption for the contractor from all withholding tax on dividends, interest, technical services and royalties.

F. Financing considerations

The Egyptian income tax system contains significant rules regarding the classification of debt and equity instruments and, depending on the level of funding, rules that have an impact on the deductibility of interest. These rules can have a significant impact on decisions regarding the financing of oil and gas projects.

The measures provide for a safe-harbor debt-to-equity ratio of 4:1. Interest deductions are denied for interest payments on the portion of the company's debt that exceeds the safe-harbor ratio.

G. Transactions

As mentioned earlier, the concession agreement provides that any assignment, sale, transfer or any other such conveyance done in accordance with the provisions of the concession agreement, shall be exempted from any transfer/capital gain tax and any other taxes including, without limitation, income tax, sales tax, stamp duty tax and/or any similar taxes.

H. Indirect taxes

Value-added tax (VAT)

The VAT Law No. 67 of 2016 was published in the *Official Gazette* on 7 September 2016 to be effective on the day following its publication.

Scope of VAT application

VAT is applicable to all local and imported goods and services except those specifically exempted. Services are defined in the law as any imported or local work done and not classified as goods.

There are 57 exempted goods and services listed in a separate table, including:

- Tea, sugar and coffee
- Gas, electricity and water
- Banking services
- Medicines and the active substances used in the manufacture of medicines, whether locally manufactured or imported
- Health services except plastic surgery and weight loss services other than for medical purposes
- Public education and scientific research services, including schools offering international curricula
- Public hospitals, public Medicare services, public clinics and nonprofit organizations
- Free radio and TV transmission services
- Sale and lease of vacant plots, agricultural lands, buildings and housing and non-housing units
- Advertisement services

VAT rate

The general VAT rate was 13% for the fiscal year ended 30 June 2017. However, from 1 July 2017, the general VAT rate increased to 14%. Machinery and equipment used in producing taxable or nontaxable goods or rendering services are subject to a 5% VAT and exported goods and services are subject to a zero VAT rate.

Special rates apply to a number of goods and services listed the VAT Law, as follows:

- Goods and services subject to the Table rates only
- Goods and services subject to the Table rates and the VAT general rate, with a right to deduct the input VAT in the application of the VAT general rate

This threshold does not apply to persons selling or supplying goods/services subject to the Table tax rates. They should register regardless of their sales amount.

Taxable value

The general value that should be declared as the amount subject to VAT for goods and services is the amount actually paid or payable by any means of payment.

The value subject to VAT for locally used goods is 30% of the sale value, without applying the deduction rules provided in Article No. 22 of the VAT law, on the condition that the goods should be used for a period of not less than two years.

With respect to installment sales, the value subject to VAT should include the installment interest exceeding the credit and deduction rate announced by the Egyptian Central Bank on the date of sale.

The value subject to VAT for Table goods and services subject to the Table rate and VAT is as follows:

- Local goods and services: Actual purchase amount paid or payable amount + Table tax amount
- Imported goods: Customs duty value + Customs duty + Table tax + any other imposed taxes or fees
- Imported service: Actual paid amount + Table tax
- The VAT taxable amount includes:
  - The amount paid by the purchaser or the service recipient
  - All related expenses spent as commissions, packing, stacking, transportation, insurance, charged by the seller to the purchaser or importer
- In the case of related-party transactions, the sale value should be according to arm's-length standards

Registration threshold

Each natural person or legal entity selling goods or services subject to VAT whose gross sales of taxable and exempted goods and services equals or exceeds EGP500,000 within the 12 months preceding the date of the VAT law enforcement, is obligated to register with the Egyptian Tax Authority within 30 days from the date of the enacted law.

A natural person or legal entity, reaching or meeting this threshold after the enactment of the VAT law is obligated to register within 30 days from the date of reaching the VAT registration threshold.

VAT returns

A monthly return should be filed for the VAT and/or the Table tax due within two months following the tax accounting month. As an exception, for the April VAT return, the filing deadline is 15 June. The return must be filed even if no sales are made within the tax period.

If the tax return is not filed before the legal deadline, the Egyptian Tax Authority has the right to make a deemed assessment by providing the basis of this assessment. This action would not remove the legal responsibility of the taxpayer.

VAT input deduction

VAT input is the VAT incurred or charged to the registrant upon purchasing or importing goods and services, including machinery and equipment, whether directly or indirectly related to the sale of goods and services subject to VAT.

When calculating the tax, the following should be deducted from the VAT output on the sales value:

- VAT paid or accounted for returned sales
- Tax charged on inputs, including the tax charged to the goods and services sold by the registrant through all distribution phases according to the conditions and situations that will be provided by the executive regulations relating to the VAT law

Items not entitled to input deduction include:

- Table tax whether goods and services subject to this tax or inputs of goods and services subject to this tax
- Input tax included in the cost items
- Exempted goods and services

Services rendered by a nonresident person (reverse charge)

If a nonresident person (both natural and legal) not registered with the Egyptian Tax Authority renders a service subject to VAT in Egypt to a person not registered in Egypt:

- The nonresident person is obligated to appoint a representative or an agent in Egypt to fulfill all the nonresident's obligations, as provided by the law, including registration, payment of VAT, the additional tax and any other taxes due according to the VAT law.
- If the nonresident party does not appoint a representative or agent in Egypt, then the Egyptian resident receiving the service is obligated to remit the VAT and any other tax due according to the VAT law to the tax authority without breaching his right to reimburse the tax payments made from the nonresident vendor.

If a nonresident person not registered with the Egyptian Tax Authority renders a service to a VAT registrant not necessary for their activity to a governmental entity or a general authority or an economic authority:

- Then the service recipient should account and remit the VAT due to the Egyptian Tax Authority within 30 days from the date of sale in case the nonresident party does not appoint tax representative or agent on his behalf

VAT registrants who import a service necessary for their VAT taxable activity are considered as an importer and a supplier of the said service at the same time.

In case the VAT is not paid within the legal deadline, an additional tax will be payable with and through the same procedures of the original tax payment.

The VAT registrant who paid the VAT due on the services received from a nonresident person is entitled to deduct this input tax if all conditions and rules stated in Article No. 22 of the law are fulfilled.

VAT application to oil and gas production and exploration companies

The VAT Law No. 67 of 2016, provided in Article 8 of promulgation articles, states this: "The provisions of this Law and the attached law shall not prejudice the exemptions established by virtue of the agreements concluded between the Egyptian Government and the Foreign Countries, and International or Regional Organizations, or the Petroleum and Mining Agreements."

Previously, under the umbrella of the sales tax law (now canceled since the issuance of the abovementioned VAT law), Egyptian General Petroleum Corporation (EGPC) used to issue a list of the goods and services that should be exempted from sales tax; consequently, the seller or vendor of these items did not add sales tax to its invoices addressed to the oil and gas production and exploration companies.

Currently, under the umbrella of the VAT law, EGPC issued a list of 20 items not eligible for oil and gas exemption. This list is planned to be reviewed and revised on an annual basis.

Import and export restrictions

Egyptian entities are not permitted to import without obtaining an importation license under certain criteria.

Importation with commission arrangements is no longer available.

Import restrictions

The Government imposes import controls to improve Egypt's balance of payments. Importers must obtain approval to open a letter of credit. A cash deposit ranging from 15% to 100% is also required, depending on the type of goods imported. The origin of goods must be certified in order to enter Egypt.

Travelers entering Egypt may import modest quantities of alcohol, cigarettes and perfumes free of duty. Visitors may also purchase certain quantities of duty-free liquor using foreign currency after passing through customs. Valuable personal effects may be declared to permit them to be taken out of the country on departure.

The concession agreement states that the public sector partner, the contractor and the operating company shall be allowed to import and shall be exempt from customs duties, any tax (i.e., sales tax and WHT at the customs clearance point, being the point of importation), and levies or fees of any nature, as well as from importation rules.

Such an exemption should be granted only in cases where oil and gas companies have an official certificate issued by EGPC confirming that such imports are required for their operations in accordance with the concession agreement.

For oil and gas companies operating in Egypt with no supervision, under the EGPC, according to Decree No. 7 dated 7 March 2017, importer registration requires the following for corporations:

- The company should be registered with the commercial register. Partnership companies and limited liability companies should be registered for at least one year; gross turnover of the year prior to registration should not be less than EGP5 million as per the corporate tax return submitted to the tax authority; companies that already have an importation ID are exempted from the condition related to the turnover at the timing of the issuance of the executive regulations.
- The company's headquarters should be in Egypt and established according to Egyptian regulations.
- For partnerships and limited liability companies, the capital should be not less than EGP2 million. This should be shown in the last financial statements submitted to the tax authority or proven by submitting a certificate confirming deposit of the capital in one of the banks registered with the central bank of Egypt in case the company has only started its activity. The partnership and limited liability companies that already have an importation ID at the time of this law enforcement should settle their situation according to this law provision within six months from the issuance of the executive regulations.
- For joint stock companies and private companies limited by shares, the issued capital should not be less than EGP5 million. At least 51% of the shares and quotas of the joint stock companies, private companies limited by shares, limited liability companies and partnerships should be owned by Egyptians. Corporations and companies holding an importation ID at the timing of this law enforcement should settle their status according to this law's provisions within six months from the date of its enforcement.
- The business turnover for the year prior to the registration applications should not be less than EGP5 million as evidenced by the corporate tax declaration submitted to the tax authority. Companies already having an importation ID are exempt from this condition.
- The company's authorized person responsible for importation should be an Egyptian national.
- Partners and company managers and persons authorized for importation must fulfill the conditions stated in Paragraphs C and D of the conditions required to register natural persons with the importers' register.

Export restrictions

Most goods may be exported free of duty. Certain items must be inspected before an export license is granted.

Stamp duty

Stamp duty is a state- and territory-based tax that is usually imposed on specified transactions but, in general, is very minor.

The concession agreement provides an exemption from stamp duty tax for oil and gas exploration and production companies.

Other significant taxes

Other significant taxes include cash remuneration (or fringe benefits) tax on noncash employee benefits of 10% to 20% and payroll taxes paid by employees of 10% to 20%.

I. Other

Foreign direct investment

The Government sets a high priority on attracting foreign direct investment (FDI) into the country. FDI helps improve technological innovations, creates more jobs and expands the country's ability to compete in international markets. Equally important, FDI opens the Egyptian economy to trade in semifinished products and other intermediate goods.

As part of the economic reform program, and in an effort to attract foreign investors, changes were made in various areas, such as corporate tax reform, lowered customs duties and streamlined investment procedures. Changes have also affected the system of national accounting, the modernization of Egyptian insurance supervision and intellectual property rights.

Exchange control regulations

There are no restrictions on transferring money to Egypt, except for illegal operations provided for by the money laundering Law No. 80 for 2002, amended by Law No. 78 for 2003.

There is a restriction on transferring money from Egypt. The maximum transfer amount allowed for individuals is US$100,000, except transfers required for trading transactions and certain other specific transactions. As for the oil and gas industry, on the assumption that transactions will be in the nature of trading transactions (e.g., sale of oil well pipes, provision of services), such restrictions are not expected to apply. (Restrictions were fully abolished.)

In all situations, bank approval on the transfer is subject to receiving proper evidence and documents related to the transfer. The transfer should take place after at least five working days from the company's request.

Repatriation of profits abroad

There is no restriction on the repatriation of profits abroad.

Business presence

Forms of business presence in Egypt typically include companies, foreign branches and joint ventures (incorporated and unincorporated). In addition to commercial considerations, the tax consequences of each business are important to consider when setting up a business in Egypt.

Unincorporated joint ventures are commonly used by companies in the exploration and development of oil and gas projects.

Equatorial Guinea

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Tax regime applied to this country

☐ **Concession** ☐ Royalties ☐ Profit-based special taxes ☐ Corporate income tax	■ **Production sharing contracts** ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies to the oil and gas industry is provided by the Equatorial Guinea Tax Code (EGTC) dated 28 October 2004, the Hydrocarbon Law No. 8/2006 dated 3 November 2006, and production sharing or other similar contracts concluded between the Equatorial Guinea (EG) Government and the contractor.

The main taxes applicable in the oil and gas sector are:

- Corporate income tax (CIT) — 35%
- Taxes on transfers and assignments — if a transaction generates capital gains not invested in Equatorial Guinea, it is subject to CIT.
- Export duties — generally exempt, subject to conditions[1]
- Royalties — not less than 13%
- Bonuses — determined under the terms of each production sharing contract (PSC)
- Surface premiums on rental rates — determined under the terms of each PSC
- Discovery, production and marketing bonds — determined under the terms of marketing bonds of each PSC[2]
- Urban property tax — 1% of tax base
- PSC — the State is entitled to a percentage of all hydrocarbons[3]

1 *Materials and equipment directly related to petroleum operations and imported under the temporary import regime may be exported from Equatorial Guinea free of all export duties.*

2 *"Discovery" here means the finding by the contractor of hydrocarbons whose existence within the contract area was not known prior to the effective date or hydrocarbons within the contract area that had not been declared a commercial discovery prior to the effective date, and that are measurable by generally accepted international petroleum industry practices.*

3 *The State is entitled to a percentage of all hydrocarbons won and saved from a contract area, based on the terms agreed in each contract and after deduction of royalties and investment recovery oil. The participation of the State should not be less than 20%.*

- Capital allowances — straight-line depreciation[4]
- Investment incentives — RD[5], L[6]

B. Fiscal regime

Production sharing contract

The main type of oil contract in Equatorial Guinea is a PSC. The contract is concluded either by international public invitation to tender in order to guarantee competition between the potential contractors or by direct adjudication.

Each contract comes into force only after it has been ratified by the President of the Republic and on the date of the delivery to the contractor of a written notice of this ratification.

Corporate income tax

EG companies are subject to CIT of 35% on the territorial principle. EG companies are those registered in Equatorial Guinea regardless of the nationality of the shareholders or where the companies are managed and controlled. Foreign companies engaged in business in Equatorial Guinea are subject to CIT on EG-sourced profits.

Company net profit will be determined by deducting from the gross income or gross profit all expenses tied to the performance of the taxable activities in Equatorial Guinea.

Operations carried out offshore (i.e., outside the international boundaries of Equatorial Guinea) do not fall within the scope of EG corporate tax. However, the EG tax authorities might try to attract profits from operations performed outside Equatorial Guinea when they could be linked to a branch or company in Equatorial Guinea.

Ring-fencing

EG law does not provide that the profit from one project can be offset against the losses from another project held by the same tax entity. Accordingly, petroleum operations should be accounted for separately.

Government share of profit oil

In addition to royalties, the State is entitled to a percentage of all hydrocarbons that have been extracted and kept from a contract area, based on the terms agreed in each contract and after deduction of royalties and investment recovery oil.

Non-recoverable expenditures

The following expenditures are not recoverable:

- Interest on loans obtained by the contractor from any affiliated company, or the parent company or non-affiliated third parties, that exceed the commercial rates charged by official banks
- Expenses incurred by the contractor prior to and during contract negotiations, and any expense incurred prior to the effective date of the contract
- Bonuses paid by the contractor upon execution of the contract
- Discovery bonus paid by the contractor
- Annual surface rental rate paid to the State

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4 *The EGTC provides the straight-line system of depreciation: all assets are depreciated in a uniform manner over a period representing the probable useful life of the assets in question.*

5 *The EG investment regulations provide financial and fiscal advantages for companies that create jobs and offer professional training for nationals and for research and development (R&D).*

6 *Net operating losses incurred during the previous year are deductible up to a maximum of five years.*

- Amounts in excess of 7.5% of the annual budget approved by the appropriate Branch Ministry during the initial exploration period, and in excess of 5% of the annual budget approved by the Ministry during the development and exploitation phase
- Any payments made to the Government as a result of failure to comply with minimal exploration work obligations as agreed upon in the contract
- Any sanctions imposed by the Government on the contractor as a result of environmental contamination (oil spills, etc.)
- Fines or sanctions that may be levied as a result of a violation of EG laws, regulations and other legal provisions
- Audit and inspection expenses incurred by the EG Government at the contractor's headquarters, as a result of the absence of original documents in the contractor's office in the republic
- Contractor's expert's expenses according to the contract

Determination of cost oil

Cost oil is the sum of all expenses borne by the holder in the framework of the PSC, determined in accordance with accounting methods. All costs related to petroleum operations are classified in accordance with their end use,[7] and classification criteria are included in the approved annual work program and annual budget for the calendar year in which the expenditure is made.

Uplift available on recovered costs

With the exception of general and administration costs incurred in Equatorial Guinea directly assignable to the annual budget, an uplift is available on the general and administration expenditures incurred by the contractor outside national territory with respect to petroleum operations. The uplift should be determined using a sliding scale set out in the PSC, based on total petroleum operational costs incurred during the year and duly justified by the contractor and approved by the Ministry.

Annual surface rent

An annual surface rent is due when the PSC or service contract is signed. The surface rental is prorated from the effective date through to 31 December of such year and is paid within 30 days of the effective date.

Surface rentals are calculated based on the surface of the contract area and, where applicable, of a development and production area occupied by the contractor on the date of payment of such surface rentals.

Royalty regimes

Contractors are subject to the payment of a royalty on the value of the hydrocarbon produced (including the government share of the production), and this payment is due from the first day of production based on the total disposable production volume from a development and production area.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Tax depreciation rules

Depreciation will be estimated from the calendar year in which the asset is placed into service, with a full year's depreciation allowed for the initial calendar year. Depreciation is determined using the straight-line method. The following rates are some of those applicable:

- Developed land — 5%
- Housing — 5%

7 *Exploration costs, development and production costs, operating or production costs, commercialization costs, and an allocation of general and administrative costs.*

- Temporary buildings — 20%
- Light vehicles — 25%
- Heavy vehicles — 33.33%
- Office furniture — 20%
- Naval and air material — 20%

EG law does not provide for any accelerated depreciation for the assets of a petroleum company.

D. Incentives

Carryforward losses

Net operating losses incurred during the previous year are deductible up to a maximum of five years. EG law does not provide that the profit from one project can be offset against the losses from another project held by the same tax entity. Accordingly, petroleum operations should be accounted for separately.

Research and development incentives

R&D incentives are determined according to each PSC.

E. Withholding taxes

Dividends

Dividends paid by an EG company to a nonresident are subject to a withholding tax (WHT) at the rate of 25%.

Dividends received by resident individuals are included in taxable income and subject to income tax at the progressive tax rates. In practice, some tax inspectors applied a 10% WHT on dividends earned by resident individuals. Resident companies also must include dividends received in taxable income.

Interest

Interest paid by an EG company to a nonresident is subject to WHT at the rate of 25%.[8]

WHT on resident and nonresident income

Gross income obtained in Equatorial Guinea for any kind of commercial or industrial activity, services, manpower supply or analogous services is subject to WHT at the rate of 6.25% when the economic activities are performed and invoiced by a resident, while the rate is fixed at 10% for nonresidents.

Amounts paid for mobilization, demobilization and transportation services in Equatorial Guinea in the petroleum sector are subject to WHT at the rate of 5% for nonresident entities.

Branch remittance tax

There is no branch remittance tax in Equatorial Guinea.

F. Financing considerations

Interest on loans is tax-deductible only when the rate does not exceed the interest invoiced by the banks. The bank interest rate is currently at 2.45%[9].

G. Transactions

The assignment, transfer or other disposition of the rights granted by a contract requires prior written authorization from the Ministry. Such assignment, transfer or other disposition is subject to the payment of a non-recoverable, nondeductible fee and to other requirements that are established in the authorization granted by the Ministry.

8 *This rate may be changed at any time by the Bank of Central African States.*

9 *This rate might change at any time by the Central bank.*

The transfer of the ownership of more than 50% of the shares in capital of any person making up a contractor, in which the transfer affects the ownership of the rights under the relevant contract, is deemed to be an assignment of contractual rights under a contract. All profits resulting from any assignment, transfer or other disposition of rights under a contract — regardless of the beneficiary, type or location of the transaction — are subject to taxes in accordance with the laws of Equatorial Guinea.

Capital gains will be included in the taxable profit calculation for CIT purposes, in accordance with the provisions of EG tax law.

The registration fees to be paid depend on the kind of asset — for example:

- Shares — 2%
- Transferable bonds — 2%

These registration fees are paid by the assignee.

H. Indirect taxes

Import duties

Provisions of customs duties are identical for most EG production sharing agreements (PSAs). They usually provide that the person designated as a contractor under a PSA, as well as its subcontractors, are allowed to import into Equatorial Guinea without restrictions and without payment of duties on goods, materials, machinery, equipment and consumer goods that are necessary for carrying out qualifying operations under a PSA, so long as the importation is in its own name or in the name of its subcontractors under regulations of temporary admission (AT) or temporary imports (IT), either normal or special, and on condition that these goods are to be used exclusively for qualifying operations and will be re-exported at the end of their use.

Export duties

The materials and equipment directly related to petroleum operations and imported under the IT regime may be exported from Equatorial Guinea free of all export duties, provided that the ownership of such materials and equipment has not been transferred to the State.

Stamp duties and registration fees

Registration fees are based on a percentage of the foreign company's share capital for a branch registration and of the share capital for a subsidiary registration. Registration costs pertaining to a subsidiary or to a branch are similar.

Provided that the share capital for a subsidiary or for the foreign company's share capital does not exceed XAF10 million (which is the legal minimum share capital for any public limited company (PLC) under the Organisation pour l'Harmonisation en Afrique du Droit des Affaires (OHADA) regulations), registration costs may be estimated at XAF8 million.

Registrations have to be renewed every year at different administrations (mines, trade, promotion of small- and medium-sized businesses, and city council).

I. Other

Urban property tax

All owners, holders and equitable owners of assets will be required to pay this tax, including heirs, joint owners and other entities that, while lacking their own legal status, constitute an economic unit and are the owners of record of assets that are urban in nature.

The tax base for urban property tax, which will coincide with the net base, will be constituted by 40% of the sum of the value of the land and the construction. It will enter into effect for taxation purposes on the fiscal year immediately following its notification.

The tax debt will be the result of calculating 1% of the tax base. This tax will be due for each complete six months and paid in the second quarter of the respective fiscal year.

Personal income tax

Employers are liable to personal income tax (as a payroll deduction) on behalf of their employees and must pay it back to the tax administration no later than 15 days after the beginning of the month following that in which the deduction took place.

The taxable basis is the previous month's gross salary. The rate of deduction is 0% to 35% on a progressive scale. The deduction for professional expenses amounts to 20% of gross salary, after social contributions have been deducted, up to XAF1 million per year.

Employers are also liable to withhold (as a payroll deduction) the following individual contributions on behalf of their employees, and must pay them to the tax administration no later than 15 days after the beginning of the following month:

- Social security contribution — taxable basis is the previous month's gross salary; rate of deduction is 21.5% for employers and 4.5% for employees
- Worker Protection Fund (WPF) — employers' rate is 1%on a taxable basis of gross salary; employees' rate is 0.5% on a taxable basis of net salary

Applicable domestic production requirements

All contractors are obliged to sell and transfer to the State, upon written request of the Ministry, any amounts of hydrocarbons from a contract area and any amounts of natural gas processed in Equatorial Guinea by a contractor or its associate that the State deems necessary in order to meet domestic consumption requirements.

Tax treaties

Equatorial Guinea has entered into the tax treaty of the Central African Economic and Monetary Community (CEMAC).[10]

10 *CEMAC, whose six member states are Cameroon, Chad, the Central African Republic, Equatorial Guinea, Gabon and Republic of the Congo.*

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ■ **Service contract**

A. At a glance

Fiscal regime

A new Hydrocarbon Code was published in *Official Journal* 221 of August 2014 by the Gabonese Government. See Section F below for further information.

The fiscal regime that applies in Gabon to the upstream petroleum industry consists of the Gabonese Tax Code, the Gabonese petroleum laws and the production sharing contract (PSC) or service contract between the Gabonese Government and the contractor. Under the new Hydrocarbon Code, concession rights are no longer possible.

The main taxes applicable in the oil and gas industry are the following: corporate income tax, annual surface rent and royalties on production. The main features are as follows:

- Royalties — between 6% and 12% of total production
- Bonuses:
  - On production: between US$1 million to US$2 million, depending on the volume of production
  - On signature: US$215/km² minimum (from US$0.5 million to US$1 million, depending on the area)
- PSC[1] — at least 50% should be in favor of the State
- Corporate tax:
  - Corporate income tax rate — 35% in general; 35%–40% for holders of an exploitation and production sharing contract (CEPP); 73% for holders of a concession agreement
- Annual surface rent:
  - On exploration: US$3 to US$6/km²
  - On production: US$4 to US$8/hectare
- Resource rent tax — none
- Investment incentives — D[2], L[3]

1 *PSC government share is based on production. A service contract regime called CEPP is in place.*
2 *D: Accelerated depreciation for capital goods.*
3 *L: Losses can be carried forward until the third fiscal year following the deficit period.*

- Additional petroleum levies:
  - Contribution to the Petroleum Support Fund:
    - On exploration — US$200,000/year (included in cost oil)
    - On production — US$0.05/barrel (not included in cost oil)
- Contribution to the fund of reconstruction of deposits:
  - Around US$200,000/year (depending on the value of equipment removed or upgraded)
  - For the restoration of site: maximum amount of 0.5%/year of the value of original equipment and facilities involved
- Contribution to training:
  - On exploration: paid three times at US$50,000, US$100,000 and then US$100,000 per year
  - On production: US$200,000/year
- Investment contributions:
  - Contractors will be required to contribute 1% of their turnover to a fund for diversified investments and 2% of their turnover to the fund for the development of the hydrocarbons industry.

B. Fiscal regime

Corporate tax

Tax rate

For oil and gas net profits, the tax rate is 35%. Companies following the CEPP regime are exempted from corporate or any other tax, except for those taxes that are expressly stated in the CEPP.

Ring fencing

In principle, ring fencing is limited to activities in the exploitation zone. However, the contract can extend coverage to the whole area covered by the contract.

Production sharing contract

A production sharing contract (PSC) is an agreement between the State and a company. It is a type of service contract in which a company is viewed as a service provider, and the State is considered a master builder. All the operations are realized by the company in favor of the State, which is the owner of the resources and investment.

Treatment of exploration and development costs

Depreciation deductions applicable in the petroleum industry are calculated by the operator in accordance with the rate defined in the CEPP. In practice, this mostly concerns companies operating under a concession agreement that has this specified in the agreement. In such a case, rates depend on the time period for depreciation, which in turn depends on whether expenses are exploration expenses or development and exploitation expenses. The rates can be readjusted if the actual time period for utilization is shorter (particularly in the case of an accidental loss or if the material wears out more quickly than expected).

However, within the framework of a PSC, depreciation is subject to special treatment. It is excluded from cost oil and does not impact corporate income tax as this is paid in kind. In practice, development and exploitation costs are recovered first, and exploration costs are recovered afterwards.

Determination of cost oil and profit oil

Once production has started, it is divided into two parts: cost oil and profit oil. These are divided pursuant to the terms of the service contract between the service provider and the State.

Cost oil

Cost oil is the part of oil production that serves to recover the exploration expenses, operating expenses and development expenses. Cost oil is calculated using an annual basis but can be recovered monthly. The calculation is based on net production (total production available of hydrocarbons, less royalty payments made).

Profit oil

Profit oil, or the remaining production volume, is the net production less the cost oil. The contractor and the State share the profit oil according to a rate specified in the contract. Depending on the contract, the rate in favor of the State can be two-thirds, three-quarters or four-fifths. The rate is progressive and depends on the volume of production. The law does not define the minimum share that must be allocated to the company or to the State.

Corporate tax

Companies must pay corporate tax in-kind. Corporate tax is not based on annual sales but on the level of production. The companies give the State a quantity of petrol that corresponds to the amount of tax owed (i.e., the quantity of petrol given is equivalent to the amount of corporate tax that companies would otherwise pay in cash). This amount is included in the profit oil as part of the State's entitlement.

For accounting purposes, the amount of corporate tax is calculated according to a special method called a "grossing-up" method (which is not specified in the contract). The amount of corporate tax of the company is calculated as follows:

$$\textbf{Amount of corporate tax} = \frac{\textbf{(Profit oil} \times \textbf{tax rate)}}{\textbf{(1 – tax rate)}}$$

where the tax rate is expressed as a decimal number rather than a percentage.

In addition to their operating accounts, companies have to establish special petroleum cost accounts. The amount of corporate tax calculated should normally correspond to the amount calculated in the operating account. However, as the expenditures differ between the operating account and the petroleum cost account, there could be a discrepancy between these numbers.

Royalties

The CEPP generates a royalty that is calculated at the production stage. The rate of royalty depends on the daily average of the total production (for a limited zone and for one month only). This rate is proportional to the total production and is not progressive. The rate can be fixed or variable within a production bracket (as determined in the contract) and is generally between 6% and 12% of the total production.

The rate is determined according to the following formula:

Amount of royalty = (Official sale price/transfer) × contractual royalty rate × gross production

Royalty regimes are not affected by the characterization of production as onshore or offshore.

Expenditure recovery

Non-recoverable expenses

The following expenditures are non-recoverable:

- Expenses that are not tax-deductible
- Bonuses
- Expenses related to the period before the effective date of the contract

- Expenses related to operations carried out for commercialization purposes
- Taxes, duties and royalties that the tax legislation does not authorize as deductible expenses or for which recovery is excluded by a provision of the contract

Caps that apply to expenditure recovery

The contractor reports to the State the amount of expenses incurred during the exploration according to the terms of the contract. Those expenses are refunded by the State at a later time, but are limited by a "cost stop." The amount of a cost stop is determined in the contract and is generally around 60% to 70% of net production. If the costs incurred in a particular year are higher than this limit, they can be deducted in the next year.

Uplift available on recovered cost

Uplift is available on recovered costs, but overhead costs are limited to 3%.

Fiscal uncertainty clauses

Fiscal uncertainty clauses are generally included in the contract.

VAT treatment

During the exploration phase and until the quantity produced is sufficient for commercialization, the contractor is exempted from paying value-added tax (VAT), as are suppliers, subcontractors, service providers and affiliated companies.

However, during the production phase, contractors, suppliers, subcontractors, service providers and affiliated companies are required to pay VAT at the rate in force (normally 18%, or 10% to 5% for certain products[4]), but they can recover these payments later. For operations between companies on the UPEGA list,[5] the rate is 0%.

Resource rent tax

Gabon does not have a resource rent tax.

Annual surface rent

An annual surface rent is due in the calendar year following the grant of title to a parcel of land. This fee is based on the surface of the site:

- On exploration, the annual surface rent is US$3 to US$6/km²
- On production, the annual surface rent is US$4 to US$8/hectare.

Unconventional oil and gas

No special terms apply for unconventional oil or unconventional gas.

C. Incentives

Accelerated depreciation

The tax depreciation rules are provided for in the applicable CEPP contract. Depreciation can be calculated using either the straight-line method or the declining-balance method. The declining-balance method is only possible for goods that are part of a list of specific goods made by a joint order of the Minister of Finance and the minister of the activity sector.

Only goods that are necessary to the production, transformation or development of petroleum, and those companies that participate in the industrial development of the country, can benefit from the use of the declining-balance method.

The Gabonese Tax Code allows accelerated depreciation for certain fixed assets.[6] The list of fixed assets eligible for accelerated depreciation is made

4 *That is, the customs rate.*

5 *UPEGA is the Gabonese Petroleum Union.*

6 *Under Article 11(V)(b) of the Gabonese Tax Code.*

available by the Minister of Finance and the Minister of Mines, but this list has not yet been released. All the fixed assets of the company that are eligible for accelerated depreciation are specified in the applicable CEPP contract.

In order to use the accelerated-depreciation method, a letter must be sent to the director of the tax office within three months of the acquisition of the fixed asset. The director must then consent within three months from the date of acknowledgment of receipt of the request. If no answer is received within those three months, the request is presumed to be accepted by the tax office.

Carryforward losses

Losses can be carried forward until the third fiscal year following the deficit period. The Finance Bill 2014 provides that losses would be carried forward until the fifth year following the deficit period.

D. Withholding taxes

A 20% withholding tax (WHT) is levied on capital gains (e.g., dividends, attendance fees and bondholder fees) paid by a resident company to an individual.

A 20% WHT is levied on distributions (e.g., dividends, attendance fees and bondholder fees) paid by a resident company to another company. The rate is expected to increase to 20% through the Finance Bill 2014. The levied rate can be reduced if the recipient is resident in a tax treaty partner country.

A 10% WHT is levied on most other payments made to a nonresident or foreign company. This withholding tax applies to services, industrial property, royalties or interest. There is also a branch remittance tax of 15%, which can be reduced to 10% should the head office of the relevant company be resident in a tax treaty partner country.

E. Indirect taxes

Import duties

Exploration and production (E&P) companies are subject to the Customs Code of the Customs and Economic Union of Central Africa (UDEAC) and its regulations.

Products, materials and equipment exclusively related to the prospecting and researching of petroleum are exempt from customs duties. Contractors, subcontractors or others related to the contractors have to produce a final certificate of utilization. For customs administration, the exploration period ends when the production reaches 10,000 barrels per 24-hour period.

The same exemption exists for the personal belongings of the company's foreign employees who are engaged in the prospecting, researching or exploitation of petroleum.

Products, materials and equipment related to the production, storage, treatment, transport, expedition and transformation of hydrocarbons are subject to a reduced rate of 5%. A contractor must request the Director General of Customs to grant permission for this reduced rate to be applicable. The reduced rate is not applicable after five years following the beginning of exploitation.

Products, materials and equipment that are exclusively related to the activity of a petroleum company and that are destined to be re-exported at the end of their utilization can be imported under the normal temporary regime, in which customs duties on imports for certain goods that are destined to be re-exported are suspended. Such materials must be necessary to the petroleum company's activities and should not belong to the State.

For all other goods, normal customs rules are applicable.

Export duties

Materials and equipment that are destined to be re-exported at the end of their utilization will be exempt from customs duties.

F. New Hydrocarbons Code

The main changes provided by the draft Hydrocarbons Code include the following topics:

- The duration for a branch that undertakes exploration can exceed four years before a branch should be converted into a local entity.
- The Gabon (national) Oil Company has the possibility of participating directly in the share capital of a contractor holding a PSC and contracts for exploration and the sharing of production, but such participation cannot exceed 15%.
- There must be a minimum 20% participation of the State in a PSC.
- Minimum cost recovery is 65%, up to a maximum of 75%, adjustable depending on profitability.
- The duration of exploration and exploitation phases is fixed.
- There is a strengthening of the obligation to contribute to the promotion of national employment (by submission of the realization of efforts in hiring nationals, including advertisement of vacancies in local newspapers and through firm recruitment).
- Priority is given to awarding a subcontract to companies incorporated in Gabon (with 80% national participation expected).
- A framework for the activity of gas flaring has been created.

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Tax regime applied in the country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

- Income tax rate — approx. 29.8%
- Royalties — 0%–40%
- Bonuses — None
- Production sharing contracts (PSCs) — none

	Oil and gas companies	Other companies
Ordinary tax	Approx. 29.8%	Approx. 29.8%
Royalties	0%–40%	None

B. Fiscal regime

The fiscal regime that applies to the oil and gas industry in Germany consists of a combination of royalties (called "Foerderabgaben") and corporate profits tax, i.e., corporate income tax, solidarity surcharge and trade tax.

In principle, there is no special taxation regime applicable to the oil and gas industry in Germany. Oil and gas companies are subject to the general accounting and taxation principles, i.e., they are subject to corporate income tax, solidarity surcharge and trade tax. In addition to that, oil and gas companies are subject to royalties for the exploration of oil and gas in Germany. Germany does not impose signature or production bonuses, and there are no state participation arrangements.

The German Ministry of Finance has set out its opinion regarding the tax treatment of issues related to oil and gas in a decree dated 13 December 1957, followed by an amendment dated 20 May 1980. The content of this decree is generally still applicable on the basis of decrees at state level containing guidelines as to whether expenses have to be capitalized or can be deducted, the useful lifetime of an extraction right, the treatment of provisions for abandonment, etc. In particular, no generally admitted federal decree currently exists, and so a taxpayer subject to taxation in one local state can generally not rely on a decree issued by the tax authority of another local state.

Right of taxation

Resident corporations, such as stock corporations (e.g., companies suffixed AG or GmbH) having their legal seat or effective place of management in Germany, are subject to taxation on all nonexempt worldwide business income. All income qualifies as business income.

In contrast, a nonresident corporation, whose corporate seat and place of management are located outside Germany, is subject to corporate income tax as well as to a solidarity surcharge and may be subject to trade tax (if a commercial business activity is carried out in Germany) only on income derived from German sources. Income from German sources includes, among others, business income from operations in the country through a branch, office or other permanent establishment.

German offshore activities

Germany's rights to the taxation of income also extends to certain activities in Germany's Exclusive Economic Zone (EEZ) in the North Sea and thus, in the German offshore area. The EEZ stretches seaward out to 200 nautical miles. Such activities particularly comprise the exploration or exploitation of the seabed and subsoil and their natural resources as well as the production of renewable energy.

Corporate profits taxes

Corporate income tax is imposed at a rate of 15% on taxable income, regardless of whether the income is distributed or retained.

A 5.5% solidarity surcharge is imposed on corporate income tax, resulting in an effective tax rate of 15.825%.

In addition, income from a commercial business activity in Germany is subject to trade tax. Trade tax is levied under federal regulations but at rates determined by the local authority where the business has a permanent establishment. These rates vary from approximately 7% up to 18.2%, whereas the average trade tax rate amounts to 14%.

The overall combined corporate profits tax rate amounts to approximately 22.8% up to 34% (with an average of 29.8%).

Royalties

Royalties are imposed annually at individual state level and can vary between 0% and 40% based on the market value of the produced oil or gas at the time of the production due to the federal mining law. The royalties can be deducted from the tax base for German corporate income tax and trade tax purposes.

Furthermore, the royalty-owning oil and gas company is also allowed to offset field handling charges against the royalty assessment base. These field handling costs include transport costs from well to treatment plant, preliminary treatments and the disposal of wastewater, but exemptions may apply.

Oil is mainly produced in Lower Saxony and Schleswig-Holstein, with a combined share of around 90% in 2016.

Gas is mainly produced in Lower Saxony, with a share of about 97% in 2016.

The royalty rates applicable in these states are outlined below:

State	Oil	Gas
Lower Saxony	18%*	30%*
Schleswig-Holstein	21%–40%**	40% or 18%***

* General royalty, which may be decreased to 0%/9% for oil and 7.5%/18% for gas, depending on the location of the oil or gas field and the method used for exploration of gas

** General royalty rate is 40%, which may be decreased to 21%, depending on the location of the oilfield as well as the amount of oil exploited (North Sea blocks A6/B4 and Heide-Mittelplate I)

*** General gas rate of 40%, which may be decreased to18%, depending on the location of the gas field (North Sea blocks A6/B4 and Heide-Mittelplate I)

Constitution of permanent establishments abroad during the exploration activities

According to Germany's Ministry of Finance, the activities for searching and producing have to be split into three different phases:

- Phase 1, "Project acquisition": The project pursuit and acquisition phase covers the geologic, economic and political assessment of the target country
- Phase 2, "Exploration": The project acquisition phase is followed by a detailed geological and seismic analysis as well as exploration drillings. Where there are successful results, further investigations are made as to whether the resources are economically feasible to exploit the oil and gas deposits.
- Phase 3, "Development and production": The third phase comprises the construction of the production sites and infrastructure as well as the production of oil and gas.

In general, activities during the exploration phase result in a permanent establishment if the exploration activity takes more than six months in total, either as a single exploration activity or as a series of simultaneous or consecutive exploration activities. However, activities in double tax treaty countries during the exploration phase may not give rise to a permanent establishment even if a fixed place of business is present (as they are deemed as preliminary or ancillary activities in terms of a double tax treaty), unless the exploration itself is a service rendered to third parties.

If exploration is not economically feasible, generally all related costs can be deducted from the German tax base since no permanent establishment is constituted abroad (exemptions may apply for certain expenses). Upon determination of economic feasibility, an intangible asset (oil or gas production/extraction right) is developed and a permanent establishment is generally constituted abroad. As a consequence, all tangible and intangible assets relating to that foreign permanent establishment have to be attributed and are deemed to be transferred to it, generally leading to an exit taxation in Germany. In general, the value for the transferred assets equals its fair market value. According to the German ministry of finance, the fair market value of the intangible asset is deemed to correspond to the amount of costs incurred in Germany, irrespective of whether the costs were deducted or capitalized in the past.

Capital gains resulting from the transfer of intangible assets to a foreign permanent establishment located in a double tax treaty country are generally subject to taxation immediately. In a case where the foreign permanent establishment is located within the European Union (EU), however, the taxation of the capital gain can (upon application) be deferred and apportioned over a period of five years.

Unconventional oil and gas

No special terms apply for unconventional oil or unconventional gas.

C. Capital allowances

Depreciation

For tax purposes, "depreciating" assets include assets that have a limited useful life and that decline in value over time. The German Ministry of Finance has issued an overview containing industry-specific assets required for the exploration and production activities, as well as their assumed useful lifetime.

A taxpayer is generally entitled to choose either the straight-line or reducing-balance method of depreciation, taking account of special considerations established in Germany's Tax Code. It should be noted that the straight-line method of charging depreciation is generally used in relation to oil and gas extraction right (if time-wise limited) and buildings.

Based on the aforementioned decrees of the German Ministry of Finance, expenditures for geological studies including preliminary exploration drillings and dry drill holes can generally be deducted from the tax base at the point in time when they are incurred. However, expenditures for deep wells have initially to be capitalized, leading to a separate tangible asset for each deep well. Such tangible assets are depreciated over an assumed lifetime of 8 or 15 years, depending on the period in which oil is produced or the kind of gas produced (8 years for acid gas and 15 years for natural gas).

Acquisition costs for exploration rights and seismic data have to be capitalized as intangible assets and amortized over the useful lifetime based on the straight-line approach.

In the case of a legal or contractual obligation to refill the drilled holes, the estimated abandonment costs have to be time-wise allocated over the useful lifetime of the hole — i.e., generally 8 or 15 years. The same applies to field clearance costs, where the period is assumed to be generally 20 years.

D. Incentives

No specific tax incentives are available for the oil and gas industry in Germany.

E. Withholding taxes

Dividends

Dividends paid by a resident corporation to both residents and nonresidents are subject to withholding tax. The domestic withholding tax amounts to 26.375% (i.e., 25% plus a solidarity surcharge of 5.5% thereon). For nonresidents, full or partial relief from withholding tax is generally available under an applicable double tax treaty, the EU Parent–Subsidiary Directive as well as under domestic law, but any such relief is also subject to strict German anti-treaty shopping rules.

Interest

Interest payments to nonresidents are generally not subject to withholding tax, unless for the following types of interest:

- Interest paid by financial institutions
- Interest from "over-the-counter business," which refers to bank transactions carried out over the bank counter without the securities being on deposit at the bank
- Interest from certain types of profit-participating and convertible debt instruments

Nonresidents may apply for a refund of the withholding tax if a treaty or EU directive exemption applies.

Royalties

Royalties paid to nonresidents are subject to corporate income tax, which is imposed by withholding at a rate of 15% (15.83% including the 5.5% solidarity surcharge).

Nonresidents may apply for a refund of the withholding tax if a treaty or EU directive exemption applies.

Branch remittance tax

There is no branch remittance tax in Germany.

F. Financing considerations

Thin capitalization

Under the interest expense limitation rule, the deduction of interest expense exceeding interest income (net interest expense) is limited to 30% of taxable earnings before (net) interest, tax, depreciation and amortization (EBITDA). Tax-exempt income and partnership income are not considered in the calculation of the taxable EBITDA. The limitation rule does not apply if one of the following exemption rules applies:

- *Exemption threshold:* annual net interest expense is less than €3 million.
- *Group clause:* the company is not a member of a consolidated group (a group of companies that can be consolidated under International Financial Reporting Standards (IFRS)). The group clause does not apply if both of the following circumstances exist:
  - A shareholder who, directly or indirectly, holds more than 25% in the corporation or a related party of such shareholder grants a loan to the company.
  - The interest exceeds 10% of the company's net interest expense.
- *Escape clause:* the equity ratio of the German subgroup is at least as high as the equity ratio of the worldwide group (within a 2% margin). A "group" is defined as a group of entities that could be consolidated under IFRS, regardless of whether a consolidation has been actually carried out. The equity ratio is calculated on the basis of the IFRS/US generally accepted accounting principles (GAAP)/EU local country GAAP consolidated balance sheet of the ultimate parent. The same accounting standard is applied to a German group but subject to several complex technical adjustments, such as a deduction for unconsolidated subsidiaries. The access to the escape clause is limited in the case of certain loans from nonconsolidated shareholders (the "related-party debt exception").

Unused EBITDA can be carried forward over a five-year period. Nondeductible interest expense can be carried forward indefinitely but is subject to German change-in-ownership rules.

G. Transactions

Asset disposals

Oil and gas licenses (i.e., exploration rights) can generally be transferred by way of an assets deal, but the transfer might be subject to restrictions arising from German mining law. The disposal of assets is a taxable event, so gains and losses are generally taxable or deductible, respectively.

Farm-in and farmout

A decree issued by the German Ministry of Finance dated 14 September 1981 deals with the tax consequences of the farm-in and farmout. The farmee (the party entering into a farm-in agreement) is deemed to have acquired an intangible asset. The acquisition cost corresponds to the amount the farmee has to pay or, alternatively, the amount the farmee is obliged to pay under the arrangement in the future. Upon economic feasibility, the farmee is allowed to depreciate the acquired intangible asset over its useful lifetime.

Selling shares in a company

Gains derived from a disposal of shares in a German corporation are generally tax-exempt at the level of resident corporate investors for corporate income tax and trade tax purposes. The "gain" is the difference between the purchase price and the book value of the sold shares. However, 5% of the capital gain is treated as a deemed nondeductible business expense subject to corporate income tax and solidarity surcharge thereon and to trade tax. Accordingly, any exemption is limited to 95% of the capital gain.

The disposal of shares in a German corporation by a nonresident should, in the absence of double tax treaty protection, generally qualify as a taxable event in Germany under German domestic law, but such disposal could also be 95% tax-exempt at the level of corporate investors. However, no trade tax is generally levied in the case of a nonresident corporate shareholder that is only subject to limited taxation in Germany, unless the shares are attributed to a German permanent establishment. In contrast, if double tax treaty protection exists, there should be no taxable capital gain in Germany.

H. Indirect taxes

VAT

Value-added tax (VAT) is applied at a standard rate of 19% for local supplies and 0% for exported oil, oil products, gas and gas condensate. Taxation depends on the place of supply. However, there are specific rules concerning the place of supply, in which a distinction between the supply of goods and of services must be made. Gas, water, electricity and heat are considered as a supply of goods.

VAT is potentially chargeable on all supplies of goods and services made in Germany. The territory does not include Helgoland, Büsingen, free harbors and territorial waters. However, some supplies made in free harbors and territorial waters have to be treated as German domestic supplies.

As a general rule, German VAT applies to:

- The supply of goods or services made in or to Germany by a taxable person
- The acquisition of goods from another EU Member State (known as "intra-community acquisition") by a taxable person
- Reverse-charge services or goods received by a taxable person
- The importation of goods from outside the EU, regardless of the status of the importer.

A "taxable person" is anyone who independently carries out an economic activity. If goods are exported or sold to a VAT-registered entity in another EU Member State (known as "intra-community supply"), the supplies may qualify as free of VAT if they are supported by evidence that the goods have actually left Germany.

In Germany, nonresident businesses must also register for VAT in Germany if any of the following apply:

- Goods are located in Germany at the time of supply
- The business acquires goods into Germany from other EU countries
- The business imports goods from outside of the EU
- Distance sales exceed the annual threshold for services taxable in Germany
- If the reverse-charge mechanism is not applicable.

A nonresident company that is required to register for German VAT can register directly with the German tax authorities; there is no requirement to appoint a VAT or fiscal representative. The input VAT incurred by an entity that is VAT-registered in Germany is normally recoverable on its periodic VAT returns.

As of 1 September 2013, Germany introduced a new domestic reverse-charge mechanism applicable for the domestic supply of gas to a company that itself renders supplies of gas (this is interpreted as being a reseller of gas) and for the domestic supply of electricity if the supplier and the customer are resellers of electricity. Furthermore, Germany implemented the reverse charge to certain supplies of gas and electricity through the natural gas system or electricity grid by non-established suppliers.

Natural gas and associated products imported into Germany (via a gas pipeline) from a field outside Germany are subject to formal customs import procedures — although from 1 January 2011 the importation of natural gas has been exempt from import VAT.

Import duties

As a Member State of the EU, Germany is also part of the customs union of the EU. The EU's customs territory includes generally the national territory of all EU Member States, including the territorial waters. The territorial waters of Germany include 12 nautical miles into the North Sea and certain areas defined by geographic coordinates in the Baltic Sea. Hence, any offshore activities outside German territory are generally not relevant under EU customs law. Goods circulating within the EU are free of any customs duties and restrictions; only when goods are imported into Germany from outside of the EU are they potentially subject to customs duties.

The rate of customs duties is based on the customs tariff classification (combined nomenclature) of the goods and might be lowered to 0% when the goods qualify for preferential treatment. Besides the preferential benefits, customs relief regimes may apply, resulting in reduced or zero rates of duty. Under the end-use relief, the goods have to be subject to a certain use under customs control. Other special customs regimes (e.g., customs bonded warehouse use or temporary use) may require a special authorization, which is usually limited to the owner and applied for by the importer because in most cases an EU-resident company is required.

Export duties

There are no export customs duties in Germany. However, export control restrictions might apply under certain conditions. In these cases, export licenses may become necessary, or the export itself is prohibited.

Excise duties

In contrast with customs regulations, excise tax regulations are country-specific. However, excise tax regulations are largely harmonized within the EU. The territory of the German excise duty laws generally includes the national territory of Germany and its territorial waters. The territorial waters of Germany reach 12 nautical miles into the North Sea and also cover certain areas defined by geographic coordinates in the Baltic Sea. Hence, any offshore activities outside German territory are generally not relevant under German excise laws. The respective excise duty law has to be considered in all cases of importations into Germany, including intra-EU transactions. In Germany, excise duties might accrue for certain hydrocarbon products (generally energy tax).

An energy tax is generally incurred when the taxable product is imported into Germany or removed from an energy tax warehouse. The excise duty rate of hydrocarbon products is based on the customs tariff classification of the product and calculated on the basis of the volume (e.g., per 1,000 liters). The energy tax can be suspended under a special procedure for transportation or storage in an energy tax warehouse, which is subject to prior authorization. For certain products and uses, a tax exemption might apply.

Stamp duties

There are no stamp duties in Germany.

Registration fees

There are no registration fees in Germany.

I. Other

Transfer pricing

In Germany, extensive related-party transfer pricing regulations apply, which are substantially in line with the Organisation for Economic Co-operation and Development (OECD) reports. The German Ministry of Finance has issued a decree regarding permanent establishments. This decree also includes oil and gas industry-specific regulations.

Gas to liquids

There is no special tax regime for gas–to-liquids conversion.

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies to the petroleum industry consists of the combined use of four basic tax laws: the Income Tax Act[1] (the ITA); the Revenue Administration Act, 2016, Act 915 (the RAA); the Petroleum (Exploration and Production) Act, 2016, Act 919 (the E&PA); and the Petroleum Agreement (PA). The ITA and RAA repealed the Petroleum Income Tax Act, PNDCL 188 (PITA) and the Internal Revenue Act, 2000, Act 592 (as amended).

Notwithstanding the coming into force of the ITA, entities that have existing PAs that provide for protection against adverse tax consequences upon the enactment of new laws shall not be affected by the changes.

PAs are signed between the Government of Ghana (GoG), the Ghana National Petroleum Corporation (GNPC) and the respective petroleum company or contractor.

The principal aspects of the fiscal regime that are affecting the oil and gas industry are as follows:

- Royalties — Royalty rates are not fixed. The PAs signed so far prescribe royalty rates ranging from 3% to 12.5% for gas and crude production.
- Production sharing contract (PSC) — The PA deals with specific PSC issues that exist between the petroleum company, the GNPC and the GoG. Generally, the PA indicates that the GoG's share may be taken in cash or in petroleum lift. An initial participating carried interest of at least 15%, to be held by the GNPC, has been introduced. The old law and all PAs in existence before the new law provided for an initial carried interest of at least 10%. Additional interest, which is a paying interest, may be acquired by the GNPC.
- Income tax rate — The income tax rate for upstream petroleum activities is 35%. For downstream petroleum activities, the applicable income tax rate is 25%.
- Capital allowances — D[2]
- Investment incentives — L[3]

1 *(2015) Act 896 as amended.*
2 *D: accelerated depreciation.*
3 *L: losses can be carried forward for five years.*

B. Fiscal regime

Corporate tax

Ghana's petroleum fiscal regime is governed by the ITA[4], RAA, E&PA and the PA. The commissioner-general of the Ghana Revenue Authority (GRA) administers the ITA, RAA and the taxation portions of the E&PA and of the PA.

The ITA, RAA and the taxation portions of the E&PA and of a PA are the main laws covering direct taxation of upstream petroleum activities. The ITA and RAA govern the downstream sector.

The applicable corporate income tax rate provided is 35%.

The corporate income tax rate is applied on the chargeable income derived by the petroleum contractor. The chargeable income is arrived at after deducting all expenditures "wholly, exclusively and necessarily" expended and specified expenditures, including prior-year losses of not more than five years, and permitted capital allowances for the year, from the gross income from petroleum operations. Expenditures of a capital nature, private outgoings and costs paid in respect of taxes are not deductible.

Ghana applies ring fencing. Profits from one petroleum agreement cannot be used to offset the losses of another petroleum agreement. Annual and quarterly tax returns must be filed by the contractor or the petroleum operator. Annual corporate tax returns must be filed within four months after the financial year-end of the contractor. In addition, within 30 days after the end of every quarterly period, the contractor must submit a quarterly tax return to the commissioner-general. The quarterly return must disclose an estimate of taxable income from petroleum operations for the quarter, an estimate of the tax due and a remittance in settlement of the tax due on that income. The commissioner-general has the power to grant a further 60-day extension for the contractor to file an annual return.

The commissioner-general may in writing request further information for the purposes of making an assessment on the contractor in respect of any quarterly or annual return, where the commissioner-general deems it necessary.

Taxation of gains on the disposal of capital assets

Consideration derived from the disposal of a depreciable asset of a contractor shall be included in determining the income of the contractor from petroleum operations. The company shall continue to claim capital allowance on the disposed asset that would still be in the pool of depreciable assets. In addition, gains made from the assignment or other disposal of an interest in a petroleum right shall be included in determining the income of the contractor from the petroleum operations. The gains will be subject to the corporate income tax rate applicable to the contractor (i.e., 35%). The assignment of interest in a petroleum agreement reduces the written-down value of the interest of the assignor and increases the written-down value of that of the assignee according to the proportion of the assignment. Capital losses are deducted in determining taxable income.

Functional currency

The primary and functional currency in Ghana is the Ghana cedi. All monetary transactions in Ghana, therefore, are expected to be conducted in the Ghana cedi. However, under specified conditions, the Ghana fiscal authorities permit companies that have strong reasons to report their business activities in another currency. The PA permits oil and gas companies to transact business in a currency of their choice. However, for tax purposes, the commissioner-general must give approval for the oil and gas company to report in any currency other than the Ghana cedi.

4 *(2015) Act 896 as amended.*

Transfer pricing

Ghana's tax laws include measures to ensure that cross-border trading does not unnecessarily erode local taxable profits of companies in their dealings with their parent or related entities. The commissioner-general has wide powers to disallow expenses or make adjustments if it is believed that an attempt is being made by the taxpayer, in dealing with the parent or any other related entity, to reduce the tax payable in Ghana. The commissioner-general has the power to determine the acceptability and taxability or otherwise of any pricing module that exists between related parties. The Technology Transfer Regulations (LI 1547) also attempt to ensure that the transfer of technology between an entity and its parent or other related persons is uniformly regulated in Ghana.

The GoG, with the assistance of the African Tax Administrators Forum, has enacted comprehensive transfer pricing regulations. The regulations entered into force in September 2012. The regulations apply to transactions between persons who are in a controlled relationship, among others, and require the maintenance of documentation and the filing of returns by resident associated persons using methods either prescribed or approved by the commissioner-general.

Management and technical services

The Ghana Investment Promotion Centre (GIPC) is the manager of all technical service transfer agreements that an entity incorporated or registered in Ghana can have with its parent, affiliate or other unrelated persons.

The Technology Transfer Regulations (LI 1547) regulate the types of technology that can be transferred for a fee in Ghana. The fee ranges between 0% and 8% of the net sales, or 0% to 2% of profit before tax.

Dividends

Dividends paid to a shareholder of a contractor are subject to withholding tax at the rate of 8%. However, a PA may exempt contractors from the payment of dividend tax. This means that dividend income earned by investors in a company carrying on upstream petroleum operations in Ghana is subject to tax unless exempt by a PA.

Royalties

Petroleum royalties are administered and collected by the commissioner-general and, like all taxes, are paid into the state's consolidated fund. The royalty rate is not fixed. In the PAs signed so far, the rate ranges from 3% to 12.5% of the gross production of crude oil and natural gas.

Royalty payments are based on the gross volume of petroleum produced and saved. The GoG and GNPC have the right to elect to choose oil and gas lift as payment for the royalty, or to receive a cash payment in lieu of petroleum lift.

Additional oil entitlement

The GoG and GNPC have the right to receive an additional oil entitlement (AOE), which is taken out of the contractor's share of the petroleum. The GoG and GNPC also have the right to elect that the AOE receivable be settled in cash or petroleum lift.

The AOE calculation is very complex. Broadly, it is based on the after-tax, inflation-adjusted rate of return that the contractor has achieved with respect to the development and production area at that time. The contractor's rate of return is calculated on the contractor's net cash flow and is determined separately for each development and production area at the end of each quarter, in accordance with an agreed formula.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances for petroleum capital expenditure

A petroleum capital expenditure is depreciated for tax purposes over a period of five years in equal installments.

A pre-operational petroleum capital expenditure incurred by a person carrying on petroleum operations is divided into five equal parts and claimed as a capital allowance in each of the first five years from the year of commencement (i.e., the year in which the contractor first produces oil under a program of continuous production for sale). Capital expenditure incurred after the year of commencement is also claimed equally over a five-year period. Capital allowances granted for a year must be deducted in determining the chargeable income of the person for the year.

D. Incentives

Exploration

Exploration costs incurred prior to commencement of drilling operations are capitalized, and a capital allowance is claimed equally in the first five years of commercial operations. Similarly, exploration costs incurred after commencement of drilling operations may be capitalized and a capital allowance claimed equally over a five-year period.

Tax losses

Tax losses incurred in any year of assessment can be deducted from the subsequent year's profit. The loss can be carried forward for five years. Under no circumstances may the aggregate deduction in respect of any such loss exceed the amount of the loss.

As noted previously, ring fencing applies, and, accordingly, losses from operations in respect of a petroleum agreement cannot be used to offset profits from another petroleum agreement.

Research and development

Research and development expenses are not tax-deductible.

E. Withholding taxes

Branch remittance tax

The PAs do not tax branch profit remittances. The ITA, however, imposes a tax on branch profit remittances at 8%. But since the PA indicates that no tax, duty or other impost shall be imposed by the GoG or by any political subdivision on the contractor, its subcontractors or its affiliates with respect to the activities relating to petroleum operations and to the sale and export of petroleum (other than as provided for in the PA), branch remittances are not captured as taxable transactions. That is to say, branch profit tax is applicable unless exempted under a PA.

It should be noted that remittances relating to downstream activities are subject to a branch remittance tax of 8%.

Foreign resident and foreign contractor withholding taxes

Nonresident subcontractors to a PA are subject to a final withholding tax (WHT) of 15% on gross payments received from the contractor who is a party to the PA. Resident subcontractors are subject to a withholding tax at the rate of 7.5%. This is not a final tax but a payment on account toward settling the corporate income tax liability of the resident subcontractor. However, a lower rate of say 5% shall be applicable where PAs provide for such rates. In this context, a "contractor" is generally defined as any person who is a party to a PA with the GoG and GNPC. A "subcontractor" is defined by the ITA as any person who enters into a contract with a contractor for the supply of work or services (including rental of plant and equipment) in Ghana for, or in connection with, the PA.

Generally, no variation of, or exemption from, the 15%/7.5%/5% WHT payable is available in respect of payments to subcontractors. However, WHT in respect of services provided to the contractor by an affiliate is waived, as long as such services are charged at cost.

Although the commissioner-general cannot grant any exemptions from the payment of WHT, Ghana's Parliament may grant an exemption.

Ghanaian registered or incorporated companies are required to file annual returns with the Ghana Revenue Authority. However, for a nonresident company, no returns need be filed. Under the ITA, however, a nonresident person who derives income in Ghana and whose income is not subject to a final withholding tax is required to file tax returns in Ghana.

F. Financing considerations

Ghana's tax system has significant rules governing the tax impact that the degree of debt and equity mix could have on a company. These rules should be taken into account by petroleum companies in evaluating any planning options.

Thin capitalization rules restrict the total debt and equity mix in a foreign-controlled entity for tax purposes. The permitted debt-to-equity ratio for tax purposes is 3:1. Any excess interest payment or foreign-exchange loss incurred in respect of a fall in the value of the debt obligation over and above this ratio is not tax-deductible.

The rules apply to the following entities:

- Ghanaian entities that are foreign-controlled or foreign entities that operate locally registered entities in Ghana
- Ghanaian entities that are locally controlled by other Ghanaian parent entities

The thin capitalization rules govern the extent of debt on which an "exempt-controlled entity" can obtain interest deductions on debts from the parent. An "exempt-controlled entity" is a company with 50% or more of its shares owned or controlled by the parent entity or a related entity. The deductibility of interest payments and foreign-exchange losses for tax purposes in any particular year is restricted to a debt–to-equity ratio of 3:1.

Financial institutions are excluded from the debt-to-equity rules.

Most investments are inbound, and, therefore, it is not common for Ghanaian entities to have controlling interests in other Ghanaian entities such that they could be caught by the thin capitalization rules. In the majority of instances, thin capitalization rules have been applied to Ghanaian resident companies with parents domiciled elsewhere. Such parent companies generally prefer not to tie down funds in equity. Instead, they prefer to have a mechanism to allow for quicker repatriation of funds invested in Ghana and, thus, tend to invest in debt rather than equity.

G. Transactions

Asset disposal

The disposal of an asset can have two effects, depending on whether it was sold before or after the year in which petroleum operations commenced.

If an asset is sold before the year in which petroleum operations commence, its sale has an impact on the quantity of capital allowances that may be claimed when operations commence. For the purposes of calculating the capital allowance for the year of commencement of commercial operations, the full proceeds of the sale are deducted from the accumulated petroleum capital expenditure incurred up to the year of commencement. The net expenditure, after deducting the proceeds of the sale, is treated as the petroleum capital expenditure at commencement and is subject to a capital allowance in equal installments over a period of five years.

In the case of the disposal or the loss or destruction of a petroleum capital asset in any year after the year of commencement of operations by a person carrying on petroleum operations, the full proceeds of the sale or insurance monies, compensation or damages received by the person is added to the year's gross income of the person arising from petroleum operations for the purpose of calculating the taxable income in the year in which it occurred.

Farm-in and farmout

Farm-in arrangements are a common practice within the petroleum extracting sector. A farmee entering into a farm-in arrangement is expected to be allocated the proportionate cost purchased in respect of the farm-in arrangement (i.e., the cost of the interest purchased). The farmee is entitled to a deduction for the cost it incurs over a period of five years from the date of commencement of commercial operations (see the previous section on capital allowances for more detail).

Where there is a farm-in/farmout agreement after the commencement of operations, the written-down value of the petroleum capital expenditure shall be apportioned between the farmer/farmee in proportion to their respective interests.

Selling shares in a company

Gains made on the sale of shares are subject to tax at the corporate income tax rate applicable to the person deriving the gain.

The written approval of the sector minister shall be required prior to the transfer to a third party of ownership, directly or indirectly, in a company, if the effect is to give the third party control of the company or enable the third party to take over the shares of another shareholder.

Where there is at least 5% change in underlying ownership of an entity, whether by way of direct or indirect transfer in an entity holding a petroleum right, it is deemed that the entity has:

- Disposed of a proportionate interest in its petroleum right and immediately re-acquired the interest equal to the amount received from the disposal
- Received for the disposal consideration equal to the higher of the consideration arising out of the change or the market value of the proportion of the right disposed

The implication is that gains derived from the transaction are subject to income tax in Ghana. Entities are required to notify the commissioner-general of such ownership changes within 30 days of the change.

H. Indirect taxes

Import duties

Goods imported for upstream petroleum operations are exempt from import duties. The sale of an exempt item by a contractor to another petroleum contractor remains exempt. However, the sale of an exempt item by a contractor to a non-petroleum contractor attracts duty if the item is ordinarily dutiable. The duty is assessed at the duty rate prevailing on the date the asset is transferred.

VAT

The value-added tax (VAT) regime came into effect in 1998. VAT applies in Ghana to all transactions conducted in Ghana, except for transactions that are exempt.

The VAT rate is 15%. There is a National Health Insurance Levy (NHIL) of 2.5%. The NHIL, like the VAT, is collected by the Ghana Revenue Authority. Combining the NHIL with the VAT effectively makes the VAT rate 17.5%.

The PA basically exempts upstream petroleum activities from VAT (both the 15.0% VAT and the 2.5% NHIL). However, VAT applies to goods and services supplied to companies that undertake petroleum activities. To effect the exemption, the Ghana Revenue Authority issues a VAT Relief Purchase Order (VRPO) to the petroleum company whose activities are VAT-exempt, so that it may "pay" for any VAT assessed on goods and services with the VRPO. This means that the petroleum entity is still charged VAT on supplies it receives, but it uses the VRPO instead of cash to pay the VAT element. Also, the petroleum entity does not charge VAT on its sales and transactions. However, the VRPO system is expected to be abolished and replaced with an effective refund mechanism. Under this system, the contractor shall be required to pay the tax and later apply for a refund of the taxes.

In general, exports of goods and services are zero-rated for VAT. This means that petroleum exports by a contractor attract VAT on exports at a zero rate.

Imports of equipment (machinery) and vessels are exempt from VAT. In addition, the sale of equipment (machinery, including items that constitute apparatus appliances and parts thereof) designed for use in the industry is exempt. The sale of crude oil and hydrocarbon products is also exempt.

An asset disposal is exempt from VAT if the asset is listed under the First Schedule of Ghana's VAT Act. However, if the asset is ordinarily subject to VAT, a disposal of the asset to an entity that is not a petroleum company is subject to VAT.

The VAT registration threshold is currently GHS200,000 (around US$45,455). Every person who earns or reasonably expects to earn revenue in excess of the threshold in a year, or a proportionate amount thereof in a quarter or in a month, is required to register for VAT.

Export duties

No export duties apply to the export of upstream petroleum products. Ghana does not usually charge duty on the export of goods. This is probably because the Government wants to encourage exports.

Stamp duties

The PA exempts upstream petroleum companies from the payment of stamp duties.

Registration fees

A variety of registration fees are payable at the local government level and to other governmental agencies.

I. Other

Government interest in production

The Government's approach is to take equity ownership of projects and to take the maximum equity limits agreeable to all parties involved.

In order to encourage prospecting and the development of oil and gas in Ghana, pioneer oil and gas corporate entities received very generous fiscal incentives. The GoG has become less and less generous following the oil find in 2007.

In relation to all exploration and development, the GNPC is expected to take (at no cost) at least 15% initial interest in petroleum operations. The GNPC has an interest in all exploration and development operations.

The GNPC also has the option to acquire an additional interest in every commercial petroleum discovery. However, in order to acquire the additional interest, the GNPC must notify the contractor within a specified period of time after the contractor's notice to the minister of the discovery. If the GNPC does not give the required notice, its interest shall remain as described above. If the GNPC decides to acquire the additional interest, it will be responsible for paying for its proportionate share in all future petroleum costs, including development and production costs approved by the joint management committee (JMC) (every PA signed by the GoG, GNPC and the petroleum contractor requires the establishment of a JMC to conduct and manage the petroleum operations).

Domestic production requirements

The GoG has a prescribed royalty from all petroleum and gas production. Presently, the royalty ranges from 5% to 12.5% of petroleum production; for gas, the royalty is 3%. The GoG can elect to take a cash settlement for its 3% and 5%–12.5% royalties, or it may have it settled with the supply of gas and crude petroleum, respectively. In addition to the 5%–12.5% royalty take in oil and the 3% in gas, the GoG (acting by GNPC through its equity interest) is expected to take at least 15% (10% to 12.5% for existing PAs under the old law) initial participating interest in oil and a 10% interest in gas or in their cash equivalents. Any additional interest that the Government has in petroleum production is taken in oil and/or gas or their cash equivalents.

Crude oil for domestic consumption is therefore expected to be met through the royalty and the Government's share in petroleum production. However, if domestic consumption exceeds the State's share of oil and gas, the GoG is expected to inform the other partners about the additional local need in advance as prescribed, and the contractor is expected to oblige and meet local production requirements. The State must pay for any additional supply required at the ruling market price.

Local content and local participation

Entities engaged in petroleum activities in Ghana are required to provide for local content and local participation in the conduct of their operations. In this regard, contractors, subcontractors, licensees and allied entities in the petroleum sector are required to establish local offices in their operational areas. They are also required to submit to the Petroleum Commission (PC) for approval a local content plan detailing, among other things, the consideration to be given to services that are produced locally, the employment of qualified Ghanaian personnel and the training of Ghanaians on the job. Entities are also required to submit to the PC an annual local content performance report within 45 days of the start of the year.

In addition, foreign companies that seek to provide services to the petroleum sector have to incorporate a joint venture company with an indigenous Ghanaian company. The indigenous Ghanaian company must hold at least 10% of the equity of the joint venture. Also, for an entity to qualify to enter into a PA or petroleum license, there must be at least a 5% interest held by an indigenous Ghanaian company other than the GNPC in the operations.

The Regulations were enacted on 20 November 2013 and came into force on 20 February 2014.

Recent changes in the sector

- Petroleum contractors are required to incorporate a company in Ghana.
- Written approval of the minister should be sought by a contractor before direct or indirect transfer of shares to a third party.
- Offset of VAT credit against corporate tax outstanding is possible.
- Contractors are obliged to meet domestic supply requirements (pro rata but not to exceed total entitlement).
- Contractors and subcontractors in petroleum operations are required to consider Ghanaian companies and operators first in awarding contracts.

Greece

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

Greece applies a concessionary regime for petroleum operations. Currently, there are two active licensing rounds for the exploration and exploitation of hydrocarbons offshore and onshore in Greece, the latter being regulated by the terms of a model lease agreement.

A. At a glance

- Income tax:
  - 20% and an additional 5% as a regional rate
- Surface rental fees:
  - Apply
- Royalties:
  - Linked to the so-called "R-factor"
- Signature bonus:
  - Biddable
- Production bonuses:
  - Biddable
- Training contributions:
  - Biddable, but at least €80,000 per year
- Production sharing:
  - None

B. Fiscal regime

Law 2289/95 (known as the Hydrocarbons Law) regulates the general principles of the fiscal regime applicable to lease agreements. The basic terms of the fiscal regime are included in the model lease agreement; nonetheless, further customized provisions may be included in each specific negotiated and signed lease agreement. The provisions of other tax laws that do not contradict the provisions of the lease agreement may also apply.

The companies that are concluding lease agreements are subject to a special income tax of 20% and to a regional tax of 5%, resulting in a total rate of 25%. The tax is imposed on net taxable income. The calculation of the net income is determined in the lease agreement.

Losses incurred prior to the commencement of commercial production are carried forward without any time restrictions. After the commencement of commercial production, the general income tax provisions apply in relation to the carryforward of losses (currently, tax losses can be carried-forward for five years under those provisions).

The calculation of taxable income is ring-fenced in relation to each exploration or exploitation area. Nonetheless, special consolidation rules apply stipulating that up to 50% of the expenses incurred for exploration operations in one contract area may be included in the expenses of another contract area where the production of hydrocarbons has commenced.

A depreciation rate is calculated as a percentage ranging between 40% and 70% of the annually produced and saved hydrocarbons and by-products. The rate is unified for exploration and development costs. Moreover, the exact rate is biddable.

Surface rental fees

Surface rental fees, which are tax-deductible, apply at the following annual rates:

- €50 per square kilometer of contract area during the first exploration stage
- €100 per square kilometer of contract area during the second exploration stage
- €200 per square kilometer of contract area during the third exploration stage and any further extensions
- €1,000 per square kilometer of the exploitation area annually during all phases of the exploitation stage.

The above rates of surface rental fees may be reduced.

Royalties

Royalties are based on the so-called "R-factor," as set out in the table below. The R-factor is defined thus:

R = cumulative gross inflows ÷ cumulative total outflows

where calculation of the R-factor takes into consideration the consolidated results for the contract area. The exact royalty calculation procedure, involving deductible and nondeductible costs, should be set out in the lease agreement.

The R-factor sliding scale is predetermined, with the rates being biddable (although some minimum rates are also predetermined).

R-factor	Royalty rate
$R \leq 0.5$	Negotiable
$0.5 < R \leq 1$	Negotiable
$1 < R \leq 1.5$	Negotiable
$1.5 < R \leq 2$	Negotiable
$R > 2$	Negotiable

Royalty payments are tax-deductible.

Signature bonus

Signature bonus is biddable. No minimum bonus is determined in legislation or in the model lease agreement. The signature bonus is tax-deductible.

Production bonuses

Production bonuses are linked to daily production and are biddable. No minimum bonus is specified in Greek legislation or in the model lease agreement, nor are the number of production thresholds specified or limited.

Production bonuses are tax-deductible.

Training contributions

Contractors are required to contribute annually to training and the improvement of professional skills among the local staff, in accordance with the provisions of the Hydrocarbons Law. Annual training contributions are biddable and should be set out clearly at the exploration stage, after a commercial discovery is made, and when a certain (biddable) level of average daily production has been reached.

The minimum contribution amount is set at €80,000 per year. A contribution is tax-deductible.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

There are no separate tax laws or regulations in Greenland governing the oil and gas sector. Companies are therefore subject to the general Corporate Income Tax Act, with a few special rules for license holders, including regulations under licenses.

- Royalties — yes
- Bonuses — not applicable
- Production sharing contract (PSC) — not applicable
- Income tax rate — 30%[1]
- Capital allowances — E[2]
- Investment incentives — L[3]

B. Fiscal regime

Greenland tax-resident companies are subject to corporation tax on their worldwide profits, including chargeable gains, with credit for any creditable foreign taxes. The taxable income of companies is stated as their gross income net of operating expenses — i.e., expenses incurred during the year in acquiring, securing and maintaining the income. The tax assessment is based on the net income or loss, adjusted for tax-free income, nondeductible expenses, amortization and depreciation, and tax loss carryforwards.

The taxable income must be stated for one income year at a time. The income year generally corresponds to the calendar year. However, companies may, upon request to the tax authorities, be allowed to apply a staggered income year. The area covered, generally, is activities undertaken within Greenlandic territorial borders, its territorial sea or continental shelf area.

Foreign persons and companies that engage in hydrocarbon prospecting activities, exploration activities, exploitation of hydrocarbons and related

1 *Companies subject to full and limited tax liability (including companies subject to the Act on Mineral Resources) must pay tax at a rate of 30% on their round-off income plus a charge of 6% on that, which adds up to an effective tax rate of 31.8%. In practice, licensees do not pay the 6% tax charge and, thus, pay tax at a rate of 30%.*

2 *E: immediate write-off for exploration costs.*

3 *L: losses can be carried forward indefinitely.*

business, including constructing pipelines, providing supply services and transporting hydrocarbons by ship or pipeline, are in general subject to taxation in Greenland on the income from the time the activity is commenced in Greenland. If Greenland has entered into a double tax treaty with the country where the foreign person or company is a tax resident, the treaty may modify the Greenland tax liability.

Prospecting and exploration for mineral resources may be carried out by either a branch (considered a permanent establishment for tax purposes) or a company, whereas a license to exploit mineral resources can be granted only to public limited companies that are domiciled in Greenland, that exclusively carry out business under licenses granted pursuant to the Mineral Resources Act, and that are not taxed jointly with other companies. In addition, the company cannot be more thinly capitalized than the group to which it belongs; however, the company's debt-to-equity ratio may go as far as 2:1.

Furthermore, the licensee must command adequate technical knowledge and financial resources to carry out the exploitation activities in question. If the exploration for mineral resources has been carried out by a branch, it may be necessary to convert the branch into a public limited company in connection with the transition from exploration to exploitation activities (subject to a license granted for such activities).

Such conversion is generally considered a taxable transaction, and any gains arising in connection with the transfer are subject to tax. However, provided certain conditions are fulfilled, it is possible to transfer all assets and liabilities related to a Greenland branch operation to a new Greenland public limited liability company on a tax-exempt basis. One of the conditions that must be fulfilled is that the public limited company — in all relations — must succeed to the rights and obligations of the branch as far as the Corporate Income Tax Act and the Greenland Home Rule Act on tax administration are concerned.

Carry

Under the Mineral Resources Act, the publicly owned company NUNAOIL A/S must be part of an oil/gas license. Oil and gas companies undertaking oil and gas operations in Greenland will enter into a carry contract with NUNAOIL A/S according to which NUNAOIL A/S will participate in the license with a specified share (determined on a license-by-license basis). The contractor will provide financing and bear all the risks of exploration. However, upon commencement of development and exploitation activities, NUNAOIL A/S will assume its own costs.

Royalties

Under the current regime, a special surplus royalty regime applies to all licenses. Special conditions may be found in the licenses.

Ring-fencing and losses

As a general principle, expenses and tax losses on transactions related to Greenland oil and gas exploration and exploitation activities may not be offset against non-oil and non-gas-related taxable income. For example, exploration costs are deductible against the oil- and gas-related income only to the extent that the costs de facto have been used in an oil and gas business. The ring-fence principle does not follow from tax legislation but stems from the fact that a licensee may not carry out activities other than oil and gas activities.

Losses from a loss-making field may be offset against profits from a profitable field if all fields are held by the same legal entity.

No fiscal consolidation is possible between Greenlandic entities.

When a loss-making field is closed down, any tax loss carryforward from that field may be offset against a profitable field.

Shutdown provision

Upon the granting of a license for exploration for, and exploitation of, mineral resources, pursuant to the Mineral Resources Act, a plan must be drawn up detailing the licensee's obligations to remove installations, etc., upon termination of the activities and to clear out the areas concerned. Companies that have been granted an exploitation license pursuant to the Act may, in their statement of taxable income, deduct any amounts set aside to ensure that an approved shutdown plan can be implemented. The right to deduct such amounts presupposes that the terms relating to security, etc., stipulated in the license are fulfilled.

Tax consolidation

Joint taxation and other forms of tax consolidation are, in general, not allowed in Greenland. However, companies granted a license to explore for mineral resources in Greenland pursuant to the Mineral Resources Act are allowed to compute their taxable income on an aggregate basis if, for instance, they have more than one permanent establishment at the same time or carry on other activity that is subject to limited tax liability.

Functional currency

Taxpayers must calculate their taxable income in Danish krone (DKK).

Transfer pricing

Transactions between affiliated entities must be determined on an arm's-length basis. In addition, Greenland companies and Greenland permanent establishments must report summary information about transactions with affiliated companies when filing their tax returns.

Greenland tax law requires entities to prepare and maintain written transfer pricing documentation for transactions that are not considered insignificant. The documentation does not routinely need to be filed with the tax authorities but, on request, it must be filed within 60 days.

A fine is set as a minimum penalty corresponding to twice the expenses (e.g., internal staff costs and fees to tax advisors) that have been saved by not having drawn up, or having partially omitted to draw up, transfer pricing documentation. In addition, if the income is increased because the arm's-length criterion is not met, the minimum penalty can be increased by an amount corresponding to 10% of the increase.

Unconventional oil and gas

No special terms apply for unconventional oil or unconventional gas.

C. Capital allowances

Depreciation

An acquired license right may be amortized on a straight-line restricted basis over a 10-year period. Licenses with a remaining term shorter than 10 years at the time of acquisition are amortized at a rate resulting in equal annual amounts over the remaining term.

The main rule is that fixed assets (e.g., machinery or production equipment) may be depreciated according to the reducing-balance method by up to 30% a year. Included are fixed onshore plant, etc., fixed and mobile platforms and associated equipment and machinery, pipelines, pumps, storage tanks and other equipment, and any independent accommodation platforms.

To prevent speculative trading in companies with unutilized depreciation allowances, the Greenland tax rules state that where a company provides for depreciation at rates below 30%, the company's depreciation balance is reduced to the amount to which the company's assets could have been depreciated in the following cases:

- Thirty percent or more of the share capital is owned by other shareholders or owners at the end of the income year compared with the beginning of the income year.
- The distribution of shares or voting rights in the company changes significantly during the income year, as compared with the distribution in the previous income year.

- The company's activities change significantly during the income year, as compared with the activities in the previous income year.
- The company is a party to a merger, a demerger or a similar reconstruction.

A "significant change" in relation to the distribution of shares or voting rights is, as a general rule, defined as a change of 30% or more. In relation to the company's activities, a "significant change" takes place if 30% or more of the company's income or net profit in the income year in question stems from other activities as compared with the company's income in the preceding income year.

Exploration costs

All costs related to oil and gas exploration in Greenland are allowed as a deduction for the purposes of the statement of taxable income.

D. Incentives

Tax losses

Tax losses may be carried forward indefinitely. However, there is a requirement that there is no significant change of ownership during an income year. The right to carryforward tax losses may be restricted in connection with a significant change in the company's ownership structure or activities.

Losses are forfeited if the composition of the group of shareholders is "significantly changed." A group of shareholders is deemed to have been "significantly changed" where more than one-third of the capital has changed hands. This is established by comparing the group of shareholders at the beginning of the income year showing a loss with the group of shareholders at the end of the income year in which the company wishes to deduct the loss.

Tax exemption

The Greenland tax authorities may exempt companies with a license to exploit mineral resources from taxation if this is stipulated in the license granted to the licensee.

E. Withholding taxes

Greenland companies paying dividends and royalties must withhold tax at source. Greenland distributing companies must withhold dividend tax at the rate fixed by the tax municipality of the company in question (currently 36% to 44%). Dividend tax is a final tax that must be withheld only on declared dividends. Companies with a license to explore for and exploit hydrocarbons and minerals pay withholding tax on dividends at a rate of 36%.

Royalty tax at a rate of 30% must be withheld on royalty payments to foreign companies.

Dividend and royalty tax may be reduced or eliminated under an income tax convention if the receiving company is able to document that it is domiciled in a foreign state with which Greenland has concluded such a convention. However, as long as dividends are deductible in the CIT income statement for the distributing company, a reduction of the WHT rate is not achievable.

Under Greenland law, interest and capital gains are not subject to tax at source.

Branch remittance tax

Branch remittance tax is not applicable in Greenland.

Income tax withholding and reporting obligations

A foreign company that is engaged in oil and gas exploration or exploitation activities in Greenland is required to withhold income tax from salaries paid to nonresident employees working in Greenland. If Greenland has entered into a double tax treaty with the country where the foreign company is a tax resident, the treaty may modify the Greenland tax liability.

Withholding and the payment of taxes withheld are required monthly, and reports must be filed with the Greenland tax administration on an annual basis.

F. Financing considerations

Interest expenses

Interest expenses and capital losses (e.g., due to foreign exchange) on debts incurred for financing oil and gas exploration and exploitation in Greenland are allowed as a deduction against the tax base. The interest or loss must be related to the Greenland oil and gas activity.

However, a branch of a foreign company cannot deduct interest on loans from its principal (the head office); there must be an "outside" lender (e.g., a sister company).

Capital losses are generally deductible according to the realization principle, but it is possible to opt for the mark-to-market principle on currency fluctuations.

Debt-to-equity limitation

Under the thin capitalization rules, interest paid and capital losses realized by a Greenland company or by a branch of a foreign group company are partly deductible, to the extent that the Greenland company's debt-to-equity ratio exceeds 2:1 at the end of the debtor's income year and the amount of controlled debt exceeds DKK5 million. Denied deductibility applies exclusively to interest expenses related to the part of the controlled debt that needs to be converted to equity in order to satisfy the debt-to-equity ratio of 2:1 (a minimum of 33.3% equity).

The thin capitalization rules also apply to third-party debt if the third party has received guarantees or similar assistance from a foreign group company.

Greenland tax law does not re-characterize or impose withholding tax on the disallowed interest.

G. Transactions

Asset disposals

The disposal of assets is a taxable event; gains and losses are generally taxable or deductible for tax purposes. Provided certain conditions are fulfilled, it may be possible to transfer assets and liabilities on a tax-exempt basis (see Section B above).

Transfers of license interests

All transfers of licenses (including farm-ins and farmouts) require approval from the Greenland Bureau of Minerals and Petroleum.

It is common in the Greenland oil and gas business for entities to enter into farm-in and farmout arrangements. However, the tax consequences of each farm-in or farmout must be considered on a case-by-case basis, depending on how the agreement is structured.

Provided certain conditions are fulfilled, it is possible to farmout (i.e., transfer part of a license to another company in return for the other company's defrayment of part of the exploration costs, to be paid by the seller regarding their remaining interest) a license on a tax-exempt basis for the farmer. The company farming in can deduct its share of the exploration costs against its taxable income.

Intragroup transfers are not covered by the Greenland farm-out provisions, so it applies only to the transfer of license interest to independent third parties.

Selling shares in a company

Gains and losses arising from the disposal of shares are included in taxable income irrespective of the percentage interest and period of ownership.

H. Indirect taxes

In Greenland, there is no general value-added tax (VAT) system and hence no sales tax. Also, in general, there are no energy taxes or similar. However, for a number of specific products, such as motor vehicles, meat products, alcohol and cigarettes, there are import duties.

I. Other

Business presence

Forms of business presence in Greenland typically include companies, foreign branches and joint ventures (incorporated and unincorporated). In addition to commercial considerations, it is important to consider the tax consequences of each form when setting up a business in Greenland.

Unincorporated joint ventures are commonly used by companies in the exploration and development of oil and gas projects.

Tax treaty protection

In general, oil and gas activities constitute a permanent establishment under most tax treaties; thus, treaty protection cannot generally be expected for a foreign company. For individual income tax liability, tax treaty provisions vary from country to country, and protection against Greenland taxation may be available in specific cases.

Tax returns and tax assessment

Foreign companies subject to limited tax liability and Greenland domestic limited liability companies must submit an annual tax return to the Greenland tax authorities. Tax returns must be prepared and filed with the Greenland tax authorities no later than 15 June in the income year following the income year it concerns, provided:

1. The tax return is submitted electronically through www.aka.gl;
2. Tax authorities have not carried out a discretionary tax assessment of taxable income last year

If any of the above conditions cannot be fulfilled, the deadline for submission is 1 May in the income year following the income year it concerns.

Tax is due 10 months and 20 days after the end of the income year.

Guinea

Country code 224

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Tax regime applied to this country

☐ **Concession** ☐ Royalties ☐ Profit-based special taxes ☐ Corporate income tax	■ **Production sharing contracts** ☐ **Service contract**

The fiscal system applied in Guinea is based on the General Tax Code, Petroleum Code and Petroleum Agreements (in the form of production sharing contracts (PSCs)). The fiscal terms are defined both in the PSCs and in applicable legislation. For the PSC template, the Guinea Petroleum Code refers to the model agreements used in international practice.

A new Guinean Petroleum Code, introduced by Law L/2014/034/AN dated 23 December 2014, entered into force on 1 January 2015, replacing Presidential Order 119/PRG/86 that issued the 1986 Petroleum Code. The new Petroleum Code is applicable to all oil contracts that will be signed from the date of the code's promulgation. Stabilization provisions contained in previous agreements may apply for existing oil operations. "Oil contracts" means contracts executed by the State or a national company with one or more qualified contractors to conduct hydrocarbon exploration and exploitation on an exclusive basis.

Oil contracts are generally signed after a bidding round. However, based on national interest, oil contracts can also be signed after direct negotiations in derogation of the bidding principle. The derogation is issued via a presidential decree, upon a proposal from the government ministry in charge of the oil sector.

A. At a glance

- Bonus — applies
- Surface rentals — applies
- Royalties — applies; rate is negotiated in oil contracts
- Corporate income tax (CIT) rate — 35% (was 50% under previous petroleum code)
- Production sharing — whether biddable or negotiable contract, the taxation related to oil and gas activities is put in writing in the production-sharing contract.

B. Fiscal regime

Guinea income tax regime

Income tax is levied on resident and nonresident companies. Resident companies are those incorporated under Guinea law, or those incorporated under foreign law and having a permanent establishment (PE) in Guinea.

Nonresident companies are deemed to derive income from a PE in Guinea if they derive income from, among other activities, the exploration and exploitation of natural resources, such as oil and gas.

In principle, all expenses incurred with respect to the conducting of petroleum operations are deductible. However, if expenses exceed normal arm's-length charges and are incurred directly or indirectly for the benefit of shareholders or related companies, the excess is considered to be nondeductible.

Royalties

The contractor is obliged to pay royalty as a percentage of gross production. The royalty rates are not established in the Petroleum Code, but rather defined in oil contracts. Royalty of 10% is typical.

Cost recovery

In the Petroleum Code the share of total annual production to be allocated to the recovery of petroleum costs is set at a maximum of 60% for crude oil and 65% for deposits of natural gas. Details for the recovery are left to be defined by the oil contract.

Unrecovered costs can be carried forward indefinitely within the duration of the contract.

Production profit sharing

The production remaining after royalties and cost recovery is treated as "profit oil," to be further split between the Government and the contractor.

The production profit split mechanism is not stipulated in the legislation and should be provided for in the oil contract. Information about oil contracts concluded so far suggests that the production split is linked to daily production.

The oil contract can provide that the Government's share of oil includes the contractor's corporate income tax.

Ring fencing

Each oil contract or oil interest must be reflected in a separate profit-and-loss account for the computation of CIT. A company cannot consolidate different oil contracts for tax purposes.

Surface rentals

Surface rentals are payable and should be defined via the oil contract. For the calculation of the CIT, the rentals are not deductible and are not deemed a recoverable petroleum cost.

Bonuses

Signing bonuses can be provided by the oil contract. Bonuses are neither deductible expenses nor a cost-recoverable petroleum cost.

Annual contribution toward training and industry promotion

The oil companies are subject to an annual contribution for the training of Government personnel and the promotion of the oil sector. The contributions and conditions of recovery should be stipulated in the oil contracts. The contribution is considered as a deductible expense for the calculation of the CIT as well as a recoverable petroleum cost.

Unconventional oil and gas

No special terms apply for unconventional oil or unconventional gas.

Foreign subcontractors' fiscal regime

The new Petroleum Code has implemented a simplified taxation system applicable for oil contract subcontractors with no PE in Guinea, in which the subcontractors have signed a services contract (relating specifically to oil and gas operations) with the contractor or the contractor's direct subcontractors for a maximum period of 12 months. Qualification for the simplified system requires subcontractors to obtain prior approval from the Guinean tax authorities.

The simplified regime provides that the eligible subcontractors are subject to a lump-sum tax payment at the rate of 10% of the respective turnover. The lump-sum tax is withheld directly by the contractor at the time of payment of the invoice, and it is paid to the tax authorities not later than the 15th day of the month following the payment of the invoice.

In addition to benefitting from the simplified taxation system, eligible subcontractors may also benefit from the taxation regime and the exemptions usually granted to contractors as a result of the new Petroleum Code.

Incentives

An oil contractor and its foreign subcontractors with no PE in Guinea are each entitled to the following exemptions unless otherwise provided by the oil contract:

- Withholding tax on dividends and on interest on loans
- Business license tax
- Single land tax for buildings allocated to oil operations
- Registration and stamps fees

It should also be noted that the material, machinery, equipment, engines, vehicles, spare parts and consumables intended for use in oil activities can be imported either without duty paid or via a suspension regime if they are to be exported after being used in Guinea. The listed goods should be included in an application sent to the customs authority prior to the commencement of exploration.

VAT

Under the previous code, oil companies were exempt from the payment of any tax on turnover relating to oil operations. The new Petroleum Code extends value-added tax (VAT) liability to oil companies at the standard rate (currently 18%).

Major transactions are taxed as follows:

- Exports of hydrocarbons are subject to VAT at the rate of 0%.
- Local purchases of goods and services are subject to VAT.
- Imports are subject to VAT, either at the standard rate or with temporary VAT suspension.
- Input VAT on local purchases and imports is refundable, with prior verification by the tax authorities, within 90 days following the application for a refund made in accordance with the regulations in force.

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Tax regime applied to this country

☐ **Concession** ■ Royalties ☐ Profit-based special taxes ☐ Corporate income tax	■ **Production sharing contracts** ☐ **Service contract**

A. At a glance

Fiscal regime

Companies engaged in upstream operations in Guyana are principally governed by the Petroleum Act, the Petroleum (Production) Act, Petroleum (Exploration and Production) Act, Maritime Zones Act, Income Tax Act (ITA) and Corporation Tax Act (CTA). In summary, the following taxes, levies and imposts apply to companies engaged in the exploration and production of oil and gas:

- Royalties — the applicable rate varies and is dependent on the particular agreement with the Government of Guyana (see Section B)
- Corporation tax — (see Sections B, C and D)
- Capital gains tax — (see Section E)
- Indirect taxes — (see Section H)

B. Fiscal regime

Upstream

Generally, commercial companies[1] or companies engaged in commercial activities are taxed at the rate of 40% of chargeable income or 2% of turnover, whichever is lower.[2,3] Noncommercial companies or companies engaged in noncommercial activities are taxed at the rate of 27.5%.[4] Entities engaged in both commercial and noncommercial activities are taxed at 40% on their commercial activities and 27.5% on their noncommercial activities. Entities engaged in petroleum operations would ordinarily be taxed as noncommercial companies at the rate of 27.5%.

Companies engaged in upstream operations in Guyana are principally governed by the Petroleum (Exploration and Production Act, the CTA, ITA and the terms of any Petroleum Agreement (PA).

1 *A commercial company is a company in which at least 75% of its gross income is from trading in goods not manufactured by it and is defined to include banks and insurance companies carrying on other than long-term insurance business.*

2 *Effective 1 January 2017.*

3 *Telephone companies are subject to corporation tax in Guyana at a rate of 45%.*

4 *Effective 1 January 2017.*

An entity engaged in the business of exploring for, and the winning of, petroleum in its natural state from the underground reservoir in Guyana, on land or in a marine area, must do so under a prospecting and/or a production license (license) as well as the terms of any applicable PA.

Generally, there are no provisions that specify that businesses operating under a license must be consolidated for tax purposes. However, those conducted under a PA are ring-fenced, as separate PAs are ordinarily issued with respect to discovery blocks with specific tax provisions applicable thereto.

PAs may mandate that the Government of Guyana settles the contractor's income tax liabilities out of the Government's share of profit oil or profit gas.

Corporation tax

The CTA provides that corporation tax is payable each financial year on the profits or gains (or amounts deemed to be profits or gains) of any person accruing in or derived from Guyana or elsewhere, whether received in Guyana or not. Corporation tax is assessed on an annual basis, and the corporation tax return is due on or before 30 April of the year following the year of income. Taxes are due and payable quarterly (i.e., 15 March, 15 June, 15 September and 15 December each year) with the balance of tax payable at the time of filing the return. Expenses that are wholly and exclusively incurred in the production of income are deductible in arriving at the chargeable income for corporation tax purposes, except where specific provisions govern the treatment of expenditures. Restrictions or limitations apply to the deductibility of certain expenses. For instance, the deductibility of head office expenses paid to related-party nonresidents of Guyana is restricted to a maximum of 1% of sales or gross income of the entity. In arriving at the chargeable income for corporation tax purposes, in addition to expenses wholly and exclusively incurred in the production of income, accumulated tax losses and certain allowances are also available (see Sections D and C, respectively).

Royalties

Every exploration and production licensee and PA must pay a royalty at a rate stipulated in the license in respect of the petroleum obtained in the production area. The amount of the royalty is ordinarily stipulated in the relevant license and PA. Royalties are deductible when paid.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Allowances

In arriving at the chargeable income for corporation tax purposes, a petroleum capital expenditure allowance may be claimed that allows a deduction at the rate of 20% of the petroleum capital expenditure on a straight-line basis. This allowance may be claimed from the first year of production.

Petroleum capital expenditure includes certain expenditures incurred in searching for and discovering petroleum and ascertaining and testing the extent and characteristics thereof, expenditures incurred in the acquisition of a petroleum license or a participating interest in a petroleum license, the provision of machinery or the acquisition of rights to use machinery in petroleum operations, and costs incurred in preparing a site for petroleum production, among other costs.

D. Set off of losses

Corporation tax losses that cannot be wholly offset against income for the same year may be carried forward and offset against income from succeeding years, without restriction. No loss carrybacks are allowed. Carried forward corporation tax losses can be carried forward only for corporation tax purposes. Note that there are no provisions for group relief.

Capital gains tax losses may be carried forward for 24 years.

E. Capital gains

The taxation of capital gains is dealt with under the Capital Gains Tax Act, the ITA and the CTA. Corporation tax is applied on gains arising on the disposal of assets within 12 months of the date of disposal. Capital gains tax is payable at the rate of 20% on the net chargeable gain of a person accruing in Guyana or elsewhere, whether received in Guyana or not, and on the change of ownership of property, subject to certain exceptions. If an exemption from property tax is granted to an entity undertaking petroleum operations, there would be a concomitant exemption from capital gains tax.

F. Withholding taxes

Withholding tax (WHT) is levied at source on distributions and on payments made to nonresidents (if the person or company is not engaged in trade or business in Guyana).

The term "payment" is defined as a payment without any deductions whatsoever, other than a distribution, with respect to interest, discounts, annuities or other annual or periodic payments, rentals, royalties, management charges, or charges for the provision of personal services and technical and managerial skills, premiums (other than premiums paid to insurance companies and contributions to pension funds and schemes), commissions, fees and licenses, and any other such payments as may from time to time be prescribed.

In summary, WHT is levied if all of the following conditions are met:

- A payment, as defined in the ITA, is made.
- The payment is made to a nonresident of Guyana.
- The nonresident is not engaged in trade or business in Guyana.
- The payment is deemed to arise in Guyana.

The applicable rate of WHT with regard to payments is 20%. The applicable rate of WHT on distributions made is also 20%. However, if there is a double taxation agreement in force, the rate of WHT is the lower rate provided in the treaty, if applicable.

Advanced corporation tax

In the case of a non-resident company that is engaged in trade/business in Guyana, there is an advanced Withholding Tax of 10%, which is creditable against the Corporation Tax liability. Further, the GRA has taken the position that an advanced Withholding Tax applies to gross amounts paid to resident companies in respect of the provision of goods and services at the rate of 2%, which is creditable against the Corporation Tax liability.

Branch operations

In addition to the taxes outlined above, an external company (i.e., branch of a nonresident company) that carries on a trade or business in Guyana is liable for WHT at the rate of 20% on the deemed distribution of profits to its head office.

Double tax relief

If it is established that WHT applies under domestic legislation, the provisions of an applicable double tax treaty may provide relief from the domestic provision. The Government of Guyana has successfully negotiated double tax arrangements that seek to provide, among other things, relief from double taxation.

The Government of Guyana has entered into tax treaties with Canada and the United Kingdom. In addition, a multilateral arrangement (the CARICOM Treaty) has also been entered into with the following members of CARICOM: Antigua and Barbuda, Barbados, Belize, Dominica, Grenada, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, and Trinidad and Tobago.

Unilateral relief

A credit is available to residents for foreign taxes paid on foreign-sourced income.

G. Financing considerations

Investment income

Interest received on bank deposits and certificates of deposit held at financial institutions in Guyana as well as interest on bonds and similar instruments are taxable.

Dividends received from nonresident companies paid from profits not derived from or accruing in Guyana are subject to tax. Dividends received by resident companies from other resident companies are tax-exempt.

Foreign-exchange controls

Guyana has a floating exchange rate regime. While exchange controls have been largely abolished, certain dealings in foreign currency continue to be regulated. For example, the permission of the Minister of Finance must be obtained in order for a person to lend or borrow foreign currency in Guyana. Further, permission must be obtained in order to operate a foreign currency account. However, profits may be repatriated without the approval of the Bank of Guyana. It should be noted that concessions may be available in relation to the applicability of exchange controls in the petroleum sector.

Debt-to-equity rules (thin capitalization)

In general, no thin capitalization rules apply in Guyana. However, if a local company pays or accrues interest on securities issued to a nonresident company and if the local company is a subsidiary of, or a fellow subsidiary in relation to, the nonresident company, the interest is treated as a distribution and may not be claimed as a deduction against the profits of the local company.

H. Indirect taxes

Value-added tax (VAT)

VAT is applicable on the entry of goods imported into Guyana, on the importation of services into Guyana under the reverse charge mechanism and on the taxable supply of goods or services by a registered person in Guyana.

The tax rate is 14%,[5] except in the case of an entry or a supply that is zero-rated. It should be noted that concessions may be available in respect of the applicability of VAT in the petroleum sector.

Companies and other businesses are required to register for VAT if their turnover exceeds GYD15,000,000[6] for a 12-month period. A company that is registered for VAT may recover any input VAT incurred in relation to the making of its taxable supplies.

Property tax

Property tax is payable in Guyana on the net property of a company in excess of GYD10,000,000. The tax is payable on the amount by which the aggregate value of all movable and immovable property of a person exceeds the aggregate value of all debts owed. However, a company registered or carrying on business in Guyana with net property valuing GYD500,000 or more must file a property tax return and pay property tax accordingly. Property tax returns must be filed and tax paid on 30 April of the year of assessment.

5 *Effective 1 February 2017.*

6 *Effective 1 February 2017.*

The property tax rates are as follows:

Net property value	Rate of property tax applicable (%)
On the first GYD10m of net property	Nil
For every dollar of the next GYD15m of net property	1/2%
For every dollar of the remainder of net property	3/4%

Note that an Order under the Petroleum (Exploration and Production) Act as well as the provisions of a PA may provide for an exemption from property tax that may otherwise be applicable to an entity undertaking petroleum operations.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

- General corporate income tax (CIT) — 20%
- Production levy — D, 5%
- Special hydrocarbon tax — E, progressive

B. Fiscal regime

Exploration for oil and gas in Icelandic waters is regulated by Act No. 13/2001 on prospecting, exploration and production (E&P) of hydrocarbons (the Hydrocarbons Act). Accompanying the Act are Regulation No. 884/2011 and Regulation No. 39/2009. The Act applies to the Icelandic territorial sea and exclusive economic zone, together with the Icelandic continental shelf. In addition, the Agreement on the Continental Shelf Between Iceland and Jan Mayen of 22 October 1981 between Norway and Iceland, the Agreement of 3 November 2008 between Norway and Iceland concerning transboundary hydrocarbon deposits, and the Agreed Minutes of 3 November 2008, concerning the Right of Participation pursuant to Articles 5 and 6 of the Agreement from 1981, apply to the relevant parts of the continental shelf between Iceland and Norway.

Petroleum activities are subject to general Icelandic laws and regulations on taxation, environmental protection, health and safety. Hydrocarbon accumulations are owned by the Icelandic state, and a license from the National Energy Authority (Orkustofnun, or NEA) is required for prospecting and E&P of hydrocarbons. The NEA is also responsible for monitoring hydrocarbon prospecting and E&P activities and for archiving the data generated by such activities. The NEA coordinates the response of Icelandic authorities to requests from oil companies for information regarding petroleum activities.

Iceland is a member of the European Economic Area. The European Union (EU) Directive on the conditions for granting and using authorizations for the prospecting and E&P of hydrocarbons (Directive 94/22/EC) and other relevant EU legislation therefore apply to petroleum activities in Icelandic waters.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. The scope and parties liable for taxation

Hydrocarbon extraction activities are subject to CIT of 20%, a production levy (see Section D) and a special hydrocarbon tax (see Section E).

Act No. 109/2011 on the taxation of hydrocarbon production extends the territorial scope of Icelandic CIT to all income derived from E&P and sales of hydrocarbons, including all derived activities such as transportation in pipelines or by ships and other work and services provided:

- In Iceland's territorial waters, its exclusive economic zone and on its continental shelf
- In the adjacent ocean region, where hydrocarbon resources extend across the center line with another state, when entitlement to the hydrocarbons falls to Iceland under an agreement with the other state
- Outside Iceland's territorial waters, exclusive economic zone and continental shelf where Iceland has the right to tax the activity and work in accordance with ordinary law or a special agreement with a foreign state

An obligation to pay taxes and levies lies with those parties that have received licenses for exploration or production of hydrocarbons, and also all other parties that participate, directly or indirectly, in the E&P and distribution of hydrocarbon products and other related activities. Thus, liability for taxation, in accordance with Act No. 90/2003 on income tax, rests with legal persons, self-employed individuals and wage earners who earn income through activities that take place in the areas listed above.

D. Production levy

A licensee who is liable for taxation must pay a special production levy of 5% of the value of the quantity of hydrocarbons that the licensee produces each year on the basis of its activities for which a license is required. "Production" refers to all the hydrocarbons that are delivered from the resource, including those destined for further processing and for the licensee's own use.

The value of the hydrocarbons is based on a reference price determined at the beginning of each month in respect of the month that has just passed. The reference price is based on the average price of hydrocarbons on a recognized international market trading in comparable hydrocarbon products, also taking into account the cost of sales and the point of delivery.

The production levy is a part of operational expenses and is therefore deductible for Icelandic corporate income tax and special hydrocarbon tax purposes.

E. Special hydrocarbon tax

Taxable licensees having income from exploration, production, distribution or sale of hydrocarbons, as well as other parties receiving a part of this income, are obliged to pay a special hydrocarbon tax.

The tax base for the special hydrocarbon tax for a taxable entity includes all operating revenue and capital gains, with certain costs restricted or excluded as set out in Section F. If sales of hydrocarbons during any period have been made at a price lower than the reference price for the production levy, the reference price is used when the tax base is calculated.

The tax rate of the special hydrocarbon tax is the company's profit rate multiplied by 0.45. The profit rate as a percentage is the ratio of the special hydrocarbon tax base to total income. For example, if a company's profit ratio is 40%, the special hydrocarbon tax rate is 18% (40% × 0.45). Special hydrocarbon tax is not deductible for CIT purposes.

F. Deductions from taxable income

When the base of the hydrocarbon tax is determined, certain restrictions are placed on deductions, as follows:

- Financial costs deducted from the year's income may not exceed 5% of the company's balance sheet liability position, less financial assets, including receivables and inventory, at the end of the relevant financial year.
- Financial costs shall include all interest costs, indexation adjustments, depreciation, and exchange rate gains or losses on the book value of liabilities, after interest earnings, indexation adjustments, depreciation and

exchange rate gains or losses on the book value of assets have been deducted from them. If such financial costs arise in connection with the acquisition of assets other than those that are used in the operations for which the license is required, they shall be divided in direct proportion to the outstanding balance of the depreciated value, for tax purposes, of all depreciable assets at the end of the year. That part of the financial costs that pertains to assets that are not used in connection with hydrocarbon production shall not be deductible from income when the tax base is determined.

- The minister may raise or lower the reference percentage, taking into account the currency used in the licensee's operations and financing, and the general rate of interest in the currency involved. When calculating this base, unpaid income tax or calculated unpaid hydrocarbon tax shall not be included among liabilities. The same shall apply to calculated tax commitments and tax credits arising from a permanent incongruity in the timing of the compilation of annual accounts and the payment of tax.
- Rent paid for structures or equipment used for exploration or extracting hydrocarbons, which exceeds normal depreciation and interest on the assets involved, based on the utilization time each year, may not be deducted from income. If equipment is rented by an associated party, the Icelandic tax authorities may disallow the entry of the rental as a cost item, unless the lessee submits information and other material demonstrating the cost price and accrued depreciation of the equipment in the ownership of the lessor, so that it is possible to establish that certain conditions have been met.
- The cost of the hire of labor may be deducted from income only if the work agency has registered itself in Iceland. Insurance fees, distribution costs and all service fees to related parties can be deducted from income only if the taxable entity can demonstrate that these costs are no higher than would apply in arm's-length transactions. In the year in which a production area is closed, 20% of operating income for the preceding year may be entered as income for that year.

In calculating the tax base for the special hydrocarbon tax, it is not permitted to deduct the following items:

- Losses incurred on sales of assets to related parties
- Any gifts or contributions to charities, cultural activities, political organizations or sports clubs
- Depreciation of receivables and inventories
- Losses or expenses in activities not covered by Act No. 109/2011, including places of business onshore
- Losses or expenses incurred by a taxable entity before the issuing of a license

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

India has a hybrid system of production sharing contracts (PSCs) containing elements of royalty, as well as sharing of production with the Government.

Royalties

Onshore areas:

- Crude oil – 12.5%
- Natural gas – 10%
- Coal bed methane – 10%

Shallow water offshore areas:

- Crude oil and natural gas – 10%

Deepwater offshore areas:

- Crude oil and natural gas – 5% for the first seven years of commercial production, and 10% thereafter

Bonuses:

- Crude oil and natural gas – none, as per the New Exploration Licensing Policy
- Coal bed methane – US$ 0.3million

Hydrocarbon Exploration Licensing Policy (HELP)

The Government of India has announced a new hydrocarbon exploration licensing policy, which offers a single license to explore conventional and unconventional oil and gas resources. Some of the features of the new policy are as follows:

- Single license for exploration and production of conventional as well as non-conventional hydrocarbon resources
- Open acreage policy providing for an option to select the exploration blocks without waiting for a formal bid round
- Revenue sharing model, which provides for a simple and easy-to-administer model (without cost recovery and micro-management by the government) and more operational freedom for an operator
- Pricing and marketing freedom, which is the major incentive for investors
- Exploration allowed throughout the contract period
- Increase in duration of exploration phase from 7 years to 8 years for onshore areas and from 8 years to 10 years for offshore areas
- Minimum regulatory burden for investors
- Reduced royalty rates for offshore areas as per the table below; for onshore areas, royalty has been kept unchanged, i.e., 12.5% for oil and 10% for gas

Blocks	Duration	Present royalty rates		HELP royalty rates	
		Oil	Gas	Oil	Gas
Shallow water	–	10%	10%	7.5%	7.5%
Deep water	First 7 years	5%	5%	0%	0%
	After 7 years	10%	10%	5%	5%
Ultra-deep water	First 7 years	5%	5%	0%	0%
	After 7 years	10%	10%	2%	2%

Income tax:

- Domestic companies:
  - Where the total turnover of the company in financial year 2016–17 does not exceed INR2,500 million – applicable tax rate shall be 25%[1]
  - Else the applicable rate shall be 30%[1]
- Foreign companies – 40%[1]
- Resource rent tax – none
- Capital allowances – D, E[2]
- Investment incentives – TH, RD[3]

B. Fiscal regime

India has a hybrid system of PSCs containing elements of royalty, as well as the sharing of production with the Government.

Companies enter into a PSC with the Government of India to undertake exploration and production (E&P) activities. Income from E&P operations is taxable on a net income basis (i.e., gross revenue less allowable expenses). Special allowances are permitted to E&P companies (in addition to allowances permitted under the domestic tax laws) for:

1 *In addition, a surcharge of 7% on tax for a domestic company and 2% on tax for a foreign company must be paid if income of the company is in excess of INR10 million (surcharge applicable at the rate of 12% for a domestic company and 5% for a foreign company where the company income is in excess of INR100 million). Health and education levy of 4% on the tax and surcharge is also applicable.*

2 *D: accelerated depreciation; E: immediate write-off for exploration costs and the cost of permits first used in exploration.*

3 *TH: tax holiday; RD: research and development incentive.*

- Unfruitful or abortive exploration expenses with respect to any area surrendered prior to the beginning of commercial production; after the beginning of commercial production; expenditure incurred, whether before or after such commercial production, with respect to drilling or exploration activities or services or with respect to physical assets used in that connection
- Depletion of mineral oil in the mining area post-commercial production

Domestic companies are subject to tax at a rate of 30%/25% and foreign companies at a rate of 40%. In addition, a surcharge of 7% on tax for a domestic company and 2% on tax for a foreign company must be paid if income is in excess of INR10 million. The surcharge is applicable at the rate of 12% on tax for a domestic company and 5% on tax for a foreign company if the company income is in excess of INR100 million. Health and education levy of 4% also applies.

The effective corporate tax rates are as given in the table below.

Domestic company			Foreign company		
For net income up to and including INR10 million	For net income exceeding INR10 million, up to INR100 million	For net income exceeding INR100 million	For net income up to and including INR10 million	For net income exceeding INR10 million, up to INR100 million	For net income exceeding INR100 million
31.2%	33.38%	34.94%	41.6%	42.43%	43.68%

Minimum alternate tax

Minimum alternate tax (MAT) applies to a company if the tax payable on its total income as computed under the tax laws is less than 18.5% of its book profits (i.e., accounting profits subject to certain adjustments). If MAT applies, tax would be computed at 18.5% of the company's book profits.

Credit for MAT paid by a company can be carried forward for 15 years, and it may be offset against income tax payable under domestic tax provisions. Due to the MAT regime, a company may be required to pay some tax, even during a tax holiday period.

Ring fencing

No ring fencing applies from a tax perspective. Thus, it is possible to offset the exploration costs of one block against the income arising from another block.

Treatment of exploration and development costs

All exploration and drilling costs are 100% tax-deductible. Such costs are aggregated until the year of commencement of commercial production.

They can be either fully claimed in the year of commercial production or amortized equally over a period of 10 years from the date of first commercial production.

Development costs (other than drilling expenditure) are allowable under the normal provisions of domestic tax law.

Production sharing contract regime

India has a hybrid system of PSCs containing elements of royalty, as well as the sharing of production with the Government. E&P companies (contractors) that are awarded exploration blocks enter into a PSC with the Government for undertaking the E&P of mineral oil. The PSC sets forth the rights and duties of the contractor.

The PSC regime is based on production value. Under the current regime, in PSCs for conventional crude oil and gas, the share of production for the Government is linked to profit petroleum (see later subsection below). However, the Government is considering replacing the payment system linked to profit petroleum with a production-linked payment system for future PSCs.

In case of coal bed methane (CBM) (i.e., unconventional natural gas), a production-linked payment system is followed.

Cost petroleum or cost oil

"Cost petroleum" is the portion of the total value of crude oil and natural gas produced (and saved) that is allocated toward recovery of costs. The costs that are eligible for cost recovery are:

- Exploration costs incurred before and after the commencement of commercial production
- Development costs incurred before and after the commencement of commercial production
- Production costs
- Royalties

The unrecovered portion of the costs can be carried forward to subsequent years until full cost recovery is achieved.

Profit petroleum or profit oil

"Profit petroleum" means the total value of crude oil and natural gas produced and saved, as reduced by cost petroleum. The profit petroleum share of the Government is biddable by the contractor as blocks are auctioned by the Government. The bids from companies are evaluated based on various parameters, including the share of profit percentage offered by the companies.

The law has placed no cap on expenditure recovery. The percentage of recovery of expense incurred in any year is as per the bids submitted by the companies. Furthermore, no uplift is available on recovered costs.

The costs that are not eligible for cost recovery[4] are as follows:

- Costs incurred before the effective date[5] including costs of preparation, signature or ratification of the PSC
- Expenses in relation to any financial transaction involving the negotiating, obtaining or securing funds for petroleum operations — for example, interest, commission, brokerage fees and exchange losses
- Marketing or transportation costs
- Expenditure incurred in obtaining, furnishing and maintaining guarantees under the contract
- Attorney's fees and other costs of arbitration proceedings
- Fines, interests and penalties imposed by courts
- Donations and contributions
- Expenditure on creating partnership or joint-venture arrangements
- Amounts paid for non-fulfillment of contractual obligations
- Costs incurred as a result of misconduct or negligence by the contractor
- Costs for financing and disposal of inventory

The PSC provides protection in case changes in Indian law result in a material change to the economic benefits accruing to the parties after the date of execution of the contract.

Royalties

- Land areas — payable at the rate of 12.5% for crude oil and 10% for natural gas and coal bed methane
- Shallow water offshore areas — payable at the rate of 10% for crude oil and natural gas
- Deepwater offshore areas (beyond 400m isobath) — payable at the rate of

4 *Without prejudice to their allowability under domestic tax laws.*

5 *"Effective date" means the date when the contract is executed by the parties or the date from which the license is made effective, whichever is later.*

5% for the first seven years of commercial production and thereafter at a rate of 10% for crude oil and natural gas

The wellhead value is calculated by deducting the marketing and transportation costs from the sale price of crude oil and natural gas.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Accelerated depreciation

Depreciation is calculated using the declining-balance method and is allowed on a class of assets. For field operations carried out by mineral oil concerns, the depreciation rate is 40% for specified assets,[6] while the generic rate of depreciation on the written-down basis is 15% (majority of the assets fall within the generic rate). Further, additional depreciation of 20% is available on the actual cost of new machinery or plant[7] in the first year.

Allowance for investment in new plant and machinery

In addition to depreciation and/or additional depreciation, where an undertaking set up in any of the notified backward states,[8] an additional deduction of 15% is also available on the actual cost of new machinery or plant acquired between 1 April 2015 and 31 March 2020.

D. Incentives

Tax holiday

A seven-year tax holiday equal to 100% of taxable profits is available for an undertaking engaged in the business of commercial production of mineral oil, natural gas or coal bed methane, or in the refining of mineral oil. The tax holiday is not available with respect to oil and gas blocks awarded after 31 March 2017; further, a tax holiday is not available for an undertaking that began refining after 31 March 2012.

A new tax exemption has also been introduced for foreign companies earning income on account of storage of oil in a specified facility in India and sale of crude oil to a person resident in India.

Such storage and sale by a foreign company should be pursuant to an agreement or arrangement approved by the Central Government of India. This new exemption shall be applicable with effect from 1 April 2016. This exemption has further been relaxed to include income accruing or arising from the sale of leftover stock of crude oil, if any, from a facility in India after the expiry of an agreement or an arrangement subject to such conditions as may be notified by the Central Government.

Carryforward losses

Business losses can be carried forward and set off against business income for eight consecutive years, provided the income tax return for the year of loss is filed on time. For closely held corporations, a 51% continuity-of-ownership test must also be satisfied.

Unabsorbed depreciation can be carried forward indefinitely.

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6 *Mineral oil concerns:*

(a) Plant used in field operations (above ground) distribution — returnable packages.

(b) Plant used in field operations (below ground), not including curbside pumps but including underground tanks and fittings used in field operations (distribution) by mineral oil concerns.

7 *Additional depreciation is permitted for all persons engaged in the business of manufacturing or producing any article or thing for new plant and machinery acquired after 31 March 2005.*

8 *States of Andhra Pradesh, Bihar, Telangana and West Bengal*

Research and development

Expenditures on scientific research incurred for the purposes of the business are tax-deductible.

Deduction for site restoration expenses

A special deduction is available for provisions made for site restoration expenses if the amount is deposited in a designated bank account. The deduction is the lower of the following amounts:

- The amount deposited in a separate bank account or "site restoration account"
- Twenty percent of the profits of the business of the relevant financial year

E. Withholding taxes

The following withholding tax (WHT) rates apply to payments made to domestic and foreign companies in India[9]:

Nature of income	Rate (%)	
	Domestic company	Foreign* company
Dividends**	0%	0%
Interest	10%	5%/20%***
Fees for professional or technical fees	10%	10%
Royalty	10%	10%
Nonresident contractor		Maximum 40%*****
Branch remittance tax	0%	

* The rates are to be further enhanced by the surcharge and education levy.

** Dividends paid by domestic companies are exempt from tax in the hands of the recipient. Domestic companies are required to pay dividend distribution tax (DDT) at 20.56% on dividends paid by them.

*** The rate of 20% generally applies to interest from foreign currency loans. Subject to fulfillment of certain conditions, a lower rate of 5% applies on interest payable for foreign currency loans. Other interest is subject to tax at the rate of 40% (plus applicable surcharge and education levy).

**** These rates have been reduced from 25% to 10% with effect from 1 April 2015.

***** Subject to treaty benefits. If a permanent establishment is constituted in India, the lower WHT rate depends on profitability.

For countries with which India has entered into a tax treaty, the WHT rate is the lower of the treaty rate and the rate under the domestic tax laws on outbound payments.

F. Financing considerations

Thin capitalization limits

There are no thin capitalization rules under the Indian tax regulations.

Under the exchange control regulations, commercial loans obtained by an Indian company from outside India are referred to as "external commercial borrowings" (ECBs). ECBs are generally permitted only for capital expansion purposes. However, subject to fulfillment of certain conditions, ECBs are permitted for general corporate purposes as well.

9 *In the absence of tax registration (PAN Number) in India, WHT rate is 20% (gross) or a rate prescribed in the table of WHT rates, whichever is the higher. However, if certain prescribed documents/information is provided, then the aforesaid tax rate of 20% shall not apply.*

ECBs can be raised from internationally recognized sources such as international banks, international capital markets and multilateral finance institutions, export credit agencies, suppliers of equipment, foreign collaborators, and foreign equity holders (subject to certain prescribed conditions, including debt-to-equity ratio).

Interest quarantining

Interest quarantining is possible, subject to the exact fact pattern.

G. Transactions

Asset disposals

A capital gain arising on transfer of capital assets (other than securities) situated in India is taxable in India (sale proceeds less cost of acquisition). Capital gains can be either long term (capital assets held for more than three years, except for listed securities where it is required to be held for more than one year and immovable property where it is required to be held for more than two years) or short term. The rate of capital gains tax (CGT) is as follows:

Particulars	Rate (%)[10,11]	
	Short-term capital gains	Long-term capital gains
Resident companies	30%	20%
Nonresidents	40%	20%

A short-term capital gain on transfer of depreciable assets is computed by deducting the declining-balance value of the classes of assets (including additions) from the sale proceeds.

Farm-in and farmout

No specific provision applies for the tax treatment of farm-in consideration, and its treatment is determined on the basis of general taxation principles and the provisions of the PSC. However, special provisions determine the taxability of farmout transactions in certain situations.

Selling shares in a company (consequences for resident and nonresident shareholders)

Listed securities on a stock exchange

Long-term capital gains arising from transfer of securities listed on a stock exchange shall be taxed at a concessional rate of 10% of such capital gains. Such capital gains tax shall be levied in excess of INR 1 lakh. This concessional rate of 10% will be applicable if securities transaction tax has been paid on both acquisition and transfer of such capital asset. Short-term capital gains are taxable at a reduced rate of 15%.

Transfer of listed securities outside a stock exchange

Long-term capital gains derived from the transfer of listed securities are taxed at the rate of 10% (without allowing for indexation adjustments), or at the rate of 20% with indexation benefits. Short-term capital gains are taxable at the rate of 30% for resident companies and 40% for nonresident companies.

10 *The rates are further enhanced by the applicable surcharge and education levy.*

11 *The cost of capital assets is adjusted for inflation (indexation) to arrive at the indexed cost, although the benefit of indexation is not available to nonresidents. The indexed cost is allowed as a deduction when computing any long-term capital gain.*

Unlisted securities

The CGT rate applicable to transfers of unlisted securities is as given in the table below.

Particulars	Rate (%)*	
	Short-term capital gains	Long-term capital gains
Resident companies	30%	20%
Nonresidents	40%	10%[12]

* The rates are to be further enhanced by the surcharge and education levy

H. Transfer pricing

The Income Tax Act includes detailed transfer pricing regulations. Under these regulations, income and expenses, including interest payments, with respect to international transactions[13] or specified domestic transactions[14] between two or more associated enterprises (including permanent establishments) must be determined using arm's-length prices (ALPs). The transfer pricing regulations also apply to cost-sharing arrangements.

The Act specifies methods for determining the ALP:

- Comparable uncontrolled price method
- Resale price method
- Cost plus method
- Profit split method
- Transactional net margin method
- Any other method prescribed by the Central Board of Direct Taxes (CBDT)

A revised range concept has been introduced by the CBDT for the purpose of arm's-length analysis and usage of multiple year data.

Use of multiple year data while carrying out transfer pricing analysis is permissible in certain circumstances for all methods except for the comparable uncontrolled price (CUP), profit split method (PSM) and other methods.[15]

A range concept would be used for all methods (depending on the facts) except for PSM and other methods. It will be applicable only if six or more comparable companies are available. If not, the arithmetic mean concept will continue to be used. The arm's-length range will consist of the values falling between the 35th and 65th percentile of the weighted average margins of comparable companies. For PSM and other methods, the arithmetic mean concept with a range would have to be used.

Further, the advance pricing agreement (APA) has been introduced with effect from 1 July 2012. The revenue authorities may enter into an APA with any person, determining the ALP or specifying the manner in which the ALP is to be determined in relation to an international transaction.

The APA rules provide an opportunity for taxpayers to opt for a unilateral, bilateral or multilateral APA. The APA can be valid for a maximum period of five years and requires payment of a specified fee to the Government. The APA

12 *This rate is applicable without allowing benefit of indexation or exchange fluctuation.*

13 *International transactions include transactions with unrelated parties (even if resident in India) as well as where a prior agreement exists or where the terms of the transaction are determined in substance between an unrelated party and any associated enterprises.*

14 *As specified in Section 92BA of the Income Tax Act, 1961, the specified domestic transactions are covered only if the aggregate of all such transactions in a tax year exceeds the sum of INR200 million (with effect from FY 2015–16, while from FY 2012–13 to FY 2014–15 was INR50 million).*

15 *Applicable for international/specified domestic transactions undertaken on or after 1 April 2014, i.e., from FY 2014–15.*

filing process includes a pre-filing submission, filing the APA request itself, negotiating the APA, execution and monitoring. Taxpayers are required to prepare and file an annual compliance report for each year under the APA, which is subject to a compliance audit by the tax authorities. The APA can be rolled back for a period of four years prior to the APA period as well.

In addition, safe harbors for certain classes of international transactions for eligible taxpayers have been prescribed for certain years. The taxpayer opting for safe harbor is required to make a claim for the same at the time of filing its tax return and for every year covered under the safe harbor. In addition, the taxpayer is also required to undertake the other regular compliances like preparation of transfer pricing documentation and the filing of an accountant's report.

The transfer pricing regulations require each person entering into an international transaction or specified domestic transactions to maintain prescribed documents and information regarding a transaction.

Each person entering into an international transaction or specified domestic transactions must arrange for an accountant to prepare a report and furnish it to the tax officer by the due date for filing the corporate tax return, which is 30 November. The non-maintenance of documentation or non-filing of an accountant's report attracts penalties. The due date for corporate tax return filing for taxpayers not subject to the transfer pricing provisions is 30 September.

A tax officer may make an adjustment with respect to an international transaction or specified domestic transactions, if the officer determines that certain conditions exist, including any of the following:

- The price is not at arm's length.
- The prescribed documents and information have not been maintained.
- The information or data on the basis of which the price was determined is not reliable.
- Information or documents requested by the tax officer have not been furnished.

Stringent penalties (up to 4% of transaction value) and USD1,500 (approximately) may be imposed for noncompliance with the procedural requirements. Additional penalties for understatement/concealment of profits/income or furnishing inaccurate particulars may be levied at the rate of 100%–300% of the tax that the transaction is seeking to evade.

Master file requirements

Additionally, from FY 2016–17 onward, a master file must be prepared and filed in India in case the following conditions are satisfied:

- Group consolidated turnover exceeds INR5 billion
- Value of "international transactions" as per books of accounts exceeds INR500 million (or INR100 million in case of intangible related transactions)

A master file for FY 2016–17 needs to be filed on or before 31 March 2018 (the due date for FY 2017–18 onward is the due date to file return of income, i.e., 30 November 2018 and so on).

Country-by-country reporting (CbCR) requirements

- Requirements same as recommended by the Organisation for Economic Co-operation and Development
- Applicable only if the foreign company has a permanent establishment in India
- Filing requirement only in exceptional cases (no obligation in parent company's jurisdiction, no mechanism for automatic exchange of CbCR in parent country/alternate reporting jurisdiction or systemic failure in exchange of CbCR — provided the same is notified by Indian tax authorities)

I. Indirect taxes

Indirect taxes are applicable to activities that range from manufacturing to final consumption, and include within their scope distribution, trading and imports, as well as services. Therefore, indirect taxes impact almost all transactions.

Indirect taxes in India have undergone a change since the introduction of the goods and service tax (GST) beginning in July 2017. GST consolidates all indirect tax levies into a single tax, except customs, replacing multiple tax levies such as excise duty, value-added tax, central sales tax, service tax, etc.

Customs duty

While GST has replaced various indirect taxes, customs duty will continue to be levied on import of goods into India and is payable by the importer. The customs duty on imports comprises the following:

- Basic customs duty (BCD)
- Integrated tax has replaced additional customs duty (ACD), which was levied in lieu of excise duty on goods manufactured in India
- Social welfare surcharge

However, it is to be noted that in case of import of petroleum crude, high-speed diesel, motor spirit (commonly known as petrol), natural gas and aviation turbine fuel, additional customs duty and special customs duty will be applicable as these products are kept outside the purview of GST regulations.

The rate of customs duty is based on the classification of imported goods. The classification is aligned to the Harmonized System of Nomenclature (HSN).

The rates of BCD vary across goods and range from 0% to 10%, except for certain specified items that attract higher rates.

Integrated GST is levied at a rate of 0%–28% depending upon the classification of goods.

Thus, the general effective customs duty rate for most imported products is 30.98% (excluding oil and natural gas). Further, certain exemptions or concessions are provided on the basis of classification, location or usage of the imported products.

The Government of India has entered into several free or preferential trade agreements with trade partners such as Thailand, Sri Lanka, the South Asian Association for Regional Cooperation (SAARC) countries, Singapore, and the Association of Southeast Asian Nations (ASEAN) countries. In order to promote trade-in terms, preferential tariff rates have been extended for certain identified goods traded with these countries. Similar trade agreements with the European Union and others are also currently being negotiated.

Subject to certain conditions, an importer using imported goods in the manufacture or supply of goods may obtain a credit for ACD and special additional customs duty (SACD). Further, subject to certain conditions, the credit of integrated GST would be available to the importer if the goods are used in the course or furtherance of business.

Further, up-front exemption/refund of SACD is available in cases where goods are imported for resale.

Notable issues for the oil and gas sector

Several concessions or exemptions have been provided for the import of goods for specified contracts for the exploration, development and production of petroleum goods. Further, concessions or exemptions have also been provided for the import of crude oil and other petroleum products.

Various concessions and exemptions are also available for the import of goods to be used in coal bed methane blocks, subject to the fulfillment of specified conditions.

The import of certain petroleum products attracts other customs duties in addition to the duties discussed above, such as additional duty on the import of motor spirit and high-speed diesel, and national calamity contingent duty on the import of crude oil.

Excise duty

Excise duty applies to the manufacture of high-speed diesel, motor spirit (commonly known as petrol), natural gas and aviation turbine fuel in India. The median rate of excise duty is 12.5%. Cess (earlier levied at the rate of 3%) has been exempted on all goods. Accordingly, the effective rate of excise duty on most products is 12.5%.

Excise duty is mostly levied as a percentage of the transaction value of goods. However, for certain goods, such as high-speed diesel and petrol, the excise duty is based on the quantity of goods.

The Cenvat Credit Rules of 2004 allow a manufacturer to obtain and use eligible credit of excise duty, ACD and special additional duty (SAD) on the procurement of goods and services toward payment of excise duty on manufactured goods subject to fulfilment of specified conditions.

Notable issues for the oil and gas sector

No excise duty is levied on the domestic production of crude oil, but it attracts national calamity contingent duty as well as an oil development levy. On certain petroleum products, excise duty is levied both on the basis of value and quantity. Certain petroleum products also attract other excise duties, such as additional duty (on motor spirit and high-speed diesel) and special additional excise duty (on motor spirit).

Cenvat credit is not available with respect to excise duty paid on motor spirit, light diesel oil and high-speed diesel oil used in the manufacture of goods.

Credit availed of excise duty paid on petroleum products cannot be availed for being set off against the GST liability.

Service tax

Service tax has been repealed with effect from 1 July 2017 and has been replaced by GST.

VAT or central sales tax

Value-added tax (VAT) or central sales tax (CST) is levied on the sale of goods. VAT is levied on the sale of goods within an individual state, i.e., where the goods move intra-state as a condition of sale, and CST is levied on a sale occasioning the movement of goods from one state to another.

VAT/CST is levied only on specified petroleum products with effect from 1 July 2017. VAT is levied at two prime rates of 5% and 12.5%–15%, under different VAT laws. CST is levied either at the rate of 2% (subject to the provision of declaration forms prescribed under the CST Act) or at a rate equivalent to the local VAT rate in the dispatching state.

A VAT- or CST-registered dealer is eligible for credit for the VAT paid on the procurement of goods from within the state and to utilize it toward payment of the VAT and CST liability on any sale of goods made by the dealer in that state. However, CST paid on procurement of goods from outside the state is not available as a credit against any VAT liability.

Notable issues for the oil and gas sector

Petroleum products — petrol, diesel, aviation turbine fuel, natural gas, etc. — are subject to VAT at higher rates, which range from 5% to 33% depending on the nature of product and the state where they are sold. VAT credit on petroleum products is generally not allowed as a credit against output tax liability, except in the case of the resale of such products. Petroleum products cannot be procured against Form C @2% CST for manufacture of products covered under GST.

GST

GST has been introduced with effect from 1 July 2017 and will replace central taxes such as service tax, excise and CST as well as state taxes such as VAT and entry tax.

GST is a dual tax, consisting of a central GST and a state GST. The tax would be levied concurrently by the center as well as the states — i.e., both goods and services would be subject to concurrent taxation by the center and the states. A person can claim credit of central GST on inputs and input services and offset it against output central GST. Similarly, credit of state GST can be set off against output state GST.

As per the GST Act, certain petroleum products (petroleum crude, high-speed diesel, petrol, natural gas and aviation turbine fuel) have been kept outside the realm of GST until a date to be determined by the GST Council. Until that date is confirmed, existing indirect taxes would continue to apply on petroleum products. This means that production/manufacture of petroleum products would continue to attract excise duty, as currently applied, and sale of these products would be subject to VAT/CST, as currently applied. The specified petroleum products would therefore be subject to the tax under the former regime on the output side and to the GST regime on the procurement side, with GST also applying to non-specified petroleum products. The availability of credit of input GST against output excise and VAT on specified petroleum products and vice versa is not available.

GST is a four-tier structure with effective rates at 5%, 12%, 18% and 28%. The applicable rates is based on the classification of the goods. The classification is aligned to the Harmonized System of Nomenclature (HSN).

Notable issues for the oil and gas sector

While the oil and natural gas sector has been kept outside the purview of GST regulation, other petroleum products (e.g., kerosene, naphtha, liquefied petroleum gas) are covered within the realm of GST. Through the partial coverage and partial exclusion, GST would be another addition to the complexities faced by oil and gas companies. Some of the well-known effects on the sector are:

- Reversal or non-eligibility of credits of the GST to the extent they are attributable to the manufacture and sale of excluded petroleum products; this results in a tax cost increase of 5% to 28% depending upon the nature of goods and services procured
- Adhering to compliances under the multiple tax regimes (i.e., the companies in the sector will have to comply with the existing tax regimes for the products excluded from GST, and, for the products covered under GST, they will have to comply with the GST regulations)

Current scenario

The oil and gas industry is pushing for the inclusion of excluded products in the GST regime. The industry has provided the Government with the following options:

- Including excluded products in the GST regime and stopping the levy of all other taxes
- Including excluded products at a nominal rate of 5% and continuing with all other taxes
- Including excluded products by notifying that the said products would be covered with the realm of "zero-rated supplies" and continue with all other taxes

Under the second and third options, the industry would be able to avail the input product related tax credits of GST paid on procurement of goods and services. However, the issue of complying with multiple tax regimes would continue.

J. Other

Tax regime for foreign hire companies

There is a special tax regime for foreign companies that are engaged in the business of providing services or facilities, or supplying plant or machinery for hire when it is used in connection with the prospecting, extraction or production of mineral oils.

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

The fiscal regime applicable to oil and gas companies consists of production sharing contracts (PSCs) that are entered into between contractors and the executive body for oil and gas upstream activities on behalf of the Indonesian Government. This was formerly BPMIGAS, but this body was disbanded following a decision by the Constitutional Court in late 2012 and has been replaced by an almost identical body with the name SKKMIGAS.[1] SKKMIGAS is under the authority of the Ministry of Energy and Mineral Resources (MEMR) in accordance with Presidential Decree No. 9 of 2013 dated 10 January 2013. SKKMIGAS has been assigned all of its predecessor's powers and responsibilities and has stated that existing PSCs will remain in force until their natural expiry date.

Most of the contractual arrangements between foreign oil and gas contractors and SKKMIGAS are in the form of a PSC. The other types of agreements between contractors and SKKMIGAS are joint operating contracts (JOCs), technical assistance agreements (TAAs) and enhanced oil recovery (EOR).

Fiscal regime

The principal features for the fiscal regime applicable to oil and gas companies are as follows:

- Corporate income tax (CIT) — tax rate depends on the PSC entered into; the current rate is 25%
- Branch profits tax (BPT) — current rate is 20%
- Royalties on production — none
- Bonuses — amount varies depending on PSC terms
- Resource rent tax — none
- Surface rent tax — none, but land and building tax applies
- Withholding tax:
  - Dividends — depends on the contract in force
  - Branch remittance — depends on the contract in force
  - Other withholding tax — follows general tax law
- Capital allowances — declining-balance depreciation
- Incentives – L[2]

1 *SKKMIGAS's full name translates as Interim Working Unit for Upstream Oil and Gas Business Activities.*

2 *L: ability to carry forward losses.*

Legal regime

The existing contractual arrangements between foreign oil and gas contractors and BPMIGAS are mainly in the form of a PSC. The other types of agreements between the contractors and BPMIGAS are joint operating contracts (JOCs), technical assistance agreements (TAAs) and enhanced oil recovery (EOR).

Article 33 of the 1945 Indonesian Constitution is the fundamental philosophy underlying the taxation of the oil and gas industry in Indonesia. It stipulates that "all the natural wealth on land and in the water is under the jurisdiction of the State and should be used for the greatest benefit and welfare of the people."

Law No. 8 of 1971 gave authority to a body named Pertamina (the predecessor to both BPMIGAS and SKKMIGAS) to administer, control and carry out mining operations in the field of oil, natural gas and geothermal energy. Subsequently, Law No. 22 of 2001 differentiated between upstream (exploration and exploitation) and downstream (refining, transport, storage and trading) activities, and caused them to be undertaken by separate legal entities. That law gave authority for the Government to establish BPMIGAS, an executive agency for upstream activities, and BPHMIGAS, a regulatory agency for downstream activities. At the same time, Pertamina was transformed from a state-owned enterprise into a state-owned limited liability company, PT Pertamina (Persero). PT Pertamina is now similar to other oil and gas companies in Indonesia, but it has the authority to supply for domestic consumption.

Previous contractual agreements entered into with the Indonesian Government have also changed and are now structured as cooperation contracts. The contractor may now enter into cooperation or service agreements under similar terms and conditions to those of the previous PSCs. Government Regulation (GR) 79/2010, issued 20 December 2010, which has been amended by GR 27/2017 on 19 June 2017 and in force from that date, provides rules on cost recovery claims and Indonesian tax relating to the oil and gas industry. As set out in GR27, the provisions will automatically apply to all new PSCs. However, existing PSCs (signed prior to 19 June 2017) will remain in force in accordance with their existing terms and conditions. Contractors will be able to elect whether or not they wish to remain subject to the provisions of their existing contract or, by no later than 19 December 2017, apply to adjust the terms of their contract to be in accordance with the provisions of GR 27.

Currently, the implementing regulation of GR 27 has not yet been issued. Hence, the several Minister of Finance regulations implementing GR 79/2010 in late 2011 still apply. Such regulations relate not only to the withholding of contractors' other income in the form of uplift or other similar compensation and/or contractor's income from the transfer of participating interest, but also to the thresholds of expatriates' remuneration costs.

B. Fiscal regime

General corporate tax rules

By regulation, each interest holder, including the operator of the work area, has to register with the Indonesian tax office from the moment it obtains an interest in the work area.

The income tax rates, consisting of CIT and dividend tax or BPT for branch operations, vary depending on the year the contract was entered into.

The contractor's taxable income is broadly calculated as gross income less tax deductions. The calculation embraces the "uniformity concept" as the basis for determining which costs are recoverable and which are tax-deductible. Under this concept, very broadly, costs that are recoverable are tax-deductible.

Ring fencing

The Government applies the tax ring-fencing rule, meaning that costs incurred by the contractor in one working interest are not allowed to be offset by income of another working area. As a result, an entity is likely to hold working interest in only one contract area.

GR 79/2010 and GR 27/2017 specifically also requires costs relating to gas activities and oil activities in the contract area to be separated, and it provides rules on how to offset and recover the costs from the different products.

There are no tax consolidations or other group relief facilities available in Indonesia.

General terms of a PSC

The general concept of the PSC is that contractors bear all risks and costs of exploration until production. If production does not proceed, these costs are not recoverable. If production does proceed, the contractor can receive the following:

- A share of production to meet its recoverable costs
- Investment credit (see below)
- An equity interest of the remaining production

Generally, the following points are included as part of a PSC agreement:

- Management responsibility rests with SKKMIGAS
- The contractor pays a bonus at the time the contract is signed, which, based on GR 79/2010 and GR 27/2017, is not cost recoverable and not tax-deductible
- The contractor agrees to a work program with minimum exploration expenditures for a 3- to 10-year period
- Exploration expenses are recoverable from only commercial production
- The contractor is reimbursed for the recoverable cost in the form of crude oil called cost oil
- The contractor's profit share oil is called equity oil and is taken in the form of crude oil
- The contractor has to settle its taxation obligations separately on a monthly basis

Relinquishment

Each PSC also stipulates the requirements for part of the working area to be relinquished during the exploration period. The PSCs can vary in the timing and percentage to be relinquished. Typically, 15% to 25% of the contract is relinquished after three years and 30% to 35% by the end of five years.

Calculation of equity oil and sharing of production

The following simplified example may serve to illustrate the amount of equity oil to be shared. Broadly, it is crude oil production in excess of the amounts received for first tranche production, cost recovery and investment credit, adjusted with the contractor obligation to supply a domestic market obligation (DMO), DMO fee and lifting price variance. These terms are further explained below.

First tranche petroleum

Usually, first tranche petroleum (FTP) is equal to 20% of the production each year (before any deduction for cost recovery) and is split between the government and the contractor according to their equity oil share as stipulated in the agreement with the Indonesian Government. FTP is taxable income.

On 14 November 2017, DGT issued a new regulation pertaining to calculation of First Tranche Petroleum (FTP) tax. The regulation is effective beginning in the November 2017 tax period. The regulation changed the FTP tax to be due when the accumulated Contractor's FTP share balance becomes higher than the accumulated unrecovered costs balance, calculated on a monthly basis, regardless of whether Equity to be Split (ETS) has been reached or not in the relevant month. Previously, the FTP was calculated only when the ETS had been reached.

Domestic market obligation

Broadly, after commencement of commercial production from the contract area, a contractor is required to supply a specific portion of the crude oil to the domestic market in Indonesia from its equity share. A DMO can also apply to gas production. The DMO is negotiated for each agreement and usually ranges from 15% to 25%. GR 79/2010 and GR 27/2017 requires that the DMO for oil and gas be 25% of production.

Usually, the quantity of DMO that is required to be supplied under the PSC will be limited by the quantity of equity oil or gas to which they are entitled. Any difference between the maximum DMO to be supplied and the DMO to be supplied based on the equity share will usually not be carried forward to subsequent years.

The compensation to be received for the DMO by the contractor is governed by the agreement signed with the Indonesian Government. Usually, the contractor is compensated by SKKMIGAS for the DMO at the prevailing market price for the initial five years of commercial production. The difference between the DMO costs and the DMO fee received is subject to tax.

Cost recovery

Cost recovery is usually stipulated in Exhibit C of the agreement with the Indonesian Government and is the reimbursement of PSC cost (through cost oil) prior to the determination of profit oil. GR 79/2010 and GR 27/2017 reconfirms the uniformity concept of operating expenses (i.e., costs that are recoverable are also deductible for tax purposes). The basic principles for operating expenses to be recoverable and tax-deductible are as follows:

- The costs are incurred in order to earn, collect and maintain income and have a direct connection with the operation of the production block of the respective contractor.
- The costs are at arm's length and are not influenced by a special relationship.
- The petroleum operation is conducted in accordance with accepted business and technical practice.
- The operation is in accordance with a work program and budget approved by the Indonesian regulatory body.

GR 79/2010 and GR 27/2017 provide that direct and indirect allocation of expenses from a company's head office can be charged only to an Indonesian project and is cost-recoverable and tax-deductible if certain conditions are met.GR 79/2010 and GR 27/2017 further define costs that cannot be claimed as recoverable or tax-deductible. Several items from the list of non-recoverable costs under GR 79/2010 have been removed and amended by GR 27/2017. In total, there are 22 items listed as non-recoverable and not tax-deductible.

Capital allowances

The depreciation and amortization of assets are usually stipulated in Exhibit C of the agreement with the Indonesian Government.

All equipment purchased by contractors becomes the property of SKKMIGAS once the equipment is in Indonesia. The contractors have the rights to use and depreciate such property until it is abandoned or for the life of the work area, subject to approval by SKKMIGAS.

Depreciation will be calculated at the beginning of the calendar year in which the asset is placed into service, with a full year's depreciation allowed for the initial calendar year. The method used to calculate each year's allowable recovery of capital costs is the declining-balance depreciation method.

An asset falls into one of three groups, and calculation of each year's allowance for recovery of capital costs should be based on the individual asset's capital cost at the beginning of that year multiplied by the depreciation factor as follows:

- Group 1 — 50%
- Group 2 — 25%
- Group 3 — 10%

The balance of unrecovered capital costs is eligible for full depreciation at the end of the individual asset's useful life.

GR 27/2017 allows the book value of fixed assets that are no longer used to be charged as operating cost.

GR 79/2010 and GR 27/2017 provide a list of assets, useful life and depreciation rates. The regulations again provide for a declining-balance depreciation method, but depreciation starts only from the month the asset is placed into service. The assets are again grouped into three groups with the depreciation factors as follows:

- Group 1 — 50%
- Group 2 — 25%
- Group 3 — 12.5%

In order to increase production, the Minister of Energy and Mineral Resources may determine a different method of calculating depreciation expenses.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

Land and building tax

Oil and gas pajak bumi dan bangunan tax (or, oil and gas property tax) (PBB tax) applies to land and/or buildings that are located in areas that are used for oil and gas mining activities. Such areas include the working areas or other similar areas and areas outside working areas or other similar areas that are an integral unit and used for oil and gas mining activities. The PBB tax object covers land, i.e., the earth's surface: (i) surface-onshore, which are productive areas, not yet productive areas, unproductive areas and emplacement areas; (ii) surface-offshore (essentially the water surface); (iii) subsurface (essentially the seabed); and (iv) buildings, including technical construction, including those permanently attached in the land area (onshore) or offshore waters area (offshore).

The basis of charging PBB tax varies for onshore projects, offshore taxable projects, as well as for the exploration and exploitation phases of a project.

C. Incentives

Several incentives are available to oil and gas companies: e.g., investment credit, interest recovery, indefinite carryforward of prior year unrecovered costs, and exemption from importation tax and duties on certain equipment and assets. The availability of the incentives depends on the agreement with the Indonesian Government.

Investment credit

Usually, the contractor will be permitted an investment credit of 8.8% net after tax on the capital investment cost directly required for developing production facilities out of new oilfields. This investment credit is allowed for capital investment on production facilities, including pipeline and terminal facilities, and the investment credit must be claimed in the first or second production year after the expenditure has been incurred. The investment credit is treated as taxable income as it is considered additional contractor lifting. The investment credit rules that apply can depend on the year the agreement was signed and the types of field involved.

The Director General of Taxation's (DGT) Regulation No. PER-05/PJ/2014 (PER-05), dated 18 February 2014, stipulates that investment credit is taxable in advance, even when unrecovered costs mean the equity to be split is still in a negative position. Effective from 2013 CIT returns onwards, investment credit is taxable at the time investment credit is received. PER-05 does not, however, cover tax treatment of investment credit prior to 2013. From a legal perspective, regulations cannot be applied retrospectively; it is possible, therefore, that the regulation may be interpreted differently by taxpayers and the Indonesian tax authority.

Oilfields entitled to the incentive must meet the following criteria:

- They must be located in the production working area.
- They must have an estimated rate of return of less than 15%, based on the terms and conditions in the contract and other prevailing intensive package regulations.

VAT reimbursement

In December 2014, the Minister of Finance issued Regulation No. 218/PMK.02/2014 (PMK-218) dated 5 December 2014 regarding procedures for VAT reimbursement by PSC contractors from SKKMIGAS. PSC contractors are entitled to reimburse VAT paid on acquired VATable goods or services when the equity is split with the PSC and FTP of Indonesian Government. VAT reimbursement is not allowed for the following: input VAT relating to operating costs of liquefied natural gas (LNG) plants and LNG transportation costs up to the point of sales; VAT that is treated as non-creditable or nondeductible based on the Indonesian laws and regulations; and VAT where other VAT exemption facilities are otherwise available.

On 25 October 2016, the Minister of Finance issued a new regulation, No. PMK 158/PMK.02/2016, amending PMK 218/PMK.02/2014 on the Procedures for VAT Reimbursements to Production Sharing Contractors under the upstream oil and gas activities. The main revisions are as follows:

1. The PSC contractor is entitled to reimburse VAT input when there is FTP unless the PSC governs that the VAT reimbursement is after equity and FTP.
2. VAT reimbursement for an LNG plant is allowed if it is covered in the contract and/or legislations.

Interest recovery

Interest costs on loans do not normally form part of the cost recovery, irrespective of whether the loans are internal or third-party "loans," unless specifically approved by SKKMIGAS. Approval is not common, and there are certain conditions that must be satisfied for the recovery of interest on loans.

The claim for interest recovery must be included in the financing plan, and the amount must be included in each year's budget for the approval of SKKMIGAS. The interest rate should not exceed the prevailing commercial rate. Subject to tax treaty relief, the interest is subject to withholding tax of 20% of the gross amount if it is provided by a non-Indonesian lender. The contractors can gross up the interest amount to reflect the withholding tax amount.

Based on GR 27/2017, qualified interest recovery has been removed from the list of non-cost-recoverable and non-tax-deductible expense under GR 79/2010.

Loss carryforward and unrecovered cost

Contractors are allowed to carry forward for tax purposes the preproduction expenses to offset against production revenues. However, these capital and non-capital costs incurred during the preproduction stage are not expensed, and accordingly, no tax loss originates from these costs.

Generally, these preproduction costs may be carried forward indefinitely to future years. The tax loss carryforward limitation outlined in the tax laws is not applicable to preproduction costs.

Land and building tax reduction for PSCs in exploration stage

The Minister of Finance Regulation No. 267/PMK.11/2014 (PMK-267) dated 31 December 2014 provides tax incentives for land and building tax (pajak bumi dan bangunan/PBB) reduction for PSC contractors in the exploration stage. This reduction is granted on the subsurface component (tubuh bumi) in the amount of 100% of the PBB due and applicable for the year 2015 onwards under the following requirements:

- The PSC must be signed after 20 December 2010 (i.e., the effective date of GR 79/2010).
- The PSC contractor has submitted a PBB tax return (surat pemberitahuan objek pajak/SPOP).
- A recommendation letter from the Minister of Energy and Mineral Resources (MoEMR) stipulates that the land and building in question are being used by the PSC and are still in the exploration stage.

The reduction is granted yearly for a maximum of six years from the PSC signing date and can be extended by up to four years (subject to a recommendation letter from the MoEMR).

D. Withholding taxes

The rate of dividend withholding tax and the rate of BPT depend on the year that the PSC was entered into.

Withholding tax on all other amounts follows the general tax law. For example:

- Interest — 15%/20%[3]
- Royalties from patents, know-how, etc. — 15%/20%[4]
- Fees for services paid to residents of Indonesia:
  - Technical, management and consultant services — 2%[5]
  - Construction contracting services — 2%/3%/4%[6]
  - Construction planning and supervision — 4%/6%[7]
  - Other services — 2%
- Fees for services paid to nonresidents — 20%[8]

E. Financing considerations

Refer to Section C above in relation to interest recovery.

F. Indirect taxes

Generally, PSCs are VAT collectors and are required to collect the VAT and remit it to the Indonesian Government on a monthly basis. However, for PSCs that are signed under the law prior to Law No. 22/2001, import duties, VAT on importation and import withholding tax on the importation of capital goods and equipment are generally exempted by the Indonesian Government through the use of a "master list" arrangement.

3 *A final withholding tax of 20% is imposed on payment to nonresidents. Tax treaties may reduce the tax rate. A 15% withholding tax is imposed on interest paid by nonfinancial institutions to residents.*

4 *A final withholding tax of 20% is imposed on payment to nonresidents. Tax treaties may reduce the tax rate.*

5 *This tax is considered a prepayment of income tax. It is imposed on the gross amount paid to residents. An increase of 100% of the normal withholding tax rate is imposed on taxpayers subject to this withholding tax that do not possess a tax identification number.*

6 *This is a final tax. The applicable tax rate depends on the types of service provided and the qualification of the construction company.*

7 *The applicable tax rate depends on the types of service provided and the qualification of the construction company.*

8 *This is a final tax on gross amounts paid to nonresidents. The withholding tax rate on certain types of income may be reduced under double tax treaties.*

For PSCs that are signed under Law No. 22/2001, the import duty is exempt, and VAT on importation is borne by the Indonesian Government relating to the import of capital goods and equipment used in exploration activities through the use of a "master list" arrangement. The import withholding tax may also be exempt but it will require separate approval from the Indonesian tax office.

G. Other

Disposal of PSC interest

Generally, under the terms of most agreements, a contractor has the right to transfer its interest under the contract to a related party or other parties with either written notification to or the prior written consent of SKKMIGAS. The income tax laws provide that the transfer of assets is subject to income tax.

GR 79/2010 and GR 27/2017 provide that the transfer of a direct or indirect participating interest in the exploration stage is subject to a final tax of 5% of gross transaction proceeds. However, the final rate is 7% if the transfer is conducted when the participating interest is in the exploitation stage. Transfers of participating interest to domestic companies, as required by a cooperation contract, are exempt from tax. In addition, the transfer of participating interests in the exploration stage with the intention to share risks is not considered taxable income if all of the following conditions can be satisfied:

- The transfer is not of the entire participating interest owned.
- The participating interest is owned for more than three years.
- Exploration activities have been conducted (i.e., working capital has been spent).
- The transfer is not intended to generate profit.

The implementing regulation to GR 79/2010, which was issued in December 2011, further outlines the mechanism for the reporting, withholding and remittance of the final tax. It also provides transitional rules in relation to the transfer of participation interests that occurred between the date of issue of GR 79/2010 (i.e., 20 December 2010) and the date of the implementing regulation.

GR 27 stipulates that there is no further tax payable after payment of 5%/7% tax on the transfer of PSC Interest. Prior to GR27, Minister of Finance Regulation No. 257/PMK.011/2011 (PMK 257) provides for the imposition of BPT on transfer of PSC interest. PMK 257 has not yet been revoked. Accordingly, there remains uncertainty as to how Article GR 27 will be implemented in practice alongside PMK 257.

CIT rate

GR 79/2010 provides that taxpayers can choose to adopt the prevailing CIT rate for PSCs, cooperation contracts and service contracts at the time of signing, or such contracts can be subject to the CIT rate as it varies over time.

Uplift income

Income received by a participating interest holder in relation to funding support provided to other participating interest holders for operational expenses for the contract area is "uplift income." Uplift or similar income is subject to a final tax of 20% of gross transaction value.

PMK 257 outlines the requirement to pay BPT on the after-tax income from the uplift payments. However, GR 27 stipulates that there is no further tax after payment of 20% tax on the uplift. The implementing regulation to GR 27 has not been issued, and PMK 257 has not yet been revoked.

Gross split PSC

On 16 January 2017, the Minister of Energy and Mineral Resources announced a new "gross split" regulation for PSCs for upstream oil and gas activities to replace the existing cost-recovery system. Under Minister Regulation No. 08 Year 2017 (Permen 08), which has been amended by Minister Regulation No.

52 Year 2017 dated 29 August 2017 (Permen 52) titled "Gross Split Production Sharing Contract," any newly issued PSC will apply a gross split mechanism, and the mechanism will also apply to an expired PSC that is renegotiated. The PSC contractor will be allocated a higher percentage share of gross production to substitute for loss of the cost recovery mechanism.

Existing PSCs will be largely unaffected, although the PSC contractor may request to apply the PSC gross split. The unrecovered cost balance may be taken into account to increase the contractor's split in such circumstances.

Under a gross split PSC, gross production will be allocated between the Government and the contractor. The initial base production split will be:

a. Government's share of 57% and contractor's share of 43% for oil
b. Government's share of 52% and contractor's share of 48% for gas

The initial based production split can be adjusted further (previously up to 5% under Permen 08) based on the Government's discretion depending on the commercial projections of the field(s).

The initial based production split for the contractor can also be adjusted further based on the characteristics of the fields if required (e.g., reservoir type, availability of supporting infrastructure). The initial based production split may also be further adjusted based on progressive split considerations. Broadly, the progressive split considerations that will be applied to the contractor's share will depend on the oil prices and the amount of production.

The Government take under PSC gross split consists of Government split, bonuses, corporate and dividend (C&D) tax and indirect tax, and the contractor take is the contractor split less C&D tax plus upstream oil and gas tax facilities and incentive.

On 28 December 2017, the Government issued Regulation No. 53 Year 2017 (GR 53/2017) which provides the tax rules for gross split PSC. GR 53/2017 stipulates that the taxable income of the contractors will be based on their contractor share less deductible expenses. The deductible expenses will follow the applicable general income tax law. The corporate income tax rates will apply based on the general income tax law. The profit after tax is also subject to a 20% branch profit tax, if applicable and may be subject to tax treaty relief if available.

GR 53/2017 provides that contractors are entitled to a 10 years tax loss carryforward. This is longer than the 5-year period under the general income tax law, but a significant reduction from the unlimited tax loss carryforward under the previous PSC cost recovery scheme.

Similar to the PSC cost recovery scheme, the uplift income is subject to 20% final tax on the uplift amount, and the transfer of gross split PSC interest is subject to a final income tax at either 5% for an exploration PSC or 7% for an exploitation/production PSC on the gross sales proceeds. GR 53/2017 also stipulates that there is no further tax after payment of final tax. Thus, this should mean that there is no BPT for uplift income and transfer of gross split PSC interest.

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Before engaging in any transaction relating to Iran, readers should be mindful of compliance requirements with the laws and regulations, as may be applicable, of any given jurisdiction in relation to engaging in business in or relating to Iran.

Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ☐ **Production sharing contracts**
- ■ **Service contract**

The upstream fiscal regime currently applied in Iran is a service-type contract, referred to as an Iran Petroleum Contract (IPC) which replaces the former buyback contract. After the international sanctions relating to Iran relaxed in 2016, Iran is expecting to attract international investments in its petroleum sector and is developing a new contractual framework under which international investors will be able to participate in oil and gas projects. Final terms of the new framework are not yet available.

Some highlights of the general corporate tax regime are provided in this chapter.

Corporate income tax regime

The standard corporate income tax rate for resident companies is 25%. The same 25% rate applies to profits of Iranian branches of foreign companies. Income tax at 22.5% applies if the company is listed on the stock exchange and 23.75% if the company is listed and traded over the counter (OTC).

Withholding tax applies on payments to nonresident contractors or service providers with effective rates being in the range of 2.5% to 7.5% of gross payment. For oil and gas upstream contracts (exploration, development and operation), the effective withholding tax rate is 3.75% of each payment to a nonresident. The price of contract paid to a nonresident for purchase of materials, equipment and supplies will be exempt from withholding tax, provided that the respective amounts are shown separately in the contract or subsequent addenda thereto.

VAT

Value-added tax (VAT) at 9% applies to most taxable goods and services, including imports. A higher rate applies to certain goods such as petrol and cigarettes.

Contract social security

Contract work performed in Iran shall be subject to a contract social security charge of either 7.78% or 16.67%. The lower rate applies where the contract includes local supplies or mechanical services; otherwise, the higher rate applies.

Customs duties

Import duties apply to all goods imported in Iran, unless exempt. No duties apply to exports from Iran.

Incentives for foreign investors

Different tax and customs incentives are available, including special benefits (tax exemptions and tax holidays) provided for various free-trade zones, special economic, and areas designated as underdeveloped.

Tax treaties

Iran has 46 double tax treaties in force with Algeria, Armenia, Austria, Azerbaijan, Bahrain, Belarus, Bulgaria, China, Croatia, Cyprus, Czech Republic, France, Georgia, Germany, Hungary, Indonesia, Jordan, Kazakhstan, South Korea, Kuwait, Kyrgyzstan, Lebanon, Macedonia, Malaysia, Oman, Pakistan, Poland, Qatar, Romania, Russia, Serbia, Slovenia, South Africa, Spain, Sri Lanka, Sudan, Switzerland, Syria, Tajikistan, Tunisia, Turkey, Turkmenistan, Ukraine, Uzbekistan, Venezuela and Vietnam.

Double tax treaties with many countries are currently in various stages of negotiation, ratification or entry into force, including Afghanistan, Bangladesh, Ecuador, Ethiopia, Ghana, India, Iraq, Italy, Ghana, Kenya, Mauritius, Morocco, Norway, Senegal, Slovak Republic, Tanzania, Thailand, Yemen and Zimbabwe.

Iran also has bilateral investment treaties with 66 countries, 53 of which are in force.

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ■ **Service contract**

A. At a glance

In Iraq, including the Kurdistan Region of Iraq (KRI), there are two main contract models used when engaging international oil companies (IOCs) for upstream oil and gas activities: (1) the service contract (which may be in one of three formats: Technical Service Contract (TSC); Development and Production Service Contract (DPSC); or Exploration, Development and Production Service Contract (EDPSC)) and (2) the production sharing contract (PSC). While the Iraqi federal government (FG) has been persistent in using the service contract model developed by the Iraqi Ministry of Oil (MoO) rather than the PSC model, the PSC model is the contract of choice for the official ruling body of the semi-autonomous KRI in the north — the Kurdistan Regional Government (KRG) — when engaging IOCs for upstream oil and gas activities. The most notable differences between the two models are in the cost and profit provisions.

For tax purposes, it is important to distinguish between the two models, since there are differences in the tax regimes of each model and in the tax laws and the practices adopted by the tax authorities in each jurisdiction implementing the different models.

Overview of the fiscal regime under the Iraqi FG service contract model:

- Corporate income tax (CIT) rate for upstream oil and gas activities — 35%[1]

1 *In 2010, the Iraqi Parliament ratified a tax law for foreign oil and gas companies. As per this law, the CIT rate applicable to income earned in Iraq from contracts undertaken by foreign oil and gas companies and by contractors working in the fields of production and extraction of oil and gas and related industries is 35%. Companies, branches or offices of oil and gas companies and service companies, and subcontractors working in fields of production and extraction of oil and gas and related industries are all subject to this law. This law has not been adopted by the KRG, and the 35% rate is not applicable in the KRI.*

- Party responsible for CIT payment — contractor/IOC
- Duration of service contract — 20 years extendable to 25 years
- Remuneration — fixed remuneration fee per barrel based on a sliding R-factor and a plateau rate (performance factor)[2] and 25% share of remuneration fee transferred to the regional oil company
- Cost contribution — full carry of all costs, including petroleum and supplementary costs, with possible recovery
- Signature bonus — varies
- Royalty — not applicable
- Cost recovery — capped at 50% of petroleum revenue[3]
- Fiscal reporting requirements — quarterly basis
- Tax filing requirements — within five months of the fiscal year-end
- Capital gains tax rate on upstream oil and gas activities:
  - Per tax law, 35%[4]
  - Per service contract, not specified
- Withholding tax on payments made to nonresidents per tax law:
  - Dividends — 0%
  - Interest — 15%
  - Royalties — 15%
  - Branch remittance tax — 0%
- Net operating losses (years):
  - Carryback — none
  - Carryforward — per tax law, 5; per service contract, 5[5]

Overview of the fiscal regime under the KRG PSC model:

- CIT rate for upstream oil and gas activities:
  - Per tax law, 15%
  - Per PSC, generally applicable rate prescribed in the Law of Taxation (Law No. 5 of 1999), but in no event in excess of 40%[6]
- Party responsible for CIT payment — KRG
- Duration of PSC — 25 years, extendable to 30 years
- Profit petroleum — Profit sharing based on R-factor[7] and 20% share of profit generated to KRG after recovery of recoverable costs

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2 *See Section C.*

3 *Costs approved by the MoO and the Joint Management Committee (JMC) should be recoverable.*

4 *In 2010, the Iraqi Parliament ratified a tax law for foreign oil and gas companies. As per this law, the CIT rate applicable to income earned in Iraq from contracts undertaken by foreign oil and gas companies and by contractors working in the fields of production and extraction of oil and gas and related industries is 35%. Companies, branches or offices of oil and gas companies and service companies, and subcontractors working in fields of production and extraction of oil and gas and related industries are all subject to this law, although the tax law does not expressly specify that capital gains are subject to the 35% CIT rate. This law has not been adopted by the KRG, and the 35% rate is not applicable in the KRI.*

5 *See Section D.*

6 *In 2010, the Iraqi Parliament ratified a tax law for foreign oil and gas companies. As per this law, the CIT rate applicable to income earned in Iraq from contracts undertaken by foreign oil and gas companies and by contractors working in the fields of production and extraction of oil and gas and related industries is 35%. Companies, branches or offices of oil and gas companies and service companies, and subcontractors working in fields of production and extraction of oil and gas and industries are all subject to this law. This law has not been adopted by the KRG, and the 35% rate is not applicable in the KRI.*

7 *The requirement to apply the withholding tax on payments to a nonresident is not actively monitored or applied by the KRG's tax authority in the KRI; however, one cannot entirely rule out the possibility of the current practice changing in the future or of the KRG's tax authority picking up on the requirement during its tax audits.*

- Cost contribution — full carry of costs during the exploration phase with subsequent sharing of operating costs if commercial discovery is made
- Signature bonus — varies
- Production bonus — varies in terms of recoverability, value and payment due date depending on the specific PSC
- Capacity building bonus — varies in terms of recoverability, value and payment due date depending on the specific PSC
- Capacity building payment — 20%, but could vary depending on the specific PSC
- Royalties — 10%
- Cost recovery (cost oil) — once the block starts producing, 40% for crude oil and 60% for natural gas after deducting royalty
- Fiscal reporting requirements — annual basis
- Tax filing requirements — within six months of the fiscal year-end
- Capital gains tax rate on upstream oil and gas activities – 15%[8]
- Withholding tax on payments made to non-residents per tax law:
  - Dividends — 0%
  - Interest — 15%
  - Royalties — 15%
  - Branch remittance tax — 0%
- Net operating losses (years):
  - Carryback — none
  - Carryforward – per tax law, 5; per PSC, indefinitely[9]

B. Fiscal regime

Corporate income tax

In general, CIT is imposed on profits arising from commercial activities (or activities of a commercial nature), vocations and professions, including profits arising from contracts and undertakings. The tax authorities in Iraq and the KRI generally rely on the following factors to determine if income is deemed to arise in Iraq and therefore taxable in Iraq:

- The place of signing the contract by the party performing work under the contract (vendor or service provider) is in Iraq.
- The place of performance of work is in Iraq.
- The place of delivery of goods or services is in Iraq.
- The place of payment for the work is in Iraq.

The above four factors were amended in 2015 by the Iraqi Ministry of Finance's Instructions No. 1 of 2014. Under the new instructions, the taxability of (i) supply contracts, (ii) supplementary or complementary services performed in relation to a supply contract, and (iii) professional services, is addressed separately. In respect of a supply contract, income arising from a supply contract would be considered taxable in Iraq if any one of the following factors applies:

- The vendor or service provider has a branch or an office in Iraq, and the contract is signed by the branch/office representative, any of the branch/office's employees, or any other person who is resident in Iraq and is authorized to sign the contract.

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8 *In 2010, the Iraqi Parliament ratified a tax law for foreign oil and gas companies. As per this law, the CIT rate applicable to income earned in Iraq from contracts undertaken by foreign oil and gas companies and by contractors working in the fields of production and extraction of oil and gas and related industries is 35%. Companies, branches or offices of oil and gas companies and service companies, and subcontractors working in fields of production and extraction of oil and gas and related industries are all subject to this law. This law has not been adopted by the KRG, and the 35% rate is not applicable in the KRI.*

9 *See Section G.*

- The vendor or service provider has a branch or an office in Iraq, and the contract is performed or executed by the branch/office representative, any of the branch/office's employees, or any other person who is resident in Iraq and is authorized to perform the contract.
- The contract's legal formalities and requirements are completed in Iraq in the name of the vendor or service provider (e.g., customs clearance, payment of customs duties, opening of letter of credit, and any related procedures taking place in Iraq, irrespective of whether the vendor or service provider has a branch, an office or an agent in Iraq).
- Payments under the contract, to the vendor or service provider, are received fully or partially in Iraq, regardless of the currency used to make the payments

  Or
- The vendor or service provider receives payment in barter

In respect of services supplementary or complementary to the supply contract, tax would be imposed on income arising from supplementary or complementary services performed in relation to a supply contract (such as construction, supervision, maintenance or engineering services), whether included as part of the supply contract or in an independent contract, if these activities are carried out in Iraq. Furthermore, the taxability of the service component would be determined separately from the taxability of the supply contract.

In respect of professional services or services agreed to in the supply contract, tax would be imposed on income arising from these services, whether included as part of the supply contract or in an independent contract, if they are carried out in Iraq, regardless of the place of payment or whether the services were provided by an individual or a legal person. Furthermore, the taxability of the service component would be determined separately from the taxability of the supply contract.

No formal adoption of the above instructions was made by the tax authorities in the KRI; however, similar principles of analysis are often applied in practice.

Tax rate

The general CIT rate applicable to all activities (except upstream oil and gas activities) is a unified flat rate of 15% of taxable income. Activities that relate to oil and gas production and extraction activities and related industries, including those under service contracts, will be subject to CIT at the rate of 35% of taxable income. The higher CIT rate of 35% has not yet been adopted in the KRI and, therefore, the CIT rate of 15% continues to apply to all activities in the KRI, including upstream oil and gas activities under the KRG's PSC model in the KRI.

Withholding tax

IOCs and oil service companies are required to retain taxes from payments they make to their subcontractors and remit the retained taxes to the Iraqi tax authority on a monthly basis (with exceptions applicable to the final payment). Generally, a retention rate of 7% applies to oil and gas activities and a rate of 3.3% applies to all other activities. This retention and remittance process is not currently observed in the KRI.

Capital gains

Capital gains derived from the sale of fixed assets should be taxable at the normal CIT rate of 15% (35% for oil and gas production and extraction activities and related industries, including service contracts — except in the KRI where the 35% CIT rate has not been adopted). Capital gains derived from the sale of shares and bonds not in the course of a trading activity should be exempt from tax; otherwise, capital gains should be taxed at the normal CIT rate.

Administration

In Iraq, tax returns for all corporate entities must be filed in Arabic within five months from the end of the fiscal year together with audited financial statements prepared under the Iraqi Unified Accounting System (IUAS). The KRG's tax authority currently requires for tax returns and audited financial statements prepared using IUAS to be filed by large taxpayers within six months after the end of the fiscal year. Companies not classified as large taxpayers are only required to submit audited IUAS financial statements. A rate of 10% of the tax due is imposed as a delay fine, up to a maximum of IQD500,000 (as per current practice, up to a maximum of IQD75,000 in the KRI), on a taxpayer that does not submit or refuses to submit an income tax filing within five months (within six months in the KRI) after the fiscal year-end. In addition, foreign branches that fail to submit financial statements by the CIT filings' due date are also subject to an additional penalty of IQD10,000. A similar penalty is not currently being imposed in the KRI. However, in the KRI, the tax authority has been very aggressive and is sending to a Tax Tribunal the files of companies that have failed to submit their tax filing package to the tax authority in a timely manner. The Tax Tribunal will assess late filing penalties, ranging from 10% to 25% of taxable income.

After a CIT filing is made, the tax authority will undertake an audit of the filing made, may request additional information and will eventually issue a CIT assessment. Payment of the total tax amount is due after the Iraqi tax authority sends the taxpayer the tax assessment based on the Iraqi tax authority's audit of the CIT filing package. In Iraq and the KRI, if the tax due is not paid within 21 days from the date of assessment notification, there will be a late payment penalty of 5% of the amount of tax due. This amount will be doubled if the tax is not paid within 21 days after the lapse of the first period. The tax authority in Iraq also applies an annual simple interest of 11% on the amount of tax due if the tax due is not paid within three days from the date of assessment notification. This interest is not currently being imposed in the KRI.

An IOC working under a service contract should be responsible for the settlement of the CIT due; however, under the PSC tax regime, the payment of the CIT due should be the responsibility of the KRG for the account of the IOC and not the responsibility of the IOC.

C. Service contracts of the Iraqi FG

The Iraqi MoO developed the service contract in collaboration with its state-owned regional oil companies; the service contract is used as a basis for engaging with IOCs for long-term oil and gas exploration and development. Under the service contract, the IOC operates as a contractor to a regional oil company; the IOC generally bears all costs and financial risk, including petroleum costs, supplementary costs and tax costs, for undertaking its upstream oil and gas activities in return for a fixed fee known as a remuneration fee per barrel (RFB). The IOC should also be entitled to recover all of its petroleum and supplementary costs, up to a maximum of 50% of petroleum revenue, provided that these costs are approved by the MoO and the JMC.

The terms of service contracts may vary from one oilfield to another and on the service contract format used (TSC, DPSC or EDPSC). The guidance below is general in nature.

Duration

The service contract would typically be for a term of 20 years, with a maximum of 25 years, divided into a period of 3 years covering the first phase of exploration, a period of 2 years covering the second phase of exploration (with a possible extension for 2 additional years), an appraisal period of 2 years, a development period of 7 years, and, finally, a transfer period of 4 years. Upon the termination of the transfer period, the contractor is required to hand over all petroleum operations to the regional oil company.

Petroleum costs

The service contract defines petroleum costs as recoverable costs and expenditures incurred and/or payments made by a contractor in connection with or in relation to the conduct of petroleum operations (except the CIT paid in Iraq or as otherwise stipulated in the service contract).

Supplementary costs

Under the service contract, supplementary costs are known as recoverable costs and expenditures incurred by the contractor other than petroleum costs. These costs include signature bonus, de-mining costs, costs incurred for additional facilities and costs incurred for remediation of pre-existing environmental conditions.

Supplementary costs should not exceed 10% of petroleum revenue.

Signature bonus

A contractor is required to pay a signature bonus as determined by the service contract to the bank account of the regional oil company. The amount of signature bonus should be amortized in the books of the contractor and recovered over 20 equal quarterly payments. The recoverability/non-recoverability of the signature bonus varies depending on the terms of the service contract.

Transportation costs

All transportation between the production measurement point in the contract area and the delivery point is done by the transporter (an entity appointed by the MoO).

Training, Technology, and Scholarship Fund

Under the service contract, a contractor is required to contribute to the Training, Technology, and Scholarship Fund an amount of US$5 million (at a minimum). The fund payment is regarded as a non-recoverable cost.

Training costs

All costs and expenses incurred by the contractor or operator in organizing, setting up and conducting training activities for their Iraqi personnel engaged in petroleum operations or contractor's training activities, including the planning, designing, constructing, commissioning and running training facilities and the related software, are recoverable.

Importation of equipment

The MoO is currently importing material and equipment on behalf of IOCs; any costs suffered by the IOC should be considered recoverable.

Cost recovery

Recoverable costs should be approved by the MoO and JMC and should not exceed 50% of petroleum revenue.

Non-recoverable costs

The following non-exhaustive list of items should be treated as non-recoverable costs for the purpose of cost recovery:

- Costs incurred as a result of any proven gross negligence or willful misconduct of the contractor and operator, including any amount paid in settlement of any claim alleging gross negligence or willful misconduct whether or not gross negligence or willful misconduct is admitted or whether such sum is stated to be paid on an ex gratia or similar basis
- Any expenditure incurred directly or indirectly in connection with the raising of money to finance petroleum operations and other incidental costs and charges related thereto by whatever method raised, which includes, but is not limited to, interest, commissions, fees and brokerage
- Any costs, charges or expenses, including donations relating to public relations or enhancement of the contractor's corporate image and interests, unless expressly approved by the JMC
- Any expenditure incurred that is not related to petroleum operations or on matters or activities beyond the delivery point(s)
- CIT
- Signature bonus (varies)

- Training, Technology, and Scholarship Fund
- Any other expenditure that is stated elsewhere in the service contract to be a non-recoverable expenditure

Remuneration fee

In return for the petroleum operations, a contractor is entitled to a fixed fee per barrel known as the RFB if the production exceeds a certain specified minimum level. The RFB is determined based on the stage of the contractor's cost recovery in the service contract, which is based on an index called the "R-factor." The R-factor, calculated annually, is a coefficient of the contractor's overall payback over the contractor's total expenditures. The R-factor is used to adjust the contractor's RFB with the increase in the contractor's cost recovery. The R-factor corresponding to the RFB for which a contractor is entitled is as follows:

R-factor	Percentage of the remuneration fee (set in USD per barrel) payable depending on the R-factor
R < 1	100%
1 < R < 1.25	80%
1.25 < R < 1.5	60%
1.5 < R < 2	50%
R ≥ 2	30%

The RFB is also adjusted based on a performance factor calculated as the ratio of net production rate to the bid plateau production target. If the contractor fails to reach the designated performance factor, i.e., the net production is below the minimum level of production, the contractor may lose out on remuneration.

Under the service contract, the governmental party has a 25% share of remuneration fee without investment.

Unconventional oil and gas

No special terms apply to unconventional oil or gas.

Local content requirements

According to the service contract, a contractor is required, to the maximum extent possible, to employ, and require subcontractors to employ, Iraqi nationals having the requisite qualifications and experience.

Taxes

An IOC should comply with the tax laws and regulations governing Iraq, including CIT, withholding tax, employee income tax, social security, customs duty and stamp duty, and complete the required registrations and filings, as required by the tax laws and regulations (including modifications to the laws of general applicability as introduced by the service contract).

D. Production sharing contracts of the KRG

Under the PSC model, the ownership of the oil or gas is shared between the IOC and the KRG, represented by the Ministry of Natural Resources (MoNR), and the IOC is permitted to use revenue from produced oil or gas to recover costs after the deduction of royalty. Once costs are recovered, profit, known as profit petroleum, is split between the KRG and the IOC. Therefore, under the PSC, the KRG and the IOC share revenues and operating costs. However, the IOC would be required to bear all capital costs and financial risk.

Duration

The exploration period is seven years, divided into a first phase of three years, plus two two-year renewals. The contractor is entitled to two one-year further extensions of the exploration period in order to carry out appraisal work. There is also a possibility for an additional two-year extension for gas marketing work.

In case of a commercial discovery, there is a development and production period of 20 years with an automatic extension of five years under the same terms and conditions.

If a field is still producing at the end of the extended development and production period, the contract can be extended further for another five years. This means that for oil, the total maximum contract period is 39 years, and for gas, 41 years.

Royalty

Under the PSC model, there is a royalty of 10% applied to the daily quantity of petroleum produced and saved from the contract area, covering crude oil and non-associated natural gas. The KRG may elect payment of the royalty to be made in cash or in-kind. Royalty payments made in cash in regard to crude oil and non-associated natural gas would be valued at the international market price and at the actual price, respectively, and would need to be made to the KRG on a quarterly basis.

Any royalty payments made in-kind would require the delivery of the crude oil or non-associated natural gas, or both, at the agreed delivery point where legal title and risk of loss are transferred.

Signature bonus

A contractor is required to pay a signature bonus to the MoNR as determined by the specific PSC. The recoverability/non-recoverability of the signature bonus varies depending on the terms of the PSC.

Production bonus

A contractor is required to pay production bonuses to the KRG at different stages of the petroleum operations as determined by the specific PSC. The payment of the production bonuses would be due once the first production date is reached and again upon reaching crude oil commercial discovery.

Production bonuses are generally regarded as non-recoverable, but this could vary depending on the terms of the PSC.

Capacity building bonus

Although the applicability, recoverability, and amount of the capacity building bonus may vary from one PSC to another, a contractor would generally be required to pay a capacity building bonus to the Government within 30 days from the contract date.

The capacity building bonus is generally regarded as non-recoverable, but this could vary depending on the terms of the PSC.

Capacity building payments

Although the applicability, recoverability and amount/percentage of the capacity building payments may vary from one PSC to another, a contractor would generally be required to pay a capacity building payment of 20% of the profit petroleum attributable to each contractor with participation under the PSC, in cash and in US dollars.

The recoverability/non-recoverability of the capacity building payments varies depending on the terms of the PSC.

Importation of equipment

The MoNR is currently importing material and equipment on behalf of IOCs, subcontractors, and employees without applying a customs duty.

Cost recovery

Cost recovery is limited to a portion of production after deduction of the royalty, to a maximum not exceeding 40% for crude oil, and not exceeding 60% for natural gas.

According to the PSC model, cost recovery should occur in the following order and may not exceed the relevant percentages indicated above:

- Production costs
- Exploration costs (including appraisal costs and further exploration within the contract area)
- Gas marketing costs
- Development costs
- Decommissioning costs

If cost recovery exceeds the relevant percentages, unrecovered costs may be carried forward indefinitely until they are recovered in full.

Non-recoverable costs

Non-recoverable costs include all costs except the following:

- Production costs
- Exploration costs (including appraisal costs and further exploration within the contract area)
- Gas marketing costs
- Development costs
- Decommissioning costs

Profit petroleum

A contractor is entitled to a percentage of the oil and/or gas produced from remaining production after the recovery of costs allowable for recovery in accordance with the terms of the specific PSC (and considering the cost recovery limit). This percentage is determined according to a formula that takes into account cumulative revenues and cumulative petroleum cost, and provides the contractor with reasonable returns (the R-factor), which equals cumulative revenues actually received by the contractor divided by cumulative costs actually incurred by the contractor.

The share of profit petroleum to which the contractor will be attributed and allocated from first production for profit oil is an amount equal to the quantities of petroleum resulting from the application of the relevant percentage (as indicated below) to the daily volume of production of profit oil within the contract area at the corresponding delivery point:

R-factor	Contractor's % share*
$R \leq 1$	35%
$1 < R \leq 2$	$35 - (35 - 16)(R - 1)/(2 - 1)\%$
$R > 2$	16%

* The percentage share varies from one PSC to another and differs slightly based on the type of petroleum produced (i.e., oil or gas).

The remaining share of profit petroleum not attributed to the contractor, after applying the above formula, is allocated to the KRG.

Unconventional oil and gas

No special terms apply to unconventional oil or gas.

Technological and logistical support

According to the PSC model, a contractor is required to provide the KRG technological and logistical assistance before the end of the first contract year. The form of assistance should be agreed with the MoNR.

Environmental fund

Under the PSC model, a contractor is required to contribute to the environmental fund established by the government after a certain period of time from the signature of the contract.

Local content requirements and training plans

According to the PSC model, the contractor shall give employment preference to Iraqi nationals to the extent that such persons have the technical capabilities, qualifications, competence, and experience required to perform the work. This, however, does not preclude the contractor from appointing foreign workers to perform the work under the specific PSC, provided that Iraqi nationals do not have the necessary qualifications and capabilities. The contractor would be required to train Iraqi nationals to reach the level of expertise of the foreign workers. The contractor would need to submit a proposed training plan to the JMC for approval and make training payments to the Government as determined by the specific PSC.

Taxes

According to the PSC model executed with the KRG, each contractor entity, its affiliates and any subcontractor should, for the entire duration of the PSC, be exempt from all taxes as a result of its income, assets and activities under the contract. The KRG shall indemnify each contractor entity upon demand against any liability to pay any taxes assessed or imposed upon such entity, which relate to any of the exemptions granted by the KRG. Each contractor entity should be subject to CIT on its income from petroleum operations as per the applicable tax rates. Payment of the CIT at a rate of 15% should be made, for the entire duration of the contract, directly to the KRG's tax authorities by the MoNR, for the account of each contractor entity, from the KRG's share of the profits received.

Notwithstanding the tax provisions of the MoNR's PSC, it is important to note that the KRG's MoNR is not the government body that is legally mandated with the responsibility of administering the KRG's income tax law. There is a regional tax authority within the KRI, under the umbrella of the KRI's Ministry of Finance, which is responsible for tax administration and for issuing instructions in respect of the tax law applicable within the KRI. The KRG tax authority has consistently disregarded the provisions of the PSCs, even after the release of Ministerial Decree No. 667 of 2015, which stated that oil and gas companies operating in the KRI should be exempt from taxation based on the provisions of the PSC. The KRG tax authority's position was clarified in one of its internal circulars that was made public on 6 December 2015. Based on the internal circular, the KRG tax authority instructed its directorates across the KRI to normally assess the CIT and the personal income tax (PIT) liabilities of oil and gas companies operating under a PSC based on their tax filings. However, the circular did not require direct tax payment demands from the oil and gas companies.

In another circular, the KRG tax authority clarified that oil and gas companies operating in the KRI under PSCs should not be liable to pay the PIT with respect to their expatriate employees which requires obtaining confirmation from the MoNR.

E. Withholding tax on payments to nonresidents

Dividends

Dividends paid to nonresidents are not subject to withholding tax in Iraq and the KRI.

Interest

Interest paid to nonresidents is subject to a withholding tax rate of 15%. This requirement is not currently applied in the KRI.

Royalty

Royalty paid to nonresidents is subject to a withholding tax rate of 15%. This requirement is not currently applied in the KRI.

F. Foreign tax relief

A foreign tax credit is available to Iraqi companies on income taxes paid abroad. In general, the foreign tax credit is limited to the amount of an Iraqi company's CIT on the foreign income, calculated on a country-by-country basis. Any excess foreign tax credits may be carried forward for five years.

G. Determination of taxable income

General

Generally, all income generated in Iraq is taxable in Iraq, except for income exempt by the income tax law, the industrial investment law, or the investment law.

Business expenses incurred to generate income are allowable, with limitations on certain items, such as entertainment and donations. However, provisions and reserves are not deductible for tax purposes.

Under the service contract, the remuneration fee constitutes a contractor's taxable income to which the 35% rate is applied, whereas under the PSC model, profit petroleum is used when determining a contractor's CIT liability.

Tax depreciation

The Iraqi Depreciation Committee (IDC) sets the maximum depreciation rates for various types of fixed assets. The tax regulations provide for straight-line depreciation rates for the financial sector (banks and insurance companies) and other sectors.

Depreciation percentages applicable to selected oil and gas companies' assets include:

- Pure butane production unit — 6.5%
- Gas drying and cooling units — 5%
- Electrical system technology — 5%
- High-pressure vessels — 8%
- Machinery and equipment — 20%
- Electrical air compressors — 8%
- Cranes and rollers — 7.5%
- Liquid gas tanks — 4%
- Bulldozers and shovels — 20%
- Precision machinery and equipment — 10%

Used assets are depreciated at statutory rates established by the tax authorities, calculated on the purchase price.

When petroleum contractors or operators under a service contract acquire fixed assets, they are not allowed to capitalize such costs. This is because this expenditure is reimbursed to the petroleum contractors or operators by the regional oil company under the service contract arrangement.

An exception to the above general rule is the signature bonus paid by the petroleum contractors or operators to the MoO for the right to benefit from an oil field. This item may be amortized by the petroleum contractors or operators over a period of 10 years using the straight-line method. However, the Iraqi tax authority may require the bonus to be amortized over the term of the contract instead, and may not accept the bonus as a tax-deductible expense. No formal position has yet been communicated by the Iraqi tax authority on this matter.

A contractor operating under the PSC model, on the other hand, is allowed to depreciate its capital assets and expenditures using the declining-balance method and the depreciation rates set out in the provisions of the PSC.

If the depreciation rates used for accounting purposes are greater than the ones computed under the rates prescribed for tax purposes, the excess is disallowed.

Relief for losses

Taxpayers may carry forward unabsorbed losses for five years to offset profits in future years. However, the amount of losses carried forward that may be used to offset taxable income is limited to 50% of each year's taxable income. If the Iraqi tax authority applies a deemed profit percentage to a book loss year, the losses with respect to that year will be lost.

The above is the general practice, whether losses were incurred under a service contract or otherwise. However, under the PSC model, losses may be carried forward indefinitely.

Losses may not be carried back. Losses incurred outside Iraq cannot be offset against taxable profit in Iraq.

Ring fencing

Under the PSC model, petroleum costs under one PSC may not be considered as recoverable against another PSC held by the same contractor. Ring-fencing rules are not addressed under the service contract.

Groups of companies

Iraqi law does not contain any provisions for filing consolidated returns or for relieving losses within a group of companies.

H. Other significant taxes

The following table summarizes other significant taxes.

Nature of tax	Rate (%)
Stamp fees; imposed on the total contract value:*	
Iraq and KRI	0.2
Property tax; imposed on the annual rent:	
From buildings	10.8
From land	2
Employee income tax; imposed on individuals' income after applicable allowances:	
Iraq	3-15
KRI	5
Social security contributions, imposed on salaries and benefits of local and expatriate employees; a portion of employee allowances up to an amount equaling 30% of the basic salary is not subject to social security contributions:	
Employer	12
Employer (oil and gas companies)	25
Employee	5

*The stamp duty rate provided is the most commonly applied rate in Iraq and the KRI. In practice, the application of stamp duty may vary.

I. Miscellaneous matters

Foreign exchange controls

The currency in Iraq is the Iraqi dinar. Iraq does not currently impose any foreign exchange controls.

Debt-to-equity rules

There are currently no debt-to-equity rules in Iraq. The only restrictions on debt-to-equity ratios are those stated in a company's articles and memoranda of association.

J. Tax treaties

Iraq does not have a large double tax treaty network in place. However, in practice, the Iraqi tax authority does not apply double tax treaties.

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Tax regime applied to this country

■ **Concession**	☐ **Production sharing contracts**
☐ Royalties	☐ **Service contract**
■ Profit-based special taxes	
■ Corporate income tax	

A. At a glance

Fiscal regime

Ireland's fiscal regime that applies to the petroleum industry consists of a combination of corporation tax, a profit resource rent tax (PRRT) and a petroleum production tax (PPT).

- Royalties — none
- Bonuses — none
- Production sharing contract (PSC) — not applicable
- Income tax rate — corporation tax rate of 25%
- PRRT — rate between 5% and 15%, depending on field profitability relative to capital investment[1]
- Petroleum production tax (PPT) — rate between 10% and 40%, depending on field profitability
- Capital allowances – D, E[2]
- Investment incentives – L, RD[3]

B. Fiscal regime

Ireland's fiscal regime for the petroleum industry consists of a combination of a corporation tax, PRRT and PPT.

Corporation tax

Irish resident companies are subject to corporation tax on their worldwide profits (i.e., income and gains). Income from Irish trade is subject to corporation tax at a rate of 12.5%; however, certain "excepted trades" are subject to corporation tax at a rate of 25%. The definition of "excepted trades" includes dealing in land, working minerals and petroleum activities.

Nonresident companies are also subject to Irish corporation tax if they carry on a trade in Ireland through a branch or agency. Profits or gains arising for a nonresident person from exploration or exploitation activities carried on in Ireland or in a "designated area," or from exploration or exploitation rights, are regarded for tax purposes as profits or gains of a trade carried on by that person in Ireland through a branch or agency. A designated area is an area

1 *PRRT is not deductible for corporation tax purposes.*

2 *D: accelerated depreciation; E: immediate write-off for exploration costs.*

3 *L: losses can be carried forward indefinitely; RD: research and development incentive.*

designated by order under Ireland's Continental Shelf Act 1968. Accordingly, income arising for a nonresident company from petroleum activities is regarded as arising from an excepted trade and is subject to corporation tax at a rate of 25%.

Chargeable gains accruing from the disposal of "petroleum-related assets" are subject to tax at a rate of 33%. Petroleum-related assets include any petroleum rights, any assets representing exploration expenditure or development expenditure, and shares deriving their value or the greater part of their value, whether directly or indirectly, from petroleum activities, other than shares quoted on a stock exchange.

Corporation tax is charged on taxable income. This is determined by starting with income before taxation according to accounting principles and then adjusting it for certain add-backs and deductions required under the tax legislation. Expenses are generally allowed if they are incurred "wholly and exclusively" for the purposes of the trade, but certain expenses are not permitted under the legislation, such as capital expenditure.

Deductions for expenditure of a capital nature may be available under the capital allowances regime. For the petroleum industry, this is in the form of a 100% deduction for both exploration expenditure and development expenditure that become available when petroleum extraction activities commence (in the case of petroleum exploration expenditure) and when production in commercial quantities commences (in the case of development expenditure). In addition to allowing full write-offs against petroleum profits for exploration and development expenditures, a provision allows for a deduction for expenditure that companies may incur in withdrawing from or shutting down an oil or gas field (see further discussion on exploration, development and abandonment expenditure in section C below).

Ring fencing

Petroleum activities are ring-fenced for tax purposes so that losses from petroleum activities may not be set off against profits from other activities. Similarly, there are restrictions on the group relief of petroleum losses and charges on income incurred in petroleum activities. The ring-fencing also prevents losses from other sectors of the economy being applied against petroleum profits. This two-way ring fencing recognizes the unique potential of the petroleum exploration and production industry for exceptionally large costs, losses and profits.

Profits from oil and gas activities undertaken by an Irish resident company in a foreign country are subject to tax in Ireland.

Profit resource rent tax

Irish tax legislation contains provisions for PRRT that apply to petroleum activities. Under these provisions, companies carrying on Irish petroleum activities will be subject to an additional charge to tax depending on the profitability of the fields affected.

The PRRT rate varies from 5% to 15%, depending on the profitability of the field as measured by reference to the capital investment required for that field. PRRT is not deductible for corporation tax purposes.

PRRT applies only to exploration licenses and reserved area licenses awarded on or after 1 January 2007 and licensing options. PRRT operates on a graded basis by reference to profitability and, in particular, by reference to the profit ratio achieved on the specific field for which a license has been granted. "Profit ratio" is defined as the cumulative after-tax profits on the specific field divided by the cumulative level of capital investment on that field.

Each field that falls within the scope of the regime is treated as a separate trade for the purposes of this tax and is effectively ring-fenced, with the result that a company would not be entitled to offset losses from any other activities against the profits of a taxable field for the purposes of calculating the PRRT. It is possible for capital expenditure incurred by one company to be deemed to have been incurred by another group company (with the necessary relationship to the first company) for the purposes of calculating the level of capital investments used in determining the profit ratio. For this provision to apply, an election must be made by the company that originally incurred the expenditure.

PRRT is calculated as follows:

Profit ratio	<1.5	≥1.5 but <3.0	≥3.0 but <4.5	≥4.5
Additional tax	0%	5%	10%	15%

PRRT applies to taxable field profits, which are defined as the amount of the petroleum profits of the taxable field for the accounting period after making all deductions for, and giving or allowing all reliefs for, corporate tax purposes. The one exception is if, in a particular accounting period, the profit ratio for a specific field is in excess of 1.5 and was less than 1.5 in the immediately preceding accounting period with respect to that field; in such a situation, the profits to which the PRRT applies are calculated by reference to the following formula:

$$(A - [B \times 1.5]) \times 100/(100 - R)$$

In this formula, A is the cumulative field profits on the field from 1 January 2007, B is the cumulative field expenditure on the field from 1 January 2007 and R is the general rate of tax for Irish petroleum activities (currently 25%). The purpose of this formula is to reduce the quantum of profits to which the PRRT applies in the period immediately following a period for which the PRRT did not apply as a result of the profit ratio being less than 1.5.

PRRT is collected in the same manner as corporation tax, and returns for PRRT are submitted with the annual corporate tax return.

Petroleum production tax

Having previously announced its intent to do so in 2014, Ireland enacted the legislation in 2015 to introduce a new taxation regime for petroleum exploration and production. The new regime, which will provide for a higher and earlier contribution to the Irish Exchequer, will apply to exploration licenses (other than those arising from licensing options issued prior to 18 June 2014), reserved area licenses or licensing options granted on or after 18 June 2014. PRRT will not apply to a license that is subject to the new PPT regime.

PPT will apply to the net profits of each field (on a field-by-field basis) using a sliding scale of rates from 10% to 40% based on the profitability of the field. However, a minimum payment of 5% of gross field revenue (less transportation expenditure) will be required, ensuring that a fiscal contribution is received even where a producing field is not yet profitable or where there are losses carried forward. The corporation tax rate applicable remains at 25%. However, as the PPT will be deductible for corporation tax purposes, the maximum effective tax rate applicable to the fields with the highest profitability will be 55%, up from the current 40%. The legislation is somewhat unclear if the 5% minimum payment will be allowed to augment a loss for corporation tax purposes.

Aside from the minimum PPT, the point at which PPT applies is expected to be earlier than the equivalent entry point under the PRRT regime. This arises because the R-factor used to determine field profitability is computed on the basis of cumulative field gross revenue less PPT paid (but pre-corporation tax)/cumulative field costs, compared to the existing "profit ratio" calculation that is based on cumulative after-corporation tax net profits for a field. It is intended that the “gross revenue” for PPT purposes should be calculated in accordance with transfer pricing rules.

PPT rates:			
R-factor	PPT rate	CT rate	Effective rate
< 1.5	0%*	25%	25%
1.5	10%	25%	32.5%
≥1.5 but < 4.5	Pro rata	25%	Varies
≥ 4.5	40%	25%	55%

*Subject to a minimum PPT of 5% of field gross revenue less transportation expenditure

Each field that falls within the scope of the regime is treated as a separate trade for the purposes of this tax and is effectively ring-fenced, with the result that a company would not be entitled to offset losses from any other activities against the profits of a taxable field for the purposes of calculating the PPT. It is possible for capital expenditure incurred by one company to be deemed to have been incurred by another group company (with the necessary relationship to the first company) for the purposes of calculating the level of capital investments used in determining the R-factor. For this provision to apply, an election must be made by the company that originally incurred the expenditure.

PPT will be collected in the same manner as corporation tax (but the due date for payment of PPT is the filing date of the corporate tax return for the period), and returns for PPT are to be submitted with the annual corporate tax return.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Development expenditure

Irish tax legislation provides for a 100% allowance for capital expenditure incurred for production and development in connection with a relevant field being worked in the course of carrying on a petroleum trade. The allowance is available for the period when the asset represented by the expenditure is brought into use for the purposes of the trade. The allowance is subject to production in commercial quantities, having started in the field for which the assets were provided.

Assets leased to a person for the purposes of a petroleum trade are treated in a broadly similar manner. The allowance is available to the lessor, provided it directly bears the burden of wear and tear. The legislation excludes from development expenditure any amounts expended on vehicles, land and buildings, machinery or plant, or structures for processing or storing petroleum won (other than initial treatment or storage) and the acquisition of, or rights in or over, deposits of petroleum. Interest payments are also excluded.

Exploration expenditure

Irish tax legislation provides for a 100% allowance for exploration expenditure against the profits of a petroleum trade. The allowance is due when petroleum extraction activities begin. Exploration expenditure is defined as a capital expenditure on petroleum exploration activities, but excludes any interest payments. If expenditure qualifies as development expenditure, it cannot also be exploration expenditure. To the extent that a loss is created by the exploration allowance, this can be carried forward against future profits of the same petroleum trade.

An allowance is given for successful and abortive exploration expenditure, subject to the abortive expenditure having been incurred not more than 25 years before the commencement of the petroleum trade against which profits such allowances are claimed. However, an abortive expenditure incurred more than 25 years previously on a field that subsequently begins production may still be claimed upon commencement of production.

No allowance for exploration expenditure will be made to the extent that the exploration expenditure is reimbursed to the claimant. A clawback provision applies (by way of a balancing charge on the amounts previously allowed) if a disposal or part disposal of an asset takes place, representing the amount of the expenditure with respect to which the allowance was originally made. The maximum balancing charge is limited to the amount of the allowances made or, in the case of a partial disposal, the appropriate part of that amount.

A person who buys assets representing exploration expenditure connected with a relevant field may claim an allowance if that person carries on a trade that consists of, or includes, working that field or part of that field. The allowance cannot exceed the exploration expenditure originally incurred or, if less, the price paid for the assets representing that expenditure.

If there is a sale or transfer of assets representing an exploration expenditure before a petroleum trade commences, the allowance due to the claimant is reduced by the proceeds of the sale or transfer.

A provision applies for granting an allowance for an exploration expenditure against the profits of a petroleum trade carried on by one company if the exploration expenditure was incurred by another company and one company is a wholly owned subsidiary of the other company, or both are wholly owned subsidiaries of a third company. A transferred expenditure is treated as incurred by the transferee company at the time it was actually incurred by the transferor, thus preventing old abortive exploration expenditure from being used by the transferee any later than it could have been used by the transferor. A provision also applies to avoid the duplication of allowances.

Abandonment expenditure

"Abandonment expenditure" is expenditure incurred on "abandonment activities" in relation to a field or part of a field. Abandonment activities in relation to a field or part of a field are activities of a company that comply with the requirements of a petroleum lease held by the company with respect to closing down, decommissioning or abandoning the field or part of it. This provision includes dismantling and removing pipelines used to bring petroleum to dry land.

A 100% allowance applies for abandonment expenditure for the chargeable period in which the expenditure is incurred. If a loss arises due to an insufficiency of income to absorb the allowance, the loss may be carried back to offset the income from the petroleum activities of the three previous years. An offset is made against later periods in priority to the earlier periods.

A provision is made for a carryforward of unused abandonment losses if a company permanently discontinues one petroleum trade and subsequently commences a new one. In these circumstances, the losses are deductible in the first chargeable period of the new petroleum trade carried on by the company.

An abandonment expenditure incurred after a petroleum trade has ceased is brought back into the final period of trading. If this creates a loss, that loss may be carried back for the three years preceding the final year of trading.

D. Incentives

Losses

Tax losses may be carried forward indefinitely against profits for the same petroleum trade. However, if within a three-year period there is both a change in ownership (effectively more than 50%) and a major change in the nature or conduct of the trade, relief for losses carried forward may be denied.

Research and development

The R&D tax credit regime provides for a 25% tax credit for expenditure on qualifying R&D activities. This is in addition to the normal corporate tax deduction.

Where the company's corporation tax liability does not exceed the available R&D tax credit, any excess R&D credits may be carried back against corporate tax of the preceding accounting period. Any remaining excess R&D credits may be cash refunded by the Irish tax authorities (Revenue) over a three-year period. Where the company does not wish to claim a repayment of the credit, the credit will be carried forward indefinitely.

A limit is placed on the amount of the refund available to a company, which is the greater of:

- The corporation tax payable by the company in the previous 10 years
- The aggregate of the total payroll tax liabilities (including employers' social insurance) combined for the current and preceding accounting periods

In the case of a company, "expenditure on R&D" is expenditure that has been incurred on R&D activities carried on by that company in the European Economic Area (EEA) in a relevant period. The expenditure must qualify for tax relief in Ireland, and, in the case of an Irish resident company, it must not qualify for tax relief in any jurisdiction other than Ireland. The R&D credit is in addition to any tax relief that may be available by way of a deduction in computing trading income, or by way of capital allowances.

"R&D activities" mean systematic, investigative or experimental activities in a field of science or technology and being one or more of basic research, applied research or experimental development. Activities do not qualify as R&D activities unless they seek to achieve scientific or technological advancement and involve resolution of scientific or technological uncertainty.

The R&D tax credit claim must be made within 12 months of the end of the accounting period (for tax purposes) in which the expenditure was incurred.

E. Withholding taxes

Dividends, interest and royalties

Under Irish domestic law, dividends, interest and royalties are prima facie subject to a withholding tax (WHT) of 20%. However, interest paid by a company in the course of a trade or business to a company resident in a European Union (EU) Member State, or in a country with which Ireland has a double taxation agreement, is exempt from WHT, provided the recipient country generally imposes tax on such interest receivable. Furthermore, under Irish domestic law, WHT on royalties applies only to certain patent royalties (in which Revenue clearance is not obtained, where appropriate) and to other payments regarded as "annual payments."

In relation to dividends, exemptions from dividend withholding tax (DWT) are provided for certain nonresidents. The principal exemptions are for:

- Nonresident companies under the control of persons resident in an EU Member State or in a country with which Ireland has a double taxation agreement (provided these persons are not under the control of persons not resident in such countries)
- Nonresident companies, or 75% parent companies of nonresident companies, the principal class of shares of which is substantially and regularly traded on a recognized stock exchange
- Companies not controlled by Irish residents that are resident in an EU Member State or a tax treaty country

Third-party declarations are no longer required to obtain this exemption. Instead, a self-assessment system applies whereby the nonresident company declares that it meets one of the conditions above. DWT does not apply to dividends covered by the EU Parent–Subsidiary Directive (subject to compliance with a bona fide parent test).

Branch remittance tax

Branch remittance tax does not apply in Ireland.

Relevant contracts tax

Relevant contracts tax (RCT) is a withholding tax under Irish domestic law that applies to persons engaged in the construction, meat processing and forestry industries. Unfortunately, the RCT provisions are very widely drawn, and the definition of "construction operations" brings "operations which form an integral part of, or are preparatory to, or are for rendering complete, the drilling for or extraction of minerals, oil, natural gas or the exploration for, or exploitation of, natural resources" within the ambit of RCT. The Irish Revenue had historically taken the view that definition of qualifying operations extended to activities carried on in a "designated area." Legislation has been enacted to provide that, with effect from 1 January 2016, this is the case.

Effective from 1 January 2012, the administration and compliance aspects of the RCT regime have moved to an electronic platform (from the previous paper-based system), with principal contractors required to communicate electronically with the Revenue via the Revenue On-Line Service (ROS) or other approved software system. Under the new system, the Revenue will issue an electronic deduction authorization to the principal contractor, stating the withholding tax rate to be applied to the specific subcontractor (i.e., 0%, 20% or 35%). By improving their tax compliance position, subcontractors can reduce the withholding rate assigned by the Revenue. Principal contractors are exposed to interest and penalties if they are found not to be compliant with the RCT regime.

The Revenue will automatically credit any RCT deducted to the subcontractor's tax record. This credit will be available for offset against other tax liabilities of the subcontractor as they arise or for repayment annually. The RCT regime extends to nonresident principals and subcontractors.

F. Financing considerations

Thin capitalization and interest quarantining

At present, Ireland does not have legislation dealing with thin capitalization and interest quarantining.

G. Transactions

Asset disposals

If a company that carries on a petroleum trade disposes of an asset representing an exploration expenditure, it is subject to a balancing charge calculated by reference to the proceeds received for the disposal. If the disposal takes place prior to the commencement of a petroleum trade, the exploration allowance to be made to the company when it commences its petroleum trade is reduced by the amount of any consideration in money or money's worth received on the disposal.

A disposal of an asset representing development expenditure is similarly subject to a balancing charge calculated by reference to the proceeds received for the disposal.

Farm-in and farmout

The legislation provides that changes in license interests at the preproduction stage that are approved by the Minister for Communications, Energy and Natural Resources do not give rise to chargeable gains if their sole purpose is the furtherance of exploration, delineation or development of a licensed area (i.e., an area licensed under the 1975 or 1992 licensing terms or subsequent licensing terms).

The legislation operates by defining a "relevant period" in relation to such a disposal as being a period beginning 12 months before and 3 years after the disposal. If the consideration received on a disposal is wholly and exclusively applied within the relevant period for the purposes of either or both petroleum exploration activities and searching for and winning access to petroleum in a relevant field, the disposal is not treated as a disposal for the purposes of capital gains tax (CGT). Therefore, no chargeable gain (or allowable loss) can arise. On a subsequent disposal of an asset acquired, brought into being or enhanced in value by the application of the consideration received, the consideration is not deductible in calculating the gain on the subsequent disposal (i.e., it does not form part of the base cost).

The legislation also treats the exchange of license interests as not involving any disposal or acquisition. It treats the asset given and the asset received as the same asset acquired, in the same manner as the asset given was acquired.

For an exchange of license interests where one party receives consideration in addition to the license interest taken by that party, the exchange rule set out above does not apply to that party unless the additional consideration is applied in full in the same manner as set out above. In this way, the disposal of the portion of the license interest that is represented by the consideration received is treated as a partial disposal for which the disposal provisions set out above apply.

If a party to an exchange of license interests gives consideration in addition to the license interest, the portion of the license interest received represented by the additional consideration is regarded as an asset that has a basis equal to the consideration given.

Selling shares in a company

Irish tax legislation contains substantial shareholding exemption provisions. However, they do not apply if the shares (other than shares quoted on a stock exchange) being sold derive the greater part of their value from exploration or exploitation rights in a designated area. If unable to exploit the substantial shareholding exemption, a resident shareholder company is liable for CGT on the disposal of shares in a company that holds exploration or exploitation rights in a designated area.

A nonresident shareholder company is also liable for CGT on a disposal of shares in a company that holds exploration or exploitation rights in a designated area. This is because Irish domestic law deems a gain on a disposal of shares that derive their value or the greater part of their value, directly or indirectly, from exploration or exploitation rights in Irish designated waters to be a gain accruing on the disposal of assets situated in Ireland. This has the effect of bringing the gain into the charge to CGT at a rate of 33%.

H. Indirect taxes

Import duties

Duties apply to the importation of goods.

If goods are imported directly to a rig that is located outside Irish territorial waters, there are no Irish customs duty issues. However, if goods are brought to the rig via Ireland, Irish customs duties issues arise (end-use authorizations). There is also the possibility for properly authorized importers to avail of "land-based operational bases," which allows duty-suspended stock to be stored or subjected to certain operations while remaining insulated from customs duty. On the assumption that correct procedures are put in place, Irish customs duty should not be a cost.

Excise duties

A European Community excise regime governs the production, processing and holding of excisable products under duty suspension within each EU Member State (including Ireland) as well as all intra-Community movement of excisable products. The rates of excise duty on mineral oils in Ireland (known as mineral oil tax) vary depending on the type of oil.

Excise duty on direct imports into Ireland of most excisable products from outside the fiscal territory of the Community is payable at the time of import unless the products are removed to a tax warehouse. In the case of excisable products dispatched to or received from other EU Member States, an intra-Community warehousing network allows duty-suspended movement of products to the premises of receipt, with excise duty being subsequently paid on release in the member state of destination. Excisable products on which duty has already been paid and that move to another member state are liable to excise duty in the member state of destination. In such cases, the excise duty paid in the member state of dispatch may be reclaimed.

Carbon tax

Carbon tax at a rate of €15 per metric ton of carbon dioxide (CO_2) emitted was introduced in Ireland in 2009. The national budget for 2012 increased the rate to €20 per metric ton of carbon dioxide. The current rates of carbon tax applied to mineral oils vary from €32.86 to €61.75.

Persons who receive, either from a tax warehouse or directly by importation, mineral oils that are exclusively for a use covered by their greenhouse gas emissions permit, can obtain oils free of the carbon charge.

Natural Gas Carbon Tax applies to supplies of natural gas to consumers In Ireland. A rate of €4.10 per megawatt hour has applied since 1 May 2012. A relief from the tax applies if it is shown to the satisfaction of the Revenue Commissioners that the gas is to be used solely for the generation of electricity.

VAT

Value-added tax (VAT) applies to the supply of goods and services, the importation of goods and intra-Community acquisitions made in the territory of Ireland.

If a company is not established in Ireland and it undertakes activities outside the 12-nautical-mile limit from the shore of Ireland (and thus outside the EU), the supply of those activities is deemed to occur outside the jurisdiction. In these circumstances, the company is not entitled to register for Irish VAT (unless it has an establishment in Ireland). Supplies of goods from Ireland to such an offshore location are charged at a zero rate because they are effectively exports.

If goods or services supplied to an offshore company are liable to Irish VAT, VAT reclaims may be made through the electronic VAT refund (EVR) procedure (if the claimant company is established in the EU) or the EU 13th Directive reclaim process (if the claimant is established outside the EU). Alternatively, if an offshore company has an administrative office in Ireland that would constitute an establishment for VAT purposes, it may be allowed to register for VAT in Ireland in order to recover any Irish VAT incurred through its Irish VAT returns.

An offshore company that operates outside the Irish jurisdiction makes supplies that are outside the scope of Irish VAT, and accordingly, any invoices raised by the company are also outside the scope of Irish VAT.

Stamp duty

Stamp duty applies to certain documents that are executed in Ireland or relate to Irish property or to something done or to be done in Ireland. Stamp duty is chargeable under different heads, with the most significant related to the conveyance or transfer of property on a sale. Stamp duty can represent a significant cost. The rate applicable to transfers of nonresidential property is 6% (previously 2%).[4] The rate of stamp duty applicable to transfers of Irish-registered shares is 1%. Stamp duty is payable by the purchaser.

Because stamp duty is a tax on documents, if assets such as plant and machinery pass by delivery and no document evidences the transfer, no stamp duty should arise.

Also, full relief from stamp duty can apply to the transfer of property between companies that are 90% associated. An exemption from stamp duty is provided

4 *The 6% rate applies to instruments executed on or after 11 October 2017. The Finance Act 2017 provides for transitional arrangements. Under the arrangements, a 2% rate of duty is chargeable on instruments executed before 1 January 2018 if there is a binding contract in place before 11 October 2017 and if the instrument contains a certificate.*

for the grant of a license or lease or the sale, assignment or transfer of such license and lease granted under the Petroleum and Other Minerals Development Act 1960. The exemption extends to the sale, assignment or transfer of any right or interest in any such license or lease.

I. Other

Rules for valuation of petroleum in certain circumstances

For accounting periods commencing on or after 1 January 2011, Irish transfer pricing regulations apply. These regulations apply to intercompany trading transactions to impose the arm's-length principle and documentation requirements.

Irish legislation provides rules for the valuation of petroleum disposed of other than by way of sale at arm's length or appropriated for use in activities that fall outside the ring fence (e.g., if the oil is appropriated by a production company for use in its own refinery).

Petroleum disposed of other than by way of sale at arm's length is treated as disposed of for a consideration equal to the market value at the time of disposal. Petroleum that is "relevantly appropriated" for use in activities outside the company's ring-fenced activities without being disposed of is treated, for the purposes of the ring-fenced activities and the activities to which it is appropriated, as having been sold and bought, respectively, for a price equal to its market value at the time it is appropriated.

The market value of petroleum at any time is the price that the petroleum could be expected to fetch in a sale on the open market at that time.

Employee taxation

Income tax

Irish tax legislation brings into charge income arising from the exercise of employment in Ireland, whether or not an individual is tax resident in Ireland (although there are some exemptions from this charge, which are discussed below). The charge extends to both income tax and the universal social charge (USC). The legislation provides that duties performed in a designated area in connection with exploration or exploitation activities are treated as performed in Ireland. Thus, income tax and the USC arise on an individual under domestic legislation, but they might be mitigated or exempted under a relevant double tax treaty.

An Irish income tax charge will not generally apply if an individual spends fewer than 30 working days in Ireland (which, for this purpose, includes a designated area of the continental shelf) in a fiscal (calendar) year. There will therefore not be any income tax, USC liability or withholding requirement if the individual spends fewer than 30 working days in Ireland.

A working day is any day in which any work is performed in the State.

If no exemption is applicable, an obligation arises on a foreign employer to withhold income tax, pay-related social insurance (as applicable — see next subsection) and the USC under the Pay As You Earn (PAYE) system from individuals that exercise duties in Ireland, regardless of whether those individuals ultimately have a tax liability in Ireland. If the employer is a nonresident and does not comply with this obligation, the entity benefiting from the services in Ireland may be held liable. However, two exemptions from the requirement for the employer to operate Irish PAYE exist.

The first exemption states that PAYE withholding will not be required if:

1. The individual is resident in a country with which Ireland has a double taxation agreement and is not resident in Ireland for tax purposes for the relevant tax year.
2. There is a genuine foreign office or employment.
3. The individual is not paid by, or on behalf of, an employer resident in Ireland.
4. The cost of the office or employment is not borne, directly or indirectly, by a permanent establishment in Ireland of the foreign employer.

5. The duties of that office or employment are performed in Ireland for not more than 60 total working days in a year of assessment and, in any event, for a continuous period of not more than 60 working days.

The Irish tax authorities have recently (December 2016) stated that, with regard to condition 3 above, in line with Organisation for Economic Co-operation and Development (OECD) guidance, it will not accept that the individual is not paid by, or on behalf of, an employer resident in Ireland if the individual is:

- Working for an Irish employer in which the duties performed by the individual are an integral part of the business activities of the Irish employer
- Replacing a member of staff of an Irish employer
- Gaining experience working for an Irish employer

Or

- Supplied and paid by an agency (or other entity) outside the State to work for an Irish employer

The release from the obligation to operate PAYE will not be granted (i) simply because the remuneration is paid by a foreign employer and charged in the accounts of a foreign employer or (ii) where the remuneration is paid by a foreign employer and the cost is then re-charged to an Irish employer.

The second exemption states that condition 5 above may be extended to 183 days if an employee pays withholding taxes in his or her home country on the same income, but only if conditions 1 through 4 above are satisfied. In this instance, it would also be necessary for the employer to apply to the Irish Revenue for clearance from the obligation to operate Irish PAYE. This clearance must be applied for within 21 days of the individual commencing his or her employment duties in Ireland. If Revenue clearance is not granted or not due, the obligation to operate Irish tax remains.

The information set out above reflects the legislation and Revenue practice at the current date. We understand that the Revenue is currently in the process of reviewing and updating its published guidance on short-term business travelers. It is expected that the updated guidance will be published in the coming months. Pending any update, the treatment outlined above will be applied.

Social insurance

Pay-related social insurance (PRSI) is payable with respect to every individual who exercises duties of employment in Ireland, regardless of the duration. Various classes of contribution apply, depending on the nature of the employment and the level of the emoluments. The most common class is A1, which imposes a charge of 10.85% on the gross earnings (including benefits) of the employer and 4% on the employee. There is no ceiling on the earnings liable to employer or employee contributions.

A charge to PRSI can be avoided only if the employer provides an appropriate authorization from the employee's home country to remain within the home country's social insurance regime. The authorization may be either an E101/A1 form (for EU countries, Iceland, Liechtenstein, Switzerland and Norway) or a Certificate of Coverage (for Australia, Canada (including Quebec), New Zealand, the United States, Japan and South Korea). For countries not covered by the E101/A1 or Certificate of Coverage provisions, there may be an entitlement to an exemption from PRSI for the first 52 weeks of a posting in Ireland. Advice should be sought on the specific conditions applicable to this exemption.

Israel

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Israel has an income tax regime that is applicable across all industries, and it has a windfall tax for oil and gas activities.

- Corporate income tax (CIT) rate — 23%
- Capital gains tax (CGT) rate — 23%
- Windfall profits tax rate — 0% up to 46.8%
- Value-added tax (VAT) rate — 17%
- Incentives:
  - A large number of incentives are offered.
  - Losses may be carried forward indefinitely.

B. Fiscal regime

Corporate income tax

The income tax regime is applicable across all industries. Resident companies are subject to Israeli tax on their worldwide income. Nonresident companies are subject to Israeli tax on income accrued or derived in Israel, unless otherwise provided for in an applicable tax treaty.

A company is considered resident in Israel for Israeli tax purposes if either of the following applies:

- The company is incorporated in Israel.
- The company's business is controlled and managed in Israel.

Effective from 1 January 2018, the regular rate of company tax is 23% for 2017 (24% for 2017). The combined Israeli taxes on profits for 2018, taking into account the 30% withholding tax (WHT) on dividends paid to shareholders holding 10% or more of the company (counted as "material shareholders") and the 25% WHT imposed on shareholders holding less than 10% of the company, are:

- Material shareholders — 46.1% for 2018. For 2018, individual shareholders whose taxable income exceeds NIS641,880 will be subject to an additional 3% tax rate on their taxable income that is in excess of the NIS641,880 threshold.
- Other shareholders — 42.25%. For individual shareholders, an additional tax of 3% may apply as described in the preceding bullet point.

The dividend WHT rates mentioned above may be reduced in accordance with applicable tax treaties.

Determination of trading income

Taxable income is based on financial statements that are prepared in accordance with generally accepted accounting principles and derived from acceptable accounting records. In principle, expenses are deductible if they are wholly and exclusively incurred in the production of taxable income. Various items may require adjustment for tax purposes, including depreciation, research and development (R&D) expenses, and vehicle and travel expenses.

Payments subject to WHT, such as salaries, interest and royalties, are not deductible unless the requisite tax is withheld and paid to the tax authorities.

Provisions

Bad debts are deductible in the year they become irrecoverable. Special rules apply to employee-related provisions, such as severance pay, vacation pay, recreation pay and sick pay.

Tax consolidation

Subject to certain conditions, consolidated returns are permissible for a holding company and its industrial subsidiaries if the subsidiaries are all engaged in the same line of production. For this purpose, a holding company is a company that has invested at least 80% of its fixed assets in its industrial subsidiaries and maintains control of at least 50% (or two-thirds in certain cases) of various rights in those subsidiaries. For a diversified operation, a holding company may file a consolidated return with the subsidiaries that share the common line of production in which the largest amount has been invested.

Group returns may also be filed by an industrial company and industrial subsidiary companies if the subsidiaries are at least two-thirds controlled (in terms of voting power and appointment of directors) by the industrial company and if the industrial company and the subsidiaries are in the same line of production.

Detailed rules concerning the deferral of CGT apply to certain types of reorganizations, including corporate mergers, divisions and shares-for-assets exchanges. In many cases, an advance ruling is necessary.

Holding companies and participation exemption

To qualify for the participation exemption, an Israeli holding company must satisfy various conditions, including the following:

- It must be incorporated in Israel.
- Its business is controlled and managed in Israel only.
- It may not be a public company or a financial institution.
- It must not have been formed in a tax-deferred reorganization.
- For 300 days or more in the year, beginning in the year after incorporation, the holding company must have an investment of at least NIS50 million in the equity of, or as loans to, the investee companies, and at least 75% of the holding company's assets must consist of such equity investments and loans.

Specific conditions should be satisfied by a foreign investee.

An Israeli holding company is exempt from tax on the following types of income:

- Capital gains derived from the sale of an entitling shareholding in an investee company
- Dividends distributed during the 12-month minimum shareholding period with respect to an entitling shareholding in an investee company
- Interest, dividends and capital gains derived from securities traded on the Tel Aviv Stock Exchange
- Interest and indexation amounts received from Israeli financial institutions

In addition, dividends paid by Israeli holding companies to foreign resident shareholders are subject to a reduced rate of dividend WHT of 5%.

Capital gains and losses

Resident companies are taxable on worldwide capital gains. Capital gains are divided into real and inflationary components. The following are descriptions of the taxation of these components:

- Effective from 2018, for companies the tax rate on real capital gains is 23% (24% in 2017) and 30%/25% for individual shareholders; an additional 3% tax rate may apply as detailed above.
- The inflationary component of capital gains is exempt from tax to the extent that it accrued on or after 1 January 1994, and is generally taxable at a rate of 10% to the extent that it accrued before that date.

Unless a tax treaty provides otherwise, nonresident companies and individuals are in principle subject to Israeli tax on their capital gains relating to Israeli assets. Exemptions are available for disposals of certain types of Israeli securities and subject to certain conditions. Foreign resident companies pay CGT in accordance with the rules and rates applicable to residents, as described above. However, nonresidents investing with foreign currency may elect to apply the relevant exchange rate rather than the inflation rate to compute the inflationary amount.

Generally, a foreign resident may be exempt from taxation on capital gains, when the capital gain is derived from the sale of a security of an Israeli resident company and then is subject to the fulfillment of the conditions of the Article. However, such an exemption will not apply, among other things, to gains generated from the sale of a security of a company that has derived most of its assets in the prior two years from the right to exploit natural resources.

Windfall tax

According to the Natural Resources Profits Taxation Law, 2011 (the Natural Resources Law), in effect from 10 April 2011, oil profits from an oil project will be levied in the relevant tax year. The levy is designed to capitalize on the economic dividend arising from each individual reservoir. The levy will be imposed only after the investments in exploration, development and construction are fully returned plus a yield that reflects, among other things, the developer's risks and required financial expenses. The levy is progressive and will be at a relatively low rate when first collected, but it will increase as the project's profit margins grow.

The basic economic unit used to calculate the collection of the levy is an oil project, based on a single oil right that is an early permit, license or lease, according to the oil project's current development stage.

According to the Natural Resources Law, the levy rates will be determined using the R-factor, which establishes the project's profitability. Oil profits from an oil project will be calculated for every individual tax year at the end of that year as the difference between total current receipts in the tax year and total current payments in that year. The R-factor formula takes into consideration the levy on oil and gas profits in the early years, the timing of discovery and production, investments, normative interest, and certain expenditures, including royalties paid to the government. The R-factor will be calculated for each tax year, and a relative levy factor will be calculated for each month in an amount equal to retained profits divided by accrued investments. The levy rate will be 0% as long as the relative levy factor is less than 1.5. Once a project's relative levy factor reaches 1.5, the levy rate will be 20%. This rate will increase linearly as the relative levy factor increases, up to a maximum of 46.8% (which is imposed when the relative levy factor is 2.3).

It has been determined that the levy will be a deductible expense for corporate tax purposes.

In order to allow tax benefits arising from the allocation of taxable income or losses to the qualifying holders and to allow effective tax assessment and collection procedures, specific provisions regarding the taxation of oil partnerships were determined that will apply to the taxable income or losses of the oil partnership in the tax year 2011 onward.

It is determined that the owner of the oil right will have a special deduction from the base price of the "deductible asset" in its possession, effective from the tax year in which commercial production commences. This special deduction — 10% annually — will replace the depreciation of the deductible asset pursuant to the provisions of Section 21 to the Income Tax Ordinance ("ITO") for each of the holders of the oil right, pro rata, to their share in the project. The Natural Resources Law states that the depreciation provisions applicable pursuant to the ITO apply to such deduction as if it were depreciation, under the necessary adjustments.

The Natural Resources Law prescribes transitional provisions that allow a gradual transition to the determined system in order to prevent any impairment to the construction of the oil projects that are in planning and construction stages and that are designed to supply oil to the Israeli market in the coming years.

On 17 December 2015, the Israeli Prime Minister, who also serves as the Minister of Economy, signed the Natural Gas Framework (the Framework) in order to propel the halted development of Israel's offshore natural gas resources, in the face of much opposition in the regulatory, political and environmental spheres. According to the Framework, a memorandum will promptly be disseminated for the amendment of the Natural Resources Law to include revisions to eliminate tax loopholes and to provide clarifications and processes for assessment and collection of tax.

On 17 November 2017, a memorandum for the amendment of the Natural Resources Law was published. The memorandum consists of mainly the following: correction of the determination of "intakes" as to include intakes generated by the peripheral activities to the sale of oil and gas; correction of the method according to which the various financial reports was conducted, from "cash basis" to "accumulative basis"; prolongation of the time period for the ITA to perform tax assessment procedures; encouraging and incentivizing the exploration of smaller oil and gas fields.

As for 8 March 2018, the memorandum is yet to be finalized and assimilated into the Natural Resources Law.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Depreciation

Depreciation at prescribed rates, based on the type of asset and the number of shifts the asset is used, may be claimed with respect to fixed assets used in the production of taxable income.

Accelerated depreciation may be claimed in certain instances. For example, under the Inflationary Adjustments regulations (accelerated depreciation), for assets first used in Israel between 1 June 1989 and 31 December 2013, industrial enterprises may depreciate equipment using the straight-line method at annual rates ranging from 20% to 40%. Alternatively, industrial enterprises may depreciate equipment using the declining-balance method at rates ranging from 30% to 50%.

The following are some of the standard straight-line rates that apply primarily to nonindustrial companies:

Asset	Rate (%)
Mechanical equipment	7–10
Electronic equipment	15
Personal computers and peripheral equipment	33
Buildings (depending on quality)	1.5–4
Goodwill	10
Solar energy-producing plant	25

D. Incentives

Capital Investment Encouragement Law

An amendment to the Capital Investment Encouragement Law was effective from 1 January 2011. Significant aspects of the amended law are summarized below.

The law has the following objectives:

- Achieving enhanced growth targets in the business sector
- Improving the competitiveness of Israeli industries in international markets
- Creating employment and development opportunities in outlying areas

Precedence is granted to innovation and development areas. The country is divided into national priority areas, which benefit from several reduced tax rates and benefits based on the location of the enterprise.

A reduced uniform corporate tax rate for exporting industrial enterprises (over 25% of turnover from export activity) is applicable. The reduced tax rate does not depend on a program and applies to the industrial enterprise's entire income. As from 1 January 2017, the reduced tax rates for industrial enterprises are 7.5% for Development Area A and 16% for the rest of the country.

In addition, accelerated depreciation is applicable, reaching 400% of the standard depreciation rate on buildings (not exceeding 20% per annum and exclusive of land) and 200% of the standard depreciation rate on equipment.

As from 1 January 2014, a reduced tax on dividends of 20% (15% previously) is imposed without distinction between foreign and local investors. On the distribution of a dividend to an Israeli company, no WHT is imposed.

On 16 May 2017, the Israeli Parliament Finance Committee approved tax regulations that formally conclude the legislation process of Israel's new Intellectual property (IP) tax regime. Accordingly, the recently enacted tax incentives law immediately entered into force, with retroactive effect as of 1 January 2017.

The new legislation provides qualifying companies with reduced corporate tax rates on IP-based income generated after 1 January 2017 as well as on capital gains from the future sale of IP. The reduced tax rates provided for are as follows:

- 6% for a qualifying Israeli company which is part of a group whose global revenue is over ILS10 billion (approx. US$2.5 billion)
- 7.5% for a qualifying company whose group's global revenue is below ILS10 billion and is operating in Jerusalem or in certain northern or southern parts of Israel
- 12% for a qualifying company whose group's global revenue is below ILS10 billion and is operating in other parts of Israel

Moreover, withholding tax on dividends distributed to foreign shareholders holding at least 90% of the shares shall be subject to a reduced rate of 4% for all qualifying companies (regardless of size or location). A unique tax benefit is granted to certain large industrial enterprises, which entitles such companies to a reduced tax rate of 5% in Development Area A and 8% in the rest of the country. Furthermore, fixed-asset grants of 20% to 32% of the investment cost of fixed assets may be granted to enterprises in Development Area A.

Some of Israel's tax treaties include tax-sparing clauses under which regular Israeli taxes, rather than reduced Israeli taxes, may be credited against tax imposed on dividends received from an Israeli company in the investor's country of residence. As a result, the Israeli tax benefits may be partially or fully preserved for an investor in an Israeli company enjoying the benefits of the law.

Oil and gas activity is not entitled to benefits under the Capital Investment Encouragement Law.

Eilat free port

Corporate tax exemptions and other benefits are granted to authorized enterprises in the Eilat free port and free trade area.

Other incentives

Approved industrial, commercial and residential rental properties qualify for reduced company tax rates on rental income (and on gains derived from sales of certain buildings that have a residential element; a building has a residential element if at least 50% of the floor space is rented for residential purposes for a prescribed number of years, according to detailed rules). The reduced rates range from 10% to 18%. A tax holiday or grants may be available to approved industrial properties, depending on their location.

Preferential tax treatment may also be allowed with respect to the following:

- Real estate investment trust (REIT) companies
- International trading
- R&D financing
- Nonresidents' bank accounts

Significant nontax incentives include financial support for the following:

- R&D
- Development of production prototypes
- Investment in new facilities or products to promote competition with foreign companies (trade exposure fund)
- Exporters
- Export agents
- Equipment leasing to approved enterprises

Foreign resident investors may qualify for exemption from CGT in certain circumstances.

Relief for losses

In general, business losses may be offset against income from any source in the same year. Unrelieved business losses may be carried forward for an unlimited number of years to offset business income, capital gains derived from business activities, or business-related gains subject to land appreciation tax (see Section B). According to case law, the offset of losses may be disallowed after a change of ownership and activity of a company, except in certain bona fide circumstances.

Special rules govern the offset of foreign losses incurred by Israeli residents. Passive foreign losses (for example, relating to income from dividends, interest, rent or royalties) may be offset against current or future foreign passive income. Passive foreign rental losses arising from depreciation may also be offset against capital gains from the sale of the relevant foreign real property.

Active foreign losses (relating to a business or profession) may be offset against the following:

- Passive foreign income in the current year
- Active Israeli income in the current year if the taxpayer so elects and if the foreign business is controlled and managed in Israel; however, in the preceding two years and in the following five years, foreign-sourced income is taxable up to the amount of the foreign loss
- Active foreign income and business-related capital gains in future years

E. Withholding taxes

Dividends

A 30% WHT is generally imposed on dividends paid to individual shareholders holding 10% or more of the shares in an Israeli company (material shareholders), and a 25% WHT is imposed on dividends paid to individual shareholders holding less than 10% of the shares in an Israeli company. However, resident companies are exempt from company tax on dividends paid out of regular income that was accrued or derived from sources within Israel. Companies are generally subject to tax at a rate of 25% on foreign dividend income that is paid from a foreign source or from income accrued or derived abroad (foreign-sourced income that is passed up a chain of companies).

A reduced WHT of 15%/20% is imposed on dividends paid out of the income of a company enjoying the benefits of the Capital Investment Encouragement Law.

Interest

An exemption from Israeli tax is available to foreign investors that receive interest income on bonds issued by Israeli companies traded on the Israeli stock exchange.

In addition, interest is exempt from Israeli tax when it is paid to nonresidents on Israeli governmental bonds that are issued for 13 months or more.

Overseas remittances

Israeli banks must withhold tax, generally at the CIT rate of 23% (in 2018), from most overseas remittances unless the remittances relate to imported goods. An exemption or a reduced withholding rate may be obtained from the Israeli tax authorities in certain circumstances, such as when a treaty applies or when the payments are for services that are rendered entirely abroad. A 30% WHT rate applies to dividend payments to recipients who hold 10% or more of the payer entity.

F. Other significant taxes

Other significant taxes are as set out in the table below.

Nature of tax	Rate (%)
VAT, standard rate	17
Wage and profit tax, imposed on financial institutions instead of VAT; this tax is imposed in addition to company tax	17
National insurance contributions on monthly employment income (subject to an upper income limit that changes periodically)	Various
Payroll levy on salaries of foreign employees (although the levy does not apply if monthly salary exceeds twice the average monthly salary)	20
Acquisition tax, imposed on purchasers of real estate rights; maximum rate	5–10
Annual municipal taxes on property	Various

G. Other

Foreign-exchange controls

The Israeli currency is the new Israeli shekel (NIS). On 14 May 1998, exchange control restrictions were abolished.

However, transactional and periodic reporting requirements apply in certain circumstances, principally to Israeli residents when the amounts involved or overseas assets total more than US$5 million. Furthermore, shekel-to-foreign-currency swap transactions and foreign residents' transactions in short-term Israeli government bonds are also sometimes subject to reporting requirements. These reports are filed with the Bank of Israel.

Debt-to-equity rules

No thin capitalization rules are imposed in Israel. However, approved enterprises and approved properties must be at least 30% equity-financed if they received their approval before 1 April 2005.

Transfer pricing

Transactions between related parties should be at arm's length. Detailed transfer pricing regulations apply. An Israeli taxpayer must report on each international transaction undertaken with a related party and indicate the arm's-length amount for such transaction. Advance rulings may be requested regarding transfer pricing.

Free trade agreements

Israel has entered into free trade agreements with Bulgaria, Canada, the European Free Trade Association, the European Union, Mexico, Romania, Turkey and the United States.

Foreign tax relief

A credit for foreign taxes is available for federal and state taxes but not municipal taxes. Any excess foreign tax credit may be offset against Israeli tax on income from the same type in the following five tax years.

Foreign residents that receive little or no relief for Israeli taxes in their home countries may be granted a reduced Israeli tax rate by the Minister of Finance.

Administration

The Israeli tax year is normally the calendar year. However, subsidiaries of foreign publicly traded companies may sometimes be allowed to use a different fiscal year.

Companies are generally required to file audited annual tax returns and financial statements within five months after the end of their fiscal year, but extensions may be obtained.

Companies must normally file monthly or bimonthly reports and make payments with respect to the following taxes:

- Company tax advances, which are typically computed as a percentage of a company's sales revenues
- Supplementary company tax advances with respect to certain nondeductible expenses
- Tax withheld from salaries and remittances to certain suppliers
- VAT

Nonresidents are required to appoint an Israeli tax representative and VAT representative if any part of their activities is conducted in Israel. The VAT representative is deemed to be the tax representative if no other tax representative is appointed. The tax representative is empowered to pay tax out of the foreign resident's assets.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Italian companies and Italian branches of foreign companies are subject to the general Corporate Income Tax Act in Italy, with some specific additional provisions that may apply to the oil and gas sector:

- Royalties – yes
- Bonuses – none
- Corporate income tax rate – 24%
- Regional income tax – 3.9%

The Italian tax regime for oil and gas companies requires the payment of specific concessions to the state, and also royalties to be calculated on the amount of production.

Companies establishing new oil and gas activities (e.g., extraction, distribution, research, tillage or storage) in Italy must apply to the Italian State for certain specific licenses. Once granted, the licenses facilitate the calculation of the concessions due.

A summary of licenses and concessions is as shown in the table below.

Yearly fees for oil and gas concessions	€/km^2
Prospection license	3.59
Research license	7.18
Research license (first extension)	14.37
Research license (second extension)	28.74
Tillage license	57.47
Tillage license (extension)	86.21
Storage license under tillage license	14.37
Storage license without tillage license	57.47

The Italian State also requires payment of certain royalties to be calculated on the gross value of oil and gas production. Such royalties may vary on the basis of the location of production plants (land or sea), and some exemptions are available relating to production value below certain thresholds. For plants established on land, an additional royalty is payable to the so-called *Fondo Idrocarburi*, the purpose of which is to reduce the fuel price of the region in which the plant is located.

A summary of royalties is as shown in the next table.

Production		Exempted production quota	Royalty rate	*Fondo idrocarburi* additional rate
Oil	Land	20,000 tons	7%	3%
	Sea	50,000 tons	7%	
Gas	Land	25 million cubic meters	7%	3%
	Sea	80 million cubic meters	10%	

The abovementioned royalties are not due on the productions dispersed, burned or reinjected into a well.

B. Fiscal regime

Italian tax-resident companies are subject to corporate income tax (CIT or IRES) on their worldwide income, while Italian branches (permanent establishments) of foreign companies are taxed only on their Italian-sourced income. A resident company is a company that has any of the following located in Italy for the majority of the tax year:

- Its registered office
- Its administrative office (similar to the "place of effective management" concept)
- Its principal activity

In addition, a mine, an oil or gas well, a quarry or any other place of extraction of natural resources is also included in the term "permanent establishment."

Nonresident companies are subject to IRES on their Italian-source income only. Certain deemed residency provisions apply to foreign entities controlling an Italian company.

The IRES rate is fixed at 24%, and it is applied to the IRES taxable income.

To determine taxable income, profits disclosed in the financial statements are adjusted for exempt profits, nondeductible expenses, special deductions and losses carried forward.

The following general principles govern the deduction of expenses:

- Expenses are deductible if and to the extent to which they relate to activities or assets that produce revenue or other receipts that are included in income.
- Expenses are deductible in the tax year to which they relate (accrual basis rule). Exceptions are provided for specific items, such as compensation due to directors, which is deductible in the tax year in which it is paid.

Write-offs of the value of Italian and foreign shareholdings may not be deducted.

Starting from fiscal year (FY) 2016, companies may deduct expenses incurred in transactions with enterprises and consultants resident in non-EU tax havens, without any specific limitation.

Additional surcharge imposed on oil, gas and energy companies

An additional surcharge tax was levied on companies and Italian branches of foreign companies operating in the oil, gas and energy sector with revenues exceeding €3 million and a taxable income exceeding €300,000 in a previous tax year. This surcharge tax, also known as the "Robin Hood" tax, was levied at the rate of 6.5% of the IRES taxable basis. However, in February 2015, the Italian Constitutional Court declared that the surcharge is unconstitutional. The Court affirmed that the Robin Hood tax is incompatible with some principles of the Italian constitutional chart and that it is no longer justified by the economic conjuncture. The Court's decision has determined the repeal of the Robin Hood tax with effect from the day after the constitutional decision (i.e., 12 February 2015). The repeal will not apply retroactively. Nevertheless, it is important to point out that, according to the interpretation given by the Provincial Tax Court of Reggio Emilia (Decision No. 217/3/2015) to the mentioned Constitutional Court decision, the inapplicability of the retroactivity should not apply to the pending cases but only to the defined ones. This interpretation should be in due course confirmed by the Regional Court and the Supreme Court in the higher levels of jurisdiction. Consequently, the aforementioned scenario could change again.

Regional tax on productive activities

Resident and nonresident companies are subject to a regional tax on productive activities (so-called IRAP) on their Italian-sourced income. The taxable basis of such tax is represented by the net value of production, which is calculated by subtracting the cost of production from the value of production and applying some adjustments provided by law.

IRAP is fixed at 3.9%, but each Italian region may vary such rate up to 0.92 basis points. Certain regions further increased the IRAP rate to around 5% for companies operating in the oil and gas sector. Companies generating income in more than one region are required in the IRAP tax return to allocate their taxable base for IRAP purposes among the various regions and to pay the applicable tax to the local tax authorities.

Certain deductions are not allowed for IRAP purposes, such as the following:

- Certain extraordinary costs
- Credit losses
- Labor costs for short-term contract employees
- Interest expenses

Groups of companies

Groups of companies may benefit from tax consolidation and consortium relief. These regimes allow the offsetting of profits and losses of members of a group of companies.

Tax consolidation

Italian tax consolidation rules provide two separate consolidation systems, depending on the companies involved:

1. A domestic consolidation regime is, in principle, available for Italian resident companies only. However, in line with Case C-40/13 of the Court of Justice of the European Union, the Legislative Decree No. 147 of 2015 (hereinafter, Internationalization Decree) introduced the possibility to elect a domestic tax consolidation between two or more Italian sister companies with a common parent residing in any European Union (EU) or qualifying European Economic Area (EEA) countries that grant adequate exchange of information (horizontal consolidation).
2. A worldwide consolidation regime, with slightly different conditions, is available for multinationals.

To qualify for a tax consolidation, more than 50% of the voting rights of each subsidiary must be owned, directly or indirectly, by the common Italian parent company. For domestic consolidation, the election is binding for three fiscal years. The tax consolidation includes 100% of the subsidiaries' profits and losses, even if the subsidiary has other shareholders. Domestic consolidation may be limited to certain entities.

Tax losses realized before the election for tax consolidation can be used only by the company that incurred such losses. Tax consolidation also allows net interest expenses to be offset with spare earnings before income taxes, depreciation and amortization (EBITDA) capacity of another group's company.

The "special" tax realignment (granted by paragraphs 10-bis and 10-ter of art. 15 Law Decree 185/2008)

The "special" tax realignment, granted by paragraphs 10-bis and 10-ter of art. 15 Law Decree 185/2008, provides for the possibility to increase the tax values of controlling equity investments recorded in the consolidated financial statements due to goodwill, trademarks and other intangible assets following an extraordinary transactions. The Financial Law 2018 extends the scope of the "special" tax realignment also to transactions in nonresident controlled companies without a permanent establishment in Italy. The aforesaid extension applies to purchases of controlling participations starting from the tax period before the one in progress as at 1 January 2018, by means of the substitute tax payment set forth by paragraph 10 of the art. 15 law Decree 185/2008, equal to 16%. In order to avoid the double tax deduction of the intangible assets step-up values, the 2018 Budget Law delegates to a measurement of the Italian Revenue Agency the definition of the procedures for implementing the introduced legislation.

Consortium relief

Italian corporations can elect for consortium relief if each shareholder holds more than 10% but less than 50% of the voting rights in the contemplated Italian transparent company. Under this election, the subsidiaries are treated as look-through entities for Italian tax purposes, and their profits and losses flow through to the parent company in proportion to the stake owned. Dividends distributed by an eligible transparent company are not taken into account for tax purposes in the hands of the recipient shareholders. As a result, Italian corporate shareholders of a transparent company are not subject to corporate income tax on 5% of the dividend received.

Transfer pricing

Italy imposes transfer pricing rules on transactions between related resident and nonresident companies. Under these rules, intragroup transactions must be carried out at arm's length. Italian transfer pricing rules do not apply to domestic transactions; however, under case law, grossly inadequate prices in these transactions can be adjusted on abuse-of-law grounds.

No penalties will be levied as a result of transfer pricing adjustments if the Italian company has complied with Italian transfer pricing documentation requirements, allowing verification of the consistency of the transfer prices set by the multinational enterprises with the arm's-length principle. The following documentation is required:

- A "master file," with information regarding the multinational group
- Country-specific documentation, with information regarding the enterprise

The Internationalization Decree clarifies that transfer pricing rules set forth by the Italian Income Tax Code do not apply to transactions that have occurred between resident entities.

Controlled foreign companies

The Internationalization Decree made some relevant changes to the Italian controlled foreign company (CFC) rules.

According to the old rules, the income of a CFC is attributed to the Italian parent under a flow-through taxation principle if the subsidiary is located in a blacklist country unless an advance ruling is obtained under the following alternative exceptions:

- The foreign entity carries out as a main activity an actual industrial or commercial activity in the market of the state or territory in which it is located (first exemption).
  Or
- The participation in the foreign entity does not have the purpose to allocate income to countries or territories with a privileged tax regime, i.e., the income is subject to an adequate level of tax in white-list jurisdictions (second exemption).

CFC legislation also applies to non-blacklist subsidiaries if (i) the effective tax rate applicable to the income of the foreign entity is lower than 50% of the applicable Italian corporate tax rate and (ii) more than 50% of the foreign entity's gross revenues have a "passive income" nature. In this scenario, CFC rules do not apply if the taxpayer proves through a tax ruling that the foreign company is not an artificial arrangement to obtain undue tax savings.

The Internationalization Decree has introduced some changes to the above legislation, in particular:

- The ruling procedure to avoid CFC legislation consequences is no longer mandatory, but it remains as an optional procedure. The conditions required for the exemption from the regime can now be proved during the tax audit process.
- CFC rules apply only to controlled companies as opposed to under the old legislation, which provided a similar regime also for non-controlled subsidiaries under qualifying participations.

On 4 August 2016, the Italian Tax Authorities (ITA) issued Circular No. 35/E (the Circular), providing extensive clarifications on the Italian Controlled Foreign Companies (CFC) regime.

The Circular also summarizes the recent changes to the CFC rules introduced by 2015 and 2016 Budget Laws (Law No. 190/2014[1] and Law No. 208/2015[2]) as well as by Legislative Decree No. 147/2015 (Internationalization Decree[3]). The Circular gives particular attention to the following:

- CFC blacklist countries and blacklist income: as of FY 2016, a blacklist country for CFC purposes is deemed to exist if the relevant nominal tax rate applied is lower than 50% of the Italian tax rate. In this regard, the foreign applicable income taxes shall be considered, while for Italian tax purposes, the nominal tax rate is established by the Corporate Income Tax (IRES) and the Regional Tax on Productive Activities (IRAP).

The presence of an adequate exchange of information between Italy and the foreign state is therefore no longer necessary in order to assess the presence of a blacklist jurisdiction, which now shall be identified on a case-by-case analysis.

To verify whether the foreign income is derived from a blacklist country, the Circular clarified that the FY in which the income has been collected shall be taken into account by the taxpayer.

- Definition of special tax regimes: a blacklist jurisdiction for CFC purposes is also deemed to exist if a "special tax regime" (i.e., more favorable tax provisions than the ordinary rules) applies to the foreign subsidiary. The Circular clarifies that such special tax regime:
  - Applies to all taxpayers satisfying all the requirements laid down in the local tax rules
  - Provides for: (i) a decrease of the applicable tax rate or (ii) exemptions or other erosions of the taxable basis (including notional interest deduction) that de facto result in a lower tax due

A special tax regime agreed between the tax authorities through a ruling procedure does not exclude the application of the CFC provisions.

On the contrary, if a foreign subsidiary was located in a state having a nominal tax rate lower than the 50% of the Italian rate, but was subject to a final tax burden higher than the mentioned 50% due to special applicable tax rules, no CFC regulations would apply (i.e., no special tax regime would exist).

In the case of multiple economic activities only partially subject to special tax regimes, CFC rules would be triggered if, under a prevailing criterion, the majority of the revenue generated were covered by the more favorable tax provisions.

- Clarification on the second exemption to avoid CFC rules — CFC rules do not apply if the Italian parent obtains an advance ruling under the following alternative exceptions: the foreign company carried out as a main activity an actual industrial or commercial activity in the market of the state or territory in which it was located (first exemption); the overseas entity does not constitute an artificial structure aimed at achieving undue tax advantages (second exemption).

The Circular considers that the second exemption might successfully be invoked by the Italian shareholder when any of the following requirements are met:

- More than 75% of its revenues are generated and fully taxed in a white-list country
- A privileged tax regime applies to the foreign subsidiary, which is either (i) resident for tax purposes in a white-list country; (ii) has its place of effective management in a white-list country; or (iii) carries out its main economic activity in a white-list country and the profits generated therein are fully subject to tax
- A white-list foreign subsidiary has a permanent establishment located in a blacklist jurisdiction, but the income attributable to the permanent establishment is fully taxed in the hands of the head office
- Computation of the CFC income: The Circular points out that the CFC income shall be determined in accordance with the applicable Italian Corporate Income Tax rules (save specific exclusions), which must be adopted irrespective of the nature of the entity (e.g., corporation or partnership) or the activity carried out by the latter.
- Clarification Foreign Tax Credit (FTC): If a taxpayer has obtained a positive ruling based on the first exemption contained in the Italian CFC provision (i.e., proper business substance), when dividends are actually paid by the foreign company, the Italian shareholder is subject to full taxation but is allowed to benefit from an underlying FTC for any taxes paid abroad by the blacklist subsidiary. The Circular clarifies that the credit in question is considered as an "indirect" credit, as it is granted for taxes paid by the CFC (i.e., not directly by the Italian shareholder) and falls within the ordinary Italian FTC rules.

As the general FTC rules are concerned, the Internationalization Decree set forth that the right to an FTC is deemed to arise not only with reference to the taxes covered by a treaty between Italy and the foreign State, but also to any other income tax or duty levied on the income generated abroad. In order to seek relief through the FTC, it would therefore be necessary to assess whether the tax levied on the foreign income may be considered as an income tax under the Italian rules.

- Procedural aspects: Pursuant to some changes made by the Internationalization Decree, the ruling procedure to avoid CFC legislation consequences is now no longer mandatory, but it remains as an optional procedure. The conditions required for the exemption from the regime can now be proved during the tax audit process. Accordingly, tax assessments concerning the CFC regime cannot be issued if the taxpayer has not been given the opportunity to provide evidence of one of the mentioned exemptions within 90 days from the clarification request.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Depreciation and amortization

Depreciation at rates not exceeding those prescribed by the specific ministerial decree is calculated on the purchase price or cost of manufacturing. Incidental costs, such as customs duties and transport and installation expenses, are included in the depreciable base. Depreciation is computed on a straight-line basis. Rates for plant and machinery vary between 3% and 15%.

In general, buildings may be depreciated using a 3% annual rate; land may not be depreciated. If a building has not been purchased separately from the underlying land, for tax purposes, the gross value must be divided between the non-depreciable land component and the depreciable building component. The land component may not be less than 20% of the gross value (increased to 30% for industrial buildings). As a result, the effective depreciation rate for buildings is 2.4%.

A tax credit of up to 15% of the costs incurred in excess of the average amount of investment in capital goods in a previous five fiscal years for the purchase of specific tangible assets (engines, turbines, pumps, compressors, valves and fluid power equipment, furnaces, portable power tools, non-domestic equipment for cooling and ventilation, etc.) classified in the category ATECO 28 (equivalent to various NACE categories) and of a minimum amount of €10,000 is available. The assets have to have been purchased in the period from 25 June 2014 to 25 June 2015. The tax credit is divided into three equal yearly amounts, and it is used exclusively in compensation by the F24 model (i.e., the model used for the payment of the taxes).

The budget law for FY 2016 introduces a 40% uplift (i.e., up to a total of 140% tax amortization) for tangible assets whose amortization rate for tax purposes exceeds 6.5%.

Purchased goodwill may be amortized over a period of 18 years. Know-how, copyrights and patents may be amortized over two fiscal years. The amortization period for trademarks is 18 years.

In relation to research expenses and advertising expenses, a company may choose that these expenses be deducted either entirely in the year incurred or in equal installments in that year and in the four subsequent years.

Amortization allowances of other rights may be claimed with reference to the utilization period provided by the agreement.

Under the budget law for FY 2017, the measure will be applicable to new assets that are purchased (or leased under a finance lease agreement) by 31 December 2017; however, real estate assets, pipelines, "rolling stock," airplanes and — as from 2017 — company cars are excluded from the benefit. Assets that are purchased by 30 June 2018 may benefit from the additional depreciation, provided the relevant purchase order is made and at least 20% of the purchase price actually is paid by 31 December 2017.

The extra 40% depreciation deduction also will be extended to apply to new intangible assets (e.g., software, systems, platforms) related to the technological transformation mentioned below (the "Industry 4.0" plan).

The budget law also introduces an extra 150% depreciation deduction (i.e., total tax depreciation of up to 250% of the cost) for new assets acquired for the technological transformation of enterprises, under an initiative known as the Industry 4.0 plan (relating to plant, equipment and machinery whose operations are digitally controlled and/or operated by smart sensors and drives interconnected with a factory's computer systems).

This measure is applicable to assets purchased from 1 January 2017 to 31 December 2017 (or 30 June 2018, provided the relevant purchase order is made and at least 20% of the purchase price actually is paid by 31 December 2017).

The 2018 Budget Law, provides an extension, for the entities investing in new assets from 1 January 2018 to 31 December 2018 (or within 30 June 2019, providing that the purchase orders are accepted by the seller by 31 December 2018 and at least 20% of their price is paid by the same date) and a decrease from 40% to 30% of the extra applicable depreciation.

It also extends the terms for the 150% extra-amortization, proving that the investments have to be made within 31 December 2018, or within 31 December 2019.

Amortization and depreciation for oil and gas distribution and transportation companies

A particular amortization rule applies to companies operating in the gas and electricity distribution and transportation sectors. Such companies have to calculate the tax amortization of goods used for the above-mentioned activity at an amount not higher than the one resulting from dividing the purchase price by the useful life as established by the Italian Authority for Gas and Electricity.

Exploration costs

All costs related to oil and gas exploration in Italy are allowed as a deduction for the purposes of the statement of taxable income.

D. Incentives

Allowance for corporate equity

Italian companies and Italian branches of foreign companies are entitled to a corporate income tax deduction corresponding to the notional interest of any qualifying equity increase that occurred after the 2010 year-end, and this is known as an allowance for corporate equity (ACE). The ACE has been fixed by the Italian government as follows:

- 4.75% for fiscal year 2016
- 1.6% for fiscal year 2017
- 1.5% for fiscal year 2018

The qualifying equity increase must be computed on a yearly basis and corresponds to the positive difference between the equity as at the 2010 year-end and the equity as at the year-end of any following year, to the extent that it derives from the formation of profit reserves available for distribution (or for the setting-off of operating losses) and from cash contributions.

Any cash contribution triggers a qualifying equity increase from the moment of the actual injection (i.e., on a pro rata temporis basis), while any increase deriving from the creation of a profit reserve will count retroactively from the first day of the year — e.g., the creation of a reserve with 2010 profits upon a resolution taken during 2011 will count as an equity increase as of the first day of 2011.

The rule specifically provides that the 2010 year-end equity (i.e., the starting reference value to consider when computing any equity increase for ACE purposes) should not include the 2010 profit. It follows that Italian companies that have set aside 2010 profit will benefit from the 4.75% corporate income tax deduction on such amount. The relevant provisions also specify that the computation of the equity increase should be reduced by any capital distribution to the shareholders, any purchase of participations in controlled companies, and any purchase of going concerns.

In the case of companies incorporated after 2010, the notional deduction is computed on the entire equity resulting at the end of any relevant fiscal year, with no starting reference value.

Tax losses

For IRES purposes only, losses may be carried forward with no time limit and deducted from income for the following periods for a total amount equal to 80% of taxable income. Stricter rules apply to loss carryforwards if ownership of the company is transferred or if the company changes its main activity.

Losses incurred in the first three years of an activity may also be carried forward for an unlimited number of tax periods, but the limit of 80% of the taxable income does not apply.

Under certain circumstances, the company resulting from or surviving after a merger may carryforward unrelieved losses of the merged companies against its own profits for the unexpired portion of the loss carryforward periods.

E. Withholding taxes

Under Italian domestic law, a 26% withholding tax is imposed on loan interest paid to nonresidents. Lower rates may apply under double tax treaty protection.

A 30% withholding tax applies to royalties and certain fees paid to nonresidents. The taxable basis of royalties is usually reduced to 75% of the royalty paid (effective tax rate of 22.5%–75% of the income, taxed at 30% withholding). Lower rates can apply under double tax treaties.

As a result of the implementation of EU Directive 2003/49/EC, withholding tax on interest payments and qualifying royalties paid between "associated companies" of different EU Member States is abolished. A company is an "associated company" of a second company if any of the following circumstances exist:

- The first company has a direct minimum holding of 25% of the voting rights of the second company.
- The second company has a direct minimum holding of 25% of the voting rights of the first company.
- A third company has a direct minimum holding of 25% of the voting rights of both the first company and the second company.

Under the EU directive, the shareholding must be held for an uninterrupted period of at least one year. If the one-year requirement is not satisfied as of the date of payment of the interest or royalties, the withholding agent must withhold taxes on interest or royalties. However, if the requirement is subsequently satisfied, the recipient of the payment may request a refund from the tax authorities.

To qualify for the withholding tax exemption, the following additional conditions must be satisfied:

- The recipient must be a company from another EU Member State.
- The income must be subject to tax in the recipient's jurisdiction.
- The recipient must be the beneficial owner of the payment.

F. Financing considerations

Interest expenses

The deductibility of interest expenses is determined in accordance with an EBITDA test. Under this test, net interest expenses (i.e., interest expenses exceeding interest income) are deductible up to 30% of the EBITDA.

Interest expenses exceeding 30% of the EBITDA can be carried forward with no time limit. Spare EBITDA capacity is available for carryforward.

The Internationalization Decree introduced the following changes for interest expense deductions:

- Dividends received from foreign controlled subsidiaries will be included in the EBITDA of Italian companies for the purposes of computing the 30% EBITDA cap for net interest expense deduction.
- Use of the EBITDA of foreign intragroup entities will be no longer allowed for interest expense deduction purposes.

Foreign-exchange losses

Gains and losses resulting from mark to market of foreign-currency-denominated debts, credits and securities are neither taxable nor tax-deductible. An exception is provided for those gains and losses hedged against exchange risk if the hedging is correspondingly marked to market at the exchange rate at the end of the fiscal year.

Capital gains

Capital gains derived by resident companies or nonresident companies with a permanent establishment in Italy are subject to IRES and IRAP. Gains derived from sales of participations and extraordinary capital gains derived from transfers of going concerns are excluded from the IRAP taxable basis.

Capital gains on assets that have been held for at least three years can be taxed, at the taxpayer's option, entirely in the year of sale or spread in equal installments over a maximum period of five years.

Italian corporate taxpayers may benefit from a 95% participation exemption regime for capital gains derived in fiscal years beginning on or after 1 January 2008 from disposal of Italian or foreign shareholdings that satisfy all of the following conditions:

- The shareholding is classified in the first financial statements closed during the holding period as a long-term financial investment.
- The Italian parent company holds the shareholding for an uninterrupted period of at least 12 months before the disposal.
- The subsidiary actually carries on a business activity.
- The subsidiary is not resident in a tax heaven.

If the conditions described above are not satisfied, capital gains on sales of shares are fully included in the calculation of the tax base for IRES purposes. Capital gains on investments that have been recorded in the last three financial statements as fixed assets may be taxed over a maximum period of five years.

In the case of capital gains derived by nonresident companies without a PE in Italy, most tax treaties prevent Italy from levying taxation on nonresidents deriving capital gains from the sale of Italian participations.

If no treaty protection is available, capital gains derived from sales of a substantial participation in Italian companies and partnerships are subject to tax in Italy, but 41.86% of such gains is exempt. As a result, 49.72% of the gain (58.14% starting from 2018) realized by a nonresident entity from the transfer of any Italian shares is subject to corporate income tax in Italy at a 24% tax rate (i.e., 11.93% ETR for 2017 and 13.95% ETR for 2018), while starting from 2019, it would be subject to the 26% substitute tax. A "substantial participation" in a company listed on a stock exchange requires more than 2% of the voting rights at ordinary shareholders' meetings or 5% of the company's capital. For an unlisted company, these percentages are increased to 20% and 25%, respectively.

Capital gains on "non-substantial participations" are subject to a substitute tax of 26%. However, certain exemptions to the 26% rate may apply under domestic law, such as for the following:

- A nonresident (including a person from a tax haven) selling listed shares
- Nonresident shareholders resident in white-list jurisdictions under specified circumstances

Financial transaction tax

By approving the Financial Year 2013 Budget Law, the Italian Government introduced a new financial transaction tax (FTT) regime. This regime is applicable to the following:

- Cash equity transactions
- Derivatives
- High-frequency trading

Regarding cash equity transactions, the transfer of property of shares issued by Italian companies is subject to an FTT of 0.2% on the value of transaction. This rate is reduced to 0.1% in the case of transactions carried out in regulated markets. The FTT on cash equity transactions is due from the purchaser.

For derivatives, starting from 1 July 2013, a flat FTT — the amount of which amount nonetheless varies depending on the kind of the instrument and the value of the contract — is due on all the operations on derivatives based on shares or other equity financial instruments.

Starting from 2013, financial operations performed in the Italian financial market are subject to a tax on "high-frequency trading" if related to shares, other equity financial instruments or derivatives. The tax is determined by applying the rate of 0.02% on the value of the orders canceled or modified that in a daily market exceed the numerical threshold established by the implementing decree.

A FTT should not apply in certain cases specified in the implementing decree.

G. Indirect taxes

VAT

In Italy, value-added tax (VAT) rates are currently:

- Standard rate — 22%. The standard rate applies to all supplies of goods or services, unless a specific provision allows a reduced rate or exemption.
- Reduced rate — 10%. This rate is applicable to certain services and products, such as certain food products, water, gas, electricity, admission to cultural services and the use of sports installations.
- Reduced rate — 5%. This rate is applicable to provision of some social-health and educative services (e.g., medical diagnostics, provision of hospital and care) by Cooperative Sociali and their consortiums toward certain category of people and to supplies of some herbs (basil, oregano, sage, etc.) and to urban transport services by sea, lake, lagoon and river transport means.
- Reduced rate — 4%. This rate is applicable to supplies of basic necessities and mass-market items, such as certain food products and pharmaceuticals.

For transactions relating to oil and gas activities, the standard rate of 22% is generally applicable, while a 10% rate is applicable to the following cases:

- Gas aimed to be used by company in the mining, agricultural and manufacturing sector, including printing, publishing and similar ones
- Gas, methane gas and liquefied petroleum gas to be directly put into the pipelines network in order to be delivered or to be supplied to enterprises using it to produce electricity (a statement concerning the destination of the gas by the purchaser is required)
- Crude oil, combustible oil and aromatic extracts used to generate, directly or indirectly, electricity, as long as power is not below 1kW; crude oil, combustible oil (except for fluid combustible oil for heating) and filter sands remnants from the processing of lubricant oil, where it contains more than 45% in weight of oil product, to be used directly as combustible in boilers and kilns; combustible oil used to produce directly tractor-strength fuel with engines fixed in industrial, agricultural-industrial plants, laboratories or building yards; and combustible oil other than the special ones to be converted into gas to be put in the civic grid system
- Unrefined mineral oil arising from the primary distillation of raw natural oil or from the processing by plants that convert mineral oil in chemical products of a different nature, with a flash point lower than 55°C, where the distillate at 225°C is lower than 95% in volume and at 300°C is at least 90% in volume, to be converted to gas to be put into the civic grid system
- Petrol products to be used for agricultural purposes and for the fishing in internal waters
- Gas methane administration (*somministrazione*) used for combustion and for living purposes up to 480 cubic meters; administration (*somministrazione*), through distribution grid, of melted petrol gas for living purposes for cooking and hot water production; melted petrol gas included and aimed to be included in bottles from 10kg to 20kg in any phase of the trading

Excise duties

Italy implemented the EU Energy Taxation Directive 2003/96/EC providing for the application of certain excise duties on energy products. Such excises are dependent on the type of energy and its end use.

Local authorities (e.g., regions and municipalities) can levy additional charges on energy products. These vary widely and are very complex due to the number of options that may apply, including different suppliers, place of consumption and the energy use.

Furthermore, it should be pointed out that the energy tax regime on oil is also regulated by Directive 2008/118/EC, implemented in Italy via Legislative Decree No. 48 issued on 29 March 2010 that modified Legislative Decree No. 504/95 (Excise Duties Act).

The abovementioned legislation assumes the following definitions:

- "Authorized warehouse keeper." A natural or legal person authorized by the Customs Authority, in the course of his business, to produce, process, hold, receive or dispatch excise goods under a duty suspension arrangement in a tax warehouse (see Article 4(1) of Directive 2008/118/EC, implemented by Article 5(3) of Legislative Decree No. 504/95 (Excise Duties Act).
- "Tax warehouse." A place where excise goods are produced, processed, held, received or dispatched under duty suspension arrangements by an authorized warehouse keeper in the course of its business:
  - The management of a tax warehouse by an authorized warehouse keeper is subject to authorization by the Customs Authority (see Article 4(11) of Directive 2008/118/EC, implemented by Article 5(1) of Legislative Decree No. 504/95).
- "Registered consignor." A natural or legal person authorized by the Customs Authority of the state of importation to only dispatch excise goods under a duty suspension arrangement upon their release for free circulation (see Article 4(10) of Directive 2008/118/EC, implemented by Article 9 of Legislative Decree No. 504/95).
- "Registered consignee." A natural or legal person authorized by the Customs Authority to receive excise goods moving under a duty suspension arrangement (see Article 4(11) of Directive 2008/118/EC, implemented by Article 8(3) of Legislative Decree No. 504/95).

Even if the current legislation does not provide for a precise definition of "commercial warehouse" for energy products or of a "commercial warehouse keeper," it is possible to affirm that the commercial warehouse is a place where excise goods are held, since excise duties have been already paid (see Article 25 of Legislative Decree No. 504/95). Commercial warehouses need always to be registered, whatever the capacity of the warehouse.

All the aforementioned subjects need to be registered with the Customs Authority for their activities.

As for excise duties on energy products:

- The following products included within the combined nomenclature code CN 2710 19 are subject to taxation at the time of their release for consumption: kerosene (CN 2710 19 21 and CN 2710 19 25), gas oils (from CN 2710 19 41 to CN 2710 19 49), fuel oils (from CN 2710 19 61 to 2710 19 69).
- Natural gas (from CN 2711 11 00 to 2711 21 00) is treated similarly.
- Other products included in the CN 2710 19 range are subject to taxation as long as they are used as motor fuel or as heating fuel (e.g., lubricant oils and bitumen).

Italian legislation provides for a specific tax rate with regard to products listed in the first and second bullet points immediately above. For others, the tax rate to be applied has to be identified "for equivalence," taking into consideration similar products.

The taxpayer is obliged to file a yearly excise return reporting information regarding the amount of natural gas dispatched. The tax return has to be filed by March 31 of the year following the one referred to in the tax return.

The following tables show the main excise duties on oil and gas (last official update of Customs Authorities is as at 1 January 2017; data could change from year to year).

Energy products

Products	Propellant	Heating	Industrial use
Leaded/ unleaded petrol	€728.40 per 1000 liters	N/A	N/A
Kerosene	€337.49064 per 1,000 liters	€337.49064 per 1,000 liters	N/A
Gas oil	€617.40 per 1,000 liters	€403.21391 per 1,000 liters	N/A
Heavy fuel oil			
ATZ (Alto Tenore di Zolfo) with a sulfur content > 1%	N/A	Thick – €128.26775 per 1,000 kg Semi-fluid – €216.92378 per 1,000 kg Fluid – €234.65477 per 1,000 kg Very fluid – €465.15982 per 1,000 kg	Thick – €63.75351 per 1,000 kg Semi-fluid – €168.53796 per 1,000 kg Fluid – €189.49475 per 1,000 kg Very fluid – €461.93403 per 1,000 kg
BTZ (Basso Tenore di Zolfo) with a sulfur content < 1%	N/A	Thick – €64.2421 per 1,000 kg Semi-fluid – €168.90413 per 1,000 kg Fluid – €189.83664 per 1,000 kg Very fluid – €461.95830 per 1,000 kg	Thick – €31.38870 per 1,000 kg Semi-fluid – €144.26449 per 1,000 kg Fluid – €166.83934 per 1,000 kg Very fluid – €460.31597 per 1,000 kg
Liquid petroleum gas (LPG)	€267.77 per 1,000 kg	€189.94458 per 1,000 kg	

For the abovementioned products, the tax obligation arises at the time of their production, including extraction from the subsoil where excise duty is applicable, or at the time they are imported. The excise duties are payable at the time of release for consumption of the product within the state.

As a general rule, the taxpayer is:

- The holder of the tax warehouse from which the products are released for consumption
- The registered recipient who receives the excisable products
  Or
- For the importation of goods subject to excise, the person liable to customs duties

There is an obligation for the taxpayer to electronically register any movement of energy products so that transactions can be monitored across Europe.

The Budget Law 2018, published on the *Official Journal* on 29 December 2017, introduced new rules regarding petrol and diesel to be used as motor fuels introduced in a fiscal warehouse or in a warehouse of a "registered consignee"; in this respect, the general rule provides that the release for consumption from the fiscal warehouse and the withdrawal from the warehouse of a registered consignee are subject to the payment of VAT through the F24 form, without possibility of offsetting the amount with VAT or other taxes. Specific rules regarding the means of applications and the exclusions were further specified through a Ministerial Decree and a Tax Authority Resolution, both published in February 2018.

Moreover, the same law also introduced the obligation to request authorization from the Customs Authority in order to store energy products in third-party tax warehouses or in the warehouse of a registered consignee. For economic operators, who are also tax warehouse managers of energy products in Italy, the aforementioned authorization is replaced by a communication, with annual validity, to be transmitted to the Customs Authority before the first storage of the goods.

Lubricant oils and bitumen

Products	Any use
Lubricant oils	€787.81 per 1,000 kg
Bitumen	€30.99 per 1,000 kg

Lubricant oils (from CN 2710 19 81 to CN 2710 19 99) that are aimed, sold or used for purposed other than combustion and carburation, bitumen (CN 2713 20 00) other lubricant oils and lubricant preparations (CN 3403) and other products as listed by Article 62 of Excise Duty Act, even if not subject to excise according to Directive 96/2003/EC, are subject to a pure domestic energy tax. The specific rate is listed in the Annex 1 to the Excise Duty Act.

For lubricant oils and bitumen, the tax obligation arises at the time of supply to the final consumer. As a general rule, the taxpayer is the supplier with legal seat in Italy, duly registered with the Italian Customs Authority.

Natural gas

Natural gas			
	Carburation	Industrial use	Non-industrial use
Natural gas	€0.00331 per m³	€0.012498 per m³	Annual consumptions: Up to 120 m³: €0.044 per m³ From 120 m³ to 480 m³: €0.175 per m³ From 480 m³ to 1,560 m³: €0.170 per m³ Exceeding 1,560 m³: €0.186 per m³
Natural gas (South of Italy)	€0.00331 per m³	€0.012498 per m³	Annual consumptions: Up to 120 m³: €0.038 per m³ From 120 m³ to 480 m³: €0.135 per m³ From 480 m³ to 1,560 m³: €0.120 per m³ Exceeding 1,560 m³: €0.150 per m³

Natural gas (CN 2711 11 and CN 2711 21) to be used either for civil or industrial use, or for motor use, is subject to excise duty at the moment it is provided to final consumers or at the moment of consumption in case of self-usage.

As per Article 26 of the Excise Duty Act, the taxpayer is:

- The national entity billing the natural gas to final consumers
- The entity that purchases for its own use natural gas from EU countries or third countries, using a network of pipelines or transmission facilities for the product
- The entity that purchases natural gas packaged in cylinders or other containers from EU countries or third countries
- The entity that extracts natural gas for its own use in the state

Stamp duties

There are no significant stamp duties.

Registration fees

There are no registration taxes specifically applicable to the oil and gas sector.

Other significant taxes

No carbon taxes on CO_2 emissions have been introduced yet. However, specific taxes on NOx and SO_2 emissions are applicable. For such emission taxes, reference should be made to the EU Large Combustion Plant Directive 2001/80/EC, implemented in Italy by Legislative Decree 152/2006, to identify the eligible combustion plants.

The following table shows the relevant rates.

Emission taxes	
NOx emission	€209 per ton/year
SO_2 emission	€106 per ton/year

H. Other

Local tax on real estate

A local tax on real estate (also called IMU) has been introduced by the Italian Government, to be calculated as 0.76% of the cadastral value revalued for certain multiples established by law.

Starting from 2016, for oil and gas companies, such cadastral value is to be assumed net of any movable equipment fixed to them and pipelines.

For properties lacking of cadastral value, the taxable basis is represented by the historical cost sustained for the purchase or for the construction of the building, as reported in the financial statements. The cost is revaluated on an annual basis.

Another local tax on real estate (also called TASI) has been recently introduced by the Italian government, to be calculated as 1 per mil of the same taxable basis of the IMU.

Tax treaty protection

Italy has entered into a number of double taxation treaties with other states.

Tonnage tax

As from 1 January 2005, shipping companies may opt for tonnage taxation, which applies for 10 years and is available for "qualified" vessels (i.e., those registered in the Italian international shipping register with a tonnage higher than 100 tons). If the tonnage tax regime is not elected, the ordinary regime for these vessels states that the income attributable to them is reduced by a special deduction of 80%.

In addition, IRAP does not apply to qualified vessels.

Tonnage taxation depends on the net tonnage of the vessel, and is determined as follows:

Tonnage	Daily fixed income per ton (€)
0–1,000	0.0090
1,001–10,000	0.0070
10,001–25,000	0.0040
More than 25,000	0.0020

Tonnage taxation applies to:

a. Qualified owned vessels
b. Qualified bareboat chartered-in vessels
c. Chartered-in (also non-qualified) vessels, but only up to 50% of the tonnage of all the employed vessels (a + b + c). Income from chartered-in vessels with tonnage in excess of 50% is taxed under the ordinary rules[1]

1 *This rule follows a ministerial interpretation dated 26 December 2007.*

d. Italian partnerships (similar to German KG legal structures)
e. Qualified vessels employed in national traffic

In case d in the list above, although partnerships are tax-transparent entities, only partners are eligible to be taxed under the tonnage tax rules.

Capital gains and losses on transactions on qualified vessels are included in the fixed income of the table above.

Shipping groups should apply this taxation to every vessel owned by group companies, although the current understanding is that the law applies only to Italian companies/permanent establishments.

Under certain conditions, income from bareboat-out qualified vessels may not be subject to the tonnage tax but can be reduced by 80%.

Tax returns and tax assessment

Income tax returns must be filed by the end of the ninth month following the end of the company's fiscal year. Companies must make advance payments of their corporate and local tax liability equal to a specified percentage of the tax paid in the previous year.

A tax assessment could be issued by the Italian tax authorities within 5 years following the year subject to assessment, and the 5-year period could be extended up to 10 years in some particular cases.

E-invoicing

Mandatory e-invoicing will apply from 1 July 2018 to trading of petrol and diesel intended for use as motor fuel. E-invoicing will become mandatory for all the other goods starting from 1 January 2019 (unless the transactions are carried out with counterparties that do not have an Italian VAT number).

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime described here applies to all existing and new contracts except production sharing agreements that became effective prior to 1 January 2009 and contracts specifically approved by the President of Kazakhstan.

The generally applicable fiscal regime for exploration and production (E&P) contracts in the petroleum industry consists of a combination of corporate income tax (CIT), rent tax on export, bonuses and royalty-type taxation. Oil and gas production activities are ring-fenced from downstream activities and from each other (i.e., contract by contract) for tax purposes.

Mineral extraction tax

Mineral extraction tax (MET) is a volume-based, royalty-type tax applicable to crude oil, gas condensate and natural gas. Rates escalate depending on volume. Different rates apply, depending on what is produced and whether it is exported or sold domestically.

Bonuses

Subsurface users are expected to pay a signature bonus and a commercial discovery bonus. It is also important to note that the commercial discovery bonus will be abolished in 2019.

Corporate income tax

CIT is applied to all companies at a rate of 20% of taxable income.

Rent tax on export

The tax base is determined as the value of the exported crude oil and crude oil products, including gas condensate, based on the same tax valuation as for MET. The tax rate ranges from 0% to 32%.

Excess profit tax

Excess profit tax (EPT) is calculated annually. The tax is paid at progressive rates on tranches of income that remain after deduction of CIT. The taxable tranches are derived by applying percentages of the deductible expenses.

Capital allowances

Capital allowances are available for CIT and EPT.

Investment incentives

Losses relating to subsurface use contracts can be carried forward for up to 10 years.

Crude oil export duty

Crude oil export duty is currently paid at a progressive rate, which depends on the monthly average market price for crude oil for the previous period.

B. Fiscal regime

In Kazakhstan, oil and gas E&P concessions are referred to as "subsurface use contracts." The taxes applicable to subsurface users are as follows:

Applicable taxes	Rate
Bonuses	Variable
MET	0.5% to 18%
EPT	0% to 60%
Payment for compensation of historical costs	Variable
Rent tax on export	0% to 32%
Excise on crude oil and gas condensate	KZT 0 per ton
Alternative subsurface use tax	0% to 30%
Land tax	Generally immaterial
Asset tax	1.5%
Environmental fees	Variable
Other fees (e.g., fee for the use of radio frequency spectrum, fee for the use of navigable waterways)	Variable
Other taxes and payments	Variable
Value-added tax (VAT)	12%
Crude oil export duty	Variable

Excess profit tax

EPT is calculated annually. The taxable object is the portion of net income (if any) that exceeds 25% of "deductions". The net income is calculated as aggregate annual income (with some adjustments) less deductions less CIT and branch profits tax, if any. For EPT purposes, "deductions" is the expenditure deductible for CIT purposes (with some adjustments). The tax is calculated by applying the following rates to the tranches of excess income, each tranche being allocated the marginal net income determined as a percentage of deductions until the limit of net income is reached.

Net income allocation schedule for EPT, % of deductions	% for calculating marginal net income allocation for EPT	EPT rate (%)
Less than or equal to 25%	25%	Not set
From 25% to 30% inclusively	5%	10%
From 31% to 40% inclusively	10%	20%
From 41% to 50% inclusively	10%	30%
From 51% to 60% inclusively	10%	40%
From 61% to 70% inclusively	10%	50%
Over 70%	Any excess	60%

Special rules apply to determine the taxable object if the hydrocarbon production is processed prior to sale — for example, by refining crude oil into gasoline or diesel. In such cases, it is unlikely that an EPT liability would actually arise.

Payment for compensation of historical costs

The payment for compensation of historical costs is a fixed payment of the subsurface user to compensate the state for geological survey and development costs of the contract territory incurred before the subsurface use contract is concluded.

The obligation to compensate for historical costs arises from the date when the confidentiality agreement is concluded between the subsurface user and the authorized state body on subsurface study and usage.

Mineral extraction tax

Mineral extraction tax (MET) applies to crude oil, gas condensate and natural gas. The taxable object is the value of production. For export sales, the value is based on world prices without deductions. The "world price" of crude oil and gas condensate in this context is determined as the arithmetic mean of daily quotations for each of the Urals Mediterranean (Urals Med) or Dated Brent (Brent Dtd) brands in the tax period on the basis of information published either in the *Platts Crude Oil Marketwire* issued by The McGraw-Hill Companies or, if that source does not provide price information for those brands, in the Petroleum Argus source. The "world price" for natural gas is determined as the arithmetic mean of daily quotations in the tax period on the basis of information published either in the *Platts European Gas Daily* issued by The McGraw-Hill Companies or, if that source does not provide price information for natural gas, in the Argus European Natural Gas source.

The rates of tax are determined by the annual volume of production at the rates shown in the table below. Different rates apply to crude oil and gas condensate on the one hand and natural gas on the other, as noted below.

Volume of annual oil production, including gas condensate, for each calendar year (thousand tons)	MET 2018
Up to 250 inclusively	5%
From 251 to 500 inclusively	7%
From 501 to 1,000 inclusively	8%
From 1,001 to 2,000 inclusively	9%
From 2,001 to 3,000 inclusively	10%
From 3,001 to 4,000 inclusively	11%
From 4,001 to 5,000 inclusively	12%
From 5,001 to 7,000 inclusively	13%
From 7,001 to 10,000 inclusively	15%
Over 10,000	18%

These rates are reduced by 50% if the production is processed domestically in Kazakhstan either by the producer or by a purchaser. There are special rules for the calculation of tax bases in such cases.

In the case of natural gas that is exported, a flat rate of 10% applies. If the gas is sold to the domestic Kazakhstan market, rates are reduced to between 0.5% and 1.5%, depending on the level of annual production.

Bonuses

Subsurface users are expected to pay two types of bonuses:

- Signature bonus
- Commercial discovery bonus

Signature bonus

The signature bonus is a lump-sum amount paid by a subsurface user for the right to use the subsurface.

For oil exploration contracts, the bonus is a fixed amount of 2,800 MCI,[1] which is equivalent to KZT6,734,000. For oil production contracts where reserves have not been approved, the bonus is a fixed amount of 3,000 MCI, which is equivalent to KZT7,215,000. Where reserves have been approved, the bonus is calculated by a formula that applies a rate of 0.04% to the approved reserves and 0.01% to the provisionally approved reserves, but not less than 10,000 MCI. For production contracts, the signature bonus should not be less than the amount of the commercial discovery bonus.

Commercial discovery bonus

The commercial discovery bonus is a fixed payment paid by subsurface users when a commercial discovery is made on the contract territory.

The basis for calculation of the commercial discovery bonus is defined as the value of the extractable minerals duly approved by the competent state authorities. The value of the mineral resources is determined using the market price established at the International (London) Petroleum Exchange in Platts. The rate of the commercial discovery bonus is fixed at 0.1% of the value of proven extractable resources. The commercial discovery bonus will be abolished in 2019.

Corporate income tax

CIT is calculated annually at the rate of 20% of taxable income. Taxable income is calculated as the difference between aggregate annual income (after certain adjustments) and statutory deductions.

Deductions

All expenses incurred by a taxpayer in carrying out activities that are directed at the receipt of income are deductible for the purpose of determining taxable income. Examples of expenses that are allowed for deduction can be found below (but this list is not exhaustive):

- Interest expense (within limits)
- Contributions to the decommissioning fund; the procedure for making such contributions and the amount to be established in the subsurface use contract
- Expenditure on geological studies and exploration and preparatory operations for the extraction of mineral resources
- Expenditure on R&D and scientific and technological works

Geological studies and exploration, and preparatory operations for production of useful minerals, include the following: appraisal, preparatory work, general and administrative expenses, and costs associated with the payment of the bonuses. These costs, together with expenditure on the purchase of fixed assets and intangible assets (expenditure incurred by a taxpayer while

1 *The monthly calculation index (MCI) is KZT2,405 as of 1 January 2018.*

acquiring the right to geological exploration, development or extraction of mineral resources), form a depreciation group that is separate from fixed assets for tax purposes.

The costs may be deducted by declining-balance depreciation at a rate not exceeding 25%. Similar expenses incurred after the separate depreciation group has been formed (such as expenses incurred after depreciation starts) are included into the group to increase its balance value if, under International Financial Reporting Standards (IFRS), such expenses are capitalized into the value of assets already included in the group.

Depreciation of the pool of such expenses begins when production commences after commercial discovery. In the case of a farm-in, the subsurface user is allowed to capitalize the cost of acquiring a subsurface use right. Upon farmout, the subsurface user is liable for tax on capital gains.

The following are examples of other deductible expenses:

- Expenses incurred under a joint operating agreement based on information provided by the operator
- Business trip and representative expenses (per diems are deducted in full, based on the taxpayer's internal policy, whereas representative expenses are deductible in the amount up to 1% of payroll)
- Net foreign-exchange loss when a foreign-exchange loss exceeds a foreign-exchange gain
- Expenses on social payments to employees
- Insurance premiums, except for insurance premiums paid according to accumulative insurance contracts
- Amounts paid as redemption of doubtful payables previously written off as income
- Doubtful receivables not redeemed within three years
- Taxes paid (except for the taxes already excluded prior to determining aggregate annual income, income tax paid in Kazakhstan and in any other states, EPT and alternative subsurface use tax
- Fines and penalties, except for those payable to the State budget
- Maintenance or current repair expenses
- Capital repair (within the statutory limits)
- Expenditure actually incurred by a subsurface user with respect to training Kazakhstan personnel and the development of the social sphere of rural areas, within amounts stipulated in subsurface use contracts

The Tax Code also provides for certain expenses to be deducted directly from taxable income up to 4% of the taxable income, such as sponsorship aid and charitable contributions (subject to certain conditions).

The depreciation regime for fixed assets is discussed in Section C.

Dividends

Dividends distributed domestically (i.e., by a local subsidiary to a local parent company) are tax-exempt. Dividends paid abroad by subsurface users are subject to withholding tax (WHT) as discussed in Section E. Branches are subject to an equivalent branch profit tax at the same rates but applied to net profit after deduction of CIT.

Rent tax on export

The rent tax on export is paid by legal entities and individuals that export crude oil and crude oil products, including gas condensate. The tax base is calculated as the volume of the exported crude oil multiplied by the world price of crude oil and crude oil products, including gas condensate. The world price is determined as the arithmetic mean of daily quotations for each of the Urals Med or Brent Dtd brands in the tax period on the basis of information published either in *Platts Crude Oil Marketwire* issued by The McGraw-Hill Companies or, if that source does not provide price information for those brands, in the Petroleum Argus source. The tax rates applied to exported crude oil and crude oil products, including gas condensate vary, as shown in the next table.

Market price (US$/bbl)	Rate (%)
US$20/bbl inclusively	0%
US$30/bbl inclusively	0%
US$40/bbl inclusively	0%
US$50/bbl inclusively	7%
US$60/bbl inclusively	11%
US$70/bbl inclusively	14%
US$80/bbl inclusively	16%
US$90/bbl inclusively	17%
US$100/bbl inclusively	19%
US$110/bbl inclusively	21%
US$120/bbl inclusively	22%
US$130/bbl inclusively	23%
US$140/bbl inclusively	25%
US$150/bbl inclusively	26%
US$160/bbl inclusively	27%
US$170/bbl inclusively	29%
US$180/bbl inclusively	30%
US$190/bbl inclusively	32%
US$200/bbl inclusively	32%

The tax period for rent tax on export is a calendar quarter.

Alternative subsurface use tax

Alternative subsurface use tax (ASUT) may be applied by oil producers as a substitute to MET, EPT and payment for compensation of historical costs. ASUT may be applied only by oil producers carrying out oil production on continental shelf or certain deep oilfield deposits. ASUT applies at the discretion of the oil producer and upon the filing of an application for use of ASUT. ASUT is calculated annually. The taxable base is calculated as the difference between aggregate annual income determined for CIT purposes (after certain adjustments) and deductions determined for CIT purposes (after certain adjustments). The tax rates applied to the taxable base are shown in the next table.

Oil world price (US$/bbl)	Rate (%)
US$50/bbl inclusively	0%
US$60/bbl inclusively	6%
US$70/bbl inclusively	12%
US$80/bbl inclusively	18%
US$90/bbl inclusively	24%
From US$90/bbl and above	30%

Oil world price is determined in the same way as for MET (please see above).

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

For tax depreciation purposes, fixed assets are split into four groups. Assets are depreciated at the maximum depreciation rates set out in the table below.

Group number	Type of fixed assets	Maximum depreciation rate (%)
I	Buildings, structures (except for oil and gas wells and transmission devices)	10%
II	Machinery and equipment, except for machinery and equipment of oil and gas production	25%
III	Office machinery and computers	40%
IV	Fixed assets not included in other groups, including oil and gas wells, transmission devices, machinery and equipment for oil and gas production	15%

Fixed assets, among other things, include:

- Fixed assets, investments in real estate, intangible assets and biological assets recorded in accordance with IFRS and Kazakhstan accounting standards
- Assets with a useful life exceeding one year, manufactured and/or acquired by concessionaires under concession agreements
- Assets with a useful life exceeding one year that are objects of social infrastructure projects
- Assets with a useful life exceeding one year that are intended for use in activities directed at the receipt of income and received by a fiduciary for fiduciary management under a fiduciary management agreement, or on the basis of another document, which is a basis on which fiduciary management arises

The following items, among other things, are not considered as fixed assets:

- Intangible assets with an indefinite useful life
- Assets commissioned under investment contracts concluded before 1 January 2009

Subsurface users have the right to use double depreciation rates in the year of commissioning "newly created" fixed assets, provided they will be used in their contract activities for three years.

Expenses actually incurred in the use, repair, maintenance and liquidation of fixed assets are defined as "subsequent costs" and are deductible in the tax period when they are actually incurred.

D. Investment incentives

Losses

Losses pertaining to subsurface use contracts may be carried forward for up to 10 years. Tax losses may not be carried back.

Tax holidays

Kazakhstan does not have a tax holiday regime for subsurface users.

E. Withholding taxes

In the absence of a permanent establishment in Kazakhstan of a nonresident company, Kazakhstan WHT applies to a nonresident's income derived from Kazakhstan sources. The general WHT rate is 20%, except for dividends, capital gains and interest income (15%), income from international transportation services and insurance premiums payable in accordance with reinsurance risk agreements (5%), and insurance premiums (10%).

Further, double tax treaties provide either an exemption from Kazakhstan WHT or application of reduced WHT rates. Generally, interest and royalty rates in treaties are 10% and dividends are 5%, provided certain conditions are met.

Any type of income payable to a nonresident registered in a country with a preferential tax regime is subject to WHT at a rate of 20%. The list of such countries is approved by Governmental decree.

F. Financing considerations

A 4:1 debt-to-equity ratio limit applies on both Kazakhstan and non-Kazakhstan sourced financing obtained from, or guaranteed by, a related party or obtained from an entity registered in a tax haven. Interest on debt-to-finance construction should be capitalized.

G. Transactions

Any capital gains derived from a sale of an equity interest in a subsurface use contract or in a Kazakhstan resident company or a nonresident company, may give rise to Kazakhstan-sourced income.

The gains realized by nonresidents and not associated with a permanent establishment in Kazakhstan are subject to WHT in Kazakhstan at 15%, unless specifically exempt from tax according to Kazakhstan domestic tax law or by virtue of an applicable double taxation treaty.

The capital gain from the sale of shares or participating interests in a resident or nonresident legal entity or consortium may be exempt from Kazakhstan taxation provided that the following conditions are simultaneously met:

- The shares or participating interests have been owned by the taxpayer for more than three years.
- The legal entity (consortium) in which the shares or participating interests are being sold is not a subsurface user.
- No more than 50% of the asset value of the legal entity (or consortium) in which the shares or participating interests are being sold consists of the property of an entity that is a subsurface user.

The above exemption is inapplicable if the capital gain is made by a nonresident registered in a country with a preferential tax regime and without a registered presence in Kazakhstan. Such capital gains are subject to WHT at a rate of 20%, unless the applicable double tax treaty provides for an exemption.

In the case of a farm-in, the subsurface user may capitalize the cost of acquiring a subsurface use right. Upon farmout, the subsurface user is liable for tax on capital gains.

H. Indirect taxes

Import duties

Certain old subsoil use contracts and production sharing agreements benefit from grandfathered customs exemptions; however, new contracts do not. Moreover, imports from the Eurasian Economic Union countries (Russia, Belarus, Armenia and Kyrgyzstan) are exempt from import customs duties, and imports are not subject to customs clearance.

The customs legislation provides for a temporary import regime for goods that will be re-exported. It either exempts goods and equipment from customs duties and import VAT or it allows for partial payment, provided the goods and equipment are re-exported.

VAT

A European Union-style VAT applies in Kazakhstan. The VAT rate has been reduced from 20% in the late 1990s to 12% currently.

Crude oil, natural gas and gas condensate sold in the territory of Kazakhstan are subject to 12% VAT. Export sales of crude oil, natural gas and gas condensate are subject to zero-rated VAT.

Under the Tax Code, international transportation services (including the transportation of oil and gas via trunk pipelines) are subject to zero-rated VAT.

Imports of goods and equipment from the Eurasian Economic Union countries and other countries are subject to 12% import VAT. Special tax administration rules apply to import VAT.

Electronic VAT invoicing

The following groups of taxpayers are required to issue electronic VAT invoices:

- Taxpayers who are authorized economic operators, customs brokers, customs carriers, owners of temporary storage warehouses, owners of customs warehouses as per the Kazakhstan customs law
- Taxpayers, if required by international treaties ratified by Kazakhstan and covered by Kazakhstan legislation
- Large taxpayers subject to state monitoring

All other VAT payers, starting from 1 January 2019 will also be obliged to issue electronic VAT invoices.

Place of supply rule

The applicability of Kazakhstan VAT is determined based on the deemed place of supply of a given supply. It is important to note that, under the place of supply rules, a service may be physically performed outside Kazakhstan but deemed to be supplied inside Kazakhstan for VAT purposes. Examples of services taxed in this way include a supply of a service related to immovable property located in Kazakhstan, or a consulting service performed outside Kazakhstan for a customer inside Kazakhstan. If the place of supply is deemed to be outside Kazakhstan, the underlying supply is not subject to Kazakhstan VAT.

The rules determining the place of supply are generally as follows:

- For goods:
  - The place where transportation commences if goods are transported or mailed

  Or

  - The place where goods are transferred to the purchaser (but it is not clear whether this involves a physical transfer or a transfer of rights)
- For works and services:
  - The place where immovable property is located for works and services directly related to such property
  - The place where works and services are actually carried out for works and services related to movable property
  - The place of business or any other activity of the customer for the following works and services: transfer of rights to use intellectual property, consulting services, audit services, engineering services, design services, marketing services, legal services, accounting services, attorney's services, advertising services, data provision and processing services, rent of movable property (except for rent of motor vehicles), supply of personnel, communication services and others
  - Otherwise, the place of business or any other activity of the service provider

Sales of goods or services that are merely auxiliary to a principal sale are deemed to take place wherever the principal sale takes place — no definition of auxiliary sales is provided in the tax legislation.

Export duties

An export customs duty is applicable to export of crude oil. Starting from 1 March 2016, the export customs duty rate is calculated depending on the monthly average market price for crude oil for the prior period determined by the authorized state body.

Export customs duty rates are provided in the table below.

No.	Average market price for crude oil for previous period	Export customs duty, US$ per ton
1	Below US$25 per barrel	0
2	From US$25 to US$30 per barrel	10
3	From US$30 to US$35 per barrel	20
4	From US$35 to US$40 per barrel	35
5	From US$40 to US$45 per barrel	40
6	From US$45 to US$50 per barrel	45
7	From US$50 to US$55 per barrel	50
8	From US$55 to US$60 per barrel	55
9	From US$60 to US$65 per barrel	60
10	From US$65 to US$70 per barrel	65
11	From US$70 to US$75 per barrel	70
12	From US$75 to US$80 per barrel	75
13	From US$80 to US$85 per barrel	80
14	From US$85 to US$90 per barrel	85
15	From US$90 to US$95 per barrel	90
16	From US$95 to US$100 per barrel	95
17	From US$100 to US$105 per barrel	100
18	From US$105 to US$115 per barrel	115
19	From US$115 to US$125 per barrel	130
20	From US$125 to US$135 per barrel	145
21	From US$135 to US$145 per barrel	160
22	From US$145 to US$155 per barrel	176
23	From US$155 to US$165 per barrel	191
24	From US$165 to US$175 per barrel	206
25	From US$175 to US$185 per barrel	221
26	From US$185 per barrel and above	236

Stamp duties

No stamp duty applies in Kazakhstan.

Registration fees

Insignificant fixed fees apply.

I. Other

Payroll

Based on Kazakhstan legislation, any income paid for the work in Kazakhstan (regardless if it is paid from inside or outside of Kazakhstan) is deemed as Kazakhstan source income subject to statutory payroll taxation in Kazakhstan via payroll by tax agent, i.e., a Kazakhstan entity.

In order to be compliant with requirements of local legislation, host companies must run so-called "shadow" payroll to process income for work in Kazakhstan in the month income was actually paid, regardless of whether it is further recharged to the host entity. Foreign income is processed for tax purposes only, while net payment may be made by the home-country employer.

Personal income tax

Income of local and foreign employees and any payments made by the tax agent to or for nonemployees (except for individual entrepreneurs) is subject to personal income tax at the following rates:

1. Employment income (both tax residents and tax nonresidents) is -10%
2. Dividends received by residents — 5%
3. Other (nonemployment) income paid to nonresidents — 20%.

Social tax

Employers should pay a social tax on their employee's income at 9.5% (including social insurance contributions) of employment income.

Social insurance contributions

Employers pay 3.5% social insurance contributions from employment income of Kazakhstan citizens, foreigners and stateless persons holding a residence permit in Kazakhstan or citizens of the Eurasian Economic Union (i.e., Russia, Belarus Armenia, Kyrgyzstan) at a rate of 3.5%. Income in excess of 10 times minimum monthly salary (approximately USD$870) per month is not subject to social insurance contributions.

Obligatory social medical insurance

Employers also pay at their own expense contributions to the Social Medical Insurance Fund at a rate of 1.5% from income paid to employees who are citizens of Kazakhstan, foreigners and stateless persons holding a residence permit in Kazakhstan or citizens of the Eurasian Economic Union (i.e., Russia, Belarus Armenia, Kyrgyzstan). Income subject to social medical insurance contributions is capped by 15 times minimum monthly salary (approximately USD$1,300) per month.

Pension fund contributions

Ten percent of obligatory pension fund contributions are withheld from an employee's income. Income received in excess of 75 times minimum monthly salary (approximately USD$6,430 per month is not subject to obligatory pension fund contributions. These contributions apply only to citizens of Kazakhstan, foreigners and stateless persons holding a residence permit in Kazakhstan.

Obligatory professional pension contributions

For employees in certain professions (list is established by the local law) that are involved in hazardous working conditions (e.g., oil and gas) an employer must also at its own expense make 5% obligatory professional pension fund contributions (without a cap) of employment income.

Contract transfers

The Kazakhstan State has a priority right on transfers of subsurface use contracts and interest in subsurface users or entities that own them directly or indirectly, for oilfields of strategic importance.

Transfer pricing

In the legislation of Kazakhstan, transfer pricing control applies to transactions that directly or indirectly relate to international business. The tax authorities work actively to collect all the tax they believe could be due from transactions involving transfer pricing.

Kenya

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

- Corporate income tax (CIT) — standard rate 30%:
  - Other rates apply for nonresident companies, newly formed companies and companies operating under Special Economic Zones.
- Branch tax rate — 37.5%
- Tax loss carryback:
  - This applies only to a petroleum company that has ceased operations. If a contractor incurs a loss from a contract area where he or she has ceased operations, the loss can be carried back as a deduction against income to a maximum of three previous years of income from the year of income in which the loss arose and the operations ceased. However, the contractor will be required to apply to the Commissioner to treat the loss as such.
- Tax loss carryforward:
  - Losses incurred by a contractor in a contract area shall be carried forward and allowed as a deduction against income in the next following years until the loss is fully deducted or the operations in the contract area cease.

B. Fiscal regime

The fiscal regime that applies to the petroleum industry in Kenya is fairly similar to the regime that applies to other industries. It consists of CIT, value-added tax (VAT), import duty and royalties. It includes some tax exemptions on import duties and relief on VAT for exploration companies. Under CIT, however, a special regime applies for petroleum companies.

This is guided by the 9th Schedule to the Income Tax Act on "Taxation of Extractive Industries." The Schedule guides the taxation of both petroleum and mining operations in Kenya. It became effective from 1 January 2015.

The Schedule is applicable to the following persons:

- Licensee, a person who has been issued with, or granted, a mining right
- Contractor, a person with whom the Government has concluded a petroleum agreement, including any successor or assignee of the person

- Subcontractor, a person supplying services other than a person supplying services as an employee to:
  - A licensee in respect of mining operations undertaken by the licensee Or
  - A contractor in respect of petroleum operations undertaken by the contractor

The National Oil Corporation of Kenya (NOCK) is a limited liability company incorporated by the Government of Kenya for the development of the exploration, prospecting and production of oil and gas. The company acts on behalf of the Government in the coordination of exploration activities. It operates both upstream and downstream. The cabinet secretary in charge of Petroleum and Mining is mandated to sign production sharing contracts (PSCs) on behalf of the Government.

Corporate income tax

The taxable income of a petroleum company is the value of the production to which the company is entitled under a petroleum agreement in that year of income. A resident corporation is subject to CIT on its worldwide income at the rate of 30%. A nonresident corporation is taxed on income derived or accrued from Kenya at the rate of 37.5%. However, a new company is taxed at a reduced rate of 20% or 25% for a period of five years, or 27% for a period of three years, if at least 40%, 30% or 20% respectively of the issued share capital of the company is listed on the Nairobi Securities Exchange.

CIT is imposed on net taxable income. Taxable income is determined based on audited financial statements and is calculated as gross revenue less tax, less deductible expenses and other qualifying expenditures under the Income Tax Act Cap. 470. Allowable deductions include expenses incurred wholly and exclusively in the production of income, as well as those deductions under the special regime for the taxation of petroleum companies as provided under the 9th Schedule to the Income Tax Act.

Ring fencing

Ring-fencing rules apply. Expenditure incurred by a contractor in undertaking petroleum operations in a contract area during a year of income can be allowed only against income derived by the contractor from petroleum operations in the contract area during the year. Petroleum operations means authorized operations undertaken under a petroleum agreement.

Hedging transactions

Hedging transactions entered into by a contractor to manage commodity price risk are treated as specified sources of income unless the transaction entered has an annual turnover of less than 10 million shillings and is approved by the Commissioner.

Capital gains or losses

Capital gains on the disposal of depreciable assets are treated as business income for the corporate entity and are taxed at the normal corporate income tax rate of 30% for resident corporations and 37.5% for nonresident corporations.

Taxation of the consideration for disposal of petroleum interest/agreement or information

A consideration for the assignment of a right is treated as a receipt for a petroleum company and taxed accordingly. Only the net gain from a disposal in a petroleum interest is subject to tax. The net gain is computed as the consideration for the disposal reduced by the cost of the interest. If the interest transferred derives 20% or more of its value, directly or indirectly, from an interest in a petroleum agreement, the amount of net gain to be included in the income chargeable to tax is the amount computed using the formula: A*B/C, where:

- "A" is the net gain
- "B" is the value of interest derived directly or indirectly from an interest in petroleum agreement in Kenya
- "C" is the total value of the interest

Functional currency

Accounting income must be reported in the local currency, namely Kenyan shillings (KES).

Transfer pricing

There are transfer pricing rules and guidelines that should be adhered to by all companies that have nonresident related-party transactions.

Indirect transfers of interest

A contractor is required to notify the Commissioner immediately in case of change in the underlying ownership of a contractor of 10% or more. If the interest is disposed of by a nonresident, the contractor shall be liable, as the tax agent of the nonresident person, for tax payable as a result of the disposal.

Other petroleum taxes

The following taxes are payable under PSCs, with the applicable rates negotiated at the time of signing each PSC:

- Signature bonus
- Surface fees
- Training fee
- Windfall profits
- Profit oil — to be shared, taken and disposed of separately by the Government and contractor according to increments of profit oil

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

For a petroleum company, capital expenditures incurred with respect to each development area are tax-deductible. Other capital expenditures are pooled into classes and granted wear-and-tear allowances at the applicable rates.

Deductibility of exploration expenditure

A contractor is allowed a deduction for exploration expenditure in the year of income in which the contractor incurred the expenditure. The rate of depreciation for machinery first used to undertake exploration operations is 100%.

Deductibility of development expenditure

Development expenditure is deductible over a period of five years at the later of the dates when the expenditure was incurred or production commenced. The allowable deduction is apportioned accordingly in the year in which production commences.

D. Deductibility of interest (thin capitalization threshold)

Interest expense for petroleum companies is to be restricted if the debt-to-equity (D:E) ratio exceeds 2 to 1.

E. Incentives

Exploration

Expenditure of a capital nature on exploration qualifies for deduction in the year of income in which it is incurred.

Escrow account

The Income Tax Act allows establishment of an escrow account/rehabilitation fund for the purpose of decommissioning/rehabilitation of petroleum operations. Contributions to an escrow account/rehabilitation fund as well as expenditure incurred under an approved decommissioning/rehabilitation plan will be allowed as a deduction. Amount accumulated in or withdrawn from an escrow account/rehabilitation fund to meet expenditure incurred under an approved plan and interest income and investment income in respect of a rehabilitation fund is exempt from tax. However, any surplus amount upon completion of the decommissioning/rehabilitation plan or amount withdrawn and returned to the contractor is taxable as gains or profits from business in the year in which the amount was returned.

Social infrastructure

Social infrastructure expenditure (e.g., public schools, hospitals) will be tax-deductible subject to approval by the Cabinet Secretary for the National Treasury.

Tax holiday

Kenya does not have a tax holiday regime, other than for companies operating in export processing zones and the recently enacted special economic zones.

Tax losses

For petroleum companies, income tax losses can be carried forward indefinitely.

The amount of loss from petroleum operations can be carried backward as a deduction against income to a maximum of three previous years of income from the year of income in which the loss arose and the operations ceased. However, the contractor will be required to apply to the Commissioner to treat the loss as such.

F. Withholding taxes

Below are the withholding tax rates that are applicable to petroleum companies:

Description	Rate
Interest	15%
Dividends	10%
Royalties or natural resource	20%
Management, training or professional fees	12.5%

Withholding tax on "service fees"

The rate of withholding tax on service fees paid by a contractor and a licensee to a nonresident subcontractor will attract withholding tax at a rate of 5.625%.

Sale of property or shares

The amount or value of the consideration from the sale of property or shares in respect of oil companies, mining companies or mineral prospecting companies is not subject to withholding tax.

Branch remittance tax

Branch remittance tax and exchange control regulations do not apply. Repatriation of branch profits can be effected freely after payment of statutory taxes.

G. Transactions

Books, accounts and audits

A contractor must keep books and accounts in accordance with the accounting procedures and submit to the Cabinet Secretary for Petroleum and Mining a statement of those accounts not more than three months after the end of each calendar year.

At the request of the Cabinet Secretary, the contractor must appoint an independent auditor of international standing, approved by the Government, to audit the books and accounts of the contractor annually and report thereon, with the cost of such audit borne by the contractor.

The Government may audit the books and accounts within two calendar years of the period to which they relate and is required to complete that audit within one calendar year.

Farmout transactions

With effect from 1 January 2015, farmout transactions will be taxed on the gain if the net gain will form part of the taxable income of the transferor and will be taxed at the corporation tax rates.

If interest is transferred at the time of the agreement, the consideration shall not include value of any work undertaken by the transferee on behalf of the contractor. If the transfer of interest is deferred until some or all of the work undertaken by the transferee is completed, the amount payable to be included in the taxable income of the contractor as gains or profits from business excludes the value of the work undertaken by the transferee on behalf of the contractor.

Local content and preference for Kenyan goods and services

The petroleum sharing contracts signed between the Government and the contractors require them to employ Kenyans in the upstream petroleum operations. During the employment period, they are also required to conduct training courses and programs that will progressively increase employment of Kenyans. In addition, the contractors and subcontractors are obliged to give preference to Kenyan materials and supplies for use in the upstream petroleum operations.

Domestic supply obligations

In accordance with the provisions of the production sharing contracts, contractors are obliged to supply in priority crude oil and/or natural gas for domestic consumption in Kenya and to sell to the Government that portion of the contractor's share of production which is necessary to satisfy the domestic supply requirements.

H. Indirect taxes

VAT

Taxable supplies — excluding motor vehicles imported or purchased for direct and exclusive use by companies engaged in exploring and prospecting for oil and gas — are exempt from VAT.

Import duties

All goods imported into Kenya are subject to customs import taxes, unless specifically exempt. The general rate ranges from 0% to 25% of the customs value of the imported goods. However, special exemptions apply to companies engaged in the exploration and prospecting of oil and gas for machinery and other items necessary for the oil and gas business.

Excise duties

Excise duty is levied on some goods manufactured in Kenya, including petroleum products.

Stamp duty

Stamp duty applies to specified transactions. It is imposed under different heads of duty, the most significant being a conveyance duty on a transfer of property (e.g., land, buildings, certain rights, goodwill).

I. Other

Pay as you earn

Resident individuals, including expatriates, are taxed on their worldwide income based on the resident tax rates, while nonresidents pay taxed on Kenyan-sourced income only. The resident minimum tax rate is 10%, and the maximum rate is 30%. Employers have the responsibility to withhold and pay the tax due from employees' entire remuneration on a monthly basis. Employees are required to file annual tax returns.

National Social Security Fund (NSSF)

NSSF is a statutory contribution for both the employee (including expatriates) and the employer. Each contributes KES200 per month. However, the Government of Kenya enacted the NSSF Act No. 45 on 24 December 2013 to replace the NSSF Act (Cap. 258). The Act was to be effective 31 May 2014, but its implementation was halted by a court injunction. Upon implementation, contributions in the first year will range from KES360 to KES1,080 per month.

National Health Insurance Fund

This is a statutory health insurance to which employees are required to contribute. Depending on the salary scale, contributions range from KES150 to KES1,700 per month.

Double tax treaties

Kenya has double tax treaties with Canada, Denmark, France, Germany, India, Norway, Sweden, the UK, Zambia and South Africa.

Taxation of petroleum service subcontractors

A distinction is made between taxation of subcontractors with a permanent establishment (PE) in Kenya and those without a PE. Subcontractors without a PE are subject to withholding tax, while those with a PE in Kenya are taxed on business profits.

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

There are no separate tax laws or regulations in Kuwait governing the oil and gas sector. Foreign (i.e., non-Gulf Cooperation Council (GCC)) companies are therefore subject to the corporate income tax (CIT) law as amended by Law No. 2 of 2008 and Executive Bylaws (the Bylaws) thereto.

For fiscal periods commencing after 3 February 2008, the principal regime comprises the following:

- Royalties — 15%[1]
- Bonuses — none
- Production sharing contract — none
- Income tax rate — 15%
- Resource rent tax — none
- Investment incentives — a number of offered incentives

B. Fiscal regime

Corporate income tax

There are no separate tax laws or regulations in Kuwait governing the oil and gas sector.

Foreign "bodies corporate" are subject to tax in Kuwait if they carry on a trade or business in Kuwait, either directly or through an "agent" (see below), in the islands of Kubr, Qaru and Umm al Maradim, or in the offshore area of the partitioned neutral zone under the control and administration of Saudi Arabia.

Kuwaiti-registered companies wholly owned by Kuwaitis, as well as companies incorporated in GCC countries that are wholly owned by GCC citizens (GCC entities), are not presently subject to income tax. The members of the GCC are Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates.

1 *Royalties are considered in the same manner as normal business income and are subject to tax at 15%.*

However, the Kuwait Ministry of Finance (MOF) in consultation with the International Monetary Fund (IMF) has submitted a proposal to the Kuwait Parliament to introduce a business profit tax at 10%, which is currently under review.

The term "body corporate" refers to an association that is formed and registered under the laws of any country or state and is recognized as having a legal existence entirely separate from that of its individual members. Partnerships fall within this definition.

Law No. 2 of 2008 includes a definition of an agent. Under this definition, an agent is a person authorized by the principal to carry out business, trade or any activities stipulated in Article 1 of the law or to enter into binding agreements with third parties on behalf and for the account of the person's principal. A foreign principal conducting business in Kuwait through an agent (as defined in the preceding sentence) is subject to tax in Kuwait.

Foreign companies conducting a trade or business in Kuwait are subject to income tax under Amiri Decree No. 3 of 1955. Foreign companies conducting a trade or business in the islands of Kubr, Qaru and Umm al Maradim are subject to tax in Kuwait under Law No. 23 of 1961.

Foreign companies conducting a trade or business in the offshore area of the partitioned neutral zone under the control and administration of Saudi Arabia are subject to tax in Kuwait on 50% of the taxable profit under Law No. 23 of 1961. In practice, the tax department computes the tax on the total income of the taxpayer and expects that 50% of such tax should be settled in Kuwait. Many taxpayers are currently contesting this practice. In addition, certain recently awarded contracts for work in the offshore area of the partitioned neutral zone refer to taxation in Saudi Arabia only, giving rise to the impression that, from a Saudi Arabian perspective, the entire income from these contracts may be taxable in Saudi Arabia. The Kuwait Tax Authorities (KTAs), on the other hand, expect that 50% of the tax should be settled in Kuwait, as described above. This has given rise to a degree of ambiguity, and potential taxpayers are advised to consult with tax advisers in both Kuwait and Saudi Arabia on this matter.

Amiri Decree No. 3 of 1955 and Law No. 23 of 1961 differ primarily with respect to tax rates.

Foreign companies can operate in Kuwait either through an agent or as a minority shareholder in a locally registered company. In principle, the method of calculating tax is the same for companies operating through an agent and for minority shareholders. For minority shareholders, tax is levied on the foreign company's share of profits (whether or not distributed by the Kuwaiti company) plus any amounts receivable for interest, royalties, technical services and management fees.

Virtual permanent establishment

The KTAs have recently changed their approach to the interpretation of the permanent establishment (PE) concept with respect to services rendered by nonresidents in Kuwait. The KTAs have now introduced the concept of a "virtual service PE," which may result in the denial of income tax relief claimed by nonresidents under the applicable double tax treaties of Kuwait.

The KTAs approach does not consider the physical presence of employees or contractors of a nonresident service provider for establishing the nexus to the source country, although such a threshold condition is clearly provided by the conventions of both the Organisation for Economic Co-operation and Development (OECD) and the United Nations Model and applied in many countries.

Tax rates

Under Law No. 2 of 2008, the tax rate is set at a flat rate of 15%, effective for fiscal years beginning after 3 February 2008. For the fiscal years commencing prior to 3 February 2008, the tax rates shown in the table below were applicable under Amiri Decree No. 3 of 1955.

Taxable profits		
Exceeding (KWD)	Not exceeding (KWD)	Rate (%)
0	5,250	0%
5,250	18,750	5%
18,750	37,500	10%
37,500	56,250	15%
56,250	75,000	20%
75,000	112,500	25%
112,500	150,000	30%
150,000	225,000	35%
225,000	300,000	40%
300,000	375,000	45%
375,000	–	55%

The tax rates under Law No. 23 of 1961 are shown in the next table.

Taxable profits		
Exceeding (KWD)	Not exceeding (KWD)	Rate (%)
0	500,000	20%
500,000	–	57%

Capital gains

Capital gains on the sale of assets and shares by foreign shareholders are treated as normal business profits and are subject to tax at the rates stated above.

Article 1 of Law No. 2 and Article 8 of the Bylaws provide for a possible tax exemption for profits generated from dealing in securities on the Kuwait Stock Exchange (KSE), whether directly or through investment portfolios.

The Law No. 22 of 2015 amended certain articles of Law No. 7 of 2010 concerning the establishment of the Capital Market Authority and regulating securities activities (which is effective from 10 November 2015). Under Article No. 150 (duplicate) of the Law No. 22 of 2015, the returns from securities, bonds, Sukuk and other similar securities, regardless of whether the listed company is a Kuwaiti or non-Kuwaiti company, would be exempted from the tax. This exemption is provided in addition to the exemption from capital gains tax on disposal of Kuwaiti-listed securities.

These exemptions have also been confirmed by the Department of Inspections and Tax Claims (DIT) in the amendments to Executive Rule No. 16 as per the Administrative Resolution No. 2028 of 2015 amending certain executive regulations (ERs) relating to Law No. 2 of 2008 (Corporate Tax Law) and Law No. 46 of 2006 issued by the Kuwait MOF. These amendments are effective from the fiscal year ended on 31 December 2015.

Other significant taxes

The following are the other significant taxes.

Social security contributions are levied with respect to Kuwaiti employees and employees who are citizens of other GCC countries only; it is payable monthly by employers and employees. For Kuwaiti employees, social security is at the following rates:

Nature of tax	Rate (%)
Employer (payable on monthly salary up to KWD2,750)	11.5%
Employee (if monthly salary does not exceed KWD1,500)	10.5%
Employee (if monthly salary exceeds KWD1,500 but does not exceed KWD2,750)	2.5% of KWD1,500 + 8% of total salary
Employee (if monthly salary exceeds KWD2,750)	2.5% of KWD1,500 + 8% of KWD2,750
(Different monetary ceilings and percentages are prescribed for citizens of other GCC countries who are employed in Kuwait.)	
Contribution to the Kuwait Foundation for the Advancement of Sciences (KFAS); contribution payable by Kuwait shareholding companies; contribution levied on profits after transfer to the statutory reserve and offset by any loss carryforwards	1%
National Labor Support Tax, imposed annually on the profits derived from activities in Kuwait by a Kuwaiti company listed on the Kuwait Stock Exchange; Ministerial Resolution No. 24 of 2006 provides rules for the application of the tax.	2.5%
Zakat, imposed on annual net profits of public and closed Kuwaiti shareholding companies. Ministerial Order No. 58 of 2007 provides rules for the application of Zakat.	1%

Administration

The calendar year is generally used for Kuwaiti tax purposes, but a taxpayer may ask in writing for permission to prepare financial statements for a year ending on a date other than 31 December. For the first or last period of trading or conducting a business, a taxpayer may be allowed to file a tax declaration covering up to 18 months.

Accounting records should be kept in Kuwait, and it is normal practice for the KTAs to insist on inspecting the books of account (which may be in English) and supporting documentation before agreeing to the tax liability.

The KTAs also have issued notifications restating the requirement for taxpayers to abide by Article 13 and Article 15 of the Bylaws, which relate to the preparation of books and accounting records and the submission of information along with the tax declaration. Article 13 requires the taxpayer to enclose the prescribed documents — e.g., trial balance, list of subcontractors, list of fixed assets, inventory register — along with the tax declaration. Article 15 requires the preparation of prescribed books of accounts, including the general ledger and stock list.

The KTAs have issued executive rules for 2013 (which are effective for all fiscal years ending on or after 31 December 2013), which require analyses of contract revenues, tax retentions, expenses, depreciation rates and provisions to be included in the tax declaration. In addition, these executive rules require that these analyses and the financial statements should also contain comparative figures for the prior year.

In the case of noncompliance with the above regulations, the DIT may finalize an assessment on the basis deemed reasonable by the DIT.

The Bylaws provide that a taxpayer must register with the DIT within 30 days after signing its first contract in Kuwait. In addition, a taxpayer is required to inform the MOF of any changes that may affect its tax status within 30 days after the date of change. The taxpayer must also inform the MOF of the cessation of any activity within 30 days after the date of cessation.

Under the Bylaws, a new system of tax cards has been introduced. The information required to be included in the tax card application form is generally the information that is provided to the MOF at the time of registration.

The KTAs have recently issued a unique Tax Registration Number (TRN) and tax card to all taxpayers in Kuwait. The KTAs will be using this TRN in all matters relating to a taxpayer and in all correspondence relating to a taxpayer. Taxpayers are also required to use the TRN in all correspondence with the KTAs.

A tax declaration must be filed on or before the 15th day of the fourth month following the end of the tax period (for example, 15 April in the case of a 31 December year-end). Tax is payable in four equal installments on the 15th day of the fourth, sixth, ninth and 12th months following the end of the tax period, provided the tax declaration is submitted on or before the due date for filing. The Bylaws provide that a request for extension in time for filing the tax declaration must be submitted to the DIT by the 15th day of the second month (the third month under the prior law) after the fiscal year-end. The maximum extension of time that may be granted is 60 days (75 days under the prior law).

In the event of a failure to file a tax declaration by the due date, a penalty is imposed, equal to 1% of the tax for each 30 days or fraction thereof during which the failure continues. In addition, in the event of a failure to pay tax by the due date, a penalty is imposed, equal to 1% of the tax payment for each period of 30 days or fraction thereof from the due date to the date of the settlement of the tax due.

The KTAs have also issued Circular No. 1 of 2014. This circular applies to all taxpayers filing tax declarations after the issuance of the circular. If tax declarations are prepared on an actual accounts basis, the circular requires, among other things, that all tax declarations be prepared in accordance with the tax laws and the executive rules issued by the KTAs. For these types of declarations, the circular also requires the submission of a draft income and expense adjustment computed in accordance with the last assessment finalized by the KTAs within three months of the date of submission of the tax declaration.

If tax declarations are prepared on a deemed-profit basis, the circular requires, among other things, that tax declarations should be submitted on the same percentage that was applied in the last assessment. It also requires certain supporting documents to be provided together with the tax declaration, and also requires details of all subcontractors to be provided.

Articles 24 to 27 of the Bylaws provide for the filing of objections and appeals against tax assessments. As per Article 24, an objection may be filed against the assessment within 60 days from date of assessment. The tax department has to consider and issue a revised assessment within 90 days from the date of filing the objection. If the department fails to pass a revised assessment during this period, the objection is considered as rejected.

The Bylaws allow companies to submit a revised tax declaration if an assessment of tax has not yet been issued by the DIT.

If the DIT accepts the amended tax declaration, the date of filing of the revised tax declaration is considered for the purpose of imposing delay fines.

Law No. 2 of 2008 introduced into tax law a statute of limitations for a period of five years. This change is consistent with Article 441 of the Kuwait Civil Law, which states that any claims for taxes due to Kuwait or applications for tax refunds may not be made after the lapse of five years from the date on which the taxpayer is notified that tax or a refund is due.

Article 13 of the Bylaws provides that companies that may not be subject to tax based on the application of any tax laws, other statutes or double tax treaties, must submit tax declarations in Kuwait.

Determination of trading income

General

Tax liabilities are generally computed on the basis of profits disclosed in audited financial statements and adjusted for tax depreciation and any items disallowed by the tax inspector on review.

The tax declaration and supporting schedules and financial statements, all of which must be in Arabic, are to be certified by an accountant practicing in Kuwait that is registered with Kuwait's Ministry of Commerce and Industry.

Design expenses

Under Executive Rule No. 26 of 2013 (applicable for fiscal years ended on 31 December 2013 and thereafter), costs incurred for engineering and design services provided by third parties are restricted according to the following:

- If design work is carried out in the head office, 75% of the design revenue is allowed as costs (previously 75% to 80%).
- If design work is carried out by an associated company, 80% of the design revenue is allowed as costs (previously 80% to 85%).
- If design work is carried out by a third party, 85% of the design revenue is allowed as costs (previously 85% to 90%).
- If the design revenue is not specified in the contract but design work needs to be executed outside Kuwait, the following formula may be used by the tax authorities to determine the revenue:

$$\textbf{Design revenue for the year} = \frac{\textbf{Design costs for the year} \times \textbf{annual contract revenue}}{\textbf{Total direct costs for the year}}$$

Consultancy costs

Under Executive Rule No. 26 of 2013 (applicable for fiscal years ended on 31 December 2013 and thereafter), costs incurred for consultancy services provided by various parties are restricted in the following way:

- If consultancy work is carried out in the head office, 70% of the consultancy revenue is allowed as costs (previously 70% to 75%).
- If consultancy work is carried out by an associated company, 75% of the consultancy revenue is allowed as costs (previously 75% to 80%).
- If consultancy work is carried out by a third party, 80% of the consultancy revenue is allowed as costs (previously 80% to 85%).
- If the consultancy revenue is not specified in the contract, but design work needs to be executed outside Kuwait, the following formula may be used by the KTAs to determine the revenue:

$$\textbf{Consultancy revenue for the year} = \frac{\textbf{Consultancy costs for the year} \times \textbf{annual contract revenue}}{\textbf{Total direct costs for the year}}$$

Imported material costs

- Under Executive Rule No. 25 of 2013, the KTAs deem the following profit margins for imported materials and equipment:
  - Imports from head office: 15% of related revenue (previously 10% to 15%)
  - Imports from related parties: 10% of related revenue (previously 6.5% to 10%)
  - Imports from third parties: 5% of related revenue (previously 3.5% to 6.5%)

The imputed profit described above is normally subtracted from the cost of materials and equipment claimed in the tax declaration. If the revenue from the materials and equipment supplied is identifiable, the DIT normally reduces the cost of such items to show a profit on such materials and equipment in accordance with the percentages described above. If the related revenue from the materials and equipment supplied is not identifiable or not stated in the contract, the following formula may be applied to determine the related revenue:

$$\textbf{Material and equipment revenue for the year} = \frac{\textbf{Contract revenue for the year} \times \textbf{material and equipment costs for the year}}{\textbf{Total direct costs for the year}}$$

Interest paid to banks

Interest paid to local banks relating to amounts borrowed for operations (working capital) in Kuwait may normally be deducted. Interest paid to banks or financial institutions outside Kuwait is disallowed unless it is proven that the funds were specifically borrowed to finance the working capital needs of operations in Kuwait. In practice, it is difficult to claim deductions for interest expenses incurred outside Kuwait.

Interest paid to the head office or agent is disallowed. Interest that is directly attributable to the acquisition, construction or production of an asset is capitalized as part of the cost of the asset if it is paid to a local bank.

Leasing expenses

The KTAs may allow the deduction of rents paid under leases after inspection of the supporting documents. The deduction of rent for assets leased from related parties is restricted to the amount of depreciation charged on those assets, as specified in the Kuwait Income Tax Decree. The asset value for the purpose of determining depreciation is based upon the supplier's invoices and customs documents. If the asset value cannot be determined based on these items, the value is determined by reference to the amounts recorded in the books of the related party.

Agency commissions

The tax deduction for commissions paid to a local agent is limited to 2% of revenue, net of any subcontractor's costs, if paid to the agent and any reimbursement costs.

Head office overheads

Article 5 of the Bylaws provides that the following head office expenses are allowed as deductions:

- Companies operating through an agent: 1.5% (previously 3.5%) of the direct revenue
- Companies participating with Kuwaiti companies: 1% (previously 2%) of the foreign company's portion of the direct revenue generated from its participation in a Kuwaiti company
- Insurance companies: 1.5% (previously 2%) of the company's direct revenue
- Banks: 1.5% (previously 2%) of the foreign company's portion of the bank's direct revenue

Article 5 of the Bylaws also provides that, for the purpose of computation of head office overheads, direct revenue equals the following:

- For companies operating through an agent, companies participating with Kuwaiti companies, and banks: gross revenue less subcontract costs, reimbursed expenses and design costs (except for design costs incurred by the head office)
- For insurance companies: direct premium net of share of reinsurance premium plus insurance commission collected

Inventory

Inventory is normally valued at the lower of cost or net realizable value, on a first-in, first-out (FIFO) or average basis.

Provisions

Provisions, as opposed to accruals, are not accepted for tax purposes.

Tax depreciation

Tax depreciation is calculated using the straight-line method. The following are some of the permissible annual depreciation rates:

Asset	Rate (%)
Buildings	4%
Prefabricated buildings	15%
Furniture and office tools	15%
Drilling equipment	25%
Plant and equipment	20%
Computer and its accessories	33.3%
Cars and buses	20%
Trucks and trailers	15%
Software	25%
Electrical equipment and electronics	15%

Relief for losses

Article 7 of the Bylaws provides that approved losses may be carried forward for a maximum of three years if the entity has not ceased its operations in Kuwait. The prior tax law provided that losses could be carried forward and deducted from subsequent profits without limit if no cessation of activities occurred.

Aggregation of income

If a foreign company has more than one activity in Kuwait, one tax declaration aggregating the income from all activities is required.

Foreign currency exchange gains and losses

As per Executive Rule No. 37 of 2013, gains and losses on foreign currency conversion would be classified into realized gains or losses and unrealized gains or losses.

Realized gains and losses resulting from the fluctuation of exchange rates are allowed as a deduction (for losses) and taxable (for gains), provided the taxpayer is able to substantiate the basis of calculations and supplies documents in support of such transactions.

Unrealized losses are not allowed as deductible expenses, and unrealized gains are not considered as taxable income.

Reimbursed costs

Where deemed profit filings occur, reimbursed costs will be allowed as a deductible expense subject to the following:

- Such costs are necessary and explicitly mentioned in the contract
- Such costs do not exceed 30% of gross revenues
- Supporting documentation is available for such costs

Furthermore, in cases in which the reimbursable costs exceed 30%, the taxpayer is required to file its tax declaration on an accounts basis instead of a deemed-profits basis.

Miscellaneous matters

Foreign-exchange controls

No foreign-exchange restrictions exist in Kuwait. Equity capital, loan capital, interest, dividends, branch profits, royalties, management and technical service fees, and personal savings are freely remittable.

Supply and installation contracts

In supply and installation contracts, a taxpayer is required to account to the KTAs for the full amount received under the contract, including the offshore supply element, which is the part of the contract (cost, insurance and freight to the applicable port) pertaining to the supply of goods.

Contractors' revenue recognition

Tax is assessed on progress billings (excluding advances) for work performed during an accounting period, less the cost of work incurred. Although the KTAs generally did not previously accept the completed-contract or percentage-of-completion methods of accounting, the prohibition against the use of the percentage-of-completion method has now been removed via Executive Rule No. 27 of 2013 (effective for fiscal periods ended on 31 December 2013 and thereafter). It appears that the KTAs may accept the use of the percentage-of-completion method if it results in the proper matching of revenues and costs and the method applied is reasonable.

Subcontractors' costs

The KTAs are normally stringent in allowing subcontractors' costs, particularly subcontractors' costs incurred outside Kuwait. Subcontractors' costs are normally allowed if the taxpayer provides the supporting documentation (contract, invoices, settlement evidence and other documents), complies with Article 37 of the Bylaws and Executive Rule No. 6 of 2013 (see the subsection immediately below on tax retention), and fulfills certain other conditions. The KTAs have also taken the view that they would no longer accept any loss on work that is subcontracted to other entities.

Tax retention

Under Article 37 of the Bylaws and Executive Rule No. 6 of 2013, all business entities operating in Kuwait are required to withhold 5% from each payment due to contractors and subcontractors until they present a tax clearance certificate from the DIT.

In addition, local and foreign establishments, authorities and companies conducting a trade or business in Kuwait are required to give the director of income taxes details of the companies with which they are doing business as contractors, subcontractors or in any other form. Information to be provided should include the name and address of the company, together with a photocopy of the contract.

When inspecting the tax declaration filed with the DIT, the DIT will disallow all payments made to subcontractors if the rules described above are not followed.

Article 39 of the Bylaws of Law No. 2 of 2008 empowers the MOF to demand payment of the 5% retained amount withheld by entities if the relevant contractors or subcontractors fail to settle their taxes due in Kuwait. It also provides that where business entities have not retained the 5%, they are liable for the entire taxes and penalties due from the contractors and subcontractors.

Work in progress

Costs incurred but not billed by an entity at the end of the fiscal year may be carried forward to the subsequent year as work in progress if the revenue related to the costs incurred cannot be reliably measured. Alternatively, revenue relating to the costs incurred but not billed may be estimated on a reasonable basis and reported for tax purposes if the estimated revenue is not less than the cost incurred.

Taxpayers claiming treaty relief or exemption

Executive Rules No. 47 and 48 of 2013 (effective for fiscal periods ended on 31 December 2013 and thereafter) provide that if a taxpayer claims treaty relief or exemption of certain income, the tax authorities shall disallow 20% of indirect costs (previously 15% to 20%).

Salaries paid to expatriates

In a press release issued on 23 September 2003, the Ministry of Social Affairs and Labor announced that it would impose stiff penalties if companies failed to pay salaries to employees into their local bank accounts in Kuwait. These penalties apply from 1 October 2003. The press release also stated that the DIT may disallow payroll costs if employees do not receive their salaries in their bank accounts in Kuwait.

Offset program

The MOF issued Ministerial Order 13 of 2005 to reactivate the offset program. In 2006, the National Offset Company (NOC) was formed to manage and administer the implementation of the offset program on behalf of the Kuwaiti Government and the MOF. Per Decision No. 890 of the Council of Ministers, which was taken in their session No. 2014/2-30 on 7 July 2014, the offset program was officially suspended in Kuwait. The offset program has now been canceled with respect to all tenders floated after the decision of the Council of Ministers Number 890 on 7 July 2014 and all other tenders that were floated earlier but which have not closed as of the date of the decision.

Significant aspects of the earlier offset program were:

- All civil contracts with a value of KWD10 million or more and defense contracts with a value of KWD3 million or more attracted the offset obligations for contractors. The obligations became effective on the signing date of the contract.
- Contractors subject to the offset obligation were required to invest 35% of the value of the contract with Kuwaiti government bodies.
- Contractors subject to the offset obligation were allowed to take any of the following actions to fulfill their offset obligation:
  - Option 1: equity participation in an approved offset business venture (direct participation in a project company)
  - Option 2: contribution of cash and/or in-kind technical support
  - Option 3: participation in any of the offset funds managed by certain banks or investment companies in Kuwait
  - Option 4: purchase of commodities and services of Kuwaiti origin
- Contractors covered by the offset obligation were required to provide unconditional, irrevocable bank guarantees issued by Kuwaiti banks to the MOF equal to 6% of the contract price. The value of the bank guarantee was gradually reduced based on the actual execution by the foreign contractor or supplier of its work. The MOF could cash in the bank guarantee if the company subject to the offset obligation fails to fulfill such obligation.

The following were practical considerations:

- Option 3 above was not a viable option because the NOC has indicated that investment in funds is not considered for the completion of offset obligations.
- The NOC insisted that every offset venture have a local equity partner and had issued guidelines in this respect.
- A combination of Options 1, 2 and 4 was being used.

The offset program was implemented through the inclusion of clauses in supply contracts that referred to an offset obligation of the foreign contractor.

C. Tax treaty withholding tax rates

Kuwait has entered into tax treaties with a number of countries for the avoidance of double taxation. Treaties with several other countries are at various stages of negotiation or ratification.

Disputes between taxpayers and the DIT about the interpretation of various clauses of tax treaties are not uncommon. Disputes with the DIT regarding tax treaties normally arise with respect to the following issues:

- Existence of a PE
- Income attributable to a PE
- Tax deductibility of costs incurred outside Kuwait

Kuwait has also entered into treaties with several countries relating solely to international air or sea transport. Kuwait is also a signatory to the Arab Tax Treaty and the GCC Joint Agreement, both of which provide for the avoidance of double taxation in certain geographical areas. The other signatories to the Arab Tax Treaty are Egypt, Iraq, Jordan, Sudan, Syria and Yemen.

Domestic tax law in Kuwait does not provide for withholding taxes except for the distribution of dividends by companies listed on the Kuwait Stock Exchange (KSE). As a result, it is not yet known how the Kuwait Government will apply the withholding tax procedures included in the treaties. Please refer to the EY *Worldwide corporate tax guide* for the table of the withholding tax rates.

The new companies law

Kuwait has recently issued a new companies law (Law No. 1 of 2016).

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

D. Incentives

Kuwait offers a number of investment incentives, as described below.

Industry law

To encourage investments in local industrial undertakings, Industry Law No. 56 of 1996 offers:

- Reduced import duties on equipment and raw materials
- Protective tariffs against competing imported goods
- Low-interest loans from local banks
- Export assistance
- Preferential treatment on Government supply contracts

Promotion of direct investment in the state of Kuwait

The Law for the Promotion of Direct Investment in the State of Kuwait (PDISK; issued Law No. 116 of 2013) was published in the Kuwait *Official Gazette* on 16 June 2013 and became effective six months from the date of issue (i.e., in December 2013). PDISK replaces Law No. 8 of 2011 — the Direct Foreign Capital Investment Law (DFCIL). Under the new law, the Kuwait Direct Investment Promotion Authority (KDIPA) has been established, which took over from its predecessor (the Kuwait Foreign Investment Bureau (KFIB)).

On 14 December 2014, the KDIPA issued ERs to Law No. 116 of 2013 (the Law) for the promotion of foreign direct investment in Kuwait through Ministerial Decision No. 502 of 2014.

The ERs provide guidelines to simplify the process of obtaining a license for foreign direct investment and certain benefits as set out in the Law.

As of 1 January 2018, KDIPA has issued Decision No. 313 of 2016, laying down the scoring system to decide on an application as below:

- Total points are 59% or less: both the applications for the investment license and the granting of incentives are not accepted.
- Total points are 60% to 69%: only the application for the investment license is approved (without incentives).
- Total points are 70% to 79%: the investment license is granted with one selected incentive.
- Total points are 80% or higher: the investment license is granted with all the incentives stipulated in the law

Based on the total points gained in fulfillment of the criteria stipulated above, the decision may be taken. The tax incentives, if granted in the license by KDIPA, are not blanket incentives but are linked with actual performance of the investment entity. The performance is evaluated on an annual basis through a mechanism set out by the KDIPA. Ministerial Order No. 16 of 2016, amended through Resolution No. 76 of 2018 regarding the mechanism for granting a tax exemption, provides certain evaluation criteria as below:

Category SI, No. 1 relates to technology transfers. The measure is the cost of advanced equipment (over and above contractual obligations). The amount of the credit equals 20% of the value of the advanced equipment.

Category SI, No. 2 relates to the creation of jobs and training opportunities for Kuwaiti nationals. Nationals are defined as Kuwaiti employees in excess of the ratio prescribed in the Council of Ministers' Decision No. 1028 of 2014, regarding the determination of national labor. The following are the calculations for the credits in this category:

- 2.1: The measure is the total expenditure on salaries paid to Kuwaiti nationals. The credit equals five times the annual salaries paid to Kuwaiti national labor.
- 2.2: The measure is the total number of Kuwaiti national labor. The credit equals KWD36,000 (revised through the latest resolution) per Kuwaiti national labor.
- 2.3: The measure is the expenditure on the training of Kuwaiti national labor. The credit equals 10 times the annual expenditure on the training of Kuwaiti national labor.

Category SI, No. 3 relates to the expanding of local content. The local inputs are defined as the expenditure on locally manufactured products for the purposes of the licensed entity's operations, so that resultant added value from such inputs should not be less than 40% of the exit price upon completion. The following are calculations for the credits in this category:

- 3.1: The measure is the rental of the premises of the investment entity. The credit equals double the amount of the annual rental value.
- 3.2: The measure is dealings with local suppliers (especially small and medium-sized enterprises). The credit equals double the value of the annual contracts with local suppliers.
- 3.3: The measure is the use of inputs from local sources, such as raw materials. The credit equals double the annual value of inputs from local sources.

"One-stop shop"

KDIPA has reiterated its commitment to establish an administrative unit to act as a one-stop shop. The administrative unit, staffed by employees from various government authorities' units, will assist in the review of applications and approval of licenses, incentives and exemptions. Once the license is approved by KDIPA, the investor needs to establish a legal entity, legal branch or representative office (as requested in the application), that is done through the one-stop shop.

Investment entity

The ERs clarify that an entity seeking a license under the law may operate as a:

- Wholly foreign-owned limited liability company
- Branch of a foreign entity
  Or
- Representative office in Kuwait for the sole purpose of preparing market studies or studying production possibilities without engaging in any commercial activity

Incentives and exemptions

The law allows for the granting tax incentives to not exceed 10 years and an exemption from customs duty for a period of up to five years.

Non-qualifying activities

The PDISK adopts a negative-list approach to determine the applicability of the law. Under this approach, the PDISK provides a list of business activities and sectors that are not eligible for benefits under it. The negative list of business activities as provided by PDISK are as follows:

- Extraction of crude petroleum
- Extraction of natural gas
- Manufacture of coke oven products
- Manufacture of fertilizers and nitrogen compounds
- Manufacture of gas; distribution of gaseous fuels through mains
- Real estate (Level L), excluding privately operated building development projects
- Security and investigation activities
- Public administration and defense; compulsory social security
- Activities of membership organizations
- Activities of hiring labor, including domestic labor

Kuwait Free Trade Zone

To encourage exporting and re-exporting, the Kuwaiti Government has established a Kuwait Free Trade Zone (KFTZ) in the vicinity of the Shuwaikh Port. The KFTZ offers the following benefits:

- Up to 100% foreign ownership is allowed and encouraged.
- All corporate and personal income is exempt from tax.
- All imports into and exports from the KFTZ are exempt from tax.
- Capital and profits are freely transferable outside the KFTZ and are not subject to any foreign-exchange controls.

E. Withholding taxes

The domestic tax law in Kuwait does not provide for withholding taxes except in the case of dividend income received by the investors in companies listed on the KSE, as mentioned above.

However, the Capital Markets Authority (CMA) in Kuwait has issued Law No. 22 of 2015 (the Law) amending certain articles of Law No. 7 of 2010 concerning the establishment of the CMA and regulating securities activities (published in the *Official Gazette* on 10 May 2015 and effective from six months from the publishing date, i.e., effective from 10 November 2015) and as per the Law, 15% withholding tax on dividend is not required to be withheld on the dividend declared after 10 November 2015.

Please refer to Section B for comments on tax retention regulations.

F. Financing considerations

There are currently no thin capitalization rules imposed in Kuwait. However, please refer to Section B for comments on the deductibility of interest charges.

G. Indirect taxes

Import duties

The six member states of the GCC have entered into a GCC Customs Union, under the terms of which, member states have agreed to unify regional customs tariffs at 5% on all taxable foreign imports, down from individual country rates ranging from 4% to 15%, as of 1 January 2003.

In general, after landing in Kuwait, goods may be cleared through customs within two weeks if documentation is in order. Customs examination is rigorous for all imported goods, and Kuwait's department of standards and metrology has established a large number of minimum-quality standards, based on a combination of American, British, German and other national standards. Rigorous examination also applies to containerized cargoes arriving at the two main ports, Shuwaikh and Shuaiba. Lorries may be off-loaded on a random basis at a special inspection point in Kuwait City. Customs accepts no responsibility for damage, delays or losses.

Value-added tax (VAT)

The GCC countries have signed the VAT Framework Agreement, and each GCC country (including Kuwait) is currently working on VAT implementation initiatives with the aim of introducing VAT from 1 January 2019.

Export duties

Kuwait does not currently impose any export duties.

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Laos does not have laws and regulations to govern crude oil and gas extraction and production. Currently, the government of Laos applies a production sharing contract (PSC) model similar to other countries; however, conditions for each contract/agreement may be different based on a negotiation between the government and the contractor. From our observation of the agreements signed between the government and contractors, the following terms of payment may, in principle, be envisaged by the PSC:

- Rentals
- Production bonuses
- Royalties
- Lump-sum payments
- Training fees
- Environmental protection fund and other direct contributions
- Income tax — applied, but does not represent a cost to the contractor

Signature bonuses may not apply in Laos.

B. Fiscal regime

Cost recovery

There is currently no specific regulation on the cost recovery ceiling for both crude oil and gas; this will be subject to negotiation and agreement between the government and the contractor.

Profit production sharing

The production remaining after cost recovery is treated as "profit production" to be further split between the government and the contractor.

Profit production sharing for crude oil is based on a progressive sliding scale linked to daily production. The scale shall be subject to negotiation and agreement between the government and the contractor and in principle may be formatted as below:

Daily average production (barrels per calendar month)	Contractor's share of profit crude oil	Government's share of profit crude oil
Up to 25,000	35%	65%
25,001 to 50,000	32.5%	67.5%
50,001 to 75,000	30%	70%
75,001 to 100,000	27.5%	72.5%
100,001 to 125,000	25%	75%
125,001 to 150,000	22.5%	77.5%
150,001 to 175,000	20%	80%
175,001 to 200,000	17.5%	82.5%
More than 200,000	15%	85%

Similarly, production sharing for natural gas may be on a fixed basis, and the rate will be subject to negotiation between the government and the contractor.

Production bonuses

Below are examples of production bonuses, which will be subject to negotiation and agreement between the government and the contractor:

- US$1 million at 50,000 barrels
- US$2 million at 100,000 barrels
- US$3 million at 150,000 barrels
- US$4 million at 200,000 barrels

Production bonuses are not cost-recoverable.

Royalty[1]

These amounts shall be computed on the basis of sales and the royalty rate. However, there is currently no royalty rate for oil and gas, and this shall be subject to negotiation and agreement between the government and the contractor.

Lump-sum payments

These are viewed as compensation for the costs of government assistance to the contractor; however, specific amounts will be subject to negotiation and agreement between the government and the contactor.

Training fee and surface rental fee

Similar to lump-sum payments, training fees and surface rental fees will be subject to negotiation and agreement between the government and the contractor.

Environmental protection fund and other direct contributions[2]

Similar to lump-sum payments, environmental protection fund contributions will be subject to negotiation and agreement between the government and the contractor. In addition, the contractor may have to make commitments to directly contribute to community, human resources and sustainable development for the extraction area as agreed in the contract.

1 *Presidential Ordinance No. 001/OP dated 15 December 2015, Article 5 and Article 9.*

2 *Law on Minerals No. 02/NA dated 20 December 2011, Article 65.*

Income tax

The standard income tax rate in Laos is currently 24%. However, similar to the above, the income tax rate for PSC shall be subject to negotiation and agreement between the government and the contractor.

Ring fencing

Each PSC is ring-fenced. Profits from one PSC cannot be offset against losses from another PSC or other businesses, and vice versa.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Incentives

The contractor and its subcontractors may be permitted to import free of customs duties any machinery, installations, fuel, houses, transport facilities, equipment, vehicles, materials, supplies, consumable items and movable property necessary for conducting petroleum operations. This exemption may not apply for items that can be manufactured in Laos.

Exports of hydrocarbons are exempt from export duties and any other taxes.

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After discovery of hydrocarbon prospects, Lebanon has formulated its legislation related to hydrocarbon activities, including the Lebanese Petroleum Activities' Tax Law, which is different from the general tax regime. Readers should obtain updated information and seek professional advice before engaging in any transaction related to Lebanon's oil and gas deposits.

Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Lebanese oil and gas tax regime

On 24 August 2010, the Lebanese parliament approved the Offshore Petroleum Resources Law No. 132.

On 19 January 2017, the Lebanese parliament approved Decree No. 43 that includes the Tender Protocol related to the offshore licensing round, and the Exploration and Production Agreement (EPA).

On 5 October 2017, the Lebanese parliament approved the Lebanese Petroleum Activities' Tax Law — Law No. 57 (the Law) which entered into force on 12 October 2017 (date of publishing in the Official Gazette).

The Law is applicable on:

- Petroleum Right Holders Non-Operators (RhNO) and Petroleum Right Holders Operators (RhO) as defined in Law No. 132/2010 (Offshore Petroleum Resources Law)
- Contractors and Subcontractors as defined in this Law and as applicable
- Employees

The Law covers activities performed by the above mentioned taxpayers on Lebanese territories and maritime waters as defined in Law No. 132/2010.

The tax rates are summarized below:

Corporate income tax (CIT) rate	20%
Capital gains tax rate	20%
Standard movable capital tax rate	10%[1]
Value-added tax (VAT) rate	11%
Dividend tax rate	10%
Interest tax rate	10%[2]
Withholding tax rate on providing services	10%

Withholding tax rate on supply of goods	3%
Stamp duty rate[3]	0.4%
Built property tax rate on offshore oil and gas facilities	Exempt
Employees' income tax rate	From 2% to 20%
Royalties on crude oil	From 5% to 12% depending on production levels
Royalties on natural gas	4% of production

Note:

1. Movable Capital tax rate applicable to gain derived from direct or indirect transfer of shares in Rho and RhNO is 20% (Corporate Income Tax Rate).
2. It is to be noted that interest income from bank deposits are subject to a 7% tax.
3. The EPA are subject to Fixed Stamp Duty of LBP 5,000,000.

B. Fiscal regime

The fiscal regime applied to the oil and gas industry in Lebanon consists of a combination of corporate profit tax and royalties.

Petroleum companies are subject to Lebanese Petroleum Activities' Tax Law, which sets special accounting principles that a petroleum company should comply with while calculating its taxable result subject to 20% corporate income tax rate. In addition to CIT, royalties are imposed annually and can vary between 5% and 12% based on the production level per day for crude oil and 4% for natural gas.

RhO and RhNO must comply with the ring fencing, full-cost basis of accounting and accrual basis of accounting principles.

Corporate income tax

Taxable results

For the purposes of calculating the taxable income subject to CIT at 20%, crude oil and petroleum other than crude oil are valued in accordance with the valuation method determined in Law 132/2010 and its implementation provisions.

The taxable result of a defined financial year for Petroleum Right Holders and Petroleum Operators' Companies is the total revenues derived from petroleum activities covered by Law 132/2010 after deducting the allowable costs and expenses required in the performance of activities in that year provided that the allowable cost and expenses satisfy the following conditions:

Are necessary for the purpose of realizing the revenues	Are actual costs and supported by documentation	Do not increase the value of fixed assets used in the petroleum activities

The Law provides for specific revenues and expenses that should be included in the computation of taxable result.

The Law disallows the deduction of the following items:

- Capital interest
- Losses that affect the taxpayer due to the activities of institutions, branches, agencies, offices or others located outside of Lebanon
- Costs and expenses incurred abroad by the taxpayer on behalf of institutions, branches, agencies, offices or others

- Costs paid prior to signing the EPA
- Taxes stipulated in Sections 1 and 2 (income tax on petroleum activities and employees' income tax) of the second chapter of this Law and in the Legislative Decree No. 144 dated on 12 June 1959 and its amendments (Income Tax Law)
- Taxes and fees paid or due to a foreign country on income generated in Lebanon or for any other reason
- All types of fines

Capital allowance — depreciation

The Law allows the depreciation and amortization of tangible and intangible assets including capital expenditures, which include the exploration and development costs accounted for based on fixed rates of the asset's historical cost without adding the difference resulting from the revaluation operations. The principle of calculating depreciation and amortization shall be determined by a joint resolution issued by the Minister of Finance and Minister of Water and Energy.

Carryforward of taxable losses

RhO and RhNO can carry forward the deficit that occurred in a specific year to the subsequent years, provided that this deficit is recovered from the total realized profits in any of the subsequent years and the deficit or profit balance will remain subject to the legal provisions stipulated in this Law.

In case of a transfer of portion in the EPA, the new assigned taxpayer can benefit from part of the assignee's carryforward taxable losses proportionally to the portion transferred to the taxpayer, and the assignee shall no longer benefit from that part.

Movable capital tax

Gains resulting from the transfer of shares of RhO and RhNO are subject to movable capital tax at the rate of 20%, and the gains resulting from the transfer of shares of companies that own direct or indirect contributions in RhO and RhNO are subject to movable capital tax based on the share of investment in non-movable properties and petroleum rights in Lebanon from the total investment in the company whose shares are being transferred.

Investments in financial instruments are not in the scope of this Law, including hedging and derivatives, that are subject to the provisions of Legislative Decree No. 144 dated 12 June 1959 and its amendments (Income Tax Law).

Interests payments, even those related to the purchasing activity, are taxed at a rate of 10% under the provisions of title three of the Income Tax Law.

Capital gains tax

The gain resulting from the disposal of fixed tangible assets, intangible assets and financial assets shall be included in the taxable income subject to 20% CIT.

Withholding taxes

The following payments made to foreign persons not having permanent establishment in Lebanon are subject to withholding non-resident tax as follows:

- Payments for buying material that will be installed inside Lebanon, only the installation costs are taxed at 3% (based on 15% profit and 20% tax) in case separated. However, if the installation costs are not separable, the total purchase costs will be subject to tax at 3% (based on 15% profit and 20% tax).
- Payments for providing services performed inside or outside Lebanon are taxed at 10% (based on 50% profit and 20% tax).

RhO and RhNO have the withholding and reporting tax obligation of withholding tax unless the person is a registered permanent establishment or registered resident in Lebanon.

As for the person who is a resident in a country that has a double tax treaty with Lebanon, these taxpayers must withhold the mentioned tax on the amounts due to them, provided that the person requests the refund of the withheld tax based on a request submitted to the Tax Administration.

The details of application of this clause shall be determined through a decision issued by the Minister of Finance.

Employee's income tax

Foreign and local employees working in the petroleum industry or providing services and materials taking place on Lebanese territories and maritime waters are subject to employees' income tax rates, brackets and exemptions in accordance with the Income Tax Law. The income tax rates range between 2% and 20% depending on the income level.

The Law provides for the following:

- In case of a foreign nonresident employer, the liability to withhold the employee's income tax from the employee's benefits and remit it to the tax authorities on a quarterly basis is transferred to the employee residing in Lebanon.
- A resident employer who contracts a nonresident party to perform work or services in Lebanon executed by nonresident persons is responsible to withhold the employees' income tax from the nonresident persons' benefits and remit it to the tax authorities.

Social security

Employers and employees are subject to social security contributions as follows:

Each employer has to account for the following monthly contributions:

- 8.5% of the employee's total income toward the end-of-service indemnity
- 6% of the employee's total income (with an income ceiling of LBP1,500,000 (approximately US$1,000)) toward the family contributions
- 8% of the employee's total income (with an income ceiling of LBP2,500,000 (approximately US$1,670)) toward the sickness and maternity contributions

The employee has to contribute an additional 3% toward sickness and maternity.

The Law provides that employers have no social security contributions due on foreign employees who do not benefit from social security schemes

Value-added tax

Persons who practice petroleum activities or provide services and materials to these persons within Lebanese territories or maritime waters are subject to VAT at 11%.

Supply of oil and gas products outside Lebanese territories and maritime waters are considered as zero-rated (subject to VAT at zero rate with the right to deduct VAT).

The distribution of expenditures based on the EPA between RhO and RhNO is not subject to VAT. However, the exchange of services between RhO and RhNO is subject to VAT.

RhO and RhNO are considered the VAT representatives for nonresident persons with respect to common transactions that are carried out with them, including delivery of goods or services on Lebanese territories or maritime waters. RhO and RhNO must declare and settle the VAT payable on these services in accordance with applicable laws and regulations.

Stamp duty

The Exploration and Production Agreement is subject to fixed stamp duty of LBP5,000,000. However, contracts other than EPA are subject to fiscal stamps at the rate of 4 per thousand.

Customs duties

It is exempt from customs duties the equipment, machinery, tools, vehicles, spare parts and materials provided that goods do not have equivalence in the national production, are imported by RhO and RhNO or their agent to be used in the petroleum activities; and are imported to be re-exported.

It is exempted in accordance with the Customs Law particularly Article 316, the operations of importing household appliances, clothing, personal effects held for personal use by the foreign employees working for the RhO and RhNO in Lebanon, or by their families.

Goods that were exempted upon import shall not be sold, assigned, transferred, leased or have their objective of use changed in Lebanon, only after acknowledging the Customs Administration; and after payment of customs duties in accordance to the goods' condition and their value on the date of transfer.

Built property tax

Constructions, installations and fixations used to carry out petroleum activities in the maritime waters, in accordance with the definition of these waters in Law No. 132 dated 24 August 2010 (Offshore Petroleum Resources Law), are exempt from the built property tax.

C. Financing considerations

Thin capitalization

The Law sets the following rules for RhO and RhNO deductibility of interest on debt and loans:

- Interest on the portion of loans and debt that exceeds 150% of the related equity in the case of thin capitalization
- Interests on the portion of loans and debt that exceeds 60% of the recoverable costs balance approved by the Petroleum Administration

The calculation of the non-deductible interest on loans should be made as per the above two treatments, and the greater amount will be added back to the taxable result.

D. Transfer pricing requirements

The Lebanese tax authorities have the right to ignore any transaction where the main purpose (or one of the main purposes) was the avoidance of tax and to calculate taxable profits as if the transaction had not occurred. In addition, where intercompany transactions (particularly those with overseas affiliations) are undertaken at a position deemed not to be at arm's length, transfer pricing adjustments can be imposed to restate these transactions as at an arm's-length position.

Services provided between companies holding mutual license interests can also be subject to transfer pricing restrictions in Lebanon.

E. Other aspects

Double tax agreements

Lebanon has an extensive network of 32 double tax treaties in force.

Restrictions on transfer of money

There are no restrictions on the bank transfer of cash outside Lebanon.

Libya

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

In Libya, the fiscal regime that applies to the petroleum industry consists of a combination of corporate income tax (CIT) and other taxes. Production sharing contracts (PSCs) between the government and contractors are the general means of regulating the activities of the industry.

Under the PSC regime, taxes are deemed to be paid by the National Oil Corporation (NOC), and the tax computation is notional. The following apply:

- PSCs — Libya has a PSC regime and is presently contracting under the fourth generation of exploration and production sharing agreements (known as "EPSA IV"). There have, though, been no new agreements since 2007.
- Royalties — There is a notional royalty under the PSC regime of 16.67% of production.
- Bonuses — Signature bonuses are payable under a bid process. Subsequent bonuses are payable upon declaration of a commercial discovery, upon reaching a production level of 100 million barrels, and upon subsequent milestone production of each additional 30 million barrels, depending upon the specific agreement.
- CIT rate — 20% plus jihad tax of 4%. If these taxes, plus an adjustment for royalties, are less than 65% of profits, a surtax is payable so that tax, other deductions and a surtax combine to produce a composite 65% rate.
- Resource rent tax — Not applicable.
- Capital allowances — All capital expenditures are recoverable from cost oil through depreciation or amortization.
- Investment incentives — Not applicable to oil companies.

B. Fiscal regime

Corporate tax

Libyan private corporations are subject to income tax on their nonexempt worldwide income. Foreign corporations, registered as branches, including international oil companies (IOCs), are taxable on income arising in Libya.

Oil companies

Petroleum exploration and production in Libya is governed by Petroleum Law No. 25 of 1955, as amended (principally by Regulation No. 9 of 1973). Until the 1970s, oil licenses were granted via deeds of concession, and Libya received remuneration through royalties and taxes; the royalty was 16.67% of production. A combination of a royalty adjustment, rents, income taxes and a surtax created a deduction of 65% on profits. The amount paid by IOCs, therefore, was not a single petroleum tax but a payment composed of a variety of elements. With one exception, these concession agreements have been renegotiated into EPSA IV contracts.

In 1974, the first EPSA contract was introduced, and succeeding generations of EPSA contracts have introduced a variety of changes and refinements. IOCs and the NOC of Libya have shared profits in a variety of percentages and in accordance with a number of formulas.

Under the current EPSA IV, introduced in 1999 but amended a number of times since then, there is an open and transparent bid process for new acreage. A share of production is bid for and the lowest percentage bid wins the acreage. Percentage shares have been awarded for bids in the range of 7.5% to 25%. The agreement is usually for a period of 5 years, extendable by 25 years if oil is found in commercial quantities. The agreement contains a minimum exploration commitment, which may comprise, for example, the drilling of up to three wildcat wells and, for example, 3,000 kilometers of 2D seismic lines.

EPSA IV is a cost-recoverable agreement. If oil is discovered and produced, the NOC takes 100% less the share of the production bid by the IOC, until the IOC has recovered all exploration, appraisal, development and current annual production costs. Thereafter, any "excess petroleum" is allocated to the IOC based on the following formula:

Excess petroleum allocated to IOC = "A" factor × excess petroleum (barrels)

The A factor is related to the ratio of the cumulative value of production received by the IOC over the cumulative expenditure. The A factor is negotiable, but an example of a reasonable amount incurred is illustrated in the table below.

Ratio	A factor
Less than or equal to 1:5	0.90
More than 1:5 but less than or equal to 3:0	0.70
More than 3:0 but less than or equal to 4:0	0.50
More than 4:0	0.30

The crude oil value is used in determining the cumulative value of production received and is based on an average monthly international market price. The 2007 EPSA agreement values production at the monthly average price achieved by the NOC.

Calculation of corporate taxes for IOCs

Libyan private corporations are subject to CIT on their non-exempt worldwide income. Foreign corporations registered as branches, including IOCs, are taxed on income arising in Libya.

The terms of the current EPSA IV model contract state that the taxation terms of the Petroleum Law apply and that the IOC should submit royalty and tax returns despite the fact that taxes are notional. Estimated returns must be submitted, and taxes and royalties must be paid, quarterly. A final return (called a financial declaration) comprising actual production amounts for the calendar tax year must be submitted no later than 31 March of the following year.

The Petroleum Law identifies that the 65% of profits paid by an IOC under the terms of a concession deed comprises a number of elements. However, under EPSA IV, a tax computation is prepared using the 65% rate as if it were a single rate.

Taxes are deemed to have been paid on behalf of a foreign IOC by the NOC and are grossed up. The grossed-up amount is calculated thus:

$$\textbf{Grossed-up amount} = \frac{\textbf{Profit} \times \textbf{0.65}}{\textbf{(1 − 0.65)}} = \frac{\textbf{Profit} \times \textbf{0.65}}{\textbf{0.35}}$$

A tax receipt is issued for this amount.

The composite rate of 65% of profits payable by companies that are subject to the Petroleum Law comprises:

1. Income tax due under Income Tax Law No. 7 of 2010
2. Jihad tax due under Law No. 44 of 1970
3. Surface rents due under Article 14(1)(a) of the Petroleum Law
4. A surtax so that the total deductions are 65% of taxable income

To date, 65% of the profit defined under the Petroleum Law has always exceeded the amount due in items 1, 2 and 3 above, and so a surtax has always arisen.

CIT is computed in accordance with Libya's Income Tax Law (Law No. 7 of 2010) at the rate of 20% of profits. The jihad tax is payable by IOCs at the rate of 4% of corporate profits. It is charged at sliding scales on both salaries and profits. Although it is assessed under different legislation, it is therefore essentially another income tax.

The computation of revenue is generally defined in the applicable concession agreement or EPSA contract, and the EPSA tax computation is explained in Decision 394 of 2007 and Decision 96 of 2008.

Depreciation of tangible assets is allowed at 10% per year, and intangibles are amortized at 5% per year. Under Law No. 3 of 1983, the secretary of petroleum was given discretion to change these depreciation rates, and the rate applied under the terms of the old concession agreements is 33.33%.

Interest is not deductible in determining profits.

Taxpayers from some countries do not have any objection to paying one undifferentiated amount that is labeled the petroleum tax. By comparison, tax authorities of some home countries of foreign investors require them to prove the specific amounts paid for the income tax, jihad tax and petroleum surtax in order to calculate foreign tax credits or the amount that is eligible for a home-country exemption. For those taxpayers, it is important to calculate separately the various Libyan taxes arising.

Ring fencing

Historically, Libya applied the ring fence principle in determining a petroleum tax liability. Profits from one project could not be offset against the losses from another project held by the same tax entity. Similarly, a non-associated gas project had to be accounted for separately from a crude oil project. Under the current EPSA IV arrangement, ring fencing does not apply — revenue and costs may be pooled if the result is a commercially viable economic unit.

The Petroleum Law covers only upstream operations, although it includes rules relating to pipeline and terminal tariffs. Oil companies in Libya may acquire and build assets under their agreements, but, in practice, downstream activities are usually undertaken by separate entities called "oil service companies."

Royalty regime

Under the terms of the one remaining concession agreement, a royalty is payable monthly at the same time as taxes. The royalty is computed at the rate of 16.67% of production and valued at the "Libyan posted price" applicable to liftings in the month that the royalty is paid. The "Libyan posted price" is an anachronism: it is US$27.75 at 40 degrees API.

Oil service companies

An oil company may establish or have an interest in an oil service company, but such companies are subject to income tax law, not the Petroleum Law. Separate legal entities cannot form a tax consolidated group; therefore, oil companies and oil service companies are taxed individually.

Corporate tax for oil service companies is levied on taxable income. "Taxable income" is assessable income less any deductions. "Deductions" include expenses to the extent that they are incurred in producing assessable income or are necessary in carrying on a business for the purpose of producing assessable income. "Assessable income" generally comprises billings, capital gains and exchange rate gains.

Libyan tax law is straightforward, and the basis of determining taxable income, assessing and paying tax, and engaging in the appeal process, as established in the income tax law, resembles tax laws in many countries. However, practice can differ from theory.

Although corporate tax law is based on the usual "add-back" basis, whereby a disallowed expenditure is added back to declared net profits or losses, current practice is that the Libyan tax department usually raises assessments based on a percentage of turnover — a "deemed profit." Tax, therefore, is payable even when losses are declared. The 2010 tax law restates the requirement for taxation on the usual add-back basis, and the tax department confirmed that this is the basis on which taxes would be assessed in the future — the "deemed profit" basis would be the exception. However, this has not been implemented, and the deemed profit basis of assessment continues to be applied.

The level of deemed profit applied to turnover varies according to the type of business activity, but it is generally 15% to 20% for an oil service company.

Capital gains

No separate schedule exists in the tax law under which capital gains are taxed in Libya. Gains are taxed as trading income at the tax rates discussed above.

Functional currency

With the exception of oil companies, the general rule is that the functional currency is the Libyan dinar, a currency that floats against the special drawing rights (SDR).

However, for oil companies, an EPSA requires that records be maintained in both Libyan dinars and US dollars and, for cost recovery and tax purposes, that US dollar records be used. Oil company tax liabilities are determined in US dollars but paid in Libyan dinars.

Transfer pricing

Libya has no transfer pricing regulations. The Petroleum Law requires that charges from a parent company to its Libyan branch under the terms of a service agreement must be at cost.

There is no precedent, but transactions at arm's length, which include a profit to comply with regulations of the Organisation for Economic Co-operation and Development (OECD), should be identified and are subject to tax under the income tax law.

Dividends

Branches established in Libya by foreign oil companies do not declare and pay dividends.

Dividends declared and paid by an oil service company that has formed a Libyan joint stock company (JSC; the legal entity that a foreign company may establish) are taxable, but the rate to be applied has not yet been announced.

Interest and royalties more generally

Libyan tax law taxes income specifically and only under the following headings:

- Pure agricultural income
- Income arising from commercial, industrial and craft activities
- Income from the liberal professions
- Wages, salaries, etc.
- Income from bank deposits
- Tax on companies

Tax law does not, therefore, directly deal with matters such as interest, royalty payments (except royalties under the Petroleum Law, as described above), leasing and payments for intellectual property rights, and much depends upon precedent.

All contracts for services to be performed in Libya should be registered with the tax department, and stamp duty should be paid on these contracts. Thus, a foreign company registered in Libya that enters into an agreement with an overseas third party for the use of an asset or provision of a service in the Libyan jurisdiction that results in a payment should require that the contract be registered by the supplier. In these circumstances, tax is payable on the profit deemed to result from the payment, and is payable even if the company to which the payment was paid is not registered in Libya.

The same position applies to interest payable on a loan to a Libyan-registered entity.

Taxes and stamp duty must be paid in full, in advance, within 60 days of the effective date of the contract.

Branch remittance tax

Branch remittance tax is not applicable in Libya.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

There is no capital allowances regime in Libya. Statutory rates of depreciation are chargeable and deductible. Under the Petroleum Law, the rate may be determined by the NOC. Since 1983, it has been 33% for concession agreements; the rate for EPSAs is 10%.

D. Incentives

Investment Law

Investment Law No. 9 of 2010, together with the Implementing Regulations of 2010, offers:

- Exemption from company income tax on both retained and distributed profits for five years, with the possibility of an extension, and the carrying forward of losses in exemption years to subsequent years
- Exemption from customs duties for machinery, tools, equipment, spare parts and primary materials, although this is now superfluous because customs duties are at a 0% rate (with the exception of tobacco)
- Exemption from stamp duties

There is flexibility as to the corporate form. That is, an investor may establish any legal entity allowed under business law, such as a branch or company with a majority or minority shareholding.

The NOC is in the process of negotiating with a number of oil companies and international industrial companies to refurbish and extend refineries and other downstream facilities under the terms of the Investment Law. The template is for joint ventures to be established (in 50%/50% proportions), which will refurbish or build these facilities and subsequently operate them. Contracts are generally for 25 years, perhaps with an exclusive distribution agreement of 10 years.

After the expiration of the company income tax exemption period, these projects will be subject to tax under the income tax law.

Because the NOC is a shareholder or owner in such an agreement, and because revenue will be based on contracts with specific rates for throughput with defined costs, it is likely that any profit from these projects will subsequently be taxed on an add-back basis.

Exploration

As noted above, all capital expenditures and operating expenditures for exploration, appraisal, development and production are immediately cost-recoverable if a commercial discovery is declared.

Tax losses

Tax losses can be carried forward for 10 years for an oil company under the Petroleum Law and for 7 years for an oil service company under the income tax law.

Regional incentives

Regional incentives are not applicable in Libya.

Research and development

There are no incentives (or tax obligations) in relation to R&D in Libya.

E. Withholding taxes

There are no formal withholding taxes established in the law.

F. Financing considerations

Libya's tax system contains no significant rules regarding the classification of debt and equity instruments or the level of funding.

The Petroleum Law specifically prohibits interest paid to a parent to fund its Libyan operations, but agreements usually allow for the lesser of 2% or US$1 million of annual expenditures to be charged as the parent company's overhead (PCO).

Under the income tax law, PCO and interest and commissions are exclusively allowed, up to a maximum of 5% of administrative expenses included in the accounts.

There are no thin capitalization rules.

G. Transactions

Asset disposals

A profit resulting from the sale of a business, or from any of its tangible or intangible assets, is taxable income. The profit is the difference between the sale proceeds (or what is considered by the tax department to be the fair market value) and the cost or net book value.

Farm-in and farmout

It is not common in the Libyan oil and gas industry for entities to enter into farm-in arrangements.

Selling shares in a company

There is little precedent on this issue. However, a share disposal is subject to the income tax law, and any gain on disposal is subject to tax as if it were trading income, when a transaction of this nature is concluded within the Libyan jurisdiction.

H. Indirect taxes

Stamp duty

Stamp duty is chargeable according to Stamp Duty Law No. 12 of 2004, as amended by Stamp Duty Law No. 8 of 2010. Stamp duty is applied to numerous documents, both to "papers" and to "actions." There are 45 assessable schedules appended to the Law.

Stamp duty's most relevant impact on foreign companies arises from the requirement to register all contracts for work to be performed in Libya. Once a contract has been negotiated in Libya, if it is for anything other than a direct supply from abroad from an unregistered foreign company, it must be registered with the tax department within 60 days of the first date noted in the contract.

A 1% duty on the total contract value (plus 0.5% of the duty) is payable upon registration. Any invoice subsequently rendered against a registered contract must be taken to the tax department and stamped to confirm that the contract under which it is issued has been registered and the duty has been paid. Invoices should not be paid unless they are stamped as registered.

VAT and GST

There is no value-added tax (VAT) or goods and services tax (GST) in Libya.

Import duties

There are three rates of import duty, as follows:

- Base rate — 5%
- Rate on cars and vehicles — 10%
- Rate on luxury items — 15% (as set out in associated regulations)

Export duties

There are no export duties applied to goods exported from Libya.

Excise duties

There are no excise duties applied to goods exported from Libya.

I. Other

Importation

Equipment may be imported on either a permanent or temporary basis. Equipment imported on a permanent basis cannot be re-exported, whereas equipment imported on a temporary basis must be re-exported.

The conditions associated with temporary importation are strict. Equipment may be used only for the contract for which it was imported, and a deposit must be paid to the customs department.

Employment taxes

Other significant taxes include employer social security contributions of 11.25% of the gross salary, employee social security of 3.75% and taxes of 14% on all salary and benefits in kind paid to employees.

Foreign-exchange controls

The Libyan dinar is not a convertible currency, and contracts usually specify the proportion of the contract value that may be remitted abroad (the average is 80%). The balance of Libyan dinars is not transferable.

A foreign entity may hold only one Libyan dinar account at one bank. Different foreign currency accounts may be opened, but not multiple accounts in the same currency.

Branches of foreign companies may be paid directly offshore. JSCs may pay into foreign currency accounts held locally, and they may then remit the currency in accordance with the terms of their contracts, which should be deposited with the local bank.

Forms of business presence

A foreign oil company may establish a branch in Libya.

A foreign service company seeking to conduct a contract in the Libyan jurisdiction is required by law to establish either a branch (to undertake a "permitted activity" as listed by the authorities) or a Libyan JSC in which, from July 2012, the foreign company may hold a maximum of 49% of the share capital.

However, Decision 22/2013 stated that existing 65% foreign-owned Libyan JSCs could carry on working until the commercial law is reviewed. This will be undertaken at some point in the future, although a date has not yet been announced.

Permanent establishment

There is no definition of permanent establishment (PE) in Libyan Tax Law No. 7 of 2010, as amended, but Libya has signed a number of double tax agreements in which the concept of a PE is recognized under the general provisions of the model UN and OECD tax treaties. The establishment of PE status in Libya, therefore, ought to be clear and in accordance with definitions contained in the model tax treaties. However, in practice, it is a gray area.

Regardless of the definitions in the treaty, as a matter of practice on a day-to-day basis, the Libyan tax authorities work on the principle that taxable status is established if any work is undertaken or service performed in the Libyan jurisdiction. This is the case even if only a small proportion of a contract is undertaken in the Libyan jurisdiction (e.g., site visits) and regardless of the time spent in Libya.

Although it is a legal requirement for a foreign company to establish a corporate entity in Libya, in practice, it is possible to pay taxes and register contracts without registering in a situation where a particular expertise is required, usually for a single, short-term contract. In such a case, the associated contract must be registered with the tax authorities, and income taxes and stamp duties on the full contract value must be paid in full and in advance, as noted above.

Malaysia

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ■ **Service contract**

A. At a glance

Fiscal regime

The taxation of income from petroleum operations in Malaysia is governed by the Petroleum (Income Tax) Act 1967 (PITA) whereas income derived from non-petroleum operations is subject to tax under the Income Tax Act 1967.

- Royalties — 10% of gross production
- Bonus — a signature bonus may be payable to PETRONAS prior to the signing of a production sharing contract (PSC)

Production sharing contracts

Under the Petroleum Development Act 1974, PETRONAS, the national oil corporation of Malaysia, is vested with the exclusive rights of exploring and exploiting petroleum resources in Malaysia.

Oil and gas companies undertaking petroleum operations in Malaysia (other than areas within the Malaysia-Thailand Joint Development Area) will enter into a PSC with PETRONAS in which, generally, under each PSC, the contractor provides the financing and bears all the risks of exploration, development and production activities in exchange for a share of the total production.

Risk service contracts

For marginal fields, instead of entering into a PSC with oil and gas companies, PETRONAS may instead enter into a risk service contract (RSC). Under an RSC, the contractor earns a fee from PETRONAS, based on certain agreed parameters, as opposed to a share of production. From a tax perspective, a PSC would be treated differently from a RSC.

Tax rates

- Petroleum income tax:
  - Malaysia — 38% unless incentives are available
  - Joint Development Area (JDA):
    - First eight years of production: 0%
    - Next seven years of production: 10%
    - Subsequent years of production: 20%

- Income tax — 24%[1]
- Resource rent tax — none
- Real property gains tax — rates from 1 January 2014 are as follows (for disposals by companies):[2]
  - Disposal within three years from date of acquisition: 30% on chargeable gains
  - Disposal in the fourth year: 20%
  - Disposal in the fifth year: 15%
  - Disposal in the sixth and subsequent years: 5%.

B. Fiscal regime

Petroleum income tax is levied at the rate of 38% on the income of a chargeable person arising from petroleum operations (although reduced rates may apply for income from approved marginal fields — see below). The term "petroleum operations" refers to searching for and winning or obtaining petroleum in Malaysia and any sale or disposal of petroleum so won or obtained, and includes the transportation within Malaysia of the petroleum so won or obtained to any point of sale, delivery or export, but it does not include:

- Any transportation of petroleum outside Malaysia
- Any process of refining or liquefying petroleum
- Any dealings with products so refined or liquefied
- Services involving the supply and use of rigs, derricks, ocean tankers and barges

Please note that information on the fiscal regime in this section relates to petroleum upstream operations only. Downstream operations are subject to separate income tax legislation (the Income Tax Act 1967), and the tax treatment may differ from that provided under the PITA.

Chargeable person

Each PSC effectively creates a separate "chargeable person" for PITA purposes.

Generally, an operator for the PSC is appointed and is responsible for keeping the books of the PSC, as well as filing the petroleum income tax return on behalf of the PSC. The individual partners of the PSC are not required to file a separate petroleum income tax return in respect of their share of income from the PSC.

Multiple agreements and ring fencing

If a person conducts petroleum operations under more than one PSC, each PSC will be treated as a separate chargeable person. Effectively, expenses incurred in respect of a PSC can only be offset against income from petroleum operations under the same PSC.

Contiguous agreement areas

In contrast, if partners in a PSC carry on petroleum operations under two or more PSCs in contiguous areas, the petroleum operations in those areas are treated as being conducted under one PSC.

1 *The Protocol to the Malaysia-Thailand Double Taxation Agreement provides for the tax chargeable to be reduced by 50% in respect of business income or profits derived from the JDA, which are directly related to the exploration and exploitation of petroleum in the JDA and that are taxable in both countries.*

2 *Determining the date of "acquisition" and "disposal" for real property gains tax purposes can be a complex process.*

Succeeding partnerships

If, at any time during the period of the PSC, a partner in a PSC is succeeded by another, and at least one of the original parties to that PSC remains as a partner, both partnerships are treated as a succeeding PSC partnership.

Unabsorbed losses and capital allowances

Any unabsorbed losses and capital allowances can be carried forward indefinitely to offset future business income, as long as there is a succeeding partnership.

Recovery of cost oil and profit oil

Generally, the gross production of crude oil in each quarter is divided as follows:

- A maximum of 10% is first taken by PETRONAS as a royalty payment to the federal and state governments.
- Next, cost oil recovery by contractors is determined by the "revenue over cost" (R/C) ratio.
- The remaining portion, which is the profit oil, is split between PETRONAS and the contractors; the profit oil attributable to the contractors is shared, based on each party's participating interest.

Cost oil recovery excludes non-recoverable expenses such as:

- Costs incurred as a result of any proven negligent act or omission, or willful misconduct
- Replacement and/or repair costs in respect of assets or other property that is uninsured or underinsured
- Indemnity payments by contractors
- Expenses incurred in connection with the negotiation, signature or ratification of the PSC
- Expenses incurred in connection with raising money to finance petroleum operations, such as interest, bank charges and commissions
- Central administration and head office costs, and charges that are not substantiated or are excessive
- All taxes and export duties
- Costs and expenses associated with local offices and local administration, including staff benefits that are excessive

The list above is not exhaustive.

Functional currency

Upon obtaining approval from the Ministry of Finance, oil and gas operators may opt to submit their petroleum income tax returns and calculate their taxable income by reference to a functional currency (i.e., a particular foreign currency) if their accounts are solely or predominantly kept in that currency.

Transfer pricing

The Malaysia Inland Revenue Board (MIRB) has issued transfer pricing guidelines that apply to cross-border transactions and local transactions between associated enterprises. The guidelines are generally based on the arm's-length principle set forth in the transfer pricing guidelines of the Organisation for Economic Co-operation and Development (OECD) and provide several methods for determining an arm's-length price. The guidelines also provide a detailed list of information, documentation and records that need to be maintained with respect to related-party transactions.

The MIRB had historically used the anti-avoidance provision under PITA to disregard or vary any transaction that is not made on an arm's-length basis. Effective from January 2013, a specific transfer pricing and thin capitalization section has been inserted into the PITA. However, given that the thin capitalization section has been removed from the principal taxing legislation in Malaysia, the Income Tax Act 1967, it may be unlikely that rules will be introduced under the PITA to give effect to thin capitalization.

Capital allowances

Capital allowances are set out in the following table:

Qualifying plant expenditure		
	Initial allowance[(a)]	Annual allowance[(b)]
Plant		
Secondary recovery	40%	10%
Any other case	20%	8%
Fixed, offshore platform	0%	10%
Environmental protection equipment and facilities	40%	20%
Computer software and hardware	20%	40%
Buildings		
Secondary recovery	20%	3%
Any other case	10%	3%

Effective from the 2017 assessment year, the PITA defines the secondary recovery as "a project which has as its object the production of quantities of hydrocarbons by the application of external energy to the underground reservoir for the purpose of additional and accelerated recovery of those hydrocarbons which is carried out subsequent to the earlier recovery process."

(a) Initial allowance is claimable in the year the expenditure is incurred.

(b) Annual allowance is claimable in each year, commencing from the year the expenditure is incurred.

The qualifying plant expenditure incurred during the exploration and development period is accumulated and carried forward to the commercial production period, and deemed to be incurred in the year of the first sale of petroleum (i.e., when commercial production begins).

Qualifying exploration expenditure

Qualifying exploration expenditure (QEE) incurred during the exploration and development period is accumulated and carried forward until the first sale of petroleum (i.e., when commercial production begins). QEE is allowed as a graduated deduction in the form of the initial allowance and annual allowances against the gross income for each year of assessment:

- Initial allowance — 10%
- Annual allowance — the greater of:
  - 15% of residual expenditure

  Or

  - $$\frac{\textbf{(Output from petroleum operations for the basis period × residual expenditure)}}{\textbf{(Output from petroleum operations for the basis period + total potential future output of the petroleum operations)}}$$

Effective from 30 November 2010, the QEE of a chargeable person incurred prior to the first sales of petroleum may be deducted against the gross income of another chargeable person in another petroleum agreement, provided that the original parties to the petroleum agreements are the same. Other rules and conditions apply — for example, this order is not applicable to the JDA.

Disposal of assets used in petroleum operations

If an asset (for which capital allowances have been claimed) is sold, discarded or destroyed or ceases to be used by the contractor for purposes of petroleum operations, a balancing allowance or a balancing charge is computed. A balancing allowance arises when the residual expenditure of the asset exceeds the disposal value of the asset. A balancing charge arises when the disposal value of the asset exceeds the residual expenditure of the asset.

Financing considerations

Upon commencement of commercial production, interest expense on borrowings utilized in the production of gross income or laid out on assets used or held for the production of gross income is deductible. The amount of the deduction may not exceed the fair amount of interest in a similar transaction between independent parties dealing at arm's length. Once the thin capitalization rules highlighted above are in effect, the impact of these rules on the deductibility of interest expenses will also need to be considered.

Unconventional oil and gas

No special rules have been released in Malaysia with respect to unconventional oil or unconventional gas activities.

C. Incentives

The Malaysian Government had announced the following incentives to promote upstream development and boost the commercialization of hard-to-reach oil fields:

- Investment allowance (IA) for capital-intensive projects
- A reduced tax rate of 25% from 38% for marginal oil fields
- Accelerated capital allowances of up to five years
- QEE transfers between noncontiguous petroleum agreements
- A waiver from export duty on oil produced from marginal fields

Details on some of these incentives are set out below. Note that some of the incentives relating to a field or an area may be mutually exclusive.

Marginal fields

A "marginal field" is a field that is determined by the Minister of Finance and in a petroleum agreement area that has potential crude oil reserves not exceeding 30 million stock tank barrels or natural gas reserves not exceeding 500 billion standard cubic feet. A chargeable person's statutory income derived from petroleum operations in a marginal filed is effectively taxed at 25%.

Investment allowances

Investment allowances are available to a chargeable person who incurs qualifying capital expenditure for qualifying projects, as determined by the Minister of Finance, such as projects of enhanced oil recovery, high-carbon-dioxide gas, high-pressure, high-temperature, deep water or an infrastructure asset. The investment allowance rate is 60% on qualifying capital expenditure incurred within a period of 10 years. Investment allowances can be set off against 70% of the statutory income of the qualifying project. Any unutilized investment allowances can be carried forward for future utilization against income from the qualifying project. Investment allowances are given in addition to capital allowances.

Accelerated capital allowances

A chargeable person who incurs qualifying capital expenditure solely for the purpose of carrying out petroleum operations in a marginal field would qualify for accelerated capital allowances on such qualifying capital expenditure. This incentive provides an initial allowance of 25% and annual allowances of 15% (including in the year of acquisition) on qualifying plant expenditure incurred between the years of assessment 2010 to 2024.

Global Incentive for Trading program

In addition to the above upstream incentives, Malaysia has also introduced an incentive for commodity trading activities undertaken via a Labuan International Commodity Trading Company (LITC).

The Global Incentive for Trading (GIFT) program is available for a LITC. An LITC is a company that trades the physical and related derivative products of certain commodities with nonresidents in a currency other than the Malaysian ringgit. These commodities include petroleum and petroleum-related products, including liquefied natural gas (LNG). For petroleum and petroleum-related products, including LNG, the LITC is permitted to deal with Malaysian residents, though the trading must still be undertaken in a currency other than the Malaysian ringgit. The LITC must be incorporated under the Labuan Companies Act 1990 and must be licensed by the Labuan Financial Services Authority (LFSA). The following are some of the incentives that are provided to an LITC under the GIFT program:

- The corporate tax rate is 3% on chargeable profits.
- After the first five years of operations, an LITC failing to meet certain conditions would be subject to a general penalty. The conditions are as follows:
  - The LITC must have a minimum annual turnover of US$100 million.
  - The LITC must have a minimum annual business spending of MYR3 million (approximately US$770,000) payable to Malaysian residents.
  - The LITC needs to employ at least three professional traders. These traders must have a minimum salary of MYR15,000 (approximately US$3,900) per month and must be Malaysian tax residents.

D. Withholding taxes

Withholding taxes in Malaysia are currently as follows:

- Dividends – 0%
- Interest – 15%[3, 4]
- Royalties – 10%[5,6]
- Payments for specified services performed in Malaysia as well as for use of movable property – 10%[7, 8, 9]
- Payments to nonresident contractors – 13%[10, 11]
- Other gains or profits (nonbusiness) deemed to be derived from Malaysia (e.g., commissions, guarantee fees that are not business income of the nonresident) – 10%[12]

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3 *Bank interest paid to nonresidents without a place of business in Malaysia is exempt from tax.*

4 *This is a final tax applicable only to payments to a nonresident.*

5 *This is a final tax applicable only to payments to a nonresident.*

6 *The Protocol to the Malaysia-Thailand Double Taxation Agreement provides for the tax chargeable to be reduced by 50% for royalties, technical fees and contract payments in connection with income arising from activities that are directly related to the exploration and exploitation of petroleum in the JDA and that are taxable in both Malaysia and Thailand.*

7 *This is a final tax applicable only to payments to a nonresident.*

8 *The Protocol to the Malaysia-Thailand Double Taxation Agreement provides for the tax chargeable to be reduced by 50% for royalties, technical fees and contract payments in connection with income arising from activities that are directly related to the exploration and exploitation of petroleum in the JDA and that are taxable in both Malaysia and Thailand.*

9 *With respect to services provided by nonresidents during the period 17 January 2017 to 5 September 2017, generally Malaysian withholding tax would apply even if the services were performed outside of Malaysia. For services rendered prior to 17 January 2018 or after 5 September 2018, Malaysian withholding tax would apply to amounts paid or credited for services performed only in Malaysia. Certain tax treaties may provide relief.*

10 *The Protocol to the Malaysia-Thailand Double Taxation Agreement provides for the tax chargeable to be reduced by 50% for royalties, technical fees and contract payments in connection with income arising from activities that are directly related to the exploration and exploitation of petroleum in the JDA and that are taxable in both Malaysia and Thailand.*

11 *The withholding tax is treated as a prepayment of tax for the final tax liability of the nonresident.*

12 *This is a final tax applicable only to payments to a nonresident.*

E. Indirect taxes

VAT and GST

Goods and services tax (GST) has been implemented in Malaysia with effect from 1 April 2015 at a standard rate of 6% (replacing the sales tax and service tax systems). The Goods and Services Tax Act 2014 and Goods and Services Tax Regulations 2014 were published in 2014.

GST, which is similar in nature to VAT, is a multistage consumption tax applicable to every taxable supply of goods and services made in Malaysia, as well as to the importation of goods and services into Malaysia. The registration threshold for GST is MYR500,000 per annum. GST guidelines have been issued on various matters and in relation to various industries, including the petroleum upstream and downstream industries. Certain specific rules apply to the petroleum industry that are not applicable to other industries.

The Ministry of Finance has recently issued guidelines on the GST relief application for the importation of "big ticket items," which would include oil rigs for oil and gas industry. Applications for such GST relief should be submitted to the Ministry of Finance starting from 1 January 2018, and approvals will be subject to certain conditions.

Import duty

On 16 May 2018, the Royal Malaysian Customs Department issued GST (Rate of Tax) (Amendment) Order 2018, which amends the standard rate of GST from 6% to 0% on the supply of goods and services effective from 1 June 2018. The standard rate of 0% does not apply to the supply of goods and services listed under the Goods and Services Tax (Exempt Supply) Order 2014.

The following GST Orders are revoked with effect from 1 June 2018:

- Goods and Services Tax (Zero-rated Supply) Order 2014
- Goods and Services Tax (Relief) Order 2014
- Goods and Services Tax (Application to Government) Order 2014
- Goods and Services Tax (Imposition of Tax for Supplies in respect of Designated Areas) Order 2014
- Goods and Services Tax (Imposition of Tax for Supplies in respect of Free Zones) Order 2016

Notwithstanding the above, all GST registered persons are still required to adhere to the imposition of GST at the 0% standard rate and will remain subject to the current legislation and regulations, which include the issuance of tax invoices, submission of GST returns for the respective taxable periods and claiming of input tax credit. GST registered persons should also ensure that the pricing of goods and services is, at all times, in accordance with the Price Control and Anti-Profiteering Act 2011.

With the planned abolition of GST, it is proposed that the Sales and Services Tax (SST) will come into place. At this stage, very few details are available about the proposal, the transition process and the final framework any new tax will encompass.

All dutiable goods, equipment and materials that enter Malaysia from overseas are subject to customs import duty. The general rates of import duty applied to the customs value of imported goods are between 2% and 50%, depending on the types of goods imported. Goods under trade agreements are accorded the relevant preferential import duty rates. Certain classes of petroleum products under the HS code heading 27.10 are currently subject to import duty at rates ranging from 0% to 5% and may require an import license.

The petroleum upstream industry (approved companies under the relevant order involving the exploration, development and production of crude oil, including condensate and gas) currently benefits from import duty exemptions on all equipment and materials (listed in the master equipment list) used in such operations.

The petroleum downstream industry (involving the refining of crude oil into petroleum products, manufacturing of petrochemical products, gas processing and the distribution of processed gas) may apply for raw materials, components, packaging materials, machinery and equipment to be free of import duty if the goods are used in the manufacturing activity.

Export duty

Export duty at the rate of 10% applies to petroleum crude oil exported from Malaysia. Exportation of certain classes of petroleum products may require an export license.

Excise duty

Excise duty applies to a selected range of goods manufactured in Malaysia, as well as on selected goods imported into Malaysia.

Excise duty is not applicable on petroleum products.

Mauritania

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The Hydrocarbons Code (new code) was voted by the Mauritanian Parliament in 2010 and amended by the law n° 2011- 044. The code has not been issued in the *Official Gazette* and so the comments hereafter are based on the version passed by the Mauritanian Parliament.

The new code consolidates the pre-existing legal framework applicable to the oil industry, namely Ordinance No. 88.151 of 1988 (the 1988 Ordinance), which pertains to the legal and fiscal regime applicable to the exploration and exploitation of petroleum. The new code also includes the simplified tax regime (STR) introduced in 2004 by Law No. 2004–029.

Depending on the date on which the petroleum contract was signed, the Mauritanian fiscal regime applicable to the oil and gas upstream industry is governed either by the 1988 Ordinance or the new code, the production sharing contract (PSC) and the General Tax Code (GTC). Indeed, companies undertaking petroleum activities under a petroleum contract signed before 2010 remain subject to such contracts and to any non-contrary provisions of the new code.

A specific legal regime for downstream activities was introduced by Ordinance No. 2002-005 in 2002 and will not be presented here.

The main taxes applicable to the oil and gas upstream sector are the following:

- Under the 1988 Ordinance:
  - Corporate income tax (CIT)
  - Royalties
- Under the new code:
  - CIT
  - Value-added tax (VAT) at 0% rate for all transactions related to oil operations
  - Surface fee
  - Bonuses
  - Administrative Contribution

Legal regime

The 1988 Ordinance governs the legal regime applicable to the exploration and exploitation of petroleum — whether solid, liquid or gaseous — as well as the transportation, storage and marketing thereof.

The scope of the new code is broader than the 1988 Ordinance as it also provides the legal regime applicable to constructions and installations enabling the exploration and exploitation of petroleum (as well as the associated transportation and storage). However, the new code does not cover the legal regime for petroleum marketing activities or the conduct of petroleum activities by individuals.

Under the new code, the State may carry out any petroleum activities, either directly or through the national company. The State may also authorize one or more companies resident in Mauritania or with a branch there to carry out petroleum activities through:

- A reconnaissance authorization, which gives its holder the nonexclusive right, within a limited contractual perimeter, to conduct reconnaissance operations, such as geological methods.
- The initial duration of a reconnaissance authorization must not exceed 12 months and may be renewed once for the same duration.
- Exploration and production (E&P) activities into hydrocarbons, which are conducted on the basis of a PSC-style E&P contract between the contractor and the State.

A PSC provides for the sharing of oilfield production between the State and the contractor and must be approved by a State decree.

The PSC includes two phases:

- An initial research phase that cannot exceed 10 years and that should include three phases defined in the PSC
- An exploitation phase that cannot exceed 25 years if the exploitation concerns crude oil fields and 30 years for dry gas fields

Furthermore, the PSC should include a clause granting the State the option of participating in the rights and obligations of the contractor within the exploitation perimeter. This clause will state that the maximum percentage of the State's participation in the E&P activities is 10%.

Transportation of hydrocarbons

A right to transport hydrocarbons is granted to the PSC holder. The new code provides, in particular, that holders of different PSCs may form an association to build and operate transportation systems.

B. Fiscal regime

Contracts signed before the new code came into force remain governed by any of its non-contrary provisions. This analysis therefore covers the main taxes applicable in Mauritania under both regimes (the 1988 Ordinance and the new code).

Main taxes applicable under the 1988 Ordinance

Royalties

Contractors holding a so-called "B-type" exploitation permit are subject to a royalty on production, to be paid in cash or in-kind. The amount of this royalty is determined by the total quantity of hydrocarbons produced from the exploitation permit (and not used in petroleum operations, excluding storage and marketing). The royalty will be specified in the contract but should not be less than 10% of production. Royalties are deductible when determining taxable net profits.

The holder of an exclusive right of exploitation, excluding the holder of the B-type permit of exploitation, is not subject to royalties.

Corporate income tax

Companies conducting petroleum operations within the Mauritanian national territory are liable to CIT as provided for in the GTC. CIT is determined based on the net profit arising from such operations. The applicable rate will be specified in the contract; however, it must be at least equal to the common tax rate applicable at the time the contract was signed.

CIT is paid directly by the contractor. For CIT purposes, the contractor has to maintain separate accounts for its petroleum operations in each calendar year. These accounts must include a profit-and-loss statement and a balance sheet that will show the results of the petroleum operations and the assets and liabilities assigned or directly related to the petroleum operations.

For the purpose of CIT, the following expenses are deductible (provided that they have actually been recorded in the financial statements and the annual tax return of the current fiscal year that have been submitted to the tax administration):

- Petroleum costs, including costs of supplies, salaries and costs of services provided to the contractor in connection to the petroleum operations (the costs of supplies or services rendered by affiliated companies are deductible, provided that they do not exceed the arm's-length amount for identical or similar supplies of services)
- Depreciation of capital expenditure, in accordance with the rates applicable in the oil industry and covered by the contract
- Overhead related to petroleum operations performed under the contract, including rentals for movable and immovable property, and insurance premiums
- Interest paid to creditors of the contractor, subject to the limits stated in the contract
- Any accounting provisions made for clearly identified future losses or liabilities for probable future events
- With respect to a holder of a B-type permit, the total amount of royalties paid in cash or in-kind

The amount of prior-year losses that a company might have incurred during commercial production cannot be deducted from the taxable profit beyond the time limit allowed under the GTC, unless otherwise provided for in the contract.

Additional petroleum tax

An additional petroleum tax may be incurred by a holder of a B-type exploitation permit. This tax is calculated on the profits arising from petroleum operations. The applicable rate is determined in the contract.

Main taxes applicable under the new code

Corporate income tax

Similarly to the 1988 Ordinance, companies conducting petroleum operations within Mauritanian national territory are liable to CIT as provided for in the GTC. CIT is determined from the net profit arising from such operations — the applicable rate is specified in the contract, but it must be at least equal to the common tax rate applicable at the time the contract was signed. The current applicable rate is 25%.

From the first year of production and for each subsequent fiscal year, contractors must submit their annual tax return and financial statements to the Mauritanian tax authorities. The tax return and financial statements must be submitted before 31 March of the subsequent year, as specified in Article 74 of the new code. The deadline for the filing of a tax return has in fact been postponed to 1 April of the subsequent year, under the regular GTC regime, but the tax administration has yet to specify whether this amendment will apply to oil companies.

The PSC may provide that the production sharing that the State receives includes the CIT due by the contractor.

The same deductible expenses as those provided in the 1988 Ordinance are applicable under the new code, with the exception of royalties since there are no royalties payable under the new code.

Surface fee

The surface fee is an annual tax that is not deductible. The PSC determines the basis and rate for each phase of the research period and for the exploitation period.

Bonuses

Contractors are required to pay a bonus upon signing the contract. They are also liable to pay a production bonus when the quantity of hydrocarbons produced has reached certain thresholds determined in the contract.

These bonuses are not deductible for CIT purposes.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas under either of the regimes.

C. Capital allowances

Capital allowances are governed by the GTC and the PSC, and not by the hydrocarbons legislation.

Under the GTC and the PSC, for the purposes of determining the taxable net profit arising from petroleum operations, capital expenditure incurred by the contractor that is necessary for the petroleum operations is depreciated on a straight-line basis. The rates shown in the table below can be used as guidance, but the PSC may provide otherwise:

Nature of capital asset to be depreciated	Annual depreciation rate
Permanent buildings	5%
Temporary buildings	33.3%
Office and home furniture and fixtures	20%
Productive wells	20%
Production and delivery equipment	20%
Drilling equipment	33.3%
Pipelines	10%

D. Incentives

Under the 1988 Ordinance, contractors are exempt from any further tax on income that is in addition to royalties, CIT and additional petroleum Tax. There is therefore no additional tax on profits and the distribution of profits, nor is there any other levy, duty, tax or contribution on any transfer of funds or export of hydrocarbons. This exemption extends to income or activities of companies affiliated with companies holding exclusive petroleum exploration and exploitation rights, provided that such activities are directly related to petroleum operations.

In addition, as noted above, under the 1988 Ordinance, the holder of an exclusive right of exploitation is exempt from royalties.

The new code provides for an exemption from the following taxes:

- The minimum tax (*impôt minimum forfaitaire*)
- General income tax (usually due by individuals) and any other tax on profits
- Tax on movable property, as well as any other withholding taxes (WHTs) on profits distribution
- Any tax on turnover, including any tax on services
- Patent fees

- Registration fees
- Learning fees
- Any other tax, duty or contribution related to petroleum activities

Similarly to other oil-producing countries, Mauritania introduced an optional Simplified Tax Regime (STR) in 2004 for foreign companies providing services to contractors in the oil industry, and the STR has recently been integrated within the new code. Operations conducted in Mauritania by foreign subcontracting companies can be taxed under the STR, which provides for an exemption from all taxes with the exception of CIT and payroll tax (ITS). Using the STR is, though, optional.

E. Withholding taxes

Under the new code, contractors must withhold ITS at source and remit it to the Mauritanian tax authorities as provided by Article 84 of the General Tax Code. The ITS capped rate is 35% for expatriate employees in Mauritania.

The STR mentioned in Section D above is based on a withholding system that transfers the tax collecting burden from subcontractors to contractors. The STR covers taxes on salaries and CIT and consist to withhold 8% of the remuneration paid to sub-contractors. As the STR regime is an optional regime, a contractor must confirm, prior to making any payments to a subcontractor, whether that subcontractor has elected for the STR to apply.

If foreign subcontractors are taxable on their Mauritanian sourced income and do not opt for the STR, or if their application for the STR is rejected by the tax administration, they will be subject to the general tax regime.

The Finance Act for tax year 2013 introduced a 15% final WHT regime (RSI), which is applicable to nonresident providers of services or goods where those providers have entered into contracts with resident companies for a period not exceeding six months. This regime is optional and should also apply to foreign oil services companies. The resident oil company should request a prior-approval agreement on behalf of the nonresident services or goods provider and should withhold 15% of the amount paid to the latter.

The RSI exempts the foreign services or goods provider from General Income Tax, Minimum Tax, the tax on movable property (IRCM) and any other taxes and duties. However, contrary to the STR, expatriate personnel are still liable for ITS, capped at the rate of 35%. The RSI will constitute a tax credit, which the foreign services or goods provider is entitled to claim back from the Mauritanian tax administration.

If foreign subcontractors do not opt for the RSI, or the six-month period has expired, they should be subject to the general tax regime. However, the RSI regime can still be applied after the initial six-month period has expired to newly incorporated foreign companies or individuals who have not yet complied with their tax filing and payment obligations.

F. Financing considerations

Under the 1988 Ordinance, interest paid to creditors of the contractor is treated as a deductible expense, subject to the limits stated in the accounting procedure determined in the contract.

The new code provides for the same. However, its scope for deductibility is broader as it also includes interest paid to affiliated companies, provided they are related to financing petroleum activities and do not exceed the rates that would normally be charged in arm's-length transactions.

G. Transactions

There is no specific issue or limitation regarding transactions (e.g., transfers of shares) under either of the hydrocarbon regimes.

H. Indirect taxes

Under the 1988 Ordinance, the holder of an exclusive petroleum exploration or exploitation right is exempt from any taxes on turnover. Under the new code, contractors are subject to VAT at 0% rate regarding all transactions related to oil operations.

Local purchases of goods and services related to oil operations are subject to VAT at 0% rate. Imports are subject to VAT at 0% rate for all equipment related to oil operations and included in a list approved by Mauritanian Authorities or to the temporary import procedure (where a suspension of VAT applies). As noted above, the export of hydrocarbons is subject to VAT at 0% rate.

I. Other

Foreign-exchange controls

Contractors are subject to the exchange control legislation established by the Central Bank of Mauritania, in particular Law No. 2004-042 of 2004, which sets forth the applicable regime for financial relations with foreign countries.

Expatriate employees of contractors have the right of free exchange and free transfer of their Mauritania-sourced income to their own country, within the limits of the exchange control legislation.

Stability clauses

Under both regimes, the contract is expected to provide for a "stability clause" stating that the contractor shall not be subject to any legislative provision that would disadvantage it when compared with the legislation and regulations in force on the date of signing the contract.

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Tax regime applied to this country

- ☐ **Concession**[1]
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ■ **Service contract**

A. At a glance[1]

In December 2013, the Mexican Constitution was amended to loosen restrictions on the energy industry. These constitutional amendments represented a game changer for Mexico's state-owned hydrocarbon resources, as the basis to expand the types and nature of hydrocarbon investment contract models with private investors.

1 *Based on the last amendment made to the Mexican Constitution, private companies are now allowed to invest in exploration and production activities in Mexico through different contract regimes, such as license contracts, profit/production sharing contracts and service contracts. However, concessions to participate in these kinds of activities remain prohibited.*

In addition, the Mexican energy reform loosened control of other aspects of the energy industry, including a full liberalization of the midstream and downstream activities within the oil and gas industry, as well as an open market for the generation of power.

In August 2014, the secondary legislation was implemented, along with its regulations, in order to provide a strong legal framework for the opening up of the oil and gas industry. In general terms, this secondary legislation relies on the principle that un-extracted hydrocarbons remain property of the Mexican Nation; however, private companies can get remunerated through in-kind payments for the hydrocarbons that are extracted and according to the mechanisms established by each type of exploration and production contract. Additionally, the adopted legislation provides the road map for a free and open competition between State-owned companies (i.e., Petroleos Mexicanos, or PEMEX, the National Oil Company) and private companies, for the exploration and production of hydrocarbons.

Round 0 provided PEMEX with a new, slimmed-down portfolio of assets to exploit on its own or enter into first-ever joint ventures with major international oil companies. PEMEX requested 100% of proved reserves (P1), 83% of the proved and probable (P2), 71% of the proved, probable and possible (P3), and 31% of the prospective resources. The Mexican Government allocated P1, P2 and P3 reserves as requested by PEMEX and only 21% of the prospective resources.

In November 2014, the Mexican Government, through the National Hydrocarbons Commission (CNH), announced the launch of its inaugural bidding processes for Round 1, which started in 2015. Through Round 1, private companies were able to participate in the bidding processes for carrying out exploration and production of hydrocarbons activities in different types of blocks (i.e., shallow waters, onshore and deep water). See below the summary for Round 1 bidding processes that took place between years 2015 and 2016:

- Round 1 Phase 1 (R1.01 — exploration and extraction blocks in shallow waters) bid took place on 15 July 2015. Fourteen blocks were offered, but only two were awarded to a consortium. In this bidding procedure, a production sharing contract (PSC) was implemented. Terms and conditions of said contracts are summarized in the following section.
- Round 1 Phase 2 (R1.02 — extraction blocks in shallow waters) bid took place on 30 September 2015. The bid included five blocks for extraction of hydrocarbons in shallow waters. Out of the five blocks offered, three were awarded. As in R1.01, a similar PSC regime was implemented for this phase, with some differences, which are explained later in this guide.
- Round 1 Phase 3 (R1.03 — extraction in onshore blocks) bid took place on 15 December 2015. The bid included 25 onshore blocks. All contractual areas had offers and were assigned. A license contract regime was implemented in this phase.
- Round 1 Phase 4 (R1.04 — exploration and extraction blocks in deep water) bid took place on 5 December 2016. It included 10 blocks in two locations; 8 of them were awarded. As in R1.03, a similar license contract regime was considered for this phase. Differences in the contract regimes are explained later in this guide.

Later, in 2016, the CNH launched the bidding processes for Round 2, which also consisted of bidding for carrying out exploration and production of hydrocarbon activities in different types of blocks (i.e., shallow waters, onshore and deep water). See the summary below for the Round 2 bidding processes that have been taking place during 2016, 2017 and 2018:

- Round 2 Phase 1 (R2.01 — exploration and extraction in shallow waters) bid took place on 19 June 2017. The bid included 15 blocks in the Gulf of Mexico in three different areas: Tampico-Misantla, Veracruz and Cuencas del Sureste. Ten out of the 15 blocks received economic proposals and were awarded. A PSC similar to R1.01 was implemented for this bidding procedure.

- Round 2 Phase 2 (R2.02 — exploration and extraction of hydrocarbons — gas — in onshore blocks) bid took place on 12 July 2017. The bid included 10 blocks in three different areas: Cuenca Burgos, Cinturón Plegado de Chiapa and Cuencas del Sureste. Seven out of the 10 blocks received economic proposals and were awarded. A license contract similar to R1.03 was implemented for this bidding procedure.
- Round 2 Phase 3 (R2.03 — exploration and extraction of hydrocarbons in onshore blocks) bid took place on 12 July 2017. The bid included 14 blocks in four different areas: Cuenca Burgos, Tampico-Misantla, Veracruz and Cuencas del Sureste. All contractual areas had offers and were awarded. A license contract similar to R1.03 was implemented for this bidding procedure.
- Round 2 Phase 4 (R2.04 — exploration and extraction of hydrocarbons in deepwater blocks) bid took place on 21 January 2018. The bid included 29 blocks in three different areas: Perdido Fold, Cordilleras Mexicanas and Cuenca Salina. Nineteen out of the 29 blocks received economic proposals and were awarded. A license contract similar to R1.04 was implemented for this bidding procedure.

In addition, during the third quarter of 2017, CNH launched the bidding process to inaugurate Round 3, in which State-owned and private companies have been able to compete to carry out hydrocarbon exploration and production activities in different types of blocks (i.e., shallow water and onshore). It is important to highlight that for the first time, unconventional onshore blocks became part of a bidding process. See below the summary prepared for the Round 3 bidding process since its development date:

- On 28 September 2017, the CNH published the drafts of the bidding guidelines and license contract for shallow-water blocks offered in Round 3 Phase 1 (R3.01 — exploration and extraction of hydrocarbons in shallow water blocks), which includes 35 blocks in the Gulf of Mexico in four different areas: Burgos, Tampico-Misantla, Veracruz and Cuencas del Sureste. Sixteen out of the 30 blocks received economic proposals and were awarded. A PSC similar to R2.01 was implemented for this bidding procedure.
- Additionally, on 31 January 2018, CNH published the drafts of the bidding guidelines and license contract for onshore blocks offered in Round 3 Phase 2 (R3.02 — exploration and extraction of hydrocarbons in onshore blocks), which includes 37 blocks in four different areas: Sabinas-Burgos, Tampico-Misantla, Veracruz and Cuencas del Sureste. The bidding day is expected to happen in September 2018. A license contract similar to R2.03 was approved for this bidding procedure.
- Moreover, on 2 March 2018, CNH published the drafts of the bidding guidelines and license contract for onshore blocks offered in Round 3 Phase 3 (R3.03 — exploration and extraction of hydrocarbons in conventional and unconventional onshore blocks), which includes nine blocks in the Burgos area. The bidding day is expected to happen in September 2018, same as R3.02. A license contract similar to R2.02 was approved for this bidding procedure; however, said license contract includes some key differences, which are outlined later in this guide.

Furthermore, it is important to mention that, as part of PEMEX's strategy, Trion's block located in deep water off the coast of the Gulf of Mexico, which was assigned to PEMEX in Round 0 back in 2014, was migrated into a license exploration and production contract and was farmed out to other operators through a bidding process. In this regard, CNH handled the bidding process and published the drafts of the bidding terms for the election of a partner for PEMEX's subsidiary Pemex Exploración y Producción (PEP) to carry out jointly exploration and extraction activities in the Trion deepwater block (Farm Out Trion/2016), as well as the license contract and the joint operating agreement (JOA) models. The bid took place on 5 December 2016 with the license contract being signed by CNH on 3 March 2017. A license contract similar to R1.04 was implemented for this bidding procedure.

A similar process was launched on 7 March 2017 but, in this case, for farming out the Ayin-Batsil shallow-water block (Farm Out AYIN-BATSIL/2017), which was also assigned to PEMEX in Round 0. However, in this case, the contract regime that was considered for the bidding procedure was a PSC, similar to those considered for R1.01 and R2.01. The bidding day took place in October 2017; however, no proposals were submitted for the Ayin-Batsil block, and it was declared deserted.

Also on 2 May 2017, a bidding process for farming out Ogarrio and Cárdenas-Mora conventional onshore blocks (Farm Out OGARRIO/2017 and Farm Out Cárdenas-Mora/2017) was launched by CNH. These two blocks were also assigned to PEMEX in Round 0. In this case, the contract regime that was considered for the bidding process was a license contract, similar to those considered for R1.03, R2.03 and R2.03. The bid of both the Ogarrio and Cárdenas-Mora blocks took place in October 2017 with both license contracts being celebrated with CNH in March 2018.

Additionally, on 18 September 2017, a bidding process for farming out the second deepwater block, Nobilis-Maximino (Farm Out Nobilis-Maximino/2017) was launched by the CNH. The contract regime that was considered for this bidding process was a license contract, similar to the one considered for R1.04. However, since no companies registered for the bidding process, the bid was canceled in December 2017.

It is important to mention that recently, the Ministry of Energy has grouped several Pemex Asignaciones in order to form attractive exploration and production clusters (E&P clusters). CNH has announced that such clusters will be subject to migrate from Asignacion titles into exploration and extraction contracts through farmout bidding processes.

In addition, derived from the Mexican energy reform, the applicable legislation permits PEMEX to migrate its existing service contracts entered into with private companies (i.e., Integrated Service Contracts — CIEPs and Financed Public Works Contract) into exploration and extraction contracts. In this regard, as of the date of publication of this analysis, one CIEP and one COPF have migrated into PSC. The corresponding former service providers have become the operators of the blocks and PEMEX's partners.

Lastly, it is relevant to mention that in 2015, the Ministry of Energy (SENER) published the five-year licensing plan. In 2016 and 2017, the plan was revised, and an updated version was published in January 2018, which represents a new strategy that attempts to take into account both the industry's comments and the economic feasibility of upstream projects in Mexico.

Expansion of investment alternatives

Ending PEMEX's exclusive rights to Mexican hydrocarbons, the Mexican energy reform permits investors (both Mexican and non-Mexican investors through Mexican vehicles) to participate throughout the oil and gas value chain — from exploration activities to the refining of hydrocarbons. The Mexican energy reform specifically provides for four different types of contracts:

- Licensing contracts, whereby investors may be granted licenses offering the possibility of transferring oil to private companies once the hydrocarbons have been extracted, with the right to market such hydrocarbons
- Service contracts
- Profit sharing contracts, giving private companies a share of profits from operations in cash
- PSCs, in which oil barrels are divided between the State and the private companies

The Mexican energy reform also mandated the creation of a trust fund with the Mexican Central Bank. This trust was created in September 2014 and has been responsible for managing and distributing profits (excluding taxes) from the awarded contracts. Additionally, minimum local content requirements and other provisions will continue to enhance local Mexican participation in the expected build-out of the fields and related infrastructure.

Most importantly, the Mexican energy reform has generally permitted foreign companies to "book" the petroleum reserves (for financial and accounting purposes), by complying with certain requirements; however, as noted above, the hydrocarbons and ownership thereof will continue to remain the property of the Mexican Nation.

Fiscal regime

The Hydrocarbons Revenues Law (HRL) establishes that in order to participate in a contract bidding process to carry out exploration and production activities, companies must be Mexican, be residents in the country for tax purposes, have as their exclusive purpose the exploration and extraction of hydrocarbons, and not be taxable under the optional integration tax regime for group of companies (new limited tax consolidation regime in Mexico).

State-owned companies and private companies are entitled to participate in a bidding process either individually, through a consortium, or a joint venture.

In general terms, the Mexican fiscal regime that applies to the oil and gas industry consists of a combination of corporate income tax (CIT), government takes (depending on the type of contract), value-added tax (VAT), and other local taxes.

The HRL provides that depending on the contract (license, profit and production sharing, or service), contractors will pay the following considerations in favor of the Mexican State:

- Up-front signing bonus
- Contractual quota for exploration period (CQEP)
- Revenue-based royalty
- Profit sharing payment based on the net operating profit or value of hydrocarbons
- Over-royalty
- Tax on exploration and extraction of hydrocarbons (E&E tax)

On the other hand, a new entitlement regime is applicable to PEMEX and its subsidiaries by means of which those entities will become subject to CIT and government fees.

Other fiscal arrangements primarily include:

- Income tax rate — 30%
- Dividend payments income tax withholding — 10%
- VAT — 0% (i.e., E&P activities), 16%

B. Fiscal regime

As for the fiscal regime (oil revenues and taxation), the regulations are contained in the HRL. The HRL establishes that contractors would not only continue to be subject to the general federal taxes, including income tax and VAT, but also to additional types of fees, royalties and other payments that would have to be made under the new contracts and activities.

Contracts

The Government take varies depending on the contractual regime to which the Mexican entity is subject.

License contracts

Under the HRL, when the Mexican State enters into a licensing agreement with a contractor, the Government may receive an up-front signing bonus, CQEP, revenue-base royalties, and payments based on the value of hydrocarbons (over-royalties). In exchange, contractors will receive the transfer of the extracted hydrocarbons.

i. ***Signing bonus:*** The signing bonus consists of a lump-sum payment made upon signing of the licensing agreement. The lump-sum amount, as well as its payment conditions, will be determined by the Ministry of Finance on each contract and will be revealed during the bidding process. It should be mentioned this payment was only triggered in the event of a tie on the economic proposal values offered in the bidding process. However from the date in which the Round 2.4 bidding terms were published (i.e., 19 July 2017), it was established that just with the fact of bidding the maximum bid variables, the signing bonus, would automatically become part of the economic proposal value. In other words, even in the case that there is no tie in the economic proposal values, with only the fact of bidding the maximum bid variables, the bidder will have the obligation to pay the signing bonus.

ii. ***CQEP:*** The CQEP is a periodic payment that is made before extraction activities begin. For the 2018 fiscal year, the CQEP for the first 60 months is MXN1,294.71 (approximately US$69) per square kilometer and increases to MXN3,096.04 (approximately US$167) thereafter. These figures are indexed by Mexican INPC variation *(Indice Nacional de Precios al Consumidor)* on a yearly basis.

iii. ***Revenue-based royalties:*** Revenue-based royalties are payments to the Mexican State based on the gross income derived from oil, gas and condensate production.

- **Oil royalty.** The oil royalty rate is based on the value of the barrel of oil. If the price is under US$47.95 per barrel, the rate is fixed at 7.5%. If the price per barrel is above US$47.95, the rate will be increased according to the following formula:

  Rate = [(0.126 × contractual oil price) + 1.5]%

- **Gas royalty.** The royalty rate for:
  - Associated natural gas is the contractual price divided by 99.90.
  - Non-associated natural gas uses the following formulas:
    - If the price is less than or equal to US$5 per million BTUs, the royalty is 0%.
    - If the price is between US$5 and US$5.79 per million BTUs, the following formula should be used:

      Rate = ([contractual natural gas price − 5] × 60.5)/contractual natural gas price

    - If the price is more than US$5.79 per million BTUs, the formula for determining the royalty rate is the same as for associated gas (i.e., the contractual price divided by 99.90).
- **Condensates royalty:** With respect to condensates (i.e., natural gas liquids formed primarily by pentanes and heavier components of hydrocarbons), a progressive rate is established based on the price of the condensates. Under US$59.94, the royalty rate will be fixed at 5%. Over US$59.94, the following formula applies for determining the royalty rate:

  Rate = ([0.126 × contractual condensate price] − 2.5)%

- The revenue-based royalty formulas are indexed on a yearly basis according to Bureau of Labor Statistics of the United States of America *index WPU000000*. The figures provided are those applicable to fiscal year 2018.

iv. Over-royalties: The over-royalties are payments made to the Mexican Government based only on a percentage rate of the value of hydrocarbons.[2] The over-royalty has been one of the main bid variables elected by the Mexican Government in order to award license contracts on the bidding procedures corresponding to R1.03, R1.04, R2.03, R2.04, and farm outs from Trion, Ogarrio, and Cárdenas-Mora blocks. Also, it will be used as one of the bidding variables for the upcoming bidding procedure corresponding to R3.02.

2 *Unlike previous license contracts, for R3.03 the consideration that shall be paid to the Government will be a percentage of the operating profit. The former shall be calculated in accordance with the provisions set forth in the license contract as explained below.*

- **Adjustment mechanism***:* An adjustment mechanism to effectively capture extraordinary profits for the Government should be included in the contracts. For purposes of license contracts corresponding to R1.03, R2.02, R2.03 and R3.02, an adjustment mechanism determined according to daily average production of hydrocarbons was included.[3] In other words, if the daily production reaches a determined cap, the over-royalty that is paid to the Mexican State is increased by a formula that is contained in the contract. On the other hand, license contracts corresponding to R1.04, R2.04 and Trion's farm out, consider an adjustment mechanism (R-factor) based on the profitability; which is a ratio between the revenues of the contractor and its expenditures.

Profit and production sharing contracts

Under profit sharing contracts and PSCs, the Mexican State may receive CQEP, revenue-based royalties and a percentage on the net operating profit. The contractor may receive cost recovery and compensation based on the remaining percentage of the operating profit:

i. ***CQEP*** is determined using the same terms described in the license contracts.
ii. ***Revenue-based royalties*** are determined using the same terms described in the license contracts.
iii. ***Government's percentage of operating profit:*** This consideration is determined by the application of a percentage to the operating profit. Said variable has been one of the main bid variables elected by the Mexican Government in order to award PSCs on the bidding procedures corresponding to R1.01, R1.02 and R2.01. Also, it will be used as one of the bidding variables for the upcoming bidding procedure corresponding to R3.01.
iv. ***Adjustment mechanism:*** An adjustment mechanism to effectively capture extraordinary profits for the Government should be included in the contracts. For the purposes of PSCs corresponding to R1.01, R1.02, R2.01 and R3.01, an adjustment mechanism determined on an IRR-based system was included.

The operating profit is determined by subtracting from the contractual value of the hydrocarbons, the amount of revenue-based royalties and the recovery of costs, expenses, and investments.[4] It is important to mention that the costs, expenses and investments recovered in each period are capped to a percentage of the contractual value of hydrocarbons (cost recovery limit).

Additionally, the HRL provides that the following costs will be considered non-recoverable: (i) financing costs; (ii) costs derived from negligence or fraud; (iii) donations; (iv) costs and expenses derived from easements and acquisition of land or rights over land (including legal hydrocarbons easements constituted under the Hydrocarbons Law); (v) non-approved advisory services; (vi) cost from noncompliance of the relevant provisions, including risk administration; (vii) unqualified training expenses; (viii) cost from non-compliance of warranties conditions; (ix) expenses for the use of owned technology unless proven to be at arm's length; (x) most provisions and reserves; (xi) legal fees; (xii) broker fees; (xiii) royalties and contractual payments during the exploration phase as well as payments of compensations, costs, expenses and investments related to other contracts; and (xiv) those not strictly necessary for the execution of the contract.

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3 *For R3.03 license contract, adjusted mechanism will be calculated on a yearly basis based on an accumulated profitability factor (i.e., contractual value of hydrocarbons net from revenue-based royalties, CQEP and E&E Tax/costs, expenses and investments incurred for the development of petroleum activities.)*

4 *For purposes of R3.03 license contract, unlike PSC and profit sharing contracts, the operating profit will be equivalent to the contractual value of hydrocarbons net from revenue-based royalties, CQEP, E&E Tax and costs, expenses and investments incurred for the development of petroleum activities.*

Additionally, for R1.01, R1.02, R2.01 and R301, the contracts included other limitations on cost recovery, such as: (i) only up to 60% of the value of production in any month may be allocated to cost recovery and any unrecovered costs would be carried forward until fully recovered; (ii) the costs, expenses or investments that are unrelated to the contract and those incurred before the effective date of the contract or after its termination are not recoverable; (iii) the costs, expenses or investments that don't have supporting documentation, those that have not been registered in the operating account, or those that have not been included in the budgets and work programs approved by the CNH; and (iv) the costs, expenses or investments that raise the total budget over 5% of the original budgeted amount or 10% over the original budgeted amount for a specific item; among others.

Lastly, it is worth mentioning that in both profit sharing contracts and PSCs the operating profit is determined in the same way, but the difference between these two contracts is the following:

- In a profit sharing contract, all of the production shall be delivered to the State's marketer, which shall deliver the proceeds of the sale of such production to the Mexican Petroleum Fund. The Petroleum Fund will receive and distribute the payments in cash that correspond to the Mexican State and contractor.
- In a PSC, the Petroleum Fund will receive all the production of hydrocarbons and will distribute the proportion of the production of hydrocarbons that corresponds to the Mexican State and the contractor.

Service contracts

Under service contracts, the contractor is obliged to provide services to the State in exchange of a consideration in cash.

Many of the existing CIEPs and COPFs are on the process of migrating into exploration and extraction contracts; however new services contracts (i.e., exploration and extraction integrated services contracts — CSIEEs) are being offered to private companies by the Mexican authorities through a bidding process.

Entitlements (Asignaciones)

Under this regime, PEP (PEMEX subsidiary) is obliged to pay the corresponding income tax, as well as the following government fees for the exploration and production activities regarding the blocks that were assigned in Round 0:

i. ***Profit sharing fees:*** The assignation holders should annually pay the profit sharing fee by applying a percentage rate to the difference resulting from subtracting the deductions allowed under the HRL from the value of the hydrocarbons extracted during the fiscal year in question, including the consumption of these products by the assignation holder, as well as the reductions derived from spills or burnings of said products. For 2015, the applicable rate was 70%, with transitory provisions that change the rate to 68.75% for 2016, 65% for 2017, 66.25% for 2018, and 65% for 2019 and thereafter. The aforementioned fee should be paid by means of a return submitted at the latest by the last working day of March of the year.
ii. ***Hydrocarbon extraction fee:*** The assignation holder will be obliged to pay on a monthly basis the hydrocarbon extraction fee, applying the respective rate to the value of the hydrocarbon in question extracted during the month.
iii. ***Hydrocarbons exploration fee:*** The assignation holder will be obliged to pay on a monthly basis the hydrocarbon extraction fee, for the portion of the assignation area that is not in a production phase, in accordance with the following rates. The fee starts at MXN1,294.71 (approximately US$69) per square kilometer for the first 60 months and increases to MXN3,096.04 (approximately US$167) thereafter.

Tax on exploration and extraction of hydrocarbons

The HRL imposes a tax on exploration and extraction of hydrocarbon activities that is applicable to contractors and assignation holders. The tax during the exploration phase will be MXN1,688.74 (approximately US$91) per square kilometer assigned to the contractor (or assignation holder) and MXN6,754.99 (approximately US$364) per square kilometer during the extraction phase.

In this regard, and according to the HRL, the exploration phase encompasses the timeframe starting from the contract execution until the beginning of the extraction phase. On the other hand, according to Mexican Miscellaneous Tax Resolution for 2018, the extraction phase is triggered at the moment in which the CNH notifies the contractor the approval of the first development plan for the contractual area.

This tax should be paid on a monthly basis, and the amount is adjusted on a yearly basis.

Compensation for the acquisition or temporary use of land

As mentioned above, the Hydrocarbons Law establishes a special procedure for the acquisition of land or rights to use land when required to perform exploration and production activities under a contract. The consideration that will be paid to the landowners shall cover the following: (i) encumbrances over goods or rights that are different from rights over lands; (ii) foreseen damages calculated on the basis of habitual activity of the property; (iii) rent for occupation, easement or land use; and (iv) for projects that reach commercial production of hydrocarbons, a percentage between 0.5% and 2% (3% in the case of non-associated natural gas) of the contractor's income, after payments are made to the Government. The consideration agreed can be paid in cash or by any of the following means: (i) contracting commitments to become part of the labor; (ii) the purchase of manufactured goods or services; (iii) commitment to be part of projects and developments; (iv) any other consideration that is not contrary to the law; or (v) a combination of the above.

Local content

The Hydrocarbons Law and its regulations establish that exploration and production of hydrocarbons activities in Mexico should reach a minimum local content requirement for cost, expenses, and investments. Local content minimum percentages that have been applicable in Round 1 and Round 2 have been the following:

Local content applicable for R1.01:

- 13% on the exploration phase
- 25% in the development phase, increasing annually until in 2025 to at least 35%
- 35% from 2025 onwards

Local content applicable for R1.02:

- 17% in the appraisal period
- 25% in the development phase, increasing annually until 2025 to at least 35%
- 35% from 2025 onwards

Local content applicable for R1.03:

- 22% in the appraisal period
- 27% in the development phase, increasing annually until 2025 to at least 38%
- 38% from 2025 onwards

Local content applicable for R1.04:

- 3% during the initial exploration phase
- 6% during the first extension of the exploration phase
- 8% during the second extension of the exploration phase
- 4% from the approval of the development plan and upon the beginning of the regular commercial production; such minimum percentage shall increase up to 10% of the referred concepts, from the beginning of the regular commercial production in any development area

Local content applicable for R2.01:

- 15% during the exploration phase
- 17% during the appraisal phase

- 26% in the first year of the development phase, increasing annually until 2025 to at least 35%
- 35% from 2025 onwards

Local content applicable for R2.02:

- 26% during the exploration phase
- 26% during the appraisal phase
- 27% in the first year of the development phase, increasing annually until 2025 to at least 38%
- 35% from 2025 onwards

Local content applicable for R2.03:

- 26% during the exploration phase
- 26% during the appraisal phase
- 27% in the first year of the development phase, increasing annually until 2025 to at least 38%
- 35% from 2025 onwards

Local content applicable for R2.04:

- 3% during the initial exploration phase
- 6% during the first extension of the exploration phase
- 8% during the second extension of the exploration phase
- 4% from the approval of the development plan and upon the beginning of the regular commercial production; such minimum percentage shall increase up to 10% of the referred concepts, from the beginning of the regular commercial production in any development area

Local content applicable for R3.01:

- 15% during the exploration phase
- 17% during the appraisal phase
- 26% in the first year of the development phase, increasing annually until 2025 to at least 35%
- 35% from 2025 onwards

Local content applicable for R3.02:

- 26% during the exploration phase
- 26% during the appraisal phase
- 27% in the first year of the development phase, increasing annually until 2025 to at least 34%
- 35% from 2025 onwards

Local content applicable for R3.03:

- 26% during the exploration phase
- 24% during the appraisal phase
- 21% in the first year of the development phase, increasing annually until, in a term no longer than eight years from the beginning of the development phase, start is at least 35%
- 35% from 2025 onwards

Local content applicable for Trion Farm Out:

- 3% during the initial exploration phase
- 6% during the first extension of the exploration phase
- 8% during the second extension of the exploration phase
- 4% from the approval of the development plan and upon the beginning of the regular commercial production; such minimum percentage shall increase up to 10% of the referred concepts from the beginning of the regular commercial production in any development area

Local content applicable for Ogarrio and Cárdenas-Mora Farm Outs:

- 27% in the first year of the development phase, increasing annually until 2025 to at least 38%
- 38% from 2025 onwards

It is worth mentioning that if the above percentages are not met, the contractor will be subject to penalties that will be determined by the Ministry of Economy. However, the guidelines regarding the application of the methodology is still pending to be published.

Corporate income tax

Under the Mexican Income Tax Law (MITL), the CIT rate is 30%. Mexican resident companies are taxed on their worldwide earnings. A corporation is considered to be a Mexican resident if its "effective place of management" is located in Mexico. It is important to mention that remuneration in-kind (in favor of the contractor) for the onerous transmission of the hydrocarbons, once extracted from the subsoil, shall not be accrued as an income.

A permanent establishment (PE) of a foreign resident is generally taxed in the same manner as a Mexican resident, but it is taxed only on income attributable to the PE. It is important to have in mind that a PE could be created without the signing of an agreement; only services need an agreement to be provided.

The HRL includes an expanded definition of PE, which would also be applicable for income tax purposes for nonresidents performing any activity under the Hydrocarbons Law in Mexican territory for more than 30 days in any 12-month period. Nevertheless, it is important to analyze the interaction that it has with double tax treaties.

Dividends

Dividend withholding tax

Starting in 2014, the MITL incorporated a 10% dividend withholding tax rate on dividends paid to Mexican individuals as well as foreign residents. Therefore, dividends between Mexican resident entities are still not subject to withholding tax at the shareholder level. In certain instances, the Mexican tax treaties may provide tax relief from this dividend withholding tax.

The definition of "dividend" for purposes of the 10% dividend withholding tax includes, among others: (i) interest paid on preferred shares; (ii) loans to shareholders and partners, unless the loan is established for less than one year, is incurred in the operations of the business and meets certain requirements; (iii) payments that are considered nondeductible and benefit the shareholders; (iv) amounts not recognized as a result of omissions of income or unrealized purchases; and (v) transfer pricing adjustments to income or expenses as a result of assessments by the tax authorities for related-party transactions.

In addition to the dividend withholding tax, distributing companies are subject to CUFIN (taxed earnings account) rules, which result in a tax to the extent that a dividend is paid in excess of CUFIN. If the Mexican company has enough CUFIN balance to cover the dividends, no tax at the corporate distributing company level should be triggered. If the amount of the dividend distribution exceeds the CUFIN balance, the excess amount would be subject to 30% CIT on a grossed-up basis (i.e., the dividend multiplied by a gross-up factor of 1.4286). Therefore, the effective tax would be 42.86%.

The Mexican tax treaties should not provide any relief from this tax, because it is imposed at the Mexican corporate level and not the shareholder level, through a withholding tax. The tax paid under the foregoing test should be creditable against the current annual income tax liability of the Mexican distributing company in the year in which the excess distribution is made and the following year if any portion cannot be credited in the first year.

A reduction of capital may be reclassified as a dividend for the excess CUFIN distribution tax if certain conditions are met.

Branch remittance tax

A 10% distribution tax applies on distributions from a Mexican PE to its foreign head office. As mentioned above, a 10% dividend withholding tax applies on distributions from a Mexican PE to its foreign head office. In certain instances, the Mexican tax treaties may provide tax relief from this dividend withholding tax.

Distribution rules similar to those for dividends from Mexican resident entities apply to nonresident entities with a PE or branch in Mexico. For this purpose, the branch is required to keep an account (known as the CURECARE) for capital remittances made to the non-Mexican-resident head office. In general terms, the CURECARE balance shows the amount of earnings that have been subject to corporate income tax by the PE. Additionally, Mexican branches are also required to record their previously taxed earnings through the CUFIN account. If a remittance is made to the head office of the Mexican PE, it is deemed to be a dividend distribution from previously taxed earnings. If the payment of the remittance exceeds the CURECARE and CUFIN balances, the excess dividend must be grossed up with a 1.4286 factor, with the result multiplied by the CIT rate (currently 30%).

Deductibility requirements

In general, expenses related to the business activity of a taxpayer are deductible for income tax purposes. In addition, Mexico has formalistic documentation requirements that must be met to support the deduction, including requirements related to accounting records, as well as invoices.

Some additional concepts applicable to companies engaged in oil and gas extraction and production activities, such as abandonment funding and payments to the State, have been included as deductible expenses as long as they meet the requirements provided in the applicable legislation

Payroll-related expenses

Fifty-three percent of payroll-related expenses, including contributions to pension funds that are considered exempt income for employees, are considered nondeductible. The nondeductible amount may be reduced to 47%, as long as the amount of the benefits that are exempt for employees has not been reduced compared with the amount paid to employees in the prior year.

Interest, royalties and technical assistance

Deductions are denied for interest, royalties or technical assistance if the income is not subject to tax for the foreign recipient. Specifically, the deduction is denied for payments that are made to a foreign entity that controls or is controlled by the Mexican taxpayer and meets one of these conditions:

- The payments are made to a foreign entity that is fiscally transparent (as defined), unless the shareholders or partners are subject to tax on the foreign entity's income and the payments are made at arm's length.
- The payments are not deemed to exist for tax purposes in the country or territory in which the entity is resident.

  Or
- The foreign entity does not accrue the taxable income under the applicable tax rules.

For this purpose, control is deemed to exist when one of the parties has, either directly or through an intermediary, effective control or control of the administration of the other to the level of deciding the moment to distribute or share revenue, income or dividends. It is notable that the rule references and defines "controlled" or "controlling" recipients, rather than all related parties, which is already a broadly defined term under Mexican income tax rules.

Among other related-party transactions, agreements and structures related to the lease of vessels, rigs or other type of machinery and equipment used by the oil and gas industry have to be revised based on these rules, as rental payments are deemed royalties for tax purposes in Mexico.

Expenses deducted by an affiliate

- Deductions of expenses that are also deducted by a related party in another jurisdiction are denied, unless the affiliate is also recognizing income of the Mexican taxpayer in the same year or the subsequent year.

Capital gains

Capital gains and losses are treated as ordinary income and deductions, except for most losses arising from the disposal of shares. Losses arising from the disposal of shares are generally not deductible against ordinary income. Unless otherwise provided, losses from the disposal of shares may only be used to offset gains derived from the sale of stock or securities during the same tax year or the subsequent 10 tax years.

A "gain" or "loss" is computed as the difference between the sale proceeds and the cost of the asset. The cost of the assets is adjusted for inflation using updated factors based on the National Consumer Price Index. The tax basis of shares of a Mexican entity is also adjusted for changes in the CUFIN account of the company, as well as the net operating losses.

Capital gains from the sale of publicly traded shares are taxed at a rate of 10% for individuals and nonresidents. As defined in the MITL, certain requirements must be met to qualify for the 10% rate as opposed to the general 35% tax rate on the net gain, including, but not limited to, the requirement that a shareholder or a related group of shareholders should not sell more than 10% of the capital of the issuer in a two-year period and/or the transaction should not be deemed to be as a planned transaction.

Notwithstanding the above, the MITL includes an exemption from capital gains on the sale of shares of publicly traded companies over a recognized stock exchange when made by a resident of a country with which Mexico has entered into a tax treaty. For this purpose, the shareholder is required to file, with the custodian, a sworn statement of residence and compliance with the treaty.

Profit sharing

Employers in Mexico must pay profit sharing to employees each year equal to 10% of the taxable income of the business. It is important to analyze the structure implemented to operate in Mexico.

Transfer pricing

Mexican taxpayers are required to conduct transactions with related parties on an arm's-length basis. In addition to filing an annual informational return, taxpayers are required to produce and maintain contemporaneous documentation (i.e., a transfer pricing study) demonstrating that income and deductions arising from intercompany transactions are consistent with the amounts that would have resulted had these transactions taken place with unrelated parties under similar conditions. In recent years, transactions between related parties have been subject to greater scrutiny.

It may be possible to reach an advance pricing agreement (APA) with the Mexican tax authorities (commonly known as "Hacienda") in order to obtain confirmation of a method used. These agreements may apply for a period of up to five years in the case of unilateral agreements and for more years in the case of mutual agreements.

According to HRL for purposes of cost recovery and the computation of the operating profit in the profit sharing and PSCs, transfer pricing provisions should be met. Likewise, the HRL establishes that in cases in which contractors carry out transactions with related parties, the Transfer Pricing Guidelines issued by the OECD would apply. Contracts from Rounds 1, 2 and, 3 include the obligation for the contractors to file a transfer pricing report on annual basis.

There are three new comprehensive informative tax returns (envisioned to be in line with the reports to avoid base erosion and profit shifting practices issued by the OECD) for certain Mexican tax residents that carry out transactions with foreign and Mexican related parties. These returns aim to obtain comprehensive information of the whole multinational group on a yearly basis:

- Master informative return
- Local related parties informative return
- Country-by-country informative return

Functional currency

The functional currency for Mexican tax purposes is always the Mexican peso. It is not possible to elect any other currency as the functional currency. As established in the license and PSCs applicable in Rounds 1, 2, and 3 the Mexican peso must be used for accounting purposes, registration, and taxes. US dollars shall be used for operations and reporting of the operating account.

C. Capital allowances

Taxpayers are required to depreciate the costs of pre-operating expenses, fixed assets and intangible assets using the straight-line method. The amount of the depreciation deduction is adjusted for inflation from the date of the acquisition until the tax year in which the deduction is taken. For this purpose, the MITL provides statutory depreciation rates; however, taxpayers may elect a lower rate than provided for by law.

In addition to the percentages included in the MITL, the HRL establishes the following rates for asset depreciation that could also be used for tax purposes:

- 100% of original investment amount for exploration, secondary and enhanced oil recovery, and non-capitalized maintenance.
- 25% of original investment amount in the exploration and development of oil and natural gas deposits.
- 10% of original investment amount made in infrastructure for storage and transportation required for the execution of the contract, such as oil and gas pipelines, terminal, transportation, or storage tanks required for the contractual production

The Mexican tax authorities issued regulations that state that percentages established in Articles 32 and 46 of the HRL are not maximums, contrary to the depreciation rules established in the MITL that allow the application percentages lower than the maximum at the election of the taxpayer.

It is important to take into account that these rates apply only to oil and gas exploration and extraction companies and not to the entire oil and gas industry.

D. Tax losses

As a general rule, the MITL establishes that net operating losses (NOLs) obtained in one fiscal year may be carried forward for 10 years, however, no carryback is allowed. The HRL establishes that losses derived from the execution of deep water contracts may be carried forward for 15 years. The amount of NOLs' that may be used in a particular tax year is adjusted for inflation by multiplying the amount by the inflation factor for the period from the first month of the second half of the tax year when the loss was incurred until the last month of the first half of the tax year when the NOL is used.

In a merger, only the NOLs of the surviving company continue to exist after the merger. Furthermore, the NOLs of the surviving entity may be used exclusively to offset income generated by operations of the same category as the operations that produced the losses. Thus, the merger of a profitable company into a loss-making company, designed to use the latter's losses to offset profits, is effective only if the activities conducted by the profitable company prior to the merger are in the same line of business as the loss-making company.

The NOLs of a company that undergoes a corporate split survive after the transaction. The NOL balance of the original company is allocated between the old and new entities based on the type of businesses the companies are engaged in. The NOL allocation is based on inventory and accounts receivable balances if the entities are engaged in commercial activities, and the allocation is based on the fixed asset balances if the entities are engaged in industrial activities.

In the case of a change, either direct or indirect, of the shareholders of a company that has tax losses, the usage of the NOLs may be restricted. This rule applies when the sum of the gross income in the three prior tax years is less than the amount of the available NOLs, adjusted for inflation. If this test is met, the tax losses may be exclusively used to offset income from the same business activity that generated the losses. A change in the controlling partner or shareholder is deemed to occur when there is a change of shareholders, either directly or indirectly, of more than 50% of the shares or social parts with voting rights of the company, in one or more transactions over a period of three years.

Pursuant to newly issued Mexican regulations, taxpayers carrying out deep water activities (areas with a water depth greater than 500 meters) and in different areas should compute two different tax results: one comprising income and deductions applicable for those activities carried out in deep water and the second tax result applicable for that income and deductions applicable to different areas. Additionally, regulations include a procedure on how to calculate the aforementioned tax results when the income and deductions are not clearly identified to one specific area.

E. Withholding taxes

Mexico collects taxes borne by foreign residents with Mexican source income via the withholding mechanism. To qualify for a beneficial treaty rate, a certificate of tax residence is required; among other formal requirements that may be applicable under domestic and treaty regulations. With respect to related-party transactions, the tax authorities may request that the foreign resident documents the existence of a legal double taxation, through a sworn oath signed by the legal representative stating that the income subject to tax in Mexico to which the treaty benefit is also subject to tax in the country of residence. Some exceptions may be applicable to this requirement.

Some of the entries in the table below have been described in more detail in section B above.

Item of income	Domestic withholding rate*	Regular reduced rate available with treaties
Dividends	10%	0%–5%
Branch remittance tax	10%	0%–5%
Royalties for the use of patents, certificates of invention or improvements, trademarks and trade names	35%	10%
Other royalties, including know-how and payments for the use of commercial, scientific or industrial equipment	25%	10%
Technical assistance	25%	0%
Bareboat charter of vessels (with cabotage in Mexico)	10%	10%
Timer charter of vessels	25% or PE	0% or PE
Payments for services rendered in Mexican territory	25%	0% or PE
Payments for services rendered outside Mexican territory	Not subject to withholding	–
Interest	4.9% to 35%	10%–15%

* Withholding tax may increase up to 40% in any case, if paid to a tax haven or certain tax-transparent vehicles.

F. Financing considerations

Thin capitalization rules

Mexico adopted thin capitalization rules denying the deduction of interest expense on loans with nonresident related parties when the company has a debt-to-equity ratio that exceeds three to one. Notwithstanding, the MITL establishes that the three-to-one debt-to-equity limitation is not applicable if debt is contracted for financing the construction, operation, or maintenance of infrastructure that is related to certain strategic sectors. Due to the consideration of exploration and production of hydrocarbons activities as a strategic sector in Mexico, thin capitalization rules may not apply to certain oil and gas activities.

Dividend re-characterization rules

Interest paid on a loan from a related party is treated as a nondeductible dividend if the loan has any of the following characteristics:

- The loan agreement provides that the debtor unconditionally promises to repay the loan at any time determined by the creditor.
- In the event of default, the creditor has the right to intervene in the administration of the debtor's business.
- The payment of interest is conditional on the availability of profits, or the amount of the interest is determined based on the profits.
- The interest rate is not stated at a fair market rate.
- The interest is derived from a back-to-back loan, including a back-to-back loan entered into with a financial institution.

Inflationary adjustment

Mexican companies must recognize for tax purposes the inflationary gains or losses attributable to their monetary liabilities and assets. Thus, in determining how to finance an investment in Mexico, consideration must be given to the income tax treatment of interest expense, whereby the inflationary gains arising from the debt may, in whole or in part, offset the interest expense and thereby erode the tax benefit from the interest expense deduction.

Exchange gains and losses

In the case of financial assets and liabilities denominated in a foreign currency (i.e., any currency other than Mexican pesos), the resulting exchange gains and losses are treated in the same way as interest, and they are recognized on an accruals basis.

G. Transactions

Asset disposals

The transfer of assets in Mexico is generally a taxable transaction subject to the general CIT rate of 30%, unless the transfer occurs as a result of a qualified reorganization. Mergers and demergers can be done tax-free between Mexican-resident entities if certain conditions are met.

Selling shares in a company

The MITL provides that a foreign resident is deemed to have Mexican-sourced income if it sells (i.e., transfers) shares of a Mexican-resident company or if it transfers shares in a non-Mexican entity whose accounting value (more than 50%) is derived from real property located in Mexico. Under domestic rules, the seller has the option of being taxed at either 25% on gross proceeds or 35% on the net gain (the difference between the sales price and the tax basis of the shares). It should be noted that the net-gain treatment is allowed exclusively for shareholders resident in countries that are not deemed to have a preferential tax regime or territorial tax jurisdiction. The tax basis is determined as the historical acquisition price of the shares, net of capital redemptions, adjusted for inflation, with the addition or subtraction of positive or negative fluctuations in the Mexican company's CUFIN account and an adjustment for the increase or decrease in the balance of NOLs during the period the shares were held. The 35% tax rate can only be elected if certain requirements are fulfilled. Note that sellers that are residents of tax havens are subject to tax on a gross basis at the rate of 40%.

In the case of a group restructuring, it is possible to transfer the shares and defer the income tax due until the shares leave the group (a group is considered to be a group of companies when at least 51% of the voting shares are directly or indirectly owned by the same corporate entity). Certain tax treaties entered into by Mexico provide an exemption for capital gains tax or for tax-free corporate reorganizations. Please refer to Section B's subsection on "capital gains" for further details of the tax treatment on capital gains from the sale of publicly traded shares.

H. Indirect taxes

VAT

Under the Mexican VAT Law, VAT is imposed on legal entities and individuals that carry out any of the following activities in Mexico: sell goods and property, render independent services, grant the temporary use or enjoyment of goods (e.g., leasing), and import goods or services. While the general 16% VAT rate is applicable to most transactions, there is also a 0% rate applicable to certain transactions; such as the exportation of goods and certain services, and sales of food, medicines, books, and gold.

The HRL establishes that any activity that requires compensation to be paid between the contractor and the Government will be subject to a 0% VAT rate. This provision does not apply to contracts entered into between the contractor and other third parties.

Generally, the VAT that is paid to suppliers (input tax) is creditable against the VAT charged to customers (output tax). Consequently, the amount that companies must remit to the Mexican tax authorities is the excess of the total VAT collected during the tax period from their customers over the VAT paid to suppliers. If, in a given period, VAT credits exceed the VAT collected from customers, the excess may be carried forward to the following tax period or, alternatively, the taxpayer may obtain a refund for such excess or offset the excess against other federal taxes.

It is important to mention that there has been an amendment to the VAT Law regarding VAT paid on expenses and investments made during the pre-operative period. In this sense, for upstream companies, pre-operative period means the exploration for the location and quantification of new hydrocarbons reservoirs that can be exploited. Such pre-operative period will have a one-year term, unless the taxpayer proves otherwise to the tax authorities through the investment project. In case taxpayers do not start taxable operations once the pre-operative period has elapsed, they shall repay the VAT refunded plus an inflation adjustment and applicable interest.

However, the same article provides for a special rule that establishes that for the upstream companies, when the extraction of hydrocarbons is not feasible, or when the extraction is financially unsustainable for reasons not attributable to the contractor, the obligation to repay the VAT refunded should not be applicable.

On 22 December 2017, Mexican Miscellaneous Tax Resolution for 2018 was published in the *Official Gazette*. In this regard, Mexican tax authorities issued certain rules for clarifying the determination and refund request procedure of VAT accrued within preoperative period for contractors and for companies that have not been awarded with a contract.

Notwithstanding the above there is still some uncertainty regarding VAT treatment for both kind of companies.

Import duties

All foreign goods, equipment, and materials that enter Mexico are subject to import duties as well as VAT. There are exemptions for import duties under certain free trade agreements and special trade programs. Special preferential duty rates are available under the North American Free Trade Agreement (NAFTA) and the free trade agreements between Mexico and Bolivia, Chile, Colombia, Costa Rica, El Salvador, the European Free Trade Association (EFTA) (Iceland, Liechtenstein, Norway and Switzerland), the European Union (EU), Guatemala, Honduras, Israel, Japan, Nicaragua, Peru, and Uruguay, among others. To qualify for these preferential duty rates, the importer must present a certificate of origin at the time of customs clearance.

Temporary importation regime

The VAT exemption on the temporary importation of goods under certain import regimes was eliminated under the tax reform for 2014 tax year. However, it is important to bear in mind that these tax changes did not affect the temporary importation regime of vessels, rigs, platforms, or other similar equipment used in the oil and gas industry.

Export duties

In general, the export of goods is not subject to VAT or other duties. However, it is important to bear in mind that the exportation of certain services (not goods) is subject to the general VAT rate of 16%, which implies an additional cost for the recipient of the services outside Mexico.

Excise tax

Under the Mexican Excise Tax Law, the importation or sale of certain products, as well as the rendering of certain services, is subject to excise taxes based on specific characteristics (e.g., alcoholic beverages, gasoline and diesel).

Excise tax applies to the importation and sale of fuels. Excise tax on fuels is computed in proportion to the volume of imported or sold fuels. The tax rates included in the Excise Tax Law are reinstated by inflation on a yearly basis. The applicable tax rates are, therefore, published in the Mexican *Official Gazette* on a yearly basis (usually the second half of December). The 2018 Excise Tax Law provides a tax exemption for crude oil and natural gas.

Excise tax for 2018 is imposed on the importation and sale of the fossil fuels listed in the table below:

	Fossil fuel	Rate
1.	Propane	6.93 cents per liter
2.	Butane	8.98 cents per liter
3.	Gasoline, avgas	12.17 cents per liter
4.	Jet fuel and other kerosene	14.54 cents per liter
5.	Diesel	14.76 cents per liter
6.	Heavy oil (combustóleo)	15.76 cents per liter
7.	Fuel oil	18.29 pesos per ton
8.	Fuel coal	42.88 pesos per ton
9.	Mineral coal	32.29 pesos per ton
10.	Other fossil fuel	46.67 pesos per ton of carbon in the fuel

Two additional tax rates are applicable for gasoline and diesel only. For 2018, the excise tax applicable to gasoline and diesel for importation and sale is as follows:

Importation fees (amounts in MXN per fuel liter)			
Concept	Gasoline < 92 octanes	Gasoline > 92 octanes	Diesel
Fixed fee	4.59	3.88	5.04
Incentive applicable to fixed fee(1)	(1.578)	(0.0363)	(1.74)

Importation fees (amounts in MXN per fuel liter)			
Concept	Gasoline < 92 octanes	Gasoline > 92 octanes	Diesel
Additional fee for fossil fuels(2)	0.1217	0.1217	0.1476
Total fees applicable for importation	**3.1337**	**3.9654**	**3.4476**

Sale fees (amounts in MXN per fuel liter)			
Concept	Gasoline < 92 octanes	Gasoline > 92 octanes	Diesel
Fixed fee	4.59	3.88	5.04
Incentive applicable to fixed fee(1)	(1.578)	(0.0363)	(1.74)
Additional fee for fossil fuels(2)	0.1217	0.1217	0.1476
Fixed fee applicable to sales only	0.4052	0.4944	0.3363
Total fees applicable for importation	**3.5389**	**4.4598**	**3.7839**

(1) This incentive, which applies to the fixed fee, has been changing on a weekly basis. Readers should check the exact incentive's rate for computing the final Mexican Excise Tax.

(2) These fees are the same as those depicted in the first chart of this section.

Price controls on gasoline and diesel were fully lifted to reflect open market conditions on November 2017. The fuel market in Mexico, began deregulation in March 2017 with the Northwest states and continued to move downward to the Southeast states. In this regard, unlike past years, for gasoline and diesel markets, Mexican authorities no longer set forth maximum prices.

I. Other

FIBRAs E (new investment vehicles)

In 2015, several actions seeking to promote Mexico's economic development were announced. Among such initiatives, Mexican tax authorities issued regulations for FIBRAs E as a new investment vehicle. FIBRAs E are Mexican trusts that issue publicly traded securities in the form of trusts bonds *(certificados bursátiles fiduciarios de inversion en energía e infraestructura or "CBFEs")* listed in the Mexican Stock Exchange.

FIBRAs E's main purpose is the investment in equity interest of Mexican resident companies that own assets and perform exclusive activities in infrastructure and energy projects. The FIBRAs E ownership may be divided into two main groups of security holders: the public and a sponsor (they typically form and contribute to the FIBRA E equity interest of Mexican companies that comply with specific requirements). The FIBRAs E tax regime provides different tax advantages to investors, such as tax transparency for Mexican companies owned by the FIBRA E, tax deferral in transfer of shares, preferred returns to security holders, reduction of withholding taxes and tax amortization of assets, among others.

Foreign-exchange controls

Mexico currently does not have foreign-exchange controls.

Stamp duties

No stamp duty applies in Mexico.

Registration fees

No significant registration fees apply in Mexico.

Morocco

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

The oil and gas industry is regulated in Morocco by Law No. 21-90 as amended and completed by Law No. 27-99, which together form the Hydrocarbon Code. Most of the tax provisions and incentives initially laid down in the Hydrocarbon Code are also now included in the Moroccan Tax Code.

The tax treatment provided for the oil and gas industry in Morocco consists mainly in a combination of corporate income tax (CIT), withholding tax (WHT) on dividends, royalties and interest, branch remittance tax, value-added tax (VAT), registration duties, import duties and business tax.

The common tax rates regarding each tax category that apply to oil and gas industry are as follows:

- CIT progressive rates — 10%–31%
- WHT (dividends) — 15%
- WHT (royalties and interest) — 10%
- VAT — 20% (10% for hydrocarbon products sold locally)
- Registration duties — Fixed/proportional rate depending on the type of transaction
- Import duties — Exempt (subject to certain conditions)
- Branch remittance tax — 15%
- Business tax — Proportional rate depending on the activity
- Royalties due to the Government — 3.5%–10%
- Training duties — Included in the petroleum agreement with the Government

B. Fiscal regime

Corporate income tax

Companies operating in Morocco are subject to CIT on their Moroccan-sourced income. The progressive tax rates are based on the taxable income as follows:

Taxable income in MAD	Rate
Less than or equal to 300,000	10%
Between 300,001 and 1,000,000	20%
More than 1,000,000	31%

These rates apply to any type of income, including that generated from oil and gas activities.

Nevertheless, the Moroccan Tax Code provides a temporary exemption for companies operating in the hydrocarbon industry. A holder or, where applicable, each of the co-holders of any exploitation concession of hydrocarbon deposits is entitled to a total exemption from CIT for a period of 10 consecutive years running from the beginning of regular production. Before the beginning of regular production, the exemption does not apply and thus any tax benefits are taxable in normal conditions.

Beyond the 10 years tax holiday, exporting oil & gas companies are eligible to export tax incentives. The taxable benefit related to export turnover is subject to 17.5% reduced CIT rate.

CIT computation and filing requirements

Taxable income is derived from the difference between the revenues derived during the fiscal year and the deductible expenses incurred for performing the activities that generated the revenue.

An income tax return has to be filed on an annual basis, within three months following the closure of the fiscal year.

The Moroccan Tax Code does not provide any tax rules specific to oil and gas activities. However, the Hydrocarbon Code provides that:

- Taxable revenue corresponds to the value of the portion of hydrocarbons attributable to the concession holder during the considered fiscal year.
- Deductible expenses correspond to the sum of:
  - Expenses and depreciation related to the fiscal year
  - Carried forward losses.

"Expenses" include in particular:

1. Start-up costs for the setup and launch of oil and gas operations
2. The costs of reconnaissance, exploration and development, drilling costs not compensated, and costs incurred in the drilling of wells that do not produce oil or gas in marketable quantities
3. Operating costs
4. Surface rental and concession royalties

Costs referred to in 1 and 2 above may be considered, according to the option selected annually by the holder of the concession, as deductible expenses in the fiscal year during which they are incurred, or they can be depreciated over the period provided by the oil and gas agreement (although the depreciation period must not exceed 10 years).

Tax losses

Standard carryforward rules apply to oil and gas activities. Tax losses can be carried forward for a period of four years. Losses corresponding to depreciation can be carried forward without time limitation.

Consolidation of activities

The Hydrocarbon Code provides that, for the computation of corporate income tax, the holder (or, where applicable, each of the co-holders) of an exploitation concession may consolidate the revenues, expenses and results derived from all exploration permits and all exploitation concessions of which it is a holder.

It should be noted that the Moroccan Tax Code does not provide any other option for the computation of the taxable benefit in cases of multiple activities or licenses at different stages.

Withholding taxes

Dividends

Benefits and dividends remitted by holders of exploitation concessions of Hydrocarbon Deposits are exempt from WHT on dividends as well as branch remittance tax.

Royalties

Royalties paid by Moroccan-based companies to nonresident entities are subject to 10% WHT, unless otherwise provided by double tax treaties concluded with Morocco. Furthermore, domestic tax rules provide a 10% WHT on royalties as well as on payments for services rendered by nonresident entities to Moroccan companies.

Interest

Interest paid to nonresident entities is subject to 10% WHT, unless otherwise provided by double tax treaties concluded with Morocco.

Unconventional oil and gas

- Shale oil is treated as a mining product under the Mining Code of 16 April 1951 and therefore viewed as such from a tax perspective.
- In this regard, mining companies with exporting activities (or those selling their products to other companies that will export such products after their technological treatment) benefit from a reduced CIT rate of 17.5%, instead of the standard progressive rates.
- Shale gas should be treated as an oil product, since it is not expressly excluded from the scope of application of the Hydrocarbon Code (Law no. 27-99). Activities related to shale gas are subject to the provisions that apply to conventional oil and gas.
- No special terms apply to other unconventional oil or unconventional gas.

C. Indirect taxes and duties

VAT

VAT applies to all transactions involving the supply of goods and services performed in Morocco and to the importation of goods and services, including the one-off supply or importation of goods. According to the Moroccan Tax Code, the common applicable tax rate is 20%.

The Moroccan Tax Code provides an exemption from VAT for the holders of a reconnaissance license, exploration permit or exploitation concession, as well as for their contractors and subcontractors, regarding all acquisition operations pertaining to goods or services necessary for their oil and gas activities. Such exemption applies to goods and services purchased locally or imported. It is subject to administrative procedures and prior authorization from the Moroccan tax administration.

The Moroccan Tax Code also provides for a VAT exemption during the first 36 months for equipment used for investment projects, whether acquired locally or imported. The 36-month period starts as from the start of such eligible activity. For companies that are undertaking their own construction project, the 36-month period starts as from the date a construction authorization is received.

Existing companies may also perform investment projects with VAT exemption provided such investments amount to or exceed MMAD 100 and are executed in the frame of a convention with the Moroccan government.

Export is VAT-exempt, with a right to deduct VAT charged by suppliers. However, sales of oil and gas products on the Moroccan market are subject to a VAT rate of 10%.

Registration duties

No specific incentives are provided for oil and gas activities regarding registration duties. They remain applicable for transactions related to such duties (company formation, capital increase, transfer of real estate or other ongoing concerns).

Import duties

Pursuant to the provisions of the Hydrocarbon Code, all equipment, materials and products necessary for reconnaissance, exploration and exploitation operations are exempt from all duties and taxes upon import, provided that the goods are not available on the local market within the limit of 10% (cost, insurance and freight (CIF)) price difference and for the same conditions of quality and delivery.

Business tax

Business tax is a local tax, provided by Law No. 47-06 related to local communal taxation. It is computed on the basis of the rental value of assets and means that are used for the operation of the business. The current rates are 10%–20% and 30%, depending on the nature of the activity.

Holders of exploration permits and exploitation concessions of hydrocarbon deposits are permanently exempted from business tax (but exemption is not provided for holders of reconnaissance licenses).

Royalties due to the Moroccan Government

The holder (or, where applicable, each of the co-holders) of an exploitation concession is required to pay to the Moroccan Government an annual concession royalty on their share in the production of hydrocarbons derived from the concession. The royalty is payable wholly or partly in cash or in kind.

The rates are as follows:

- Onshore, and offshore up to 200 meters' water depth: 10% for oil and 5% for gas:
    - The first 300,000 tonnes of oil and 300 million cubic meters of gas produced from each exploitation concession are exempt.
- Offshore in more than 200 meters' water depth: 7% for oil and 3.5 % for gas:
    - The first 500,000 tonnes of oil and 500 million cubic meters of gas produced from each exploitation concession are exempt.

D. Other

Foreign-exchange controls

Foreign holders of exploitation concessions may maintain abroad the proceeds of their sales of hydrocarbons performed outside Morocco. The exit of hydrocarbons from Morocco has to be performed in compliance with Moroccan regulations. Periodic information in this regard has also to be provided to the Moroccan exchange office.

Notwithstanding the foregoing, foreign holders of exploitation concessions are required to repatriate to Morocco necessary funds in order to cover local expenses and their financial and tax obligations, as well as the proceeds from sales of hydrocarbons in the domestic market.

Moroccan legal entities holding an exploitation concessions are required to repatriate to Morocco the proceeds of their sales of hydrocarbons performed outside Morocco, unless otherwise authorized by the Moroccan exchange authorities, in particular in order to allow them to cover necessary expenses abroad within the framework of their oil and gas activities abroad.

It should be noted that Moroccan foreign-exchange regulations guarantee the right of foreign license holders to repatriate benefits and dividends derived from their activities in Morocco, as well as the transfer price upon the sale of their activities. The transfer guarantee covers:

- Any initial capital contribution made in foreign currency
- Capital gains derived from the transfer

Government partnerships

The Moroccan Government owns as a matter of course a participation in any permit for research, but the proportion owned cannot exceed 25%.

Mozambique

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Tax regime applied to this country

■ **Concession** ■ Royalties ☐ Profit-based special taxes ■ Corporate income tax	■ **Production sharing contracts** ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies to the petroleum industry in Mozambique consists of a combination of corporate income tax (CIT), royalty-based taxation and production sharing. The main elements are as follows:

- CIT rate — 32%
- Royalties — from 6% to 10%
- Bonuses — applicable under the public-private partnerships law, in which a signature bonus between 0.5% and 5% of fair value of assets applies; other bonuses might be paid, but they are not enshrined in law
- Production sharing — based on R-factor
- Withholding taxes (WHT) — applied to dividends
- Resource rent tax — none
- Capital allowances — see Section C
- Investment incentives — exemption from customs duties on the importation of equipment, machinery and tools

B. Fiscal regime

Concession contracts

In Mozambique, oil operations are engaged based on concession contracts resulting from public tender, which can be for reconnaissance, research and production, or the construction and operation of pipelines. Such contracts determine, among other things, the terms and conditions of state participation in the oil operations.

Mozambican law states that no tax benefits apply to oil operations other than the ones indicated in Section D. This means that the concession contracts effectively formalize only what is already foreseen in the law and determine which of these terms and conditions apply in each case. Contract terms and conditions must, of course, be determined or agreed within the legal limits established.

It is important to note that, in 2010, new legislation on public-private partnerships (PPPs) was introduced, which provides between 5% and 20% of local participation. As well as that local participation, the new law introduced a signature bonus and an annual concession fee between 2% and 5% of the fair value of the assets made available by the Government.

Revised legislation dealing with the specific taxation regime applicable for petroleum operations was approved in 2014 effective from January 2015 and explicitly covers ring-fencing, cost definition, depreciation rates, capital gains taxation and the mechanisms for production sharing with the state. This law does not apply to concessions that were in place at the time of its entry into force.

Corporate income tax

Under the Corporate Income Tax Code, companies and similar corporate entities (including oil and gas companies) are liable for CIT on income generated in Mozambique and abroad (i.e., their worldwide income). The standard rate that applies for CIT is currently 32%.

Companies that are tax resident in Mozambique or that are nonresident but have a permanent establishment (PE) in Mozambique and a turnover of more than MZN2.5 million (approximately US$55,000) are required to keep organized accounts for tax purposes.

The financial year is normally a calendar year, but taxpayers can apply for a different financial year if it is justified and when more than 50% of share capital is held by entities adopting a different financial year (e.g., for consolidation purposes). Once granted, that arrangement must be maintained for a minimum of five years.

Transfer pricing

Transfer pricing regulations were introduced in 2018 according to which taxpayers have to maintain transfer pricing documentation and report transactions with related entities with submission of tax return. Transactions between entities with special relations must be undertaken on an arm's-length basis. Special relations exist between two or more entities in situations where one has the power to directly or indirectly exercise significant influence on the management decisions of the other.

Thin capitalization

The thin capitalization ratio is two to one, irrespective of the existence of special relations.

Dividends

Dividends distributed by Mozambican taxpayers are subject to a 20% WHT.

Dividends distributed by a resident company to resident corporate shareholders are not subject to WHT, provided that the beneficiary holds at least 20% of the share capital and the shares have been held for a minimum of two years. Dividends paid in these circumstances do not form part of the taxable income of the shareholder.

Losses can be carried forward for five years.

Ring fencing

There is ring fencing per concession. However, if the taxpayer benefits from a partial exemption or a reduction in the tax rate, the losses of the activity that benefits from such incentives cannot be offset against the losses of the remaining activities.

Mozambique does not have tax consolidation rules.

Tax-deductible costs

Costs or losses confirmed as indispensable for the generation of profits or gains, or costs or losses relating to the maintenance of the production source, are tax-deductible. Under the tax regime applicable to oil and gas operations, these costs or losses include:

- Functioning, assistance, maintenance and repair of production wells and injection and all field infrastructure completed during the phase of development and production

- Planning, production, control, measuring and petroleum flow tests, as well as gathering, treating and storing the petroleum and transporting it to the point of delivery
- Professional training of Mozambique employees
- Contributions in cash to the demobilization fund and effective costs with demobilization
- General administration costs with certain limitations in relation to total costs incurred
- Depreciation
- Provisions
- Capital losses
- Any other costs or losses that fall within the definition of costs given in the first sentence of this subsection

The Mozambican tax system also allows for the following deductions:

- Economic double taxation of distributed profits
- Credit for foreign tax paid (international double taxation)
- Tax benefits
- Provisional payments

Oil production tax (royalty)

An oil (including natural gas) production tax (equivalent to a royalty) is due on the value of the oil (gas) produced in Mozambique at the development and production site. The rate is 10% for oil and 6% for natural gas. The tax rate is reduced by 50% when production is destined for the development of the local industry. The determination of the amount payable varies according to the purchaser as follows:

- For sales to nonrelated entities, the payable amount is determined based on the average sales price charged per barrel at the point of delivery, assessed with reference to free-on-board (FOB) prices.
- For sales to third parties under conditions different from FOB, an FOB price shall be applied calculated in the form of net-back, established by the deduction to the agreed price, of the effective and direct costs incurred by the concessionaire with compliance of the respective sale agreements.
- For sales to entities where the concessionaire is a shareholder, the price is agreed between the Ministry of Mineral Resources and Energy, the Ministry of Finance and the concessionaire.

The tax becomes payable at the time the petroleum produced enters the measuring station or, in cases of payment in kind, at the time the petroleum is delivered to the government.

Oil production tax is not considered a cost for CIT purposes.

Branch remittance tax

There is no branch remittance tax in Mozambique.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

Cost recovery

Cost recovery is limited to 60% per year of the disposable oil, and excludes interest and other financial costs.

Production sharing

Profit oil is based on R-factor.

Fiscal stability

Fiscal stability may be negotiated for a period of 10 years, as from the date of commencement of commercial production, without affecting the feasibility and profitability assumptions and conditioned to proven investment equivalent to US$100 million. This period may be extended up to the end of the initial concession period, by means of the payment of an additional 2% to the oil production tax (royalty), from the 11th year of production.

C. Capital allowances

Provisions created by companies involved in the petroleum-extracting industry related to the reconstruction of wells can be deducted for tax purposes.

See the appropriate subsection in Section B above for more detail on what is allowable as a tax-deductible expense.

Expenses are depreciated on a straight-line basis at the following rates, unless the period of useful life in a petroleum operation approved by the development plan is shorter; in such cases, the rate is one divided by the number of years expected for the petroleum operations:

- Expenses with exploration and appraisal — 100%
- Expenses with development — 25%
- Petroleum production assets — 20%
- Acquisition of petroleum rights — 10%
- Other assets — 10%

Depreciation commences in the year in which the expense is incurred, or the year in which production commences, whichever occurs later.

D. Incentives

Import duties

One particular incentive needs to be mentioned:

- Equipment destined to be used in oil operations classified in Class K of the customs classification list, including explosives, detonators, igniting tubes, machines and explosives-blowing devices, are exempt from import duties.

E. Withholding taxes

Withholding is required for both corporate and individual income tax.

The following income generated by nonresident entities in Mozambique is subject to a 20% WHT:

- Income generated from intellectual or industrial property (e.g., royalties), and the supply of information relating to experience acquired in the industrial, commercial or scientific sectors
- Income derived from the use or concession for use of agricultural, industrial, commercial or scientific equipment
- Income from technical assistance, management services and directors' fees
- Income derived from the application of capital (e.g., dividends and interest) and immovable property income

Telecommunications and international transportation services, and related assembly and installation, as well as those relevant to aircraft maintenance and freight performed by nonresident entities, are subject to a 10% WHT.

The special tax regime for petroleum operations provides for a reduced tax rate of 10% for services related to the concession agreement, rendered by nonresident entities.

F. Financing considerations

Thin capitalization

In terms of the special tax regime, thin capitalization rules apply if a taxpayer's debt related to an entity — an entity that is not a resident in Mozambique — is excessive with regard to the equity of the taxpayer. Any interest paid as well as any other financial costs in respect of the excess is not deductible for the purposes of determining taxable income.

An excessive indebtedness is considered to exist if the value of the debt in respect of each of the entities involved, with reference to any date in the taxation period, is more than twice the value of the corresponding percentage held in the equity of the taxpayer.

Effective from 1 January 2014, a new provision has been introduced that limits the deduction of interest charged on shareholder loans to the amount corresponding to the Maputo Inter-Bank Offered Rate (MAIBOR) rate of reference for 12 months plus two percentage points.

G. Transactions

Asset disposals

The transfer of immovable property is subject to real estate tax at a rate of 2%.

Moreover, any gains or losses arising from the disposal of the fixed assets of a company, and the gains and losses derived from the disposal of fixed assets permanently used for a purpose not related to oil production activity, are considered to be capital gains or losses. The amount of such capital gains or losses is determined with reference to the difference between the realization value (proceeds) and the base cost, which is calculated in accordance with Mozambican tax laws.

Gains obtained by nonresidents from direct or indirect transfer, gratuitous or for a consideration of petroleum rights are considered to be gains resulting from immovable property and are subject to taxation in Mozambique, at the rate of 32%. In relation to nonresidents, only 50% of the gain is considered for taxation.

Nonresidents must appoint a tax representative in Mozambique to comply with their tax obligations. The purchaser or the holder of the petroleum rights has joint and several responsibility for the payment of the tax in case the seller is a nonresident entity without a PE in Mozambique.

In the case of resident taxpayers, the gain is included in the taxable income of the respective financial year and is taxed at a general rate of 32%.

Farm-in and farmout

In a farm-in transaction, the interest acquired is considered to be a depreciating asset, which is depreciated at the rate of 10%.

In a farmout transaction, a gain resulting from the transaction represents a capital gain that is included in the taxable income for the relevant financial year. For nonresident entities, 50% of the capital gain is taxed for CIT at a rate of 32%. A nonresident entity must appoint a tax representative to comply with its tax obligations and the purchaser or holder of the petroleum rights has joint and several responsibility for the payment of the tax.

Transfer of shares

Gains resulting from a transfer of shares are considered as resulting from the transfer of immovable property and are taxed as:

- Extraordinary income if the shareholder is a company, the amount being included in the taxable income in the relevant financial year
- Capital gains income if the shareholder is an individual, the amount being included in the individual's total taxable income for the relevant calendar year
- A capital gain for nonresident shareholders; tax must be paid within 30 days after the conclusion of the transaction

A nonresident shareholder must appoint a tax representative in Mozambique to comply with its tax obligations arising from the transfer of shares and the purchaser or holder of the petroleum rights has joint and several responsibility for the payment of the tax. The tax is levied at 32% on 50% of the gain for nonresidents.

VAT

VAT is levied on the sale of goods and the rendering of services, and on imports, at a rate of 17%.

Exports are exempt from VAT (and customs duties).

Stamp duty

Stamp duty is levied on all documents, books and acts listed in a table approved by the Council of Ministers.

Registration fees

Holders of the right to undertake oil operations are subject to payment of a registration fee in the following cases:

- Application for granting oil operation rights: approximately US$20,000
- Renewal of a concession contract: approximately US$5,000
- Review of a development plan, except in cases of pipeline construction and operation contracts: approximately US$20,000
- Authorization to commence oil operations: approximately US$5,000
- Approval of a demobilization plan: approximately US$10,000

H. Other

Social responsibility

A percentage of the income generated by an oil activity is allocated to the community in the area where the oil project is located. The percentage payable is established by the state budget law, which takes into account estimated oil production income for the period.

Exchange control regulations

Mozambique has strict exchange control regulations. Except for payments for services and the importation of goods, which qualify as current transactions, most payments (such as repayments of loans, repatriation of capital invested and remittance of profits or dividends) are subject to the prior approval of the Central Bank of Mozambique.

Service agreements require registration with the Central Bank. Depending on the respective conditions, loan agreements require the prior approval of the Central Bank. For shareholder loans provided by nonresident entities specifically, the Central Bank under its discretionary powers has determined a debt-to-equity ratio of three to one. Notwithstanding the foregoing, shareholder loan agreements which maturity is minimum three years, with interest rate lower than the base lending rate for the respective currency and up to the amount of US$5 million are approved.

Commercial banks require proof of payment of the relevant taxes prior to granting approval for overseas payments.

Oil and gas companies are normally authorized to open and keep offshore bank accounts for specific purposes. Notwithstanding, during the production phase, all payments of services and goods to resident and nonresident entities shall be made via the Mozambican banks.

Myanmar

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Tax regime applied to this country	
☐ **Concession** ☐ Royalties ☐ Profit-based special taxes ☐ Corporate income tax	■ **Production sharing contracts** ☐ **Service contract**

A. At a glance

Companies are required to sign production sharing contracts (PSCs) with Myanmar Oil and Gas Enterprise (MOGE), which is a 100% state-owned enterprise under the Ministry of Electricity and Energy (MOEE), in order to undertake petroleum exploration and production activities in Myanmar. As the investment in the oil and gas business is capital-intensive, several foreign oil and gas companies sometimes jointly invest in the PSC, and the majority stakeholder acts as the "operator."

The Myanmar Investment Commission (MIC) will handle each application for foreign investment under the Myanmar Investment Law (MIL), and the MIC will approve the PSC under the MIL upon the issuance of an MIC permit.

In relation to the fiscal and other financial elements that apply for a company involved in oil and gas exploration or production in Myanmar, the following are relevant:

- Signature bonuses apply.
- Production bonuses apply.
- Rentals do not occur.
- Royalties are at the rate of 12.5%.
- Production bonuses are paid at progressive rates.
- Income tax is charged at 25%.
- Training/R&D payments apply.
- Investment incentives are available.

B. Fiscal regime

The fiscal regime that applies to the petroleum industry in Myanmar centers on the PSC, the Myanmar Investment Law (MIL), the Myanmar Companies Act (MCA), the Myanmar Income Tax Law (MITL), the Myanmar Commercial Tax Law (MCTL) and Myanmar Special Commodities Tax Law (MSCTL). Moreover, the PSC has the full force of law.

Rentals

No rentals or other acreage fees are currently envisaged in Myanmar.

Bonuses

Signature bonuses and production bonuses apply. The rates are based on the standard PSC. Neither signature bonuses nor production bonuses are cost-recoverable.

Royalties

Royalties apply at a 12.5% rate of the value of production. The same rate applies for both oil and natural gas. Royalties are not cost-recoverable.

Cost recovery

The cost recovery ceiling varies for oil and for natural gas, as well as for a project's logistics (whether onshore, shallow water or deepwater activity). Exploration costs are recoverable from the start of production. Development costs and other capital costs are recovered at the percentage agreed in the PSC from the start of production. Unrecovered costs can be carried forward in an unlimited fashion.

Profit production sharing

Production net of royalties and cost petroleum is shared between the PSC parties, based on a progressive sliding scale linked to average daily production levels from the production area. The rates are distinguished for oil and for natural gas.

Training contribution

A training contribution is payable annually by concession holders. Different annual payments apply during the exploration and production periods. Any training contribution made is cost-recoverable.

R&D contribution

Contractors should annually pay a contribution to a Research and Development (R&D) Fund from the start of production. The contribution equals 0.5% of contractor's share of profit production.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

Accounting period

The Myanmar fiscal accounting period was previously April to March of each year. However, Myanmar's fiscal year will be changed from October to September. Therefore, there will be a six-month budget year from April 2018 to September 2018. Thereafter, the fiscal year will be changed to October to September; companies may be given a choice of establishing their own fiscal year. However, fiscal year law is not yet enacted. Myanmar-incorporated companies, or branches of foreign companies, have a duty to file income tax returns related the Myanmar fiscal year. A three- to seven-year tax holiday period begins from the date of commercial operation and, after that tax holiday period has ended, the joint venture (JV) company must begin to pay the tax due.

Income tax

PSC contractors are subject to corporate income tax (CIT) at the rate of 25% on net income, unless specifically exempt under a tax holiday period.

According to the Union Taxation Law 2017, the branch of the foreign company will be subject to the same 25% CIT rate that Myanmar local companies are subject to.

Consolidation of tax results

Each PSC is subject to tax on its own operating results; no tax consolidation is allowed for different PSCs. However, in the case where a PSC includes several oil and gas blocks, the operating results of the different blocks are to be consolidated under the PSC for tax purposes.

Determination of profit

As stated above, corporate income tax at 25% is applicable on the net income of the JV. The selling price of oil and gas, on which income is calculated, is determined by the JV company. For oil and gas supplied to the Myanmar market through an oil and gas pipeline, the selling price is set at 90% of the market value.

Deductible expenses of the JV company for the oil and gas business in Myanmar are as follows:

- Petroleum costs
- Labor and labor-related costs
- Assigned personnel
- Materials
- Inventories
- Transportation and employee relocation costs
- Services
- Damages and losses to material, and facilities insurance claims
- Legal expenses
- Charges and fees
- Offices, camps and miscellaneous expenses
- Credits under contract
- Various other expenditures

C. Incentives

Tax holiday

Myanmar Investment Law (MIL) issued on 18 October 2016 new classified tax exemption and relief for the following regions: Zone 1, less developed regions, may grant income tax exemption for a period of seven years; Zone 2, moderately developed regions, may grant income tax exemption for a period of five years; and Zone 3, adequately developed regions, may grant income tax exemption for three years.

Onshore and offshore oil and gas activities are excluded from the classified Zones above, and tax exemption is to be granted by MIC with the recommendation of the Ministry of Electricity and Energy.

Tax losses

Tax losses can be carried forward for three years under the normal Corporate Income Tax Act.

D. Withholding taxes

Dividends and profit remittance tax

Dividend distribution and profit remittance are not subject to tax of any kind in Myanmar.

Other types of income

When the payment of income is made by a Myanmar entity, such as the branch of a JV company or a PSC operator, to Myanmar citizens and/or resident foreigners (such as local distributors or nonresident foreigners), the company in Myanmar is required to withhold tax at various rates depending on the type of income and payee. The withholding tax rates applying in Myanmar are set out in the table below.

Types of income	Paid to Myanmar citizens and resident counterparties	Paid to nonresident counterparties
Interest	–	15%[1][2]
Royalties for the use of licenses, trademarks, patent rights, etc.	10%	15%[1][2]

Types of income	Paid to Myanmar citizens and resident counterparties	Paid to nonresident counterparties
Payment for purchase of goods within the country, work performed or supply of services and hiring under a tender, contract, quotation or other modes by foreign companies, foreign enterprises and organizations and local companies.	2%(4)	2.5%(1)(3)(4)

Notes:

(1) Payments to nonresidents are treated as final tax to such nonresidents. However, the withholding tax deducted from a branch office of a nonresident foreigner established in Myanmar shall be available for offset against the tax due per final tax assessment as the branch office is being assessed on its local business income under the MITL.

(2) If a payment is made to a treaty country, the relevant tax treaty needs to be considered to find out whether reduction/exemption is available.

(3) If a payment is made to a treaty country, exemption may be available under the relevant tax treaty if there is no permanent establishment in Myanmar.

(4) Payment for goods or services in Myanmar that is (i) not exceeding MMK1,500,000 (approximately US$1,100) per transaction made by the companies under the tax assessment of the Self-Assessment System (SAS) or (ii) not exceeding MMK500,000 (approximately US$370) per transaction made by the companies not under the SAS, is not subject to withholding tax.

E. Financing considerations

The legally permitted debt-to-equity ratio of the JV is within the maximum range of 3:1 and 4:1. Generally, interest can be a deductible expense, from the date of commercial operations, for the purposes of a JV company's income tax calculation.

F. Transactions

Selling shares in a JV company

If any shareholder in a JV company disposes of or sells its shares to another party and a capital gain is realized, the shareholder is required to pay capital gains tax (CGT) to the Myanmar Internal Revenue Department (MIRD) at the rate of 40% to 50%, the rate depending on the amount of share capital amount being sold.

G. Indirect taxes

Import duties

Generally, oil and gas companies incorporated under an MIC permit do not need to pay import duties during the construction phase. In the case of a PSC that is also incorporated under an MIC permit, it is exempt from import duties on the importation of goods and equipment during the exploration and production period.

Commercial tax

If the total sales proceed or service revenue exceeds MMK50 million (around US$37,000) within one financial year, commercial tax (CT) at the rate of 5% applies for domestic sale and importation of crude oil. A 5% CT rate applies for domestic sale of imported natural gas and for trading (purchase and sale locally) of natural gas. A 5% CT rate applies on the landed cost, including a Special Commodities Tax, for the importation of natural gas; a 5% CT rate applies also on the sale, including the Special Commodities Tax, of natural gas produced in Myanmar. Rates of 5% and 0% apply on exports of crude oil and natural gas, respectively. The CT exemption threshold of MMK50 million above is not relevant to export sales. The CT on exports could be exempted under the MIC permit. Transportation service for the export of crude oil and gas will be through cross-border oil and gas pipelines, and the levy of commercial tax at 5% will be applicable beginning in fiscal year 2016–2017. According to Rights and Obligations signed with MOGE, if commercial tax is applicable, MOGE is to pay commercial tax for and on behalf of oil and gas pipeline companies.

Special Commodities Tax

The special commodities that have been previously taxed under the Commercial Tax Law are now taxed according to the newly enacted Special Commodities Tax Law, and the special commodities will be taxed under this law only. Special commodities tax at the rate of 8% applies for the importation of natural gas, sales of natural gas produced in the country and export of natural gas.

Export duties

Companies in the oil and gas business are exempt from export duties.

Stamp duties

A PSC is subject to a maximum stamp duty of MMK150,000.

Domestic supply obligations

Myanmar imposes an obligation on oil and gas production companies to supply a certain percentage of production domestically, with a 10% discount to the market price. Such an obligation is capped at a certain percentage of a contractor's production profit.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies to the petroleum industry in Namibia consists of a combination of petroleum income tax (PIT) under the Petroleum (Taxation) Act No. 3 of 1991 (the PTA), income tax on certain disposals under the Income Tax Act No. 24 of 1981 (the Income Tax Act), the administrative provisions as contained in the Income Tax Act and royalties levied on sales under the Petroleum (Exploration and Production) Act No. 2 of 1991 (the Petroleum Act).

The main elements of taxation and allowances applicable in this context in Namibia are as follows:

- Production sharing — No applicant is compelled to offer a production sharing contract (PSC) to the National Petroleum Corporation of Namibia (NAMCOR) or to share in a license; thus, no applicant is penalized for not making an offer to NAMCOR. However, NAMCOR can participate in licenses if negotiated initially as part of the contract and if NAMCOR decides to accept the invitation to participate. NAMCOR's interests are carried during the exploration phase, but it contributes fully from the development phase onward.
- A corporate income tax rate of 35% and an additional profits tax (APT) are levied on the after-tax net cash flows from petroleum operations.
- The corporate income tax on disposals of licenses and/or rights and shares in companies that directly or indirectly own such rights is 32%.
- Royalties are 5% of gross revenues.[1] The value of the crude oil for royalty and tax purposes is the market value.
- Capital allowances – E[2]
- Investment incentives – L[3]

1 *A rate of 12.5% applies to exploration licenses issued prior to the commencement of the Petroleum Laws Amendment Act of 1998, effective from 1 April 1999.*

2 *E: Write-off of accumulated exploration costs in the year of first production (unless transferred to another field under circumstances prescribed in the PTA) and one-third of development expenditure. The rest of the development expenditure is written off in equal installments in the two subsequent years.*

3 *L: Assessed losses can be carried forward indefinitely.*

B. Fiscal regime

The fiscal regime that applies in Namibia to the petroleum industry consists of a combination of PIT under the PTA, income tax on certain disposals under the Income Tax Act, the administrative provisions as contained in the Income Tax Act and royalties levied on sales under the Petroleum Act.

Corporate tax

Corporate income tax on petroleum operations is levied under the PTA and not under the Income Tax Act. Under Section 5 of the PTA, taxable income received by a person from a license area within the Namibian territorial sea is taxed at a rate of 35%, levied in respect of each license area. License areas are taxed separately even if the taxpayer has been granted the right of exploration in different license areas.

Effective from 30 December 2015, the following items must be included in gross income and taxed at the corporate tax rate of 32%: amounts received as consideration on the sale, donation expropriation, cession, grant or other alienation or transfer of ownership of a petroleum license; a right to mine petroleum; and shares held directly or indirectly in a company that holds such a license or right to mine. Provision is made for the deduction of costs of the acquisition of the license or right and, in the case of petroleum licenses and rights, costs of improving the licenses and rights.

Additional profits tax (APT)

APT is levied on the after-tax net cash flows from petroleum operations, determined by deducting the exploration and development expenditure and the PIT from gross income. The first tranche of APT is payable only if operations in a license area earn an after-tax rate of return of at least 15%. If operations in the license area earn an after-tax rate of return of 20% to 25%, the second and third tranches of APT become payable.

Gross income

Under Section 7 of the PTA, "gross income" is the total amount, in cash or otherwise, received by or accrued to, or in favor of, a person from a license area in connection with exploration operations, development operations or production operations, excluding amounts of a capital nature, but specifically including the following amounts, whether they are capital in nature or not:

- Amounts received or accrued in or outside Namibia, related to petroleum produced, saved or delivered and sold in an arm's-length sale
- The market value of petroleum produced, saved or delivered and sold in a non-arm's-length sale
- The market value of petroleum produced and saved in the license area and appropriated for refining purposes
- 50% of the market value of petroleum produced or saved, and which was not lost in any manner, not disposed of or acquired for refining purposes, or disposed of but not delivered
- Insurance proceeds in respect of any loss of petroleum produced or saved or any income that would have been included in gross income had the loss not occurred
- Any income received or accrued to the person from the license area and deemed to form part of gross income under Section 12 of the PTA
- Any income received or accrued to a person from the sale of petroleum information in relation to such license area
- Any other income received or accrued to a person under a condition of the license

Any amounts received or accrued to the license holder prior to the year of production in respect of these items are carried forward to the year of first production and are included in gross income in that year.

The share of petroleum in crude form produced and saved by a person in a license area is a contractually proportionate amount under any agreement if there are joint holders of a license. If no agreement was entered into, the petroleum is divided equally. If a person is the sole holder of the license area, all the petroleum produced and saved accrues to that person.

Deductible expenditure

Under Section 8 of the PTA, allowable deductions are expenses actually incurred, in respect of the particular license area, in the production of gross income. Other specific deductions, apart from the general deduction, include:

- Repairs and maintenance of premises occupied for exploration, development and production purposes and machinery used for these purposes
- Charges for rent of land or buildings occupied for exploration, development and production purposes
- Contributions to a fund or scheme approved by the permanent secretary in respect of a person employed in the production operations
- Interest on borrowings relating to exploration, development and production in respect of a license area
- Royalties paid under the Petroleum Act
- Education and training of Namibian citizens and educational or scientific materials and equipment
- Wages and salaries in connection with production operations in the license area
- Consumables in connection with production operations in the license area
- The right to use any plant, machinery or equipment in connection with exploration, development and production operations
- Customs duties in respect of plant, machinery or equipment imported in connection with production operations
- General administrative and management costs in connection with production operations
- Restoration costs after exploration operations cease
- Debts proven to be bad, provided that the amount is included in the income in the current tax year or was included in income but not deducted in any previous tax year
- Amounts included in the immediately preceding tax year under Section 7(1)(d) (i.e., amounts included in respect of petroleum produced or saved but not lost, not disposed of or acquired for refining purposes, and not delivered)
- The amount determined in accordance with Section 68B(1)(a) of the Petroleum Act and deposited with reference to the trust fund and decommissioning shortfalls as referred to in Section 68D(3)(a)

Under Section 13 of the PTA, deductions are not allowed in respect of the following:

- Expenditures incurred in respect of improvements not specifically allowed under Section 8 of the PTA
- Rental or costs of acquisition of land and buildings not occupied for the purposes of production in the license area
- Contributions to a fund or scheme not approved by the permanent secretary
- Expenditures incurred in obtaining a loan or other debt not specifically allowed under Section 8 of the PTA
- Capital withdrawn or any sum used as capital
- Any royalty not levied under the Petroleum Act
- Expenses related to the purchase of an interest in petroleum
- Any tax payable within or outside of Namibia

Section 14 of the PTA provides that deductions for rent incurred outside Namibia in respect of the general administration and management of the business, as well as capital expenditures directly related to the general management and administration of development operations, are only allowed to the extent that provision is made in the production license, or to the extent that the permanent secretary considers it "just and reasonable."

Section 17 of the PTA provides that excessive expenditures incurred under an arrangement between associated persons may be disallowed by the permanent secretary.

Each license area is assessed separately, and losses incurred in one license area cannot be offset against profits earned in another, but losses resulting from allowable deductions are deductible as an allowable loss against the gross income from the license area in the following year. However, exploration expenditures from a license area without gross income may be deducted from license areas with gross income from production. The license holder is not required to have taxable income after deducting its expenses. Nor is it a requirement that the license area where the exploration expenditure arose has to be in production before the license holder is able to deduct exploration expenditures incurred in respect of a license area without gross income from a license area with gross income.

Section 9 of the PTA provides for an allowance for exploration expenditures and development expenditures incurred in the years before production commences. This allowance is discussed in more detail in Section C.

Capital gains tax

Namibia does not generally impose capital gains tax (CGT).

Under the definition of "gross income" in Section 7 of the PTA, the gross income is the total amount, in cash or otherwise, received by or accrued to, or in favor of, such person from a license area in connection with exploration operations, development operations or production operations, excluding amounts of a capital nature. However, certain amounts specifically listed (as detailed above) are included in the gross income, whether or not they are of a capital nature.

In addition, if the license holder receives an amount from the disposal, loss or destruction of any asset used in exploration and development operations, capital expenditure is allowed only to the extent that it does not exceed the amount received (see Section G for further information).

Section 12 effectively provides that capital gains arising on the disposal of assets are included in gross income and are taxable in the hands of the license holder.

These provisions, however, apply to disposals only *after* production has commenced, and any gain realized on a disposal prior to production will be taxable only when production commences. If production never commences, or the participant sells its entire interest prior to production, there will not be any tax on the gain. Furthermore, although a gain on the sale of assets will attract tax after production has commenced, any amount attributable to the petroleum license itself will not attract tax under the PTA

From 30 December 2015, any amount attributable to the petroleum license or right will be taxable at the corporate tax rate of 32% in terms of the Income Tax Act. Costs incurred in acquiring the petroleum license as well as costs incurred in improving such license or right may be deducted in calculating the amount subject to tax.

Amounts received on the disposal of shares in a company that directly or indirectly owns a petroleum license or right are likewise taxable from 30 December 2015.

Functional currency

Books of account must be kept in Namibian dollars (NAD). Even though taxpayers may invoice or be invoiced in other currencies, the invoices must be converted to Namibian dollars for value-added tax (VAT) purposes at the ruling exchange rates of those transactions.

There are no special provisions in the PTA that deal with the exchange rates to be used for PIT purposes. However, under generally accepted accounting principles, income and expenses are converted to Namibian dollars when the transactions take place.

Transfer pricing

As the PTA specifically provides that no tax may be levied under the Income Tax Act, the transfer pricing provisions contained in that Act do not apply.

However, the PTA contains provisions that are similar in scope to the transfer pricing provisions in the Income Tax Act in respect of the determination of gross income. Under Section 7 of the PTA, a sale of petroleum is considered to be at arm's length if the price provided for in the sale agreement is the only consideration, the sale is not affected by any relationships other than the sale relationship created in the sale agreement, and the seller or any person associated with the seller has no interest in the subsequent resale of the petroleum. The market value of the petroleum produced and saved in the license area is determined in accordance with any of the terms and conditions of the license of that license area or, in the absence of such an agreement, an amount determined by the permanent secretary with regard to the amount that would be obtained between a willing buyer and a willing seller acting in good faith.

Further, Section 17 of the PTA provides that excessive expenditures incurred under an arrangement between associated persons may be disallowed.

Dividends

Petroleum companies are exempt from withholding taxes on dividends, or the so-called nonresident shareholders' tax (NRST).

Interest

Withholding tax on interest paid to nonresidents is effective from 30 December 2015 and is imposed at a rate of 10%.

Royalties

Royalties are payable at a rate of 5% of gross revenues under the Petroleum Act. The value of the crude oil for royalty and tax purposes is the market value.

Royalties are generally payable quarterly. If the payer fails to remit payment, the Ministry of Mines and Energy may prohibit the removal of petroleum from the production area and any other dealings in respect of the petroleum.

Under the PTA, the royalty paid is deductible in the determination of the taxable income of the license holder.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Capital allowances are divided according to exploration expenditure and a development expenditure, both of which are defined in great detail in Section 1 of the PTA. However, no separate definition for production expenditure is provided.

"Exploration expenditure" is expenditure actually incurred, whether directly or indirectly, in, or in connection with, carrying out exploration operations in, or in connection with, a license area, including, among other things, expenditures actually incurred in respect of:

- The acquisition of machinery, implements, utensils and other articles employed for purposes of such operations
- Labor, fuel, haulage, supplies, materials and repairs in connection with a survey or study, excluding drilling for appraisal purposes
- Contributions to a fund or scheme, approved by the permanent secretary, in respect of any person employed in, or in connection with, exploration operations
- The advancement of training and education of Namibian citizens at institutions approved by the permanent secretary
- Charges, fees or rent for, or in respect of, land or buildings occupied for purposes of carrying out exploration operations

- The general administration and management directly connected with exploration operations
- The restoration of a license area, or any part thereof, after cessation of exploration operations
- Customs duties in respect of the importation of plant, equipment, spare parts, materials, supplies or consumable items for use in, or in connection with, exploration operations in such license areas

Under Section 1 of the PTA, "development expenditures" are actually incurred in, or in connection with, carrying out development operations in, or in connection with, a license area, including, among other things, expenditures actually incurred in respect of:

- The acquisition of machinery, implements, utensils and other articles used for purposes of such operations
- The acquisition of furniture, tools and equipment used in offices and accommodation and in warehouses, export terminals, harbors, piers, marine vessels, vehicles, motorized rolling equipment, aircraft, fire and security stations, water and sewerage plants, and power plants
- Labor, fuel, haulage, supplies, materials and repairs in connection with drilling, laying, installation and construction
- Contributions to a fund or scheme, approved by the permanent secretary, in respect of any person employed in, or in connection with, development operations
- The advancement of training and education of Namibian citizens at institutions approved by the permanent secretary
- Charges, fees or rent for, or in respect of, land or buildings occupied for purposes of carrying out development operations
- General administration and management directly connected with development operations
- The restoration of such license area, or any part thereof, after cessation of development operations
- Customs duty in respect of the importation of plant, machinery, equipment, spare parts, materials, supplies or consumable items for use in, or in connection with, development operations in such license areas

Section 9 of the PTA provides an allowance for the exploration expenditure and development expenditure incurred in the years before production commences. These allowances can be carried forward to that year in the same way as income is carried forward. In the year when production commences, all the exploration expenditures can be deducted (unless they have already been transferred to another license area that has gross income from production), as well as one-third of the development expenditure. The rest of the development expenditures can be deducted in the two subsequent years in equal installments.

Section 10 of the PTA provides that exploration expenditures incurred after the year when production commenced are immediately deductible, while all other capital expenditures may be deducted in three equal installments commencing in the year they were incurred.

No allowance is granted for any costs attributable to a petroleum license itself. However, in terms of the amendments to the Income Tax Act, effective from 30 December 2015, such costs are deductible in calculating the taxable amount on the sale or other disposal of a petroleum license.

D. Incentives

Exploration expenditure

Accumulated exploration expenditures are deductible in full in the first year of production (unless they have already been transferred to another license area that has gross income from production). Exploration expenditures incurred after the year when production commences are immediately deductible.

Development expenditure

Accumulated development expenditures are deductible in three equal installments commencing in the first year of production.

Losses

Losses resulting from allowable deductions may be deducted as an allowable loss against the gross income from the license area in the next year. Losses may be carried forward without limitation. However, losses incurred in one license area may not be offset against income from another license area or other operations.

E. Withholding taxes

Dividends

Petroleum companies are exempt from the withholding tax (WHT) on dividends, or the NRST on any dividend distributed out of taxable income from mining for natural oil or gas in Namibia.

Services

Payments for management, consultancy or technical services (as defined) to nonresidents (as defined) are subject to WHT at a rate of 10% on the gross amount of the service fees from 30 December 2015. The WHT deducted must be paid by the Namibian company or branch, which pays the tax on behalf of the nonresident, unless the provisions of a double taxation agreement (DTA) provide relief.

Royalties

Royalty WHT applies to payments to nonresidents for the use or right to use defined intellectual property in Namibia. The scope of the withholding tax on royalties has also been extended with effect from 30 December 2015 to include payments for the use of commercial, industrial or scientific equipment to a nonresident. The rate of WHT on royalties is 10% with effect from 30 December 2015 and may be reduced by the provisions of a DTA.

In terms of the amendments to the Income Tax Act, the rate is no longer determined by applying the regular corporate tax rate to a deemed taxable profit of 30% of gross royalties, and a flat rate of 10% applies.

Export levy

An export levy of 1.5% applies to free-on-board (FOB) value of exported crude oil and unrefined natural gas. The relevant Act is effective from 1 June 2017 and has come into operation from the same date as determined by the Minister of Finance by notice in the *Government Gazette*.

Interest

Withholding tax on interest paid to nonresidents was introduced and is effective from 30 December 2015, and the rate of tax is 10%.

F. Financing considerations

Thin capitalization limits

There are no thin capitalization provisions in the PTA. However, exchange control rules may affect the choice of funding. The acceptance by a local entity of loan funds from abroad is subject to specific exchange control approval.

The remittance of interest to nonresidents may be allowed upon provision of evidence of indebtedness, provided the rate is reasonable. Currently, a debt-to-equity ratio not exceeding 3:1 is required by the Bank of Namibia.

G. Transactions

Asset disposals

The license holder is not taxable on the proceeds from the sale of a share in physical assets. Section 7 of the PTA does not include capital receipts in taxable income, and even though Section 7(2) provides that an amount from the sale of an asset is deemed to have been received during the year of production, an amount received from the sale of an asset prior to the first year of production is not included in gross income. If, however, any portion of the amount received relates to prospecting information, it is taxable in the hands of the license holder in the year that production commences. Furthermore, although the license holder is not taxable on the amount received on the sale of the asset, the asset's capital expenditure is allowed (or carried forward) only to the extent that it exceeds the amount received (i.e., the amount received is "deducted" from the capital expenditure carried forward from that year).

Capital gains arising on the disposal of assets that are sold after the first year of production are included in gross income, and they are taxable in the hands of the license holder.

Amounts received on the disposal of petroleum licenses or rights are taxable in terms of the Income Tax Act at a rate of 32% from 30 December 2015. Costs incurred in acquiring the license or right as well as costs incurred in improving the license or right may be deducted in calculating the amount subject to tax.

The purchaser is able to deduct the consideration in the year that production commences, provided that the amount paid relates to the transfer of part ownership in an asset and not to the right to participate in the petroleum produced under a production license, or the license itself.

Farm-in and farmout

Recoupment provisions do not apply if an interest in a petroleum license is sold (e.g., where a disposal of part of an interest in a license area takes place in a year prior to the first year of production). As such, even if the consideration received — whether it is cash, an asset or a carryforward of an expenditure — exceeds the value of the share of the interest sold, it is not included in the license holder's gross income because there is no tax on the profits of the sale of capital assets in Namibia in the years prior to the first year of production.

The recoupment provisions reduce the expenditure claimable in respect of the assets and reduce the capital expenditure claimable in the year that the consideration is received, whether the amount relates to an asset or to capital expenditures other than in respect of an asset.

The purchaser is able to deduct the consideration in the year that production commences, provided that the amount paid relates to the transfer of part ownership in an asset and not to the right to participate in the petroleum produced under the authority of a production license.

Amounts received for the disposal of petroleum licenses or rights are taxable in terms of the Income Tax Act at a rate of 32%. Costs incurred in acquiring the license or right as well as costs incurred in improving the license or right may be deducted in calculating the amount subject to tax.

Selling shares in a company

Namibia does not impose CGT generally. However, amounts received on the disposal of shares in companies that directly or indirectly own petroleum licenses or rights are taxable in terms of the Income Tax Act at a rate of 32% from 30 December 2015.

Stamp duties also apply at a rate of NAD2 for every NAD1,000 of the market value of the shares transferred.

H. Indirect taxes

Import duties

License holders are exempt from paying import VAT under Schedule V of the Value-Added Tax Act No. 10 of 2000 (the VAT Act).

VAT

VAT is chargeable on the taxable supply of goods by every registered person, under Section 6(1)(a) of the VAT Act. "Taxable supplies" are defined in Section 1 of the same Act as the supply of goods or services in the course or in the furtherance of a taxable activity. Namibia is defined for the purpose of the VAT Act as including the territorial sea, the economic zone and the continental shelf. As such, for VAT purposes, goods or services supplied by a registered person up to 200 nautical miles from the low-water mark may be subject to VAT.

If taxable supplies exceed NAD200,000, voluntary VAT registration may be applied for. The threshold for compulsory registration has been increased to NAD500,000 effective from 1 January 2016.

For VAT purposes, "taxable activity" means any activity that is carried on continuously or regularly by any person in Namibia or partly in Namibia, whether or not for a pecuniary profit, that involves or is intended to involve, in whole or in part, the supply of goods or services to any other person for consideration. No guidelines define the terms "continuously" or "regularly," but, in practice, the Directorate of Inland Revenue views an uninterrupted presence in Namibia of 4 weeks or of 3 times in any 12-month period to be a sufficient presence to oblige the enterprise to register for VAT.

License holders must levy VAT at 15% on invoices for goods or services unless they are exported, in which case VAT at 0% may be levied.

As VAT-registered persons, license holders are entitled to claim credit for VAT paid on invoices issued by Namibian suppliers against VAT charged on supplies made in Namibia.

Stamp duties

Stamp duties are payable at varying rates under the Stamp Duties Act No. 15 of 1993. Although there is no requirement to register the petroleum agreement, the stamping thereof ensures that the contract is valid for litigation purposes. Stamp duties on a contract are NAD5.

Registration fees

License holders are required to pay annual charges for the benefit of the State Revenue Fund, calculated by multiplying the number of square kilometers included in the contracted block or blocks by the amounts provided for in Section 67 of the Petroleum Act. In the case of exploration licenses, the charge is calculated as follows:

- During the first four years, NAD60 per square kilometer
- During the next two years, NAD90 per square kilometer
- During the subsequent two years, NAD120 per square kilometer
- Thereafter, NAD150 per square kilometer

In the case of production licenses, the fee is NAD1,500 per square kilometer.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Direct taxes

Holders of a Dutch exploration and/or production license are generally subject to (a combination of) the following direct taxes: (i) corporate income tax (“CIT”), (ii) surface rental taxes, (iii) state profit share (“SPS”) and/or (iv) a royalty-based taxation (in *Dutch:* ‘cijns’). The main elements are as follows:

- CIT rate: 20% to the first EUR 200,000 of taxable profit, 25% to the remainder[1]
- SPS levy – 50%[2]
- Royalties – 0% to 7%
- Bonuses – None
- Production sharing contract (“PSC”) – Not applicable
- Surface rental:
  - Offshore exploration areas – EUR 261 to 784 per km²
  - Production areas – EUR 784 per km²
- Remittance to the province
- Capital allowances – U, E[3]
- Investment incentives – Research and development (R&D) credit (CIT), additional 25% deduction on capital investments in qualifying small fields (SPS)[4]

B. Direct taxes

The fiscal regime that applies in the Netherlands to the petroleum industry may consists of a combination of CIT, a surface rental tax, an SPS levy and royalty-based taxation.

1 *For Dutch CIT purposes – inter alia – the SPS levy is deductible.*
2 *The Dutch CIT is creditable for SPS purposes.*
3 *U: capital uplift or credit; E: immediate write-off for exploration costs.*
4 *Effective as of September 2010.*

Filing requirements (CIT/SPS)

For Dutch CIT and SPS purposes, the fiscal year is in principle equal to the book year. A Dutch taxpayers' book year is determined on the basis of its articles of incorporation and may end on any date during the calendar year.

A Dutch CIT return, in principle, needs to be filed within five months after the end of a fiscal year. A Dutch taxpayer can, however, file a request with the Dutch tax authorities for an extension of this deadline (generally resulting in an extension of five months). Alternatively, an intermediary can include the Dutch taxpayer in its extension program with the Dutch tax authorities. This generally results in an extension of 11 months.[5]

For Dutch SPS purposes, a (co-)production license holder must prepare profit and loss statements in accordance with the provisions of the Mining Act, together with a balance sheet showing the assets and liabilities relating to the production as of the fiscal year-end. If a (co-)holder holds more than one production license, consolidated profit and loss statements may be prepared. The SPS information should be included as an appendix to the Dutch CIT return.

Dutch CIT and Dutch SPS are imposed on an assessment basis. The competent authority for Dutch CIT and Dutch SPS purposes is the Dutch tax authorities.

Dutch CIT

General

Dutch CIT is imposed on resident and non-resident taxpayers. Resident taxpayers are legal entities incorporated under Dutch civil law and companies having their place of effective management in the Netherlands. Resident taxpayers are taxable on their worldwide taxable income. Certain income may effectively not be included (and hence exempt from Dutch CIT), such as income derived from qualifying shareholdings and income derived by and attributable to foreign permanent establishments ("PE").

Legal entities residing abroad may be regarded as non-resident taxpayers subject to Dutch CIT on specific Dutch source income, such as income derived by and attributable to a PE situated in the Netherlands.

For 2018, the statutory Dutch CIT rate is 25%, but a reduced rate of 20% applies to the first EUR 200,000 of taxable profit.

It is important to note that — inter alia — the SPS due is deductible for Dutch CIT purposes.

Substance

Legal entities incorporated under Dutch civil are deemed to be residents of the Netherlands for – inter alia – Dutch CIT purposes. Substance requirements are, however, in place in the Netherlands, which typically are of relevance if a Dutch taxpayer would want to obtain certainty in advance by entering into an Advance Tax Ruling or Advance Pricing Agreement with the Dutch tax authorities. Substance requirements also apply to entities primarily engaged in intragroup financing, leasing and/or licensing activities.

Determination of taxable profit

The taxable amount for Dutch CIT purposes equals the taxable profit minus any losses carried over from other fiscal years. The taxable profit is equal to profit minus gifts. Profit is hereby defined as 'the total income derived from a business, in whatever form and under whatever name'.

The profit is subsequently allocated to the a fiscal year under application of the so-called 'sound business practice' (i*n Dutch:* 'goed koopmansgebruik') and consistent accounting practice. The concept of sound business practice is not defined in Dutch tax law, but developed in case law. It is based on general accounting principles, but deviates where such principles are not in line with the Dutch tax concepts.

5 *This means that the annual Dutch CIT return should be filed within 16 months after the end of a fiscal year. In certain circumstances, an additional extension of two months can be requested for.*

The broad definition of profits allows that expenses incurred in connection with the conduct of a business, in principle, are deductible for Dutch tax purposes, unless a specific provision disallows such deduction. Expenses triggered by the shareholder's relationship are, in principle, not deductible.

The above also implies that exploration costs may in principle immediately be deducted from the taxable base for Dutch CIT purposes. This is however different if the costs have been incurred in respect of a well meeting the criteria to become a production well within the near future and the development of reserves found through such well is reasonably certain taking into account the facts and circumstances known at that time. A Dutch taxpayer is, however, allowed to capitalize the exploration costs in connection with the (current) unsuccessful wells. Typically, the tax treatment of exploration costs can be discussed with the Dutch tax authorities upfront.

Arm's-length principle

The arm's length principle is codified in Dutch CIT law. According to this principle, the pricing of transactions between a Dutch taxpayer and its affiliated entities should be in line with the pricing of comparable transactions between independent companies in comparable situations. If this is not the case, corrections may be made for Dutch CIT purposes and secondary corrections maybe imposed (e.g. a deemed dividend).

Tax losses and credits

Under Dutch CIT law, the carry back of losses is limited to one year and the carry forward is limited to nine years. The carry forward and/or carry back of losses may however be restricted, in particular for holding and/or financing companies or in case of a change in ultimate ownership to prevent the trading in 'loss companies'.

For Dutch CIT purposes, a credit can — inter alia — be taken into account for the SPS levy. Furthermore, a credit for foreign withholding taxes may be taken into account, provided certain conditions are met.

Functional currency

The default currency for Dutch CIT purposes is the Euro. A Dutch taxpayer can however file a request with the Dutch tax authorities to allow the Dutch taxpayer to calculate its taxable amount in another currency (e.g. USD), provided certain requirements are met. The main requirement is that in the first year the Dutch taxpayer would like to apply such functional currency, its financial statements are prepared in the currency requested for. After the request is granted and a corresponding decision is issued by the Dutch tax authorities, the functional currency must in principle be used for at least 10 years.

Fiscal unity

Upon request, a Dutch corporate taxpayer can form a fiscal unity with one or more of its (indirect) Dutch tax resident subsidiaries. This implies that the results of such subsidiaries are included in the result of the parent company for Dutch CIT purposes. In addition, transactions within a fiscal unity are typically ignored, as a result of which, for example, assets may be transferred between entities forming part of the fiscal unity without consequences and loans may be disregarded.

One of the key requirements to be met is that the legal entities to be included in the fiscal unity are tax residents in the Netherlands.[6] Furthermore, the parent company must hold 95% of the economic and legal interest in the subsidiary. Another requirement is that the parent company and its subsidiary/ subsidiaries must have the same fiscal year.

6 *In certain cases, Dutch permanent establishments of foreign companies can be included.*

Termination of the fiscal unity, e.g., because the requirements are no longer met, could have adverse Dutch tax consequences.

On February 22, 2018, the Court of Justice of the European Union ("CJEU") issued a decision in two cases that may impact the current application of the fiscal unity. In view of the significant impact that this decision may have, the Dutch Government announced emergency response legislation on October 25, 2017. The draft legislative proposal for the amendments to the Dutch fiscal unity regime were published on June 6, 2018.On the basis hereof, and as per October 25, 2017, 11.00 AM Dutch time, the existence of a fiscal unity is ignored for application of certain provisions of the Dutch tax law (in particular as regards the applicability of interest deduction limitation legislation).

Participation exemption

Dividends received and capital gains realized from a qualifying shareholding are exempt from Dutch CIT, provided that the Dutch participation exemption is applicable. Generally, the following requirements must be satisfied in order for the Dutch participation exemption to apply:

- The taxpayer is not an investment company within the meaning of certain provisions of the Dutch corporate income tax act;
- The taxpayer holds at least 5% of the nominal issued and paid-up share capital of a subsidiary with capital divided into shares.[7]; and
- The subsidiary is held with the objective the obtain a return that is greater than a return that may be expected from normal asset management / not (deemed to be) held as a portfolio investment ("motive test").

If the subsidiary is (deemed to be) held as a portfolio investment, the Dutch participation exemption nevertheless still applies if either:

- The assets of the subsidiary, on an aggregated basis, do not directly or indirectly consists of low-taxed free portfolio investments (e.g., intercompany receivables, permanent excess cash, intangibles put at the disposal of related entities) ("asset test); or
- The subsidiary is subject to an effective tax rate of at least 10% in accordance Dutch standards ("subject-to-tax test").

Depreciation of business assets

For Dutch CIT purposes, assets should be capitalized at their acquisition costs and depreciated over their expected lifespan. The expected lifespan should be determined in an objective manner, i.e., the period in which the Dutch taxpayer expects to be using the asset is, in principle, irrelevant. For Dutch CIT purposes, the maximum allowed annual depreciation is generally 20% of the assets' acquisition costs. Assets cannot be further depreciated than their residual value. Depreciating an asset, if possible, is obligatory. Hence, a Dutch taxpayer cannot chose not to depreciate an asset while such asset is subject to wear and tear and the residual value is not yet reached.

Treatment of foreign branches

Under application of the so-called 'object exemption' (*in Dutch:* 'objectvrijstelling'), income derived by and attributable to a foreign PE may be exempt from Dutch CIT. Under the object exemption, positive PE results are excluded from the Dutch tax basis (thus reducing the taxable income), and negative PE results are added to the Dutch tax basis (thus increasing the taxable income). As a result, the PE income is effectively exempt. This treatment is effective for PEs located in both treaty and non-treaty countries, although differences may arise. Profits derived by and attributable to passive low-taxed branches are in principle not exempt under application of the object exemption, unless the Netherlands is required to exempt the income derived by and attributable to such low-taxed branches under application of a tax treaty.

7 *In case the taxpayer is a less than 5% shareholder in the nominal issued and paid-up share capital, this requirement should — inter alia — also be met in case a related party of the taxpayers holds a participation in the company as meant in Dutch tax law.*

Application of the Dutch object exemption implies that foreign branch results cannot (immediately) be deducted from the Dutch taxable profit. However, if the branch is terminated, the ultimate loss will still be deductible, subject to certain deductions.

It is furthermore important to note that grandfathering rules apply regarding the recapture of historical (i.e., pre January 1, 2012) claimed foreign PE losses.

SPS

General

The (co-)holder of a Dutch onshore and/or offshore production license is, in addition to Dutch CIT, subject to a Dutch SPS levy. The Mining Act hereby provides for a Dutch SPS levy of 50% on profit resulting from mineral production activities. The profit for Dutch SPS purposes is ring-fenced, implying that — inter alia — income and expenses related to non-mineral production activities should ignored.

For Dutch SPS purposes, there is no distinction between foreign or domestic (co-) holders of a production license. The mere fact that the license holder (co-) owns the production license is sufficient.

It is unlikely that gas storage activities fall within the realm of Dutch SPS. However, conversion of an upstream site into a storage facility may trigger Dutch SPS "exit tax" discussions with the Dutch tax authorities.

Determination of the taxable basis for SPS purposes

The Mining Act specifically indicates that the determination of taxable income for Dutch SPS purposes is based on the same principles as the Dutch CITA. However, the Mining Act lists a number of specific income and expense items that are either included or excluded from the taxable basis for SPS purposes.[8]

The taxable base for Dutch SPS purposes includes, by all means:

- The movement of inventory;
- The gain or loss realized in relation to the (partial) alienation of a production license;
- The fair market value of the hydrocarbon products not used for sale;
- Costs pertaining to the exploration phase, to the extent that these have not already been deducted for SPS purposes.

Examples of excluded income and expense components for Dutch SPS are:

- Amortization of the purchase price of an exploration license, to the extent that the purchase price exceeds costs that have not been deducted before for SPS purposes — implying that a payment for an exploration license is only deductible for SPS purposes to the extent that this purchase price reflects costs that have not been deducted before for SPS purposes, so goodwill paid in addition to the true costs of an exploration license is not deductible
- The value of extracted minerals that have been used for the upstream activity itself

Third-party tariff income generated by the license holder, through making available platforms or pipelines by the license holder, is excluded from the taxable basis for Dutch SPS purposes. As a consequence, costs relating to third-party tariff income should also be excluded from the taxable basis at the level

8 *Amongst others the following provision of the Dutch corporate income tax act also apply for SPS purposes: (i) the concept of 'sound business practice', (ii) the provision with respect to depreciation of certain assets, (iii) the provision relating to the formation of a reinvestment reserve, (iv) the provision relating to the definition of 'year' (see paragraph 1 ; and (v) the provision relating to the functional currency (see paragraph 2.5. The following provisions of the Dutch corporate income tax – inter alia – do not apply for SPS purposes: (i) the provision to allow a taxpayer to form a fiscal unity, (ii) the provision to allow taxpayers to deduct an investment allowance, a small-scale investment allowance, an energy investment allowance and/or an environmental investment allowance and (iii) the provisions with respect to the compensation of tax losses incurred.*

of the license holder. Based on the historic practice that was confirmed in 2014 by the Dutch Supreme Court, such attributable costs are equal to one third of the tariff income.

The result for Dutch SPS purposes has to be adjusted if the arm's length criteria is not met.

Uplift

All expenses included in the profit- and loss account are in principle increased with a 10% uplift for Dutch SPS purposes, with the exception of:

- Any taxes and public levies borne by the license holder;
- Amortization of the purchase price of a production license, to the extent that the purchase price exceeds costs that have not been deducted before for Dutch SPS purposes, so the uplift is only available for "truly incurred expenses" and not for a goodwill payment; and/or
- Additions to an abandonment provision, to the extent that the transferor of the production license has already made additions to the abandonment provision earlier (this exception prevents multiple uplifts).

SPS investment incentive for marginal gas fields

(Co-)Holders of a Dutch gas exploration and/or production offshore license are allowed to claim an additional investment allowance of 25% with respect to certain capital investments related to qualifying marginal gas fields for Dutch SPS purposes. Whether a (potential) gas field qualifies depends on a number of factors, such as the expected productivity of the gas well, the technically producible gas volume of the reservoir and the shortest distance to an existing platform.

The additional allowance of 25% can be claimed in the SPS return in the year in which the (co-) license holder has entered into the obligation to purchase the capital asset or has incurred production costs in respect of the capital asset, to the extent that such obligation of costs are incurred by the (co-) holder of the license. If the asset is not yet in use at the end of the book year and the amount of the investment allowance would exceed the amount that has been paid on such investment, only the amount that has been paid can be taken into account. The excess can be taken into account in following years to the extent that payments are made, but not later than in the year in which the capital asset is taken into use.

The investment allowance could effectively result in a subsidy of 12.5% of the amount of investment.

Tax rate and credits

The SPS rate is set at 50%. A loss may be carried back for three years and carried forward for an indefinite period of time. This provision differs from the loss relief rules in place for CIT purposes.

After the amount of SPS due is determined by taking into account the losses available for set-off and the possible investment allowance, a creditable amount may be taken into account, which may result in a decrease of the amount of SPS due. The credit is determined as follows:

1. The SPS income is adjusted for the 10% uplift.
2. The adjusted SPS income is reduced by SPS that will be due after credits.
3. The number computed under the previous bullet item is then multiplied with the Dutch CIT rate prevailing for the year.

Surface rental

Surface rental is a tax levied on each (co-) holder that either has an offshore exploration license or an onshore or offshore production license at January 1st of a calendar year. The 2018 rates are EUR 261 to EUR 784 per km² for offshore exploration areas[9] and EUR 784 per km² for production areas.

9 *The applicable rate depends on the duration of the license. The first year is hereby defined as the year in which the license is applicable on January 1st.*

The surface rental is paid on a "return" basis. The ultimate filing date is 1 April of the calendar year in question.

Royalty regimes

Royalties (*in Dutch:* 'cijns') are charged to (co-) holders of an onshore or offshore production license. Effectively, the royalties are only due on onshore production licenses, as the applicable rate for offshore licenses is set at zero percent.

The amount of royalties due depends on the kind of produces (i.e., oil or gas) and the turnover. The turnover is hereby determined by multiplying the units produced with the at arm's length price at which the units are sold.

Production does not include: units used for the exploration of production within the surface area, units used for processing the products and transportation them to the place where they are being processed and units attributable to the Dutch state based on the participation agreement with the Dutch government.

The following rates for 2018 are shown in the table below.

Bracket	Oil (in thousands of cubic meters)	Gas (in millions of cubic meters)
0–199 units	0%	0%
200–599 units	2%	2%
600–1,199 units	3%	3%
1,200–1,999 units	4%	4%
2,000–3,999 units	5%	5%
4,000–7,999 units	6%	6%
8,000 units and more	7%	7%

The above rates increase by 25% in the event that the average price of an imported barrel of crude oil exceeds EUR 25,-. A 100% increase applies in the event of an absence of state participation in the license.

Royalties are paid on a return basis. The ultimate filing date is April 1st of the year following the calendar year in question.

Remittance to provinces

A one-time remittance fee is due to the relevant province within the Netherlands for each onshore production license. The fee due depends on the size of the production area used for the mining equipment (e.g., not necessarily the area as stated on the production license). The fee is collected by the provincial authorities, which have to announce the amount due to the (co-)holder of the production license.

Unconventional oil and gas

No special tax regime currently applies to unconventional oil and gas. The Dutch Government is currently further investigating the general possibilities of shale gas production in the Netherlands and what kind of incentives and regulatory rules are required.

C. Indirect taxes

VAT

The standard rate of value-added tax ("VAT") in the Netherlands is 21%, with a reduced rate of 6%, which is potentially chargeable on all supplies of goods and services made in the Netherlands and its territorial waters (within a zone of 12-nautical sea miles). In addition, a 0% VAT rate (exempt with credit) could be applicable. Dutch and non-Dutch resident companies may be required to register for Dutch VAT if supplies are made that are VAT taxable in the Netherlands. This also applies for supplies subject to the 0% rate. No registration thresholds apply in the Netherlands, although an administrative simplification regime may be applicable to small entrepreneurs.

A non-resident company that is required to register for Dutch VAT can register directly with the Dutch tax authorities; there is no requirement to appoint a fiscal representative, unless specific supplies are made that require a fiscal representative. Appointment of a fiscal representative is, among others, obligatory for supplies made within a VAT or excise warehouse, or for import of goods by nonresident companies using the import VAT deferment scheme (article 23 license, see below).

VAT incurred by an entity that is VAT registered in the Netherlands is normally recoverable on its periodic VAT returns, provided that it performs VAT taxable activities in the Netherlands. Otherwise, VAT may be refundable via a European Union (EU) or 13th Directive refund request.

A VAT cash flow advantage can be obtained in the Netherlands by importing goods from non-EU countries into the Netherlands, using an import VAT deferment license (article 23 license). A company can obtain its own import VAT deferment license or make use of the import VAT deferment license of its limited fiscal representative. If an import VAT deferment license is used, no import VAT is due at the time of import. Rather, the import VAT is reported in the periodic Dutch VAT return. Provided that the company has a full input VAT recovery right, the import VAT reported can be deducted in the same VAT return, not leading to an adverse VAT cash flow.

Oil rigs and similar production platforms on sea could be regarded as "seagoing vessels" from a Dutch VAT perspective. As a consequence, the supply, lease and services with respect to these rigs and other platforms could be subject to the 0% Dutch VAT rate (still enabling input VAT recovery). Also, the provisioning and other supplies to such rig or platform could under conditions benefit from the 0% Dutch VAT rate.

As of January 1, 2019, the Dutch VAT rules on what qualifies as a "sea-going vessel" will change, which may also impact the supplies to/with respect to rigs and production platforms.

The supply of goods to oil rigs and similar production platforms from a Dutch onshore location to a place outside the 12-nautical sea miles zone should be regarded as an export supply, subject to 0% VAT, provided that all formal requirements are met. For services performed to such rigs or platforms, it should first be determined based on the place of supply rules where these services would be VAT taxable. For location-bound services, such as services to immovable property, these services are outside scope of Dutch VAT if performed outside the 12-nautical sea miles zone. Services subject to the general place of supply rule for cross-border services should be VAT taxable where the recipient is established. In that country, it should be determined whether the services are subject to the standard VAT rate, or, for example, to the 0% VAT rate/exemption. As mentioned above, in the Netherlands, a 0% VAT rate may be applicable for services related to oil rigs and similar production platforms.

Input VAT incurred with respect to the exploration of hydrocarbon products should be recoverable, provided that the company that incurs these costs can objectively demonstrate its intention to perform VAT taxable activities in case of a successful discovery further to the exploration performed. It is key to (timely) document this intention, for example in business plans, contracts and/or board resolutions.

In the Netherlands, the VAT treatment of the sale of hydrocarbon products produced as a result of a successful exploration and production program depends on the product itself, where it is sold and to whom it is sold. Natural gas and associated products imported into the Netherlands from a field outside the Netherlands' territorial waters are subject to formal customs import procedures, although the 0% VAT rate is applicable to the import of natural gas into the Netherlands to the gas distribution network.

Dutch companies holding subsidiaries (besides potential oil and gas activities) may face input VAT deduction limitations on costs incurred as pure shareholding activities do not lead to any input VAT recovery. In order to avoid such input VAT deduction limitations, upfront consideration and review of envisaged activities is recommended.

Excise duty

In the Netherlands excise duty is payable on specific mineral oils and hydrocarbon products, including biofuels, if these products are used or, based on their objective characteristics, intended for use as motor or heating fuel. Duty is due based on the removal from an excise warehouse for "home use" (i.e., they are removed for domestic use). As long as these products are stored in an excise warehouse, they are duty suspended, and the VAT rate is 0%. The rate of excise duty payable in respect of mineral oils is based on the customs classification of the product. Excise dutiable products are among others: fuel, gasoil, heavy fuel oil, liquid petroleum gas ("LPG"), biodiesel and E85.

Oil rigs and similar production platforms on sea are regarded as "seagoing vessels" from a Dutch excise duty perspective. As a consequence, the supply of oil products to these rigs and other platforms are excise duty-exempted, if used for propulsion and provided that all formal requirements are met. The supply of oil products to oil rigs and similar production platforms from a Dutch onshore location to a place outside the 12-nautical sea miles zone, is regarded as an export for excise purposes as well as supplies to seagoing vessels in international traffic, which result in exemption or repayment of excise duties irrespective the use of the mineral oils.

Customs duty

All goods imported into the Netherlands from outside the EU are potentially liable to customs duty. Customs legislation and duties are harmonized in the EU. The rate of customs duty is based on the classification of the goods in the EU Customs Tariff (the Combined Nomenclature based on the worldwide Harmonized System) and whether the goods qualify for preferential rates. For certain products, antidumping and countervailing duties might also be due, e.g., currently, for bioethanol (fuel ethanol) from the US, an antidumping duty was due, and for biodiesel from the US, including certain blends from Canada, antidumping and countervailing duty are due.

Customs reliefs and regimes may allow goods to be imported at a reduced or zero rate of duty, provided the goods are used for a prescribed use under customs control, within a specified time limit. Normally, a business must seek prior authorization from Dutch Customs to apply any customs relief or regime. Especially, products for "seagoing vessels," such as ships, oil rigs and similar production platforms on sea, are suspended from customs duties based on an end-use license.

Please note that from 1 May 2016, the Union Customs Code is in force. Based on this renewed customs legislation, among others, procedures have changed and rules for applying customs licenses (such as end-use, inward processing) became stricter and rules for determining the customs valuation have changed (e.g., customs value will be based on the last sale before entering EU, which will lead to a higher amount of duties payable).

D. Other

Dutch wage tax withholding obligation

Under the Dutch Wage Tax Act, nonresident companies that perform their business activities during a period of at least 30 days in, at or above the Dutch territorial waters and/or the Dutch Exclusive Economic Zone have the obligation to withhold and pay wage tax on the taxable employment income paid to their employees. The nonresident company should register with the Dutch tax authorities and process a wage tax withholding administration in this respect.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

New Zealand's fiscal regime applicable to the petroleum industry consists of a combination of corporate income tax (CIT) and royalty-based taxation. The main elements are:

- Royalties — 0% to 20%
- CIT rate — 28%
- Capital allowances — D, E[1]
- Investment incentives — L[2]

B. Fiscal regime

The fiscal regime that applies to the petroleum industry in New Zealand consists of a combination of CIT and royalty-based taxation.

Corporate tax

New Zealand resident corporations are subject to income tax on their worldwide income at the rate of 28%.

CIT is levied on taxable income. "Taxable income" is defined as assessable income less deductions, less any available net losses. "Assessable income" includes ordinary income (determined under common law) and statutory income (amounts specifically included in the Income Tax Act). In general, deductions include expenditures incurred in deriving assessable income or expenditures incurred in the course of conducting a business for the purpose of deriving assessable income.

An expenditure of a capital nature is generally not deductible when incurred, although depreciation deductions may be available (other than buildings with an estimated useful life of at least 50 years). However, deductions for certain oil and gas expenditures of a capital nature are available under a specific petroleum mining regime — see Section C below for an outline of exploration and development costs.

1 *D: Accelerated depreciation; E: Immediate write-off for exploration costs.*
2 *L: Losses can be carried forward indefinitely.*

Ring-fencing

New Zealand does not generally apply ring-fencing in the determination of corporate tax liability. However, expenditures on petroleum mining operations undertaken through a foreign branch of a New Zealand resident company cannot be offset against other New Zealand sourced income. Otherwise, the same tax entity may offset losses against any of its project profits (or other group companies with at least 66% of common ultimate ownership).

New Zealand has tax consolidation rules under which various wholly owned New Zealand entities may form a tax-consolidated group and thereby be treated as a single tax entity.

Capital gains tax

There is currently no comprehensive capital gains tax (CGT) in New Zealand. However, generally, all gains on financial arrangements are subject to tax. Further, gains on the sale of property that is purchased for the purpose of resale, or as part of a profit-making scheme, are taxable. An amount that has been derived from a business is also taxable, unless the amount is of a capital nature.

The specific taxing provisions that apply to petroleum miners may override these general principles. For example, special provisions tax the proceeds from the sale of petroleum mining assets, such as license areas and geological information.

The Government has announced its intention to establish a Tax Working Group to consider the introduction of a capital gains tax. The stated purpose of the group would be to consider the balance between the taxation of income and assets, in particular capital gains associated with property speculation. The outcomes of the Tax Working Group, if any, will not take effect until 1 April 2021.

Dividends

New Zealand has a dividend imputation regime. So, the benefit of tax paid by a New Zealand company can be passed on to its New Zealand resident shareholders.

Fully imputed dividends (sourced from tax-paid profits) are liable to a 0% rate of nonresident withholding tax (NRWT) if paid to a nonresident shareholder who holds at least a 10% direct voting interest in the company or, if less than 10%, where the relevant tax treaty reduces the withholding rate to below 15% (although none of the existing treaties allow for this second alternative to apply).

In other cases, a nonresident shareholder can receive a dividend that is fully imputed from a New Zealand company without further tax costs under the foreign investor tax credit (FITC) regime. The mechanism is somewhat complex but, in brief, a New Zealand resident company can effectively compensate a foreign shareholder for the NRWT by paying an additional supplementary dividend. The supplementary dividend is funded through an FITC, as the company can claim a tax credit or refund equivalent to FITC.

Treaty relief may also be available. (see Section E below).

Mineral royalties

The royalty regime applies to petroleum permits granted on or after 1 January 1995. The regime is set out in detail in the Minerals Program for Petroleum 2013 (as provided for under the Crown Minerals Act 1991).

Royalties are payable if petroleum is discovered and sold, used in the production process as fuel, exchanged or transferred out of the permit boundaries without sale, or where petroleum remains unsold on the expiry of a permit. However, no royalty is payable in respect of:

- Petroleum that is flared or otherwise unavoidably lost
- Petroleum that is returned to a natural reservoir within the permit area (e.g., reinjected gas)
- Petroleum that is removed from an approved underground storage facility and upon which a royalty has previously been paid by the producer

Mining permits issued under the Crown Minerals Act 1991 prior to 1 January 1995, or mining licenses issued under the Petroleum Act 1937 prior to the passage of the Crown Minerals Act 1991, continue to pay the royalty specified at the time the permit or license was granted.

A company with a permit granted prior to 1 January 1995 may apply to the Secretary of Commerce to have the royalty calculated as if the permit were granted on or after 1 January 1995.

On 7 March 2012, the Government of New Zealand released a discussion document outlining proposed changes to the Crown Minerals Act 1991. A detailed review of the royalty regime for petroleum was undertaken, and the royalty and taxation regime was seen as generally fit for purpose; as such, no major amendments to the royalty regime have been included in the Crown Minerals Amendment Act 2013 or in the Minerals Program for Petroleum 2013 (the Minerals Program for Petroleum provides guidance on how the legislation and associated regulations will be interpreted and applied).

Discoveries between 30 June 2004 and 31 December 2009

There are special royalty provisions applying to discoveries made, and prospecting and exploration costs incurred, between 30 June 2004 and 31 December 2009. The purpose of the special provisions is to encourage increased exploration to identify new gas discoveries, given the decline of existing fields.

For any discoveries made under a mining permit between those dates, the royalty regime is a hybrid regime that stipulates an annual payment that is the greater of:

- An ad valorem royalty (AVR), which is levied on 1% of the net sales revenue for natural gas and 5% of the net sales revenue for oil.
- An accounting profits royalty (APR), which is levied on:
    - 15% of accounting profits on the first NZD750 million (cumulative) gross sales for an offshore discovery and 20% accounting profits on additional production

      Or
    - 15% of accounting profits on the first NZD250 million (cumulative) gross sales for an onshore discovery and 20% of accounting profits on additional production

Mining permit holders are required to pay the higher of the two royalties in any year.

Prospecting and exploration costs incurred anywhere in New Zealand between 30 June 2004 and 31 December 2009 are deductible for the purposes of calculating the APR.

All other petroleum production

For all other petroleum production, including any from a discovery made after 31 December 2009, the royalty regime comprises a 5% AVR or a 20% APR, whichever is the greater in any given year.

The APR deductions can relate only to the mining permit for which the royalty applies, not the activities of the permit holder overall.

Application of AVR and APR

Application of these royalties is determined by the net sales revenue earned in a period and the type of permit held. If a mining permit has never had net sales revenue of more than NZD1 million in a reporting period, the permit holder is liable to pay only the AVR. If the permit holder anticipates having revenue from a mining permit exceeding NZD1 million, the royalty is payable at the higher of the APR and AVR. Furthermore, where an exploration permit is held, the permit holders are liable to pay only the AVR.

Detailed records of allowable operating and capital expenses should be kept, in order to claim allowable APR deductions.

Calculation of APR

The following deductions are permitted in calculating the APR:

- Production costs
- Capital costs, meaning development costs, exploration costs, feasibility study costs, and permit maintenance and consent costs (excluding permit purchase costs)
- Indirect costs
- Decommissioning costs
- Operating and capital overhead allowance
- Operating losses and capital costs carried forward (including costs from previous permit holders that have not been deducted)
- Decommissioning costs carried back

These costs are written off against sales revenues, and any excess is carried forward to the succeeding reporting periods. Note that the costs are not amortized on a time or production basis.

Unfortunately, the prescription for calculating the accounting profit does not specify:

- The manner in which exploration costs are to be treated (successful method or unsuccessful method)
- Guidelines for associated products (which may have material value) and by-products (which have relatively insignificant value)

Branch remittance tax

Branch remittance tax does not apply in New Zealand.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Specific income tax provisions relate to expenditures incurred in the course of petroleum mining operations.

Classification of petroleum expenditures

An expenditure on petroleum mining is categorized as a "petroleum exploration expenditure," a "petroleum development expenditure" or a "residual expenditure." These three categories are described next.

Petroleum exploration expenditure

The definition of a "petroleum exploration expenditure" encompasses:

- Exploratory well expenditures
- Prospecting expenditures
- Expenditures to acquire a prospecting license, a prospecting permit for petroleum or an exploration permit for petroleum

It does not include:

- Residual expenditures
- Expenditures on petroleum mining assets required to be treated as petroleum development expenditures

A petroleum exploration expenditure is allowed as a deduction in the year that the expenditure is incurred.

Petroleum development expenditure

The definition of a "petroleum development expenditure" includes an expenditure incurred that:

- Directly concerns a permit area
- Is for acquiring, constructing or planning petroleum mining assets.

It does not include:

- Residual expenditures
- Petroleum exploration expenditures
- Other expenditures otherwise allowed as a deduction elsewhere in the Income Tax Act

The term "petroleum mining asset" is defined as an interest in:

- A petroleum permit
- An asset that has an estimated life dependent on, and which is no longer than, the remaining life of the permit area, and is acquired by a petroleum miner for the purpose of carrying on in a permit area any activity in connection with:
    - Developing a permit area for producing petroleum
    - Producing petroleum
    - Processing, storing or transmitting petroleum before its dispatch to a buyer, consumer, processor, refinery or user
    - Removal or restoring operations

However, any asset acquired by a petroleum miner for the purposes of further treatment that takes place after the well stream has been separated and stabilized into crude oil, condensate or natural gas (by way of liquefaction or compression, the extraction of constituent products or the production of derivative products) is specifically excluded from the definition of a petroleum mining asset and is therefore not treated as a petroleum development expenditure. An exception applies if the treatment takes place at the production facilities.

Petroleum development expenditure is treated as a deferred deduction that is currently deductible over seven years on a straight-line or depletion basis.

The definition of a petroleum mining asset does not include underground facilities that are used to store processed gas. Instead, these facilities come within the general tax depreciation rules, being depreciated over their estimated useful life. Proceeds from the sale of an underground storage facility are capital in nature (though depreciation recovery may arise). Land is specifically excluded from the petroleum mining asset definition.

Residual expenditure

An expenditure excluded from the definition of both petroleum exploration expenditures and petroleum development expenditures is a residual expenditure.

Residual expenditure consists of:

- An expenditure on scientific research, other than a capital expenditure
- An application fee paid to the Crown in respect of a petroleum permit
- An insurance premium or royalty paid under the Petroleum Act 1937 or the Crown Minerals Act 1991
- Land tax or local authority "rates" (see Section H below) and interest
- Interest in, or expenditure under, a financial arrangement entered into prior to 20 May 1999
- Lease expenses in respect of land or buildings

A residual expenditure is deductible in the year it is incurred, subject to the general deductibility rules discussed above.

D. Incentives

Exploration

Petroleum mining exploration expenditure is immediately deductible for income tax purposes.

Tax holiday

New Zealand does not have a tax holiday regime.

Ability to carryforward losses

Losses (including New Zealand branch losses of a nonresident company) can be carried forward indefinitely. However, there is a requirement that a company satisfy a 49% "continuity of ultimate shareholding" test from the period when the losses were incurred until the losses are used. This provision requires that there be a 49% shareholder continuity based on voting interests or, if applicable, based on the market value of shares and options.

Losses may also be offset against the income of other companies in the same group (and the companies must be in the same group from the date the losses were incurred until the date they are offset). To be considered in the same group, the companies are required to have at least a 66% ultimate common ownership. Losses incurred by a dual resident company may not be offset in this manner.

Losses from foreign branches of New Zealand resident mining companies are ring-fenced against foreign income so that they cannot be used to shelter New Zealand sourced income.

Ability to carryback losses

Previously, under the Income Tax Act 2004, petroleum miners had the ability to carryback losses from unamortized development expenditure when a petroleum permit was relinquished. The loss was allowed as a deduction in the years preceding the year of relinquishment (although it was effectively limited to four years, because of the refund provisions in the Income Tax Act 2004). However, the Income Tax Act 2007 currently does not allow this. Inland Revenue has accepted that this is a drafting error, and has indicated that it will be remedied via a tax bill.

Exemption for drilling rigs and seismic ships

Until 31 December 2019, income earned from the drilling of exploratory or petroleum development wells in New Zealand, and income earned from seismic or electromagnetic survey work relating to petroleum in New Zealand, is exempt from income tax. The activities must be carried out by nonresident companies and must be confined to offshore petroleum fields.

Modular drilling rigs are excluded from the exemption.

E. Withholding taxes

Nonresident withholding tax

The NRWT rules apply to dividends or royalties derived from New Zealand by a nonresident and to New Zealand sourced interest derived by a nonresident that is not engaged in business through a fixed establishment in New Zealand.

Dividends paid by a New Zealand resident company to a nonresident are subject to 30% NRWT, unless the dividends are fully imputed (i.e., paid from tax-paid profits) or a double tax treaty applies (in which case, the rate is generally reduced to 15%, although some treaties may reduce the rate to either 5% or 0%). Further, a 0% NRWT rate may apply if the nonresident shareholder holds a 10% or more direct voting interest and the dividend is fully imputed or, if the nonresident shareholder holds less than a 10% direct voting interest, where the relevant tax treaty reduces the withholding rate to below 15%. Interest and royalties are subject to NRWT at a rate of 15% (reduced to 10% under most treaties). The approved issuer levy (AIL) regime (see next subsection below) may also apply to interest payments.

Interest

A resident petroleum mining company may deduct interest costs on an accrual basis (resident companies are generally allowed an automatic deduction for interest without establishing a nexus with assessable income), subject to thin capitalization and transfer pricing constraints (see Section F).

As noted above, interest payments to nonresidents are generally subject to 15% NRWT (reduced to 10% under most treaties). However, the tax treatment varies depending on the residence of the borrowing company and the source of the borrowings.

Previously, it was possible to claim an income tax deduction for interest (on an accruals basis) in a period earlier than the NRWT liability, in respect of both related-party debt and external debt. From 1 April 2017 (applying to related-party debt only), the income tax deduction for interest and the resulting NRWT liability arise generally in the same period.

New Zealand has an AIL system that allows a company to pay interest to a non-associated nonresident lender without having to deduct NRWT. Specific rules deem a group of independent investors to be associated if they are "acting together." The AIL is payable to the Inland Revenue at the rate of 2% (of the interest payable), which is generally tax-deductible. A specific rule allows registered banks to pay AIL on associated party funding.

New Zealand has no restrictions on the repayment of loans or foreign currency transactions.

Royalties

Royalties are generally tax-deductible if they are of a revenue nature and are incurred in the production of assessable income. Royalty payments are generally subject to NRWT when paid offshore (see the information about NRWT above).

Lease expenses

The tax treatment of lease payments is dependent on whether the lease in question is a finance lease. A finance lease includes the following:

- The ownership of the asset is transferred at the end of the lease term.
- The lessee has the option to buy the asset at a substantial discount.
- The term of the lease exceeds 75% of the asset's estimated useful life.

In the case of a finance lease, the lessee is treated as having purchased the asset, subject to a loan from the lessor. The lessee is therefore entitled to depreciation deductions on the leased asset and interest deductions in respect of the deemed loan.

If the lessor is not engaged in business through a fixed establishment in New Zealand, the lessor is potentially subject to NRWT on the deemed interest component of the lease payments. The amount of NRWT may be reduced under a relevant double tax agreement. Alternatively, a borrower may choose to pay a 2% AIL under the AIL regime (instead of NRWT) if the parties to the deemed loan are not associated.

If the lease is not a finance lease, the lessee is generally entitled to deduct the lease payments as they are incurred.

NZ International Financial Reporting Standard (IFRS) 16 will remove the distinction between operating leases and finance leases, with essentially all leases being required to be recognized as finance leases for accounting purposes. Although there are no direct changes to the tax treatment of leases, any adjustments to reverse the accounting treatment of leases will need to consider the new accounting rules. NZ IFRS 16 will take effect from 1 January 2019.

Nonresident contractors

Contract payments paid by a petroleum mining company to "nonresident contractors" for services performed in New Zealand are treated for tax purposes as payments liable for nonresident contractors tax (NRCT) deductions.

NRCT must be deducted from payments made to nonresidents in respect of any "contract activity." The definition of "contract activity" is very broad and includes:

- Performing any work in New Zealand
- Rendering a service of any kind in New Zealand
- Hiring personnel or equipment to be used in New Zealand

It should be noted from the first two bullet points that the work or service must be carried out in New Zealand. If work or service is carried out in any other country, the contract payments are not liable for NRCT even though they may relate to a New Zealand project.

Some payments are expressly excluded from treatment as a contract payment to a nonresident contractor. These are:

- Royalty payments, which are subject to NRWT
- Cost reimbursing payments, which constitute a reimbursement of expenditures incurred by the nonresident contractor; however, this exclusion does not apply if the parties to the cost reimbursement payment are associated persons
- Where the nonresident contractor has full New Zealand tax relief under a double tax agreement and is present in New Zealand for 92 days or less in a 12-month period
- When total payments do not exceed NZD15,000 in a 12-month period
- Where the nonresident contractor has provided an exemption certificate to the payer

F. Financing considerations

Thin capitalization

New Zealand's income tax system contains significant rules regarding the classification of debt and equity instruments, and rules impacting the deductibility of interest.

New Zealand's thin capitalization rules require the ratio of debt to assets to not exceed 60%. Interest deductions are not allowed to the extent that the debt-to-asset ratio exceeds this ratio and the debt percentage of the New Zealand taxpayer also exceeds 110% of the consolidated worldwide debt-to-asset ratio of the controlling nonresident group.

When calculating the debt-to-asset ratio, only interest-bearing debt is considered (i.e., non-interest-bearing debt is not included in the calculation).

Further, there is an on-lending concession that allows the New Zealand taxpayer to subtract on-lent amounts from both the debt component (numerator) and asset component (denominator) of the calculation.

New rules concerning thin capitalization will take effect from income years beginning on or after 1 July 2018. In particular, non-debt liabilities will be required to be subtracted from the calculation of assets (i.e., reducing the asset base).

Transfer pricing

New Zealand has a transfer pricing regime in respect of cross-border payments between associated parties. Broadly, the rules require the payments to be calculated on an arm's-length basis.

New rules concerning the interest deductibility on related party inbound loans will take effect for income years beginning on or after 1 July 2018:

- The deductible interest rate will be capped at the credit rating of the global ultimate parent of the group, with a one downward notch allowance
- The tenor of the related-party loan will be deemed to have a cap of five years
- Other terms and conditions that could result in an "excessive interest rate" will be ignored, unless the taxpayer can demonstrate that it has substantial third-party debt featuring the same terms and conditions

Debt remission income

Previously, an asymmetric tax outcome could arise when debt was remitted between associated parties, as the borrower could derive taxable income and the lender would be denied a bad debt deduction.

Under the current rules, debt remission income does not arise where the debt remission causes no change in the net wealth of the economic group.

G. Transactions

Removal or restoration expenditure

An immediate deduction for removal or restoration operations is permitted in the year when the expenditure is incurred. It is recognized that these costs generally arise after the well has ceased production. Accordingly, any loss that cannot be offset can be carried back and offset against prior-year profits if necessary (but such carryback is limited to four years).

The Government is currently proposing a refundable tax credit for losses arising for removal or restoration costs, which will replace the existing spread-back provision for petroleum miners. The tax credit will be limited to the amount of tax paid in previous years and the miner's available imputation credits, and will be refunded without prior tax periods being reopened. No time limit will apply for taking into account past tax paid.

Relinquishment of petroleum license

If a petroleum permit or license is relinquished, any deferred deductions that have not been deducted previously are deductible in the year of relinquishment (or otherwise carried back and offset against prior-year profits, once the Income Tax Act 2007 is amended to reflect the previous position under the Income Tax Act 2004).

Disposal of petroleum mining assets

Consideration received by a petroleum miner from the disposal of a petroleum mining asset is assessable income in the year the consideration is derived. Any deferred expenditure not yet deducted is deductible at that time, subject to the rules in the next paragraph in respect of associated person transactions.

If a petroleum mining asset is sold to an associated person, a petroleum miner's deduction for the balance of the deferred expenditure is limited to the amount of assessable income (i.e., consideration) that the person derives from the disposal. This rule prevents a petroleum miner from claiming a loss on disposal by selling the assets below value to an associated person. The balance of any deferred expenditure can be claimed by the associated person if the asset is subsequently sold to a third party.

Use of exploratory well for commercial development

If an exploratory well is subsequently used for commercial production, the "exploratory well expenditure" that has been deducted in respect of that well must be added to the assessable income of the petroleum miner. The expenditure incurred is then treated as a petroleum development expenditure and deducted over seven years on a straight-line or depletion basis.

Dry-well expenses

If a well that has commenced production subsequently becomes dry, the balance of any deferred expenditure is immediately deductible.

Farm-in and farmout

Generally, the farm-in party's contribution to exploration or development work undertaken on a petroleum license area is deductible for the farm-in party according to whether it is a petroleum exploration or development expenditure. The farm-in party's contributions are specifically excluded from being assessable income for the farmout party.

Disposal of petroleum mining shares

The proceeds from the sale of shares in any "controlled petroleum mining entity" are not taxable in New Zealand.

H. Indirect taxes

Import duties

Import duties are payable on the importation of some goods into New Zealand. Import goods and services tax (GST) at 15% may also be payable, but is refundable if the importer is GST-registered.

Temporary import exemptions are available for goods that will be re-exported within 12 months.

Value-added tax (VAT) and GST

GST is imposed under the Goods and Services Tax Act 1985 on the supply of goods and services in New Zealand. The tax is paid (and reclaimed) at each step along the chain of ownership, until the goods or services reach the end user (who cannot reclaim the GST). From an economic perspective, therefore, GST is ultimately paid by the consumer or end-user.

GST is charged at the rate of 15% on goods and services supplied by a registered person. The principal exemptions are for the supply of residential accommodation and financial services. Also, the sale of land or a business as a going concern may be zero-rated for GST purposes (i.e., charged at 0%). Generally, GST is not imposed on goods exported from New Zealand (i.e., they are zero-rated for GST purposes).

The GST that a company pays when purchasing goods and services is called "input tax." Registration enables a company to claim this amount back from the Inland Revenue if the goods and services are purchased for the principal purpose of carrying on a "taxable activity."

The GST that the registered company is liable to charge on the supplies made is called "output tax." The company collects the output tax from the consumer and reports it to the Inland Revenue.

GST registration is compulsory if the total value of goods or services supplied exceeds (or will exceed) NZD60,000 in any 12-month period.

Petroleum mining companies exploring in New Zealand may not make supplies and are therefore not required to register. However, they have the option of voluntarily registering for GST, which then allows them to recover GST charged on supplies received.

Export duties

No duties apply to goods exported from New Zealand. However, a fee may be paid to the exporting company for the documentation necessary for the process of exporting goods.

Stamp duties

No stamp duty applies in New Zealand.

Local authority rates

Local authorities in New Zealand levy so-called "rates" on landowners for the purpose of funding their activities. These "rates" are based on the Government's valuation of the property held. The amount charged varies from district to district.

Climate change emissions trading

New Zealand has a carbon tax on greenhouse gas emissions and also an emissions trading scheme. The emissions trading scheme enables organizations to manage their carbon tax obligations.

I. International tax

Base Erosion and Profit Shifting (BEPS)

The Organisation for Economic Co-operation and Development (OECD) and G20 have been working on a coordinated global solution to address BEPS. BEPS tax strategies allow multinationals to exploit gaps and discrepancies in tax rules to shift their profits to foreign countries where tax rates are lower.

New Zealand is committed to the OECD/G20 initiative on BEPS. A tax bill, introduced to Parliament on 7 December 2017, contains measures intended to prevent multinationals from using:

- Artificially high interest rates on loans from related parties to shift profits out of New Zealand (see Section F above)
- Hybrid mismatch arrangements
- Artificial arrangements to avoid having a taxable presence in New Zealand
- Related-party transactions to shift profits into offshore group members in a manner that does not reflect the actual economic activities undertaken in New Zealand and offshore

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Companies carrying on petroleum operations are deemed to be in the upstream regime and taxed under the Petroleum Profits Tax Act (PPTA) 2004 (as amended). "Petroleum operations" are defined under the PPTA as the winning or obtaining, and the transportation, of chargeable oil in Nigeria by or on behalf of a company for its own account. Petroleum operations include any drilling, mining, extracting or other such operations or processes (not including refining at a refinery) in the course of a business carried on by a company, including all operations incidental thereto and any sale of, or any disposal of, chargeable oil by or on behalf of the company.

Nigeria operates both a licensing and a contractual regime. Under the licensing regime, there are two arrangements. These are the joint ventures between the Federal Government of Nigeria and either an international oil company (IOC) or a sole risk operator (SRO). The contractual regime arrangements involve risk service contracts (RSCs) and the production sharing contracts (PSCs).

Of the four types of arrangement, those involving RSC operators are not deemed to be carrying on petroleum operations but are placed under performance schemes with the Federal Government and are paid as service providers; they are taxed under the Companies Income Tax Act at a far lower rate and not under the PPTA. The Federal Government of Nigeria, under all the arrangements, operates through the Nigerian National Petroleum Company (NNPC).

- Royalties — 0% to 20%
- Bonuses — Yes[1]
- PSC — Yes[2]

Income (profit) tax rate

Under Section 21 of the PPTA (Cap P13) LFN 2004, the rates apply as follows:

- First five years (newcomers) — 65.75%
- First five years (existing companies) — 85%

1 *A company to which a concession has been granted to explore for and produce oil is liable to pay a signature bonus as consideration for the award of the concession. The amount payable is generally fixed at the absolute discretion of the Government and may not be determined in advance.*

2 *The Government share of each PSC is based on production.*

- Subsequent years (all companies) — 85%
- Resource rent tax — yes
- Capital allowances – D[3]
- Investment incentives – L[4]

B. Fiscal regime

Petroleum profit tax

All companies liable to pay petroleum profit tax (PPT) are assessed for tax on a current-year basis. As a result, the accounting period, which should cover the assessable profit, is from 1 January to 31 December of the relevant tax year, except in the year of commencement or cessation of business, when it may be shorter. For a company that is engaged in upstream crude oil operations, its profits for any accounting period are made up of the following:

- The proceeds from sales of all chargeable oil sold by the company in that period
- The value of all chargeable oil disposed of by the company in that period
- All income of the company during that period that is incidental to and arising from any one or more of its petroleum operations

In arriving at the taxable profits of the company, Section 10 of the PPTA provides for deductible expenses to include expenses "wholly, exclusively and necessarily" incurred in obtaining the profits.

To determine the assessable profits of an oil-producing company from its adjusted profits, the law allows all un-recouped losses suffered by the company during any previous accounting periods to be deducted from its adjusted profits. If all the losses cannot be relieved from the adjusted profits in any accounting period (e.g., because there is insufficient profit from which such losses could be offset), the PPTA allows the unrelieved losses to be carried forward to succeeding accounting periods.

Production sharing contracts

PSCs have recently become the vehicle of choice for Nigeria in participating in the exploration of petroleum resources over time, particularly for offshore acreages. A PSC is an agreement between the state oil company, i.e., the NNPC, and any other exploration and production (E&P) company or companies for the purpose of E&P of oil in the deep offshore and inland basins. In Nigeria, the PSC is governed by the Deep Offshore and Inland Basin Production Sharing Contracts Decree No. 9 1999 Act (Cap D3) LFN 2004, amended by the Deep Offshore and Inland Basin Production Sharing Contracts (Amendment) Decree No. 26 1999.

Under a PSC, the contractor funds exploration and production activities and recovers the cost of winning crude oil. A PSC is based on a production split, shared between the parties in agreed proportions. The contractor undertakes the initial exploration risks and recovers its costs if and when oil is discovered in commercial quantities — if no oil is found, the company receives no compensation. Under the PSC, the contractor has the full right to only cost oil (i.e., oil to recoup production costs) and profit oil (i.e., oil to guarantee a return on investment). The contractor can also dispose of tax oil (i.e., oil to defray tax and royalty obligations) on behalf of the NNPC.

The balance of the oil (if any) is shared between the parties. The contractor is subject to a petroleum profits tax at 50% of the chargeable profit.

Resource rent tax

These are annual or periodic charges made in respect of licenses granted under the Petroleum Act. The rent payable is determined as follows:

- NGN5,000 for each square kilometer or part thereof for an oil exploration license (OEL)

3 *D: accelerated depreciation.*

4 *L: losses can be carried forward indefinitely.*

- US$10 for each square kilometer or part thereof for a nonproducing oil mining lease (OML) or an oil prospecting license (OPL)
- US$20 for each square kilometer or part thereof of a producing OML.

Royalty regimes

Any company engaged in upstream oil and gas operations is required to pay royalties in accordance with the provisions of the Petroleum Act and the Petroleum Drilling Regulations 2004. This is usually in the form of monthly cash payments and oil liftings at an agreed percentage of the quantity of oil produced, after making adjustments for treatment, handling and related expenses. The royalty payable is dependent on the concession agreement between the company and the government.

Royalty rates for joint venture operations are as follows:

- Onshore production — 20%
- Production in territorial waters and continental shelf up to 100 meters water depth — 18.5%
- Offshore production beyond 100 meters — 16.67%

The Deep Offshore and Inland Basin Production Sharing Contracts Act specifies the royalty rates that apply to production from PSC fields beyond 200 meters, which are as shown in the next table.

Area	Rate (%)
Up to 200 meters' water depth	16.67%
In areas from 201 to 500 meters' water depth	12%
In areas from 501 to 800 meters' water depth	8%
In areas from 801 to 1,000 meters' water depth	4%
In areas in excess of 1,000 meters' water depth	0%
Inland basin	10%

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Under the PPTA, accounting depreciations are not allowable for tax calculations. Instead, the PPTA gives both petroleum investment allowance (PIA) and annual allowance (AA) to oil-producing companies that have incurred a "qualifying capital expenditure" (QCE). These allowances are allowed against the assessable profit to arrive at the chargeable profits. The relevant tax rate is applied to the chargeable profits to determine the amount of PPT payable.

Petroleum investment allowance

The PIA is an allowance granted to an E&P company in the first year when it incurs QCE for the purpose of its operations. The rates depend on the fiscal regime (contract form) under which the E&P company operates. The following rates apply to companies in joint venture operations.

- Onshore operations — 5%
- Operations in areas up to 100 meters' water depth — 10%
- Operations in areas between 101 meters' and 200 meters' water depth — 15%
- Operations in areas beyond 200 meters' water depth — 20%

Annual allowance

The annual allowance (AA) is an allowance granted annually at a flat rate of 20% on the original cost of an asset, subject to the requirement that the taxpayer retains 1% of the original cost in its books until the asset is finally disposed of. The retention of the 1% cost in the books of the company effectively means that the AA granted for the fifth (and last) year is 19%, rather than the 20% for each of the previous four years. For the ease of reference, the rates of AA are as follows:

- First year — 20%
- Second year — 20%
- Third year — 20%
- Fourth year — 20%
- Fifth year — 19%

The capital allowance for which relief may be claimed in any particular tax year is the sum of any PIA and AA.

QCE is defined as capital expenditures incurred in an accounting year in respect of:

- Plant, machinery and fixtures
- Pipelines and storage tanks
- Construction of buildings, structures or works of a permanent nature
- Acquisition of rights in or over oil deposits; searching for, or discovering and testing, petroleum deposits or winning access thereto; or construction of any work or buildings likely to be of little value when the petroleum operations for which they were constructed cease

No capital allowance is granted for any expenditure that would have been a qualifying expenditure, except in respect of deductions that have been made in arriving at the adjusted profit of the company pursuant to Section 10 of the PPTA.

Investment tax credits or investment tax allowances

A company engaged in petroleum operations in the deep offshore and inland basin, pursuant to a PSC executed in 1993, is allowed an investment tax credit (ITC) at the rate of 50% of the qualifying expenditure, in accordance with the terms of the PSC for the accounting period when the asset was first used for the purpose of its petroleum operations. In the same way, a company that has executed a PSC after 1 July 1998 is entitled to an investment tax allowance (ITA) at a flat rate of 50% of the qualifying expenditure in the accounting year in which the relevant asset is first used in the business.

Restrictions on capital allowances

Under the PPTA, the capital allowance relief that can be claimed is the aggregate capital allowance for the relevant tax year. This, however, is subject to a limitation. Capital allowance relief is limited to the lower of either the aggregate capital allowance computed for the tax year or a sum equal to 85% of the assessable profits of the accounting period, less 170% of the total amount of the deduction allowed as PIA for that period. The purpose of this restriction is to ensure that the tax chargeable to the company is no less than 15% of the tax that would have been chargeable if no deduction had been made for capital allowances.

Unrelieved capital allowances may be carried forward until they are finally relieved.

D. Incentives

In order to encourage the development and utilization of the country's gas resources, the following incentives are available:

- An investment required to separate crude oil and gas from the reservoir into usable products is considered part of the oilfield development.
- A capital investment in facilities equipment to deliver associated gas in a usable form at utilization or the designated custody transfer point is treated, for tax purposes, as part of the capital investment for oil development.
- Capital allowances, operating expenses and the basis for tax assessments are subject to the provisions of the PPTA and the tax incentives under the revised memorandum of understanding.

Conditions for the incentives are as follows:

- Condensates extracted and re-injected into the crude oil stream are treated as oil, but those not re-injected are treated under the existing tax arrangement.
- The company pays the minimum amount charged by the Minister of Petroleum Resources for any gas flared by the company, currently at US$3.50 per thousand standard cubic feet of gas flared. The company must, where practicable, keep the expenses incurred in the utilization of associated gas separate from those incurred in crude oil operations, and only expenses that cannot be separated are allowable against the crude oil income of the company under the Act.
- Expenses identified as incurred exclusively in the utilization of associated gas are regarded as gas expenses and are allowable against the gas income and profit to be taxed under the Companies Income Tax Act.
- Only companies that invest in natural gas liquid extraction facilities to supply gas in usable form to downstream projects — including aluminum smelter and methanol, methyl tertiary-butyl ether and other associated gas utilization projects — benefit from the incentives.
- All capital investments relating to the gas-to-liquids facilities are treated as a chargeable capital allowance and recovered against crude oil income.
- Gas transferred from the natural gas liquid facility to the gas-to-liquids facilities incurs 0% tax and 0% royalty.

The effect of these incentives is to give wider latitude to gas-producing companies on expenditures for which they can claim capital allowance relief.

E. Withholding taxes

Under Nigerian law, certain income is subject to withholding tax (WHT) regulations. Income subject to WHT includes rent, interest, dividends, fees, commissions and payments in respect of contracts. Thus, if a company makes a payment on one of these types of income, the payor company is required by law to deduct WHT from the payment at the applicable rate and remit the sum to the Federal Inland Revenue Service (FIRS) or the State Inland Revenue Service (SIRS). The relevant tax authority issues a receipt for the payment, which is forwarded to the payee as evidence of payment of the WHT on its behalf. However, WHT does not apply to dividends declared from profits that have suffered PPT.

The WHT rates are as follows:

- Interest — 10%
- Royalties — 10%
- Technical services — 10%
- Management services — 10%
- Consultancy services — 10%
- Other contracts for supply of goods and services — 5%
- Branch remittance tax — not applicable

The WHT rates above differ if paid to individuals.

Nigeria has treaty agreements with countries that include Belgium, Canada, China, France, the Netherlands, Pakistan, Philippines, Romania, South Africa and the United Kingdom. These countries are granted a reduced rate of WHT, usually at 75% of the generally applicable WHT rates. Thus, the applicable rate of WHT for treaty countries on interest, dividends and royalties is generally 7.5%. Nigeria also has treaty agreements with Mauritius and South Korea (signed but yet to be ratified) and Italy (air and shipping agreements only). The Federal Government of Nigeria, on 26 January, 2018, ratified the double tax agreement between the Federal Republic of Nigeria and the Kingdom of Spain, making it part of Nigeria's domestic law.

F. Financing considerations

Thin capitalization

A company is thinly capitalized if its capital is made up of a much greater proportion of debt than equity. The tax authorities regard this as a cause for concern, given the potential for abuse through excessive interest deductions. Some tax authorities limit the application of thin capitalization rules to corporate groups with foreign entities to avoid "tax leakage" to lower tax jurisdictions.

Nigeria does not have a specific thin capitalization rule, but it does apply general anti-tax avoidance rules. Under Section 15 of the PPTA 2004,if the tax authorities believe that any disposition is not, in fact, given proper effect, or that any transaction that reduces or would reduce the amount of tax payable is artificial or fictitious, they may disregard the disposition or direct that such adjustments be made in respect of the liability to tax as the authorities consider appropriate to counteract the reduction in the liability to tax, or the reduction that would otherwise apply, resulting from the transaction. The companies concerned are accordingly subject to tax. The expression "disposition" includes any trust, grant, covenant, agreement or arrangement.

As an example of the foregoing, the following transaction is deemed to be artificial or fictitious: a transaction between persons if one of them has control over the other or between persons if both of them are controlled by another person if, in the opinion of the tax authorities, the transaction has not been made at arm's length (i.e., on the terms that might have been fairly expected to be made by independent persons engaged in the same or similar activities dealing with one another at arm's length).

Transfer pricing

The Income Tax (Transfer Pricing) Regulations No 1 of 2012 (the Regulations) were published on 24 September 2012. Prior to the introduction of these regulations, the Nigerian domestic tax laws merely provided general anti-avoidance rules whereby related-party transactions must be conducted at arm's length, and no detailed guidelines on the application of the arm's-length principle were provided. Accordingly, the Regulations were introduced to provide guidance on the application of the arm's length principle.

The commencement date of the Regulations was specified as 2 August 2012. The Regulations define "commencement date" as the basis for periods beginning after the "effective date" of the Regulations, after which taxpayers should comply with the transfer pricing documentation requirements or the submission of the preprinted declaration form along with the taxpayers' annual tax returns. However, the Regulations do not provide further guidance as how "effective date" is defined.

The Regulations are to be applied in a manner consistent with the arm's-length principle in Article 9 of the United Nations and Organisation for Economic Co-operation and Development (OECD) Model Tax Conventions on Income and Capital and the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD Guidelines). The Regulations further provide that the provisions of the relevant tax laws shall prevail in the event of conflict in the application of any applicable law, rules or regulations, the UN Practical Manual or the OECD Guidelines. The documentation should be provided to the Revenue within 21 days, upon request.

PSC expenditure recovery exclusions for financing costs

All the expenses incurred for exploration activities prior to the effective date of the PSC are operating costs recoverable by the contractor from cost oil.

Alternative funding arrangement in petroleum operations

This is an arrangement in which the international oil companies in joint venture (JV) arrangements agree to fund all the capital costs of a project, whereby no cash call is made upon NNPC for its own equity participation. NNPC pays back its share of the capital costs through allocation of additional crude oil produced. NNPC in this arrangement is termed the carried partner while the IOC is called the carrying partner.

The Federal Government has disclosed that it has formally exited the JV cash calls arrangements it has had with the international oil companies operating in the country and has signed an agreement to exit the cash call policy with the major international oil and gas companies operating in Nigeria. The Federal Government of Nigeria has concluded on the arrangement to settle the IOCs with the sum of US$5billion for the JV cash calls debts it owed between 2010 and 2015. NNPC has moved to enter into agreements with the IOCs with a view to settling the indebtedness over the next five years. The US$5billion payments will be made in the form of barrels of new crude production in excess of a particular threshold over the next five years. This, in effect, means that the IOCs would not receive any cash but perhaps recover something through NNPC effectively under-lifting its share of crude oil over the next five years.

G. Transactions

Asset disposals

If a company disposes of a capital asset, capital gains accruing from the disposal are subject to tax under the Capital Gains Tax Act 2004 at the rate of 10%. The amount of capital gains is calculated after deducting expenses associated with the disposal of the assets. A company may claim rollover relief, and therefore postpone the tax liability, if the proceeds from the disposal are used to acquire an asset similar in nature to the one disposed of.

Farm-in and farmout

The Nigerian Petroleum (Amendment) Decree 1996 (Decree No. 23) provides that "farmout" means "an agreement between the holder of an oil mining lease and a third party which permits the third party to explore, prospect, win, work and carry away any petroleum encountered in a specified area during the validity of the lease." Farming in is, therefore, a way of acquiring a license interest, and, conversely, farming out is a way of disposing of a license interest while allowing the farmor to benefit from income generated from the farmee's activities within the area that has been farmed out. The terms "license interest" and "concession interest" are used in this chapter to include the bundle of rights owned by a participant in an oil or gas JV.

Selling shares in a company

The sale of shares does not attract capital gains tax (CGT) for resident and nonresident shareholders. A minimal stamp duty applies to the share transfer of documents. It is important to note that sales of interests in assets attract CGT. The consent of the Minister of Petroleum Resources is required for the transfer of interest in licenses and controlling shares in an oil and gas company.

H. Indirect taxes

Import duties

Generally, customs duties are payable on various goods, including plant, machinery and all equipment according to the provisions of the Customs, Excise Tariff (Consolidation) Act 2004.

The act provides that any machinery, equipment or spare part imported into Nigeria by a company engaged in exploration, processing or power generation through utilization of Nigerian oil and gas is exempt from customs duties. Unlike the value-added tax (VAT) exemption (see below), the benefit for customs duty relief may be claimed by a company engaged in the upstream or downstream sector of the oil industry.

VAT

Under the Value Added Tax Act 2004, VAT is imposed at the rate of 5% on the supply of all goods and services, except the supply of any goods and services that have been exempted specifically under the act. Taxable supplies include the sale, hire, lease and any other disposal of taxable goods. VAT charged by vendors in the oil and gas industry is deducted at source and remitted to the FIRS.

VAT incentive for gas businesses

VAT is not payable on the supply of plant, machinery and equipment imported or purchased locally for utilization of gas businesses in downstream petroleum operations. In addition, VAT is not payable on supplies of exported goods and services, including oil and gas products.

The following transactions are placed on a zero rate in line with the Value Added Tax Act 2007 (as amended):

- Non-oil exports
- Goods and services purchased by diplomats
- Goods purchased for use in humanitarian donor projects

By virtue of the 2007 amendment to the VAT Act and guidelines, oil and gas companies are required to deduct VAT at source and remit the amount directly to the relevant VAT authority.

I. Other

Tertiary education tax

A tertiary education tax is assessed alongside the PPT or income tax liability of a company. Tertiary education tax is assessed at 2% of the assessable profits of a company. For a company subject to tax under the PPTA, the tertiary education tax paid is an allowable deduction under Section 10 of the PPTA in arriving at the adjusted profits of the company for tax purposes.

Appointment of third-party consultants for FIRS tax audit exercise

As part of the measures to achieve the revenue projections for the year 2016 and beyond, the FIRS has engaged the services of consulting firms to carry out tax audit/investigation exercises on corporate taxpayers in Nigeria in order to boost tax collection. Although the role of these consulting firms does not include the actual assessment of tax, which statutorily remains the function of the FIRS, the consultants will assist to collate relevant information during the tax audit and investigation exercises. This engagement of tax consulting firms is statutorily backed by Section 12(4) of the Federal Inland Revenue Service Establishment Act, which provides that the FIRS may appoint and employ such tax consultants or accountants and agents to transact any business or to do any act required to be transacted or done in the execution of its functions under the Act.

Oil terminal dues

Subject to the provisions of the Oil Terminal Dues Act and the Nigerian Ports Authority Act (the NPA Act), Section 1 of the Oil Terminal Dues Act stipulates that terminal dues may be levied on any ship evacuating oil at any oil terminal and in respect of any services or facilities provided under that Act. Under the Oil Terminal (Terminal Dues) Regulations, the amount payable as terminal dues is US$0.02 per barrel of oil loaded onto a ship.

Pursuant to the NPA Act, the Port Authority has the power to levy harbor dues on any ship. The harbor dues levied apply to all goods discharged or loaded within a harbor. The rate for a cargo of crude oil as specified under the NPA Act (Terminal Dues) Regulations is NGN0.1166 per ton.

Oil pipeline license fees

If a company seeks to construct and operate an oil pipeline for transportation of mineral oil or natural gas to any destination, it must obtain a license from the relevant authority. The application for a license and the granting of a license attract separate fees under the Oil Pipelines Act. Annual fees, chargeable in accordance with the length of the pipelines are also payable.

The application is made to the Minister of Petroleum Resources through the Department of Petroleum Resources. The fees are as follows:

- Application for permit — NGN20 on submission
- Grant of permit — NGN50
- Application for license — NGN50 on submission of application
- Grant of license — NGN200
- Variation of permit — NGN50
- Variation of license — NGN200
- Annual fee on each license — NGN20 per mile of pipeline, subject to a minimum of NGN200

The holder of a license is required to pay a fee of NGN100 upon submitting its application for an order restricting anyone from constructing any building or type of building or similar structures on lands adjoining pipelines. A maximum fee of NGN400 is payable upon the grant of this order.

State and local government rates

The Taxes and Levies (Approved List for Collection) Cap T2, Laws of the Federation 2004 sets out the various taxes and levies that may be collected by the three tiers of government in Nigeria. By virtue of the provisions of Section 10 of the PPTA, all these rates and levies are allowable as deductions in arriving at the adjusted profits of a company subject to tax under the PPTA. Some of the local taxes that may apply to oil and gas businesses are discussed below.

State government business registration fees

For a business located in an urban area, the maximum fee payable on registration is NGN10,000, while NGN5,000 is the maximum payable upon annual renewal of the registration. For a business located in a rural area, the maximum fees are NGN2,000 and NGN1,000 for initial registration and renewal, respectively.

Right of occupancy fees

Right of occupancy fees apply on lands in urban areas of a state. The rates vary from state to state.

Local government

Tenement rates

"Tenement rates" are rates chargeable on a building and payable by the occupier(s) of the building. The various state governments have enacted statutes under which tenement rates are imposed. The actual collection of the rates is done by the local authority for the area where the relevant building is situated. The tenement rate is usually assessed on the rental value of a building. In Lagos State, for example, the tenement rate has been subsumed into the Land Use Charge (LUC). For example, the LUC rates to be applied on owner-occupied residential property in Lagos State is 0.076% per annum of the Assessed Property Value.

Signboard and advertisement permits

The rate for a signboard and advertisement permit varies between different local governments.

Oil and Gas Export Processing Zone

Under the Oil and Gas Export Free Zone Act 2004, any approved enterprise established within Onne, the Oil and Gas Export Processing Zone, is exempted from all taxes, levies and rates imposed by the federal, state or local governments in Nigeria.

Service company taxation

Pursuant to the Companies Income Tax (Amendment) Act 2007, services companies are taxed at a rate of 30%, in addition to the 2% tertiary education tax assessed on the assessable profit of all Nigerian companies.

A deduction is available for capital allowances, as shown in the table below.

	Table I: Initial allowances	Table II: Annual allowances	Rate %	Rate %
Building (industrial and non-industrial)	15	10		
Mining	95	0		
Plant: agricultural production	95	0		
Others	50	25		
Furniture and fittings	25	20		
Motor vehicles: public transportation	95	0		
Others	50	25		
Plantation equipment	95	0		
Housing estate	50	25		
Ranching and plantation	30	50		
Research and development	95	0		

Interim dividends tax provision

A public notice issued by FIRS requires any company paying interim dividends to its shareholders to pay the company's income tax at 30% to the FIRS prior to the payment of the dividend, in line with S.43(6) of the Companies Income Tax Act. The tax paid will serve as deposit/advance against the company's income tax due on the profits of the company from which the dividend was paid. As stated in the public notice, the FIRS has stated to carry out random compliance checks and apply penalties and interests on all erring companies from the date of default.

Taxation of nonresident companies (NRC)

Commencing from the tax year 2014, FIRS demands that the income tax returns for NRC be prepared and filed on an actual profit basis against the traditional deemed-income approach. Essentially, if the actual profit basis is adopted for the preparation of the company's income tax returns, the NRC is usually allowed to deduct for income tax purposes expenses that are wholly, reasonably, exclusively and necessarily incurred for its business operations in Nigeria. However, for the deemed-profit basis of income tax computations, the NRC is not allowed to set off against the turnover such expenses incurred.

The Petroleum Industry Bill

The Petroleum Industry Governance Bill (PIGB) is the latest of the institutionalized reforms within the Nigerian oil and gas industry (the Industry), and a more cautious approach toward ultimately achieving the initial goals of the Petroleum Industry Bill (PIB), which was first introduced in 2008.

The PIB has been split into four bills: the PIGB, the Fiscal Regime Bill, the Upstream and Midstream Administration Bill, and the Petroleum Revenue Bill. The PIGB is the only bill that is currently in circulation at the National Assembly. The PIGB proposes to establish the Nigerian Petroleum Regulatory Commission (the Commission), as a one-stop shop Industry regulator that will be responsible for licensing, monitoring and supervising petroleum operations, as well as enforcing Industry laws, regulations and standards.

Under the PIGB, the portfolio of NNPC will be reorganized. To achieve this, the PIGB will establish three principal commercial entities: the Ministry of Petroleum Incorporated (MOPI), the NPC, and the Nigerian Petroleum Assets Management Company (NPAMC). It remains to be seen when this will be passed into law by the National Assembly.

The Senate passed the PIGB in May 2017 with the concurrent assent of the House of Representatives received on 18 January 2018. Following this, the PIGB has now been passed by the National Assembly and awaiting the President's assent. Essentially, the PIGB deals strictly with the corporate and governance structures of the petroleum industry, as they relate to state-owned operators in the sector.

Nigerian Oil and Gas Industry Content Act 2010 (NOGIC Act)

The Nigerian Oil and Gas Content Act 2010 (commonly known as the NOGIC Act) was signed into law on 22 April 2010 and effective from this date. The NOGIC Act is the legal framework and mechanism for the creation of an environment aimed at increasing indigenous capacity building. The implementation of the provisions is to be carried out by the Nigerian Content Monitoring Board. Every entity awarding a contract in the upstream sector of the Industry should deduct and remit 1% to the National Content Development Fund. The 1% mandatory deduction is not applicable to contractual arrangements executed prior to 22 April 2010 even if ongoing after that date. The 1% mandatory deduction applies to all contracts of any nature in the upstream sector and without any minimum limits.

IFRS conversion

The International Financial Reporting Standards (IFRS) conversion road map, which is in three phases, mandates publicly listed and significant public-interest entities to have prepared their financial statements based on IFRS by 1 January 2012 — i.e., full IFRS financial statements are required by such entities for the accounting period to 31 December 2012 and thereafter. Other public interest entities are required to have adopted IFRS for statutory purposes by 1 January 2013. The third phase requires small and medium-sized entities to have adopted IFRS by 1 January 2014.

The 2018 Budget of Consolidation

The 2018 budget is projected at a crude oil benchmark price of US$45 per barrel at an exchange rate of NGN305 to a dollar and an estimated 2.3 million barrels per day as against US$44 per barrel under the 2017 budget.

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

- Royalties – none
- Bonuses – none
- Production sharing contracts (PSCs) – none
- Income tax rate – 23%
- Resource rent tax – 55%
- Capital allowances – O, E[1]
- Investment incentives – L[2]

B. Fiscal regime

A company involved in extractive (i.e., upstream) activities within the geographic areas described in Section 1 of the Norwegian Petroleum Tax Act is subject to a marginal tax rate of 78% (23% ordinary corporate income tax and 55% resource rent tax) on the net operating profits derived from its extractive activities. The area covered, generally, is the area within Norwegian territorial borders or on the Norwegian continental shelf (NCS).

The tax basis for calculating taxes on extractive activities is essentially the same as for ordinary taxes except for the treatment of interest costs and uplift allowances. Overall tax rates are as shown in the table below.

	Oil and gas companies (offshore tax regime)	Other companies (onshore tax regime)
Ordinary tax	23%	23%
Special tax	55%	None
Total tax	78%	23%

1 *O, E: offshore investments are depreciated over six years. An additional 21.2% uplift applies against the special (resource rent) tax for upstream activities (5.3% for four years).*

2 *L: losses from offshore activities may be carried forward indefinitely with interest.*

Transportation and extractive activities (including related activities) performed outside Norwegian territorial borders may be subject to Norwegian tax if the Norwegian authorities have the right to impose tax on these activities under international law or bilateral agreements.[3]

The Norwegian petroleum tax system is based on the taxation of the entity, rather than on specific assets and licenses. Thus, there is no ring fencing between different licenses or fields on the NCS.

Income derived from offshore activities, in principle, may not be offset against losses incurred from onshore activities, or vice versa. However, 50% of a company's onshore losses may be offset against income from offshore activities that are subject to the ordinary tax rate of 23%. Similarly, losses from offshore activities may be offset against income from onshore activities that are subject to the ordinary tax rate of 23%.

See Sections C and D for an explanation of the treatment of both exploration costs and development costs. See Section F for an explanation of the allocation of interest costs between onshore and offshore activities.

Group relief

Norway does not have a "group taxation" regulation. However, under Section 10-4 of the General Tax Act, if a company holds more than 90% of the shares in a subsidiary, each entity may contribute profits to the other company to offset losses incurred by the other company.

With respect to oil and gas companies, such contributions are limited to distributions from onshore activities; for instance, an upstream company with onshore income, such as interest income or foreign-exchange gains, may contribute this income to its more than 90%-owned subsidiary to offset any losses from onshore activities incurred by that entity.

Norm price

A "norm price" or administratively determined price is used to calculate the taxable income derived from the sale of petroleum products (currently only crude oil and propane from Karsto), regardless of the actual sales price obtained. If the sales price achieved is higher than the norm price, the additional amount is tax-free. Correspondingly, if the price achieved is lower than the norm price, the seller is still taxed at the norm price. The norm price is published quarterly and is based on actual prices obtained, although the Norm Price Board sets the norm price for crude oil from each field or blend on a daily basis (for each lifting day).

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

For taxable income subject to a marginal tax of 78%, investments in offshore production facilities, pipelines and installations (tangible assets) used in extraction activity are depreciated over a six-year period beginning with the year of investment.

Additional allowances are permitted at a rate of 21.2% when calculating the special tax basis for the 55% tax rate (i.e., 5.3% each year over a four-year period). This means that 89.66% (i.e., 55% + 23% + [21.2% × 55%]) of offshore investments are nominally borne by the Government.

Other investments and assets located onshore (e.g., buildings and office equipment) used in the upstream business are depreciated on a declining-balance method (from 2% to 30%) from when the assets are utilized; however, depreciation from such investments or assets is deductible in the offshore regime at a marginal tax rate of 78%.

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3 *See the Petroleum Tax Act, Section 1.*

D. Incentives

Losses may be carried forward indefinitely for offshore activity. Interest on such losses is set by the Ministry of Finance annually; for 2017, the rate was 0.7%.

In addition, losses can be transferred in connection with the sale of the total activity or by a merger with another "upstream" company. The tax value of the losses can be refunded when the extraction activity on the NCS ceases. These rules apply for losses incurred effective from 1 January 2002 and for cessation of petroleum activity after 1 January 2005. Thus, a company subject to the offshore tax regime is guaranteed full tax deduction or refund of all costs incurred.

An upstream company may also be refunded the tax value of exploration expenses for each tax year loss, including direct and indirect expenses related to exploration activities on the NCS (except for financing costs). The refund is limited to the tax loss incurred for the year. The refund is made within three weeks after the issuance of the final tax assessment (which should be no later than 1 December) in the year following the tax year for which the expenses were incurred. For example, NOK100 million spent on exploration expenses in 2018 would be expected to result in a cash refund of NOK78 million no later than within three weeks after 1 December 2019. This is regardless of whether drilling is successful or not.

The refund of exploration costs has opened up the opportunity for third parties to fund exploration activities. The claim on the state can also be pledged. In general, banks may typically be willing to fund 80% to 90% of the tax value of the exploration tax refund (i.e., 65% to 70% of the exploration-cost basis).

E. Withholding taxes

Withholding tax (WHT) is not levied on distributions from income subject to petroleum taxation, provided the recipient owns at least 25% of the distributing entity. However, any onshore income part may be subject to a prorated dividend WHT, depending on the tax treaty status of the recipient.

Dividend distributions from onshore activity are not subject to WHT if (i) the shareholder is a company resident within the European Economic Area (EEA), (ii) the shareholder performs economic activity through an establishment in the EEA and (iii) Norway has entered into an agreement concerning the exchange of such information or the shareholder can provide such documentation from the tax authorities.

If the receiving company is situated outside the EU/EEA, WHT may be levied on dividend distributions pending if further conditions are met.

F. Financing considerations

Thin capitalization

There are no explicit or fixed thin capitalization rules.

However, if a company has entered into an internal funding agreement, the company may risk a discretionary deviation if the rates and terms agreed are not in compliance with the arm's-length principle (i.e., if the company exceeded its loan capacity compared with what it would have been able to obtain in the free market on a stand-alone basis). Also, under Norwegian company law, a limited company must, as a general rule, have a reasonable equity and liquidity to make dividend distributions.

Only a portion of interest costs (and related foreign exchange) is deductible in the offshore tax regime and total of 78% tax. The remaining interest costs are subject to onshore taxation at the ordinary 23% tax rate.

The allocation of interest cost to the offshore district is calculated as follows:

$$\textbf{Allocation of offshore interest cost} = \frac{\textbf{(Total interest and forex related to interest bearing debt)} \times \textbf{50\%} \times \textbf{remaining tax balances of offshore-related assets at year-end}}{\textbf{Daily average interest-bearing debt}}$$

If the company has no investments or assets, all interest costs and related foreign-exchange costs are allocated onshore. However, if the company has no other onshore income, the financial costs may be allocated back to the offshore regime for deduction against the 23% corporate tax rate (and it may be carried forward with interest). The maximum amount of interest costs that are deductible in relation to an offshore activity is the company's total interest cost incurred.

G. Transactions

Asset disposals

In general, any gain on disposal of assets is taxable or deductible at a marginal tax rate of 78%.

Transfer of license interests (Section 10 ruling)

All transfers of production licenses (including farm-ins and farmouts) require approval from the Ministry of Petroleum and Energy. The tax treatment must be approved by the Ministry of Finance. If the respective transaction is covered by the detailed regulations introduced in 2009, approval from the Ministry of Finance is granted automatically.

If the transaction is not covered by the detailed regulations, an explicit application for a Section 10 ruling has to be submitted to the Ministry of Finance.

The standard conditions in a license sale/transfer include:

- License sales are treated as nontaxable for the seller and as nondeductible for the buyer (i.e., "after-tax" basis).
- The buyer inherits the seller's basis for depreciation and uplift.
- All other costs or income (refunds) follow the ordinary rules.

Reference is made to the Section 10 guidelines issued by the Ministry of Finance on 1 July 2009, with subsequent updates.

H. Indirect taxes

VAT

Suppliers of goods and specific services to drilling companies, license owners, owners and lessees of platforms, and foreign companies that are not liable to register for VAT in Norway are exempt from VAT provided certain requirements are fulfilled. The repair, building and maintenance of rigs and specialized vessels for use in petroleum activities outside Norwegian territorial waters are exempt from VAT when invoiced to the end user. The exemption for the supply of services applies regardless of whether the services are performed offshore or onshore, provided the services rendered are related to installations or equipment on these installations, for use in petroleum activities outside Norwegian territorial waters. Certain documentation requirements must be maintained to comply with the rules.

Transportation between offshore facilities outside Norwegian territorial waters and onshore is also exempt from VAT.

Further, pursuant to the Norwegian export regulations, the supply of services "entirely for use outside Norwegian territorial waters" is regarded as an export and consequently exempt from VAT. The export of goods to the NCS is also exempt from VAT, provided that the goods are exported directly by the supplier, and the supplier can prove the export. The export regulations apply regardless of who the purchaser is and will therefore (for example) also apply on sales to oil service companies registered for VAT in Norway.

Please note specific rules apply for export supply of intangible services (services that can be delivered from a remote location). Intangible services are always regarded as exported and are consequently VAT-exempt if the purchaser is established outside of Norway.

Environmental taxes

Upstream companies are subject to CO_2 tax, which is levied on gas consumed or flared on production installations offshore. The CO_2 tax for upstream companies is NOK1.06 per standard cubic meter (Sm^3) effective from 1 January 2018.

From 1 September 2010, CO_2 tax was introduced on natural gas and liquefied petroleum gas (LPG) in Norway. The tax applies on importation, including importation from offshore production installations and upon withdrawal from a warehouse. The rate in 2018 is NOK1.00 per Sm^3 for natural gas and NOK1.50 per liter for LPG.

A fee of NOK21.94 per kilogram per date is levied on NOx emissions for 2018. However, the Norwegian Oil Industry Association and several other industry associations reached an agreement with the Ministry of Environment in 2008 to establish a fund to reduce NOx emissions. Participating companies must commit to emission reductions, and a fee equal to approximately NOK12 per kilogram must be paid to the fund. A tax deduction of 78% is granted when the payment is made.

Subsequently, any contribution from the fund will be regarded as taxable income when the contribution is made.

The Ministry of Environment and the industry associations agreed in 2017 to extend the NOx fund cooperation for seven years and further reduce emissions in the period of 2018 to 2025.

Area fees

All production licenses are subject to an area fee that is paid after the initial exploration period has expired. The exploration period is normally four to six years. The annual area fee increases from NOK34,000 per square kilometer in year one to a maximum of NOK137,000 per square kilometer in year three and thereafter. Special rules and exceptions apply for continued exploration activities beyond the initial period.

I. Other

Tax returns and tax assessment

Companies involved in extraction activities must calculate and pay advanced tax. The first three installments are due on 1 August, 1 October and 1 December in the year of income. The remaining three installments are due on 1 February, 1 April and 1 June in the following year.

The tax return is due on 30 April in the year following the year of income. A draft assessment from the Oil Taxation Office is available from mid-November, and the final assessment is published no later than 1 December. The taxpayer has six weeks from this day to file a complaint to the appeal board for special taxes.

The tax exploration refund is made three weeks after the publishing of the tax assessment no later than 1 December.

Transfer pricing reporting and documentation requirements

The Norwegian tax authorities have increased their focus on intragroup transactions and transfer pricing-related topics with the recent introduction of transfer pricing reporting and documentation obligations. Any legal entity that is obliged to file a tax return in Norway and has transactions with related parties is covered by the reporting and documentation requirements.

A company involved in extraction activities and subject to the PTA is exempt from only the reporting obligation (and subsequently the transfer pricing documentation obligation), provided that the total transactions are less than NOK10 million during the year and less than NOK25 million in receivables or debts at the end of the year (real values are based on arm's-length principles).

These reporting obligations require a standard form to be filed with the tax return. The purpose of this reporting form is to give the tax authorities an overview of the extent and nature of the taxpayer's intragroup transactions. The oil tax authorities can and will also often request documentation to demonstrate that intragroup transactions are in compliance with the arm's-length principle, as outlined in the Organisation for Economic Co-operation and Development (OECD) Guidelines. The deadline for this documentation is 45 days from the date of the request.

Norwegian authorities tend to have an aggressive approach when reviewing these reports. Even if the Norwegian documentation requirements are based on the OECD Guidelines, the interpretation and implementation requirements may differ slightly from other countries' practices.

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Tax regime applied to this country

- ■ **Concession**
  - □ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ■ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies in Oman to the oil and gas exploration and production industry sector consists of corporate income tax (CIT) in accordance with the production sharing contract (PSC) arrangement. The main elements are as follows:

- PSC — concession agreement on profit oil after allocating cost oil
- CIT rate — 55% (see also Section B)
- Royalties — not applicable
- Bonuses — applicable for PSC contracts only
- Resource rent tax — not applicable
- Capital allowances — specific depreciation rates for specific types of assets, but not applicable for PSCs
- Investment incentives — dependent on the concession agreement

B. Fiscal regime

Corporate income tax

Oil and gas exploration and production companies are taxed at the rate of 55% on their taxable income. Taxable income is determined in accordance with the concession agreement to which the PSC applies. PSC arrangements generally involve a series of elements, as follows:

- Expenditures for exploration, production and related activities are fully funded by the company (concession holder) (i.e., the Government does not fund any of that activity).
- The Government shares in production.
- Production sharing depends on production for the period, valued at prices determined by the Government.
- From the production for the period, cost oil is first determined. Cost oil is a portion of produced oil that the operator applies on an annual basis to recover defined costs under the relevant production sharing agreement. Depending on the PSC, there may be a cap on the recovery of cost oil as a percentage of the total production for a year. However, if the cost oil required to recover costs fully is more than the maximum cap allowed, cost oil is as set out under the PSC. The remaining cost is carried forward for future recovery. The remaining oil (i.e., after allocating cost oil) is profit oil.

Profit oil is shared between the company and the Government in accordance with the sharing percentage agreed in the concession agreement. The Government generally takes a major share of the profit oil.

- The PSC does not involve royalty payments.
- The following payments may be made to the Government under a PSC, depending on the terms agreed in the concession agreement:
  - Annual rental payments
  - Signature bonus upon signing of the agreement
  - Renewal bonus upon each renewal of the agreement
  - A one-time discovery bonus upon declaration of the first commercial discovery of oil or gas
  - A one-time anniversary bonus after the first anniversary of commercial production
- Certain expenditures qualify for cost recovery. Generally, a PSC requires that costs and expenses of activities carried out by the company or its affiliates (i.e., operating expense (opex) and capital expenditure (capex)) are to be included in recoverable costs only to the extent that such costs and expenses are directly or indirectly identifiable with such activities, and they should be limited to the actual costs that are fair and reasonable. Certain costs are specifically prohibited for cost recovery. Excluded costs are bonus and rental payments made by the company to the Government in accordance with the PSC, the company's Omani income taxes paid in accordance with the PSC, foreign income taxes, or other foreign taxes paid by the company, etc.
- A tax rate of 55% applies to taxable income, which is computed in accordance with the formula set out in the PSC. Taxable income is arrived at by applying the following formula:

  TI = NI + (55% × TI)

  Where TI = taxable income and NI = net income determined as the market value of oil or gas lifted by the company, less recoverable costs.
- The Government settles the company's tax liability from the Government's share of production. This implies that the company is not required to settle taxes and claim reimbursement. The share of profit oil by the company is considered net of taxes. The tax authorities issue a tax receipt and a tax certificate for the taxes settled on behalf of the company.

Service contracts

Service contracts are taxed at 15% from the tax year starting on or after 1 January 2017.

Pursuant to RD 9/2017 the corporate income tax rate was increased from 12% to 15% (along with the removal of statutory deduction of OMR30,000 (US$78,000). As per RD 9/2017, this amendment shall be effective for tax years starting on or after 1 January 2017.

Resource rent tax

Resource rent tax does not currently apply in Oman.

Bonuses

Bonuses apply to PSCs only, as explained above.

Royalty regimes

Royalty regimes do not currently apply in Oman.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

The tax law provides specific depreciation rates for particular types of assets — for example, pipelines are to be depreciated at 10% and vehicles and heavy equipment at 33.33%.

However, capital allowances do not apply in respect of PSCs because the entire capital expenditure qualifies as recoverable cost in accordance with the concession agreement.

D. Investment incentives

All incentives, such as tax holidays and R&D uplift, are dependent on the concession agreement. Currently, there are no PSCs that qualify for a tax holiday.

Losses may be carried forward for five years but may not be carried back. Net losses incurred by companies benefiting from tax holidays may be carried forward without any time limit under certain circumstances. Loss carryforwards do not apply to PSCs because the entire cost is carried forward for future recovery (as outlined in Section B above).

E. Withholding tax and double tax treaties

The following payments made to foreign persons not having permanent establishments (PEs) in Oman are subject to a final withholding tax (WHT) at the rate of 10%:

- Royalties
- Consideration for R&D
- Consideration for use or right to use computer software
- Management fees or performance of services
- Interest
- Dividends

Amendments issued by the Royal Decree 9/2017 in February 2017 have expanded the WHT base to include interest, dividend and performance of services. These changes are effective from 27 February 2017. The Income Tax Law does not define what constitutes a "service." However, based on clarification issued by the Secretariat General for Taxation (SGT), with an exception to trading of tangible goods, everything else qualifies as service. The SGT has also stated that WHT on dividends will apply to dividends from only publicly listed shares. Government ministerial institutions and other bodies are now required to deduct WHT when making payments as set out above.

WHT is also applicable if a foreign company has a PE but the PE does not account for income in Oman that is subject to WHT.

WHT is final, and foreign companies have no filing or other obligations in this regard.

The term "royalty" is defined to include payments for the use or right to use software, intellectual property rights, patents, trademarks, drawings, equipment rentals and consideration for information concerning industrial, commercial or scientific experience, and concessions involving minerals. WHT of 10% on royalties under Omani domestic law generally applies to royalties paid to companies resident in most treaty countries. Under the Mauritius treaty, no WHT is imposed on royalties paid to a company resident in that country, subject to the satisfaction of certain conditions. Certain treaty countries, such as China, the UK, France, the Netherlands, South Korea, Switzerland, Singapore and South Africa, provide reduced rates of WHT on royalties, subject to satisfaction of certain conditions.

Oman has entered into double tax treaties with Algeria, Belarus, Brunei, Canada, China, Croatia, France, India, Italy, Iran, Japan, Lebanon, Mauritius, Moldova, Morocco, the Netherlands, Pakistan, Seychelles, Singapore, Spain, South Africa, South Korea, Switzerland, Syria, Thailand, Tunisia, Turkey, Uzbekistan, the United Kingdom, Vietnam and Yemen.

Oman has also signed double tax treaties with Algeria, Belgium, Egypt, Germany, Hungary, Portugal, the Russian Federation and Sudan, but these treaties are not yet in force.

Oman has ratified a free trade agreement with the United States, effective from 1 January 2009. The Gulf Cooperation Council (GCC) countries (of which Oman is one) have entered into a free trade agreement with Singapore but this agreement has not yet been ratified by Oman. Double tax treaties mentioned above should be referred to in order to determine whether relief, if any, is available on WHT mentioned in Section E above.

F. Financing considerations

Thin capitalization

The following deductions are subject to thin capitalization restrictions:

- Interest paid to a sole proprietor or another person controlled by a sole proprietor
- Interest payable by an Omani company (other than banks and insurance companies)
- Interest paid by a PE to a head office or controlled entity

Rules for deduction of interest on loans

- Interest expense must be real and incurred and relate to earning gross income and not financing or capitalization of the business.
- Omani companies claiming deductions of interest costs on loans from related parties are required to comply with minimum capital requirements — i.e., the thin capitalization rules. Omani companies that exceed a debt-to-equity ratio of 2:1 will be subject to a proportionate disallowance of deductions for interest expenses on loans from related parties.
- Interest expenses incurred by branch offices are deductible only if the interest-bearing loan is actually borrowed by the head office from a third-party lender or bank for the specific benefit of the Oman branch and is used by that branch for financing working capital.

In addition, individual PSCs may contain rules regarding deductibility of interest cost.

G. Transactions

Expenditure that qualifies for cost recovery (opex and capex) is explained in Section B. Other major transactions are explained below.

Asset disposals

Under the PSC, if the assets that qualify for cost recovery are sold, the proceeds are remitted to the Government (i.e., they are considered to be the Government's assets). A balancing charge or allowance does not apply.

Relinquishment

Generally, a PSC requires a specified percentage of the stake held by a company to be relinquished from time to time. For example, the PSC may state that the company should relinquish from time to time its stake in the contract in order to retain no more than 50% of the original contract area by a certain date. A PSC also allows a company to relinquish all or any part of the contract area at any time, as long as the company fulfills its obligations under the contract.

H. Indirect taxes

Customs duty is the only indirect tax imposed in Oman.

Customs duty

The Government of the Sultanate of Oman, as a member of the GCC, follows the Unified Customs Act across the GCC; the uniform customs duty of 5% applies on all imports. This means that any goods that come into a port of entry of a GCC member state that have been subjected to customs duty in that state are not subjected to customs duty again if the goods are transferred to another GCC member state.

An exemption or reimbursement of customs duty will depend on the wording of the PSC.

VAT

As of 1 January 2018, the United Arab Emirates and the Kingdom of Saudi Arabia went live with value-added tax (VAT), and the remaining GCC states are expected to go live with VAT by early 2019. In Oman, the Shura Council has approved the GCC Framework Agreement, which provides the general provisions of the VAT regulation.

Currently, there is no VAT in Oman.

Registration fees

Registration fees are payable to various ministries.

Municipality and other taxes

Oman does not impose estate tax, gift tax or dividends tax. Municipalities may impose certain consumption taxes, including tax on the income categories outlined below:

- Hotel and restaurant bills — 5%
- Hotels, motels and tourism restaurants — 4%
- Tax at a rate of 2% on electricity bills exceeding OMR50 per month
- Tax at a rate of 3% on lease agreements, payable by landlords

In addition, a border toll is levied on all vehicles that cross the Oman border at any points of entry.

I. Other

Payroll taxes and employee benefits

The Social Security Law (Royal Decree No. 72 of 1991 as amended) introduced a system of social security to insure employees against old age, disability, death and occupational injuries and diseases. The law currently applies exclusively to Omanis working in the private sector.

Under the law, private sector employers must make monthly contributions to the Public Authority for Social Insurance at a rate of 10.5% of each Omani employee's monthly wage; employees contribute at a rate of 7% of their monthly wages. Employers contribute an additional 1% of each Omani employee's monthly wage as security against occupational injuries and diseases. The government contributes 5.5% of each Omani employee's monthly wage. The Public Authority for Social Insurance invests all funds received, and it pays out sums due to employees upon their retirement and as compensation for injuries and diseases.

In accordance with the Labor Law (Royal Decree No. 35 of 2003 as amended), employers must pay an end-of-service benefit (ESB) to their foreign employees. The ESB is calculated on an employee's final wage and paid according to the following guidelines:

- For the first three years of service, an equivalent of 15 days' basic pay for each year worked
- For each subsequent year, the equivalent of one month's basic pay

Special requirements for foreign nationals

An employer must make biannual contribution of OMR300 toward the vocational training levy for each non-Omani employee.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies to the petroleum industry in Pakistan consists of a combination of corporate income tax (CIT), a windfall levy and royalties in respect of the exploration license. In summary, we have:

- Royalties — 12.5%
- Bonuses — varied amounts, linked with the level of commercial production
- Production-sharing contract (PSC) — applies only to offshore operations, on a sliding-scale basis
- Income tax rate — 40% as envisaged under the Petroleum Exploration & Production Policy 2012
- Capital allowances — accelerated depreciation

B. Fiscal regime

Petroleum exploration and production (E&P) activities in Pakistan may be undertaken in accordance with two different types of agreements:

- For onshore operations, a system based upon a petroleum concession agreement (PCA)
- For offshore operations, a system based upon a production-sharing agreement (PSA)

Corporate income tax

In accordance with the Petroleum Exploration & Production Policy 2012, the rate of CIT is 40% of the profits or gains from all new PCAs and PSAs.

The Income Tax Ordinance 2001 (the 2001 Ordinance) is the governing income tax legislation. Part I of the Fifth Schedule to the 2001 Ordinance deals with the computation of profits and gains or income from petroleum E&P activities in Pakistan. The Fifth Schedule provides that all expenses incurred after commencement of commercial production that are not capital or personal in nature are deductible, provided they are incurred “wholly and exclusively” for the purpose of petroleum E&P activities. However, certain expenses, such as royalty payments and depreciation, are deducted based on specific provisions of the 2001 Ordinance.

Ring fencing

In accordance with the provisions of the Fifth Schedule to the 2001 Ordinance, there is no concept of ring fencing for corporate tax calculations.

Dry holes

Any expenditure for searching, exploring and inquiring that results in a "dry hole" is treated as a loss on its completion or a surrender of the area back to the Government. As may be opted for by the working-interest owner in the PCA or PSA, this loss is adjusted in either of the following ways:

- The loss in any year is set off against the income of that year, chargeable under the head "income from business" or any income chargeable under any other head of income (other than income from dividends). Excess losses are carried forward for no more than six years from the year incurred.
- The loss in any year is offset against the income of such undertaking in the tax year in which commercial production commenced. Where the loss cannot be wholly offset against the income of such undertaking in that year, the excess is carried forward for no more than 10 years.

Offshore operations

In respect of offshore operations, the cost limit is 85%, including the royalty of 12.5%. The contractor can recover 100% of the cost from up to a maximum of 85% of the gross revenues.

A sliding-scale PSA is used for offshore operations instead of direct Government participation. The agreement is generally executed by the contractor with a Government-owned entity, which is also granted the exploration license and the development and production lease. The contractor therefore initially receives the oil and gas profit shares and is responsible for managing the PSAs.

The profit split is established on the basis of a sliding scale for shallow, deep and ultra-deep grids. The sliding scale is based on the cumulative production, permitting a rapid recovery of investments and a higher net present value. The profit split is set out below:

1. Profit oil and gas share for wells in shallow grid areas of less than 200 meters' water depth, with a depth to reservoir shallower than 4,000 meters:

Cumulative available oil or available gas from contract area	Government share of profit oil or profit gas in contract area		Contractor share of profit oil or profit gas in contract area	
Million barrels of oil equivalent (MMBOE)	Crude oil, liquefied petroleum gas (LPG) or condensate	Natural gas	Crude oil, LPG or condensate	Natural gas
0–100	20%	10%	80%	90%
> 100–200	25%	15%	75%	85%
> 200–400	40%	35%	60%	65%
> 400–800	60%	50%	40%	50%
> 800–1,200	70%	70%	30%	30%
> 1,200	80%	80%	20%	20%

2. Profit oil and gas share for wells in deep grid areas of more than or equal to 200 meters' but less than 1,000 meters' water depth, or deeper than 4,000 meters to the reservoir in the shallow grid area:

Cumulative available oil or available gas from contract area	Government share of profit oil or profit gas in contract area		Contractor share of profit oil or profit gas in contract area	
MMBOE	Crude oil, LPG or condensate	Natural gas	Crude oil, LPG or condensate	Natural gas
0–200	5%	5%	95%	95%
> 200–400	10%	10%	90%	90%
> 400–800	25%	25%	75%	75%
> 800–1,200	35%	35%	65%	65%
> 1,200–2,400	50%	50%	50%	50%
> 2,400	70%	70%	30%	30%

3. Profit oil and gas share for wells in ultra-deep grid areas of more than or equal to 1,000 meters' water depth:

Cumulative available oil or available gas from contract area	Government share of profit oil or profit gas in contract area		Contractor share of profit oil or profit gas in contract area	
MMBOE	Crude oil, LPG or condensate	Natural gas	Crude oil, LPG or condensate	Natural gas
0–300	5%	5%	95%	95%
> 300–600	10%	10%	90%	90%
> 600–1,200	25%	25%	75%	75%
> 1,200–2,400	35%	35%	65%	65%
> 2,400–3,600	45%	45%	55%	55%
> 3,600	60%	60%	40%	40%

Windfall levy

A windfall levy also applies to onshore concessions. The windfall levy on oil (WLO) applies to crude oil and condensate from an onshore concession using the following formula:

$$\mathbf{WLO = 0.4 \times (M - R) \times (P - B)}$$

Where WLO = windfall levy on crude oil and condensate

M = net production

R = royalty

P = market price of crude oil and condensate

B = base price:

- The base price for crude oil and condensate is US$40 per barrel.
- This base price increases each calendar year by US$0.50 per barrel starting from the date of first commercial production in the contract area.

WLO applies to crude oil and condensate from an offshore PSA, using the following formula:

$$\mathbf{WLO = 0.4 \times (P - R) \times SCO}$$

Where WLO = windfall levy on share of crude oil and condensate

P = market price of crude oil and condensate

SCO = share of crude oil and condensate allocated to a contractor

R = base price:

- The base price for crude oil and condensate is US$40 per barrel.
- This base price increases each calendar year by US$0.50 per barrel starting from the date of first commercial production in the contract area.

For the sale of natural gas to parties other than the Government, a windfall levy on gas (WLG) applies to the difference between the applicable zone price and the third-party sale price using the following formula:

WLG = 0.4 x (PG − BR) x V

Where WLG = windfall levy on share of natural gas

PG = third-party sale price of natural gas

BR = base price

V = volume of gas sold to third party, excluding royalty

The base price is the applicable zone price for sale to the Government. If the third-party sale price of gas is less than or equal to the base price, the WLG is zero.

The windfall levy does not apply to sales of natural gas made to the Government.

Royalty regimes

A royalty is payable in respect of onshore operations at the rate of 12.5% of the value of the petroleum at the field gate. At the option of the Government the royalty must be paid in cash or in kind on liquid and gaseous hydrocarbons (such as LPG, natural gas liquids (NGL), solvent oil, gasoline and others), as well as on all substances, including sulfur, produced in association with such hydrocarbons. The lease rent paid during the year is not deductible from the royalty payment.

A royalty is treated as an expense for the purpose of determining the income tax liability. Ten percent of the royalty will be utilized in the district where oil and gas is produced for infrastructure development.

The following royalty schedule applies to offshore operations:

- The first 48 calendar months after commencement of commercial production — no royalty
- Calendar months 49 to 60 inclusive — 5% of field gate price
- Calendar months 61 to 72 inclusive — 10% of field gate price
- Calendar months 73 onward — 12.5% of field gate price

Similar to onshore operations, at the option of the Government the royalty is payable either in cash or in kind on liquid and gaseous hydrocarbons (such as LPG, NGL, solvent oil, gasoline and others), as well as for all substances, including sulfur, produced in association with such hydrocarbons. The lease rent paid during the year is not deductible from the royalty payment. Royalties are treated as an expense for the purpose of determining the income tax liability.

For the purpose of calculating the amount due by way of royalty, the value of the petroleum produced and saved must be determined by using the actual selling price in the following manner:

1. If the petroleum is sold in the national market, the actual selling price means the price determined in accordance with the relevant sale-and-purchase agreement between the petroleum rights holder and the Government or its designee, less allowed transportation costs beyond the delivery point.
2. In all other cases, the actual selling price means the greatest of:
   a. The price at which the petroleum is sold or otherwise disposed of, less allowable transportation costs
   b. The fair market price received through arm's-length sales of the petroleum, less the allowed transportation costs
   c. The price applicable to the sales made under sub-rule 2(a) above

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

The following depreciation rates apply for onshore operations:

- On successful exploration and development wells — 10% on a straight-line basis
- On dry holes (exploratory wells) — expensed immediately upon commencement of commercial production or relinquishment, whichever is earlier
- Below-ground installation — 100% upon commencement of commercial production or relinquishment, whichever is earlier
- Initial allowance in respect of eligible depreciable assets in the year of use or commencement of commercial production, whichever is later — 25% of cost for plant and machinery and 15% of cost for building
- First-year allowance in respect of eligible plant, machinery and equipment installed in a specified rural and underdeveloped area — 90% of cost
- Normal depreciation rate on plant and machinery — 15% using the diminishing-balance method

It is permitted to carry forward unabsorbed depreciation for a maximum period of six years. If a depreciable asset is completely used and not physically available at the time of commencement of commercial production and it relates to a dry hole, it becomes a lost expenditure, and it can be amortized on a straight-line basis over a period of 10 years after the commencement of commercial production (see the treatment of a lost expenditure for a "dry hole" above). In these circumstances, the entire cost of the asset is amortized as part of the lost expenditure and not as depreciation.

The following depreciation rates apply to offshore operations:

- On successful exploration and development wells — 33% on a straight-line basis
- On dry holes (exploratory wells) — expensed immediately upon commencement of commercial production or relinquishment, whichever is earlier
- Noncommercial well (exploration wells) — expensed upon relinquishment of license
- On facilities and offshore platforms — 25% using the declining-balance method
- Below-ground installation — 100% upon commencement of commercial production or relinquishment, whichever is earlier
- Initial allowance in respect of eligible depreciable assets in the year of use or commencement of commercial production, whichever is later — 25% of cost
- Normal depreciation rate on plant and machinery — 15% using the diminishing-balance basis

It is permitted to carry forward any unabsorbed depreciation in respect of plant and machinery until the depreciation is fully absorbed

A depletion allowance, after commencement of commercial production, is allowed at the lesser of:

- 15% of the gross receipts representing wellhead value of the production
- 50% of profits of such undertaking before any depletion allowance

From tax year 2010 onward, decommissioning cost is allowed on the following basis, subject to a certification by a chartered accountant or a cost accountant:

- Where commercial production has not commenced, with effect from tax year 2010, decommissioning cost is allowed over the lower of the following terms:
  a. 10 years
     Or
  b. The remaining life of the development and production or mining lease

Such cost is permitted to be claimed starting from the year of commencement of commercial production.

- Where commercial production commenced prior to 1 July 2010, deduction for decommissioning cost shall be allowed from the tax year 2010 over the lower period of:
  a. 10 years
     Or
  b. The remaining life of the development and production or mining lease

D. Incentives

In accordance with the Petroleum Exploration & Production Policy 2012, prequalified E&P companies incorporated in Pakistan that pay dividends and receive payments for petroleum sold in Pakistan rupees (PKR) are entitled to the following incentives:

- E&P companies are encouraged to operate exploration blocks with 100% ownership.
- In cases of joint ventures with foreign E&P companies, local E&P companies shall have a working interest of 15% in Zone I, 20% in Zone II and 25% in Zone III on a full-participation basis (required minimum Pakistani working interest). Local E&P companies must contribute their share of exploration expenditures (denominated in PKR) up to the required minimum Pakistani working interest.
- On a case-by-case basis, during the exploration phase, local E&P companies are entitled to receive foreign exchange against payment in Pakistani currency to meet their day-to-day obligations under permits, licenses and PCAs or PSAs. After commercial discovery, local E&P companies are paid up to 30% of their sale proceeds in foreign currency to meet their day-to-day operational requirements. For project financing after commercial discovery, local E&P companies are required to make their own foreign-exchange arrangements, except for companies in which the Government holds a majority shareholding.

Furthermore, the Schedule to the Regulation of Mines and Oilfields and Mineral Development (Government Control) (Amendment) Act 1976 (the 1976 Act) provides the following concessions to an undertaking engaged in exploration or extraction of mineral deposits. The concessions noted below are applicable to petroleum operations:

- There is the concept of "freezing of law" in respect of mining operations. The effect is that any provisions of the mining rules or amendment in the tax laws, made after the effective date of an agreement for the grant of a license or a lease to explore, prospect or mine petroleum, that are inconsistent with the terms of the agreement, do not apply to a company that is a party to the agreement to the extent that they are incompatible with the agreement.
- Before commencement of commercial production of petroleum, any expenditure on searching for, or on discovering and testing, a petroleum deposit, or on winning access to the deposit that is allowable to a surrendered area and to the drilling of a dry hole, is deemed to be lost at the time of the surrender of the area or the completion of the dry hole. A lost expenditure is allowable in one of the two ways mentioned in Section B under the heading "Dry holes."
- The income derived by the licensee or lessee from the use of, and surplus capacity of, its pipeline by any other licensee or lessee, is assessed on the same basis as income from the petroleum it produced from its concession area.
- A licensee or lessee company incorporated outside Pakistan, or its assignee, is allowed to export its share of petroleum after meeting the agreed portion of the internal requirement for Pakistan.

- Sale proceeds of the share of petroleum exported by a licensee or lessee incorporated outside Pakistan, or its assignee, may be retained abroad and may be used freely by it, subject to the condition that it shall bring back the portion of the proceeds that is required to meet its obligation under the lease.
- No customs duty or sales tax is levied on the importation of machinery and equipment specified in a PCA or PSA for the purposes of exploration and drilling prior to commercial discovery.
- A concessionary, ad valorem customs duty rate of 0% to 10% applies on importation of specific plant, machinery and equipment by E&P companies, and their contractors and subcontractors, on fulfillment of specified conditions. Such plant, machinery and equipment are exempt from sales tax and federal excise duty.
- Foreign nationals employed by a licensee, a lessee or their contractor may import commissary goods free of customs duty and sales tax to the extent of US$550 per annum, subject to the condition that the goods are not sold in or otherwise disposed of in Pakistan.
- Foreign nationals employed by a licensee, a lessee or their contractor may import used and bona fide personal and household effects, excluding motor vehicles, free of customs duty and sales tax, subject to the condition that the goods are not sold in or otherwise disposed of in Pakistan.

All data in respect of areas surrendered by a previous licensee or lessee must be made available for inspection to a prospective licensee free of charge.

Initial participation by the Federal Government in exploration occurs to the extent as may be agreed upon between the Government and the licensee.

E. Withholding taxes

Dividends

The general rate of withholding tax (WHT) on payment of a dividend is 12.5% of the gross amount of the payment. The tax withheld constitutes a full and final discharge of the tax liability of the recipient shareholder if the shareholder is an individual or an association of persons. For corporate taxpayers, the tax deducted constitutes an advance tax and is adjustable against the eventual tax liability for the relevant tax year, which is 12.5% of the gross dividend.

Interest

The general rate of WHT on interest is 10% of the gross amount of interest if the recipient is a resident of Pakistan. The tax withheld constitutes the full and final discharge of the tax liability of the recipient if the recipient is a resident individual or an association of persons. For corporate tax payers, such tax withheld constitutes an advance tax and is adjustable against the eventual tax liability of the company for the year. If interest is paid to nonresidents not having a permanent establishment in Pakistan, the rate of withholding is 10% of the gross amount. The tax withheld constitutes an advance tax for the recipient lender and is adjustable against the eventual tax liability of the nonresident recipient. However, with respect to nonresidents not having a permanent establishment in Pakistan, the tax withheld constitutes final discharge of tax liability with respect to interest on debt instruments, Government securities (including treasury bills) and Pakistan Investment Bonds, provided that the investments are exclusively made through a Special Rupee Convertible Account maintained with a bank in Pakistan.

Royalties and technical services

Receipts with respect to royalties and technical services that are not attributable to the permanent establishment in Pakistan of a nonresident person are subject to WHT at the rate of 15% of the gross amount of the payment. The tax withheld constitutes the full and final discharge of the tax liability of the recipient.

Nonresident contractors

Payments made to nonresident contractors for construction, assembly or installation projects in Pakistan that are undertaken by the contractor, including services rendered in relation to such projects, are subject to WHT at the rate of 6% of the gross amount of the payment. The tax withheld constitutes the full and final discharge of the tax liability of the nonresident contractor, provided it opts for this treatment by filing a written declaration to that effect with the taxation authorities in Pakistan within three months of the commencement of the contract. If the option is not exercised, the net profit is taxable at the 31% corporate rate of tax for the tax year 2017.

F. Financing considerations

Thin capitalization rules

The income tax law has a thin capitalization rule, whereby if a foreign-controlled resident company or a branch of a foreign company operating in Pakistan, other than a financial institution, has a foreign-debt-to-foreign-equity ratio in excess of 3:1 at any time during a tax year, the deductibility of interest as a business expense is capped. Interest on debt paid by a company in that year is not a permissible deduction to the extent that it exceeds the 3:1 ratio; in other words, only the interest expenses arising from loans that are within the debt-to-equity ratio ceiling may be deducted.

For purposes of the thin capitalization rule, "foreign debt" includes any amount owed to a foreign controller or nonresident associate of the foreign controller for which profit on the debt is payable and deductible for the foreign-controlled resident company and is not taxed under the 2001 Ordinance, or is taxable at a rate less than the corporate rate of tax applicable on the assessment to the foreign controller or associate.

Interest guaranteeing

Interest guaranteeing is not applicable in Pakistan.

PSC expenditure recovery exclusions for financing costs

Whereas cost push-down is not permitted by the head office to the local branch, all expenses, including head office expenses, incurred wholly and exclusively to earn the income, are allowable for tax purposes.

G. Transactions

The working-interest owner is not permitted to sell, assign, transfer, convey or otherwise dispose of all or any part of its rights and obligations under a license or lease or an agreement with a third party or any of its affiliates, without the prior written consent of the regulatory authorities. This permission, however, is generally not withheld.

The transfer of any interest or right to explore or exploit natural resources in Pakistan constitutes a disposal for tax purposes. The amount of gain arising on the disposal of such a right is computed as the difference between the consideration received for the transfer and the cost related to the right. Consideration is explicitly provided to be the higher of the amount received or the fair market value. The amount of the gain is taxable at the rate of the tax applicable for the relevant tax year.

The 2001 Ordinance explicitly provides that the amount of gain arising from alienation of any share in a company, the assets of which consist wholly or mainly, directly or indirectly of property or a right to explore or exploit natural resources in Pakistan, constitutes Pakistan-sourced income of the transferor. The amount of the gain is computed as the difference between the consideration received and the cost of the asset. If the consideration received is less than the fair market value, the fair market value is deemed to be the consideration for tax purposes. If the shares have been held for a period of more than one year, only 75% of the gain is taxable and at the rate of the tax applicable for the relevant tax year.

If the shares represent shares of a listed company in Pakistan, the amount of gain is taxable at the following rates depending upon the period of holding of such shares:

S. no.	Holding period	Acquisition date	Rates
1	Where holding period of the security is less than 12 months	After 1 July 2012	15%
2	Where holding period of the security is more than 12 months but less than 24 months	After 1 July 2012	12.5%
3	Where holding period of the security is 24 months or more	On or after 1 July 2012	7.5%
4	Where security was acquired before 1 July 2012	Before 1 July 2012	0%

H. Indirect taxes

Sales tax

Sales tax in Pakistan is akin to the value-added tax (VAT) system in various countries, and sales tax on goods is governed by the Sales Tax Act 1990. All supplies made in the course of any taxable activity and all goods imported into Pakistan are subject to sales tax (except those listed in Schedule 6 of the Sales Tax Act). Sales tax on services is a provincial levy in Pakistan and is governed through the respective provincial sales tax laws.

Effective from 1 July 2000, the provincial governments brought certain services within the ambit of sales tax. Such services included services supplied by hotels, clubs and caterers; customs agents, ship chandlers and stevedores; courier services; and advertisements on television and radio (excluding advertisements sponsored by the Federal Government, its agencies and nongovernmental organizations related to certain prescribed social causes).

Since at the time, no provincial revenue administration and collection authority had been set up, the provincial governments authorized the Federal Government to administer and collect such sales tax on services. Subsequently, the provinces of Sindh, Punjab, Khyber Pakhtunkhwa (KPK), Balochistan, and Islamabad Capital Territory (ICT) have set up their own revenue collection and administration authorities; hence, sales tax on services as applicable in the respective jurisdictions of these provinces is now collected by the provincial governments themselves. Further, the respective provincial legislations have considerably expanded the scope of sales tax by including an extended range of services that are now liable to sales tax.

In addition to sales tax, federal excise duty is levied on certain goods and services. Those goods include cigarettes, liquefied natural gases, flavors and concentrates, while services include franchise services and other services (excluding those provided or rendered in the provinces of Sindh, Punjab and KPK). (See also the subsection below on excise duties applicable specifically to the oil and gas industry.)

The general rate of sales tax on goods is 17% of the value of the supplies made or the goods imported. However, for goods specified in Schedule 3 of the Sales Tax Act, sales tax is charged on supplies at the rate of 17% of the retail price. With respect to services, the general rate of sales tax in each province and ICT is as follows:

- 16% in Punjab and Islamabad
- 15% in KPK and Balochistan
- 13% in Sindh

Reduced rate of sales tax are also applicable on certain services. The taxable services are listed in the Second Schedule of each of the respective Provincial Sales Tax on Services Acts.

Goods exported from Pakistan and goods specified in Schedule 5 of the Sales Tax Act are subject to a zero rate of sales tax. The supply and importing of plant, machinery and equipment are subject to a reduced rate of sales tax, with certain exceptions.

Goods specified in Schedule 6 of the Sales Tax Act (and any other goods that the Federal Government may specify by a notification in the *Official Gazette*) are exempt from sales tax.

E&P companies are required to be registered under the Sales Tax Act because the supply of E&P products attracts sales tax.

Subject to certain restrictions, a registered entity may recover all or part of input tax paid on imports and the purchase of taxable goods or services acquired in respect of making taxable supplies. Input tax is generally recovered by being offset against the sales tax payable on the taxable supplies.

Import duties

The Customs Act 1969 governs the taxes that apply on the import or export of dutiable goods. Section 18 of that Act provides that customs duties are levied at such rates as prescribed in Schedules 1 and 2 (or under any other law in force at the time) on:

- Goods imported into or exported from Pakistan
- Goods brought from any foreign country to any customs station and, without payment of duty there, shipped or transported, or then carried to, and imported at, any other customs station
- Goods brought in bond from one customs station to another

Generally, the rate of customs duty applied to the customs value of imported goods ranges from 2% to 35%; the rate depends on several factors, including the type of commodity, the constituent material and the country of origin.

Customs duty on the import of plant, machinery, equipment and other accessories made by E&P companies, their contractors, subcontractors and service companies is governed by SRO.678(1)/2004 dated 7 August 2004 (the SRO) and issued under Section 19 of the Customs Act. The SRO provides exemptions from customs duty and sales tax:

- All machinery, equipment, materials, specialized vehicles or vessels, pickups (four-wheel drive), helicopters, aircraft, accessories, spares, chemicals and consumables not manufactured locally that are imported by E&P companies, their contractors, subcontractors or service companies, in excess of 5% by value and the whole amount of sales tax on import and subsequent supply
- The goods mentioned above that are manufactured locally and imported by E&P companies, their contractors, subcontractors or service companies and other petroleum and public sector companies, in excess of 10% by value and whole amount of sales tax on import

These customs duty concessions are available exclusively for E&P companies that hold permits, licenses, leases, PSCs or PSAs and that enter into supplemental agreements with Pakistan's Government. Moreover, the exemption under the SRO is available only in respect of the specified goods satisfying conditions specified in the notification.

Items imported at concessionary rates of duty that become surplus, scrap, junk or obsolete or are otherwise disposed of or transferred to another E&P company are also exempt from import duties (upon notification of the sales tax department). However, if these items are sold through a public tender, duties are recovered at the rate of 10% on the value of the sale proceeds.

Federal excise duty

Excise duty is a single-stage duty levied at varied rates on (i) specified goods produced or manufactured in Pakistan or imported into Pakistan, (ii) on specified goods produced or manufactured in non-tariff areas and brought into tariff areas for sale or consumption and (iii) on specified services provided or rendered in Pakistan. Table I of Schedule 1 of the Federal Excise Act 2005 identifies goods subject to excise duty (including cement, LPG and other liquefied petroleum gases) and the current rates of excise duty on gas-related products are listed in the table below. Certain goods and classes of persons are excluded from duty under Table I of Schedule 3 of the Federal Excise Act 2005.

S. no.	Description of goods	Heading or subheading number	Rate of duty
31	Liquefied natural gas	2711.1100	PKR17.18 per 100 cubic meters
32	Liquefied propane	2711.1200	PKR17.18 per 100 cubic meters
33	Liquefied butanes	2711.1300	PKR17.18 per 100 cubic meters
34	Liquefied ethylene, propylene, butylenes and butadiene	2711.1400	PKR17.18 per 100 cubic meters
35	Other liquefied petroleum gases and gaseous hydrocarbons	2711.1900	PKR17.18 per 100 cubic meters
36	Natural gas in gaseous state	2711.2100	PKR10 per million British Thermal Unit (MMBTu)
37	Other petroleum gases in gaseous state	2711.2900	PKR10 per MMBTu

Stamp duty

Under the Stamp Act 1899, stamp duty is paid on "instruments," where the term "instrument" means a written deed, will or other formal legal document for transfer of property.

Stamp duty is a provincial or state levy and its application varies from province to province. Stamp duty rates also vary from instrument to instrument.

I. Other

Rental payments

With respect to an onshore concession, all holders of exploration licenses are required to pay an advance rental charge at the following rates:

- PKR3,500 per square kilometer or part thereof in respect of the initial five-year term of the license
- PKR800 per square kilometer or part thereof in respect of each year of the initial term of the license
- PKR5,000 per square kilometer or part thereof in respect of each renewal of the license
- PKR2,750 per square kilometer or part thereof in respect of each year of the renewal of the license

For onshore operations, during the lease period, the following annual advance rental charges apply:

- PKR7,500 per square kilometer or part thereof covering the lease area during the initial lease period
- PKR10,000 per square kilometer or part thereof covering the lease area during the renewal period of a lease and further lease term extension

Contractors engaged in offshore operations are required to pay an advance annual acreage rental for the area covered under the PSA of US$50,000, plus a further rate of US$10 per square kilometer or part thereof every year.

Rental expenses are allowable deductions for taxpayers.

Production bonuses

A production bonus is payable for onshore operations on a contract area basis, as set out in the table below.

Cumulative production (MMBOE)	Amount (US$)
At start of commercial production	0.6 million
30	1.2 million
60	2 million
80	5 million
100	7 million

In respect of offshore operations, a production bonus is payable according to the following table.

Cumulative production (MMBOE)	Amount (US$)
At start of commercial production	0.6 million
60	1.2 million
120	2 million
160	5 million
200	7 million

Domestic supply obligation

Subject to the considerations of internal requirements and national emergencies, E&P companies are allowed to export their share of crude oil and condensate, as well as their share of gas, based on export licenses granted by the regulator. For the purpose of obtaining an export license for gas, the export volume is determined in accordance with the "L15" concept, provided a fair market value is realized for the gas at the export point.

Under the L15 concept, gas reserves that exceed the net proven gas reserves in Pakistan (including firm import commitments for projected gas demand for the next 15 years) can be considered for export. Once gas has been dedicated for export, any export licenses for agreed volumes cannot be subsequently revoked.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- □ **Production sharing contracts**
- □ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies in Papua New Guinea (PNG) to taxation of income derived by petroleum and gas companies consists of a combination of corporate income tax (CIT), royalties and development levies, additional profits tax (APT) and infrastructure tax credits.

Income tax	Resident	Nonresident
Petroleum – incentive rate	30%	30%
Petroleum – new projects	30%	30%
Petroleum – existing projects	30%	30%
Gas	30%	30%
Additional tax		
Petroleum and gas†	2%	2%
Royalties and development levies	2% of wellhead value	2% of wellhead value
Dividend withholding tax† (WHT) (petroleum and gas)	15%	0%
Interest WHT (petroleum and gas)†	15%	15%
Additional profits tax*†	30%	30%

* APT may apply to gas projects in some situations. Please refer below for further discussion on APT.

† Subject to fiscal stabilization agreements and project agreements.

B. Fiscal regime

The fiscal regime that applies in PNG to the petroleum and gas industry consists of a combination of CIT, royalties, development levies and development incentives.

Corporate income tax

General provisions applicable to petroleum and designated gas projects

Specific corporate tax rules apply to resource projects in PNG, and the application of these rules will depend on whether taxpayers are covered under these specific provisions.

A "resource project" means a designated gas project, a mining project or a petroleum project. A "designated gas project" means a gas project as defined under a gas agreement made pursuant to the Oil and Gas Act 1998. A "petroleum project" means a petroleum project as prescribed by regulation, or petroleum operations conducted pursuant to a development license or a pipeline license. There are specific provisions applicable to petroleum operations and gas operations that are discussed below.

Rate of tax (applicable to oil and gas profits)

PNG resident corporations are generally subject to PNG CIT on their worldwide net income at a 30% corporate tax rate. Nonresident corporations are generally subject to PNG income tax only on their PNG-sourced income at a 48% corporate tax rate. From 1 January 2017, both resident and nonresident companies engaged in petroleum and gas operations are subject to 30% tax.

Additional tax

If a taxpayer is subject to fiscal stabilization under the provisions of the Resource Contracts Fiscal Stabilization Act 2000, an additional 2% income tax will apply in respect of net income. However, this excludes the PNG liquefied natural gas (LNG) operations.

"Fiscal stabilization" refers to an agreement entered into by the state and the participants of long-term resources projects, where the agreement guarantees the fiscal stability of the project by reference to the law in force at the date of the project agreement.

The fiscal stabilization agreement is usually entered into when a development contract is signed between the State and the resource developer(s).

General provisions applicable to petroleum and designated gas projects

A summary of certain general provisions that apply to petroleum and designated gas projects is given below. Taxpayers should be aware that this is not an exhaustive list; other specific provisions also exist that may apply in some circumstances. In particular, specific agreements negotiated with Government authorities may modify the operation of these general provisions.

Project basis of assessment

Income derived from each petroleum or gas project is assessed on a project basis as if it were the only income of the taxpayer, notwithstanding that the taxpayer may have derived other assessable income. A petroleum or gas project may include any number of development licenses or pipeline licenses, or a designated gas project, or a combination thereof.

Deductions are available only for expenditure attributable to the project. Where there is deductible expenditure or income not directly related to the project, this expenditure or income should be apportioned on a reasonable basis. Items of income or deductions exclusively relating to other projects are excluded with limited exceptions.

Allowable deductions

Allowable deductions against the assessable income of petroleum projects and designated gas projects include normal operating and administration expenses, depreciation, amortization of allowable exploration expenditure, amortization of allowable capital expenditure, interest, management fees, realized exchange losses and consumable stores.

Capital expenditure

Once a development license is issued, a distinction is made between allowable exploration expenditure (expenditure incurred prior to the issue of a development license), allowable capital expenditure (expenditure incurred after a development license has been issued) and normal depreciating assets. The rules relating to each of these are discussed separately below.

Depreciation of property, plant and equipment

By election, capital expenditure incurred on items of property, plant or equipment with an estimated effective life of less than 10 years incurred after the issue of a development license can be depreciated under normal depreciation rules rather than as allowable capital expenditure. Depreciation of fixed assets that are used in the production of taxable income is calculated using either the straight-line method or the diminishing value (DV) method. The taxpayer is required to make the election in the first year of income in which the asset is used for income-producing purposes. Any change in the method of depreciation should be approved by the Commissioner General.

The Internal Revenue Commission (IRC) has issued guidelines providing depreciation rates in respect of selected plant and equipment. The following table shows an excerpt of some relevant assets and their accepted depreciations rates under the two methods. Note, though, that the IRC has not issued any formal guidance in respect of gas assets.

	Item	Prime cost method (%)	DV method (%)
1.	**Oil — exploration:**		
	Drilling plant	20	30
	Seismic geophysical survey equipment	20	30
	Surveying equipment	10	15
	Camp equipment:		
	Portable sleeping, messing, etc., units	20	30
	Other camp equipment	10	15
	General plant and equipment	10	15
	Oil rigs (offshore) and ancillary plant	10	15
2.	**Petroleum**		
	Drilling and down-hole equipment	20	30
	Earthmoving plant and heavy equipment	20	30
	General plant and equipment	17	25
	Laboratory equipment	5	7.5
	Onshore production plant	13	18
	Offshore production plant	13	20
	Pipelines	13	20
	Pumps, motors and control gear and fittings	13	20

	Item	Prime cost method (%)	DV method (%)
	Refining plant	13	20
	Shaft drilling equipment	20	30
	Tanks containing:		
	Natural crude oil and redistillates	13	20
	Other petroleum products	13	20
	Wharves and jetties	5	7.5
	Vehicles	20	30
3.	**Allowable exploration expenditure (see below)**		**Divided by the lesser of remaining life of project or four (i.e., 25%)**
4.	**Allowable capital expenditure (ACE) (see below)**		
	Short-life ACE (effective life less than 10 years)	n/a	25
	Long-life ACE (effective life 10 years or more)	10	n/a

Allowable exploration expenditure

"Allowable exploration expenditure" (AEE) is defined as expenditure incurred by a taxpayer for the purpose of exploration in PNG within the 20 years prior to the date of issue of a development license included in the resource project, and incurred:

- Pursuant to an exploration license from which the resource development license was drawn
- In relation to the areas (including relinquished areas) of an exploration license that has been surrendered, canceled or expired

It further includes AEE deemed to have been incurred by the taxpayer under Section 155L (see below).

AEE can effectively be carried forward for a period of 20 years. Expenditure incurred in a project area after a development license is issued is treated as ACE.

AEE is amortized by dividing the residual expenditure by the lesser of the remaining life of the project or four (i.e., a DV depreciation rate of 25%). The amount of the deduction is limited to the amount of income remaining after other deductions, except ACE; in other words, the allowable deduction cannot create a tax loss. Where there is insufficient income, the balance of AEE is reduced only by the available deduction (but the excess can be carried forward and utilized in future years).

A taxpayer will need to be carrying on resource operations to claim deductions for AEE.

Allowable capital expenditure

"Allowable capital expenditure" (ACE) is defined as capital expenditure incurred by a taxpayer carrying on resource operations after a resource development license is issued. ACE includes:

- Cost of buildings, improvements or plant necessary for carrying on the resource operations
- Feasibility and environmental impact studies
- Construction and operation of port or other facilities for the transportation of resources (oil or gas) obtained from the resource project
- Provision of buildings and other improvements or plant
- Cost of providing water, light or power, communication and access to the project site
- Expenditure incurred to provide certain residential accommodation, health, education, law and order, recreational or other similar facilities and facilities for the supply of meals for employees or their dependents
- Depreciable plant that has been elected to be treated as short-life assets
- Exploration expenditure incurred after the resource development license is issued
- Certain general administration and management expenditure relating to resource projects
- Expenditure deemed to be incurred under Section 155L (see below)

The following expenditure is excluded from ACE:

- Ships that are not primarily or principally used for the transport of gas or petroleum resources by the taxpayer in carrying out resource operations
- Office buildings that are not situated at, or adjacent to, the project site

The ACE of a taxpayer in respect of a resource project is split into two categories and amortized over the life of the project:

- Long-life ACE — capital expenditure with an estimated effective life of 10 years or more, where the allowable expenditure is broadly amortized over a period of 10 years
- Short-life ACE — capital expenditure with an estimated effective life of less than 10 years, where deductions are calculated by dividing the unamortized balance by the lesser of the remaining life of the project or four

The amount of ACE deductions each year is limited to the amount of income remaining after deducting all other deductions so ACE deductions cannot produce a tax loss. Long-life ACE deductions are utilized first, and then a deduction for short-life ACE may be claimed. Where there is insufficient income to utilize the amount of deduction available in a year, the excess can be carried forward and utilized in future years.

A taxpayer will need to be conducting resource operations to claim deductions for ACE.

Disposal of property

Where deductions have been allowed or are allowable under the resource provisions in respect of capital expenditure on property that has been disposed of, lost or destroyed by a taxpayer carrying on resource operations, or the use of which has been otherwise terminated in relation to that resource project, a taxable balancing charge may arise if the consideration received is more than the undeducted balance of the expenditure. Where the consideration received is less, a balancing deduction is allowed.

As there is no capital gains tax (CGT) in PNG, any capital gains arising on disposal of property are not assessable.

Transfer of AEE and ACE

Where an interest in a resource project is disposed of, a so-called "Section 155L notice" can be lodged to transfer the undeducted AEE and ACE balance from the vendor to the purchaser. This notice has to be lodged with the Commissioner General no later than four months after the end of the year of income in which the interest in the resource project has been transferred, subject approved extension requests.

Specific provisions applicable to petroleum projects and designated gas projects

In addition to the general provisions, some specific provisions apply to a taxpayer who undertakes petroleum operations or designated gas projects. These provisions deal with matters such as:

- Project basis of assessment
- Additional provisions relating to AEE
- Additional provisions relating to ACE
- Conversion between petroleum and designated gas projects
- Use of petroleum in operations
- Additional deductions for PNG LNG project participants

Additional profits tax

Additional profits tax (APT) potentially applies to a designated gas project, including the ExxonMobil-led PNG LNG project, in the year in which the taxpayer has recovered its investment in the project and achieved a return on its investment above a prescribed level (i.e., when the accumulated value of net project receipts of a taxpayer turns positive). From 1 January 2017, APT applies to all resource projects other than projects that are subject to fiscal stabilization.

From 1 January 2017, the accumulation rate is fixed at 15%, and the APT rate is fixed at 30%.

Capital gains

Capital gains are not subject to tax in PNG. The disposal of a capital asset may be subject to tax to the extent the disposal takes place as part of a profit-making scheme or is part of the ordinary business of the taxpayer.

While capital gains are not generally subject to tax, if depreciable plant and equipment is disposed of, a calculation of any gain or loss on disposal must be performed. Where the amount received exceeds the tax written-down value, an amount of income may be derived up to the amount of depreciation deductions previously claimed (i.e., any gain over the original cost should not be taxed). Alternatively, if the amount received on disposal is less than the tax written-down value, an allowable deduction may be able to be claimed.

Functional currency

Income and expenses must be expressed in PNG currency (the kina), unless permission has been granted by the Commissioner General to report in another currency.

Transfer pricing

International related-party transactions must be carried out at arm's length. Specific transfer pricing provisions exist that allow the Commissioner General to adjust an entity's taxable income if international related-party transactions have not been conducted on an arm's-length basis (i.e., if the transaction would not have been conducted on the same basis between independent parties).

In addition, specific provisions relate to management or technical fees paid to international-related parties.

Dividends

From 1 January 2017 dividend WHT on dividends paid out of profits from petroleum or gas operations is at the rate of 15% other than for projects that are subject to fiscal stabilization.

Interest

From 1 January 2017 the previous exemption from interest WHT on interest paid in respect of borrowings used to finance petroleum or gas operations has been removed other than for projects that are subject to fiscal stabilization.

Tax year

The PNG tax year is the calendar year. However, a substituted accounting period is often permitted on written requests to the Commissioner General.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowance and tax depreciation

There are specific rules for petroleum and gas taxpayers with respect to the depreciation and amortization of capital expenditure. Refer to the previous discussion of AEE, ACE and depreciation of certain plant and equipment in Section B above.

D. Incentives

In addition to the various income tax concessions discussed above, the Government offers other incentives to taxpayers operating in the resources sector. Some of these are discussed in further detail in this section.

While some investors have been able to negotiate specific incentives for particular projects, the Government now aims to include all tax concessions in domestic legislation and make any concessions available on an industry basis, with the goal of developing a more neutral and equitable treatment of projects.

Pooling of exploration expenditure

Resource taxpayers (mining, petroleum and gas) may elect to pool expenditure incurred by the taxpayer or a related corporation outside a resource project to form part of the AEE of a producing resource project and claim 25% of the pooled expenditure against income from a producing resource project. The total amount of deductions allowed is limited to the lesser of 25% of the undeducted balance of the expenditure in the pool or such amount as reduces the tax payable by the taxpayer and its related corporations in respect of those resource operations for that year of income by 10%.

An election to pool exploration expenditure has to be made in writing, on or prior to the date of the first tax return in relation to that resource development license.

Rehabilitation costs

For resource projects that commenced on or after 1 January 2012, a resource taxpayer is able to transfer losses incurred in respect of environment rehabilitation incurred at the end of the project to other projects it owns. PNG uses ring-fencing provisions and calculates the profits of resource projects on a project-by-project basis. Historically, losses incurred when no further income was produced were effectively lost.

Tax losses

Losses incurred by taxpayers generally may be carried forward for 20 years, subject to the satisfaction of a continuity-of-ownership test for corporate taxpayers. If the continuity-of-ownership test is failed, tax losses may still be able to be carried forward and used if the taxpayer passes the same-business test.

Losses incurred by taxpayers carrying on resources operations (including oil and gas operations) are able to be carried forward indefinitely. Losses of resource taxpayers may also be quarantined on a project basis.

For resource taxpayers, the undeducted AEE and ACE balances are not considered tax losses for PNG tax purposes and are kept in separate pools. As discussed earlier, a taxpayer would need to be carrying on resource operations to claim deductions for AEE and ACE. Where a taxpayer is entitled to a deduction during a year of income, the deduction is limited to the amount of available assessable income. Any excess deduction cannot create a tax loss.

Losses are not allowed to be carried back, and there is no provision for grouping losses with associated companies (with the specific exception of certain company amalgamations).

Prescribed infrastructure development

Where a taxpayer engaged in resource projects incurs expenditure in relation to a prescribed infrastructure development, the amount of expenditure incurred is deemed to be income tax paid in respect of that project, and hence may be offset as a credit against tax payable in respect of the project. "Prescribed infrastructure development" means an upgrade of existing roads or construction of new roads or other infrastructure development in the project area or the surrounding areas, which are approved by the state. Accordingly, in order to qualify for the tax credits, all anticipated expenditure requires approval from the government.

The amount of credit available in respect of prescribed infrastructure development expenditure is capped at the amount of the expenditure and is also limited to the lesser of:

- 0.75% of the assessable income from the project
- The amount of the tax payable in respect of the project

Credits for expenditure incurred (for income tax deemed to be paid) may be carried forward.

A taxpayer engaged in gas operations is entitled to additional tax credits in respect of certain expenditure incurred on behalf of the state with respect to the construction or repair of certain roads. The amount of credit available in these circumstances is limited to the lesser of:

- 1.25% of the assessable income from the project
- 50% of the tax payable in respect of the project

Credits for expenditure incurred (or income tax deemed to be paid) may be carried forward. This regime in respect of gas projects is separate from that relating to general infrastructure credits (see above).

Highlands Highway — infrastructure tax credits

Tax credits were previously available for expenditure incurred in the income years 2002 and 2005, in respect of a prescribed section of the Highlands Highway.

From 1 January 2012, tax credits in respect of the Highlands Highway were reinstated where the expenditure incurred by a taxpayer is for "emergency repair" and the expenditure was incurred before 1 January 2015. "Emergency repair" means, in relation to the Highlands Highway, "an activity carried out to restore traffic flow following an event that has resulted in the closure or partial closure of the highway, including bypass or replacement of a section of the highway, replacement of culverts, construction of temporary bridges and removal and repair of landslips."

The amount of expenditure incurred is deemed to be income tax paid, and a credit is therefore available, limited to the lesser of:

- 1.25% of the assessable income derived by the taxpayer in the year of income
- The amount of tax payable

This credit is in addition to the prescribed infrastructure development credit of 0.75% (refer to the discussion above). Credits for expenditure incurred (or income tax deemed to be paid) may be carried forward. The regime is available to taxpayers engaged in mining, petroleum and gas operations. This brings the total of the infrastructure credits available to resource taxpayers to 2% (infrastructure development credit of 0.75% and Highlands Highway credit of 1.25%).

Research and development

Commencing 1 January 2014, the extended deduction of 50% has been phased out for research and development (R&D) expenditure. Previously, a 150% deduction was available for "prescribed" R&D expenditure. To claim the R&D concession, taxpayers needed to complete and submit an application annually to the Research and Development Expenses Approval Committee (within the PNG IRC) for approval before the start of the fiscal year.

However, any expenditure on scientific research incurred prior to 1 January 2014 will continue to be eligible. Further, while the additional deduction (of 50%) for eligible R&D expenditure is planned for abolition, such expenditure will continue to be deductible on a 100% basis — and even if such expenditure might otherwise be capital in nature.

WHT incentives

As noted above, specific WHT exemptions are applicable to the petroleum and gas industry in respect of the payment of dividends and interest.

E. Withholding taxes

Most activities conducted by nonresidents in PNG (including PNG branches), other than individuals deriving employment income, fall under the foreign contractor and management fee WHT provisions of domestic legislation. In addition, the receipt of certain passive income (e.g., interest, dividends and royalties) will also be subject to WHT.

Foreign contractor withholding tax

Foreign contractor withholding tax (FCWT) will apply where the income is derived by nonresidents (usually referred to as foreign contractors) from contracts for "prescribed purposes" that include installation and construction projects, consultancy services, leases of equipment and charter payments.

FCWT is levied in respect of the gross contract income, and, from1 January 2017, the tax rate is 15% (12% prior to 1 January 2017) on the gross contract payment. The local contracting party has an obligation to lodge a copy of the contract with the IRC within 14 days of signing the contract and to withhold the tax and remit it to the IRC within 21 days after the end of the month in which the payment was made.

Prior to 1 January 2017, a foreign contractor could, as an alternative to paying FCWT, elect to lodge an income tax return and pay tax on actual taxable income at the nonresident corporate tax rate of 48%. The FCWT is the default tax, with requests to be assessed on a net profit basis, being subject to the discretion of the Commissioner General. In order to be assessed on a net basis, a written request must be made to the Commissioner General prior to the end of the year following the year in which the contract was entered into. The FCWT deducted by the local contracting party is allowable as credit against the tax assessed. For residents of countries that have a double tax treaty with PNG and whose treaty contains a nondiscrimination clause, the rate of tax should be reduced accordingly. The position of these foreign contractors after 1 January 2017 is subject to review by the IRC on a case-by-case basis.

Where the foreign contractor elects to be assessed on actual taxable income, a deduction should be available for all costs directly attributable to the derivation of the PNG-sourced income, including depreciation of equipment. A deduction should also be available for any indirect costs related to the income (i.e., head office general administration and management expenses). The deduction for indirect costs allowed is limited to the lesser of:

- 5% of the gross income from the prescribed contract
  Or
- A percentage of head office expenses (other than expenses incurred directly in deriving the contract income) in proportion to the ratio of gross income from the prescribed contract relative to the worldwide income of the taxpayer

Please refer below for treaty WHT rates that may provide for relief from FCWT or a reduction in the FCWT rate.

Management fee withholding tax

Subject to the availability of treaty relief, management fee withholding tax (MFWT) of 17% is required to be deducted in respect of management fees paid or credited to nonresidents.

The definition of "management fee" is very broad and includes "… a payment of any kind to any person, other than to an employee of the person making the payment and other than in the way of royalty, in consideration for any services of a technical or managerial nature and includes payment for consultancy services, to the extent the commissioner general is satisfied those consultancy services are of a managerial nature."

In practice, MFWT is generally applied to services rendered outside PNG by nonresidents and FCWT to fees for services rendered within PNG by nonresidents.

Taxpayers should also be aware that the deduction for management fees paid by a PNG resident company to a nonresident associate cannot exceed the greater of 2% of assessable income derived from PNG sources or 2% of allowable deductions excluding management fees paid. Similarly, to the extent that management fees exceed 2% of AEE or ACE, the excess is not able to be included in AEE or ACE, respectively. However, a full deduction is allowed if the management fee can be supported as an arm's-length transaction. This limit does not apply in respect of payments made to non-associates.

Please refer below for treaty WHT rates that may provide relief from MFWT or reduction of MFWT.

WHT rates

In addition to FCWT and MFWT, WHT is imposed in respect of various payments to nonresidents by entities carrying on business in PNG, including interest, dividends and royalties. Certain incentive rates exist for taxpayers operating in the oil and gas industry (refer to sections regarding dividends and interest). Set out in the table below is a summary of general WHT rates. Taxpayers self-assess for any reductions in WHT applicable as a result of a double tax agreement.

	Dividends	Interest	Royalties	Management fees (including technical fees) %	Foreign contractor %
Australia	15	10	10	Nil[1]	15[2]
Canada	15	10	10	Nil[1]	15[2]
China	15	10	10	Nil[1]	15[2]
Fiji	15	10	15	15	15[2]
Germany	15	10	10	10	15[2,3]
Malaysia	15	15	10	10	15[2]
New Zealand	15	10	10	Nil[1]	15[2]
Singapore	15	10	10	Nil[1]	15[2]
South Korea	15	10	10	Nil[1]	15[2]
United Kingdom	15	10	10	10	15[2]
Non-treaty countries	15	15	Associate – 30 Non-associate – lesser of 10% of assessable income or 48% of taxable income	17	15

Notes:

1. Where there is no specific technical services article, the payment should not be subject to WHT in PNG, provided all of the services were performed outside of PNG.
2. The income of residents of countries with which PNG has a double tax agreement will be subject to the FCWT provisions only if the nonresident is conducting business in PNG through a permanent establishment.
3. Treaty is not yet in force.

F. Financing considerations

Where a taxpayer has borrowed money for the purpose of carrying out a resource project, the interest will be deductible under the normal provisions (i.e., on an incurred basis).

Where funds are not borrowed on an arm's-length basis, the interest deduction is limited to the market rate of interest that the Commissioner General determines in consultation with the Bank of Papua New Guinea. Interest incurred prior to the issue of a development license is not deductible.

Interest incurred in connection with the construction or acquisition of an item of plant or capital asset is not immediately deductible to the extent that it is incurred prior to the date on which the taxpayer first derives assessable income or uses the plant or capital asset for the purpose of deriving assessable income. The amount should instead be capitalized to the cost of the asset.

For resource projects, no interest deduction is allowable prior to issue of a development license. Also, specific thin capitalization rules exist for resource projects. When the debt of the taxpayer and all related corporations in relation to a particular resource project exceeds 300% of equity (i.e., when the debt-to-equity ratio exceeds 3:1) in relation to that resource project, the deduction for the interest incurred is reduced by the interest on the excess debt.

G. Indirect and other taxes

Goods and services tax

Goods and services tax (GST) is imposed at the rate of 10% on virtually all goods and services, except where the goods or services are zero-rated or are exempt. The importation of goods into the country will also be subject to GST.

Effective from 1 January 2012, any entity undertaking taxable activity in PNG is required to register and charge GST where taxable supplies exceed, or are expected to exceed, PGK250,000 in any 12-month period. (The previous registration threshold was PGK100,000.) Affected taxpayers should seek specific advice in this regard. Entities that are registered for GST are required to account for GST collected (output tax) and GST paid (input tax) during each month, with any excess of GST collected to be remitted to the IRC by the 21st day of the following month.

All supplies of goods or services, other than cars, to a resource company for use in resource operations are generally zero-rated. Taxpayers require written confirmation from the IRC stating that the entity is zero-rated to qualify for zero-rating. Taxpayers can then present the written confirmation to the suppliers when purchases are made to ensure the goods and services are supplied to them GST-free.

Royalty regimes

Resource projects are subject to a royalty, equal to 2% of the gross revenue from resource sales. New petroleum projects and gas projects are also subject to a development levy that is equal to 2% of the gross revenue from resource sales.

Prior to 1 January 2018, where a project is liable for both royalty and development levy, the royalty is claimable as a credit against income tax payable, and the development levy is an allowable deduction. Effective from 1 January 2018, both the royalty and development levy are allowable tax deductions. Unutilized credits arising prior to 1 January 2018 continue to be available as tax credits until utilized.

Customs and excise duties

The importation of all goods into PNG is subject to customs and excise duty, unless the goods are duty-free or exempt. Duty is imposed on the total cost of goods, including insurance and freight. The rate of duty depends on the nature of the goods imported. It will often be the case that a zero rate will apply to goods used in the oil and gas industry, to the extent that the relevant goods are not able to be sourced in PNG. However, a specific analysis must be undertaken in each instance.

Goods and consumables imported by a PNG LNG project entity in respect of the LNG project (referred to as LNG project goods and consumables) are exempt from all customs tariffs and levies. Recent changes to the Customs Act ensure the exemption is limited to goods and consumables used specifically in connection with the initial construction and subsequent phase of the PNG LNG project.

Export duties

There is no export duty on the export of petroleum or gas products.

Stamp duty

Stamp duty is imposed on dutiable instruments, such as deeds, share transfers and a wide range of other documents at varying rates. Stamp duty may also apply to documents executed outside PNG pursuant to provisions that impose an obligation to lodge documents for assessment for stamp duty where they relate to property or things done within PNG.

Where the property transferred is a mining lease, special mining lease or exploration license issued under the Mining Act 1992, or the subject of a license issued under the Oil and Gas Act 1998, the rate of duty is 2% of the value.

Minerals and petroleum farm-ins, transfers of mining or petroleum information, and transfers of tenements and exploration licenses are subject to stamp duty at the rate of the lesser of PGK10,000 or ad valorem duty up to a maximum of 5% of the value.

Where the acquisition is an interest in a landholding private corporation and the underlying land is a mining lease, special mining lease or exploration license, the rate of duty is 2% of the value. This excludes any amount that is mining or petroleum information. Where the underlying land comprises a tenement, or licenses or rights, or options over any such leases or rights, the rate of duty is the lesser of PGK10,000 or ad valorem duty up to the maximum of 5% of the value of the dutiable property.

Where the underlying property is mining or petroleum information, the rate of duty is PGK10,000.

Certain transactions with respect to the PNG LNG project are exempt from stamp duty.

Other taxes

Prior to 1 January 2018, all businesses with an annual payroll in excess of PGK200,000 were subject to a 2% training levy. The amount payable was reduced by training expenses incurred by the employer for the benefit of PNG citizen employees.

PNG does not have fringe benefits tax. However, noncash benefits to employees are taxed. The provision of some benefits is exempt (e.g., school fees and one set of annual leave fares), and other benefits are concessionally taxed.

Statutory requirements exist for employers to make superannuation contributions in respect of PNG citizen employees. Superannuation for noncitizen employees is currently voluntary. However, future legislation might make it compulsory.

PNG also has compulsory workers' compensation insurance requirements.

H. Other

Foreign-exchange controls

A tax clearance certificate is required where certain cumulative remittances of foreign currency exceed PGK200,000 in a calendar year. Under announcements made in the November 2017 budget, this limit is to be increased to PGK500,000 from 1 January 2018. Where the remittance is to a tax haven, a tax clearance will be required regardless of the amount being remitted.

In general, PNG resident companies are not permitted to receive payment for goods or services in a foreign currency. This means that, where a contract is entered into between two PNG residents in a foreign currency, such as US dollars, the settlement of the invoice has to be made in PNG currency. For exchange control purposes, a "resident" will include a foreign company operating actively in PNG on a branch basis.

Business presence

Forms of "business presence" in PNG typically include companies, foreign branches and joint ventures.

PNG-incorporated shelf companies are readily available. To register a branch of a foreign company, an application has to be lodged with the Registrar of Companies, accompanied by the relevant documentation. As a minimum, documents that need to be lodged include copies of the relevant contract in PNG, the certificate of incorporation and the application fee.

Tax office registration

An application for a tax file number is required for a PNG-incorporated subsidiary or a branch of a foreign entity that carries on business activities in PNG.

Where an entity has employees, the entity needs to register as a group employer and remit monthly salary and wages tax withholdings to the tax office.

GST registration is also required where taxable sales exceed, or are expected to exceed, PGK250,000 in an income year (as described above).

Visas

Expatriate employees cannot be gainfully employed in PNG without a work permit issued by the Department of Labour and Industrial Relations (DLIR). A properly completed Application for Foreigner Work Permit and the applicable government fee need to be lodged with the DLIR for approval for a work permit to be issued.

In addition to work permits, an application for an entry permit or visa for the employee and dependents (if applicable) will have to be prepared and lodged with the Department of Foreign Affairs and Immigration. There are government fees that need to accompany the application.

Peru

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ■ **Service contract**

A. At a glance

Fiscal regime

Oil and gas exploration and production (E&P) activities are conducted under license or service contracts granted by the Government of Peru. The Government guarantees that the tax law in effect on the agreement date will remain unchanged during the contract term.

Royalties

Royalties can be determined based on different methodologies: production scales; economic results; R-factor calculation; and cumulative production per oil field with price adjustments.

The other main elements of the fiscal regime for oil and gas companies in Peru are as follows:

- Corporate income tax (CIT) rate — 31.5%[1, 2]
- Production sharing contract (PSC) — not applicable
- Bonuses — not applicable
- Dividend tax — 5%
- Resource rent tax — not applicable
- Capital allowances — see Section C

B. Fiscal regime

Oil and gas E&P activities are conducted under license or service contracts granted by the Government. Under a license contract, the investor pays a royalty to the Government, whereas under a service contract, the government pays remuneration to the contractor for its activities.

As stated by the Peruvian Constitution and the Organic Law for Hydrocarbons, a license contract does not imply a transfer or lease of property over the area of exploration or exploitation. By virtue of the license contract, the contractor acquires the authorization to explore or to exploit hydrocarbons in a determined area, and Perupetro (the entity that holds the Peruvian state

1 *Oil and gas companies with license or service agreements are subject to a 2% premium. These two points should be added to the current income corporate tax rate (29.5% in 2017 onward), resulting in an income tax rate of 31.5%.*

2 *In addition, oil and gas companies must pay employee profit sharing. See Section J.*

interest) transfers the property right in the extracted hydrocarbons to the contractor, who must pay a royalty to the state.

It is important to note that the Organic Law for Hydrocarbons and the related tax regulations foresee that the signing of an oil and gas agreement implies the guarantee that the tax regime in effect at the date of signature will not be changed during the life of the contract. This is intended to preserve the economy of the contract so that no further tax costs are created for the contractors.

The signing of an agreement for the exploration or exploitation of a block freezes the tax regime in force at the date that the contract is signed for the entire life of the contract. An additional two percentage points will be applicable to the income tax rate of the tax regime in force (i.e., a current income tax rate of 29.5% plus 2%). The taxes covered by this provision are the taxes that are the responsibility of the contractor as a taxpayer.

It is important to note that tax stability is, in essence, granted for the contract activities and not directly for the entities that signed the contract. Therefore, any change in the contractor's ownership will not affect the tax stability. Equally, the tax stability covers only the contract activities (i.e., the exploration and exploitation of hydrocarbons) and no other related or distinct activities that may be performed by the legal entity (e.g., refining). Taxes (i.e., dividend tax or branch profits tax) that affect profit distributions arising from the contract activities are also covered by the tax stability.

Contractors are entitled to keep their accounting records in foreign currency, but taxes must be paid in Peruvian soles (PEN).

Corporate tax

General considerations

Resident corporations are subject to income tax on their worldwide income, whereas branches, agencies or other permanent establishments (PEs) of foreign corporations, while also being considered resident corporations, are subject to income tax exclusively on their Peruvian-sourced income. Exports are considered to be Peruvian-sourced income.

Resident corporations are companies incorporated in Peru. As from 1 January 2013, Peruvian law contains controlled foreign corporation (CFC) legislation.

Tax rates

The current CIT rate is 29.5%, which applies for 2017 and onwards.

In addition, a dividend tax of 5% applies to distributions of profits to nonresidents and individuals by resident companies and branches, permanent establishments and agencies of foreign companies. The 5% rate applies beginning 1 January 2017. For profits earned from 1 January 2015 to 31 December 2016, the former 6.8% withholding rate applies, even if the profits are distributed in 2017. The law specifies various transactions that are considered profit distributions by resident entities for the purpose of the dividend tax, including a distribution of cash or assets other than shares of the distributing company and, under certain circumstances, a reduction in the company's capital or a liquidation of the company.

Expenses that are not subject to further tax control (i.e., expenses that might benefit shareholders, such as personal expenses and other charges assumed by the corporation) are considered as a deemed dividend. However, the capitalization of equity accounts is not treated as a distribution.

For PEs, branches and agencies of foreign companies, a distribution of profits is deemed to occur on the deadline for filing their annual CIT return (generally, at the end of March of the following year).

The tax on dividends is basically applied through a withholding mechanism. The withheld amount is considered a final payment. Nevertheless, dividends related to expenses not subject to further tax control are subject to a dividend tax (i.e., it will be treated as deemed dividend distribution).

Taxable year

The taxable year is the calendar year. The accounting year is also the calendar year, without exception.

Tax returns

CIT returns must be prepared by the taxpayer under the self-assessment method. The annual income tax return must be filed within the first three months of the following tax year. Income tax prepayment tax returns must be filed monthly. Value-added tax (VAT), withholding tax (WHT) and other returns (e.g., payroll tax) are also filed monthly according to a schedule published by the tax authorities, based on the taxpayer's tax number.

The contractor has to determine the tax base and the amount of tax applicable. If the contractor carries out related activities (i.e., activities related to oil and gas but not carried out under the terms of the contract) or other activities (i.e., activities not related to oil and gas), the contractor is obliged to determine the tax base and the amount of tax separately and for each activity. The corresponding tax is determined based on the income tax provisions that apply in each case (subject to the tax stability provisions for contract activities, and based on the regular regime for the related activities or other activities).

The total income tax amount that the contractor must pay is the sum of the amounts calculated for each contract, for both the related activities and the other activities. The forms to be used for tax statements and payments are determined by the tax administration.

Monthly income tax prepayments

Taxpayers are required to pay estimated monthly income tax prepayments, which must be calculated, in general terms, based on the following methods:

- Percentage method: by applying 1.5% to the total net revenue of the month
- Ratio method: by dividing the tax calculated in the previous year by the total accrued net revenues of the same year and applying the ratio to the net accrued revenues of the month.

Income tax prepayments apply as a credit against the annual income tax obligation. They can be refunded at the end of the fiscal year (once the tax return is filed) if they exceed the annual income tax assessed.

Group treatment

Peruvian tax law does not include any provisions regarding taxation on a consolidated basis.

Ring fencing

If the contractor has more than one contract, it may offset the tax losses generated by one or more contracts against the profits resulting from other contracts or related activities. Likewise, the tax losses resulting from related activities may be offset against the profits from one or more contracts.

It is possible to choose the allocation of tax losses to one or more of the contracts or related activities that have generated the profits, provided that the losses are depleted or are compensated to the limit of the profits available. The tax losses are allocated up to the limit of the profits available in the block or related activities. If there is another contract or related activity, a taxpayer may continue compensating for the tax losses until they are fully utilized.

A contractor with tax losses from one or more contracts or related activities may not offset them against profits generated by the other activities. Furthermore, in no case may tax losses generated by the other activities be offset against the profits resulting from the contracts or from the related activities.

Income recognition

For local corporate purposes, income is recognized on an accrual basis.

Transfer pricing

Peru has adopted transfer pricing guidelines, based on the arm's-length principle. The accepted methods are the comparable uncontrolled price (CUP) method, the resale price method, the cost plus method and the transactional net margin method, as well as other related methods based on margins. Guidelines of the Organisation for Economic Co-operation and Development (OECD) can be used as a complementary source of interpretation. Advance pricing agreements (APAs) may be agreed with the tax authorities.

In Peru, these rules do not apply only to transactions between related parties, but also to transactions with entities that reside in tax havens. However, adjustments to the value of related-party transactions should occur only if the value agreed between the parties results in the payment of lower taxes under specific criteria.

One or more legal entities are related parties if one of them participates directly or indirectly in the management, control or equity of the other one, or whenever the same person participates directly or indirectly in the direction, control or equity of diverse related entities.

From 1 January 2013, specific parameters will be taken into account when determining the fair market value of import and export transactions of goods (i.e., hydrocarbons and their by-products) between related parties. These parameters will apply where an international intermediary (other than the effective recipient of those goods) intervenes to carry out the import and export transaction from, towards or through a tax haven.

On 31 December 2016, Peru published Legislative Decree No. 1312 amending the Peruvian transfer pricing (TP) reporting requirements by implementing the changes proposed by the OECD under the Base Erosion and Profit Shifting (BEPS) Action 13 final report. The bill expands the TP documentation requirements by introducing an obligation to submit both a local file (2017) and a master file (2018), as well as the implementation of country-by-country reporting (2018), provided that certain revenue thresholds are reached. Failure to comply could result in penalties.

Legislative Decree No. 1312 also introduces revised guidance for pricing cross-border commodity transactions. It provides that the CUP method can be the most appropriate transfer pricing method for commodity transactions between associated enterprises using a quoted price as a reference to determine the arm's-length price.

These rules establish that the arm's-length price for Peruvian income tax purposes shall be determined by reference to the quoted price of (i) the date of shipment of the commodities exported or (ii) the date of disembarkation of the commodities imported.

In addition, it introduces general transfer pricing guidelines for intragroup services and in particular for services that qualify as low value-adding intra group services.

Specifically, it requires that the "benefit test" should be satisfied to demonstrate that the services were in fact received in order for the cost or expense to be deductible. The test will be met by considering whether an independent company in comparable circumstances would have been willing to pay for the activity if performed for it by an independent company or would have performed the activity in-house for itself.

Capital gains

Capital gains are treated as ordinary income. Capital gains, determined by resident entities are subject to a 29.5% tax rate.

From 1 January 2016, capital gains derived from the sale of shares and other securities representing shares (i.e., American depositary receipts (ADRs), global depositary receipts (GDRs) and exchange-traded funds (ETFs)) carried out through the Lima Stock Exchange are exempt from income tax, subject to certain conditions. The exemption is effective until 31 December 2019.

Expenses

Expenses incurred in the generation of revenue, in maintaining the revenue source or in the generation of capital gains, are generally deductible for determining the income tax base.

However, expenses derived from transactions executed with entities (corporations or branches) that reside in tax havens are not deductible for the computation of taxable income, with the exception of payments derived from the following transactions: credit facilities and insurance, assignment of ships or aircrafts, transportation from/to the country and the tax haven, and fees for passage through the Panama Canal.

Peruvian income tax regulations contain a list of countries considered as tax havens for income tax purposes. Notwithstanding this, countries not included on the list can be qualified as tax havens if their effective income tax rate is 0% or the effective income tax rate is less than 50% of the rate that would apply in Peru over the same kind of income. From 1 January 2013, if Peru signs a double taxation agreement that includes a clause for exchanging information with another country, that country will no longer be regarded as a tax haven for CIT purposes.

Organization expenses, initial pre-operating expenses, pre-operating expenses resulting from the expansion of a company's business and interest accrued during the pre-operating period may be deducted, at the taxpayer's option, in the first taxable year, or they may be amortized proportionately over a maximum term of 10 years. The amortization period runs from the year when production starts. Once the amortization period is fixed by the taxpayer, it can be varied only with the prior authorization of the tax authorities. The new term comes into effect in the year following the date that the authorization was requested, without exceeding the overall 10-year limit.

It is necessary to use certain means of payment for the deduction of expenses in excess of PEN3,500 (equivalent to approximately US$1,100) or US$1,000. The permitted means of payment include deposits in bank accounts, fund transfers, payment orders, debit and credit cards issued in Peru, non-negotiable (or equivalent) checks issued under Peruvian legislation and other means of payment commercially permitted in international trading with nonresident entities (e.g., transfers, banking checks, simple or documentary payment orders, simple or documentary remittances, simple or documentary credit cards).

Research and development expenses (R&D) shall be deductible in the fiscal year in which they are accrued. The deduction is allowed even if the expenses are not related to the core business of the company.

As from January 2016, R&D projects duly certified by Peruvian authorities are granted with an additional deduction of 50% (if the project is developed by a non-domiciled research institution) or 75% (if the project is carried out directly by a Peruvian company or by a domiciled research institution), if certain conditions are met. The amount of the additional deduction is capped to 1,335 tax units (approximately US$1.5m). This benefit will be effective until 31 December 2018.

Valuation of inventory

Inventory is valued for tax purposes at the acquisition or production cost. Finance charges are not allowed as part of the cost. Taxpayers may choose any one of the following methods to calculate annual inventory for tax purposes, provided that the method is used consistently: first-in, first-out (FIFO); daily, monthly or annual average; specific identification; detailed inventory; or basic inventory.

Foreign income tax

Under certain circumstances, income tax paid abroad may be used as a tax credit. However, it should be noted that unused tax credits cannot be carried forward.

Controlled foreign corporation rules

As from 1 January 2013, the "international fiscal transparency regime" is applicable to all Peruvian residents who own a CFC. Under these rules, passive income earned by CFCs in other jurisdictions must be included and recognized in the taxable income of resident taxpayers in Peru, even though there has been no effective distribution.

A nonresident subsidiary company will constitute a CFC of a Peruvian company if:

- The Peruvian company owns more than 50% of the subsidiary's equity, economic value or righting votes.
- The nonresident entity is resident of either a tax haven jurisdiction or a country in which passive income is either not subject to CIT, or is subject to a CIT, that is equal to or less than 75% of the CIT that would have been applicable in Peru.

For the application of this CFC regime, the law has established an exhaustive list of items that qualify as passive income (dividends, interest, royalties, capital gains from the sale of properties and securities, etc.).

Royalties

Oil and gas E&P activities are conducted under license or service contracts granted by the Government. Under a license contract, the investor pays a royalty to the Government, while under a service contract, the Government pays remuneration to the contractor.

In both cases, however, the distribution of the economic rent (royalty or remuneration) between the Government and the investor is determined based on the following methodologies:

- Production scales
  - Under this methodology, the percentage of the royalty (or brackets of royalties starting at 5%) is determined over certain scales of production (volume of barrels of liquid hydrocarbons, natural gas liquids and natural gas, called "fiscalized hydrocarbons," per calendar day) for a specific period, according to the following scale:

Scales of production (barrels per calendar day)	Percentage royalty
< 5	5%
5–100	5% to 20%
> 100	20%

- Economic results (RRE)
  - According to this methodology, the royalty percentage is obtained as result of adding a fixed royalty percentage of 5% to a variable royalty percentage. The variable royalty percentage (in a range between 5% and 20%) is calculated once the ratio between revenues and expenditures as of the previous year is at least 1.15.
- Other methodologies
  - R-factor and cumulative production per oilfield with price adjustments. In the case of the R-factor, the royalty is calculated by applying a ratio between revenues and expenditures of certain periods established in the contract. For these purposes, the minimal percentage of royalty is as given in the table below.

R-factor	Minimum royalty percentage
From 0.0 < 1.0	15%
From 1.0 < 1.5	20%
From 1.5 > 2.0	25%
From 2.0 or more	35%

The definitive percentages will generally be negotiated and established in each contract. However, in the case of cumulative production per oilfield with price adjustments, the royalty is calculated based on a specific percentage per oilfield for a contract. The royalty is adjusted based on two factors: the cumulative production of each oilfield and the average price per barrel of such production.

Hydrocarbon royalties paid by oil and gas companies shall be considered as deductible expenses for income tax purposes.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Depreciation of tangible assets

According to the income tax regulations, the maximum annual depreciation rates for income tax purposes are as follows: 20% for vehicles; 20% for machinery and equipment used in the mining, oil and construction industries; 10% for other machinery and equipment; 25% for hardware; and 10% for other fixed assets. Under the income tax general provisions, depreciation is deductible provided that it does not exceed the maximum rates and it is registered in the taxpayer's accounting records, regardless of the depreciation method used.

Buildings are subject to a fixed 5% depreciation rate, without the accounting record requirement. However, the Government has recently approved an exceptional and temporary depreciation regime applicable for years 2015–16, which allows taxpayers to depreciate buildings by applying an annual rate of 20% for income tax purposes. This regime only applies if the goods are used for business purposes and if the following conditions are met:

- The construction of the building had begun by 1 January 2014.
- By 31 December 2016, the construction has been at least 80% completed.

Special oil and gas rules regarding investments aimed to produce hydrocarbons

The hydrocarbon law provides that exploration and development expenditures, and the investments that contractors may make, up to the date when commercial extraction of hydrocarbons starts, including the cost of the wells, are accumulated in an account. At the contractor's option and with respect to each contract, the amount is amortized using either of the methods below:

- Units of production
- Linear amortization, deducting the expenditures in equal portions over a period of no less than five fiscal years

Any investments in a contract area that did not reach the commercial extraction stage and that were totally released can be accumulated with the same type of investments made in another contract that is in the process of commercial extraction. These investments are amortized in accordance with the amortization method chosen in the latter contract.

If the contractor has entered into a single contract, the accumulated investments are charged as a loss against the results of that contract in the year of total release of the area for any contract if the area did not reach the commercial extraction stage. Investments consisting of buildings, power installations, camps, means of communication, equipment and other goods that the contractor keeps or recovers to use in the same operations or in other operations of a different nature cannot be charged as loss against the contract.

Once commercial extraction starts, all amounts corresponding to disbursements with no recovery value are deducted as expenses for the fiscal year. Expenses with no recovery value at the start of commercial extraction include:

- Investments for drilling, completing or producing start-up wells of any nature, including stratigraphic ones, and excluding acquisition costs of surface equipment

- Exploration investments, including those related to geophysics, geochemistry, field geology, gravimetry, aerophotographic surveys and seismic surveying, processing and interpreting

The *Manual of Accounting Procedures* to be filed before Perupetro must detail the accounts considered expenditures without any recovery value.

D. Corporate tax incentives

Carryforward losses

Tax losses can be carried forward and offset against net income derived in future fiscal years. The provisions currently in force require the taxpayer to elect one of the following procedures to offset the tax losses:

- Offset the total net tax losses from Peruvian sources incurred in a tax year against net income derived in the four fiscal years following its generation. The amount of losses not offset after this term are canceled.
- Offset the total net tax losses from Peruvian sources obtained in the tax year against 50% of the net income obtained in the following years, without limitation.

The election should be made when the annual income tax return is filed (see Section B), and it cannot be changed until the accumulated losses are fully utilized.

Loss carrybacks are not allowed.

E. Withholding taxes

Dividends or branch profits tax

Dividends and profits obtained by branches are subject to a 5% WHT.

The event that triggers the withholding obligation is the dividend distribution agreement. However, in the case of branches, it is triggered when the tax return is filed at the end of the income year.

It should be noted that the effect of the increase of the dividend tax rate combined with the reduction of the corporate tax rate results in a total tax burden of 33% (approximately) in each fiscal year.

Interest

The WHT rate on interest paid abroad is 30%. However, if certain conditions are met, this rate can be reduced from 30% to 4.99%. The 4.99% reduced WHT rate applies if the following conditions are met:

- For loans in cash, the remittance of funds to Peru must be duly documented and, to meet this requirement, the funds should enter the country through a local bank or be used for import financing.
- The loans are subject to an annual interest rate (including fees and any additional amounts) no higher than the London Interbank Offered Rate (LIBOR) plus seven basis points.
- The lender and the borrower are not regarded as economically related parties.
- The loan does not qualify as a "back-to-back" or "covered" operation between related parties.

The WHT rate on interest paid abroad to nonresident individuals is 30% when the transaction is performed between related parties or with entities that reside in tax havens; otherwise, a 4.99% WHT rate will be applicable.

Royalties

Royalties are defined as any payment in cash or in kind from the use or the privilege to use trademarks, designs, models, plans, process or secret formulas and copyrights for literary, artistic or scientific work, as well as any compensation for the assignment of software or the transfer of information related to industrial, commercial or scientific experience (know-how).

The WHT rate applicable to royalties is 30%.

Capital gains

Gains on the sale, exchange or redemption of shares, bonds and other securities issued by companies, investment funds or trusts incorporated or organized in Peru are considered to be Peruvian-sourced income. The same applies to capital gains derived from ADRs and GDRs whose underlying company is incorporated in Peru.

The income tax treatment of capital gains made by non-domiciled entities depends on whether the transfer takes place within or outside Peru. If the transfer takes place in Peru, the WHT rate is 5%; otherwise, it is 30%, unless it qualifies for the exemption mentioned in C (capital gains derived from the sale of shares and other securities representing shares (i.e., ADRs, GDRs, and ETFs) carried out through the Lima Stock Exchange. When the disposal is conducted through a centralized negotiation mechanism, the settlement agent (CAVALI in Spanish) will have to withhold the corresponding income tax (if applicable).

Since capital gains on shares listed on a local stock exchange before 1 January 2010 were exempt from income tax, some specific rules are applicable to determine their referential value (tax cost). In this context their value at the end of fiscal year 2009 would be the acquisition cost, or the value of entry to the equity, whichever is the highest.

Indirect transfers of shares

From 16 February 2011, Law No. 29663 introduced a new category of Peruvian-sourced income that may lead to a scenario under which a nonresident will be levied for income tax. Broadly, Law No. 29663 provides that a 30% income tax is imposed on any capital gain realized upon the transfer of the shares of a company located outside Peru that, directly or indirectly, holds shares (or participation interests) in one or more Peruvian subsidiary (i.e., an "indirect transfer") in one of the following situations:

1. Fifty percent or more of the fair market value of the nonresident holding company's shares is derived from the shares or participations representing the equity capital of one or more Peruvian subsidiaries at any time within the 12 months preceding the disposition

   Or

2. The overseas holding company is located in a tax haven or low-tax jurisdiction, unless it can be adequately demonstrated that the scenario described in (1) above did not exist.

Law No. 29757, which amended Law No. 29663 from 22 July 2011, clarifies that the transaction described in the preceding text will be taxable only if shares or participation interests representing 10% or more of the nonresident holding company's equity capital are transferred within the 12-month period. This means that transfers of shares (or participations) representing less than 10% of the nonresident holding company's equity capital are not subject to taxation in Peru even when 50% or more of the fair market value of those shares is derived from the shares (or participations) representing the equity capital of one or more Peruvian subsidiaries at any time within the 12 months preceding the dispositions.

Services

Technical assistance, digital services and other services

Revenue received from certain activities performed by non-domiciled companies is subject to Peruvian WHT on a portion of the gross revenues earned from such activities. The WHT rate varies according to the activity performed. For services, the following distinctions can be made:

- Payments for services that qualify as "technical assistance" (defined below) are subject to a 15% WHT rate, provided that they are "economically utilized" within Peru regardless of whether the services are physically rendered in Peru.
- Technical assistance is considered to be economically utilized if it helps in the development of activities or the fulfillment of the purpose of resident entities, regardless of whether it generates taxable income. Moreover,

Peruvian corporations that obtain business income and consider the compensation for technical assistance as a cost for income tax purposes are deemed to utilize the service in the country economically.

Current Peruvian income tax regulations define the concept of "technical assistance" as any independent service, whether performed abroad or within the country, through which the provider employs its skills by applying certain procedures or techniques, with the sole purpose of providing specialized knowledge that is not the subject of a patent, that are required for the productive process (including commercialization), rendering services or any other activity performed by the user of the service. "Technical assistance" also comprises training people for the application of the specialized knowledge.

Even though it is necessary to verify that all the characteristics are met in order to determine whether an activity qualifies as technical assistance, it is important to highlight that the income tax regulations cite three cases in which technical assistance is understood to exist:

- Engineering services
- Investigation and project development
- Assistance and financial consulting

These terms are all defined in the income tax law.

If technical assistance services are provided together with another type of services, the compensation corresponding to each of the activities must be identified in order to grant the corresponding tax treatment. However, if it is not possible to identify the amounts separately due to the nature of the operation, the amount must be treated under the rules that apply to the essential and predominant operation.

It is important to note that if the total consideration for rendering technical assistance services exceeds 140 tax units (where 1 tax unit = PEN4,150, equivalent to approximately US$1,277), taxpayers must supply a certification from an audit company stating that the hours and services provided have been effectively rendered, in order to apply the 15% WHT rate for technical assistance.

Payments for "digital services" (a term that covers a group of activities developed through the internet) are subject to a 30% WHT if they are economically utilized in Peru, regardless of where they are performed in Peru.

Services that do not qualify as technical assistance or digital services are subject to a 30% WHT, provided that they are developed within Peru. No WHT applies to services performed wholly abroad. If services are performed partially in Peru and partially abroad, a pro rata or allocation system may be used to determine the portion of the compensation for the service that is subject to WHT.

Other activities rendered partially in Peru and partially abroad

Activities undertaken partially in Peru and partially abroad by non-domiciled companies, including revenue generated by their branches or PEs, are subject to WHT on a portion of the gross revenues generated, according to the following chart (and, unless otherwise indicated, the WHT rate is 30%):

Activities	Percent of gross revenues	Effective tax rate %
Air transport	1	0.3
Ship leases	80	8.0*
Aircraft charters	60	6.0*
Supply of transport containers	15	4.5
Storage of transport containers	80	24.0
Insurance	7	2.1
International news services	10	3.0

Activities	Percent of gross revenues	Effective tax rate %
Sea transport	2	0.6
Motion picture distribution	20	6.0
Television broadcast rights	20	6.0
Telecommunications services	5	1.5

* The WHT rate for these activities is 10%

Services rendered by independent professionals

Independent professionals are subject to WHT at a 24% effective rate. This is the result of applying the general 30% rate to 80% of the income received.

Tax treaties

Peru has entered into a multilateral tax treaty with the Andean Community countries (Bolivia, Colombia and Ecuador), which calls for exclusive taxation at source and bilateral income tax treaties with Brazil, Chile, Canada, Mexico, South Korea, Portugal and Switzerland.

Some existing treaties are being renegotiated and others are in various stages of negotiation with countries, such as France, Italy, Thailand, Sweden, Singapore and the UK.

Except for the tax treaty with the other Andean Community countries, tax treaties entered into by Peru generally follow the OECD model, although they incorporate provisions derived from the United Nations model.

F. Financing considerations

Thin capitalization

Thin capitalization rules prohibit a tax deduction for interest paid by domiciled taxpayers to related or associated enterprises. To date, the maximum debt-to-equity ratio allowed under the thin capitalization rules is 3:1.

G. Transactions

The transfer of assets, as well as of interests in contracts (farm-in or farm-out arrangements), are subject to the common income tax and VAT rules.

H. Indirect taxes

VAT

VAT is subject to tax stability, but only for the transferable nature of the VAT charged by the buyer to the seller. The stabilized regime for VAT and other selective consumption taxes (e.g., Peru's luxury tax, the so-called *Impuesto Selectivo al Consumo*) also applies for exporters, which means that exports are not subject to any tax.

It should also be mentioned that the import of goods and inputs required for exploration activities is free from any taxes (based on a list detailing such goods approved by the Government authorities).

VAT at 18% applies to the following operations:

1. The sale of goods within Peru
2. Services performed within Peru
3. Services performed by nonresidents within Peru
4. Construction
5. The first sale of real estate by a builder
6. The import of goods (including intangible assets).

For activities 1, 2, 4 and 5, the VAT payable is determined on a monthly basis by deducting credited VAT paid (i.e., input tax) from the gross tax charged (i.e., output VAT) in each period. As a result, VAT does not necessarily represent a financial cost but can be met through offsetting the input tax against the output tax charged in the tax period.

However, VAT paid on the import of goods or the utilization of services within Peru must be paid directly to the tax authorities, meaning that the VAT to be paid must equal the output tax with no deduction for any input VAT credit. This payment may be used as a VAT credit once paid. This can result in a financial cost as a VAT credit for the period from the date of payment until the amount is applied to offset the output tax arising from the activities in 1, 2, 4 and 5.

The output tax due for each taxable operation is calculated by applying the 18% VAT to the tax base (made up of the price of goods, services or construction contracts). The VAT credit consists of the VAT separately itemized in the payment voucher (or corresponding document) issued for any of the activities in 1 to 6.

VAT paid can be used as a VAT credit if the following conditions apply:

- The acquisition is allowed as an expense or cost for income tax purposes.
- The acquisition is intended for operations that give rise to an obligation to pay the VAT.
- The tax must be stated separately in the payment voucher that must be completed according to the corresponding legal provisions.
- The amount must be registered appropriately in the accounting records of the purchaser (i.e., in the purchase ledger).

Nonresident purchasers of goods or services are not permitted to use the VAT charged as a credit, and no reimbursement is allowed under the Peruvian VAT law. Any VAT paid by a nonresident purchaser, therefore, becomes an additional cost.

The VAT credit treatment is summarized in the charts below (where the dates used are examples only). For purchasing goods in Peru, the acquisition of services performed by local entities, construction contracts or acquisitions of real estate under its first sale, we have:

Acquisition in March 2016	→	Generates a 18% VAT credit (input VAT)	→	VAT credit may offset gross tax (output VAT) for March 2016 or become a VAT credit if exports are made.	→	Pay VAT if gross tax exceeds VAT credit (tax return to be filed within first 10 days of April 2016)

For the utilization of services in Peru performed by nonresident entities, we have:

Service used in March 2016	→	VAT of 18% (gross basis without credit deduction) should be paid by domiciled entity to tax authorities when compensation is paid or when an invoice is recorded in the purchase ledger. Payment is made together with the March 2016 monthly tax return that is filed within the first 10 days of April 2016.	→	VAT paid in April should be included in a VAT credit for the period covered by the tax return filed within the first 10 days of May 2016.

For imported goods subject to VAT, we have:

Import in March 2016	→	VAT of 18% is paid when customs clearance is requested; payment is made to the customs authorities (assuming they are cleared in March 2016) and supported by an import declaration.	→	VAT paid in March could be considered as a VAT credit for the period covered by the tax return filed within the first 10 days of April 2016.

Exporters are reimbursed with any VAT paid on the acquisition of goods and services. Also, exporters can apply this reimbursement as a credit in order to offset VAT or income tax liabilities. Any balance may be refunded by the tax administration.

Early recovery VAT system

Peru's early recovery VAT system allows early recovery of the VAT credit for acquisitions of goods, services, construction contracts, importations, etc., without waiting to recover such amount from a client when the invoice, including VAT, for the sales of goods, services or construction contracts is issued to the client. In other words, this regime provides relief of financial costs (cost of money) for projects with a significant pre-operating stage and for which no advance invoice (transferring the VAT burden) can be issued periodically to the client.

The law provides a general and a specific early recovery system:

- General early recovery VAT system: for the recovery of VAT on capital goods only
- Specific early recovery VAT system: for companies that (1) enter into investment contracts with the Peruvian Government and (2) make a minimum investment commitment of US$5 million for projects with a preoperative phase of at least two years:
  - This system is applicable to the recovery of VAT on capital goods, services and construction contracts.

The use of one system does not preclude the possibility of using the other, as they each have a different scope.

Definitive VAT recovery for hydrocarbon exploration activities

Under this regime, VAT paid on the acquisition of goods and services used directly in oil and gas exploration activities can be recovered without having to wait until a commercial discovery takes place or production begins.

The application of this regime has been extended until 31 December 2018.

Joint ventures

VAT does not apply to the allocation of costs and expenses incurred by the operator in a joint venture that does not keep independent accounting records. Nor does it apply to the assignment of resources, goods, services and construction contracts made by the parties of a joint venture agreement for the performance of their common business or the allocation of the goods produced for each party under the agreement.

Likewise, any grant, sale, transfer or assignment of an interest in a joint venture is not subject to VAT.

Joint ventures that keep independent accounting records are considered to be legal entities, and they are subject to VAT. Joint ventures that do not keep independent accounting records must allocate the income to each of the parties involved in the contract in proportion to their interest in the contract.

Customs duties

The custom duty rates that apply on the importation of goods into Peruvian territory are 0%, 6% and 11%, depending on the tariff classification of the goods. Customs value is assessed using the valuation rules of the World Trade Organization (WTO). Most capital goods are covered by the 0% rate.

The importation of certain goods and inputs during an oil or gas exploration phase is tax-free; however, these goods must be included in a list to be approved by means of a Ministerial Resolution.

Goods can be temporarily imported for a period of up to four years. Import taxes (customs duties, if applicable, plus VAT) are suspended for temporary imports.

Selective consumption tax

The selective consumption tax (Spanish acronym ISC) applies to luxury goods, whether individually or jointly with others such as jewelry, cars, cigars, cigarettes, liquor, soft drinks, fuel and others. ISC rates range from 10% to 100%, generally based on the cost, insurance and freight (CIF) (imports) or sale value, depending on the goods. However, for certain goods, such as soft drinks and fuel, the ISC is calculated on a specific basis depending on the amount of goods sold or imported. The following chart shows ISC applicable to fuels:

Selective Consumption Tax on fuels			
Tariff heading	Products	S/per gallon	US$ per gallon*
2701.11.00.00	Anthacites for energetic use	51.72 (per ton)	170.16
2701.12.00.00-2701.19.00.00	Bituminous coal for energetic use, and other coals	55.19 (per ton)	181.58
2710.12.13.10	Gasoline for motors with Research Octane Number (RON) less than 84	1.27	0.39
2710.12.19.00			
2710.12.20.00			
2710.20.00.90			
2710.12.13.21	Gasoline for engines with RON equal or over 84, but less than 90, and with 7.8% volume of fuel alcohol	1.22	0.37
2710.12.19.00			
2710.12.20.00			
2710.20.00.90			
2710.12.13.29	Gasoline with RON equal or over 84, but less than 90	1.27	0.39
2710.12.19.00			
2710.12.20.00			
2710.20.00.90			
2710.12.13.31	Gasoline for engines with RON equal or over 90, but less than 95, and with 7.8% volume of fuel alcohol	1.16	0.35
2710.12.19.00			
2710.12.20.00			
2710.20.00.90			
2710.12.13.39	Other fuels with RON over or equal to 90 but less than 95	1.21	0.37
2710.12.19.00			
2710.12.20.00			
2710.20.00.90			
2710.12.13.41	Gasoline for engines with RON equal or above 95, but less than 97, and with 7.8% volume of fuel alcohol	1.13	0.34
2710.12.19.00			
2710.11.20.00			
2710.20.00.90			
2710.12.13.49	Other fuels with RON over or equal to 95 but less than 97	1.17	0.36
2710.12.19.00			
2710.12.20.00			
2710.20.00.90			

Selective Consumption Tax on fuels			
Tariff heading	Products	S/per gallon	US$ per gallon*
2710.12.13.51 2710.12.19.00 2710.1.20.00 2710.20.00.90	Gasoline with RON equal or above 97 and engines with 7.8% volume of fuel alcohol	1.13	0.34
2710.12.13.59 2710.12.19.00 2710.12.20.00 2710.20.00.90	Other fuels with RON equal or above 97	1.17	0.36
2710.19.14.00/ 2710.19.15.90	Kerosene and Jet Fuels (Turbo A1), except certain sales in the country or imports for airships.	1.93	0.59
2710.19.21.10/ 2710.19.21.90	Gasoils, except Diesel B2	1.47	0.45
2710.19.21.11/ 2710.19.21.99	Gasoils	1.58	0.48
2710.19.21.11/ 2710.19.21.99	Rest of gasoils, except Diesel B2 and Diesel B5	1.26	0.38
2710.19.21.20	Diesel B2	1.44	0.44
2710.19.21.21	Diesel B2 with sulfur content equal or below 50 ppm	1.04	0.32
2710.19.21.29	Rest of Diesel B2	1.24	0.38
2710.19.21.31	Diesel B5 with sulfur content equal or below 50 ppm	1.01	0.31
2710.19.21.39	Rest of Diesel B5	1.20	0.36
2710.19.22.10	Residual 6, except sales in the country or imports by certified seacraft fuel marketers.	0.92	0.28
2710.19.22.90	Other fuels	1.00	0.30
2710.20.00.11	Diesel B2 with sulfur content equal or below 50 ppm	1.70	0.52
2710.20.00.12/ 2710.20.00.13	Diesel B5 and Diesel B20 with sulfur content equal or below 50 ppm	1.49	0.45
2710.20.00.19	Other mixes of Diesel B2 with Biodiesel B 100	1.70	0.52
2711.12.00.00/ 2711.19.00.00	Liquefied Oil Gas	0.00	0.00

*US$1 = PEN 3.29

Taxable persons for ISC purchases are producers and economically related enterprises engaged in domestic sales of listed goods, importers of listed goods, importers and economically related enterprises engaged in domestic sales of listed goods, and organizers of gambling activities.

Liability to ISC arises under the same rules that apply to VAT.

To avoid double taxation, a credit is granted for any ISC paid on imports and in other specific cases.

I. Other taxes

Financial transaction tax

Operations made through Peruvian bank accounts (deposits and withdrawals) are subject to a financial transaction tax, charged at the rate of 0.005%.

Temporary net assets tax

Temporary net assets tax (Spanish acronym ITAN) has been in force since fiscal year 2005 and is equal to 0.4% of the value of the total assets more than PEN1 million. The ITAN obligation is determined based on the balance sheet as of 31 December of the previous year.

ITAN may be paid in a single amount or nine monthly quotas (i.e., a fractional payment). In the first case, the payment must be made with the ITAN return submitted in April. ITAN payments may be used as a tax credit to offset income tax liabilities (i.e., monthly prepayments and the income tax payment due when the annual income tax return is filed).

Likewise, according to the ITAN law, taxpayers that are obliged to pay taxes abroad related to income arising from Peruvian sources may choose to pay the ITAN due with the amount paid for the monthly prepayments of income tax. This option may be used only if the taxpayer has chosen to make the payment in fractional amounts.

Taxpayers choose the option by filing a sworn declaration; this declaration must be submitted when the taxpayer files its ITAN returns. If the declaration is not filed on time, it is considered not submitted and, therefore, the taxpayer may not apply for the option for the remainder of the fiscal year.

Taxpayers that choose this option may use the amount paid as a tax credit, as shown in the next table.

Income tax prepayment corresponding to period	May be used as a tax credit against the quota of ITAN expiring in the corresponding month
March	April
April	May
May	June
June	July
July	August
August	September
September	October
October	November
November	December

If the amount of the income tax prepayments is higher than the amount of the ITAN to be offset, according to the chart above, the balance may not be used against the next quota.

If the taxpayer chooses the option and directly pays some quotas of ITAN, it may not use the ITAN paid as a credit against income tax. In such cases, the ITAN paid may be regarded as an expense.

The income tax prepayments, which have been used as a tax credit against the ITAN, may also be used as a tax credit (without a right of refund) against the income tax due.

Municipal taxes

Real estate tax

The real estate tax affects real estate held by corporations and individuals. The tax rates are determined using a progressive accumulative scale based on the property's value, as set out in the table below.

Real estate value	Rate
Up to 15 tax units	0.2%
More than 15 and up to 60 tax units	0.6%
More than 60 tax units	1.0%

Vehicle tax

The vehicle tax applies to vehicles held by corporations and individuals. The tax rate is 1% of the original value upon acquisition or importation of the vehicle.

This tax applies to vehicles registered with the Vehicular Properties Office of the Public Registry in the previous three years.

Alcabala tax

Real estate transfers are subject to a 3% alcabala (sales) tax. The taxable base is the transfer value, which cannot be less than the self-assessed value of the property. The first 10 tax units are exempt.

Alcabala tax must be paid by the purchaser within the calendar month following the month the transfer is made.

J. Regulatory contributions and other charges

- Osinergmin contribution

  This contribution must be paid by oil and gas companies that import or produce fuels, including liquefied petroleum gases and natural gas, or carry out transportation and distribution activities. The rate of this contribution is 0.36% (for import or production activities) and 0.57% (for transport and distribution activities), and it is based on their monthly billing, deducting VAT.

- Agency for Environmental Assessment and Enforcement (OEFA) contribution

  Oil and gas companies that import or produce fuel, including liquefied petroleum gases, or carry out transport and distribution activities should pay the OEFA contribution. The rate of this contribution is 0.09% (for import or production activities) and 0.11% (for transport and distribution activities), and it is based on their monthly billing, deducting VAT.

- Energetic Fund for the Social Inclusion (FISE)

  This contribution must be paid by oil and gas producers and importers for the sale of liquid hydrocarbons and natural gas liquids. This surcharge for each sale will be equal to US$1 for each barrel of the mentioned products.

K. Other tax issues

General anti-avoidance rule (GAAR)

Starting from 19 July 2012, a GAAR has been introduced into the Peruvian Tax Code to assist the tax administration in responding to situations of tax avoidance and simulated transactions.

When facing tax avoidance situations, the tax administration will be able to coercively request the corresponding tax debt, reduce tax credits or tax losses, or eliminate a tax benefit (including the restitution of taxes unduly refunded). To exercise the powers under the GAAR, the tax administration must determine two things, namely that:

- The taxpayer has performed artificial or improper acts to achieve a specific tax result — whether individually or jointly with others.
- The use of such artificial or improper acts has created legal or economic results different from regular tax savings obtained from routine or proper acts.

Despite the aforementioned, the Government has suspended the application of the GAAR, with the exception of the provisions of the first and last paragraphs relating to acts, facts and situations prior to 19 July 2012.

Profit sharing

Employers are obliged to distribute a share of their profits among their employees. The rate depends on the company's activity, as follows:

- Fishing — 10%
- Telecom — 10%
- Industry — 10%
- Mining — 8%, including exploitation of coal mines; production of petroleum and natural gas; and extraction of iron, uranium, thorium, iron-free minerals, construction stone, clay, talc, sand and gravel, feldspar and salt
- Commerce and restaurants — 8%
- Other — 5%, including farming, stockbreeding and forestry; production and distribution of electricity; production of gas; transportation services and services related to air transportation (such as travel agencies, storage and deposit); financial services of insurance and real estate; legal, audit and accounting activities; business consulting, consulting related to informatics and data processing; and advertising, health and medical services, and education

Many oil and gas companies calculate their employee benefit rates using the 5% rate, and the validity of such action has been a matter of discussion at the judicial level.

Profit sharing is calculated on pretax income, and the amount is deductible as an expense for determining income tax. An illustrative example of the combined-effect calculation using a 5% profit-sharing rate follows:

- Net income: 100
- Profit sharing: 5
- Net income for CIT purposes: 95
- Income tax (31.5% of 95): 33.2
- Combined effect: 33.2 + 5 = 38.2 (38.2% of net income)

It must be noted that the 31.5% rate includes the 29.5% CIT rate plus the 2% premium applicable to oil and gas license and service contracts.

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ☐ **Production sharing contracts**
- ■ **Service contract**

A. At a glance

Fiscal regime: corporate tax and production sharing

- Production sharing:
  - The service contractor receives its share of petroleum as a service fee of up to 40% of the net proceeds from petroleum operations, and the government share under a service contract is not to be less than 60% of the net proceeds.
- Bonuses:
  - Bonuses are payable by the contractor to the Government upon signing, discovery or production, but only if stipulated in the service contract.
- Corporate income tax rate:
  - The service contractor is subject to the corporate income tax (CIT) of 30% based on net income, as provided under the 1997 Tax Code for the country, as amended by Section 28(A)(1) of the Republic Act No. 9337.
- Capital allowances — accelerated depreciation; E: immediate write-off for exploration costs
- Investment incentives:
  - The service contractor is entitled to exemption from all taxes, except income tax.

B. Fiscal regime

The Philippine Government, through its Department of Energy, as the owner of natural resources (including oil and gas reserves) in the Philippines, may directly explore for and produce indigenous petroleum. It may also enter into a service agreement with a service contractor for the exploration and development of oilfields under Presidential Decree (PD) No. 87, as amended (otherwise known as the Oil Exploration and Development Act of 1972). The agreement is embodied in a service contract with the Philippine Government.

The service contractor receives its share of petroleum as a service fee equivalent to no more than 40% of the net proceeds from the petroleum operations (under the Department of Energy Model Service Contract pursuant to PD No. 87, as amended). The service contractor's income is subject to CIT at a rate of 30% based on net income (proceeds), as provided under the 1997 Tax Code, as amended by Section 28(A)(1) of the Republic Act No. 9337.

Petroleum operations

"Petroleum operations" are defined as searching for and obtaining petroleum within the Philippines through drilling and pressure, or suction, or similar activities and other operations incidental to these activities. The term includes the transportation, storage, handling and sale, whether for export or for domestic consumption, of petroleum, but it does not include any transportation of petroleum outside the Philippines or any processing or refining at a refinery, or any transactions in the products so refined (Section 3(d) of PD No. 87, as amended).

Net proceeds

"Net proceeds" are defined as the gross income less the recoverable operating expenses and the Filipino Participation Incentive Allowance (FPIA).

Gross proceeds

"Gross proceeds" are defined as the proceeds from the sale, exchange or disposition of all petroleum, crude oil, natural gas or casing head petroleum spirit produced under the service contract and sold or exchanged during the calendar year, and all such other income that is incidental to or arising from any one or more of the petroleum operations under the contract.

Deductions

At the outset, operating expenses incurred by a service contractor are reimbursed by the Philippine Government. The reimbursement may not exceed 70% of the gross proceeds from production in any year. If the operating expenses exceed 70% of the gross proceeds from production in any year, unrecovered expenses may be recovered from the operations of the succeeding years (PD No. 87, as amended by PD No. 1857). There is no time limitation for recovery on the carryforward of unrecovered expenses to succeeding years.

Recoverable expenses

In arriving at the net proceeds, the following are allowable deductions (reimbursable expenses) for the contractor.

General expenses

All ordinary and necessary expenses paid or incurred by the contractor during the taxable year in carrying on the petroleum operations under a service contract (Rev. Reg. 1–81).

Interest

In general, interest expense paid or incurred within the taxable year is deductible (to the extent of two-thirds of the amount), except for interest on any loan or indebtedness incurred to finance exploration expenditures, for which no interest deductions will be allowed (PD No. 1857, amending PD No. 87). The prohibition on the deductibility of interest with respect to indebtedness incurred to finance petroleum exploration is explained in Section 34(B)(2)(c) of the 1997 Tax Code.

Depreciation

The service contractor is granted the option of using the straight-line or double-declining-balance method of depreciation on all tangible assets initially placed in service in a taxable year and directly related to the production of petroleum. The method elected for a particular taxable year must be used for assets placed in service during that year.

The general rule is that the useful life of assets used in, or related to, production of petroleum is 10 years, or such shorter life as allowed by the Commissioner of Internal Revenue. The useful life is five years under the straight-line depreciation method for property not used directly in the production of petroleum (Section 34(F)(4), 1997 Tax Code; Section 6(e), Rev. Reg. 1–81).

However, pursuant to PD No. 1857, the depreciation of all tangible exploration costs, such as capital expenditures and other recoverable capital assets, are to be depreciated for a period of five years using the straight-line or double-declining-balance method of depreciation, at the option of the contractor.

Intangible development and drilling expenses

If intangible development and drilling expenses for producing wells are incurred after the commencement of commercial production, they can be allowed as a deduction in the taxable year they are paid or incurred. The contractor has the option to capitalize and amortize these costs on the basis of the recoverable units of reserves in the particular oilfield involved plus the units produced and sold during the same year from that oilfield, or over a shorter amortization schedule as allowed by the Commissioner of Internal Revenue (Section 6(h), Rev. Reg. 1-81).

If the contractor chooses to capitalize and amortize the drilling expense of producing wells (including any well that is subsequently determined to have failed to find petroleum in commercial quantities), all unamortized costs regarding the well may be deducted in full in the year of the determination (Section 6(i), Rev. Reg. 1-81).

Intangible exploration costs

Intangible exploration costs can be reimbursed in full under the provisions of PD No. 1857.

Abandonment losses

If a contract area is abandoned, any expenditure incurred on or after 1 January 1979 may be deducted from the income derived from any other activity as an abandonment loss. The unamortized costs of a previously producing well and undepreciated costs of equipment are allowed as a deduction in the year that the well, equipment or facilities are abandoned by the contractor (Rev. Reg. 1-81).

Filipino participation incentive allowance

A Filipino Participation Incentive Allowance (FPIA) is allowed as a deduction under general principles for computing taxable net income (Section 21(1), PD No. 87). An FPIA is the subsidy granted by the Government to a service contractor if Philippine citizens or corporations have a minimum participating interest of 15% in the contract area. An incentive not exceeding 7.5% of the gross proceeds may be computed by deducting the FPIA from the market price of crude oil produced under the contract and sold during the year (Section 28, PD No. 87).

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

A service contractor is granted the option of using the straight-line or double-declining balance method of depreciation for all tangible assets initially placed in service in a taxable year that are directly related to the production of petroleum. The method elected for a particular taxable year must be used for all assets placed in service during the year.

The general rule is that the useful life of assets used in, or related to, production of petroleum is 10 years, or such shorter life as allowed by the Commissioner of Internal Revenue. The useful life of property not used directly in the production of petroleum is five years under the straight-line depreciation method (Section 34(F)(4), 1997 Tax Code; Section 6(e), Rev. Reg. 1-81).

However, under PD No. 1857, all tangible exploration costs, such as capital expenditures and other recoverable capital assets, are to be depreciated for a period of five years, using the straight-line or double-declining balance method of depreciation, at the option of the contractor.

D. Incentives

Under PD No. 87, known as the Oil Exploration and Development Act of 1972, the following fiscal incentives are provided for petroleum service contractors:

- A service fee of up to 40% of net production (note that, Section 18(b) of PD No. 87 provides that the annual share of the Government, including all taxes paid by or on behalf of the contractor, shall not be less than 60% of net production)
- Cost reimbursement of up to 70% of gross production with carryforward of unrecovered costs
- FPIA grants of up to 7.5% of the gross proceeds for service contracts with a minimum Philippine company or citizen participation of 15%
- Exemption from all taxes except income tax (although for service contracts executed after 1991, a local business tax ranging from 0.5% to 3% of gross receipts may be imposed)
- Exemption from all taxes and duties for the importation of materials and equipment for petroleum operations
- Easy repatriation of investments and profit
- Free-market determination of crude oil prices (i.e., prices realized in a transaction between independent persons dealing at arm's length)
- A special income tax rate of the 8% of gross Philippine income for subcontractors (although for subcontracts executed after 1991, a local business tax ranging from 0.5% to 3% of gross receipts may be imposed)

E. Withholding taxes

Dividends

Dividends received by a domestic or resident foreign corporation from a domestic corporation (i.e., a locally incorporated petroleum service contractor) are not subject to income tax.

Dividends received by a nonresident corporation from a locally incorporated petroleum service contractor are subject to withholding tax (WHT) at 30%. The tax is reduced to 15% if the recipient foreign corporation is a resident of a country that does not impose any tax on dividends received from foreign sources or allows a credit against the tax due from the nonresident foreign corporation taxes deemed to have been paid in the Philippines, equivalent to 15%.

However, if the recipient is a resident of a country with which the Philippines has a tax treaty, the more favorable tax treaty rate applies.

Interest

In general, the 1997 Tax Code imposes a final WHT of 20% on interest on foreign loans received by a nonresident foreign corporation (Section 29(B)(5)(a)). However, if the lender is a resident of a country with which the Philippines has a tax treaty, the more favorable tax treaty rate applies.

Royalties

Royalties (e.g., payments for the supply in the Philippines of scientific, technical, industrial or commercial knowledge or information) paid to a domestic or resident foreign corporation are subject to a 20% final tax. Royalties paid to a nonresident foreign corporation are subject to 30% income tax, or the treaty rate if the recipient is a resident of a country with which the Philippines has a tax treaty, in which case the tax is withheld at source plus a 12% final withholding value-added tax (VAT).

Technical services

Fees or income derived by nonresident foreign corporations for performing technical services (not related to petroleum operations) within the Philippines are generally subject to a 30% final WHT based on the gross amount.

If the provider of technical services is a domestic corporation or a resident foreign corporation, it is subject to regular CIT or the minimum corporate income tax (MCIT), whichever is higher. Beginning with the fourth taxable year immediately following the year when a corporation commences its business operations, MCIT is imposed if this tax exceeds the tax computed under the normal tax rules. As provided for by Sections 27(E) and 28(A)(2) of the 1997 Tax Code, as amended, in computing the gross income subject to the 2% MCIT for sellers of services, "gross income" means gross receipts less sales returns, allowances, discounts and the cost of services. "Cost of services" means all direct costs and expenses necessarily incurred to provide the services required by customers and clients. It includes salaries and employee benefits of personnel, consultants and specialists directly rendering the service, and the cost of facilities directly utilized in providing the service, such as depreciation, rental equipment and costs of supplies. Any excess of the MCIT above the normal tax may be carried forward and credited against the normal tax for the three immediately succeeding taxable years.

For as long as the services are performed in the Philippines, a 12% VAT on gross receipts applies.

In the case of technical services related to petroleum operations, Section 1 of PD No. 1354 applies. It provides that every subcontractor, whether domestic or foreign, that enters into a contract with a service contractor engaged in petroleum operations in the Philippines is liable for a final income tax equivalent to 8% of its gross income derived from the contract. The 8% final tax is in lieu of all national and local taxes. A petroleum subcontractor provides the means necessary for the service contractor to pursue its petroleum operations (Zapata Marine Service Ltd., S.A. v. CIR, CTA Case No. 3384, 30 March 1987).

Note, however, that for subcontracts executed after 1991, a local business tax ranging from 0.5% to 3% of gross receipts may be imposed.

Branch remittance tax

A branch profits remittance tax (BPRT) of 15%, or the treaty rate if the branch is a resident of a country with which the Philippines has a tax treaty, applies to any profit remitted by a branch to its head office. The tax is based on the total profit earmarked for remittance without any deduction for the tax component (Section 28(A)(5), 1997 Tax Code).

F. Financing considerations

Under PD No. 1857, two-thirds of the interest expense paid or incurred within the tax year is deductible and reimbursable (except for interest on loans incurred to finance exploration expenditures).

G. Transactions

In general, gains derived from the sale of assets, such as machinery and equipment used in business, are subject to 30% income tax and 12% VAT.

Gains from the sale of shares of stock not listed or traded in the local stock exchange by resident individuals and domestic corporations are subject to 15% capital gains tax (CGT) on the net gains beginning 1 January 2018 under Republic Act (RA) No. 10963. However, gains from the sale of shares of stock not listed or traded in the local stock exchange by resident and nonresident foreign corporations are subject to 5% CGT on net gains not exceeding PHP100,000, and to 10% tax on the excess.

A documentary stamp tax (DST) also applies to the sale or transfer of shares at the rate of PHP1.50 per PHP200 par value beginning 1 January 2018 under RA No. 10963.

H. Other

A service contractor must register with the Department of Energy all existing service contracts and all contracts to be entered into relating to oil operations between the service contractor and a subcontractor engaged in petroleum operations (Section 6, Rev. Regs. 15–78).

Administrative contracts do not need to be registered, but the contractor must provide a copy to the Department of Energy (Section 6, Rev. Regs. 15–78).

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies in Poland to the oil and gas industry consists of a combination of corporate income tax (CIT), capital gains tax (CGT), value-added tax (VAT), excise duty, real estate tax (RET), special hydrocarbons tax (SHT) and tax on the mining of certain minerals as follows:

- CIT rate — 19%
- CGT rate — 19%
- Branch tax rate — 19%
- VAT rate — 23%
- RET rate — 2% (on value of constructions), max. 23.1PLN/m² (on the surface of buildings), max. 0.91 PLN/m² (on the surface on land)
- SHT — 0%–25%
- Tax on the mining of certain minerals (royalty) — 1.5%–6%

B. Fiscal regime

Current fiscal regime

The fiscal regime for upstream business is currently under-regulated in Polish tax law. The main current tax issues are: CIT/VAT treatment of joint operations (timing of revenue recognition, treatment of buy-in payments, farm-in/farmout) and CIT treatment of exploration and evaluation expenses and asset recognition (e.g., dry wells). These issues are therefore presented based on the general CIT and VAT regulations and the practice of the tax authorities (expressed in the official tax rulings issued by the Ministry of Finance).

New fiscal regime for hydrocarbon sector from 2016

The new law concerning the regulatory and tax framework for the exploration and extraction of hydrocarbons came into force in 2016, (the new ad valorem royalties, however, will not be payable until 2020, as per the new law). The law introduces a hybrid model of taxation consisting of a special hydrocarbons tax chargeable on a cash basis (cash flow tax) and ad valorem royalty (i.e., the tax on the extraction of selected minerals).

Special hydrocarbons tax

SHT is a profit-based tax imposed on an excess of sale revenues over eligible expenses related to the hydrocarbons extraction business, both onshore and offshore, with rates linked to investor returns.

As a rule, revenues include monies received, monetary values and the value of receivables settled in-kind from supplies of the extracted hydrocarbons. Eligible expenses are all expenses incurred to generate revenue or retain/secure a source of revenue, including expenses to explore, appraise, extract, store or supply hydrocarbons and to wind up the hydrocarbon extraction business.

The SHT should be charged based on a cash basis; however, some exemptions are provided to tax revenues on an accrual basis, e.g., if the sale proceeds are not paid within three months from the supply of hydrocarbons.

If the ratio of revenues cumulated from the beginning of the entity's extraction activity over cumulative eligible expenses would be higher than 1.5 and lower than 2.0, a progressive rate between 12.5% and 24.9% would apply to profit generated in a given year; a 25% rate would apply if the ratio were to be higher than 2.0. A ratio below 1.5 does not trigger SHT (the applicable tax rate is 0%).

Since SHT should be charged only on upstream activities, ring-fencing will be applicable in the case of an entity undertaking upstream and downstream activities simultaneously. However, no ring-fencing rules are envisaged where the entity holds several upstream projects.

The new tax regime came into force in 2016. However, tax holidays from both new levies (SHT and royalty tax) apply in a transition period lasting until 2020.

Tax on the mining of certain minerals (royalty tax)

Royalty tax is chargeable on the extraction of natural gas and oil. The taxable base is the value of the extracted natural gas and oil. The tax base is calculated as the volume of the extracted natural gas and oil multiplied by the average price of natural gas, determined by reference to the daily quotations at Towarowa Giełda Energii S.A., or the average price of oil per metric ton established by reference to the prices of oil set by the Organization of the Petroleum Exporting Countries (OPEC). The Minister of Finance shall announce the prices by the 15th day of each month.

The rate of royalty tax (determined by the technical parameters of a deposit, i.e., average permeability or average effective porosity) is:

- For natural gas — 1.5% (for gas from seabed and deposits where the average permeability is less than 0.1 millidarcy and the average effective porosity does not exceed 10%), 3% (for deposits other than specified)
- For oil — 3% (for oil from seabed and deposits where the average permeability is less than 0.1 millidarcy and the average effective porosity does not exceed 10%), 6% (for deposits other than specified)

The tax point is the day when natural gas or oil is released into a pipeline or directly to a distribution network, or where it is loaded into a vehicle/vessel.

Like SHT, the royalty tax took effect on 1 January 2016; liability to pay the tax does not apply for hydrocarbons extracted prior to 1 January 2020.

Relation between CIT, SHT and royalty tax

Relations between CIT, SHT and royalty tax can be characterized as follows:

- Neither SHT nor royalty tax will be a deductible cost for CIT purposes.
- Paid CIT and royalty tax related to oil and gas exploration activities may be deductible for SHT purposes (being eligible costs).
- Nineteen percent of cumulative CIT losses from extraction activities that have not been carried forward in whole (because of the expiry of the five-year period) may be deductible from the royalty tax.

C. Corporate income tax

Corporations operating in Poland are subject to CIT on their Polish-sourced income at a rate of 19%. This rate applies to any type of income, including that from oil and gas activities.

CIT basis

Taxable income in a given year is the difference between aggregated taxable revenues and aggregated tax-deductible costs. Accumulated expenditures on an unsuccessful investment (usually recognized in the books as an asset under construction) may also constitute the tax-deductible cost, provided that the investment is no longer continued (i.e., liquidated or sold). A reduced 15% CIT rate may be applicable to so-called small taxpayers, i.e., as a general rule taxpayers starting business operations or taxpayers whose revenues from sales in the previous year did not exceed €1.2m.

Since 1 January 2018, CIT regulations have been modified by splitting the revenues into two separate sources:

- Capital gains (e.g., dividends, redemption of shares, disposal of receivables, merger, demerger, contribution in kind, participation loans, revenues from certain intangible assets)
- Other sources of revenues

The above implies the obligation to determine two separate CIT results. There is no possibility to offset profits from one source with losses from the other. If it is not possible to assign specific costs to a specific source of revenue, these costs are apportioned (in proportion to the revenues from a given source of income in the overall revenues generated in the tax year).

Tax losses

Aggregated annual tax-deductible costs exceeding annual taxable revenues generated within the particulate source of income constitute a tax loss. Losses may be carried forward to the following five tax years to offset with tax revenue from a given source that is derived in those years. Up to 50% of the original loss may offset income in any of the five tax years. Losses may not be carried back. As stated in Section B earlier, 19% of expired cumulative CIT losses from extraction activities may be deductible from the royalty tax.

Ring fencing

Poland does not apply ring fencing in determining an entity's corporate tax liability in relation to its oil and gas activities. Profit from one project can be offset against losses from another project held by the same Polish legal entity and, similarly, profits and losses from upstream activities can be offset against downstream activities undertaken by the same Polish entity. A new oil and gas taxation approach in this respect was, however, introduced by regulations on special hydrocarbons tax (see earlier in Section B).

Unconventional oil and gas

For income tax purposes, no special terms apply to unconventional oil or unconventional gas — but see earlier in Section B in which royalties on unconventional oil and gas introduced into the new legislation are described.

D. Capital allowances

Depreciation

For tax purposes, depreciation calculated in accordance with the statutory rates (or below) is deductible. Depreciation is usually calculated using the straight-line method, but in certain circumstances the reducing-balance method may be allowed. The following table shows some of the applicable annual straight-line rates.

Type of depreciating asset	Rate (%)
Buildings	1.5% to 10%
Wells	4.5%
Machinery and equipment	7% to 25%
Computers	30%

Accelerated depreciation is available for machinery and equipment, but not for wells.

Additionally, starting from 2016, the individually set tax amortization rate may be applicable to:

- Appraisal and production wells
- Drilling and production platforms

The individual rate cannot, however, be higher than 20%.

E. Incentives

Starting from 2016, new R&D tax relief applies to the R&D-related costs, such as gross remuneration with surcharges paid to employees recruited to conduct R&D works, costs of supplies and raw materials directly connected with R&D activity, expertise, opinions, advisory and other related services, as well as cost related to acquisition of scientific research result conducted or provided by academic units and the cost of using research and development equipment utilized exclusively for R&D activities.

As of 2018, depending on the type of costs incurred and the status of the taxpayer, the tax base may be reduced by:

- 100% of labor costs with related surcharges
- 100% of other costs incurred if taxpayer is a micro-entrepreneur, small or medium entrepreneur within the meaning of the Freedom of Business Activity Act

F. Withholding taxes

The rate for withholding tax (WHT) on dividends is 19%. The rate for WHT on interest and royalties is 20%. However, the rates may be reduced for countries with which Poland has negotiated double tax treaties, or in line with European Union (EU) directives implemented to the Polish law.

G. Financing considerations

Thin capitalization

From 1 January 2015, new rules for thin capitalization in CIT came into force in Poland. Thin capitalization restrictions apply if an entity's debt-to-equity (equity is understood as share capital and other reserves) ratio exceeds 1:1, and loans are drawn from directly or indirectly affiliated companies with a minimum shareholding level of 25%.

Taxpayers may opt — upon notification — for an alternative method for thin capitalization purposes. Under this regulation, the limitation of the tax deductibility on loans received is extended also to unrelated entities (such as banks and other financial institutions), in which interest expense deductible for CIT purposes cannot exceed the tax value of assets (excluding intangible assets) multiplied by the reference rate of the National Bank of Poland increased by the index of 1.25%; at the same time, only interest not exceeding 50% of operating profit (calculated according to the accounting rules) may be deducted in a given tax year.

Starting from 1 January 2018, a new thin capitalization regime replaced the previous regulations. Nondeductible is a surplus of financing costs exceeding 30% of earnings before interest, taxes, depreciation and amortization (EBITDA). Restrictions apply to all types of debt financing, also provided by unrelated parties, including banks. There is a possibility to roll nondeductible costs over the next five tax years according to the rules and within the limits.

Safe harbor of PLN3m (ca. €0.7m) exists.

Based on interim rules, the previous regime may be applied only to debt financing received before 1 January 2018, but only until the end of 2018.

Transfer tax

As a rule, a 2% transfer tax is chargeable on such a debt, unless specific exemptions apply (shareholder's debt is not subject to transfer tax).

H. Transactions

Asset disposals

It is not possible to sell licenses or oil and gas extraction permits. It is possible to sell an enterprise as a property complex, together with all its assets and liabilities (but not licenses) as a whole. Such a transaction is outside the scope of VAT.

Farm-in and farmout

Polish tax law does not recognize farm-ins and farmouts, as the license issued by the State cannot be traded; therefore farm-ins and farmouts are exercised through joint ventures, joint operations or share deals.

Joint operations

The Polish CIT Act outlines a general rule on the allocation of profits (i.e., revenues and costs) applicable, among others, to a joint undertaking. Assuming that cooperation is considered a joint undertaking within the meaning of the CIT Act, the CIT settlements between parties should be established in line with the abovementioned provision and the general CIT rules.

The revenue generated within a joint undertaking should be allocated to the parties according to their shares in the undertaking, as declared in the agreement between the parties. This rule should be applied accordingly to tax-deductible costs, costs not deductible for tax, tax exemptions and tax reliefs. Here, the rule affects the recognition of revenues (and costs), in particular during the exploration and production (E&P) phase.

Currently, the tax authorities tend to accept that upstream cooperation should follow the CIT rules applicable to joint ventures. What is still unclear is the point of revenue recognition for the operators when non-operators provide extra funding for the operations in excess of their participation interest.

With regard to SHT and royalty tax, the law directly stipulates that in the case of joint operations carried out based on the cooperation agreement as defined in the Geological and Mining Act, parties of this agreement are taxed proportionally to their participating interests.

I. Indirect taxes

VAT

VAT is imposed on goods sold and services rendered in Poland, as well as on exports, imports and acquisitions and supplies of goods within the EU. Poland has adopted most of the EU VAT rules.

The standard rate of VAT is 23%. Lower rates may apply to specified goods and services. The local supply of certain goods may be subject to a reverse charge mechanism. A 0% rate may apply to exports and supplies of goods within the EU. Certain goods and services are exempt altogether.

A split payment mechanism is to be introduced starting from July 2018 as a voluntary option.

Excise duties

Excise duty is applied on energy products (including petroleum products), alcoholic beverages, tobacco products, electricity and passenger cars. The duty rates applying for main petroleum products are shown in the table below.

Item	Type of oil and gas product	Rate
1	Engine gasolines	PLN1,540 per 1,000 liters
2	Diesel oils	PLN1,171 per 1,000 liters
3	Oils intended for heating purposes	PLN64 or PLN232 per 1,000 liters
4	Liquefied gases used for propulsion of combustion engines (liquefied natural gas (LNG) and liquefied petroleum gas (LPG))	PLN670 per 1,000 liters
5	Other engine fuels	PLN1,797 per 1,000 liters
6	Other heating fuels	PLN64 or PLN232 per 1,000 liters
7	Gases used for propulsion of combustion engines in gaseous state	PLN10.54 per gigajoule
8	Gases for heating purposes	PLN1.28 per gigajoule

Fuel charge

Placement on the domestic market of motor fuels and gas used to power internal combustion engines is subject to a fee, termed "fuel charge," paid by the producers and importers of motor fuels.

Motor fuels and gas subject to this fuel charge include:

- Motor gasoline with combined nomenclature (CN) codes: CN 2710 11 45 or CN 2710 11 49 and the products resulting from the mixing of these fuels with bio-components that meet the quality requirements specified in separate regulations (fuel charge in 2018 equal to PLN131.40 per 1,000 liters)
- Gas oils falling within CN code 2710 19 41 and the products resulting from the mixing of these oils with bio-components that meet the quality requirements specified in separate regulations (fuel charge in 2018 equal to PLN293.05 per 1,000 liters)
- Bio-components that are self-contained fuel, meeting the quality requirements specified in separate provisions for combustion engines, regardless of the CN code (fuel charge in 2018 equal to PLN293.05 per 1,000 liters)
- Natural gas (wet) and other gaseous hydrocarbons, aliphatic hydrocarbons and natural gas and liquefied gaseous state for combustion engines, codes CN 2711 and CN 2901 (fuel charge in 2018 equal to PLN1167.27 per 1,000 liters)
- Products other than those mentioned above, intended for use, offered for sale, or used for combustion engines, regardless of the CN code (fuel charge in 2018 equal to PLN167.27 per 1,000 liters)

Transfer tax

As a general rule, the transfer tax applies to transactions made by entities that are not VAT- registered (or those that are specifically VAT-exempt) and are not involved in professional commerce. Nevertheless, the transfer tax is also imposed on other businesses in specific situations; in particular, an incorporation of company and an increase of share capital is taxed at a rate of 0.5% on the created or increased share capital value; any additional payment contributing to a company's supplementary capital is taxed at a 0.5% rate; transfers of shares are taxed at a 1% rate; and sales of real estate are taxed at a 2% rate.

Stamp duties

Stamp duty is levied by notaries and is generally capped at insignificant amounts.

Registration fees

There are no significant registration fees.

Other significant taxes

RET applies to land and buildings (rates per square meter) and all constructions (the rate is 2% p.a. of the initial value used for tax depreciation purposes). Many doubts surround the definition of "construction" in this context, so the scope of RET taxation in the oil and gas industry is not entirely clear. Indeed, it has been the subject of disputes between taxpayers and the tax authorities. Close monitoring of the legislation and practice in this respect is required.

J. Other

Foreign-exchange controls

There are no foreign-exchange restrictions on inward or outward investments, apart from a requirement of disclosure imposed by a foreign-exchange law.

Gas to liquids

There is no special regime for gas-to-liquids conversion.

Concessions and mining usufruct agreements

The searching, exploration and production of natural resources are licensed activities. Concessions must be obtained separately for each activity, or joint concessions may be obtained. As the main rule under the Geological and Mining Act, hydrocarbons are state-owned, upstream activities require concluding a mining usufruct agreement (MUA) with the Polish Government and are subject to an annual mining usufruct fee (in the form of an ad valorem fee based on the value of deposits) and annual extraction royalties (based on the volume of extracted minerals).

Rates for the extraction royalty effective from 2017 are as follows:

- PLN24.73 for 1,000 m^3 of extracted high methane gas (total extracted gas > 2,500k m^3)
- PLN6.43 for 1,000 m^3 of extracted high methane gas (total extracted gas ≤ 2,500k m^3)
- PLN20.61 for 1,000 m^3 of extracted low methane gas (total extracted gas > 2,500k m^3)
- PLN5.34 for 1,000 m^3 of extracted low methane gas (total extracted gas ≤ 2,500k m^3)
- PLN51.52 for 1 ton of extracted oil (total extracted oil > 1000t)
- PLN37.96 for 1 ton of extracted oil (total extracted oil ≤ 1000t)

Transfer pricing

Transactions with related parties need to be concluded at arm's-length prices. The Polish transfer pricing regulations do not refer directly to the Organisation for Economic Co-operation and Development (OECD) Guidelines directly; however, the regulations are based on and aligned with the OECD Guidelines. Moreover, tax authorities tend to refer to the OECD Guidelines when applying transfer pricing principles — e.g., during advance pricing agreement (APA) negotiations.

Moreover, taxpayers carrying out transactions in excess of certain amounts with related parties and PEs of foreign companies operating in Poland are required to prepare transfer pricing documentation.

As of 2017, new transfer pricing documentation regulations apply, providing substantial changes to transfer pricing documentation requirements and significantly broadening the information obligation. The scope of the documentation and the relevant thresholds for the transactions to be covered depend on the size of the taxpayer's business.

The proper transfer pricing documentation should be drawn up within the deadline to submit the annual tax return — what needs to be confirmed by means of an official statement filed to the tax office within the deadline to submit an annual CIT return. In addition, a separate CIT-transfer pricing return should be attached to the CIT return for taxpayers whose annual revenues/costs exceed €10 million.

Since 1 January 2018, limitation of tax deductibility of certain costs applies with respect to payments made to related parties, which are not covered by APA (if the volume of these exceeds of 5% of EBITDA). This covers costs of advisory services, market research, advertising, management and control, data processing, insurance, guarantees and sureties and similar services. Royalties for the use of certain intangible assets, including trademarks, are also covered. Safe harbor of PLN3m (ca. €0.7m) applies.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Fiscal regime — Traditionally, the State of Qatar has favored production sharing contracts (PSCs) as the mechanism for agreements between the Government and oil and gas companies. However, more recent agreements have been drafted as development and fiscal agreements (DFAs).

The principal elements of the fiscal regime for oil and gas companies in Qatar are as follows:

- Corporate income tax (CIT) rate — 35%. Note that the rate of 35% is applicable to companies carrying out petroleum operations as defined under Law No. 3 of 2007; certain PSCs may define a higher CIT rate. Please see Section B for full details.
- Royalty rate — Payable on the total sales under a DFA with the rate(s) set by each DFA.
- Bonuses — Payable under a PSC at signature and based upon production targets. DFAs do not include bonuses.

B. Fiscal regime

Corporate tax

Companies carrying on petroleum operations in Qatar are subject to CIT in accordance with the specific terms of agreements negotiated with the state, which is represented by the national oil company (NOC) of Qatar. "Petroleum operations" are defined by Law No. 3 of 2007 as the exploration for petroleum, improving oil fields, drilling, well repair and completion; the production, processing and refining of petroleum; and the storage, transportation, loading and shipping of crude oil and natural gas.

The CIT rate applicable to companies carrying out petroleum activities is generally 35% (or rates ranging from 35% to 55% for agreements that precede the enactment of Law No. 21 of 2009 (the Income Tax Law)).

Fiscal agreements

Taxable income is determined in accordance with the provisions of the underlying PSC or DFA.

PSC arrangements generally involve the following elements:

- All risks are borne by the company. Expenditures for exploration, development, production and related activities are fully funded by the company, and the Government does not fund any activity.
- The company is responsible for all costs but entitled to recovery out of annual production.
- Exploration and development costs are generally capitalized and are depreciated on a straight-line basis.
- Production is shared between the company and the NOC (there being no concept of the sharing of profits).
- The PSC will provide for signature and production bonuses, which are not cost-recoverable.
- "Pay on behalf" arrangements are no longer offered by the NOC.
- The Government is usually not entitled to a royalty.

It is worth noting that as Qatar's oil and gas market matures, a shift is being observed from traditional PSCs to DFAs. This is most often the case when contractors come to renew their existing PSCs.

Joint venture arrangements typically see the NOC and an oil and gas company establish a joint venture company. That joint venture company in turn enters into a development agreement with the Government of the State of Qatar. The royalties payable under such joint venture agreements are directly linked to both the production levels and the market rate for the product produced.

Taxable income

Under a PSC, the taxable income for the purposes of determination of Qatar CIT is defined in the PSC and is generally defined as the total sums received from the sale or other disposition of the company's share of all net production (petroleum revenues) less allowable petroleum costs.

Under a DFA, the tax is paid at the level of the joint venture company and computed in line with the Income Tax Law and specific computational clauses in the DFA.

Petroleum revenues

"Petroleum revenues" here represent the sales value of the company's share of net production, as measured at the point of delivery but as adjusted for over- and under-lifting and any change in inventories at year-end.

Petroleum costs

All expenditure and costs defined by a PSC as exploration, appraisal and development costs are capitalized and carried forward for recovery against future production revenues or write-off at the time of relinquishment of interests.

Expenditure qualifying for cost recovery is subject to specific rules in the PSC. Generally, the PSC requires that costs and expenses of activities carried out by the company or its affiliates be included in recoverable costs only to the extent that such costs and expenses are directly or indirectly identifiable with such activities, and should be limited to the actual costs that are fair and reasonable.

Certain costs are specifically prohibited for cost recovery. Excluded costs include bonuses paid by the company to the Government in accordance with the PSC, the company's Qatari income taxes paid in accordance with the PSC, and foreign income taxes and other foreign taxes paid by the company. Additionally, the following costs are generally disallowed:

- Finance costs
- Marketing and sponsorship costs
- General head office/shareholder costs
- "Personal" costs
- "Unnecessary" costs (e.g., those arising from inefficiencies or waste, or what may be determined as "excessive" amounts)

The Government of Qatar generally no longer enters into "pay on behalf" arrangements. However, under some older PSCs, the oil company CIT may still be paid by the NOC on the company's behalf. The NOC settles the company's tax liability from its share of production, and the tax authorities issue a tax receipt and a tax certificate for the taxes that apply to the company.

Since under DFAs a joint venture company is established, such companies are not subject to cost recovery or profit restrictions.

Losses

Under the Income Tax Law, losses may be carried forward for three years but may not be carried back.

Loss carryforward restrictions do not apply to PSCs because the entire cost allowed is carried forward for future recovery.

Ring fencing

Historically, operations under each PSC have been ring-fenced. However, under more recent agreements, this has been relaxed so that revenues and costs from outside the agreement have been allowed to be introduced in computing net taxable profit.

For DFAs, such ring-fencing issues do not apply as activities are assessed to CIT at the level of the joint venture company.

Oil service companies

Oil and gas service companies are taxed at a 10% rate.

Resource rent tax

Qatar does not have a resource rent tax.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas activities in Qatar.

C. Capital allowances

Under PSCs, capital costs are generally capitalized and are depreciated on a straight-line basis from the quarter in which the capital cost is incurred. The most recent agreements have provided for a rate of 5% per quarter (20% per annum) with no limit on cost recovery.

Capital costs incurred under a DFA are capitalized and depreciated in line with the Income Tax Law. The Executive Regulations to the Income Tax Law provide specific depreciation rates for various asset classes. Depreciation is calculated by applying the following rates to the actual total cost on a straight-line basis:

- Buildings, pipelines and storage tanks — 5%
- Ships and vessels — 10%
- Aircraft — 20%
- Drilling tools — 15%

Depreciation is applied to other categories of assets on a pooled basis at the following rates:

- Computers — 33%
- Plant and equipment — 20%
- Office furniture and fittings — 15%

D. Investment incentives

All incentives under development and fiscal agreements are dependent on fiscal negotiations with the Government. The typical incentives offered under the Foreign Capital Investment Law include the following:

- A six-year tax holiday (although it is very unlikely any contractor operating in the upstream oil and gas sector under a PSC or DFA would be granted such an exemption)

- Customs duty exemptions until the start of commercial production
- Land lease of 50 years at subsidized rates
- No restriction on repatriation of capital and dividends
- Feedstock gas or gas reserves at subsidized rates
- Favorable treatment with respect to compliance with general commercial, tax and other regulatory requirements in Qatar.

E. Withholding taxes and double tax treaties

Payments made to foreign companies that are not tax resident or that do not have a permanent establishment in Qatar are subject to a final withholding tax (WHT).

WHT is applicable at the following rates:

- 5% — on the gross amount of royalties as well as technical services rendered partially or wholly in Qatar
- 7% — on the gross amount of interest, commissions, brokerage fees, director's fees and fees for any other payments in relation to services rendered partially or wholly in Qatar

Thus, if an entity in Qatar makes any of these payments to a foreign company, it must deduct either 5% or 7% WHT from such payments and remit this to the tax authorities, as appropriate.

WHT is not levied on dividends and certain categories of interest.

Relief may be available from WHT under a relevant double tax treaty. Qatar currently has around 60 double tax treaties in force.

F. Financing considerations

Thin capitalization

Interest paid to a head office or related party may not be deductible for tax purposes, and such interest is not subject to WHT.

The accounting and tax treatments of finance costs are generally determined in accordance with the specific agreements underlying the oil and gas project; however, finance costs are a non-recoverable cost under most PSCs.

G. Transactions

Farm-ins, farmouts and assignments

Farm-ins, farmouts and assignments are permissible; however, before any agreement is entered into, it is mandatory for the contractor to obtain written authorization from the NOC (under a PSC) or the joint-venture partner (under a DFA), which will generally also be the NOC.

Under the terms of the PSC or DFA, any assignment should be free of transfer or related taxes, charges or fees (other than those that are customary administrative costs).

Asset disposals

Under a PSC, if the assets that qualify for cost recovery are sold, the proceeds are offset against recoverable costs or remitted to the NOC (i.e., they are considered to be the assets of the NOC). A balancing charge or allowance does not apply.

Relinquishment

The taxation of a disposal or relinquishment of an interest in a PSC is governed by the specific provisions of the PSC; however, these disposals are generally not subject to taxation.

Government buy-in rights

Under the most recent PSCs, the Government of Qatar has retained the right to acquire up to 65% of the contractor's interest until 30 days after the development plan is submitted. Such buy-in can by law be made only at cost (plus London Interbank Offered Rate (LIBOR) interest on costs incurred).

H. Indirect taxes

Customs duty and legalization fees are the only indirect taxes currently imposed in Qatar.

Customs duty

Qatar is a member of the Gulf Cooperation Council (GCC) and follows the Unified Customs Law applicable throughout the GCC. The uniform customs duty of 5% applies on all imports. This means that any goods that come into a port of entry of a GCC Member State that have already been subjected to customs duty in any GCC Member State are not subject to customs duty again in the import state.

An exemption or reimbursement of customs duty will depend on the wording of the PSC or DFA. The import of drilling rigs is an exempt import under the GCC customs regulations.

Legalization fees

Commercial invoices must be legalized by the Commercial Department of the Qatari Embassy in the country of origin or by the customs authorities at the point of import into Qatar. Legalization fees are levied on the basis of invoice value and range from QAR100 on an invoice value of QAR5,000 to 0.4% of value for invoice amounts in excess of QAR1 million.

Free trade agreements

The Greater Arab Free Trade Agreement (GAFTA) has established preferential treatment for goods of GAFTA member origin. GAFTA maintains that goods originating from Arab countries (i.e., countries signed up to GAFTA, including Algeria, Egypt, Iraq, Jordan, Lebanon, Libya, Morocco, Palestine, Sudan, Syria, Tunisia, Yemen and the GCC Member States) may receive preferential treatment from a customs duty perspective when imported into another GAFTA member country. The provisions of GAFTA state that in order for a good to be treated as "Arab," it must meet the rules of origin, and the value added as a result of production in a GAFTA country must not be less than 40% of the finished good.

In addition, the GCC states have entered into a free trade agreement with Singapore that is effective for trade between Singapore and Qatar.

VAT

Currently, there is no VAT in Qatar. However, VAT is expected to be introduced with effect from 1 January 2019, in line with an initiative for all Gulf Cooperation Council (GCC) member countries to introduce the tax. The standard VAT rate is set at 5% and exports are zero rated. Special concessional arrangements are anticipated to apply to the supply of hydrocarbon products from upstream to downstream and marketing of exported products that, in effect, zero rate the supply of hydrocarbon products along the oil and gas supply chain. Refined hydrocarbon products supplied to domestic consumers will be subject to the 5% standard VAT rate.

Registration fees

Registration fees are payable to various ministries. However, these fees are not significant.

Municipality and other taxes

Qatar does not impose estate tax, gift tax or dividend tax. Municipalities impose a license fee that is aimed at compensating the municipal authorities for central governmental services, such as the cleaning and maintenance of urban and rural areas and waste collection.

I. Other

Payroll taxes and employee benefits

Employee earnings are not taxed. Self-employed foreign professionals are subject to income tax on their business profits. There are no social security insurance contribution requirements or other statutory employment-related deductions, nor are any similar contributions required from employers. The Qatar Labor Law requires all private-sector business entities to pay terminal benefits for all employees at the rate of three weeks' pay per annum.

The Government operates a contributory pension scheme for Qatari employees. The scheme applies to Qatari employees in both state and public sectors. Employees are required to contribute 5% of their salary to a pension fund operated by the General Corporation for Retirement and Pensions, and the employer's funding obligation is 10%. Qatari employees employed in the oil and gas sector will generally be covered by this pension fund requirement, and, accordingly, an operator under a PSC, or a joint venture company operating under a development and fiscal agreement, will be required to apply the pension fund requirements for its Qatari employees.

Local content and environmental concerns

More recent PSCs and DFAs concluded by the Government of Qatar notably contain provisions concerning environmental compliance and personnel matters (i.e., Qatarization) as well as imposing a preference for local goods and services in meeting purchase requirements.

Research and development

The Qatar Tax Law and PSCs/DFAs do not include a specific provision for research and development expenditure (R&D). However, Qatar has established the Qatar Science & Technology Park, which is a free trade zone, and this makes it easy and attractive to establish a 100%-owned technology-based company in Qatar.

A number of oil and gas companies have established entities in the Qatar Science & Technology Park to undertake research activities.

Marketing

Contractors must establish joint marketing committees with the Government of Qatar, which are responsible for deciding to which entities all crude oil and natural gas products can be sold.

In addition, certain regulated products must be sold exclusively to a state-owned marketing and distribution group on preset terms and conditions. These products are:

- Liquefied petroleum gas
- Sulfur
- Field condensates
- Refined products

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ■ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime applicable to the petroleum industry in the Republic of the Congo consists of the Congolese Tax Law (especially the Value-Added Tax (VAT) Law of 1997 and the VAT Decree of 2001), the Congolese Tax Code, the Congolese Hydrocarbon Code (law No. 28/2016, 12 October 2016, which applies since October 2016), the production sharing contract (PSC) and the service contract.

The rules for taxation rate, control, sanctions, prescription and tax litigation in relation to corporate tax and mineral fees (*redevance minière proportionnelle*) are contained within the general tax rules and the Hydrocarbon Code.

The principal elements of the applicable fiscal regime are as follows:

- Corporate income tax (CIT) — 30%, but under PSC not less than 35%
- Surface rent[1] — Exploration permit: XAF3,000/km², Exploitation permit: US$800/km²
- Bonuses — amount specified in the government decree that grants the exploration or exploitation permit
- Royalties — rate depends on the terms of the PSC
- Mineral fee — 15%[2] with a reduced rate of 12% for specific zones (e.g. deep waters drilling)
- Capital allowances — 100% for exploration cost and 20% for all other expenses
- Incentives — L, RD[3]

B. Fiscal regime

There are two kinds of oil companies in the Republic of the Congo:

- Upstream companies that specialize in the exploration and production of oil and gas
- Companies, known as subcontractors, providing petroleum services to upstream companies

1 *Annual surface rent is applicable to the PSC holder or participants.*

2 *Mineral fee is paid by oil equivalent except specific request from the State.*

3 *L: ability to carry forward losses.*

The fiscal regime that applies to upstream oil and gas companies differs from that which applies to the subcontractor companies. This guide will focus only on the fiscal regime applicable to upstream oil and gas companies.

Petroleum contracts

There are two different types of petroleum contracts entered into between oil companies and the Congolese Government: a PSC and a service contract. For each petroleum contract, participating interests must be owned at the minimum of 15% by a public company (i.e., company held in majority by the Congolese State). Also, each petroleum contract must be detained, except derogation from Minister of Hydrocarbons, at 15% by one or several local private companies (i.e., company owned in majority by Congolese citizen).

Production sharing contract

The first type of petroleum contract, and the most common, is the PSC, under which the Congolese Government gives a right to an oil company to exploit a specific area. If oil is discovered by the company, the exploitation is made in the name of the Congolese Government. If oil is not discovered, all the costs of exploration are lost for the company.

Pursuant to the Hydrocarbon Code, one part of the oil production is used to reimburse the costs of exploration and development incurred by the company. This is called "cost oil" and is limited to net production, called "cost stop." This part of production cannot exceed 50% of the net production of a specific exploitation permit. However, when the work is especially difficult (e.g., deep areas, high prices of technologies, etc.), this rate can be increased to 70%.

The part of the oil production accrued to the company and the Congolese Government as a payment is called "profit oil." It is calculated based on all production after deduction of the cost oil and the mineral fees (*redevance minière proportionnelle*). Cost oil and profit oil are determined for each contract.

The share of the Congolese Government cannot be less than 35% of the profit oil for a specific civil year. The PSC can state a higher rate. The part of the production attributed to each party depends on net production of the year, and the level of net production is re-examined each year to ensure compliance with the terms of the PSC.

The accounting system for a PSC is specified in the contract itself. The PSC has an appendix called "accounting procedure" that lists the methods, rules and procedure that must be followed.

Service contract

The second type of petroleum contract — which is still rare in practice — is a service contract, under which the contractor performs petroleum operations on a specific surface and gets paid by a flat or variable revenue in cash or in oil. It can be concluded, notably, at the end of a PSC term.

Corporate income tax

CIT is applied on net revenue at the rate of 30% after deduction of all costs and expenses, in compliance with the rules provided by the General Tax Code and Hydrocarbons Code. However, under the PSC, the CIT is paid through the Congolese State "profit oil" part. The rate cannot be less than 35% of the profit oil, but the PSC can mention a higher rate.

Bonuses

A bonus is paid to the Congolese Government in awards of the granting of an exploration or exploitation permit, modification of a Petroleum contract, or extension of an exploitation permit. The amount is different for each permit, and it is fixed by the government decree that grants the permit.

Annual surface rent

An annual surface rent (*redevance superficiaire*) is due from the company to the Congolese Government.

This annual surface rent must be paid each year on 20 January. It is based on the surface area stated on the permit and granted during the previous year. Pursuant to the decree dated 10 August 2000, the rates of this tax are as follows:

- Exploration permit: XAF3,000/km²
- Exploitation permit: US$800/km²

The rates above are applicable, but the new Hydrocarbon Code states that a specific decree should be published to provide the new basis, rate and modality of payment of this tax.

Royalty regime

The royalty regime is determined by the contract if the contract provides for payment of a royalty. There is no difference in the royalty rates between onshore and offshore production.

Mineral fee

A mineral fee is payable by the company to the Congolese Government at the rate of 15% with a reduced rate at 12% for specific zones. It is payable on the amount of the net oil production of the previous month and paid in crude oil, except when the State opts to be paid in cash.

The mineral fee is due for payment on the 20th of each month.

National funds for prevention of environmental risks

This contribution is equal to 0.05% of the net oil production. It is paid annually but the rules detailing the payment, collection and addressing other matters will be issued later (such rules are not available as of 1 January 2018).

C. Capital allowances

The tax depreciation rules for the petroleum sector are provided in the PSC according to the straight-line method of depreciation. The depreciation rates are fixed by the Hydrocarbon Code as follows:

- Cost incurred for exploration can be depreciated at the rate of 100%.
- All other capital expenditure is depreciated over a period of five years at the rate of 20% from the beginning of commercial production of each deposit.

The Congolese Hydrocarbon Code does not provide any accelerated depreciation for the assets of the petroleum company.

D. Incentives

There are incentives available in the establishment contract (*convention d'établissement*), which is related to the Investment Charter adopted by the Congolese Government to promote the role of investment in the country's economic development program. The incentives are specific for each contract. The relevant incentives are described below.

E. Withholding taxes

Dividends

Dividends distributed by an oil company to its shareholders are taxable.

Interest

The rate of interest for withholding tax (WHT) is 15%.

Technical services

The rate of WHT for technical services is 20%.

Special tax on capital gains

Capital gains realized by individuals or legal entities located abroad on the sale of all or part of their shareholdings in the capital of Congolese companies are taxed at 10% of the amount of the capital gain withheld. A capital gain is calculated as the difference between the price of sale and the amount of cost oil that still need to be recovered by a company selling the share.

Nonresident contractors

For subcontractors, the inclusive tax (*taxe forfaitaire*) rate is 7.7% where the subcontractor applies for a short-term business license (ATE), or 20% without an ATE. The withholding tax must be paid on the 20th of each month.

Foreign contractor wages and salaries

The wages and salaries received by foreign contractors from oil companies are subject to WHT at the rate of 20%, based on 80% of a lump-sum salary fixed in a wage scale. Except where international convention applies, foreigners are taxable if more than 14 days are spent in the Republic of the Congo.

Branch remittance tax

From the 2012 financial year, 70% of the profits earned by a branch of a foreign company are deemed to be distributed to the shareholders. The defined 70% portion is taxable under the tax on movable assets at a rate of 15%. The applicable rate is 1.5015%, and this taxation is also applicable to foreign companies doing business under an ATE.

F. Indirect taxes

VAT

The VAT rate in the Republic of the Congo is 18%.

The VAT treatment is the same for PSC and service contracts, as follows:

- VAT on sales: for export, there is an exemption of VAT for sales; for the local market, the VAT is due from the oil distributors.
- VAT on purchases: the important criterion here is the purpose for which the services and goods are to be used after purchase. There is:
  - Exemption of VAT for all goods or services used directly for research, exploration, development, exploitation, production, transport and storage of hydrocarbons (pursuant to Decree No. 2001/152 of October 2001 and Law No. 12–97 of May 1997)
  - Redeemable VAT for all goods and services indirectly connected with petroleum activities
  - Non-redeemable VAT for all goods and services acquired from entities that are not on the list of suppliers and subcontractors established by the company and communicated to the tax authorities

Where a company's VAT on acquisitions exceeds the VAT on its sales in a reporting period, the excess is refundable to the company.

Import duties

All the goods and materials listed in Act No. 2-92-UDEAC-556-CD-SE1 of April 1992 and used for oil exploration or exploitation work are exempted from customs duties.

Export duties

In general, all exported goods are taxed at a rate of 0% to 13% plus ancillary exit tax (*droit accessoire de sortie*) of 2% on the customs value. However, all materials, vessel and aircraft of an oil company is taxed at only 1% (*redevance informatique*) of the free-on-board value limited to XAF1,000,000.

Stamp duties

Pursuant to the Hydrocarbon Code, all stamp duties are due from the oil company.

All contracts signed between an oil company and another foreign company must mention the price of the contract and be registered at fixed fees of XAF1,000,000 and translated into French.

Registration fees

All registration fees (e.g., in relation to contracts or lease agreements that are not specifically exempted) are due by oil companies pursuant to the Hydrocarbon Code and the Congolese Tax Code.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies in Romania to companies operating in the petroleum industry generally consists of corporate income tax (CIT), petroleum royalty and other oil-related taxes for special funds. In summary, the main elements are as follows:

- CIT rate — 16%
- Royalties — 3.5% to 13.5% on oil extraction, 10% on certain transportation/transit of oil; and 3% on the underground storage of natural gas
- Bonuses — none
- Production sharing contracts (PSCs) — none
- Resource rent tax — The Romanian authorities charge a duty for issuing the drilling and excavation authorizations needed for research and prospecting of land for oil and gas wells. The duty amount is computed by multiplying the surface area affected by drilling and excavation activities by an amount that ranges between RON0 and RON15. Within 30 days after the research and prospecting phases are completed, taxpayers are liable to declare the area actually affected by drilling or excavation, and if it differs from the one initially declared (for which relevant authorizations were issued), the applicable duty is therefore revised to reflect the actual area affected.
- Special taxes (e.g., taxation of monopoly activities in the energy and natural gas industries, tax on income obtained from the exploitation of certain natural resources (including crude oil), and tax on supplementary income further to deregulation of the prices in the natural gas industry)[1]
- Capital allowances[2]

1 Applicable from 1 February 2013 until 31 December 2018.

2 The taxpayer may opt for the accelerated depreciation method in the case of technical equipment, tools, and work installations, as well as computers and related peripheral equipment.

B. Fiscal regime

Administration

In general, the tax year is the calendar year. However, taxpayers may opt for a tax year different from the calendar year.[3]

Corporate tax

Romanian resident companies are subject to a 16% CIT on their worldwide taxable profits. Profits are computed as the difference between the total income and total expense booked in the company's accounts, subject to certain adjustments (e.g., nontaxable revenues are subtracted; nondeductible expenses are added). Generally, expenses are treated as deductible for tax purposes if they are incurred for business purposes.

The value of depreciable assets is recovered through tax depreciation, which is computed based on the useful life of the asset and the depreciation method applied by the taxpayer. Costs related to locating, exploring, developing or any other preparatory activity for the exploitation of natural resources, including investments made for the discovery of useful mineral resources, for opening and preparing drilling extraction, which are directly expensed in the company's profit and loss account (as per relevant accounting regulations in place) are recovered in equal amounts over a period of five years, starting from the month when the expenses are incurred. If these costs are capitalized, recovery shall be performed as follows:

- As the natural resources are exploited, proportionally to the recovered value compared with the total estimated value of the resources
- In equal installments over a period of five years, if natural resources are not found

Abandoned exploration wells are also subject to the abovementioned provisions.

Expenses related to the acquisition of any exploitation right in respect of natural resources are recovered as the resources are exploited, in proportion to the recovered value compared with the total estimated value of the resources.

Depreciation of buildings and constructions used in oil extraction, for which the useful life is limited to the duration of the reserves and which may not be used after depletion of reserves, is computed per unit of production, depending on the exploitable reserve of mineral substance. The production factor for per-unit depreciation is recalculated at every fifth year of oil extraction.

Titleholders of petroleum agreements and their subcontractors that carry out petroleum operations in maritime areas (which include waters deeper than 100 meters) compute the depreciation of tangible and intangible assets related to petroleum operations for which the useful life is limited for the period of the reserve for each unit of product with a 100% degree of use, based on the exploitable reserve of the useful mineral substance over the period of the petroleum agreement.

Titleholders of petroleum agreements must create a tax-deductible provision for environmental recovery of the area affected by extraction. Such tax-deductible provisions should be of 1% applied to the accounting result from operations related to the segment of exploitation and production of natural resources, with the exception of the result from operations corresponding to marine perimeters including deepwater areas greater than 100 meters, and excluding the result of other segments of activity of the taxpayer, throughout the functioning duration for the exploitation of natural deposits.

Moreover, for titleholders of petroleum agreements that carry out offshore operations at depths of more than 100 meters, the tax-deductible provision for the dismantling of wells, installations and annexes, as well as for environment rehabilitation, is 10% (applied to the part from the accounting result in relation to the segment of exploration and production of natural resources corresponding to

3 Changes to the tax year should be communicated by taxpayers to the relevant Romanian tax authorities within 15 days from the beginning of the modified tax year or from their registration date, as the case may be.

these marine perimeters, and excluding the result of other activity segments of the taxpayer, throughout the whole oil exploitation period).

In addition to the above, reserves set up by taxpayers, representing the level of expenses required for the development and modernization of oil and natural gas production, oil transport and distribution, as well as for the geological program or other activities, which are regulated by legal norms, are included in the taxpayer's taxable income along with the depreciation of such assets or their write-off, respectively along with the expense incurred, which are financed from this source.

Romanian companies (including petroleum companies) are permitted to opt[4] for the declaration and payment of annual CIT with advance payments performed on a quarterly basis, based on the CIT paid in the previous year and adjusted with the annual consumer price index. Such an option is mandatory for at least two consecutive tax years.

Starting from 1 January 2018, companies operating in the oil and gas sector are no longer excluded from the categories of taxpayers required to apply the Romanian micro-enterprise tax regime. Therefore, provided certain conditions are met (including, among other things, a level of revenues lower than €1 million in the previous tax year), a company operating in the Romanian oil and gas industry may be subject to the micro-enterprise tax regime. Additional criteria were introduced starting April 2018 regarding the possibility to opt for CIT regime (the option being a definitive one).

Romanian companies (including petroleum companies) benefit from a tax credit for revenues obtained through a permanent establishment (PE) located in another country and for income subject to withholding tax (WHT) abroad if the revenues are taxed both in Romania and abroad and provided that the relevant double tax treaty concluded between Romania and the respective state is applicable and mentions the credit method in case of double taxation. However, any tax credit is limited to the tax that would have been levied on the income in Romania under domestic tax rules.

Romanian PEs of foreign legal entities that are resident in an EU Member State or in a state of the European Economic Area and derive income from another EU member state, or from a state of the European Economic Area, benefit under certain conditions of a tax credit for the tax paid in the state where the income included in the taxable income of the PE from Romania was derived.

In case a Romanian legal entity derives profits from a foreign state through a PE, which can be taxed in the respective foreign state according to the double tax treaty, and the treaty provides for the exemption method, the respective profits shall be exempt from CIT in Romania.

A foreign company that derives income from a PE in Romania is subject to a rate of 16% on profits attributable to the PE. The Romanian legislation contains specific provisions regarding the conditions under which PEs arise in Romania. These rules are generally in line with the Organisation for Economic Co-operation and Development (OECD) Guidelines.

Starting 1 July 2013, tax consolidation was introduced for foreign legal entities having several PEs in Romania (i.e., offsetting the taxable profits of a PE against the tax losses of another PE).

Starting 1 January 2016, special anti-abuse provisions in respect of cross-border artificial transactions (please also refer to Section E) that have no economic purpose, reclassification of a transaction activity to reflect its economic substance, redefinition of transactions that constitute an abuse of law, etc., were introduced as well.

Separately, as of 1 January 2018, a general anti-abuse rule has been introduced for profits tax purposes, following the early transposition of the EU Anti-Tax Avoidance Directive (ATAD) into the Romanian tax law, stating that for the purpose of calculating the corporate income tax liabilities, an arrangement or a series of arrangements that has been put into place for

4 *The official deadline for registering the option is 31 January of the respective year.*

the main purpose of obtaining a tax advantage should be ignored. Additional anti-abuse provisions transposed in the Romanian Tax Code and applicable starting 1 January 2018 refer to the following:

- Introduction of controlled foreign company (CFC) rules
- New tax provisions related to the transfer of assets, tax residency and/or economic activity carried out through a PE for which Romania loses its taxing right
- New rules regarding the deductibility of borrowing costs (as detailed in Section F hereinafter)

Capital gains

Please refer to Section G for an explanation of the taxation of capital gains.

Functional currency

In general, accounting records must be kept in the Romanian language and in Romanian currency (RON). Accounting records relating to operations carried out in a foreign currency must be kept both in national and foreign currency. Tax amounts must be declared and paid in Romanian currency.

Transfer pricing

Overview of the transfer pricing documentation requirements

Under the Romanian fiscal law, transactions between related parties must be performed in accordance with the arm's-length principle. The Romanian transfer pricing regulations generally follow the OECD transfer pricing guidelines. Taxpayers are required to prepare a specific transfer pricing documentation file and present it to the tax authorities upon request.

Starting with 2016, large taxpayers that carry out transactions with related parties of a total annual value above certain thresholds have to prepare on an annual basis the transfer pricing documentation within the legal deadline for submission of the annual corporate income tax return (the transfer pricing documentation does not have to be submitted together with the annual corporate income tax return).

The transfer pricing documentation may be requested during or outside a tax audit for transactions undertaken starting from 2016.

The thresholds considered for establishing the annual mandatory preparation of the transfer pricing documentation (thresholds obtained by cumulating the value of transactions with all related parties, excluding VAT, per transaction flow) are €200,000 for interest paid/received for financial services, €250,000 for services provided/received and €350,000 for acquisitions/sales of tangible or intangible assets.

The transfer pricing documentation is to be provided to the tax authorities within 10 days from the request date, but not earlier than 10 days from the deadline set for its preparation.

Large taxpayers that perform intercompany transactions that do not exceed the abovementioned thresholds, as well as small and medium taxpayers, are required to prepare the transfer pricing documentation only upon request from the tax authorities during a tax audit — in case any of the following thresholds (obtained by cumulating the value of transactions with all related parties, excluding VAT, per transaction flow) are exceeded: €50,000 for interest paid/received for financial services, €50,000 for services provided/received and €100,000 for acquisitions/sales of tangible or intangible assets.

The deadline for providing the transfer pricing documentation is set by the authorities between 30 and 60 days (the taxpayer having the possibility to request a single extension of at most 30 days).

The information that should be included in the transfer pricing documentation prepared in compliance with the Romanian transfer pricing documentation requirements has been significantly expanded, considering the amendments of the OECD transfer pricing guidelines further to the OECD Action Plan on Base Erosion and Profit Shifting (BEPS).

Advance pricing agreement (APA) program

The advance pricing agreement program is available for taxpayers in Romania. The following types of APAs are available:

- Unilateral APAs: agreements that are between only the taxpayer and the tax authority in one country (i.e., Romania) and are not binding for the tax authorities from other countries
- Bi-/multilateral APAs: agreements that are concluded with tax authorities from more than one country (existence of double tax treaties between the countries involved is required)

APAs in Romania can only be obtained for future transactions/operations and can be issued for a maximum period of five years, with the possibility of obtaining extension(s).

Country-by-country reporting requirements

The country-by-country reporting requirements were enacted in Romania in June 2017. Such requirements apply to Romanian entities that are part of multinational enterprise groups having consolidated income reported in the last fiscal year prior to the reporting period of at least €750 million. Depending on certain specific circumstances, the Romanian entities that are part of such multinational groups will have to file with the Romanian tax authorities either the country-by-country report together with a notification, or the notification only.

Dividends

Starting 1 January 2016, dividends paid by Romanian companies to resident companies are subject to a 5% withholding tax. This tax is considered a final tax, and accordingly, from a CIT perspective, the dividends are not included in the taxable income of the recipient. However, dividends paid by Romanian legal entities to Romanian shareholders (legal entities) that hold at least 10% of the share capital of the dividend payer for an uninterrupted period of one year ending on the date of dividend payment will be exempt from dividend tax.

Dividends received by Romanian shareholders from member state companies or third-country companies (with which Romania has concluded a double tax treaty) are exempt from CIT in Romania, provided certain conditions are met, including also the ones mentioned above regarding the minimum 10% shareholding for an uninterrupted period of one year.

This tax exemption will not apply in case the dividends distributed to the Romanian legal entities or to the Romanian permanent establishments of foreign legal entities located in another EU state are tax-deductible at the level of the foreign subsidiary.

Moreover, it is stated that the abovementioned provisions are not applicable in case of actions made with the purpose of obtaining a tax benefit and which may be linked to fraud and tax evasion.

Royalty regimes

The law does not generally apply different royalty regimes to onshore and offshore production.

Generally, petroleum royalties represent the amounts payable by the titleholders of petroleum agreements with the Romanian State for the exploitation of oil fields that are public property, for the transport and transit of oil through oil mains piping, for operation of oil terminals, and for underground storage of natural gas.

The petroleum royalty due to the Romanian State by the titleholders of petroleum agreements is computed based on reference prices established by competent authorities.

The petroleum royalty is payable from the commencement date of petroleum operations. It is payable on a quarterly basis, by the 25th day of the first month following the relevant quarter. Nonpayment or late payment of the petroleum royalty may trigger late payment charges and, in certain cases, may lead to the cancellation of the concession title granted to the titleholder of the petroleum agreement.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas since the law does not generally apply different royalty regimes to unconventional oil and gas.

Special taxes

A 60% tax is charged on the supplementary revenues derived by natural gas producers and distributors (including their subsidiaries and/or economic operators that are part of the same economic interest group), from the deregulation of natural gas prices in case of supplies to final consumers. The taxable base is computed by deducting from the supplementary revenues:

- Related royalties
- Upstream investments, capped at 30% of the supplementary revenues.

Please note that starting 1 April 2018, the special tax on supplementary revenues derived by natural gas producers and distributors will be amended as follows:

- A 60% tax will be charged on the supplementary revenues in case of prices up to RON85/megawatt hour (MWh) inclusively
- In case of prices exceeding RON85/MWh, an 80% tax will be charged on the supplementary revenues obtained from the difference between the RON85/MWh and the actual price used
- The special tax will be applicable for an unlimited period of time (as per the current provisions, the special tax was applicable only until the end of 31 December 2018)

Companies (including their subsidiaries and/or economic operators that are part of the same economic interest group) exploiting natural resources (such as coal, crude oil, ore), with the exception of natural gas, will be liable to pay a tax of 0.5% of their revenues (computed based on specific regulations).

Also, a tax is due in respect of the activities of companies that transport electricity and natural gas and certain distributors of electricity and natural gas (natural monopolies) that hold licenses issued by ANRE (the Romanian regulatory authority in the field of energy). The tax is charged for each MWh for which electricity and natural gas transportation and distribution services are invoiced, the level of the tax ranging from RON0.1/MWh to RON0.85/MWh.

These taxes are payable on a monthly basis by the 25th of the following month.

C. Capital allowances

Generally, depreciable assets are any tangible, immovable assets that:

- Are held and used in production or supply of goods or services, to be rented or for administrative purposes
- Have a tax value equal to or exceeding the limit established by the government at the date of their entry in the taxpayer's patrimony (currently RON2,500)
- Have a useful life exceeding one year

The law also specifically enumerates other items that should be treated as depreciable fixed assets (e.g., investments in fixed assets granted under a concession, investments made for the discovery of useful mineral resources, improvements to the pre-existing fixed assets).

The useful lives to be used for the computation of tax depreciation are specified by legislation. The table below summarizes the useful lives of certain general categories of assets relevant to the oil and gas industry.

Item	Type of depreciating assets	Period (years)
1	Oil and gas extraction assets	4-12
2	Assets for processing oil	7-18
3	Oil and gas transportation and distribution assets	12-60
4	Oil and gas derricks	8-12
5	Sea drilling and extraction platforms	24-36

The tax depreciation methods that may be used depend on the nature of the asset, as follows:

- The straight-line depreciation method alone may be applied for buildings.
- For technological equipment, machinery, tools, work installations, and computers and related peripheral equipment, the taxpayer may choose between the straight-line, the declining-balance and the accelerated depreciation methods.
- For other depreciable assets, the taxpayer may choose between the straight-line and the declining-balance tax depreciation methods.

Specific regulations have been introduced regarding the deductibility of the remaining undepreciated tax value in the case of the retirement of fixed assets used in the oil industry by taxpayers that apply accounting regulations in line with the International Financial Reporting Standards (IFRS) and that set accounting policies specific to the industry's activity for depreciation of these assets.

D. Incentives

Annual tax losses may be offset against taxable profits during the following seven consecutive years. Losses must be recovered in the sequence they were recorded. Tax losses may not be carried back.

A 50% additional tax deduction for eligible research and development expenses can be granted for qualifying companies when computing their taxable profit. Furthermore, this incentive could be granted for research and development activities carried out in Romania or in other EU and European Economic Area Member States. The tax incentives for research and development expenses are granted separately for each project undertaken.

The Fiscal Code allows "sponsorship" expenses to be claimed as a credit against CIT due, subject to certain limitations (the lower amount between 0.5% of turnover and 20% of the profit tax due). Sponsorship expenses that were not used for obtaining a tax credit can be carried forward for seven consecutive years. Additionally, starting 1 January 2016, the limitations for tax credit to be claimed in respect of sponsorship have been increased. Also, the deductibility limit for social expenses has been increased to 5% as of 1 January 2016.

Furthermore, the profits invested in production and/or acquisition of certain technological equipment, computers and related peripheral equipment, cash control and invoicing machines, as well as software, as listed in the catalog regarding the classification and the normal useful life of fixed assets is exempt from corporate income tax. The profits tax exemption is applicable in case of technological equipment put into use up to 31 December 2016. The period of retention in the patrimony of the technological equipment should be of at least half of their useful life, but not more than five years, with certain exceptions (e.g., cases where the technological equipment is destroyed, lost or stolen).

E. Withholding taxes

Romanian tax regulations specifically define the income derived by nonresidents from Romania that is subject to WHT in Romania. The main categories of income covered by this provision are dividends, interest, royalty, commissions, income from management and consultancy services in any field (if such income is obtained from a resident or if the respective income represents cost attributable to a PE in Romania), income from services performed in Romania (except for international transport and services ancillary to such transport) and revenue from the liquidation of a Romanian legal entity (including, in certain cases, the income obtained from the reduction of share capital). In general, the provisions of double tax treaties concluded by Romania prevail over domestic legislation. Therefore, these provisions may be invoked when levying Romanian WHT. To qualify, the nonresident income beneficiary must provide (i.e., at the moment when the payment is performed) the Romanian income payer with a tax residency certificate attesting that the income recipient was a tax resident in the relevant country during the period when the relevant income was derived from Romania, as well as an "own liability" statement in cases where EU legislation is applicable to the beneficiary of the income.

However, in the case of "net of tax" arrangements, whereby the Romanian party bears the WHT (instead of retaining the tax from the amount paid to the nonresident), the application of the double tax treaty provision is restricted under Romanian law. In such cases, the applicable WHT must be determined based on the gross-up method. The related expenses with such tax would also be nondeductible for CIT purposes at the level of the Romanian income payer. The provisions of double taxation treaties cannot be applied by taxpayers for cross-border transactions or series of transactions qualified by the Romanian tax authorities as "artificial." Artificial cross-border transactions are defined in Romanian tax legislation as transactions or series of transactions without economic substance and which cannot normally be utilized in usual economic practices, their main purpose being tax avoidance and obtaining tax benefits that otherwise would not be granted.

Revenues of a nonresident that are attributable to a Romanian PE of the nonresident are not subject to WHT in Romania (because the income is subject to a 16% Romanian CIT at the level of the PE).

Also, specific provisions are applicable with regard to:

- The taxation of income derived by joint ventures/entities that carry out activities/derive income in/from Romania
- Rules applicable in the case of joint ventures/tax transparent entities without corporate status that are established in accordance with the Romanian law or in the case of nonresident entities/joint ventures that are established in accordance with the law of a foreign state (please also refer to "Forms of business presence" in Section I)

Dividends

Starting 1 January 2016, dividends paid to nonresidents are generally subject to a 5% WHT (this rate is applied even in the case of dividends distributed from profits pertaining to previous reporting exercises, but paid after 1 January 2016).

However, dividends paid by a Romanian legal entity or by a legal entity having its legal headquarters in Romania (i.e., a *societas europaea*) to a legal entity residing in another EU state or to a PE of an EU entity (situated in another EU state) may be reduced to nil if certain conditions related to the legal entity receiving the dividends and to the Romanian income payer are met.

These conditions include the following, whereby the legal entity:

- Should be set up in one of the legal forms provided by the law and should be resident in the respective EU state and, from a tax perspective, according to the double tax treaties concluded with third parties, should not be resident outside the EU
- Should be liable to pay CIT or other similar tax as per the tax legislation in the state of residence without the possibility of exemption or choice of tax treatment
- Holds at least 10% of the participation titles in the Romanian legal entity for an uninterrupted period of at least one year ending on the date of the payment of the dividends.

Conditions regarding the Romanian legal entity paying the dividends include that it:

- Should have one of the following legal forms: joint stock company, limited liability company, general partnership, limited partnership or partnership limited by shares
- Should be liable to pay CIT without the possibility of exemption or choice of tax treatment

Moreover, starting from 1 January 2016, the Romanian tax legislation provides that no dividend tax is due in the case of dividends that are distributed, but not paid by the end of the year, when the annual financial statements were approved, provided that on the last day of the calendar year/amended tax year the conditions for applying the exemption mentioned above are met.

Interest and royalties

Interest and royalties are generally subject to a 16% WHT rate.

However, based on the EU Interest and Royalty Directive implemented in Romanian tax legislation as of 1 January 2011, an interest or royalty payment is exempt from Romanian WHT if the recipient is a legal entity resident in another EU state (or a PE, situated in another EU state of a legal entity from an EU state) that holds at least 25% of the share capital of the Romanian interest or royalty payer for an uninterrupted period of at least two years (ending on the date of the interest or royalty payment).

Technical services and nonresident contractors

According to the Romanian tax regulations, fees paid by a Romanian entity to a nonresident service provider are subject to WHT in Romania if such services are rendered in Romania (except for international transport and services ancillary to international transport) or abroad (in case of management and consultancy services). The WHT for these services is 16% under the domestic legislation.

Specific concern arises for service contracts (e.g., technical services contracts) whereby the nonresident transfers know-how or rights triggering royalty payments. In these cases, the provisions regarding the WHT treatment of royalties applies (at least to the part of the contract corresponding to the transfer of know-how or rights).

Attention should also be paid to the potential PE exposure that could arise, which is based on the specific characteristics of the activity carried out by the nonresident in Romania.

In this respect, Romanian legal entities, individuals and PEs of nonresidents in Romania should register with the competent tax authorities the service agreements concluded with nonresidents that perform services generating taxable revenues in Romania, or any other supporting documents attesting that the transaction was performed (e.g., worksheets, market research reports, feasibility studies). The agreements/supporting documents should be registered within 30 days from their conclusion. No registration requirement is imposed for those contracts concluded with nonresidents that imply performing economic activities outside Romania.

A withholding tax of 50% applies, among other things, for interest, royalties, commissions and income from the rendering of certain types of services in Romania or abroad if this income is paid in an account from a state with which Romania does not have in place a legal instrument for the exchange of information for those transactions qualified by the Romanian tax authorities as "artificial."

Branch remittance tax

No branch remittance tax is imposed under Romanian legislation.

F. Financing considerations

Deductibility of borrowing costs

Starting 1 January 2018, Romania has introduced the interest limitation rule based on earnings before interest, taxes, depreciation and amortization (EBITDA), as provided by ATAD. As such, the exceeding borrowing costs (i.e., the amount by which deductible borrowing costs exceed taxable interest revenues) above the annual threshold of €200,000 in relation to various types of financing (including, e.g., bank loans, intercompany loans, finance leasing) may be deducted for CIT purposes only up to 10% of the company's (adjusted for tax purposes) EBITDA. Non-deductible borrowing costs (i.e., exceeding 10% on the adjusted EBITDA) would be available for carryforward for an unlimited period of time (i.e., until the CIT deduction would be available).

G. Transactions

Asset disposals

Gains derived by a Romanian company from the sale of assets are included in taxable profits and are subject to the standard 16% CIT rate. Gains are generally computed as the difference between the selling price of the immovable property and its acquisition cost, as adjusted with the related tax depreciation (as the case may be). Any revaluation of assets must be considered from a tax perspective when establishing the assets' fiscal value. However, the unrealized revaluation reserves (i.e., those not realized through depreciation) pertaining to the assets that are disposed of are taxed upon their disposal at the 16% CIT rate, like other elements in the nature of income.

From a value-added tax (VAT) perspective, sales of immovable property (i.e., buildings and land) are generally exempt from VAT, without credit for input VAT paid on related costs and expenses. However, companies may opt for taxation for these operations (i.e., they may opt to apply VAT and, therefore, recover input tax). As a derogation, the sale of a new building and of building land (as defined by law) is a taxable operation for VAT purposes (i.e., it cannot be exempted). Starting 1 January 2016, the sale of buildings and land is subject to simplification measures (i.e., the beneficiary may apply the VAT reverse charge mechanism, provided that both the supplier and the customer are registered for VAT purposes in Romania).

Also, income derived by foreign legal entities from sales of immovable property located in Romania (i.e., including rental or lease of immovable property located in Romania), from the exploitation of natural resources located in Romania or from the sale of shares owned in a Romanian legal entity is subject to the 16% CIT.

Farm-in and farmout

Generally, a new company or a consortium (e.g., a joint venture) is set up in Romania by the parties involved in a farm-in agreement. Consortiums are entities without legal status that are subject to specific CIT, VAT and accounting rules. Please refer also to Section E and to "Forms of business presence" in Section I.

From a VAT perspective, a consortium does not give rise to a separate taxable person. Under certain conditions, the rights and obligations of the participants relating to VAT may be fulfilled by one of the members.

Selling shares in a company

Similar to an asset disposal, and for CIT purposes, gains derived by a Romanian CIT payer from the sale of shares are added to profits derived from other activities and are taxed at 16%. Capital gains derived by a taxpayer from the sale/assignment of shares held in Romanian legal entities or in legal entities from countries with which Romania has concluded a double tax treaty are not taxable if the taxpayer holds, for an uninterrupted period of one year, at least 10% of the share capital of the legal entity whose shares were sold/assigned.

Capital gains derived by nonresident legal entities from the sale of ownership rights in shares held in Romanian legal entities are taxable in Romania at the standard CIT rate of 16%.

It should be noted that starting 1 January 2016, the Romanian domestic legislation provides that if particular conditions are met, an exemption of the abovementioned taxation rule for capital gains obtained by nonresident legal entities from the sale of shares owned in a Romanian entity would be applicable (i.e., (i) the foreign legal entity provides a tax residency certificate, (ii) a double tax treaty is concluded between Romania and the country where the nonresident is established and (iii) taking into considerations the provisions of the double tax treaty, the right of taxation is not in Romania).

Also, proceeds obtained by a Romanian CIT payer from the liquidation of another Romanian legal entity or of foreign legal entities from countries with which Romania has concluded a double tax treaty are not taxable in Romania provided that the minimum shareholding requirement of 10% for a period of one year is met.

H. Indirect taxes

Import and export duties

Import and export duties are based on the combined nomenclature classification of the imported or exported goods involved, in accordance with EU customs regulations.

VAT

The Romanian VAT legislation is based on the EU VAT Directive.

As a general rule, to fall within the scope of Romanian VAT, a transaction must satisfy all of the following conditions. It must:

- Qualify as a supply of goods or services for consideration
- Have its place of supply in Romania (according to the VAT place-of-supply rules)
- Be performed by a taxable person (as defined by the VAT law), acting as such
- Be derived from an economic activity

Generally, operations subject to Romanian VAT fall into one of the following categories:

- Taxable, at 19% (the standard VAT rate starting with 1 January 2017) or 9%/5% (the reduced VAT rates)
- Exempt with credit (as specifically set out in the law, such as exports and intra-Community supplies of goods)
- Exempt without credit (as specifically set out in the law)
- Imports or intra-Community acquisitions (taxable at the same rate as domestic transactions)

Specific VAT rules apply to supplies of goods (intra-Community supplies and intra-Community acquisitions of goods) or services between Romanian persons and persons from other EU member states and non-EU countries.

A taxable person established in Romania who performs taxable or exempt-with-credit supplies must register for VAT purposes in Romania if its annual turnover (computed based on specific rules) exceeds RON300,000. A taxable person established in Romania may also opt for VAT registration in Romania even if this threshold is not exceeded (subject to certain conditions imposed by the Romanian tax authorities). Different VAT registration rules apply to taxable persons that are not established in Romania or that are established via a fixed place of business.

If a taxable person who is established in another EU member state is liable to register for VAT in Romania, the registration may be made either directly or through a fiscal representative. A person who is not established in the EU, and who is required to register for VAT in Romania, must obtain registration through a fiscal representative.

The VAT cash accounting system was introduced into the Romanian VAT legislation. The taxable persons that are registered for VAT purposes in Romania, having the place of economic activity in Romania and an annual turnover (computed based on specific rules) under RON2,250,000 can opt for applying the VAT cash accounting system.

Taxable persons opting for implementation of the VAT cash accounting system, or for the cancellation of this system, are required to submit by 25 January a notification to the relevant tax authorities.

Where a taxable person exceeds the threshold of RON2,250,000 during the year, the system is applied until the end of the next fiscal period in which the threshold was exceeded (by submitting a notification in this respect).

Taxable persons opting for implementation of the system are required to maintain the option until the end of the year. However, starting with the second year, the option may be canceled at any time during the year, between the 1st and 25th of the month.

The VAT cash accounting system is not applicable to the following taxable persons:

- Taxable persons established in Romania that are part of a VAT group
- Taxable persons not established in Romania that are registered in Romania for VAT purposes directly or through a fiscal representative
- Taxable persons that have the seat of their economic activity outside Romania, but have a fixed establishment in Romania in respect of their outgoing activities
- Taxable persons that exceeded the threshold of RON2,250,000 during the previous year
- Taxable persons registered for VAT purposes during the current year and that exceeded the threshold in the previous year or in the current year computed for the transactions for which the taxable person used a valid VAT ID number

Moreover, certain operations (e.g., supplies of goods or services that are exempt from VAT, supplies of goods or services between related parties, and supplies of goods or services for which the beneficiary is liable to pay VAT) are excluded from the application of the VAT cash accounting system.

According to the VAT cash accounting system, the VAT chargeability occurs at the date when the invoices issued are cashed.

Furthermore, taxpayers applying the VAT cash accounting system are allowed to deduct the VAT related to their acquisitions only after paying the invoices issued by the suppliers. The same limitation of the deduction right is applicable to persons that do not apply the VAT cash accounting system, but who perform purchases of goods and services from persons that apply this system.

Starting October 2017, Romania has introduced the VAT split mechanism, according to which taxable persons registered for VAT purposes in Romania (as well as the public institutions registered according to that article) are required to open separate accounts for the collection and payment of VAT. The VAT split payment applies to all taxable supplies of goods/services, for which the place of supply is in Romania (some exceptions are provided). For the period October 2017–December 2017, the system was optional.

Starting 1 January 2018, the split payment mechanism is mandatory for taxable persons who had outstanding VAT debts toward the Romanian State Budget as at 31 December 2017 over certain thresholds or those who are undergoing insolvency proceedings or those who have outstanding VAT debts toward the Romanian State Budget older than 60 days and over certain thresholds. The system is optional for all other VAT-registered taxable persons. A tax incentive of a 5% decrease in the profit tax/income of microenterprises will be granted for the entire period during which the VAT split payment mechanism is optionally applied.

Persons not registered for VAT purposes, as well as individuals or legal persons not established in Romania, are not required to make payments into the VAT account of a supplier who applies the VAT split payment mechanism.

Certain operations have been specifically excluded from the VAT split payment mechanism, such as payments performed on behalf of another person, financing granted by credit institutions and nonbanking financial institutions in the case of assignment of receivables, payments in kind and compensation payments.

Taxpayers that do not apply the VAT split payment mechanism are liable to make split payments from their current accounts to the VAT account of any suppliers that do apply the VAT split payment mechanism.

The law also provides rules for leaving the VAT split payment mechanism.

Failure to comply with the rules surrounding the VAT split payment mechanism are subject to penalties.

Specific VAT regulations have been enforced starting 1 February 2013 for transactions carried out between related parties. Thus, the VAT taxable base for goods delivered and services rendered between related parties are the market value in the following cases:

- When the consideration for the goods and services is less than the market value and the beneficiary does not have full deduction right
- When the consideration for the goods and services is less than the market value and the supplier does not have full deduction right and the delivery is VAT-exempt
- When the consideration for the goods and services is higher than the market value and the supplier does not have full deduction right

As a general rule, taxable persons registered for VAT purposes in Romania may deduct the Romanian input VAT related to their acquisitions only if such operations are carried out with the goal of performing transactions with the right to deduct input VAT (such as taxable or exempt-with-credit transactions). Certain limitations exist on the deduction of input VAT related to the acquisition of cars and also for the input VAT for vehicle-related expenses (e.g., repair and maintenance, spare parts, fuel). Deductible input VAT may be offset against the VAT collected by the taxable person (output VAT).

Specific rules apply in the case of operations qualifying as a transfer of a going concern. Specifically, the transfer of assets or a part thereof does not fall within the scope of Romanian VAT if the transferee is a taxable person established in Romania and if the transfer of assets is the result of transactions such as a sale, spin-off, merger or contribution in kind to the share capital of a company. Such transactions mainly refer to cases where the assets transferred constitute an independent structure capable of performing separate economic activities.

Excise duties

Under Romanian law, excise duties are due for certain energy products such as gasoline, diesel oil and natural gas. Generally, Romanian regulations regarding harmonized excise duties are based on the EU excise duty legislation.

Starting 1 January 2015, the excise duty rate in the case of energy products (including natural gas) is expressed in RON per measurement unit (gigajoule, in the case of natural gas and ton/liter in the case of other energy products) and generally depends on the type and the destination of the product.

The chargeability of excise duties occurs, in principle, upon the release in consumption of the excise energy products, or when certain losses or shortages are ascertained (e.g., upon exit from the suspension regime, importation, losses of products).

Production of energy products (except for coke, coal and natural gas) is allowed only in authorized production fiscal warehouses. Storage fiscal warehouses may be used only for storage of excise products. Moreover, in the particular case of energy products, the law provides that the process of adding additives can also be performed in a storage warehouse.

Authorization of premises as a fiscal warehouse (for production or storage) is subject to specific conditions. Such locations are under the control of the competent relevant authorities and are subject to strict rules. Fiscal warehouse keepers have specific reporting obligations related to excise duty.

Excise products may be transported between fiscal warehouses or between a fiscal warehouse and a customs office under an excise duty suspension regime, provided that certain conditions are met. The intra-Community movement of excise products between EU Member States is subject to specific rules under Romanian law, which generally follows EU legislation.

Supplies of excise goods destined for certain purposes (e.g., fuel for navigation, aviation) are exempt from excise duty, subject to specific conditions.

Notary and land book fees

The sale or purchase of real estate located in Romania is subject to notary and real estate publicity fees, set by applying a specific percentage to the transaction value.

Registration fees

The registration of a company in Romania is subject to certain immaterial fees.

Certain services provided by the competent authorities in relation to petroleum operations (e.g., issuing authorizations) are subject to fees computed based on the salary and other related expenses incurred by the authorities. In addition, fees for the provision of information necessary for petroleum operations (e.g., regarding oil resources) are levied based on the volume and quality of the information and the investigation method used for obtaining such data.

Other significant taxes

Other significant taxes include salary-related social contributions paid by the employer.

I. Other

Authorization for petroleum operations

The law establishes a detailed procedure for granting petroleum concessions (whereby the state grants the right to a legal person to perform petroleum operations) and specific rules for carrying out petroleum operations. Foreign legal entities that are granted the right to perform petroleum operations are required to set up a subsidiary or a branch in Romania and to maintain it throughout the concession period.

The transfer of any rights and obligations derived from the petroleum concession is subject to prior approval of the relevant authorities.

Special fund for petroleum products

Gasoline and diesel oil produced or obtained as a result of processing are subject to a contribution to the special fund for petroleum products. A contribution is levied by including a fixed RON amount, equivalent to US$0.01 per liter, in the price of these products. The obligation to compute and pay a contribution to the special fund remains with the producers and processors that are legal entities headquartered in Romania.

Domestic quality requirements

The law imposes certain quality standards that must be met for certain energy products traded on the Romanian market.

Energy products (e.g., diesel oil and gasoline) must contain a minimum percentage of biofuels (i.e., fuels used for transport and produced from biomasses). From 2016, for diesel oil, the percentage is 6.5% of the volume, and for gasoline, starting 2018, the percentage is 8% of the volume.

Environment fund

Economic operators that own stationary sources that release air pollutants are required to pay a contribution to a special environmental fund. The amount of the contribution depends on the nature of the pollutant.

Also, economic operators that introduce dangerous substances (as defined in the specific legislation) into the Romanian market are required to pay a contribution to the same fund.

Foreign investment

The Romanian authorities generally encourage foreign investment, and they seek to ensure non-discriminatory treatment of such investments. Associations organized by foreign investors in Romania and bodies of Romanian authorities supervise and facilitate foreign investments in Romania.

Notification requirements

Competent authorities (e.g., the BNR) must be notified of certain operations (e.g., loans) carried out by Romanian entities with foreign persons.

Forms of business presence

Forms of business presence in Romania include companies, branches and associations in participation (e.g., joint ventures).

From a tax perspective, starting 1 January 2016, the new Romanian Tax Code introduces provisions regarding new type of entities, specifically tax transparent entities with or without legal personality, including, among other things, joint ventures or any associations made based on joint operating agreements, where each participant/partner is subject to tax within the meaning of CIT/income tax, as the case may be.

Moreover, the Romanian Tax Code mentions that the tax transparent entity with legal personality does not fall under the scope of Romanian CIT.

Application of IFRS for listed companies

Starting with the financial year 2012, companies whose securities are listed on a regulated market are required to apply IFRS for the preparation of individual annual financial statements.

The individual financial statements prepared according to IFRS are subject to statutory audit, as per law.

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Tax regime applied to this country

■ **Concession** ■ Royalties ☐ Profit-based special taxes ■ Corporate income tax	■ **Production sharing contracts** ☐ **Service contract**

A. At a glance

The fiscal regime that applies in Russia to the petroleum industry consists of a combination of royalties (called mineral extraction tax (MET)), corporate profits tax and export duty.

- Profits tax rate – 20%
- Royalties (MET):
  - Crude oil – RUB919[1] (US$15.3)[2] per metric ton (tonne) adjusted by coefficients
  - Natural gas – RUB35 (US$0.6) per 1,000 cubic meters adjusted by coefficients
  - Gas condensate – RUB42 (US$0.7) per tonne adjusted by coefficients
- Export duty:
  - Crude oil – 30% to 45% (linked to oil price)[1]
  - Natural gas – 30%
  - Liquefied natural gas (LNG) – 0%

1 *See respective sections for more information on rates.*

2 *An exchange rate of 60 rubles per US dollar was used throughout the chapter to provide approximate US dollar values, where relevant.*

- Bonuses — Bonuses are specified in the license. A maximum amount is not fixed in legislation. The minimum rates of one-time payments for subsurface use, which are established in relation to oil and/or gas condensate, are established at no less than 5% of the amount of the MET, calculated on the basis of the average annual planned capacity of the subsoil user.
- Production sharing contract (PSC) — No PSCs are expected to be concluded unless there is an exceptional case, such as an obligation to enter into a PSC emanating from Russia's international conventions.
- Capital allowances (see Section D)
- Investment incentives

B. Fiscal regime

Corporate profits tax

Russian tax-resident companies are subject to profits tax on their nonexempt worldwide profits. Foreign companies operating in Russia through permanent establishments (PEs) are subject to profits tax on profit received through (or attributable to) those PEs.

Taxable profit equals nonexempt revenue less deductions. Nonexempt income includes sales income (determined with reference to accounting data for sales) and non-sale income (certain items are specifically mentioned in the Tax Code). Deductions include expenses to the extent that they are economically justified and documented in accordance with Russian legislation. However, expenditure of a capital nature is not immediately deductible.

Exploration costs are generally deductible within 12 months following the month when a particular stage in exploration work has been completed. Unsuccessful exploration costs are also written off over 12 months, as are expenses related to dry holes, following notice of liquidation of the well.

Development costs are deductible through depreciation of constructed fixed assets (see Section D).

The profits tax rate is 20%. The tax rate can be reduced for particular categories of taxpayers but not to less than 15.5%. For 2017–2020, the limitation for tax loss carryforward is established at 50% of the tax base for the current tax period. It is applicable for losses accumulated from 2007. Tax losses can be carry forward within the unlimited period of time.

Since 1 January 2018 the tax legislation was added by an investment tax deduction for corporate profits tax purposes, the right to use it should be established by the regional law. The Investment deduction (as an alternative to depreciation) could be applied to fixed assets related to the third to the seventh depreciation groups (see Section D).

Ring fencing

Russia does not apply ring fencing in determining an entity's corporate tax liability in relation to its oil and gas activities. Profit from one project can generally be offset against the losses from another project by the same Russian legal entity, and, similarly, profits and losses from upstream activities can be offset against downstream activities undertaken by the same Russian entity (individual branches of foreign companies are generally taxed as separate entities for profits tax purposes). Certain ring-fencing restrictions apply to new offshore projects that commence production on or after 1 January 2016 (see Section C). Tax consolidation is available for a limited number of companies due to very high quantitative criteria (for example, the group's annual revenue should not be less than RUB100 billion (approximately US$1.7 billion)). The abovementioned limitation regarding the carryforward of losses is effective for the consolidated group of taxpayers.

Mineral extraction tax

MET is levied on extracted natural gas, gas condensate and crude oil, and is deductible in calculating corporate profits tax.

Crude oil

The rate of MET on crude oil is established as the base rate per tonne of extracted oil (RUB919 for 2018), multiplied by a coefficient reflecting movements in world oil prices (C_p) and reduced by indicator E_m reflecting oil extraction factors. Special ad valorem MET rates apply to new offshore projects (see Section C).

The adjustment coefficient reflecting oil extraction factors (E_m) is calculated according to the following formula:[3]

$$E_m = C_{met} \times C_p \times (1 - C_d \times C_r \times C_{de} \times C_{rd} \times C_{can}) - C_k$$

MET = base rate × C_p - C_{met} × C_p × (1 - C_d × C_r × C_{de} × C_{rd} × C_{can}) + C_k	
C_{met}	C_{met} = RUB559
C_p	**C_p = (P - 15) × R/261** P – average price level of Urals oil for the tax period in US dollars per barrel R – average value for the month of the exchange rate of the US dollar to the Russian ruble as established by the Russian Central Bank
C_d	**C_d = 0.3** if the level of depletion of reserves of a particular subsurface site exceeds 1
	C_d = 3.8 - (3.5 × N/V) if the level of depletion is greater than or equal to 0.8 and less than or equal to 1 N – amount of cumulative oil extraction according to the state's balance sheet of reserves of commercial minerals for the calendar year preceding the accounting year in which the coefficient C_d is applied V – initially extractable oil reserves
	C_d = 1 if the rate of depletion is less than 0.8
	C_d = 1 if C_{de} is less than 1
C_r	**C_r = 0.125 × V_r + 0.375** if the initially extractable oil reserves of a particular subsurface site are less than 5 million tonnes and the level of depletion of reserves of a particular subsurface site is not more than 5% V_r – initially extractable oil reserves
	C_r = 1 in any other case
C_{de}[4]	**C_{de} = 0.2** initially in the case of extraction of oil from a specific hydrocarbon reservoir with an approved permeability of not more than 2×10^{-15} m² and a net pay for that reservoir of not more than 10 meters **C_{de} = 1** after the expiry of 15 years starting from 1 January of the year in which the level of depletion of reserves exceeded 1% **C_{de} = 1** after the expiry of 15 years starting from 1 January 2014 if the level of depletion of reserves exceeded 1% as of 1 January 2013
	C_{de} = 0.4 initially in the case of extraction of oil from a specific hydrocarbon reservoir with an approved permeability of not more than 2×10^{-15} m² and a net pay for that reservoir of more than 10 meters **C_{de} = 1** after the expiry of 15 years starting from 1 January of the year in which the level of depletion of reserves exceeded 1% **C_{de} = 1** after the expiry of 15 years starting from 1 January 2014 if the level of depletion of reserves exceeded 1% as of 1 January 2013

3 *The application of the coefficient C_{de} of less than 1 is subject to certain other conditions.*

	C_{de} = 0.8 initially in the case of extraction of oil from a specific hydrocarbon reservoir within productive formations of the Tyumen suite
	C_{de} = 1 after the expiry of 15 years starting from 1 January of the year in which the level of depletion of reserves exceeded 1% **C_{de} = 1** after the expiry of 15 years starting from 1 January 2014 if the level of depletion of reserves exceeded 1% as of 1 January 2013 **C_{de} = 1** after the expiry of 15 years starting from 1 January 2015 if the level of depletion of reserves is greater than 3% as of 1 January 2012
	C_{de} = 1 in any other case
C_{rd}	**C_{rd} = 0.3** if C_{de} for a specific hydrocarbon reservoir is less than 1 and the level of depletion of reserves of that hydrocarbon reservoir is greater than 1
	C_{rd} = 3.8 - (3.5 × N_{rd}/V_{rd}) if C_{de} for a hydrocarbon reservoir is less than 1 and the level of depletion of reserves of that hydrocarbon reservoir is greater than or equal to 0.8 and less than or equal to 1 N_{rd} – amount of cumulative oil extraction according to the state's balance sheet of reserves of commercial minerals for the calendar year preceding the accounting year in which C_{rd} is applied V_{rd} – initially extractable oil reserves
	C_{rd} = C_d if the following conditions are simultaneously met: ‣ The hydrocarbon reservoir for which the value of C_{rd} is being determined is situated within a subsurface site that contains another hydrocarbon reservoir for which the value of C_{de} is less than 1 ‣ The value of C_{de} for the hydrocarbon reservoir for which C_{rd} is being determined is equal to 1
	C_{rd} = 1 if C_{de} is less than 1 and the level of depletion of reserves is less than 0.8
	C_{rd} = 1 if the subsurface site does not contain hydrocarbon reservoir for which C_{de} is less than 1
C_{can}	**C_{can} = 0** for high-viscous oil which is extracted from subsurface sites containing oil of a viscosity exceeding 200 mPa × s but less than 10,000 mPa × s **C_{can} = 0** for oil extracted from oil deposits located in certain designated areas, until at least one of the following conditions is met: ‣ The accumulated extraction level of oil exceeds the threshold prescribed for each designated area. ‣ The period from the date the license was registered exceeds the maximum number of years prescribed for each designated area. ‣ The reserve's depletion of the deposits exceeds 5% on prescribed dates. ‣ Occurrence of prescribed deadlines for certain deposits
	C_{can} = 1 in any other case
C_k	C_k = 357 for 2018 C_k = 428 for 2019-2020 C_k = 0 for 2021 and onward

For zero MET rate and reduced MET coefficients, see Section E.
MET is not payable on associated gas (i.e., gas extracted via an oil well).

Natural gas/gas condensate

For natural gas and gas condensate, MET is payable as follows:

$$\textbf{MET on gas} = BR \times U_{sf} \times C_{df} + T_g$$

$$\textbf{MET on gas condensate} = BR \times U_{sf} \times C_{df} \times C_{cm}, \text{ where:}$$

BR = base rate of RUB42 per tonne for gas condensate and RUB35 per 1,000 cubic meters for gas; the rate is set in accordance with the calorific value of the fuels

U_{sf} = a base value of a unit of standard fuel, calculated taking into account the following:

- The price of gas supplied to the domestic market and beyond the boundaries of the territories of member states of the Commonwealth of Independent States
- A coefficient reflecting the proportion of extracted gas to the total amount of extracted gas and gas condensate
- The price of gas condensate (linked to the price of Urals oil)
- A coefficient reflecting a return on export of a unit of nominal fuel
- A coefficient that effectively impacts the MET calculation for Gazprom-affiliated companies only

C_{df} = a coefficient reflecting the degree of difficulty of the extraction of gas or gas condensate, equal to the lowest of the values of the following coefficients in the range of 0 to 1:

- C_{dg} – a coefficient reflecting the level of depletion of gas reserves of a particular subsurface site containing a hydrocarbon reservoir
- C_1 – a coefficient reflecting the geographical location of a subsurface site containing a hydrocarbon reservoir
- C_{do} – a coefficient reflecting the depth of occurrence of a hydrocarbon reservoir
- C_{as} – a coefficient reflecting whether or not a subsurface site containing a hydrocarbon reservoir serves a regional gas supply system
- C_{rdf} – a coefficient reflecting specific factors relevant to the development of particular reservoirs of a subsurface deposit

T_g = an adjustment linked to transportation costs of gas, which for non-Gazprom-affiliated companies is a negative figure, calculated taking into account:

- The difference between the actual average tariff for the transportation of natural gas and the estimated average rate of gas in the relevant year
- The average transportation distance for natural gas on pipelines in the year preceding the year of the tax period by non-Gazprom-affiliated companies
- A coefficient characterizing the ratio of the extracted gas by Gazprom and its affiliated companies to the amount of gas extracted by other taxpayers in the year preceding the year of the tax period

C_{cm} = 6.5 divided by C_{gp}

For Gazprom-affiliated companies, C_{gp} equals:

- 1.4022 – for 2018
- 1.4441 – for 2019–2020
- 1 – for 2021 and onward

C_{gp} equals 1 for non-affiliated to Gazprom companies.

The coefficients involved in the calculation of U_{sf}, C_{df} and T_g also involve separate calculations.

For zero tax rates for extracted natural gas and gas condensate, see Section E.

MET is not payable on natural gas reinjected to maintain reservoir pressure (to facilitate the extraction of gas condensate).

Export duty

Export duty for crude oil and condensate is determined by the Russian Government based on the price of Urals blend on the Mediterranean and Rotterdam markets. The rate (in US dollars per tonne) is changed every month.

Actual price per barrel (US$)	General duty rate per barrel (US$)
Up to $15	0%
Between $15 and $20	35% × (actual price – $15)
Between $20 and $25	$1.75 + 45% × (actual price – $20)
More than $25	$4 + 30% × (actual price – $25)

For special reduced export duty rates for crude oil, see Section E.

The export duty for exported natural gas is 30%. The export duty for exported LNG is 0%.

The export duty for stable gas condensate is the same as the general rate for crude oil. The export duty for stable gas condensate with specific physical and chemical characteristics obtained as a result of the processing of non-stable gas condensate extracted from the Yuzho-Tambeiskoye deposit is 0%.

The export duty for main petroleum products is set as the percentage of the export duty for crude oil:

Oil product	2018
Light petroleum products	30%
Motor oil	30%
Gasoline	30%
Naphta	55%
Fuel oil, bitumen and other dark petroleum products	100%

Production sharing contracts

Although the legislation provides that PSCs can be concluded, none has been concluded since 1996. There are significant hurdles to overcome for any oil or gas deposit to be eligible for consideration for development under a PSC. However, in certain exceptional cases, such as an obligation to enter into a PSC emanating from Russia's international conventions, a PSC might be concluded.

Unconventional oil and gas

A zero MET rate is available for oil extracted from hydrocarbon deposits within the Bazhenov, Abalak, Khadum and Domanik productive formations (see Section E). No special terms apply for unconventional gas.

C. Special tax and customs regime for shelf projects

From 2014, a new tax and customs regime for shelf projects applies. The regime applies to offshore hydrocarbon deposits (OHDs) lying wholly within the boundaries of Russia's territorial waters, its continental shelf and/or the Russian sector of the Caspian Sea. New offshore hydrocarbon deposits (NOHDs) are OHDs for which the date of commencement of commercial extraction of hydrocarbons falls on or after 1 January 2016, excluding OHDs lying 50% and more within the south part of the Sea of Okhotsk (south of 55 degrees north latitude). The commencement of commercial extraction at a deposit is deemed to be the date of the state balance sheet of reserves that first shows that the level of depletion of reserves of one or more types of hydrocarbons (except associated gas) extracted has exceeded 1%.

MET on extraction from NOHDs

The tax base for MET is the value of extracted commercial minerals subject to a calculated minimum.

NOHDs are divided into four categories, each with special ad valorem MET rates established as follows:

a. Category one: deposits that lie wholly in the Sea of Azov or at least 50% within the Baltic Sea — the MET rate is 30% for 60 months (5 years) after production begins.
b. Category two: deposits lying at least 50% within the Black Sea (up to 100m deep), in the Pechora, White or Japan Seas, in the Russian sector of the Caspian Sea, in the southern part of the Sea of Okhotsk (south of 55 degrees north latitude) — the MET rate is 15% for 84 months (7 years) after production begins.
c. Category three: deposits lying at least 50% within the deeper waters of the Black Sea, the northern part of the Sea of Okhotsk (at or north of 55 degrees north latitude) or the southern part of the Barents Sea (south of 72 degrees north latitude) — the MET rate is 10% with respect to hydrocarbons other than natural fuel gas for 120 months (10 years) after production begins. The MET rate is 1.3% in case of extraction of natural fuel gas from deposits in this category subject to the same time limits.
d. Category four: deposits lying at least 50% within the Kara Sea, the northern part of the Barents Sea (at or north of 72 degrees north latitude) and the eastern Arctic — the MET rate is 1% for extracted natural fuel gas, 4.5% for other hydrocarbons extracted by companies that do not have the right to export LNG produced from natural fuel gas extracted at NOHD to world markets, and 5% in other cases. These rates apply for 180 months (15 years) after production begins.

The general MET rules as to the tax base and tax rate will apply after the expiration of the abovementioned incentives.

The MET rate for other OHDs

A reduced MET rate (see section E) is applicable for crude oil extracted from subsurface sites that lie to the north of the Arctic Circle wholly or partially within the boundaries of the internal sea waters and the territorial sea and on the Russian continental shelf subject to conditions.

A zero rate also applies to hydrocarbons extracted from a hydrocarbon reservoir within a subsurface site that lies wholly within the boundaries of the internal sea waters or the territorial sea, on the Russian continental shelf or in the Russian sector of the Caspian Sea, provided that at least one of the following conditions is met:

a. The level of depletion of reserves of each type of hydrocarbon (excluding associated gas) extracted from the hydrocarbon reservoir in question as of 1 January 2016 is less than 0.1%
b. Reserves of hydrocarbons extracted from the hydrocarbon reservoir in question as of 1 January 2016 have not been placed on the state balance sheet of reserves of commercial minerals.

This rate applies for no more than 60 calendar months (5 years) commencing from the first day of the month following the month in which any type of hydrocarbon from the relevant hydrocarbon reservoir which is subject to tax is first placed on the state balance sheet of commercial minerals and not beyond the end of the tax period in which the process design for the development of the OHDs was first approved.

Export duty exemptions

Crude oil, natural gas, LNG and gas condensate derived from NOHDs falling into categories one and two established for MET purposes are exempt from export duties until 31 March 2032; those from NOHDs in category three are exempt until 31 March 2042; and those from NOHDs in category four have no time limits.

Crude oil, LNG and gas condensate that are exported from Russia and were obtained as a result of the exploitation of OHDs are exempt from export duties. The exemption will apply if the deposit has 50% or more of its area in the southern part of the Sea of Okhotsk (south of 55 degrees north latitude) until 1 January 2021, provided that the level of depletion of reserves of each type of hydrocarbon (excluding associated gas) extracted at the deposit in question as of 1 January 2015 is less than 5%.

Profits taxation of license holders

The profits tax rate is established as 20%. It cannot be reduced by regional governments, and all profits tax is payable to the federal budget.

Ring-fencing rules apply to shelf projects. Income and expenses are to be recorded separately for each shelf project. If the right to use subsurface resources at a subsurface site is terminated, the license holder will have the right to treat the entire amount of expenses qualifying as expenses incurred for the development of natural resources under Article 261 of the Tax Code or any part thereof as expenses of hydrocarbon extraction activities at an NOHD which are carried out at another subsurface site (other subsurface sites) subject to no more than one-third being treated as relating to any one such other NOHD. The taxpayers that perform geological studies (exploration and appraisal of NOHD) could deduct these expenses for the profits tax purposes with application of 1.5 coefficient.

Losses made on one NOHD development project can be carry forward at 50% of the tax base for the current tax period (for 2017–2020) within an unlimited time period but cannot reduce the profits tax base for other activities.

Fixed assets of license holders and operators used in carrying out activities qualified as hydrocarbon extraction activities at an NOHD can be depreciated at up to three times the usual rates.

Taxation of operators

The operator of an NOHD must simultaneously satisfy the following conditions:

a. A direct or indirect interest must be held by an organization that possesses a license to use the subsurface site within whose boundaries the prospecting for and appraisal of and/or the exploration and/or exploitation of an NOHD are intended to be carried out or by an affiliate recognized as interdependent for tax purposes.
b. It carries out at least one of the types of hydrocarbon extraction activities specified in Clause 1(7) of Article 11.1 of the Tax Code, independently and/or through the use of contractors.
c. It carries out these activities on the basis of an (operator) agreement concluded with the license holder and that agreement provides for the payment to the operator of a fee in an amount that depends on, among other things, the volume of hydrocarbons extracted at the relevant OHD and/or receipts from sales of those hydrocarbons.

There can be only one operator in relation to an NOHD at a time. The tax base for each NOHD must be calculated separately.

Transport tax and assets tax exemptions

The transport tax exemption is for offshore fixed and floating platforms, offshore mobile drilling rigs and drilling vessels. The exemption is not limited to assets used at an NOHD.

The assets tax exemption is for assets that are situated on the Russian continental shelf, in Russia's internal sea waters and territorial sea and/or in the Russian sector of the Caspian Sea, and that are used in activities associated with the development of OHDs, including geological study, exploration and the performance of preparatory work. Where an asset was not within the specified areas throughout a tax period, it must satisfy the requirements above for not less than 90 calendar days in the course of one calendar year.

Transfer pricing

The transfer pricing rules do not apply to transactions between a license holder and an operator of an NOHD (subsoil area — until the first NOHD has been designated at the site) related to activities at the relevant NOHD.

D. Capital allowances

Depreciation

For tax purposes, depreciating assets include assets that have a limited useful life and that decline in value over time. Licenses are not depreciated as fixed assets; expenses incurred in obtaining a license from the state are amortized over the term of the license or over two years, at the election of the taxpayer. Depreciable assets are assets with a service life of more than 12 months and a historical cost of more than RUB100,000.

Depreciable assets are allocated to depreciation groups (there are 10 groups) in accordance with their useful lives, which are determined partly by statute and partly by the taxpayer. Asset groups that are relevant to the petroleum industry in Russia, and their standard depreciation periods, are set out in the table below.

Item	Type of depreciating asset	Depreciation period
1	Oil field, exploratory drilling and extraction equipment	1–5 years
2	Gas wells for production drilling	3–5 years
3	Oil and gas exploratory wells	5–7 years
4	Development oil wells, power equipment	7–10 years
5	Gas distribution network	10–15 years

A taxpayer is entitled to choose either the straight-line or reducing-balance method of depreciation, taking account of special considerations established in the Tax Code. It should be noted that only the straight-line method of charging depreciation may be used in relation to buildings, installations and transmission facilities that are included in depreciation groups 8 to 10.

Special allowances

Ten percent (and not more than 30% for fixed assets included in depreciation groups 3 to 7) of the cost of newly acquired fixed assets or expenses incurred in connection with the extension, modernization or partial dismantling of fixed assets may be expensed immediately.

Accelerated depreciation (up to three times) is available for fixed assets that are the object of a lease agreement and included in depreciation groups 4 to 10. There is also a provision for accelerated depreciation (up to twice the usual rates) for fixed assets acquired before 1 January 2014 and employed under the conditions of an aggressive environment, such as locations in the far north, above the Arctic Circle. Fixed assets of license holders and operators used in carrying out activities qualified as hydrocarbon extraction activities at an NOHD can be depreciated at up to three times the usual rates.

There is no capital uplift or credit in Russia. Exploration costs are generally written off over 12 months.

E. Incentives

Crude oil

A zero MET rate applies to superviscous oil with a viscosity under formation conditions of 10,000 mPa × s and higher.

A zero MET rate applies for a period of 15 years to oil extracted from a specific hydrocarbon reservoir within the Bazhenov, Abalak, Khadum and Domanik productive formations, subject to conditions. For oil extracted from hydrocarbon reserves that have been included in the state balance sheet of mineral reserves approved as of 1 January 2012, the depletion of reserves as of 1 January 2012 should be less than 13%. The start date to determine the 15-year period, during which the zero MET could apply, varies as follows:

Depletion of reserves	The start date for the 15 year application period
The level of depletion of reserves as of 1 January 2012 is greater than 1% inclusively, but less than 3%	From 1 January 2014
The level of depletion of reserves as of 1 January 2012 is greater than 3% inclusively	From 1 January 2015
The level of depletion of reserves (other than mentioned previously) first exceeds 1%	From 1 January of the year, in which the depletion of reserves first exceeded 1%

A zero reducing coefficient C_{can} in the MET formula is applicable to crude oil extracted for the designated areas below:

Location of the eligible deposits	Issuance of the license or its type (i) exploration and extraction (ii) geological study and extraction	The reduced coefficient ceases to apply upon the earliest of the below:		
		Level of depletion of reserves, not more than	Cumulative extraction level, not more than (in million tonnes)	Date or number of years after the license has been issued, or its type (i) for exploration and extraction (ii) for geological study and extraction
Wholly or partially within the borders of the Republic of Sakha (Yakutia), Irkutsk Region and Krasnoyarsk Territory	Before 1 January 2007	5% as of 1 January 2007	25	31 December 2016
	(i) Before 31 December 2011 (ii) Before 31 December 2006	5% as of 1 January 2015	25	31 December 2021
	For other licenses	n/a	25	(i) 10 years (ii) 15 years
Wholly or partially northern of the Arctic Circle, wholly or partially within internal sea waters and territorial waters and on the continental shelf of Russia	Before 1 January 2009	5% as of 1 January 2009	35	31 December 2018
	(i) Before 31 December 2011 (ii) Before 31 December 2006	5% as of 1 January 2015	35	31 December 2021
	For other licenses	n/a	35	(i) 10 years (ii) 15 years
Wholly or partially in the Sea of Azov	Before 1 January 2009	5% as of 1 January 2009	10	31 December 2015
	For other licenses	n/a	10	(i) 7 years (ii) 12 years

Location of the eligible deposits	Issuance of the license or its type (i) exploration and extraction (ii) geological study and extraction	The reduced coefficient ceases to apply upon the earliest of the below:		
		Level of depletion of reserves, not more than	Cumulative extraction level, not more than (in million tonnes)	Date or number of years after the license has been issued, or its type (i) for exploration and extraction (ii) for geological study and extraction
Wholly or partially in the Caspian Sea	Before 1 January 2009	5% as of 1 January 2009 (excluding the accumulated volume of oil extraction from NOHDs)	15 (excluding the accumulated volume of oil extraction from NOHDs)	31 December 2021
	For other licenses	n/a	15 (excluding the accumulated volume of oil extraction from NOHDs)	(i) 7 years (ii) 12 years
Wholly or partially in the Nenets Autonomous District and on the Yamal Peninsula in the Yamalo-Nenets Autonomous District	Before 1 January 2009	5% as of 1 January 2009	15	31 December 2015
	(i) Before 31 December 2014 (ii) Before 31 December 2009	5% as of 1 January 2015	15	31 December 2021
	For other licenses	n/a	15	(i) 7 years (ii) 12 years
Wholly or partially in the Black Sea	Before 1 January 2012	5% as of 1 January 2012	20	31 December 2021
	For other licenses	n/a	20	(i) 10 years (ii) 15 years
Wholly or partially in the Sea of Okhotsk	Before 1 January 2012	5% as of 1 January 2012	30	31 December 2021
	For other licenses	n/a	30	(i) 10 years (ii) 15 years
Wholly or partially of 65 degrees north latitude within the Yamalo-Nenets Autonomous District (except for the Yamal Peninsula within the Yamalo-Nenets Autonomous District)	Before 1 January 2012	5% as of 1 January 2012	25	31 December 2021
	For other licenses	n/a	25	(i) 10 years (ii) 15 years

Gas and gas condensate

MET is not payable on gas condensate extracted from deposits located partly or fully on the Yamal and/or Gydan Peninsula in the Yamalo-Nenets Autonomous District up to the accumulated volume of extracted gas condensate up to 20 million tonnes, but not for more than 12 years from the start of production. MET is not payable on natural gas extracted from deposits located partly or fully on the Yamal and/or Gydan Peninsula in the Yamalo-Nenets Autonomous District up to the accumulated volume of extracted natural gas up to 250 billion cubic meters, but not for more than 12 years from the start of production.

MET is not payable on natural gas and gas condensate extracted from deposits located wholly or partially within the boundaries of the Republic of Sakha (Yakutia) and/or Irkutsk Region, and the date of commercial production of natural gas falls within the period commencing from 1 January 2018. MET is not payable for 15 calendar years after the start of commercial production of natural gas (defined as the date of the state balance sheet of mineral reserves, according to which the level of depletion of reserves of natural fuel gas of a particular subsurface site first exceeded 1%). From the 16th calendar year and until the 24th, a special formula applies. Starting from the 25th, the general MET formula applies.[4]

The coefficient reflecting expenses for the transportation of natural fuel gas (Tg) is equal to 0 with respect to subsurface sites that are resource bases exclusively for regional gas supply systems.

MET deduction for Bashkortostan

Special MET deductions are provided for companies operating in Bashkortostan. To be eligible, oil companies developing subsurface sites in designated areas must satisfy certain criteria concerning the relevant mineral license, period of development and initial extractable oil reserves.

MET deduction = BR × K_p, where:

BR = the base rate, which equals RUB193.5m for Bashkortostan and is applicable until 31 December 2018.

K_p = adjustment linked to the export duty for crude oil:

K_p = 1, if the export duty rate for crude oil for the relevant tax period does not exceed the result of the following formula:

\$4 per barrel + 60% × (actual price – \$20 per barrel)

K_p = 0, if the export duty rate for crude oil for the relevant tax period exceeds the result of that formula.

MET deduction for Ugra

Special MET deductions are provided for companies operating in the Khanty-Mansiisk Autonomous District — Ugra. To be eligible, oil companies developing subsurface sites in designated areas must satisfy certain criteria concerning the relevant mineral license and initial extractable oil reserves. This deduction could be applied if the following criteria are met:

- A license for the right to use subsoil was issued before 1 January 2016
- Initial recoverable oil reserves amount to 450 million tonnes or more as of 1 January 2016.

MET deduction for Republic of Crimea

Companies registered in the Republic of Crimea or the city of federal significance of Sevastopol before 1 January 2017 may reduce the total amount of MET until 31 December 2020. The reduction is applicable to the extracted natural gas from subsurface sites located wholly or partially in the Black Sea, on the amount of tax deduction if certain conditions are met simultaneously:

- The subsurface site containing the hydrocarbon reservoir does not serve a regional gas supply system
- The deposit of the subsoil area does not belong to a NOHD

4 *Applicable for Gazprom — affiliated companies only.*

MET deduction for gas condensate

Taxpayers are entitled to reduce the total amount of MET during the extraction of gas condensate by the amount of tax deduction in connection with the production of natural gas liquids upon the processing of gas condensate (defined under the special formula) if certain conditions are met.

LNG

Export duty is not applicable to exports of LNG.

Export duty

Special reduced export duty rates for crude oil are available for the following:

a. Crude oil with a viscosity under formation conditions of not less than 10,000 mPa × s. Export duty for such crude oil should not exceed 10% of the general rate of export duty for crude oil. The reduced rate is not limited by time period if one of the following requirements is met:
   - The accumulated volume of oil extraction as of 1 January 2015 should not be more than 1,000 tonnes, and the level of reserve depletion of hydrocarbon reservoir as of 1 January 2015 in accordance with data in the state balance sheet of mineral reserves is less than 0.01.
   - Oil reserves were placed on the state balance sheet of mineral reserves after 1 January 2015.

b. Crude oil that has particular physical and chemical characteristics and is extracted from deposits located at subsurface sites lying wholly or partially:
   - In the Republic of Yakutia (Sakha), the Irkutsk Region and Krasnoyarsk Territory, the Nenets Autonomous District and north of 65 degrees north latitude wholly or partially within the boundaries of the Yamalo-Nenets Autonomous District
   - Within the Russian area (the Russian sector) of the bed of the Caspian Sea
   - Within the boundaries of the seabed of Russian internal sea waters
   - Within the boundaries of the bed of the Russian territorial sea
   - Within the boundaries of the Russian continental shelf

c. Crude oil that is extracted from deposits where at least 75% of the initial recoverable oil reserves of the deposit is within the Tyumen suite.

Companies should obtain preapproval in order to apply the reduced export duty rate for each individual field. The decision on the application of a special export duty formula is to be made on the basis of the correctness of data in the submitted documents, the level of depletion of reserves (which should not exceed 5%), and the internal rate of return (which should not exceed 16.3%). Companies applying the reduced export duty rate are subject to government monitoring of a project's economics. Once a hurdle rate of return is reached by a project subject to the reduced export duty rate, a company should apply the general rate for crude oil. These requirements apply to crude oil with particular physical and chemical characteristics and crude oil of the Tyumen suite.

The special export duty rate is calculated monthly as indicated in the following table:

Crude oil	Special duty rate per barrel (US$)
Oil listed in point a.	10% × ($4 + 55% × (actual price – $25))
Oil listed in points b. and c.	30%× (actual price – $25) – 7.7 – actual price × 0.14

F. Withholding taxes

The rate for withholding tax (WHT) on dividends paid to foreign organizations is 15%. The rate can be lower if a double tax treaty applies that contains a lower rate, but only to a minimum of 5%. The rate of WHT on interest, royalties and leases of movable property is 20%. The lowest rate possible if a double tax treaty applies is 0%.

Technical services

Technical services provided by nonresident contractors are not subject to tax if the services do not give rise to a PE.

Branch remittance tax

There is no branch remittance tax in Russia.

G. Financing considerations

Thin capitalization

Russia limits debt deductions under thin capitalization rules. Thin capitalization measures apply to the following types of debt:

a. A debt obligation to a foreign interrelated entity that has a direct or indirect participating interest (more than 25%) in the borrower company
b. A debt obligation to an entity that is interrelated with the abovementioned foreign entity
c. A debt obligation in relation to which the abovementioned foreign entity and/or an interrelated entity thereof act as a surety or guarantor or otherwise undertake to guarantee the fulfillment of the borrower's debt obligation

The measures provide for a safe harbor debt-to-equity ratio of 3:1. Interest deductions are denied for interest payments exceeding the figure calculated if the safe harbor ratio is exceeded. Furthermore, if the company's debt-to-equity ratio exceeds the safe harbor ratio, excess interest payments are deemed to be dividends and are taxed at the rate applicable to dividends payable to the foreign shareholder.

Several types of transactions are excluded from controlled debt.

The debt or equity classification of financial instruments for tax purposes is unclear. The Tax Code does not contain detailed rules on the classification of such instruments; generally, the tax authorities give more weight to the form than the substance of an agreement in their analysis. Significant analysis is necessary for instruments with a variable interest rate to determine whether the interest is deductible.

Specific exceptions apply to bank loans for 2018. Additional temporary rules apply for 2018 because of a significant devaluation of the ruble.

H. Transactions

Asset disposals

It is not possible to sell licenses or oil and gas extraction permits. It is, though, possible to sell an enterprise as a property complex, together with all its assets and liabilities (but not licenses) as a whole. For the seller, such a transaction is subject to value-added tax at a rate of 18% applicable to the sales price and to profits tax at a rate of 20% on the difference between the sale price and the net book value of the assets of the enterprise being sold.

There are no capital gains exemptions for sellers of enterprises. The state is not obliged to reissue a license to extract oil and gas to the new owner of the enterprise.

Farm-in and farmout

Russian law does not recognize farm-ins and farmouts because the license issued by the state cannot be traded, and parts of that license cannot be an object of any business transaction.

A quasi farm-in may be executed via a sale of shares of the licensee to an interested party.

Selling shares in a company (consequences for resident and nonresident shareholders)

Nonresidents that dispose of shares in a Russian company are subject to tax in Russia only if more than 50% of the assets of the company being sold consist, directly or indirectly, of immovable property in Russia.

Resident corporations that dispose of shares in a Russian company are subject to profits tax at a rate of 20% on the difference between the sale price and the acquisition costs of those shares. There are no exemptions from this tax for corporations.

Controlled foreign companies

From 1 January 2015 controlled foreign company (CFC) rules have been introduced in Russia. CFCs are companies that are tax-resident in foreign jurisdictions and that are controlled by Russian tax-resident individuals and companies. The definition of CFCs also covers structures that are not legal entities and that are controlled by Russian tax residents. The CFC rules include certain particular provisions for the oil and gas industry; for example, the profits of the following CFCs are not subject to Russian profits tax:

- A foreign company involved in projects under production sharing, concession and similar agreements, provided that these companies' profits from such projects exceed 90% of total income.
- A foreign company that is an operator of an NOHD or is a direct shareholder of an operator of an NOHD.

I. Indirect taxes

Value-added tax (VAT)

VAT is applied at a standard rate of 18%. The rate is 0% for exported oil, oil products, gas and gas condensate. There is no separate VAT registration; all companies are VAT taxpayers. All sales of hydrocarbons within Russia are subject to VAT at a rate of 18%. Acquisitions and sales of shares and other financial instruments are not subject to VAT.

All commercial transactions have a VAT impact, and this must be considered prior to entering into any negotiation or arrangement. Common transactions or arrangements that have VAT implications include:

a. The importation of equipment
b. The supply of technical and other services in Russia or to Russian customers
c. The secondment of personnel
d. The sale or lease of equipment in Russia
e. Asset disposals

A VAT withholding regime applies, and this regime is different from the reverse-charge regime. If services performed by nonresidents are subject to VAT under this regime, 18/118 of the payments must be withheld. It is not possible for nonresidents to obtain a VAT refund by obtaining a Russian VAT number.

Input VAT incurred at the development stage may generally be offset immediately, but the tax authorities often claim that it may be offset only when production starts. It is usually necessary to litigate with the tax authorities to obtain a refund before production starts. Nonetheless, a procedure for claiming an accelerated refund of VAT may be used by certain qualifying taxpayers and other taxpayers presenting a bank guarantee. Generally, there are significant obstacles to obtaining an input VAT refund in respect of exports. The administration of the tax is ineffective; as a result, litigation has often been the only effective mechanism for obtaining refunds.

Equipment for which no equivalent is produced in Russia, which is included in a special list drawn up by the Government, is exempt from VAT on importation.

Import duties

Many goods, equipment and materials that enter Russia from abroad are subject to import duties. The rates vary from 0% to 25%, but a 0% to 20% rate is typical. An exemption may be obtained for goods imported as an equity contribution, and payment by installments is available for items imported under the temporary import regime.

Export duties

Please refer to Section B for a discussion of export duties on hydrocarbons.

Excise duties

Excise duty applies to some goods manufactured in Russia, or imported into Russia, including petroleum products, alcohol and tobacco. Excise duty rates for petroleum products are revised frequently. Tax rates applicable to gasoline for 2018 range from RUB11,213 to RUB13,100 per tonne.

Stamp duties

Stamp duty is levied by notaries and is generally capped at insignificant amounts.

Registration fees

There are no significant registration fees.

Other significant taxes

Other significant taxes include contributions to social funds (a type of social security tax paid by employers). The aggregate rate for 2018 is 30%. An annual cap for contributions to the pension fund is RUB1,021,000. An annual cap for contributions to the social insurance fund is RUB815,000. There is no annual cap for contributions to the medical insurance fund. Payments exceeding the annual cap for the pension fund are taxed at a rate of 15.1%. Payments exceeding the annual cap for the social fund are taxed at a rate of 27.1%. No such contributions arise on payments to foreigners designated as highly-qualified foreign specialists for immigration purposes.

Employers should also pay compulsory insurance against accidents at the workplace and occupational illnesses. Those contributions are payable for all employees, including foreigners designated as highly-qualified foreign specialists. The rates vary from 0.2% to 8.5% depending on the level of occupational risk (there are 32 classes of risk for this purpose). The rate is typically 0.2% for office workers. Employees engaged in fieldwork (e.g., rig workers) fall into the 30th class of professional risk, and their remuneration is subject to a 7.4% rate.

Property tax applies to the net book value of fixed assets of Russian companies at a rate of 2.2% (subject to regional reductions and exemptions). Property tax is calculated on the basis of the cadastral value of assets for certain categories of immovable property at reduced rates. For foreign companies with property in Russia, their immovable property is subject to this tax, as well as other fixed assets unless exempt under a treaty. Fixed assets included in the first or second depreciation groups are not subject to property tax. All movable property put into use after 1 January 2013 is exempt from property tax, except for property obtained as the result of a reorganization or liquidation of legal entities, and obtained from related parties.

Starting 1 January 2018, the provision of the following property tax exemptions is delegated to the regional authorities:

- Tax exemption established for fixed assets that are classified as highly energy-efficient facilities
- Tax exemption established for assets that are situated in the Russian part of the bed of the Caspian Sea
- Tax exemption established for movable property (belonging to the third and following depreciation groups with useful life of more than three years) which was entered in accounting records on or after 1 January 2013. If this exemption is not established by the regional authorities, the applicable tax rate for 2018 is set at 1.1%.

J. Other

Investment in strategic deposits

The Government has powers to deny the granting of licenses for oil and gas deposits of a strategic nature to companies with foreign investment. Foreign equity investments granting 25% or more of their voting rights require prior approval.

Applicable domestic production requirements

Under the law on exports of natural gas, only Gazprom and its 100%-owned subsidiaries may export gas in a gaseous state out of Russia. The list of companies that have the right to export LNG is limited to:

- Gazprom and its 100%-owned subsidiaries
- Subsurface users engaged in the development of a deposit of federal importance (currently defined as a deposit with natural gas reserves of 50 billion cubic feet and more) if the license for such a deposit as of 1 January 2013 provides for the construction of an LNG plant, or provides that the natural gas extracted is sent for liquefaction to an LNG plant
- Russian legal entities that are more than 50% owned and/or controlled by the Russian state, engaged in the development of deposits located in Russian internal waters, territorial seas, the continental shelf, the Black and Azov seas, and that produce LNG from natural gas produced on such deposits, or produced under production sharing contacts
- Subsidiaries, more than 50% of whose capital is owned by such Russian legal entities, that produce LNG from natural gas produced on the said deposits

Foreign-exchange controls

The currency control mechanisms that existed during the 1990s were abolished in 2005. They may be reinstated if the balance of payments deteriorates.

Transactions that may be suspicious in terms of potential money laundering are routinely reported by banks to the state's financial intelligence body.

Gas to liquids

There is no special regime for gas-to-liquids conversion.

Gas flaring

Companies are permitted to flare 5% of any associated gas they produce. Producers violating this limit are charged significant emission fees, which are not tax-deductible.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Saudi Arabia's fiscal regime that applies to the petroleum and natural gas industries consists of corporate income tax (CIT) in accordance with a petroleum concession agreement (PCA). The main elements comprise:

- Royalties — PCA royalties are stipulated in the particular PCA
- CIT rate:
  - General — 20%
  - Oil production — 50% to 85%
  - Natural gas investment activities — 30% to 85%
- Capital allowances — specific depreciation rates apply for specific asset classes

B. Fiscal regime

Saudi Arabian tax law applies to companies engaged in oil and other hydrocarbons production irrespective of their Saudi or non-Saudi ownership.

Corporate income tax

Oil and other hydrocarbon activities

Companies engaged in oil and other hydrocarbons production are subject to CIT at the rate of 50% to 85% on their tax base, determined on the basis of their total capital investment (effective from 1 January 2017). Tax base is calculated as total revenue subject to tax less allowable deductions and is determined in accordance with the Saudi Arabian income tax law (effective from 30 July 2004).

Deductions include expenses to the extent that they are incurred in producing assessable income or are necessarily incurred in carrying on a business for the purpose of producing income that is subject to tax. However, expenditure of a capital nature and some other expenses specifically defined in the law are not deductible.

Natural gas investment activities

Natural gas investment tax (NGIT) applies to companies (irrespective of their Saudi or non-Saudi ownership) engaged in natural gas, natural gas liquids and gas condensates investment activities in Saudi Arabia. NGIT does not apply to a company engaged in the production of oil and other hydrocarbons.

The NGIT rate ranges from 30% to 85% and is determined on the basis of the internal rate of return on cumulative annual cash flows. The NGIT rate includes CIT of 30%.

Natural gas investment activities income is the gross income derived from the sale, exchange or transfer of natural gas, natural gas liquids, gas condensates and other products, including sulfur, as well as any other nonoperational or incidental income derived within the taxpayer's primary activity, regardless of its type or source, including income derived from the utilization of available excess capacity in any facility that is subject to NGIT.

The NGIT base is the gross revenues described above less the expenses deductible under the general tax law. The amount of royalties and surface rentals shall be considered as deductible expenses.

Taxpayers subject to NGIT must ring-fence their natural gas-related activities for each gas exploration and production contract or agreement with the Government, and file separate tax returns and audited accounts for the activities under each gas exploration and production contract or agreement. A taxpayer must file a separate tax return and audited accounts for its other activities that are not related to its natural gas investment activity.

Other activities

Activities other than oil and gas are taxed at 20% CIT.

Saudi resident companies are subject to CIT on their profits attributable to their shareholders who are engaged in the production of oil and hydrocarbons.

Capital gains

In general, capital gains are treated as ordinary income and taxed at the regular corporate rates. Capital gains realized by nonresident shareholders on the disposal of shares in a Saudi Arabian company are subject to tax at a rate of 20%.

However, capital gains arising on the sale by non-Saudi shareholders of shares in a Saudi joint stock company traded on the Saudi stock exchange are exempt from tax if the shares (investments) were acquired after the effective date of the new tax regulations (30 July 2004).

Gains (or losses) on the transfer of an asset between group companies that are fully owned, directly or indirectly, by a capital company are not taxable (or deductible) if the asset is not disposed of to a company outside of the group prior to the lapse of two years from the date of transfer.

Government royalties via a PCA

Royalty rates are stipulated in each particular PCA. Royalty payments in respect of production are deductible for tax purposes in calculating the tax base of a company engaged in oil or other hydrocarbon production activities.

Transfer pricing

Saudi Arabian tax law includes measures to ensure that the Kingdom's taxable income base associated with cross-border transactions is based on an arm's-length price.

Broadly, the tax authority has discretionary powers to:

- Disregard or reclassify transactions whose form does not reflect its substance
- Allocate income or deductions between related parties or persons under common control as necessary to reflect the income that would have resulted from a transaction between independent persons

There are no formal transfer pricing guidelines or directives with regard to pricing methodologies in Saudi Arabia, although the Ministry of Finance issued a resolution in March 2014 that Saudi Arabia shall adopt formal transfer pricing guidelines, which will be consistent with international standards. However, the tax authority often reviews transactions between related parties in considerable depth.

Losses

Losses may be carried forward indefinitely. However, the maximum loss that can be offset against a year's profit is 25% of the tax-adjusted profits for that year. Saudi tax regulations do not provide for the carryback of losses.

If a change of 50% or more occurs in the underlying ownership or control of a capital company, no deduction is allowed for the losses incurred before the change unless the company continues to practice the same activities.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Depreciation deductions are calculated for each class of fixed assets by applying the prescribed depreciation rate to the remaining value of each group at the fiscal year-end. The remaining value for each asset class is calculated as the closing tax balance for the asset class at the end of the preceding year less depreciation claimed in the preceding year, and 50% of the proceeds received from asset disposals in the current and preceding years plus 50% of the cost of assets added during the current year and the preceding years.

Expenses for geological surveying, drilling, exploration and other preliminary work to exploit and develop natural resources and their fields are subject to a 20% depreciation rate. This includes expenditure assets acquired by the taxpayer in connection with the acquisition of rights to geological surveying and the processing or exploitation of natural resources.

Assets developed in respect of build-operate-transfer (BOT) or build-own-operate-transfer (BOOT) contracts may be depreciated over the period of the contract or the remaining period of the contract, if acquired or renewed during that period.

D. Withholding taxes

The following payments made to nonresident companies are subject to a final withholding tax (WHT) at the following rates:

Type of payment	Rate of WHT
Royalties and payments made to head office or an affiliate for services including technical and consultancy services and international telecommunication services	15%
Rent, payments for technical and consulting services to non-affiliated entities, dividends or remittance of PE profits, interest, insurance or reinsurance premiums	5%
Management fees	20%

Note: Dividends paid by companies engaged in natural gas investment, oil and hydrocarbons are not subject to withholding tax.

E. Tax treaties

Tax treaties are currently in force between Saudi Arabia and Algeria, Austria, Azerbaijan, Bangladesh, Belarus, China, Czech Republic, Egypt, Ethiopia, France, Greece, Hungary, India, Ireland, Italy, Japan, Jordan, Kazakhstan, Kyrgyzstan, Luxembourg, Macedonia, Malaysia, Malta, the Netherlands, Pakistan, Poland, Portugal, Romania, Russia, Singapore, South Africa, South Korea, Spain, Sweden, Syria, Tajikistan, Tunisia, Turkey, Turkmenistan, the

United Kingdom, Ukraine, Uzbekistan, Venezuela and Vietnam. The treaty with Mexico is in force but will be effective beginning 2019. Treaty with Morocco is ratified but not in force. Treaties with the following jurisdictions are signed but not ratified: Bulgaria, Cyprus, Gabon, Hong Kong, Switzerland and the United Arab Emirates. Treaties with the following jurisdictions are initialed but not signed: Belgium, Bosnia and Herzegovina, Croatia, Georgia, Latvia, Sri Lanka and Sudan. Treaties with the following jurisdictions are currently under negotiation: Gambia, Lebanon, Mauritania, Mauritius and Seychelles. Note: Saudi-UAE treaty is now signed but not yet ratified; please see above.

In a circular, the Saudi Arabian tax authorities (GAZT) have provided that a Saudi Arabian resident party making payment to a nonresident party (beneficiary) may apply the provisions of the effective tax treaty, provided that the resident party complies with the following:

- It reports all payments made to nonresident parties (including those payments that are either not subject to WHT or subject to WHT at a lower rate as per the provisions of effective tax treaties) in the monthly WHT returns (on a prescribed format — Form Q7A)
- It submits a formal request for application of effective tax treaties' provisions, including a tax residency certificate issued from the tax authorities in the country where the beneficiary is residing confirming that the beneficiary is resident in that country in accordance with the provisions of Article 4 of the treaty, and the amount paid is subject to tax in that country (on a prescribed format — Form Q7B)
- It submits an undertaking that it would bear and pay any tax or fine due on nonresident party due to incorrectness of submitted information or a computation error or misinterpretation of the provisions of tax treaty (on a prescribed format — Form Q7C)

If the resident party is unable to submit the above requirements, it has to follow the procedure under the old GAZT circular of withholding and settling WHT in accordance with the provisions and rates specified in the Saudi Arabian income tax regulations and then later applying for a refund of overpaid WHT after submission of certain documents (e.g., Form Q7B, Request/Form for Refund, Authority Letter).

After review of the submitted documents and verification that treaty provisions are applicable on the nonresident party, the GAZT will refund the overpaid amount to the Saudi Arabian entity.

F. Indirect taxes

Customs duty

The Government of the Kingdom of Saudi Arabia, as a member of the Gulf Cooperation Council (GCC), follows the Unified Customs Act across the GCC; the uniform customs duty of 5% to 20% applies on most imports. This means that any goods that come into a port of entry of a GCC member state that has been subject to customs duty in that state are not subject to customs duty again if the goods are transferred to another GCC member state.

VAT

As at 1 January 2018, the GAZT has introduced the value-added tax (VAT) regime within Saudi Arabia. The standard VAT rate of 5% will be applicable on domestic supplies of goods and services and imports into Saudi Arabia with minimal exemptions. As with most VAT jurisdictions internationally, exports are subject to zero-rated VAT (0%).

While the GCC VAT Framework Agreement, which is the overarching framework governing the VAT Law in Saudi Arabia, has allowed the GCC Member States to apply the zero-rated VAT treatment across the oil and gas sector, the GAZT has taken the approach of subjecting the sector to the regular VAT rules with few concessions. In other words, supplies relating to oil and gas related activities (both upstream and downstream) and imports are subject to 5% VAT.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies in Senegal to the upstream oil and gas industry consists of the Senegalese tax law, the Senegalese petroleum code and the amendments to the aforementioned by virtue of a relevant production sharing contract (PSC) or contract of service concluded between the Senegalese Government and the contractor (hereafter, the holder).

The new Senegalese tax law came into force on 1 January 2013 and was amended in 2015 by Law No. 2015-06 of 23 March 2015. The new tax law provides greater certainty with respect to the maintenance of benefits received by oil and gas companies. Transitional measures apply and comprise the following:

- Tax incentives benefiting oil and gas companies subject to the petroleum code will remain applicable if they were granted before the new tax law came into force. The former regime will continue to apply during the entirety of the taxpayer's exemption title.
- At the expiration of the exemption period, the common regulations of the new tax law will become applicable, replacing the specific regime granted to the holder in the applicable PSC.

Also, under conditions, companies that have farmed in (after 2013) to a PSC concluded before the entry into force of the abovementioned law of 2013 could benefit from grandfathering clauses of the applicable PSC.

The petroleum code is currently under review of the Senegalese authorities.

The main elements of the fiscal regime for the oil and gas sector in Senegal are the following:

- Corporate tax — 30%
- Annual land royalties *(redevance superficiaire)*
- Royalty on production
- Additional petroleum tax
- Royalties — between 2% and 10%[1]
- Bonuses — none

1 *This royalty applies to the holder of a PSC.*

- PSC[2]
- Resource rent tax — an annual surface rent is levied
- Capital allowances – E[3] and O[4]
- Investment incentives – L[5] and RD[6]

B. Fiscal regime

Corporate tax

A 30% corporate tax applies to the net profit of oil and gas companies. "Net profit" is defined as the difference between the value of the opening and closing balances of the net assets in the relevant year of assessment, less extra contributions, plus any amounts taken by associated companies during the period.

The profit is established after deduction of all charges that:

- Are incurred in the direct interest of the company or related to the normal management of the company and to generate taxable profits in Senegal
- Correspond to actual charges and are supported by sufficient evidence
- Are reflected by a decrease in the net assets of the company
- Contribute to the generation of a nontax-exempt income
- Are Included in the fiscal year during which they are incurred

Holders of petroleum exploitation titles are exempted from minimum tax for three years from the date of granting the exploitation titles. "Minimum tax" is a tax commonly due when companies are in a tax loss position.

Ring fencing

The Senegalese Petroleum Code does not provide that the profit from one project can be offset against the losses from another project held by the same tax entity. Accordingly, the petroleum operations should be accounted for separately.

Production sharing contracts

A PSC is concluded between the holder and the Senegalese Government and is signed by the minister in charge of petroleum activities after the approval of the Minister of Finance.

The PSC is approved by decree of the President of the Republic of Senegal, published in the official journal and registered in accordance with the conditions provided by the law.

Government share of profit oil

The production volumes remaining after the deduction of oil costs are shared between the State and the holder according to the value of a ratio "R," defined as follows:

Value of R	Government share	Holder share
Less than 1	Percentage of ratio R depending on the applicable PSC	Percentage of ratio R depending on the applicable PSC
From 1 to less than 2	Percentage of ratio R depending on each applicable PSC	Percentage of ratio R depending on the applicable PSC

2 *The government share depends on the terms of the PSC or the service contract; it should be equal to a percentage of the production after covering the oil cost of the holder.*

3 *E: immediate write-off for exploration costs.*

4 *O: rules regarding currency exchange.*

5 *L: losses can be carried forward until the third fiscal year following the deficit period.*

6 *RD: R&D incentive — the Senegalese tax law provides tax exemptions for the holders of PSCs or service contracts during the period of exploration and development.*

Value of R	Government share	Holder share
From 2 to less than 3	Percentage of ratio R depending on the applicable PSC	Percentage of ratio R depending on the applicable PSC
From 3 or more	Percentage of ratio R depending on the applicable PSC	Percentage of ratio R depending on the applicable PSC

R is the ratio of the net accumulated revenue divided by the accumulated investments, which are determined in accordance with the accumulated amounts from the effective date until the end of the civil year. "Net accumulated revenue" is the total amount of the benefit after assessment of corporation tax. "Accumulated investments" make up the total amount of the expenditure for research, evaluation and development.

Non-recoverable expenditures

The following expenditures are not recoverable:

- Expenditures relating to the period before the effective date of the PSC
- All expenses relating to operations carried out beyond the point of delivery, such as marketing and transport charges
- Financial expenses relating to financing research, evaluation and operations, as well as those relating to financing of development and transport for production purposes

Determination of cost oil

Cost oil is the sum of all expenses borne by the holder in the framework of the PSC, determined in accordance with accepted accounting methods.

Uplift available on recovered costs

The holder can add a reasonable amount representing general expenses incurred abroad that are necessary for the performance of the petroleum operations and that are borne by the holder and its affiliated companies, determined according to the annual amount of petroleum costs (excluding financial charges and general expenses).

This additional amount may be determined as follows:

- For up to US$3 million per year — 3%
- More than US$3 million up to US$6 million per year — 2%
- More than US$6 million up to US$10 million per year — 1%
- More than US$10 million per year — 0.5%

Annual land royalty

An annual land royalty is due when the PSC or service contract is signed. Based on an example of a PSC, the annual land royalty is determined as follows:

- During the initial exploration period — US$5 per square kilometer per year
- During the first renewal period — US$8 per square kilometer per year
- During the second renewal period and during any extension provided in the PSC — US$15 per square kilometer per year

These amounts are paid for the entire year, based on the area of the permit.

Additional petroleum tax

Holders are subject to an additional petroleum tax, calculated according to the profitability of the petroleum operations. The rate, conditions of calculation, declaration, liquidation and recovery are specified in the PSC or service contract.

If the remuneration of the holder of a PSC has already been determined according to the profitability of its petroleum operations, this method of determination of the additional petroleum tax applies instead of the additional petroleum tax calculated in terms of the PSC.

The payment of the additional petroleum tax due for a given calendar year is required to be made, at the latest, within three months following the end of the relevant calendar year.

The additional petroleum tax is not a deductible charge for the determination of profits subject to the corporate tax.

Royalty regimes

Holders are subject to the payment of a royalty on the value of the hydrocarbons produced. The royalty must be paid in cash to the State. The royalty is calculated based on the total quantity of hydrocarbons produced in the concession and not used in the petroleum operations.

The royalty rates applicable to the production of crude oil or natural gas are determined as follows:

- Liquid hydrocarbons exploited onshore — 2% to 10%
- Liquid hydrocarbons exploited offshore — 2% to 8%
- Gaseous hydrocarbons exploited onshore or offshore — 2% to 6%

The amount of royalty and the rules relating to the basis and recovery of the costs are specified in the PSC.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Tax depreciation rules

The tax depreciation rules for the oil and gas sector are provided for in the PSC. The fixed assets realized by the holder that are necessary for its petroleum operations are depreciated using the straight-line method of depreciation. The minimum period of depreciation is 5 calendar years, or 10 calendar years for fixed assets relating to the transportation of the produced oil or gas. Depreciation commences with the calendar year when the fixed assets are realized, or with the calendar year when the fixed assets are put into normal operation.

The Senegalese Petroleum Code does not provide for any accelerated depreciation for the assets of an oil and gas company.

Immediate write-off for exploration costs

Hydrocarbon exploration expenses incurred by the holder in the territory of Senegal, including the cost of geological and geophysical surveys and the cost of exploration wells (but excluding the costs of producing exploration wells that may be capitalized), are considered to be fully deductible charges effective in the year they are incurred, or they may be depreciated in accordance with a depreciation method determined by the holder.

D. Incentives

The tax exemptions and incentives available to oil and gas companies were granted by Article 48 of the Petroleum Code. Given that this article has been repealed by Law No. 2012-32 dated 31 December 2012, the General Tax Code remains the main legal reference with respect to tax incentives available during R&D phases.

Carryforward losses

The unverified amount of a deficit is deductible from taxable profits until the third fiscal year following the deficit period, unless otherwise provided for in the PSC or service contract. A PSC or service contract may allow losses to be carried forward beyond the three-year period.

R&D incentives

During the R&D period, holders of petroleum research titles are exempted from the following taxes (during the period of validity of the title and its successive renewals):

- Direct tax (corporate tax)
- Tax on sales or similar tax (value-added tax or VAT)
- Employment tax (CFCE)
- Tax on developed lands except for properties for home usage
- Tax on undeveloped lands
- Business license tax

Article 48 of the Petroleum Code provided exemption from withholding tax (WHT) on interest (IRC WHT) and taxes and duties that apply to petroleum products supplied to permanent facilities and drilling facilities. However, the new Senegalese tax law has not repeated the abovementioned tax exemptions.

Any person or company that works on behalf of holders may be exempt from tax on sales or similar tax, in respect of the petroleum operations performed. However, in practice, this tax exemption may be subject to an endorsement by the Ministry of Energy and/or Ministry of Finance.

During this period, equipment intended directly and exclusively for petroleum operations is exempted from any duties and taxes on importation in the Republic of Senegal by holders or by companies working on their behalf.

E. Withholding taxes

Dividends

Dividends paid by a Senegalese company to a nonresident are subject to a WHT at the rate of 10%.

Interest

Interest paid by a Senegalese resident to a nonresident is subject to WHT at the rate of 16%. However, an 8% WHT rate should apply to interest paid by banks on some banking products.

Royalties

A WHT on profits for "non-commercial activity" must be paid by foreign companies or individuals that provide services to a resident company if such services are rendered or used in Senegal and if the nonresident service provider has no permanent professional installation in Senegal. The rate of WHT is 20% of the gross amount, unless a lower rate is provided by a tax treaty.

This tax must be paid by the local company within 15 days following the month of the payment of remuneration to the nonresident service provider.

Branch remittance tax

Profits made in Senegal by a branch of a foreign company that are not reinvested in Senegal are deemed to be distributed and are subject to a 10% WHT.

However, it should be noted that under double tax treaties concluded between Senegal and other countries, WHT may be reduced to a lower rate under certain conditions.

F. Financing considerations

Thin capitalization limits

Thin capitalization is the limitation on the deductibility of interest payments if the prescribed debt-to-equity ratio is exceeded.

The rate of interest in respect of funds placed at the disposal of a company, in addition to authorized capital, by one or more shareholders is limited to three points above the discount rate of the central bank.

There is no limitation on the deductibility of interest that a Senegalese company may pay to a third party.

G. Transactions

Asset disposals

The PSC or service contract may be terminated if all the assets are transferred.

Income realized through the transfer of certain classes of assets of the holder is credited to the account of oil costs to be recovered.

Capital gains are taxed at the corporate tax rate of 30%. The payment of the tax can be deferred in accordance with the conditions provided in the tax law.

The registration fees to be paid by the assignee depend on the kind of asset, for example:

- Shares — 1%
- Transferable bonds — 1%
- Debts — 1%

It should be noted that an adjustment should be made to the amount of VAT deducted at the time of purchase of the asset if the asset is not entirely depreciated.

H. Indirect taxes

Import duties and VAT

In general, a 22.9% customs duty applies, as well as VAT at a rate of 18%. The 22.9% rate is the maximum that can be applied on imported goods and includes the Economic Community of West African States (ECOWAS) duties (2.5%) and the levy of the Senegalese Chargers' Council (COSEC) (0.4%).

Export duty

No export duty applies. However, the goods exported or re-exported by sea are subject to the COSEC levy, collected at the rate of 0.20% of the free-on-board value.

Stamp duties

Stamp duties may apply to the registration of different contracts concluded by an oil and gas company. The amount is XOF 2,000 for each page of the agreement.

Registration fees

Registration fees depend on the type of agreement concluded.

Disposal of interests through a farm-in agreement will give rise to a registration tax at the rate of 5%.

I. Other

Exchange controls

The holder is subject to Regulation No. 9/2010 CM/WAEMU relating to foreign financial exchanges between member states of the West African Economic and Monetary Union (WAEMU).

However, in general, the PSC may provide the holder with certain rights for operations carried out within the framework of the PSC, in particular:

- The right to obtain offshore loans required for performance of the holder's activities in Senegal
- The right to collect and maintain offshore all funds acquired or borrowed abroad, including the receipts from sales, and the right to dispose freely of these funds, limited to the amounts that exceed the requirements of the holder's operations in Senegal

- Free movement of funds owned by the holder between Senegal and any other country, free of any duties, taxes and commissions of any kind, the right to repatriate the capital invested under the PSC and to transfer proceeds — in particular, interests and dividends
- The free transfer of amounts due and the free receipt of amounts receivable for any reason whatsoever, provided that the declarations required by the regulations in force are filed

These rights are granted in the PSC, and in general, the Central Bank of West African States and the Minister of Finance may not alter or reject these rights, but may request further authorizations for some specific foreign-exchange transfers or transactions.

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Tax regime applied to this country

■ **Concession** ☐ Royalties ☐ Profit-based special taxes ■ Corporate income tax	☐ **Production sharing contracts** ☐ **Service contract**

A. At a glance

Fiscal regime

Singapore has a corporate income tax (CIT) regime that is applicable across all industries. There is no separate fiscal regime for companies in the energy industry. The main elements of the regime are:

- CIT — headline rate 17%.
- Capital allowances — see Section C
- Incentives — see Section D.

Withholding tax (WHT) is applied to interest, royalties, rent and services, unless specifically exempted. Generally, the WHT rates are 10% to 17%, although tax treaties may allow for a reduced rate or an exemption. There is no WHT on dividend distributions.

B. Fiscal regime

Scope of taxation

Income tax is imposed on all income derived from sources in Singapore, together with income from sources outside Singapore if received in Singapore. A nonresident company that is not operating in or from Singapore is generally not taxed on foreign-source income received in Singapore.

A company is considered "resident" in Singapore if the control and management of its business is exercised in Singapore; the place of incorporation is not relevant.

Remittances of foreign-source income in the form of dividends, branch profits and services income into Singapore by a tax-resident company will be exempt from tax if certain prescribed conditions are met.

Rate of tax

The standard CIT rate is 17%. Seventy-five percent of the first SGD10,000 of normal chargeable income (NCI) is exempt from tax, and 50% of the next SGD290,000 of NCI is exempt from tax. The balance of NCI is fully taxable at the standard rate of 17%. This is known as the partial tax exemption (PTE) scheme, and, as proposed in the 2018 budget, it will be adjusted to provide for 75% exemption on the first SGD10,000 of NCI and 50% exemption on the next SGD190,000 (currently SGD290,000) of NCI. This change will take effect on or after year of assessment (YA) 2020 for all companies (except those that qualify for the startup tax exemption (SUTE) scheme below) and bodies of persons.

A 20% CIT rebate is granted for the year of assessment (YA) 2018 and capped at SGD10,000. However, as proposed in the 2018 budget, the CIT rebate for YA 2018 is increased from 20% to 40% of tax payable, and the cap is increased from SGD10,000 to SGD15,000; the CIT rebate will also be extended for another year to YA 2019 with a reduced rate of 20% of tax payable, capped at SGD10,000.Subject to certain conditions, a newly incorporated and tax-resident Singapore company may qualify for a full tax exemption on the first SGD100,000 of NCI and 50% of the next SGD200,000 of NCI (SUTE scheme). As proposed in the 2018 budget, the SUTE scheme will be adjusted to provide for 75% (currently 100%) exemption on the first SGD100,000 of NCI and 50% exemption on the next SGD100,000 (currently SGD 200,000) of NCI. This change will take effect on or after YA 2020 for all qualifying companies. The exemption applies only to the qualifying company's first three consecutive YAs. However, the scheme does not apply to new startups undertaking property development or investment holding.

Computation of taxable income

In general, book profits reported in the financial statements prepared under generally accepted accounting principles are adjusted in accordance with the Singapore tax rules to arrive at the taxable income.

Functional currency

If a company maintains its financial accounts in a functional currency other than Singapore dollars, as required under the financial reporting standards in Singapore, the company must furnish tax computations to the Inland Revenue Authority of Singapore (IRAS) denominated in that functional currency in the manner prescribed by law.

Deductions

For expenses to be deductible, they must be incurred "wholly and exclusively" in the production of income, and they must be revenue expenses in nature and not specifically disallowed under Singapore tax legislation.

Expenses attributable to foreign-source income are not deductible unless the foreign-source income is received in Singapore and is subject to tax in Singapore. Offshore losses may not be offset against Singapore-source income.

No deduction is allowed for the book depreciation of fixed assets, but tax depreciation (capital allowances) is granted according to statutory rates (see Section C below). However, a deduction for qualifying renovation or refurbishment expenditure is available subject to meeting specified conditions.

Double deductions are available for certain expenses relating to approved trade fairs, exhibitions or trade missions, maintenance of overseas trade offices, overseas investment development, research and development (R&D) projects, and approved salary expenditure for employees posted overseas (a sunset clause of 31 March 2020 applies to the double deduction schemes).

Relief for trading losses

Trading losses may be offset against all other chargeable income of the same year. Unutilized losses may be carried forward indefinitely, subject to the shareholding test (which requires that the shareholders remain substantially (50% or more) the same as at the relevant comparison dates).

Excess capital allowances can also be offset against other chargeable income of the same year, and any unutilized amounts may be carried forward indefinitely, subject to the shareholding test and to the requirement that the trade giving rise to the capital allowances continues to be carried on (the "same trade" test).

A one-year carryback of up to an aggregate amount of SGD100,000 of the current year's unutilized capital allowances and trade losses may be allowed, subject to meeting certain conditions and compliance with specified administrative procedures. The carryforward and carryback of losses and capital allowances is subject to the abovementioned shareholding test. If a shareholder of the loss-making company is itself a company, look-through provisions apply through the corporate chain to the final beneficial shareholder.

The carryback of capital allowances is subject to the same-trade test that applies to the carryforward of unutilized capital allowances (see above).

The IRAS has the authority to allow companies to deduct their unutilized tax losses and capital allowances, notwithstanding a substantial change in ownership at the relevant dates, if the change is not motivated by tax considerations. If allowed, these losses and capital allowances may only be offset against profits from the same business.

Groups of companies

Under group relief measures, current-year unutilized losses, capital allowances and donations may be transferred by one company to another within the same group, subject to meeting certain specified conditions. A group generally consists of a Singapore-incorporated parent company and all of its Singapore incorporated subsidiaries. Two Singapore incorporated companies are members of the same group if one is 75% owned by the other or both are 75% owned by a third Singapore incorporated company.

Transfer pricing

There is specific legislation governing the arm's-length principle to be applied to related-party transactions. The IRAS may make adjustments to the amount of income, deduction or loss of a taxpayer in cases where the terms of commercial or financial relations between two related parties are not at arm's length. A 5% surcharge will be imposed on transfer pricing (TP) adjustments made for noncompliance with the arm's-length principle with effect from YA 2019. Taxpayers with related-party transactions are expected to maintain contemporaneous TP documentation, except in certain limited situations. With effect from YA 2019, it is mandatory for Singapore taxpayers to prepare contemporaneous TP documentation, if certain conditions are satisfied, to support their transactions with related parties unless specifically exempted.

On 3 November 2016, the IRAS announced the introduction of a new requirement for companies to complete a form for reporting of related-party transactions (RPT) with effect from YA 2018, which must be completed and submitted together with the income tax return if the value of the RPT as disclosed in the audited accounts exceeds SGD15 million for the relevant YA.

Dividends

Dividends paid by a Singapore tax-resident company are exempt from income tax in the hands of shareholders, regardless of whether the dividends are paid out of taxed income or tax-free gains.

Anti-avoidance legislation

The IRAS may disregard or vary any arrangement that has the purpose or effect of altering the incidence of taxation or of reducing or avoiding a Singapore tax liability. The IRAS may also tax profits of a nonresident in the name of a resident as if the resident were an agent of the nonresident, if the profits of the resident arising from business dealings with the nonresident are viewed as less than expected as a result of the close connection between the two parties.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

Plant and machinery

Tax depreciation or capital allowances are given for capital expenditures incurred on the acquisition of plant and machinery used for the purposes of a trade or business. The qualifying plant and machinery are normally written off in equal amounts over three years when claimed. Alternatively, expenditures on such assets may be claimed in one year if each item costs no more than SGD5,000. However, the total claim for all such assets may not exceed SGD30,000 for a YA.

The cost of the following may be written off in the year of acquisition: computers or other prescribed automation equipment, generators, robots, certain efficient pollution control equipment, certain industrial noise and chemical hazards control equipment.

Businesses that incur expenditure on acquiring qualifying IT and automation equipment may qualify for the productivity and innovation credit (PIC) scheme — see Section D.

Only expenditure on certain automobiles such as commercial vehicles and cars registered outside Singapore and used exclusively outside Singapore will qualify for capital allowances.

Capital expenditures on fixtures, fittings and installations integral or attached to a building are usually considered to be part of the building and do not qualify as plant and machinery. Unless a land intensification allowance (LIA, see below) applies, this type of expenditure does not qualify for capital allowances.

Land intensification allowance incentive

The LIA incentive grants an initial allowance of 25% and an annual allowance of 5% on qualifying capital expenditure incurred on or after 23 February 2010 by businesses on construction or renovation of a qualifying building or structure, upon meeting certain conditions. The application window period for the LIA incentive is from 1 July 2010 to 30 June 2020.

Intellectual property

Writing-down allowances (WDAs) are granted for capital expenditures incurred on the acquisition of specified categories of intellectual property (IP) on or before the last day of the basis period for YA 2020, but only if the legal and economic ownership of the IP lies with Singapore companies. Companies may make an election to claim WDAs over a 5-, 10- or 15-year period. Once made, the election is irrevocable. The legal ownership requirement may be waived (upon application) if the Singapore company has substantial economic rights over the IP while the foreign parent holds the legal title.

Businesses that incur qualifying expenditure on the acquisition or in-licensing of IP rights may also qualify for the PIC scheme (see Section D).

Disposal of assets qualifying for capital allowances

Allowances are generally subject to recapture on the sale of a qualifying plant and machinery if the sales proceeds exceed the tax-depreciated value (to the extent of the excess but not more than the allowances claimed). If sales proceeds are less than the tax-depreciated value, an additional allowance is given.

D. Incentives

The following tax incentives, exemptions and tax reductions are available in Singapore.

Pioneer companies and pioneer service companies

The incentive is aimed at encouraging companies to undertake activities that have the effect of promoting the economic or technological development in Singapore. A pioneer enterprise is exempt from income tax on its qualifying profits for a period of up to 15 years. A sunset clause has been introduced such that no approval would be given for the incentive on or after 1 January 2024.

Development and expansion incentive

This incentive is available to companies that engage in high value-added operations in Singapore but do not qualify for pioneer status or to companies with expired pioneer status. Development and expansion incentive (DEI) companies enjoy a concessionary tax rate of 5% or 10% on their incremental income derived from the performance of qualifying activities.

Typically, the initial relief period is 5 years, and the company may subsequently apply for an extension in tranches of 5 years, up to a maximum relief period of 40 years. A sunset clause has been introduced such that no approval would be given for the incentive on or after 1 January 2024.

Approved royalties, technical assistance fees and contributions to R&D costs

Approved royalties, technical assistance fees and contributions to R&D costs paid to nonresidents may be awarded an exemption from WHT or a reduced WHT rate. A sunset clause has been introduced such that no approval would be given for the incentive on or after 1 January 2024.

Investment allowances

On approval, investment allowances are available to companies that engage in qualifying projects. These allowances are granted in addition to the normal tax depreciation allowances and are based on a specified percentage (up to 100%) of expenditures incurred on productive equipment. Different sunset clauses (up to 31 December 2023, depending on type of project) have been introduced such that no approval would be given for the incentive on or after the specified date.

Global trader program

The global trader program (GTP) is aimed at encouraging international companies to establish and manage regional or global trading activities with Singapore as their base. Under the GTP, approved companies enjoy a concessionary tax rate of 5% or 10% on qualifying transactions conducted in prescribed commodities and products (including energy, agricultural, building, industrial, electrical and consumer products, and carbon credits), qualifying transactions in derivative instruments and qualifying structured commodity financing activities. Income derived from qualifying transactions in liquefied natural gas, as specified by the relevant authority, are taxed at a concessionary rate of 5%.

A sunset clause of 31 March 2021 applies to the GTP scheme.

Finance and treasury center incentive

The finance and treasury center (FTC) incentive is aimed at encouraging companies to use Singapore as a base for conducting treasury management activities for related companies in the region. Income from the provision of qualifying services to approved network companies and from the carrying on of qualifying activities on their own account is subject to tax at a rate of 8%. "Approved network companies" are offices and associated companies of the company granted the FTC incentive that have been approved by the relevant authority for purposes of the incentive.

A sunset clause of 31 March 2021 applies to the FTC scheme.

International Headquarters program

The International Headquarters program applies to entities incorporated or registered in Singapore that provide substantive headquarters activities in Singapore to their network companies on a regional or global basis. Under the program, the pioneer incentive or DEI may be awarded to companies that commit to anchor substantive headquarters activities in Singapore to manage, coordinate and control regional business operations; companies may enjoy tax exemption or concessionary tax rates of 5%/10% for a specified period on qualifying income, depending upon the level of commitment to Singapore.

This commitment is demonstrated by various factors, including level of headcount, total business expenditure and quality of personnel hired.

R&D incentives

Liberalized R&D deductions are available from YA 2009 to YA 2025. A tax deduction can be claimed for undertaking R&D carried out in Singapore in any business area — there is no longer a requirement for the R&D to be related to the trade or business carried on by the company — and an additional 50% (increased to 150% effective from YA 2019 to YA 2025 as proposed in the 2018 budget) tax deduction is allowed for certain qualifying R&D expenditure. If the companies outsource their R&D activities to an R&D organization in

Singapore, the tax deduction available is at least 130% (increased to 190% from YA 2019 to YA 2025 as a consequence of the 2018 budget proposal above) of the amount of R&D expenses incurred.

Businesses that incur qualifying R&D expenditure may also qualify under the PIC scheme (see below).

IP Development Incentive

The 2017 budget proposed a new IP regime named IP Development Incentive (IDI). This incentive incorporates the base erosion and profit shifting (BEPS)-compliant modified nexus approach. The date of introduction of the IDI has however been delayed from 1 July 2017 to 1 July 2018.

Productivity and innovation credit (PIC)

Businesses that incur qualifying expenditure in the following six activities will qualify for an enhanced deduction or allowance for YA 2011 to YA 2018:

- R&D
- Eligible design activities
- Acquisition and in-licensing of IP rights
- Registering patents, trademarks, designs and plant varieties
- Acquiring and leasing of PIC IT and automation equipment, including expenditure on cloud computing services
- External training and qualifying in-house training

All businesses can claim a deduction or allowance of 400% of the first SGD400,000 of their expenditures per YA on each of the above activities from their taxable income, subject to a combined cap of SGD1.2 million of eligible expenditure for each activity for YA 2016 to YA 2018.

A PIC+ scheme is also available to support businesses that are making more substantial investments to transform their businesses. Under the scheme, which is effective for expenditure incurred in YA 2015 to YA 2018, the expenditure cap will be increased from SGD400,000 to SGD600,000 per qualifying activity per YA, and the expenditure caps may also be combined. To qualify, the entity's annual turnover must not exceed SGD100 million, or its employment size must not be more than 200 workers. The criterion will be applied at the group level if the entity is part of a group.

Qualifying entities with at least three local employees have an option to convert up to SGD100,000 of eligible expenditure for each YA into a nontaxable cash grant. The conversion rate is 40% (60% for qualifying expenditures incurred before 1 August 2016) up until YA 2018.

Tax certainty on gains on disposal of equity investments

To provide up-front tax certainty, gains derived from the disposal of ordinary shares by companies during the period from 1 June 2012 to 31 May 2022 (apart from a few exceptions) will not be taxed if the qualifying divesting company had legally and beneficially owned at least 20% of the ordinary shares in the investee company for a continuous period of at least 24 months prior to the disposal of the shares.

Deduction for acquisitions of shares of companies

A Singapore company may claim a deduction if it and/or any one or more of its acquiring subsidiaries incurs capital expenditure during the period 1 April 2010 to 31 March 2020 (both dates inclusive) in acquiring the ordinary shares in another company, subject to specified conditions. The amount of deduction currently granted is 25% of the capital expenditure, to be written off over five years. For this purpose, the capital expenditure is capped at SGD40 million (different caps apply for qualifying acquisitions made before 1 April 2016) for all qualifying acquisitions that have acquisition dates within one basis period.

A 200% tax deduction will be granted for certain transaction costs incurred on the qualifying acquisition, subject to an expenditure cap of SGD100,000 per relevant YA.

E. Withholding taxes

Interest

In general, WHT at a rate of 15% is imposed on interest and other payments in connection with any loans or indebtedness paid to nonresidents.

However, interest paid by approved banks in Singapore on a deposit held by a nonresident is exempt from tax if the nonresident does not have a permanent establishment (PE) in Singapore and does not carry on business in Singapore by itself or in association with others, or the nonresident person carries on any operation in Singapore through a PE in Singapore but does not use the funds from the operation of a PE in Singapore to make the deposit. In addition, tax exemption applies to interest paid for qualifying debt securities issued during the period to 31 December 2018 (extended to 31 December 2023 as proposed in the 2018 budget) to nonresidents who do not have a PE in Singapore. The exemption also applies to nonresidents who have a PE in Singapore but do not use the funds obtained from the operations of the PE to acquire the debt securities.

With respect to any payment for any arrangement, management or service relating to any loan or indebtedness performed by a nonresident outside Singapore or guarantee in connection with any loan or indebtedness provided by a nonresident guarantor, such payments are exempted from tax. Interest and qualifying payments made by banks, finance companies and certain approved entities to nonresident persons are also exempt from WHT, during the period from 17 February 2012 to 31 March 2021, if the payments are made for the purpose of their trade or business and not with the intent of avoiding any tax in Singapore.

Royalties

A 10% WHT is imposed on payments made to nonresidents with respect to royalties for the use of, or the right to use, intangible property and on payments for the use of, or the right to use, scientific, technical, industrial or commercial knowledge or information.

However, payments made to a nonresident and borne by a person resident in Singapore or a Singapore PE for use of or the right to use software, information or digitized goods, not involving the right to commercially exploit the copyright, will not be subject to WHT.

Rent and hire

A 15% WHT is imposed on rent and other payments to nonresidents for the use of movable property. However, payments made to nonresidents (excluding PEs in Singapore) for the charter hire of ships are exempted from tax.

Services

Payments made to a nonresident professional for services performed in Singapore are subject to a final WHT of 15% on the gross income, unless the nonresident professional elects to be taxed at 22% of net income.

In general, a 17% WHT is imposed on payments made to nonresident companies for assistance or services rendered in connection with the application or use of scientific, technical, industrial or commercial knowledge or information and for management or assistance in the management of any trade, business or profession.

Where services are performed outside Singapore, payments for such services are not subject to withholding tax.

Payers do not need to withhold tax on the above payments that are due to PEs that are Singapore branches of nonresident companies. These branches in Singapore continue to be assessed for income tax on such payments received and must declare such payments in their annual income tax returns.

Tax treaties may override the abovementioned withholding tax rules. However, if the rate under the domestic tax law is lower than the treaty rate, the domestic tax rate applies.

Dividends

Singapore does not levy WHT on dividends (see Section B).

Branch remittance tax

There is no branch remittance tax in Singapore.

F. Financing considerations

Singapore does not impose any specific debt-to-equity restrictions. To secure a deduction for interest and borrowing costs, such costs must be wholly and exclusively incurred on loans that are used to acquire income-producing assets. For borrowing costs, the deduction is further subject to certain specified conditions.

G. Transactions

Capital gains

Capital gains are not taxed in Singapore. However, in certain circumstances, the IRAS might consider transactions involving the acquisition and disposal of assets such as real estate or shares to be trading gains and hence subject to income tax. The determination of whether gains are taxable is based on a consideration of the facts and circumstances of each case.

However, certain gains on the disposal of equity investments are not liable to Singapore tax — see Section D above.

H. Indirect taxes

Goods and services tax

Singapore currently imposes a goods and services tax (GST) at the rate of 7% (the prevailing standard rate) on the following transactions:

- Supplies of goods and services (apart from zero-rated and exempt supplies described below) in Singapore, made in the course or furtherance of a business by a taxable person (i.e., a person who is registered or is required to be registered for GST)
- Imports of goods into Singapore, unless the imports qualify for import reliefs or relate to the importation of certain investment precious metals which is an exempt import for GST purposes

Exports of goods (subject to conditions and documentation requirements) and provision of international services as prescribed under the GST legislation qualify for zero-rating relief (i.e., taxed at 0%). The sale and lease of residential property, the provision of certain prescribed financial services and the sale of qualifying investment precious metals are exempt from GST.

The GST registration threshold is SGD1 million. For compulsory registration, the threshold applies as follows:

- Retrospectively: registration is required if, at the end of any quarter, the value of taxable supplies (i.e., standard-rated supplies and zero-rated supplies) in that quarter and the preceding three quarters exceeds SGD1 million. From 1 January 2019, businesses will only need to monitor the SGD1 million threshold at the end of the calendar-year basis (i.e., 31 December) instead of on a quarterly basis.
- Prospectively: registration is required if at any time reasonable grounds exist for believing that the value of taxable supplies in the next 12 months is expected to exceed SGD1 million.

Businesses that are not liable for GST registration may still apply for GST registration on a voluntary basis (subject to conditions). On the other hand, businesses that are liable for GST registration may apply for exemption from GST registration (subject to conditions).

While a GST-registered business is required to charge GST on its standard-rated supplies of goods and services, it can generally recover the GST incurred on its business expenses as its input tax, subject to satisfying conditions prescribed under the GST legislation. Input tax is generally recovered by deducting it against the output tax payable, which is GST charged on standard-rated supplies made, in the GST returns. If the input tax claimable exceeds the output tax payable, the net GST amount will be refundable to the GST-registered person.

Singapore operates various schemes that aim to ease the administrative burden associated with GST compliance, as well as to improve the cash flow of businesses. Examples of such schemes include:

- Major exporter scheme (MES) — the MES allows for the suspension of GST payable on the importation of non-dutiable goods into Singapore.
- Zero-GST warehouse scheme — similar to the MES scheme, this scheme allows for the suspension of GST payable on the importation of non-dutiable overseas goods into a zero-GST warehouse approved and licensed by Singapore Customs.
- Approved Third-Party Logistics scheme (A3PLC) — this scheme allows for the suspension of GST payable on the importation of non-dutiable goods and allows the removal and supply of imported goods locally without having to charge GST to prescribed persons (e.g., persons who enjoy MES and A3PLC schemes).
- Approved marine fuel trader (MFT) scheme — the approved MFT scheme allows approved MFT businesses to enjoy the suspension of GST on their local purchases of marine fuel oil.
- Licensed warehouse scheme — a "licensed warehouse" is a designated area approved and licensed by Singapore Customs for storing dutiable goods, with the suspension of the customs duty and import GST.
- Import GST Deferment Scheme (IGDS) — the IGDS allows approved IGDS businesses to defer their import GST payments until their monthly GST returns are due.

Import and excise duties

Singapore imposes customs or excise duties on a limited range of goods, including, alcoholic beverages and preparations, tobacco and tobacco products, petroleum (motor spirits and diesel fuel), and specified motor vehicles.

Export duties

There are no duties on goods exported from Singapore.

Stamp duty

Stamp duty is payable on instruments or documents that relate to the transfer of Singapore stocks and shares and immovable property. It is applied on the amount or value of the consideration. The rate of duty varies depending on the type of document.

A flat rate of 0.2% applies to stocks and shares.

For documents relating to immovable property, the following rates (buyer's stamp duty (BSD)) are applied:

- For every dollar of the first SGD180,000 — 1%
- For every dollar of the next SGD180,000 — 2%
- For every dollar exceeding SGD360,000 — 3%

To improve the progressiveness of the stamp duty regime, the top marginal BSD rate on acquisition of residential properties will be increased from 3% to 4%; the following revised BSD rates will apply to all residential properties acquired on or after 20 February 2018:

- For every dollar of the first SGD180,000 — 1%
- For every dollar of the next SGD180,000 — 2%
- For every dollar of the next SGD640,000 — 3%
- For every dollar exceeding SGD1,000,000 — 4%

The BSD rate for nonresidential properties, however, remains the same.

In addition, with effect from 11 March 2017, Additional Conveyance Duties will be payable on qualifying acquisition and disposal of equity interest in property-holding entities whose primary tangible assets (owned directly or indirectly) are Singapore residential properties.

Different rates apply to lease agreements and mortgages.

Sellers of residential and industrial properties may be liable for seller's stamp duty depending on when the property was acquired and the holding period. In addition, buyers of residential properties (and residential land) may be required to pay additional buyer's stamp duty on top of the existing buyer's stamp duty.

I. Other

Base erosion and profit shifting (BEPS)

Common reporting standard

On 16 June 2016, Singapore announced that it will join the inclusive framework for the global implementation of the BEPS Project. As a BEPS Associate, Singapore is committed to implementing the four minimum standards under the BEPS Project, which includes Action 13 on transfer pricing documentation. In implementing Action 13, Singapore will implement country-by-country reporting (CbCR) for Singapore-headquartered multinational enterprises (MNEs). The CbCR rules require Singapore tax-resident MNEs that have consolidated revenue of at least SGD1,125 million and have subsidiaries or operations in at least one foreign jurisdiction to submit a CbCR report to the IRAS. CbCR is effective from the financial year beginning on or after 1 January 2017 (FY 2017). Singapore-headquartered MNEs that are subject to CbCR requirements in foreign jurisdictions for FY 2016 can voluntarily file their CbC reports in Singapore despite the CbCR requirements in Singapore becoming effective for FY 2017.

On 21 June 2017, Singapore signed the Multilateral Competent Authority Agreement on exchange of CbC reports (CbCR MCAA). The signing of the CbCR MCAA will enable Singapore to efficiently establish a wide network of exchange relationships for the automatic exchange of CbC reports. As of 21 December 2017, the IRAS has activated bilateral Automatic Exchange of Information relationships for the exchange of CbC reports with more than 40 jurisdictions.

BEPS multilateral instrument

On 7 June 2017, Singapore signed the Organisation for Economic Co-operation and Development (OECD) BEPS multilateral instrument (MLI), which seeks to facilitate the efficient updating of existing tax treaties to incorporate treaty-related measures recommended by the OECD to counter BEPS, without the need for jurisdictions to bilaterally renegotiate each tax treaty. At the point of signing the MLI, Singapore indicated provisionally that it would like to amend its double tax agreement with 68 countries using the MLI.

Carbon tax

The Singapore Government aims to implement carbon tax on the emission of greenhouse gases from 2019.

It has now been proposed in the 2018 budget that a carbon tax will be applied on facilities that produce 25,000 metric tons or more of carbon dioxide-equivalent (tCO_2e) of emissions in a year. The carbon tax rate will be set at SGD5 per tCO_2e of emissions from 2019 to 2023. The carbon tax rate will be reviewed by 2023, and it is intended that it be increased to between SGD10 and SGD15 per tCO_2e of emissions by 2030. The carbon tax will apply uniformly across all sectors without exemption.

Foreign-exchange controls

Singapore does not impose any restrictions on the remittance or repatriation of funds into or out of Singapore.

Forms of business presence in Singapore

Forms of business presence in Singapore may include companies, foreign branches and partnerships (including limited liability partnerships and limited partnerships). The most suitable form of business entity depends on commercial and tax considerations.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

The fiscal regime that applies to the upstream oil and gas industry in South Africa consists primarily of a combination of corporate income tax (CIT) and royalties. Summary elements are as follows:

- Royalties[1] — 0.5% to 5%
- Bonuses — none
- Production sharing contract (PSC) — none
- CIT — 28%
- Resource rent tax — none
- Capital allowances — D, E[2]
- Investment incentives — L, RD[3]

B. Fiscal regime

The fiscal regime that applies to the upstream oil and gas industry in South Africa consists in essence of a combination of CIT and royalties. The Tenth Schedule to the Income Tax Act specifically deals with the taxation of upstream exploration and production. The Mineral and Petroleum Resources Royalty Act imposes royalties on upstream oil and gas companies.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

1 *A royalty payment is calculated according to the two critical determinants of gross sales and earnings before interest and tax (EBIT). "Gross sales" is the transfer of all mineral resources as defined in Schedule 1 and 2 of the Royalty Act. "EBIT" is defined as earnings before interest and taxes and is the aggregate of gross sales and so much of any amount allowed to be deducted in the Income Tax Act. Various inclusions and exclusions apply to gross sales and EBIT. The royalty is payable semiannually by way of estimated payments on a basis similar to provisional tax for income tax purposes. Royalties are deductible for income tax purposes.*

2 *D: accelerated depreciation; E: immediate write-off for exploration costs.*

3 *L: losses can be carried forward indefinitely; RD: R&D incentive.*

Essential definitions in the Tenth Schedule

An "oil and gas company" means any company for which one of the following is true:

- A company that holds any oil and gas right (meaning any reconnaissance permit, technical cooperation permit, exploration right, production right or any interest therein)[4]

Or

- A company that engages in exploration or post-exploration activities in respect of any oil and gas right

"Exploration" means the acquisition, processing and analysis of geological and geophysical data or the undertaking of activities in verifying the presence or absence of hydrocarbons (up to and including the appraisal phase) conducted for the purpose of determining whether a reservoir is economically feasible to develop.

"Post exploration" means any activity carried out after the completion of the appraisal phase, including:

- The separation of oil and gas condensates
- The drying of gas
- The removal of non-carbon constituents, to the extent that these processes are preliminary to refining

"Oil and gas income" means the receipts, accruals or gains derived by an oil and gas company with respect to exploration or post-exploration activities in terms of any oil and gas right, including leasing or disposing of that right, thereby including commercial royalty income and capital gains.

Determination of taxable income of an oil and gas company

Oil and gas companies are generally taxed at the normal corporate tax rate, subject to the provisions of the Tenth Schedule, which provides for a number of rate caps, allowances and incentives in the determination of oil and gas income. Under the Tenth Schedule, the rate of corporate tax may not exceed 28%.

An oil and gas company may engage in activities other than exploration or post exploration. However, these other activities are separately taxable in terms of the general provisions of the Income Tax Act without regard to the Tenth Schedule.

Foreign currency differences

Currency gains and losses (whether realized or unrealized) for the purposes of the Income Tax Act are determined with reference to the functional currency (i.e., the principal trading currency) of that company and the translation method used by the oil and gas company for the purposes of financial reporting.[5] Accordingly, if a company's functional currency is US dollars but it also transacts in UK pounds or South African rands, gains or losses with respect to the transactions will be accounted for in US dollars for tax purposes.

Once taxable income and tax due have been calculated in the functional currency, the tax figure is then translated to rands at the average exchange rate for the year concerned for purposes of payment to the South African tax authorities (SARS).

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4 *As contemplated in Schedule 1 of the Mineral and Petroleum Resources Development Act of 2002.*

5 *Paragraph 4(1) of the Tenth Schedule.*

C. Incentives

Capital allowances

An oil and gas company may deduct all expenditures and losses actually incurred (whether revenue or capital in nature) with respect to exploration and post-exploration. The only exclusion is in relation to expenditures or losses incurred for the acquisition of an oil and gas right, although certain concessions exist in relation to farm-in and farm-out transactions (see Section F).[6]

A further deduction is permitted over and above the expenditure actually incurred, including:[7]

- 100% of all capital expenditures incurred in respect of exploration activities
- 50% of all capital expenditures incurred in respect of post-exploration activities

As a result, an oil and gas company may recognize a total deduction equal to 200% and 150% of its capital expenditures related to exploration and post-exploration, respectively.

As a general rule, any expenditure or loss (including administrative expenses) that is incurred by an oil and gas company with respect to exploration is regarded as capital in nature, because it has a direct or causal relationship with the exploration activities. Acquisition of an oil and gas right does not qualify for additional allowances.

Carryforward of losses

Losses incurred during the exploration phase may be offset against oil and gas income generated in the post-exploration phase. There is no ring-fencing between oil or gas fields in this regard. Any balance of assessed loss remaining may be carried forward without limit, for so long as the company continues to trade.

Losses in respect of exploration or post-exploration may only be offset against oil and gas income of that company and income from the refining of gas acquired from South African wells. Ten percent of any excess loss may first be offset against any other income (e.g., interest income that does not constitute oil and gas income), and any balance must be carried forward to the succeeding year. Thus, a vertically integrated gas production and refining company may typically offset its exploration and post-exploration costs against new wells, refining income and incidental interest income earned on a current account used for production operations, up to the total thereof. Similarly, refining losses of such a company may, by inference, be fully offset against profits from production (typically, in respect of wells whose production is sold rather than refined).

Fiscal stability

In recognition of the need for oil and gas companies to have certainty as to the tax treatment of future revenues, and in conformity with international practice, the Minister of Finance may enter into a fiscal stabilization contract with an oil and gas company. Such a contract binds the state of South Africa and guarantees the provisions of the Tenth Schedule as of the date that the contract is concluded.[8]

An oil and gas company may unilaterally rescind any such agreement (usually to pursue a more favorable dispensation if the Tenth Schedule is further changed to the taxpayer's benefit.)[9]

6 *Paragraph 5(1) of the Tenth Schedule.*
7 *Paragraph 5(2) of the Tenth Schedule.*
8 *Paragraph 8(1) of the Tenth Schedule.*
9 *Paragraph 8(4) of the Tenth Schedule.*

D. Withholding taxes (WHT)

Dividends

Notwithstanding the provisions of the Income Tax Act, the Tenth Schedule provides that the rate of dividends tax may not exceed 0% of the amount of any dividend that is paid by an oil and gas company out of amounts attributable to its oil and gas income.

Interest

With effect from 1 March 2015, a withholding tax on interest was introduced in South Africa, calculated at the rate of 15% of the amount of any interest that is paid by any person to or for the benefit of any nonresident to the extent that the amount is regarded as having been received or accrued from a South African source.[10]

Notwithstanding the Income Tax Act, the rate of WHT on interest may not exceed 0% on any interest paid by an oil and gas company with respect to loans applied to fund exploration or post exploration expenditure.

Royalties

A 15% withholding tax currently applies to royalties on intellectual property paid to nonresidents.

Technical services

With effect from 1 January 2017, South Africa was to impose a withholding tax on service fee payments made by residents to nonresidents at the rate of 15%.

It was announced in the 2016 National Budget Speech that this withholding tax has been abolished.

Branch remittance tax

No branch remittance applies (and the former higher rate on branches has been eliminated).

Withholding of amounts from payments to nonresident sellers of immovable property

In the case where a nonresident sells an interest in an oil and gas right, it may be subject to a withholding of 7.5% to15% of the amount payable by the purchaser. This is an advance payment of tax and not a final tax, and under certain circumstances may be waived by the Tax Commissioner.

E. Financing considerations

Transfer pricing

The South African tax law includes transfer-pricing provisions (including thin capitalization considerations), which are based on the internationally accepted principles of transfer pricing. These provisions allow the South African tax authorities to treat any term or condition of a cross-border related-party transaction differently, but only to the extent that the term or condition differs from those that would exist between unrelated parties. In addition, exchange control regulations discourage unreasonable pricing by requiring that many foreign contracts, such as license agreements, be approved by the Department of Trade and Industry before payment is allowed.

Cross-border loan funding

Recent amendments to the Income Tax Act included a limitation on interest payments if a controlling relationship[11] exists.[12] Under these rules, an annual

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10 *Part IVB of the Income Tax Act.*

11 *"Controlling relationship" means a relationship between a company and any connected person in relation to that company holding at least 50% of the equity shares or exercisable voting rights.*

12 *Section 23M of the Income Tax Act, which came into effect from 1 January 2015.*

limitation is placed on the amount of interest deductions available, pursuant to a defined formula. Any interest not allowed will be carried forward to the following year and be deemed to be incurred in the following year. There appears to be no limitation on the ability to carry forward the disallowed interest indefinitely.

F. Transactions

Asset disposals

Subject to the specific provisions relating to the disposal of an oil and gas right[13] (see next subsection), the disposal of exploration and post-exploration properties is subject to the general capital gains tax (CGT) rules. A capital gain, in essence, is the amount by which the proceeds realized on the disposal of an asset exceed the base cost of the asset. Eighty percent of a capital gain realized on the disposal of an asset is taxable for years of assessment commencing on or after 1 March 2016. For years of assessment commencing prior to this date, this inclusion rate was set at sixty-six percent. In the case of a resident company, the effective tax rate is 22.4% (28% of 80%) from 1 March 2016, and 18.6% (28% of 66%) for years of assessment commencing prior to this date.

Farm-in and farm-out — rollover relief and CGT

The general CGT rules are subject to the Tenth Schedule in the case of the disposal of an oil and gas right by an oil and gas company.

The Tenth Schedule provides special rules relating to the disposal of oil and gas rights at any stage of the exploration and post-exploration process and refers to "rollover treatment" and "participation treatment," either of which can be elected by the disposing company and the acquiring company together in writing.[14] If no election is made, normal CGT rules will apply.

Rollover treatment

Rollover treatment can apply where the market value of the right disposed of is equal to or exceeds:

- The base cost of that right for CGT purposes
- The amount taken into account by the seller as a deduction in terms of Section 11(a) or 22(1) or (2), in the case of trading stock

The company is deemed to have disposed of the right for an amount equal to the CGT base cost or the trading stock deduction (as the case may be) so that, from the seller's perspective, the transaction is tax-neutral. The purchaser is deemed to have acquired the right at the same base cost or trading stock amount as previously existed in the hands of the purchaser.[15]

Participation treatment

If the company that disposes of an oil and gas right holds it as a capital asset and the market value of the right exceeds its base cost, the difference is deemed to be gross income accruing to the seller. The purchaser is entitled to deduct the same amount in determining its taxable income derived from oil and gas income (notwithstanding the general prohibition on the deduction of the cost of acquisition of oil and gas rights).[16] The provision effectively allows losses to be shifted to the purchaser (at the price of gross income for the seller).

The Tenth Schedule makes no provision in respect of other components of a farm-in or farm-out transaction, such as the disposal of physical assets and cost-

13 *In terms of the Tenth Schedule.*

14 *Paragraph 7(1) of the Tenth Schedule.*

15 *Paragraph 7(2)(i) and (ii) of the Tenth Schedule.*

16 *Paragraph 7(3)(a) of the Tenth Schedule. It appears that the actual proceeds or expenditures incurred in respect of the disposal are irrelevant in determining the tax consequences in a participation election. Subparagraph (3)(a) apparently applies in a situation where the purchasing entity is not an oil and gas company as defined, but it is probable that relaxation is unintentional.*

sharing arrangements. Unless the agreement is disguised as a consideration for the oil and gas right, it is felt that the consideration constitutes:

- A recoupment of expenditures formerly incurred by the seller
- An expenditure incurred by the purchaser in respect of exploration

The question of whether an oil and gas company holds an oil and gas right as a capital or trading asset must always depend upon the facts of, and intention behind, that company's investment. As a general rule, however, it is probable that, in terms of South African taxation principles, most oil and gas companies acquire their rights as capital assets, notwithstanding that they frequently anticipate using the disposal of undivided shares of those rights to limit financial and commercial risk.

Selling shares in a company

The CGT implications of the disposal of shares depend on the nature of the company and the tax residency of the shareholders. South African tax residents are subject to CGT on any capital gain realized on the disposal of shares held as capital assets. The tax liability is calculated on the basis outlined in "Asset disposals" above.[17]

Shareholders that are not tax-resident in South Africa are only subject to CGT on any capital gain realized on the disposal of shares if 80% or more of the market value of the shares is attributable directly or indirectly to immovable property situated in South Africa. Oil and gas rights are considered to be immovable property for this purpose. Hence, the sale of oil and gas company shares could often trigger CGT when sold by a nonresident seller.

G. Indirect taxes

Import and export duties

Special rebates exist for oil and gas rigs and related equipment used in exploration and post-exploration activities. These rebates require regulatory permits.

VAT

The normal value-added tax (VAT) rules apply to oil and gas companies. Briefly, VAT liability enables rand-based expenditures to qualify for VAT credit as input VAT.

Sales of crude oil are zero-rated (i.e., no VAT charge applies). Gas does not qualify for zero-rating.

Other transaction taxes

The normal rules in respect of securities transfer tax apply to oil and gas companies. Subject to certain group reorganization relief rules, the transfer of beneficial ownership of certain marketable securities (e.g., shares and rights to dividends in South African companies) is subject to securities transfer tax at 0.25% of the transaction or market value.

H. Other

Local participation requirements may apply for grants of oil and gas rights in South Africa. Typically, a grant is subject to state participation through the national oil company (PetroSA).

17 *Assuming they are companies and not natural persons.*

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South Sudan became an independent state in 2011 and is currently undergoing legislative formulation. As a result, the tax laws, regulations and other legislation in South Sudan are still evolving. Readers should obtain updated information and seek professional advice before engaging in any transactions.

Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal system applied in South Sudan revolves around production sharing contracts (PSCs). The Petroleum Act 2012 introduced general petroleum regulations, including the composition of fiscal provisions. Supplementary legislation, including a model PSC, have not been developed.

Under the Petroleum Act 2012, an investor is subject to production sharing (approach and instruments not yet specified), surface rental fees, cost-based fees for particular services, bonuses or royalties, as agreed in each PSC. An investor is also subject to general corporate taxes and customs duties payable by all industries (subject to the PSC provisions). The Petroleum Act also envisages other indirect fiscal instruments and other charges, such as those for training, the financing of the community infrastructure, etc.

The basic elements of the fiscal regime constitute the following:

- Production sharing contract — apply
- Rentals — apply
- Bonuses — apply
- Royalties — apply
- Corporate income tax (CIT) — rate is 10%, 20% or 25% depending on size of company's turnover
- Ring-fencing rules — do not apply currently but could be introduced in future

B. Fiscal regime

Corporate income tax

The CIT rate depends on the magnitude of a taxpayer's business, whether it is small (annual turnover of up to 1 million South Sudanese pounds (SSP1 million)), medium (annual turnover of up to SSP30 million) or large (annual turnover of more than SSP30 million). Small, medium and large businesses are subject to tax at rates of 10%, 20% and 25%, respectively.

These rates apply to income from most economic activities, including oil and gas activities. Taxable income consists of worldwide income for resident companies (for nonresident companies, only the profits sourced in South Sudan), less permitted deductions.

The rates of withholding tax on South Sudan Government contracts paid to either residents or nonresidents and payments of technical fees exceeding SSP10,000 to nonresidents are 20% and 10%, respectively.

Exploration costs are deductible over the useful life of the asset, based on actual costs incurred, units extracted and estimated total extractable units.

Losses can be carried forward for five years, but carryback is not available. A loss from oil and gas operations can be offset against any profits available during the successive five-year period.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas in South Sudan.

C. Incentives

The Investment Promotion Act provides for various tax incentives, including capital allowances ranging from 20% to 100% of eligible expenditure, deductible annual allowances ranging from 20% to 40% and depreciation allowances ranging from 8% to 10%. Tax incentives and duty exemptions are requested through an application to the Ministry of Finance and Economic Planning. However, these provisions in the Investment Promotion Act are irrelevant since they have not been anchored in the Taxation Act.

A foreign tax credit is granted to any resident company paying foreign taxes on income from business activities outside South Sudan.

D. Other

Social security

Employers are subject to social security contributions. The rates are not established by law, but the rate is typically 17% of employees' salaries.

VAT

VAT is not applicable, but the country employs a sales tax system. Sales tax regime applies on the importation of goods, the production of goods and the supply of specified services. The standard sales tax rate is 18%.

Domestic supply obligations

The Petroleum Act envisages domestic supply obligations. Both market price and special terms are envisaged for the pricing of gas supplied.

Community Development Plan and Fund

An investor is obliged to establish a fund to finance community development activities in a contract area. The activities mainly comprise construction of infrastructure, such as schools, roads, hospitals, etc.

Training

The law obliges investors to organize industry training for nationals, including postgraduate training and scholarships.

Gas flaring

Gas flaring or venting is prohibited, unless specifically authorized or in the event of an emergency. Investors are therefore obliged to invest in necessary facilities in order to utilize any gas they produce.

Transfer pricing

Transfer pricing legislation applies on cross-border transactions between related parties. The comparable uncontrolled price method is preferred; where this is not possible, the resale price method or the cost plus method can be used.

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies in Spain to the oil and gas industry consists of a combination of the general corporate income tax (CIT) regime with some special rules and surface tax.

Special CIT rules

Entities engaged in the exploration, investigation and exploitation of hydrocarbons are subject to the following special CIT rules:

- Advantageous depreciation regime for intangible assets
- Higher tax rate applicable for the income derived from the exploration and exploitation of hydrocarbons

Furthermore, the following tax rules apply for entities whose sole business purpose consists of the exploration, investigation and exploitation of hydrocarbons and hydrocarbon sub-storage:

- Reduction of the taxable base, based on the depletion factor reserve
- Specific regime for offsetting tax losses

B. Fiscal regime

Corporate income tax

CIT is imposed on the taxable income of companies and other entities and organizations that have a separate legal status. Spain-resident entities are taxable on their worldwide income, including the profits from their foreign branches. Nonresident entities are taxable only for Spanish-sourced income, which includes income from any kind of business activity conducted in Spain through a branch, office or other permanent establishment (PE).

As a general rule, the tax base is calculated by adjusting certain provisions established in the CIT Law, from the accounting profit or loss determined in accordance with Spanish generally accepted accounting principles (GAAP).

For residents and nonresidents that conduct business activities in Spain through a PE, the general corporate income tax rate is 25% (30% until 31 December 2014 and 28% until 31 December 2015). Newly incorporated entities that carry out business activities (unless they belong to a group of entities) are taxed at a 15% tax rate in the first tax period in which the taxable base is positive and in the following tax year. However, for entities engaged in the exploration, investigation and exploitation of hydrocarbons and hydrocarbon sub-storage owned by third parties, the applicable tax rate is 30% (35% until 31 December 2014 and 33% until 31 December 2015).

Functional currency

The euro is generally used as the functional currency for accounting purposes. However, oil and gas companies are permitted to use US dollars as the functional currency.

Nevertheless, the annual accounts of a company and also the CIT return must be expressed in euros. If the functional currency of a Spanish company is a currency other than the euro, the financial statements are required to be converted into euros. Differences arising from the conversion of the foreign functional currency into euros are recorded in a special equity account called the conversion differences account.

Determination of taxable income

"Taxable income" is the company's gross income for the tax year, as reduced by certain deductions. It is determined from the annual financial statements prepared under GAAP.

In general, all necessary expenses incurred in producing income during the year and depreciation on income-producing property may be deducted from gross income to arrive at taxable income. However, certain items are not deductible from gross income, such as:

- CIT
- Penalties and fines
- Gifts and donations
- Expenses derived from transactions with related persons or entities that, as a result of a different tax classification, do not generate income or whose income is exempt or taxed at a nominal rate lower than 10%
- Depreciation charges that exceed the maximum rates prescribed by law, unless it can be demonstrated that the rates used correspond to the actual depreciation incurred. However, for the 2013 and 2014 fiscal years, tax deductibility of the depreciation of tangible, intangible and real estate assets of large-sized companies (i.e., companies with a net turnover that exceeded €10 million in the previous tax period) was limited up to 70% of the corresponding expense. Depreciation expense exceeding the referred limitation will be tax-deductible to the choice of the taxpayer, on a straight-line basis during a 10-year period or during the useful life of the asset, from the first tax period started in the 2015 fiscal year.
- Expenses incurred for gifts to clients and suppliers exceeding the amount of 1% of annual net revenues
- Impairment losses on (i) property, plant and equipment; investment property; and intangible assets, including goodwill; and (ii) debt securities, except inventories or receivables; these losses will be integrated in the taxable base during the useful life of the depreciable assets or when the assets are transferred or written off
- Impairment losses on securities representing interest in equity of companies if the impairment was registered in a tax period in which such securities met the requirements to apply the participation exemption regime; impairment losses on securities representing interest in owner's equity of nonresident

entities will not be tax-deductible in case the nonresident entities are resident in tax haven jurisdictions or do not comply with the "subject-to-tax" requirement[1]

- Impairment losses on securities representing interest in owner's equity of companies that do not meet the requirements to apply the participation exemption regime or, regarding nonresident entities that comply with the "subject-to-tax" requirement, shall be tax-deductible when the losses are materialized (that is, when the shares are transferred or written off)
- Decreases in value arising from the application of the fair value criterion corresponding to securities representing interests in owner's equity of companies that meet the requirements to apply the participation exemption regime, unless an increase in the value corresponding to homogeneous securities of the same amount has been previously included in the taxable income
- Losses derived from intragroup transfers (within the mercantile group) of tangible and intangible assets, real estate investments and debt instruments; tax deductibility of these losses is deferred until sale to third parties (or when the selling entity or the acquiring entity stops being a member of the same group) or via depreciation throughout the useful life of the assets
- Losses derived from intragroup transfers (within the mercantile group) of securities representing the holding in equity of entities that do not meet the requirements for the application of the Spanish participation exemption regime and, regarding the non-Spanish resident entities, when they comply with the "subject-to-tax" requirement, will not be deductible until sale to third parties (or when the selling entity and the acquiring entity stops being a member of the same group), or when the subsidiary is liquidated (unless the winding-up takes place in the framework of a reorganization transaction or the same business activities continues being rendered through other legal entity)
- Losses derived from the transfer of securities representing the holding in equity of entities that meet the requirements for the application of the Spanish participation exemption regime cannot be taken for tax purposes. Neither can losses derived from the transfer of shares in non-Spanish resident entities that are tax haven residents or do not comply with the "subject-to-tax" requirement. On the contrary, losses generated upon liquidation of a subsidiary are deductible unless the liquidation takes place in the framework of certain types of reorganizations. In any event, the loss that can be taken for tax purposes must be reduced by dividends received in the former 10 years that they have been exempt or have given rise to a tax credit.
- Losses derived from the sale of a PE, while losses triggered upon the closing down of a PE may continue to be taken for tax purposes; the loss that can be taken for tax purposes is a loss derived from the closing down, reduced by the sum of profit from the PE that has benefitted from the exemption regime in earlier years

Recapture of the portfolio impairments

Until fiscal years starting before 2013, certain portfolio impairments (write-off to record a decline in value) were allowed as a CIT expense. When the portfolio impairment regime was abolished (for tax years starting on or after 1 January 2016), rules were introduced pursuant to which the expense taken in prior years had to be added back to the tax base if the relevant subsidiary regained value and/or distributed a dividend.

1 *If the company that had shares sold is a nonresident in Spain, it must be subject to a CIT similar to the Spanish CIT at a minimum 10% rate. The Spanish CIT Act presumes that this test is passed when the company is resident in a country that has signed a tax treaty with Spain with an exchange of information clause.*

Under the rules now in force, taxpayers that took the impairment for tax purposes and have not completely added the same back to the CIT base are subject to "minimum clawback rules" that determine that they must, at least, recapture the outstanding portfolio impairment amount over a five-year period (starting in FY16). Where the above explained rules determine that the expense must be added back over a shorter period.

Recapture of losses generated by non-Spanish PEs

Prior to 2013, losses from a PE abroad could be taken for tax purposes. Limitations are now introduced when a taxpayer transfers a PE at a gain: the amount that can be exempted from tax is the gain reduced by the sum of net losses incurred by the PE prior to FY13 that exceed the net profit generated by the PE from FY13 onward.

Participation exemption regime and foreign tax relief

The exemption method may be used to avoid double taxation on dividends received from abroad and on capital gains derived from transfers of shares of foreign companies if the following requirements are met:

- At the time of the distribution of the dividend or the generation of the capital gain, the Spanish company has owned, directly or indirectly, at least 5% of the share capital of the company or when the acquisition value of the participation is higher than €20 million (for first-tier subsidiaries).
- The minimum holding period is one year. For dividends, the one-year period can be completed after the distribution. In addition, the time period in which the participation is held by other group entities is taken into account for purposes of the computation of the one-year period.
- The minimum level of (nominal) taxation is 10% under a foreign corporate tax system similar to the Spanish CIT. This requirement is deemed to be met if the subsidiary is resident in a tax treaty country.

The exemption will not apply to capital gains derived directly or indirectly from (i) entities passively holding assets, (ii) Spanish or European Union (EU) Economic Interest Agrupations, or (iii) controlled foreign corporations (CFCs) obtaining more than 15% of passive income as defined by the CFC rules (which implies checking compliance with the substance requirements at the level of the CFC).

The abovementioned participation exemption regime is extended from 1 January 2015 onward to dividends and capital gains derived from Spanish subsidiaries, instead of applying the tax credit for the avoidance of double taxation.

The exemption method is also applicable in the case of income obtained by foreign branches of a Spanish company, provided that the requirements above are met.

If the exemption method does not apply, a tax credit is allowed for underlying foreign taxes paid by a subsidiary on the profits out of which dividends are paid and for foreign withholding taxes (WHT) paid on dividends. Such tax credit is equal to the lesser of the following:

- The Spanish corporate tax that would have been payable in Spain if the foreign income had been derived in Spain
- The actual income tax paid abroad on the foreign-sourced income

There are special application rules of the participation exemption for those situations in which the participation acquired was valued according to the special CIT regime for restructurings (neutrality tax regime). These special rules depend on whether the participation was acquired to a taxable person under nonresident income tax or to a taxable person under personal income tax:

- In the first situation it is stated that in the contributions of assets or shares that do not meet the requirements for the participation exemption in any tax year, the participation exemption for the transfer of shares does not apply on the deferred amount of the transmitting due to the contribution, unless the acquiring proves the integration of such income on its taxable income.

- In the second case, if the income derived from the contribution of shares is not considered for personal income tax purposes due to the valuation according to the restructuring regime and if the shares are transferred within two years from their contribution, the participation exemption would not be applicable on the difference between the tax value and the fair value of the shares when the contribution took place, unless an individual transferred the shares in the company after paying the personal income tax.

Capitalization reserve

For fiscal years starting from 1 January 2015 onward, Spanish CIT taxpayers can reduce their taxable base in an amount equal to 10% of the increase of their net equity on a given year, provided they book a non-disposable reserve for the same amount for a five-year term.

The increase of the net equity is calculated as the difference between the net book value of the company at the beginning (excluding for this purpose the accounting result of the previous year) and at the end of the financial year (excluding for this purpose the accounting result of the current year) minus some equity adjustments (as described below), with the limit of the positive taxable base prior to the utilization of any tax losses (any amount exceeding this limit will be carried forward the following two years).

The main equity adjustments are:

- Shareholder contributions
- Share capital increase/shareholders contributions made as a consequence of a shareholder loan waiver
- Legal/statutory reserves
- Net equity variation corresponding to the re-evaluation of the deferred tax asset registered by the company as a consequence of the new CIT rate
- Net equity increase derived from transactions involving the own shares of the company

The above 10% reduction cannot exceed the 10% of the previous positive taxable base. Any excess over this 10% of the positive taxable base can be carried forward in the subsequent two fiscal years.

Transfer pricing

Spanish tax law includes the arm's-length principle and the requirement of documenting all related-party transactions.

The arm's-length principle applies to all transactions (domestic or international) carried out by taxpayers with related parties.

The following are the principal aspects of the Spanish transfer pricing regime:

- Taxpayers must use arm's-length values in their tax returns. As a result, taxpayers bear the burden of proof on transfer pricing issues.
- The guidelines and pricing methodology of the Organisation for Economic Co-operation and Development (OECD) apply.
- The law provides for secondary adjustments. Under this measure, if the agreed value in a transaction differs from the normal market value, the difference between the values is re-characterized by following a substance-over-form approach. From 1 January 2015, the secondary adjustment will not take place if the values are reinstated by the parties involved.
- Advance pricing agreements (APAs) may be negotiated. APAs are proposed to have retroactive effects within the statute of limitations period.
- New specific statutory documentation requirements, in line with the guidelines of the EU Joint Transfer Pricing Forum, have been in force since February 2009.
- Penalties and delay interest may be imposed. Also, a specific penalty regime is applicable in the case of failure to meet the documentation requirements.

Additionally, in accordance with the Spanish CIT regulations, from 1 January 2016, the country-by-country reporting is applicable to those entities that serve as head company of a group and are resident in Spain with a turnover exceeding €750 million in the preceding financial year considered at a group level. Notwithstanding, among other cases, those companies whose ultimate owner is resident in a country where the country-by-country reporting has not been introduced are also obliged to fulfill this information requirement in Spain provided that the mentioned turnover has been exceeded.

The information to be included in this reporting is the following:

- Gross income of the group, distinguishing the income obtained with related parties or third parties
- Income before CIT or other taxes with identical or analogous nature
- CIT or taxes with identical or analogous nature to CIT, paid or accrued, including withholding taxes borne
- Amount of net capital and other equity existing at the end of the tax period
- Average workforce
- Tangible assets and real estate investments other than cash and credits
- List of resident entities, including PEs, and their main activities
- Other information deemed relevant

This reporting shall be filed after the 12-month period following the end of the tax period.

Administration

The tax year is the same as the accounting period, which can be different from the calendar year but may not exceed 12 months. The tax return must be filed within 25 days after 6 months following the end of the tax year. In April, October and December of each calendar year, companies must make installment payments on account of CIT equal to either of the following:

- Eighteen percent of the tax liability for the preceding tax year
- An amount calculated by applying a percentage of the CIT rate to the profits for the year (up to the end of the month preceding the date of the payment), then subtracting from the result the tax withheld from payments to the company and advance payments of tax previously made; this alternative is compulsory for companies with turnover of more than €6 million in the immediately preceding tax year

For CIT installment payments, the proportion of the CIT rate is determined as 5/7 of the applicable CIT rate (25%). This means that the applicable rate for the interim payments on account of 2016 onward is 17%. The applicable rate for oil and gas companies is 21%, considering that the CIT rate applicable to these companies from 2016 onward is 30%. For those taxpayers whose net turnover within the 12 months prior to the beginning of the relevant fiscal year exceeds €10 million, the CIT rate is determined as 19/20 of the applicable CIT rate. This means that the applicable rate for the interim payments is 24% (29% for oil and gas companies).

However, and also for those taxpayers whose net turnover within the 12 months prior to the beginning of the relevant fiscal year exceeds €10 million, there is a minimum CIT interim payment of 23% over the taxpayer's accounting profits. In the case of oil and gas companies, the minimum CIT interim payment is 25% of the accounting profits.

Late submission of a CIT return or late payment on account will result in the imposition of surcharges (up to 20%), and also the accrual of late penalty interest if the return is filed more than 12 months after the deadline for its voluntary submission.

Other issues

No special terms apply in relation to signature bonuses, production bonuses or other lump-sum payments. Rental, fees and royalties are subject to the general tax rules.

Entities co-owning an exploitation concession will be allocated the pro rata share of the activity income and expenses and of the gains and losses from the transfer of assets.

Spanish law does not recognize the concept of a national oil company, nor of production sharing agreements.

An R&D tax credit is not allowed for exploration, prospecting or drilling for hydrocarbons and minerals.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Special CIT rules applicable to oil and gas companies

There are special CIT rules applicable to oil and gas companies. Some of them (depreciation of intangible assets and higher tax rate) are applicable to any company engaged in the exploration, investigation and exploitation of hydrocarbons and hydrocarbon sub-storage, regardless of whether they also perform other activities.

However, some other special corporate tax rules — in particular regarding a depletion factor reserve and a specific tax losses compensation regime — are applicable only to companies whose corporate business is solely the exploration, investigation and exploitation of hydrocarbons and hydrocarbon sub-storage. These two rules are discussed further next.

Depletion factor reserve

Companies whose corporate purpose is solely the exploration, investigation and exploitation of hydrocarbons and hydrocarbon sub-storage are entitled by law to a reduction of their tax base, in respect of the depletion factor reserve, which, at the discretion of the entity, may be either of the following:

- 25% of the amount of the consideration for the sale of oil and gas products and for the provision of storage services, up to a limit of 50% of the tax base prior to this reduction

  Or
- 40% of the amount of the tax base prior to this reduction

Some accounting and material requirements should be met to benefit from the reductions above.

In particular, the amounts of the depletion factor reserve that reduce the tax base must be invested in the activities of prospecting, research or exploitation of oil and gas performed within 10 years or in "the abandonment of fields and the dismantling of marine rigs." For these purposes, consideration could also be given to prospecting, research or exploitation carried out within the four years before the fiscal year in which the tax base is reduced by the depletion factor reserve.

The taxpayer must disclose, in the notes to its financial statements for the 10 years following that in which the appropriate reduction was made, the amount of the reduction, the investments made with a charge to it, and the depreciation or amortization taken, as well as any decrease in the reserve accounts that were increased as a result of a reduction of the tax base and its use.

Specific tax losses compensation regime

Until 31 December 2014, tax losses could be carried forward for 18 years. From 1 January 2015, tax losses that are pending to be offset as of that date can be carried forward with no time limit.

From 1 January 2016, a general restriction to offset losses of 60% of the positive taxable base applies. From 1 January 2017 onward, this restriction amounts to 70% of the positive taxable base.[2] However, for taxpayers with a net

2 *The limit applies over the tax base amount prior to the offsetting of the carryforward tax losses and the capitalization reserve allowance.*

turnover exceeding €20 million in the 12 months prior to the beginning of the relevant fiscal year, the following restrictions to offset carry forward losses apply[3]:

- For companies with turnover ranging from €20 million to €60 million, the carry forward tax losses utilization is limited to 50% of the tax base.
- Companies whose net turnover within the 12 months prior to the beginning of the fiscal year is more than €60 million may only offset tax losses up to a maximum amount of 25% of the positive taxable base.

In any case, a minimum €1 million threshold is set.

Finally, companies whose corporate purpose is solely the exploration, investigation and exploitation of hydrocarbons or hydrocarbon sub-storage will apply specific rules to offset tax losses. These entities do not have a time limit for offsetting tax losses, and only 50% of each tax loss can be offset in a single tax year. The previous general restriction to offset losses will not apply to these specific companies.

Amortization of intangible assets

Companies engaged in the exploration, investigation and exploitation of oil and gas (exclusive business purpose is not required) have a special regime applicable to intangible assets.

In particular, intangible assets may be amortized at a maximum annual rate of 50%. Such intangible assets can include exploration expenses, such as prior geological, geophysical and seismic works; costs incurred to prepare access routes to the drilling site and for land preparation; exploration evaluation works; development test drilling; and restoration and conservation of wells.

There is no maximum amortization period for intangible assets or prospecting expenses.

Higher tax rate applicable for hydrocarbon activities

For residents and nonresidents that conduct business activities in Spain through a PE, the general CIT rate is 25% (28% until 31 December 2015 and 30% until 31 December 2014). However, for entities engaged in the exploration, investigation and exploitation of hydrocarbons or hydrocarbon sub-storage owned by third parties, the applicable tax rate is 30% (33% until 31 December 2015 and 35% until 31 December 2014).

If a company is engaged in the exploration, investigation and exploitation of hydrocarbons or hydrocarbon sub-storage and also carries out other activities, the applicable tax rates are 30% for the former activities and 25% for the latter. Note that, in this case, the company would not be allowed to apply the special rules mentioned earlier in this Section C under "Depletion factor reserve" and "Specific tax losses compensation regime."

Entities exclusively engaged in hydrocarbon storage activities and other possible activities, but not in the abovementioned activities of exploration, investigation and exploitation, will be taxed at the general 25% tax rate and will not be entitled to any special benefits.

Branch remittance tax

In addition to CIT, nonresident entities operating in Spain through a PE are subject to a branch remittance tax at a rate of 19% from 1 January 2016 (20% until 12 July 2015 and 19.5% from such date until 31 December 2015), unless one of the following exceptions applies:

- Branches of EU-resident entities, other than tax haven residents, are exempt from the tax.
- Branches can be exempt from the tax if a double tax treaty does not mention the tax and if the other tax treaty country provides reciprocal treatment.

3 *A new rule that was introduced in the Spanish CIT Law by the Royal Decree-Law 3/2016 re-established the existing limitations to offset carryforward losses for years 2011 to 2015.*

Ring fencing

In Spain, residents and nonresidents that conduct business activities through a PE may offset losses against any of its profits. Therefore, Spain does not generally apply ring-fencing in the determination of corporate tax liability.

However, if an entity is engaged in the exploration, investigation and exploitation of hydrocarbons or hydrocarbon sub-storage and also carries out other activities, the losses from hydrocarbon activities would be ring-fenced and are not allowed to be offset against profits of other businesses, and vice versa.

Group taxation is applicable for companies taxed on identical tax rates. Therefore, entities taxed under the special hydrocarbon regime cannot be part of a tax unity with other group entities carrying out activities subject to the general CIT rate (25% in 2016).

D. Withholding taxes

The general rule for WHT is that nonresident entities operating in Spain without a PE are taxable at a general rate of 24% (24.75% until 31 December 2014), unless an applicable double tax treaty provides a lower WHT rate. The general rate for EU residents is 19% (20% until 12 July 2015 and 19.5% from such date until 31 December 2015).

Royalties

WHT applies at the general rate of 24% on royalty payments (24.75% until 31 December 2014). A 19% rate could apply if the recipient is EU-resident (20% until 12 July 2015 and 19.5% from such date until 31 December 2015). However, from 1 July 2011, royalties paid to associated entities resident in the EU or to PEs located in the EU are exempt from WHT if specific conditions are met (an applicable double tax treaty may anyway establish a reduced WHT rate should the conditions not be met).

Interest and dividends

WHT applies at a rate of 19% on interest and dividend payments (21% until 31 December 2014, 20% from such date until 12 July 2015, and 19.5% from 12 July to 31 December 2015). An applicable double tax treaty may provide for a lower WHT rate.

Under certain circumstances, interest and dividends paid to entities resident in another EU member state are wholly exempt from WHT.

E. Financing considerations

Finance costs are generally deductible for corporate tax purposes, with the exceptions discussed below.

Interest expense deductibility limitation

The general limitations for interest deductibility rules are as follows:

- The net financial expenses not exceeding 30% of so-called "operating profit" may be taken as deductible for Spanish CIT purposes. "Operating profit" is defined as a parameter economically similar to earnings before interest, taxes, depreciation and amortization (EBITDA), increased by dividend income and participation in benefits derived from entities participated at least in a direct or indirect 5%, or whose acquisition value is higher than €20 million, excluding stock acquired in an intragroup leveraged acquisition when the interest deductibility is denied under the CIT rules.[4]
- The concept "net interest expense" is defined as the excess of interest expense over interest income for the fiscal year. Interest expense that is

4 *From 2012, tax deductibility of interest expenses on intragroup financing is disallowed when the financing is entered into for (i) the acquisition of shares in entities when the seller belongs to the same group of companies, and (ii) the capitalization of entities belonging to the same group as the borrower. However, interest deductibility is allowed when the taxpayer proves that there are bona fide commercial reasons that justify the intragroup leveraged transaction.*

considered nondeductible under the rules relating to intragroup leveraged transactions is not taken into account for these purposes.

- The net financial expense equal to or less than €1 million is fully deductible.
- If the net financial expense of the fiscal period does not exceed the 30% threshold, the difference may be carried forward and increase the threshold for the following five years.
- Any excess interest that cannot be deducted can be carried forward (subject to the same deductibility limitation) with no time limit.
- From 1 January 2015, interest from loans to purchase shares can be deducted up to only 30% of the operating profit of the acquiring entity. This new rule applies to transactions implemented after 20 June 2014. The limit applies where (i) the acquired and acquiring entities are merged within a four-year period or (ii) the acquiring entity is taxed within a tax unity. In such cases, for the purposes of the abovementioned restriction, the operating income generated by the acquired entity or any other entity included in the tax unity within a four-year period after the restricted leveraged acquisition will be excluded.

This limitation will not apply (escape clause) in the year of the acquisition, if the acquisition debt does not exceed 70% of the consideration for the shares. This limitation will not apply in the subsequent years if the acquisition debt is at least "proportionally amortized" within an eight-year period until it is reduced to 30% of the total consideration.

Finally, from 1 January 2015, intragroup profit-sharing loans are characterized as equity instruments for Spanish tax purposes. Consequently, expenses derived from the same would not be deductible at the level of the borrower for CIT purposes (this rule will not apply to profit-sharing loans granted before 20 June 2014). Symmetrically, under certain circumstances, interest income deriving from intragroup profit-sharing loans qualifies as dividend income that is exempt for CIT purposes for the lender.

Interest paid by branches to their head office

Interest paid by branches to their head office is not tax-deductible in order to determine the taxable base of the branch in Spain.

F. Surface tax

An additional tax called "surface tax" applies to oil and gas companies. This tax should be calculated yearly, based on the number of hectares of a company's exploration or exploitation sites.

In the case of research licenses, amounts paid as a surface tax are considered for accounting purposes as part of an intangible asset; they are therefore depreciated as such.

In the case of exploitation licenses, amounts paid as a surface tax are considered to be an expense of the tax year for accounting purposes and are deductible for CIT purposes.

G. Indirect taxes

VAT

Value-added tax (VAT) is potentially charged on all supplies of goods and services made in Spain and its territorial waters (within the 12-nautical-mile limit from the shore). The standard VAT rate in Spain is 21% as from 1 September 2012 (18% previously).

If a Spanish branch is constituted, it is deemed as a PE for VAT purposes, and the branch will therefore have to comply with Spanish VAT obligations, such as registration for VAT and filing of VAT returns.

A nonresident EU company that is required to register for VAT purposes in Spain can register directly with the Spanish tax authorities; however, for practical purposes, it is advisable to appoint a Spanish fiscal representative. Nonresident companies that are not from another EU Member State that wish to register for VAT purposes in Spain are required to appoint a Spanish fiscal representative.

VAT incurred by an entity that is VAT-registered in Spain is normally recoverable on its periodic VAT returns. The refund of the credit VAT can, in general, be requested at the end of each calendar year; however, under certain circumstances, this refund can be requested on a monthly basis.

Regarding VAT management, from 1 July 2017, all enterprises or professional workers whose VAT assessment period is the calendar month[5] are required to provide their invoicing records and record books for issued and received invoices to the tax authorities in real time as a consequence of the implementation of the Immediate Submission of Information (ISI) system.[6] The ISI system is voluntary for VAT taxpayers that are not forced to participate in it by law.

Customs duties

All goods imported into Spain from outside the EU are potentially liable to customs duty. The rate of customs duty is based on the classification of the goods and whether the goods qualify for preferential rates.

Natural gas and associated products imported into Spain from outside the EU are subject to normal customs import procedures. In addition, import VAT is payable at the standard rate.

Excise duty

In Spain, the retail sale of certain hydrocarbon products is subject to a special indirect tax.

H. Production royalties

Spain requires an annual payment of certain royalties calculated on the value of oil, gas and condensates being extracted within the territory of Spain. Such royalties are calculated based on the amount of gas, oil and condensates that are determined by the volume resulting from the measuring devices of hydrocarbon extractions. This measurement corresponds to the total volume measured at wellhead, reduced by the amounts of water, CO_2 and other substances that are removed in the process of purification and separation carried out by an operator.

For these purposes, the value of the extraction is calculated by applying the reference price approved by the government (generally, it will be calculated by reference to the price of the most representative markets) to the total volume of the product extracted. This volume shall be expressed in barrels, whose capacity and measurement conditions are determined by the government (oil and condensates), and in cubic meters measured at zero degrees Celsius temperature and pressure bar (gas).

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5 *Large companies (whose turnover for the prior year will have exceeded €6 million, taxpayers registered in the monthly refund register (known as the "REDEME") and taxpayers being part of a VAT group (known as the "REGE")).*

6 *The ISI system was introduced in VAT regulation by Royal Decree 596/2016, dated 2 December 2016, for the modernization, improvement and promotion of electronic means in the management of VAT.*

The royalty rates are provided in the summary table below:

		Tax rate	
	Barrels	Land exploitation	Sea exploitation
Oil and condensate products	Up to 365,000	2%	1%
	From 365,001 to 3.65 million	6%	5%
	More than 3.65 million	8%	7%
		Tax rate	
	Volume	Land exploitation	Sea exploitation
Gas	Up to 32,850,000 m³	1%–3%	1%
	From 32,850,000 up to 164,250,000 m³	3%–4%	3%
	More than 164,250,000 m³	4%–5%	4%

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

The fiscal system applied in Sri Lanka is based on petroleum resources agreements (PRAs), which are production sharing agreements. Sri Lanka has a model agreement issued by the government in 2013. The following are envisaged by the model agreement and guidelines issued in this regard:

- Royalty
- Signature bonuses
- Production bonuses
- Production split
- Training for nationals
- Utilization of local goods and services

B. Fiscal regime

Income tax

Contractors carrying out petroleum operations under PRAs are deemed to be resident in Sri Lanka and are subject to a concessionary income tax rate of 12%. The rate applies to taxable income determined as total proceeds received by the contractor from the sale or other disposition of its share of production, less the costs and expenses that are allowed for recovery.

However, contractors would normally be eligible for relief available under the Strategic Development Projects Act, which provides, depending on the level of investment, full or partial exemptions from the following taxes:

- Income tax
- Value-added tax
- Economic service charge
- Customs duty
- Excise duty
- Nation building tax
- Ports and airports development levy
- Taxes under the finance acts

Relief from the taxes above will also be available to subcontractors working with the contractor.

Royalties

Royalties are based on a progressive sliding scale linked to average daily production rates (in million barrels of oil equivalent). The rates and production tiers are not distinguished for oil and natural gas. The royalty rates as envisaged in the model contract vary from 1% to 10% with a 1% step, with the production rates being biddable.

Cost recovery

The cost recovery ceiling for petroleum is 80% of the value of petroleum produced and saved. The costs are recovered with priority given first to production costs, then to exploration costs, and finally to development costs. The unrecovered portion of the costs can be carried forward to subsequent years until full cost recovery is achieved within the duration of the PRA.

Profit production sharing

The production remaining after cost recovery is treated as "profit production" to be further split between the government and contractor. Profit production sharing for petroleum is based on a progressive sliding scale linked to average daily production rates. The contractor's share of profit production as envisaged in the model contract varies from 90% to 10%, with the production rates being biddable.

Signature bonuses

A contractor is required to pay, at a minimum, a signature bonus of US$1,000,000 for deepwater blocks and US$200,000 for shallow-water blocks. Signature bonuses are not cost-recoverable.

Production bonuses

The model contract envisages production bonuses, payable when the prescribed production tiers are achieved. The tiers are linked to average daily production from the contract area. Both the amount of bonuses and production tiers are biddable. Production bonuses are not cost-recoverable.

Surface rental fees

The surface rental fees do not apply in Sri Lanka.

Ring-fencing

In Sri Lanka, there is no clear definition of "ring-fencing" for PRA contractors — meaning that PRA contractors do not need to determine the tax base or the amount of tax separately for each PRA activity.

According to Sri Lanka's income tax law, if the taxpayer is conducting activities in multiple locations, it can report corporate income tax on a consolidated basis.

For cost recovery purposes, the cost recovery is ring-fenced to the agreement area.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Incentives

Several incentives are currently available to oil and gas companies in addition to the reliefs available under the Strategic Development Projects Act, which are discussed in Section B above. Such incentives include, among other things, the following:

- Accelerated depreciation
- Uplifts for research and development expenditure
- Deductibility of interest costs
- Claiming of costs incurred on unsuccessful wells
- Indefinite carryforward of prior year losses
- Exemption from import duties on certain plant and equipment
- Relaxation of exchange control regulations

In addition to the above, the government offers various nontax incentives to contractors when negotiating PRAs with a view of promoting the upstream sector and boosting the commercialization of hard-to-reach oil fields.

Exports of petroleum products are exempt from export duties and any other taxes.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

The principal fiscal elements applying to Syria's oil and gas industry are as follows:

- Corporate income tax (CIT) rate – 28%[1]
- Withholding tax (WHT) – payable for services[2]
- Nonresident WHT – applies[3]
- WHT on Syrian entities and individuals – applies[4]
- Dividends – subject to WHT in some circumstances[5]
- Movable capital tax – 7.5%[6]
- Wages and salaries tax – 22%[7]
- Royalties – 7%
- Bonuses – 10%
- Resource rent tax – not applicable

1 *The standard CIT rates range from 10% to 28%, with certain companies taxed at flat rates. A municipality surcharge tax of 10% and a reconstruction tax of 10% of the tax due are imposed in addition to the normal tax rate.*

2 *In general, branches of foreign companies are subject to the nonresident withholding tax; however, if a branch imports goods produced by its parent company and sells the goods on behalf of the company in Syria, it is subject to the normal CIT rates.*

3 *This tax is withheld from specified payments made to nonresident companies, regardless of whether the company has a branch in Syria. The payments subject to the tax include payments under turnkey contracts (for details, see Section D).*

4 *WHT is imposed on income derived by Syrian individuals or entities from certain contracting, construction work and services and supply work (for details, see Section D).*

5 *WHT is not imposed on dividends paid by Syrian companies if the profits out of which the dividends are paid have already been subject to tax.*

6 *A municipality surcharge tax of 10% and a reconstruction tax of 10% of the tax due are imposed in addition to the normal tax rate. The tax on movable capital is a WHT that is imposed on certain payments to resident and nonresident companies and individuals, including various types of interest payments. WHT is imposed on income derived by Syrian individuals or entities from certain contracting, construction work and services and supply work (for details, see Section D).*

7 *Resident employers other than branches of foreign companies withhold wages and salaries tax from salaries, wages and fringe benefits or other remuneration paid to resident and nonresident Syrian employees. The first SYP15,000 of annual income is exempt.*

- Various other indirect taxes — payable
- Net operating losses:
  - Carryback — not allowed
  - Carryforward — five years
  - Investment incentives — not applicable.

Oil and gas are considered to be among the most important resources in the Syrian Arab Republic. Thus, the Government has always paid special attention to oil and gas fields and their development. The General Petroleum Corporation (GPC), which replaced the Syrian Petroleum Company (SPC), is the government body responsible for supervising and monitoring operating companies working in Syria.

Given the fact that Syria does not currently have sufficient experience to explore the country's oil and gas fields fully, foreign explorers and developers are often asked to assist in excavating these raw materials from Syrian soil. Accordingly, foreign companies are present in Syria and provide their services to the Syrian Government and other oil and gas companies. Oil and gas foreign companies are either operating companies or service companies.

B. Fiscal regime

Corporate income tax

Foreign operating companies are contracted by the GPC with a production sharing agreement (PSA), through which profits generated from the exploration and development of oil are divided between the foreign company and the GPC. As per these PSAs, contracting companies do not pay CIT prior to the discovery and development phase, as the GPC is responsible for paying such taxes during this phase. However, once oil is discovered and developed, both the contractor companies and the GPC will be subject to CIT.

The table below sets out the CIT rates that apply to contracting companies.

	Tax rate
Between SYP0 and SYP50,000	Exempted
Between SYP50,001 and SYP200,000	10%
Between SYP200,001 and SYP500,000	15%
Between SYP500,001 and SYP1,000,000	20%
Between SYP1,000,001 and SYP3,000,000	24%
More than SYP3,000,001	28%

Additionally, a municipality surcharge tax of 10% and a reconstruction tax of 10% are imposed on any tax due.

Production sharing agreement

A PSA is an agreement signed between the GPC as a representative of the Syrian Government and an oil and gas company (a contractor). Generally, fiscal uncertainty clauses are not included in a PSA. According to a standard agreement, total production is divided into the following three parts:

- Royalty percentage paid to the Government
- Cost oil percentage
- Profit oil percentage

Cost oil and profit oil are calculated as a percentage of production volume. The percentages of cost oil and profit oil generally vary based on the particular PSA. The contractor incurs the actual costs related to the production of oil. The actual cost incurred is then compared with the cost oil percentage, and any costs incurred beyond the limit of the cost oil percentage are recovered from the GPC. Recoverable costs are any costs related to the production of oil.

Wages and salaries tax

Oil and gas companies are obliged to pay payroll taxes on the salaries and benefits remunerated to their employees. The tax rates are shown in the table below.

	Tax rate
Between SYP15,001 and SYP20,000	5%
Between SYP20,001 and SYP25,000	7%
Between SYP25,001 and SYP30,000	9%
Between SYP30,001 and SYP38,000	11%
Between SYP38,001 and SYP50,000	13%
Between SYP50,001 and SYP65,000	16%
Between SYP 65,001 and SYP 75,000	19%
More than SYP75,000	22%

Fixed payment such as annual bonus or any other one-off payment is subject to tax rate of 10%.

Royalties

As indicated above and in accordance with the PSA, the Government receives a share of the profits generated from the exploration and production of oil. Although oil and gas companies share these profits with the Government according to a specified allocation stipulated in the PSA, these profits are not considered royalties.

However, oil and gas companies do sometimes pay royalties outside Syria. In such cases, the oil and gas companies are required to withhold a 7% (income tax) and 3% (wages and salaries) as WHT.

Exchange control regulations

Prior to September 2005, Syria had many different exchange rates that governed its local transactions (i.e., an import exchange rate, an export exchange rate and a neighboring countries exchange rate). These rates were unified into one exchange rate, called the free exchange rate, in September 2005. The exchange rate of the Syrian pound has increased due to the crisis that started in early 2011 and had an impact on the Syrian economy in general and the level of imports and exports in particular.

The rate of the Syrian pound has experienced declines since the crisis began. The central Bank of Syria oversees the exchange rate's stability, monitors private banks and determines the Syrian pound.

Repatriation of profits abroad

Foreign currency transactions are highly regulated in Syria. Foreign currency repatriation is restricted and is only permitted in special cases. Only companies with projects licensed under specific investment laws are allowed to repatriate annual profits or capital. Oil and gas companies can be licensed under the investment law and, accordingly, can repatriate their profits. In addition, the Central Bank of Syria has issued a resolution by which companies licensed under the investment law can transfer their proceeds to their foreign partners outside Syria.

Dividends

There is no WHT on dividends in Syria as long as the profits from which they are paid have already been subject to tax. However, dividend income from non-Syrian companies is subject to a 7.5% tax in addition to a 10% administrative fee, and 10% reconstruction tax is imposed on the tax due.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Incentives

Exploration

All companies that have a PSA with the public establishment for oil refining and distribution and that are in the exploration phase are exempt from paying CIT, as no profit has been realized, and are only subject to payroll taxes.

Losses

Losses may be carried forward for five years for purposes of a deduction from taxable income. Losses may not be carried back.

D. Withholding tax

Service companies are registered as branches of foreign companies. These companies are subject to the supervision of the Ministry of Economy and Foreign Trade. As per Income Tax Law No. 24 of 2003, foreign branches of foreign companies are not subject to CIT. Instead, these service companies are subject to WHT or nonresident tax.

The rates for the abovementioned nonresident tax were amended in Income Tax Law No. 60 of 2004 and related amendments. The current withholding rates are as follows:

- 2% for all onshore supplies
- 3% for mixed services (supplies and services), plus 1% of wages and salaries tax
- 7% for pure onshore services, plus 3% of wages and salaries tax

This tax is required to be withheld by the foreign company on behalf of its customers and remitted to the Syrian tax authorities at the appropriate time. In addition, these branches of foreign companies are obliged by law to withhold the tax at the above rates when dealing with their local suppliers and service providers. Furthermore, Law No. 34 of 2008 concerning foreign companies obliged all branches of foreign companies to submit their annual audited financial statements to the Ministry of Economy and Foreign Trade within 90 days of the end of each fiscal year. However, no annual tax return is required to be filed for branches of foreign companies operating in the Syrian Arab Republic.

WHT is imposed on income derived by Syrian individuals or entities engaged in contracting, construction work and services and supply work that is performed with, or for the benefit of, the Syrian public, joint ventures (involving the private and public sectors), the private and cooperative sectors (e.g., those sectors that relate to farmers, agricultural associations and other businesses engaged in agriculture or farming) and foreign companies. The WHT rates are as indicated above.

E. Financing considerations

On 6 April 2009, the Ministry of Oil issued Letter No. 12257 regarding the application of Decision No. 93 of 2008. Decision No. 93 discusses the exchange rate that should be used when calculating the tax amount due on profits resulting from a PSA signed with the Syrian Petroleum Company. The Central Bank of Syria issued this decision on 30 June 2008 in response to a query raised by one of the operating companies in Syria. This decision obliged operating companies that have a PSA with the Syrian Petroleum Company to adopt the quarterly exchange rate issued by the Central Bank of Syria when calculating the tax amount due on profits resulting from the PSA (usually, operating companies in Syria use a monthly exchange rate by adopting the exchange price of the first day in the month).

F. Indirect taxes

VAT

Generally, value-added tax (VAT) is not applicable in Syria.

Customs duties

Customs duties are based on a basic duty plus a unified tax surcharge. The cost, insurance and freight (CIF) value of imported material is usually calculated at the free exchange rate. Duty rates are progressive and range from 1% to 100%, depending on the Government's view of the necessity of a product.

Permits must be obtained from the Ministry of Economy and Trade for the import of nearly all items. Generally, import permits are valid for six months in the private sector. Oil and gas companies often obtain some concessions under the terms of the PSA. In this regard, where a contractor or operating company, or one of its contractors or non-Syrian subcontractors, is permitted to import, it might be exempted from customs duties and import license fees with respect to various items, including (but not limited to) equipment, machinery and vehicles. All such concessions and the terms of such concessions should be granted as specified in the PSA.

Consumption tax

Consumption tax is imposed on both imported products and local products (e.g., vehicles, gold, appliances, imported carpets, alcoholic drinks, soft drinks, tea, oil and margarine, cacao, cement, sugar, salt and bananas). The consumption tax rates range from 1.5% to 40%.

The tax is imposed on:

- The value of the product that has been used for determining the custom duties, in addition to the custom duties paid and other fees imposed on the "imported product." The tax should be levied upon the receipt of the product from the customs department.
- The sales value defined in the invoice. The tax should be levied when selling the products to merchants.

Consumption tax is also imposed on luxury hotels, restaurants and tourist transportation services. Tax rates range from 3% to 30%. The tax should be levied when the services are rendered. Consumption tax for each month should be transferred to the tax authorities within 10 days after the completion of the relevant month, using manual or electronic forms approved by the tax authorities.

Stamp duty

Stamp duties are imposed on contracts signed by two parties or on any documents that include legal obligations between two parties. The stamp duty rate may be a fixed rate, which varies according to the type of transaction, or a proportional rate based on the value of the document subject to the duty. The value of the document is generally determined by the total value of the contract or agreement.

Stamp duty should be paid to the tax authorities within five days following the signing the contracts. Any delay will be subject to a penalty equal to two times the amount of the stamp duty.

Stamp duty payable can be either:

- A percentage, from contracts with a fixed amount: 0.4% for each copy
  Or
- A lump sum, for contracts that do not mention the amount: SYP500 for each copy

Property tax

The Ministry of Finance excludes real estate dealers from Law No. 24 of 2003 and subjects them to Law No. 41 of 2005, which states that real estate sold will be taxed on its estimated value stated in the tax authority's records. The tax rate applied will differ based on the type of the real estate (i.e., land, residential or commercial). The seller should bear this tax, and it is due to the tax authorities very soon after finalizing the selling agreement. The title of the sold real estate will not be transferred to the buyer unless the seller pays the tax due.

The seller should submit a statement describing the sale of real estate within 30 days of the date sold, and the tax should be transferred to the treasurer within 30 days of the submission of the statement.

Tax on income from movable capital

This tax is levied on the following types of income:

- Interest from bonds and loans issued by Syrian institutions
- Dividends from non-Syrian companies
- Interest from bonds issued by the Syrian Government or foreign governments
- Liabilities documented with real estate guarantees
- Deposits of all kinds
- Guarantees and monetary bonds issued by legal entities
- Lottery prizes exceeding SYP1 million

Additional municipality surcharge tax and administrative fees

Legislative Decree No. 35 of 2007 sets out additional municipality surcharge taxes and additional administrative fees and grants the provincial council of each governorate the right to determine the additional rates without exceeding a maximum limit of 10%. Executive and implementation instructions for the decree were issued and published in Syria's *Official Gazette* of Syrian Arab Republic on 6 March 2008 (also the effective date).

The major points of this formal decision and its implementation instructions are as follows:

- 10% of the current capital revenue tax
- 10% of the real estate revenue tax
- 5% of the stamp duty
- 10% of customs fees
- 1% penalty levied on previously applied penalty when additional charges as set are not implemented
- SYP25 on each loan that exceeds SYP5,000 from any of the joint stock, public or private banks; amount is paid once upon signing the loan contract, opening an overdraft account or letter of credit and when renewing the loan facility
- 2% on each accommodation invoice of international and first class hotels

Rebuilding contribution

Law No. 13 of 2013 imposed an additional 5% on different kind of taxes till 2015. However, a new Legislative Decree No. 3 of 2016 has been issued as an extension to the provisions of the previous Law until 2018. Also, a new Law No. 46 of 2017 has been issued to amend the Rebuilding Tax Rate and increase it to be 10%.

Taxes and fees that are subject to the additional 10% rebuilding contribution starting from 1 January 2018 are:

- Consumption tax
- Stamp duty
- Contract stamps
- Withholding/nonresident tax (income tax portion only)
- Real profit tax (annual tax return)
- Tax on movable capital (deducted directly from bank interests)
- Tax on leasing contracts
- Tourist facilities tax
- War effort tax

Taxes and fees that are not subject to the additional 10% rebuilding contribution are:

- Administration fees
- Province fees
- Wages and salaries tax

The "Martyr Stamp"

Decision No. 47 of 2014 imposed a new stamp of SYP25 on all documents and contracts without any additions, starting 1 January 2015.

G. Other

Public Establishment for Oil Refining and Oil Derivatives Distribution

Legislative Decree No. 14 dated 14 February 2009 is related to the creation of the Public Establishment for Oil Refining and Oil Derivatives Distribution. This organization plays a supervisory role over companies involved in the refining and distribution of oil derivatives.

As per Article 3 of the decree, this establishment is required to handle the following tasks:

- Suggest strategies for refining oil, petrochemical industries and the distribution of oil derivatives, including the use of natural gas in automobiles and houses
- Work on the establishment of new refineries in accordance with the Government's plans in this regard
- Prepare and develop agreements to attract investors in the areas of oil refining and storage and distribution of oil derivatives
- Determine the preferences for financing investments in projects related to oil refining and distribution of oil derivatives, based on their national importance
- Coordinate and cooperate with local, Arab and international training institutes to develop the local capabilities and develop human resources in the related institutions
- Coordinate Arab and international bodies in the field of oil refining and the distribution of oil derivatives
- Follow the latest scientific and technological developments in the field of oil refining and distribution of oil derivatives
- Evaluate the environmental impact of related activities and projects with the coordination of the Public Organization for Environmental Affairs
- Coordinate the competent authorities regarding importing and exporting activities related to associated bodies
- Supervise operating companies involved in the refining and distribution of oil derivatives

The Public Establishment for Oil Refining and Oil Derivatives Distribution replaces the Homs Refinery Company.

Tanzania

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

The principal elements of the fiscal regime applying to the petroleum industry in Tanzania are as follows:

- Corporate income tax (CIT) — 30% or 25%[1]
- Capital gains tax (CGT) — 30%[2]
- Branch tax rate — 30%
- Withholding tax (WHT):
  - Dividends — 5% or 10%[3]
  - Interest — 10%[4]
  - Royalties — 15%[5]
  - Management, technical and professional fees — 5% or 15%[6]

1 *The 25% rate applies to a newly listed company in the Dar es Salaam Stock Exchange. The rate is applicable for three years following the listing. Thirty percent of the issued shares must be held by the general public.*

2 *Capital gains are treated as business income for companies and are taxed at the regular CIT rate. However, a petroleum right disposed of before commencement of production shall be deemed to be an investment asset.*

3 *The 10% rate is the general rate for both residents and nonresidents. The 5% rate applies to dividends paid by companies listed on the Dar es Salaam Stock Exchange. The 5% rate applies to a resident recipient company that owns at least 25% of the voting capital of the payer of the dividends. Dividend WHT is a final tax.*

4 *This tax applies to residents and nonresidents. It is a final tax for resident individuals and nonresidents. Resident companies credit the WHT against their annual CIT. If a resident strategic investor pays interest to a nonresident bank, the interest is exempted from WHT.*

5 *This WHT applies to both residents and nonresidents. It is a final tax for nonresidents only.*

6 *The 5% rate applies to resident technical services providers in the extractive industry (mining, oil and gas); this means services in respect of earthmoving, engineering and construction and includes geological, geotechnical and metallurgical services, seismic survey, data interpretation, drilling or any such service. In other words, the WHT is a final tax, and the basis for taxation for entities receiving such payments is 5% on the turnover (not 30% of profit), with the liability settled by way of withholding. A 15% rate applies to nonresidents.*

- Insurance premiums – 5%[7]
- Rent, premiums and similar considerations – 10% or 15%[8]
- Natural resources payments – 15%
- Branch remittance tax – 10%[9]
- Alternative minimum tax (AMT) – 0.3%[10]
- Net operating losses (years):
  - Carryback – 0% and carryforward – unlimited

Various indirect taxes apply also to petroleum industry activities.

B. Fiscal regime

Effective 1 July 2016, Tanzania introduced a special regime in the Income Tax Act (ITA 2004) for petroleum operations that applies to upstream, midstream and downstream activities. The regime covers CIT and CGT.

However, the fiscal regime for value-added tax (VAT), import duty and royalties is similar to those applicable to other industries. It includes some tax exemptions on import duties and on VAT for exploration companies. Under the VAT Act, 2014; special VAT relief on petroleum operations was abolished.

The Tanzania Petroleum Development Corporation (TPDC) is the institution established by the Government for the development of the exploration, prospecting and production of oil and gas. The TPDC acts on behalf of the Tanzanian Government, including entering into production sharing agreements (PSAs) with investors in the oil and gas industry, signing the agreements and acting as a regulator of the industry.

In July 2015, three acts were passed into law: the Petroleum Act, 2015; the Tanzania Extractive Industry (Transparency and Accountability) Act, 2015; and the Oil and Gas Revenue Management Act, 2015. The acts update and consolidate existing enactments for the oil and gas sector; the two acts, namely the Petroleum (Exploration and Production) Act, 1980, which covered upstream petroleum operations, and the Petroleum Act 2008, were repealed. Under the Petroleum Act, 2015, profits from direct/indirect assignment, transfer or any other disposal or rights under a petroleum agreement regardless of the beneficiary or type of transaction shall be subject to taxes at rates prescribed in the income tax. Payment of interest shall be subject to withholding tax and may be deductible for corporate tax purposes if approved by the Petroleum Upstream Regulatory Authority (PURA).

In July 2017, three laws were passed into law: the Natural Wealth and Resources Contracts (Review and Re-Negotiation of Unconscionable Terms) Act, 2017; the Natural Wealth and Resources (Permanent Sovereignty) Act, 2017; and the Written Laws (Miscellaneous Amendments) Act, 2017. The latter extensively amends the Mining Act, 2010, and, to a limited extent, the Petroleum Act, 2015.

The new legislations reassert that control and ownership of natural wealth, including oil and gas, shall be exercised by the people of Tanzania through the Government and held in trust by the President on behalf of the people. Export of raw minerals for beneficiation outside Tanzania is banned. Retention of earnings from natural wealth and resources in banks outside Tanzania is banned. All disputes in respect of national wealth and resources are to be settled by local courts or tribunals. The National Assembly may review new and existing PSAs, subsequent to which the Government may order to renegotiate terms deemed unconscionable.

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7 *This tax applies to nonresidents only.*

8 *The 10% rate applies to residents. The 15% rate applies to nonresidents. This WHT is a final tax for nonresidents and for individuals not engaged in business.*

9 *This tax applies to the after-tax profits of branches of foreign companies, and it is calculated in accordance with a formula provided in the Income Tax Act.*

10 *This is a tax on turnover, which applies to companies and branches with perpetual tax losses for three consecutive years. However, this rule does not apply to a company conducting exploration operations (effective from 1 July 2016).*

Corporate tax

In Tanzania, a resident corporation is subject to income tax on its worldwide income at the rate of 30%, and income tax shall be paid by the person for each petroleum right for a year of income. A nonresident corporation is taxed on its Tanzanian-sourced income only, which is also taxed at the 30% rate. However, a company is temporarily (i.e., during three years) taxed at a reduced rate of 25% if 30% of its equity shares have been issued to the public and it is listed on the Dar es Salaam Stock Exchange.

Corporations having perpetual tax loss for three consecutive years are liable to alternative minimum tax (AMT) at a rate of 0.3% of turnover. The payment due is computed from the third year of the perpetual tax loss. However, this provision does not apply to a person in the exploration operations.

Corporate tax is imposed on net taxable income. Taxable income is determined based on audited financial statements and is calculated as gross revenue less tax-deductible expenses allowable under the Income Tax Act, 2004. Allowable deductions include expenses incurred wholly and exclusively in the production of income within one contract area operated by the same company. Bonus payment in connection with a petroleum right is not an allowable expenditure for tax purposes, and neither qualifies for tax depreciation. Royalty payment to the Government of Tanzania in connection with a petroleum right is not an allowable expenditure for tax purposes.

Expenditure of a capital nature is not tax-deductible, but a tax depreciation allowance is allowed on a 20% straight-line basis. In the context of the oil and gas industry, this is mostly in the form of a capital allowance available for depreciable assets — see further comments in Section C below.

Signature and production bonus payments

The model agreement for 2013 envisages a minimum signature bonus payment of US$2.5 million and a production bonus of at least US$5 million payable when production starts. A bonus payment is not deductible for CIT purposes.

Decommissioning payment/expenditure

Amounts paid from a decommissioning fund to the PSA holder to meet expenses of activities authorized by the decommissioning plan for which the fund was established is not considered as income of the PSA holder. However, amounts in the decommissioning fund that are paid to the PSA holder to meet expenses of activities not authorized by the decommissioning plan should be included in calculating the income of the PSA holder. In addition, any expenditure in excess of the amount contributed to the fund that is incurred during the implementation of the decommissioning plan is not deductible for tax purposes.

Development/exploration license

A petroleum right is an asset separate from any other interest in the land that constitutes the license area and separate from any other asset employed in petroleum operations. Thus, a development license or an exploration license is an asset separate from any other asset used in the petroleum operations and therefore is not allowed for deduction when calculating the company's income tax.

Ring fencing

Effective from 1 July 2016, each separate "petroleum right"[11] is treated as an independent business and a person will be required to prepare accounts and pay income tax for that business for each year of income separate from any other activity. Tax losses from a separate petroleum right may be deducted in calculating only the future income from that operation and not from income from any other activities such as upstream, midstream or downstream activities or non-petroleum activities.

Capital gains or losses

Capital gains on the disposal of depreciable assets are treated as business income for the corporate entity and are taxed at the normal corporate tax rate of 30%.

Gains from the realization of investment assets are taxed at 30%. Capital losses from the realization of investment assets are deductible against only capital gains from the same investment assets and not from ordinary income. Net capital losses can be carried forward for use in subsequent years.

See Section G for further comments on CGT on share transfers.

Functional currency

Income accounting must be reported in local currency, namely Tanzanian shillings (TZS). However, upon application and approval by the Tanzania Revenue Authority, an entity can account for income in a foreign currency under the terms and conditions in the approval.

Transfer pricing

The tax law includes provisions to ensure that controlled transactions are using arm's-length pricing. Introduced regulations impose the requirement to maintain contemporaneous transfer pricing documentation and particular procedures to be applied that are broadly consistent with the Organisation for Economic Co-operation and Development (OECD) model in determining transfer prices but contain strict reporting provisions.

Transfer pricing (TP) guidelines provide guidance to taxpayers about the procedures to be followed in determining arm's-length prices consistent with the act and TP regulations that take Tanzania's business environment into consideration. The TP guidelines provide a general overview of issues and factors to be considered in arriving at an acceptable arm's-length price.

TP provisions also apply to arrangements between a separate petroleum right and other activities of the person conducting the petroleum right, including other petroleum rights or midstream or downstream activities of the same person treated as arrangements conducted between associated persons.

Additional petroleum tax

Some of the PSAs provide for payment of additional petroleum tax (APT) calculated on the basis of a development area in accordance with the provisions of the PSA. APT is calculated for each year of income, and it may vary with the real rate of return earned by the company on the net cash flow from the development area in question. The rate for APT is either 25% or 35%, and it is possible for both rates to apply in the same year on the respective bases. The

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11 *"Contract area" in respect of petroleum operations means the area that is the subject of a petroleum agreement; and whenever any part of the contract is relinquished pursuant to a petroleum agreement, "contract area" represents the area as originally granted.*

- *Separately, the interest of a contractor under a PSA with respect to each exploration license granted for the contact area*
- *Separately, the interest of a contractor under a PSA with respect to each development license granted for the contract area*
- *Data or information pertaining to petroleum operations.*

APT is treated as tax that when due must be paid in cash at the time specified in the arrangement or PSA to the Commissioner General of Tanzania Revenue Authority or in any other time as the Commissioner may direct by written notice.

It should be noted that APT has not yet been introduced into practice, but the requirement is retained in the relevant PSAs entered into by oil and gas exploration companies with the Government of Tanzania.

Royalty regimes

Petroleum royalties are administered and collected under the Petroleum Act, 2015. Royalties are collected and paid to the Tanzanian Government at the following rates:

- For onshore/shelf areas — 12.5%
- For offshore areas — 7.5% of total crude oil/natural gas production prior to cost oil and or cost gas recovery at such royalty otherwise to be delivered to the Government in such manner as the Government may direct

Signature and production bonuses

The model agreement for 2013 envisages a minimum signature bonus payment of US$2.5 million and a production bonus of at least US$5 million payable when production starts.

Local content requirements

The PSA requires compliance with the local content policy. The policy provides for a greater use of domestic goods, services and materials and employment of Tanzania nationals.

Unconventional oil and gas

There are no special terms that apply to unconventional oil or unconventional gas in Tanzania.

C. Capital allowances

For tax purposes, depreciable assets include assets with a limited effective life that decline in value over time, such as plant and equipment, retention leases, etc., and expenditures other than financial costs incurred wholly and exclusively on reconnaissance, appraisal and prospecting or exploration operations and infrastructure.

Depreciation expenditure is allowed on a 20% straight-line basis on all assets used by the company in petroleum operations. Depreciation allowances granted to the company for a particular year of income cannot be deferred to a future year of income.

Expenditure and depreciation allowance in respect of assets covered by cost petroleum under a PSA are not allowable expenditures for tax purposes.

D. Incentives

Exploration

Please refer to Section C above.

Tax holidays

Tanzania does not have a tax holiday regime other than for companies operating in the country's Export Processing Zones (EPZs).

Tax losses

Income tax losses can be carried forward indefinitely subject to the ring fencing rules. The offset of tax losses carried forward is limited to 70% of current year profits, and any remaining balance can be carried forward for companies in the upstream, midstream and downstream activities. A change of control may also lead to losses incurred prior to the change no longer being permitted for deduction.

Research and development

A tax deduction in respect of R&D expenditure is limited to improvement of business products or processes and agricultural improvements.

E. Withholding taxes

Technical services

Effective from July 2014, the WHT regime that applies to the mining sector in relation to resident providers of technical services and management fees has been extended to the oil and gas sector. Under this regime, a 5% WHT is to be deducted from payments to resident providers of technical services and for management fees; this WHT is a final tax. In the case of a nonresident technical services provider, the WHT rate is 15%.

The Petroleum Act, 2015, mentions WHT on interest on loans. The party financing the petroleum operations is considered a subcontractor and shall be subject to WHT on the interest payment on the loan. PURA shall give approval for the percentage of the loan to be used as a portion of the total capital. The rate for the loan shall not exceed the lowest market interest rate available for such loans.

Dividends

Dividends paid by a Tanzanian entity are subject to WHT at a rate of 10%; the tax is due on an accrual basis. However, companies listed on the Dar es Salaam Stock Exchange pay WHT at a reduced rate of 5%, and the same rate applies to resident recipient companies that own at least 25% of the voting capital of the payer of the dividends.

WHT on dividends is deducted at source and is a final tax.

Interest and royalties

Interest and royalties paid to nonresidents are subject to a final Tanzanian WHT of 10% and 15%, respectively, unless altered by a relevant double tax agreement. If a resident strategic investor pays interest to a nonresident bank, the interest is exempted from WHT.

Branch remittance tax

A branch remittance tax (i.e., repatriated income of a domestic permanent establishment (PE)) is applicable at a rate of 10%. Repatriation of branch profits can be effected freely without any restrictions.

F. Financing considerations

Thin capitalization

The total amount of interest deduction (for corporations that are 25% or more foreign-owned for a year of income) is limited to the sum of interest with respect to debt that does not exceed a debt-to-equity ratio of 7:3.

G. Transactions

Asset disposals

Disposal of a depreciable asset that is wholly and exclusively used in petroleum operations is treated as business income. The gain is determined as the difference between the tax written-down value and the consideration price and taxed at a corporate tax rate of 30%.

Farm-in and farmout

Under a PSA, an entity may assign or transfer to a corporation or firm any of its rights, privileges or obligations, provided that the Government is notified and given written copies of the assignments and agreements. Any assignment shall be binding to the assignee.

In principle, disposal of a petroleum right after commencement of production is treated as business income and taxed at a corporate tax rate of 30%. However, disposal of a production right (farmout arrangement) before commencement of production is deemed as an investment asset, and the PSA holder is liable to income tax at the rate of 30% payable by way of a single installment. In addition, if a petroleum right is realized together with other assets used in petroleum operations or if a petroleum right is realized in part, the expenditure, costs and amounts derived from the realization should be apportioned.

There is a requirement to pay a transfer fee (or assignment fee) based on the amount of the consideration. In particular, the Model PSA 2013 prescribes a transfer fee on the consideration as indicated below:

- For every dollar of the first US$100 million: 1%
- For every dollar of the next US$100 million: 1.5%
- For every dollar thereafter: 2%

Selling shares in a company (consequences for resident and nonresident shareholders)

Share transfers in a Tanzanian company are subject to CGT (disposal of a domestic investment asset). An installment is payable for registration of the transfer (10% of the gain in case of a resident seller, 20% of the gain in case of a nonresident seller — which is credited against the final tax payable). The installment paid by individuals is the final tax; for entities, the tax rate is 30%.

Effective from July 2012, indirect share transfers may be taxed. If the underlying ownership of an entity changes by more than 50% as compared with the ownership at any time during the previous three years, the entity is treated as realizing any assets owned and any liabilities owed by it immediately before the change.

H. Indirect taxes

VAT

Tanzania has enacted a VAT Act, 2014, effective from 1 July 2015. Under the VAT Act, all persons who make taxable supplies of goods and services and whose turnover in any given year is TZS100 million or more must register for VAT. The standard rate of VAT is 18% for all taxable goods and services, including the importation of taxable goods and services.

VAT is a multistaged tax that applies at each transaction point throughout the supply chain.

All exported goods are zero-rated. Supply of services are zero-rated if the customer is outside Tanzania and effectively uses and enjoys the services outside of Tanzania.

Special relief schedule has been abolished. Special relief is retained for taxable persons who have concluded a binding agreement relating to exploration and prospecting of minerals, oil and gas with the Government of Tanzania before commencement of the VAT Act, 2014, i.e., 1 July 2015.

Both Tanzania-resident and nonresident entities engaged in the oil and gas industry may be subject to VAT on services and products supplied. However, exemption of VAT is granted on import of goods by a registered and licensed explorer or prospector for the exclusive use in oil, gas or mineral exploration or prospection activities to the extent that those goods are eligible for relief from customs duties under the East African Community Customs Management Act, 2004. Also, supply and importation of certain petroleum products (like petrol, diesel, kerosene and liquefied natural gas) are exempted from VAT.

VAT applies to all taxable supplies of goods and services made or imported by a taxable person who carries on economic activity in Tanzania. Financial services, other than health and life insurance, are no longer exempt unless supplied free of charge.

Intending traders are allowed by the VAT Act to be registered with VAT after completing the required conditions. A registered person may recover the VAT charged on goods and services acquired for the person's economic activity as an input tax. Input tax is generally recovered by being offset against VAT payable (output tax) on taxable supplies.

Import duties

All goods, equipment and materials entering Tanzania from overseas are subject to customs import duties, unless specifically exempt. The general rate of customs duty applied to the customs value of imported goods ranges from 0% to 25%.

However, special exemptions apply for companies engaged in the exploration and prospecting of oil and gas in relation to imported capital equipment and other items necessary for the oil and gas business. In addition, Tanzania is a member of the South African Development Community (SADC). Goods imported from member states that enter Tanzania with the accompanying certificates of origin are subject to import duty at the rate of 0%.

Based on the Finance Act, 2015, from 1 July 2015, Tanzania started to impose the Railways Development Levy (RDL) at the rate of 1.5 % imposed on customs value on imported of goods.

Export duties

There are no duties applied to goods exported from Tanzania except for raw cashew nuts and raw hides and skins.

Excise duties

Excise duty is levied on some goods manufactured in Tanzania, such as soft drinks, beer and tobacco, and on selected imported goods, including petroleum products. Excise duty at the rate of 10% is levied on charges and fees raised by financial institutions as well as telecommunication services providers for money transfer services.

Stamp duty

Stamp duty applies to specified transactions. Generally, a stamp duty is imposed under different heads of duty, the most common being stamp duty on lease agreements and the most significant being conveyance duty on the transfer of property (e.g., land, buildings, certain rights, goodwill).

Stamp duty differs depending on the types of instruments or transactions. Stamp duty on transfers/conveyances is at a rate of 1% of the consideration given.

I. Other

Pay as you earn (PAYE)

Resident individuals, including expatriates, are taxed on their worldwide income based on the resident tax rates, while nonresidents pay tax on Tanzanian-sourced income only. The resident minimum tax rate is 9%, and the maximum is 30%, while the nonresident tax rate is 15% on employment income and 20% on other income. Employers have the responsibility to withhold and pay the tax due from employees' entire remuneration on a monthly basis.

Skills development levy

Employers are obliged to pay a 4.5% skills development levy based on the monthly gross remuneration for all employees (excluding benefits in kind). This requirement applies to employers with a minimum of four employees.

Workers' Compensation Fund (WCF)

Under the Workers' Compensation Act, 2008, all employers are required to contribute to the WCF. All employers from the private sector shall contribute 1%, and the employer from the public sector shall contribute 0.5% of their annual bill for the period of one year from 1 July 2015. Contributions (also known as tariffs) shall be remitted on a monthly basis.

National Social Security Fund

It is mandatory for all employees, including expatriates, to register and contribute to one of Tanzania's national social security schemes. The common scheme in Tanzania is the National Social Security Fund (NSSF).

The NSSF is a pension scheme that requires employees to contribute 10%, and employers to contribute 10%, of the employees' monthly gross salaries.

Local municipality council services levy

The local municipal authorities impose a service levy, at a rate of 0.3% of turnover or sales, payable on a quarterly basis.

Double tax treaties

Tanzania has double tax treaties with the following countries: Canada, Denmark, Finland, India, Italy, Norway, South Africa, Sweden and Zambia. Several treaties are being negotiated. The East African Treaty is pending ratification. The following tax rates are stipulated in the treaties:

	Dividends %	Interest %	Royalties %
Canada	10%	15%	20%
Denmark	10%	12.5%	20%
Finland	10%	15%	20%
India	10%	12.5%	20%
Italy	10%	12.5%	15%
Norway	10%	15%	20%
South Africa	10%	10%	10%
Sweden	10%	15%	20%
Zambia	0%	0%	0%
Non-treaty countries	10%	10%	15%

Thailand

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Thailand's oil and gas fiscal regimes are classified as Thailand I, Thailand II and Thailand III regimes. Each regime incorporates different benefit-sharing structures.

- Royalties – 5% to 15%[1]
- Bonuses – Progressive rate[2]
- Production sharing contract (PSC) – 50%[3]
- Income tax rate – 50%[4]
- Investment incentives – TH, O[5]

B. Fiscal regime

The fiscal regime that applies in Thailand to the petroleum industry consists of a combination of petroleum income tax, production sharing and royalties. Annual bonus and special remuneration benefits (SRBs) also apply to petroleum concessions granted under the Thailand II and Thailand III regimes, respectively.

Petroleum income tax

Companies engaged in petroleum exploration and production in Thailand are subject to petroleum income tax at the rate of 50% of annual profits in lieu of corporate income tax (CIT), which is imposed under general tax laws. Petroleum income tax is regulated under the petroleum income tax law.

Taxation consequences are classified according to the regimes commonly known within the oil and gas industry as the Thailand I, Thailand II and Thailand III fiscal regimes. Each regime incorporates different benefit-sharing structures (see below for details).

1 *For petroleum concessions granted under the Thailand I and Thailand II regimes, 12.5%; and 5% to 15% under the Thailand III regime.*

2 *Petroleum concessions granted under the Thailand II regime are subject to an annual bonus at progressive rates.*

3 *PSCs apply only to contractors that operate in the Malaysia–Thailand Joint Development Area (JDA).*

4 *The income tax rate for projects in the JDA is 0% for the first eight years, 10% for the next seven years and 20% thereafter.*

5 *TH: tax holiday; O: other — deepwater incentives (depth greater than 200 meters).*

Ring fencing

Ring fencing applies in respect of projects taxed between Thailand I, Thailand II and Thailand III regimes, as described next.

Thailand I regime

The majority of the concessions awarded prior to 1982 are subject to the Thailand I tax regime. Benefits are shared in the following manner:

Royalty	12.5% of the value of petroleum sold.
Petroleum income tax	50% of annual profits; taxable profit is subject to ring fencing; all projects in Thailand I and Thailand II can be offset against one another but cannot be offset with projects in Thailand III

Thailand II regime

Petroleum concessions under the Thailand II regime are awarded in conjunction with an announcement from the Industry Ministry. They are subject to the following benefit-sharing structure:

Royalty	12.5% of the value of petroleum sold.
Annual benefits	The petroleum concessionaire undertakes to limit deductible costs and expenses to no more than 20% of annual gross revenue, or annual benefits are paid to the Government for the excess portion of deductions claimed
Annual bonus	Concessionaire pays an annual bonus to the Government at progressive rates, which depend on production volume
Petroleum income tax	50% of annual profits; taxable profit is subject to ring fencing; all projects in Thailand I and Thailand II can be offset against one another but cannot be offset with projects in Thailand III

Thailand III regime

Petroleum concessions awarded after 14 August 1986 are subject to the Thailand III fiscal regime. This regime also applies to petroleum concessions where the concessionaire has exercised an option to be regulated by the Thailand III regime. The benefit-sharing structure can be characterized as follows:

Royalty	Sliding scale (5% to 15% of the value of petroleum sold) based on production levels, calculated on a block-by-block basis
Special remuneration	The concessionaire pays SRBs to the Government based on a percentage of annual petroleum profit; the percentage can vary from 0% to 75%, depending on annual revenue per meter drilled.
Petroleum income tax	50% of annual profits; a midyear income tax payment (50% of projected annual tax) is also required; taxable profit is subject to ring fencing; all projects in Thailand III can be offset against one another, but cannot be offset with projects in Thailand I and Thailand II

Accounting period

The first accounting period officially commences on the date of the first sale or disposal of petroleum, subject to a royalty. Effective from that date, the company has a duty to file petroleum income tax returns and pay any tax due.

The accounting period is 12 months. Nevertheless, under the following circumstances an accounting period may be shorter than 12 months:

- For the first accounting period, when the company can choose any year-end date
- When the company ceases operations
- When the Director-General of the Revenue Department permits a change to the year-end date

If a company transfers its assets or rights relating to petroleum operations to another party prior to the commencement of the first accounting period, the law considers the transfer date to be an accounting period for the purpose of this transitional situation (commonly known as a "one-day" accounting period). The company is then required to file an income tax return and pay any income tax due on the transfer transaction.

Determination of profit

Petroleum income tax is levied on annual profits, based on taxable revenues less deductible expenses. "Taxable revenues" include revenue from the sale of petroleum,[6] the value of the petroleum disposed, the value of petroleum delivered in lieu of a royalty, revenue from the transfer of assets or rights relating to petroleum operations and any other revenue arising from petroleum operations (e.g., interest on surplus funds deposited with financial institutions in a savings deposit or similar account).

"Tax-deductible expenses" generally include expenses that are normal, necessary and not excessive and that are paid in total, specifically for petroleum operations, regardless of whether they are paid inside or outside Thailand. Capital expenditures (inclusive of pre-production expenditures and losses incurred prior to the first accounting period), surface reservation fees and income tax, and penalties and surcharges imposed under the petroleum income tax law are not deductible. A deduction for expenditures of a capital nature is available in the form of depreciation expenses (see below).

Inventory valuation

Closing or ending inventory may be valued either at cost or at the lower of cost or market value. The accounting method used to determine the cost may not be changed unless permission is obtained from the Director-General of the Revenue Department.

Foreign currencies

Foreign currency transactions must be translated into Thai bahts (THB) at the rates of exchange on the transaction dates. Assets and liabilities denominated in a foreign currency remaining at the year-end date are translated into bahts at the latest average buying or selling rate (as appropriate), as announced by the Bank of Thailand.

Donations

Donations to public charities are limited to 1% of taxable profit, after deducting any tax loss carried forward.

6 *The term "petroleum" includes crude oil, natural gas, natural gas liquid, by-products and other naturally occurring hydrocarbons in a free state, whether solid, semisolid, liquid or gaseous; it includes all heavy hydrocarbons that can be recovered at source by thermal or chemical processes but does not include coal, oil shale or other kinds of rocks from which oil can be extracted by application of heat or chemical process.*

Tax return filings and payment

Annual tax return

A concessionaire must file a petroleum income tax return (Por Ngor Por 70) and pay the related tax within five months after the year-end date. The tax return must be accompanied by the audited financial statements for that year. If the concessionaire holds both Thailand III concessions and non-Thailand III concessions (i.e., Thailand I or Thailand II or both), it is required to file two separate tax returns: one return for profits generated from the Thailand III concessions and the other for profits generated from Thailand I or Thailand II concessions, or both.

Half-year tax return

In addition to filing the annual return, concessionaires holding petroleum concessions under the Thailand III regime must file a midyear tax return and pay half of their projected annual income tax within two months after the midyear. This requirement does not apply to concessionaires holding only Thailand I and Thailand II concessions. The interim tax is creditable against the annual tax payable at the end of the year.

Production sharing contracts

PSCs apply only to contractors that operate in the Malaysia-Thailand Joint Development Area (JDA), which is governed under the Malaysia-Thailand Joint Authority.

Annual profits arising from the exploration and exploitation of any petroleum in the JDA are exempt from income tax for the first eight years of production, subject to income tax at a rate of 10% for the next seven years and thereafter at a rate of 20%. If the contractor is subject to tax in Malaysia, the tax payable is reduced by 50% of the amount of the tax charge.

The primary features of PSCs are:

- Royalty — 10% of gross production of petroleum
- Notional expenditure — 50% of gross production of petroleum is treated as a notional deductible expenditure
- Share profit — the remaining portion of gross production of petroleum after deducting royalty and notional expenditure is divided equally between the Joint Authority and the contractor
- R&D contribution — 0.5% of both the notional expenditure and the share profit must be paid to the Joint Authority

Royalty regimes

Petroleum royalties are collected under the Petroleum Act. Royalties are applied to both onshore and offshore production. The royalty can be paid in cash or in kind, and the rate is likely to differ between the Thailand I and Thailand II regimes and the Thailand III regime.

Royalty rate for Thailand I and Thailand II regimes

If the royalty is paid in cash, it is generally levied at a rate of 12.5% of the value of the petroleum sold or disposed of.

If the royalty is paid in kind, a volume of petroleum equivalent in value to one-seventh of the petroleum sold or disposed of, or equivalent to 14.28% of the gross revenue, is payable in kind.

The royalty paid on products sold domestically cannot be treated as a tax-deductible expense; however, the royalty payable in respect of exported crude oil qualifies as a tax-deductible expense.

The royalty payable on products sold domestically under the Thailand I and Thailand II regimes is creditable against income tax but may not exceed the tax payable.

Royalty rate for Thailand III regime

If the royalty is paid in cash, a sliding scale determines the amount of the royalty payable. The scale is as set out in the table below.

Monthly sales volume	Rate %
0–60,000 barrels	5.00
60,001–150,000 barrels	6.25
150,001–300,000 barrels	10.00
300,001–600,000 barrels	12.50
More than 600,000 barrels	15.00

The volume of royalty paid in kind is equivalent in value to the royalty paid in cash, as set out above.

A deep-sea, offshore exploration block (deeper than 200 meters) is subject to only 70% of the royalty that would otherwise be payable according to the table above.

Royalties charged on both domestic and export sales qualify as tax-deductible expenses but may not be used as a tax credit.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Capital allowances

"Capital expenditure" in this context is defined as expenditure incurred for the purpose of acquiring assets or benefits, whether directly or indirectly, if such assets or benefits aid the business for a period of more than one year. It includes expenditures and losses incurred prior to the first accounting period, which are to be depreciated at rates not exceeding the prescribed rates.

The rates are as set out below.

Type of asset	Rate % per year
Buildings:	
Durable building	5
Temporary building	100
Aircraft and accessories	33.33
Cost of acquiring concession and petroleum reserves	10
Cost of acquiring lease rights:	
No agreement or renewable	10
Limited lease period	Lease period
Other capital expenditures not mentioned above:	
Tangible capital expenditures	20
Capital expenditures for deep-sea exploration blocks (deeper than 200 meters)	20
Intangible capital expenditures incurred by a company that entered into a gas sale agreement with Petroleum Authority of Thailand before 1979	20
Others not stated above	10

D. Incentives

Tax holiday

A contractor that conducts exploration in the JDA and signs a PSC with the Joint Authority is granted a tax holiday for the first eight years of production.

Tax losses

Tax losses incurred may be carried forward for 10 years. The 10-year period begins at the same time as the first accounting period, and a one-day accounting period (see Section B) is not counted as an accounting period for this purpose. No carryback of losses is allowed.

Regional exploration incentives

A concessionaire pays a royalty equal to 70% of the full royalty that would otherwise be payable for the petroleum produced from a production area within a designated offshore exploration area. An offshore exploration area is an exploration block, designated by the Department of Mineral Fuels, that has a water depth in excess of 200 meters. The offshore deepwater block is allowed to deduct capital expenditure at the rate of 20%.

E. Withholding taxes

Dividends and profit remittance tax

Generally, dividends and remittance profits paid to overseas shareholders are subject to a 10% withholding tax (WHT). However, dividends and remittance profits distributed from profits incurred from petroleum income are exempt from income tax and WHT.

Interest

Interest paid to a company located overseas is subject to a 15% WHT. However, if the overseas country has a tax treaty with Thailand and the receiver is a financial institution, the rate may be reduced to 10%.

Royalties and technical service

Under Thai tax law, a resident entity is required to deduct 15% WHT on royalties or technical services paid to overseas residents. However, the rate may be reduced to 5%, 8% or 10% depending on the type of royalty and the particular countries involved.

F. Financing considerations

Thailand does not have thin capitalization rules. However, interest is not treated as a deductible expenditure for petroleum income tax calculation purposes.

G. Transactions

Asset disposals and farm-in and farmout

Transfer between unrelated parties

If a concessionaire transfers its assets or rights relating to petroleum operations to another party, the concessionaire must determine the profits on that transfer; the concessionaire is subject to petroleum income tax on the profits at the rate of 50%. Such profits are calculated as the excess of the transfer price over the net book value of the assets or rights transferred. Profits are, however, deemed to be "earned" only if cash or benefits are paid as consideration for the transfer.

Accordingly, profits are not deemed to be earned under a farm-in arrangement. This condition is based on the Petroleum Income Tax Act (PITA), which expressly states that if a new participant in a concession is required to incur expenses for the purpose of petroleum exploration and development in order to acquire a petroleum interest but such expenses are not paid to the existing participants, these expenses are not regarded as income of the existing participants.

Transfer between related parties

If the transfer is made between related parties (i.e., a parent company and its subsidiary company or between two fellow subsidiaries with a common parent company), it is deemed that neither profit nor loss arises from the transfer. The purchaser inherits the seller's cost base, such that any taxable gain or loss is effectively deferred until the asset or interest is sold outside the group.

Selling shares in a company

Profits incurred from share disposals between Thai resident companies are subject to CIT in Thailand at the rate of 20%. Profits incurred from share disposals between nonresident companies are not subject to Thai tax. However, a gain arising from the sale of shares by a nonresident to a Thai resident is subject to Thai WHT at 15%, unless the gain is protected by the relevant tax treaty.

H. Indirect taxes

Import duties

Equipment brought into Thailand for use in petroleum operations is exempt from import duty and VAT if it is brought by a concessionaire or a direct contractor.

VAT

VAT is levied on the value added at each stage of production and distribution, including servicing. The current rate is 7% of the domestic sale or service. VAT on exports is imposed at the rate of 0%.

A VAT registrant is obliged to submit VAT on a monthly basis by the 15th day of the month following the supply subject to VAT. VAT paid by a supplier of goods or services (input tax) is credited against VAT collected from customers (output tax). The excess of VAT claimable over VAT payable can be refunded in cash or carried forward to offset any future output tax. Goods sold or services provided in the JDA are exempt from VAT.

Export duties

Export duties are only levied on some specific products prescribed by the Customs Department, such as rice, wood and rubber.

Excise duties

Excise duties are levied on some products manufactured in Thailand, such as cars, electricity products, drinks, liquor and tobacco. Refined products are subject to excise tax, and the rate depends on the type of the product. Crude oil is not subject to excise tax.

Stamp duty

Thailand imposes a stamp duty of 0.1% on the total remuneration or value of service contracts if the service contract is concluded in Thailand or is concluded outside Thailand but brought into the country at a later date. If the agreement is signed within Thailand, the liability to pay the stamp duty arises when the agreement is executed, and the stamp duty must be paid within 15 days after execution. However, if the agreement is executed outside Thailand, it is subject to stamp duty within 30 days after the agreement is brought into Thailand.

Registration fees

The concessionaire is subject to the following registration fees:

- Application fee — THB50,000 per application
- Surface reservation fee — THB200,000 per annum
- Demarcation survey fee — THB500 per kilometer, or a fraction thereof
- Boundary mark onshore — THB1,000 per mark

I. Other

Companies that engage in petroleum exploration and production in Thailand are governed by two principal laws: the Petroleum Law and PITA. Petroleum companies are also governed and regulated by the Department of Mineral Fuels within the Ministry of Energy. Since petroleum companies are not regulated under the Foreign Business Act, they can be wholly owned by a foreigner without obtaining a business license from the Ministry of Commerce.

Trinidad and Tobago

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

Companies engaged in upstream operations in Trinidad and Tobago (T&T) are subject to a special fiscal regime, principally governed by the Petroleum Taxes Act (PTA). In summary, the following taxes, levies and imposts apply to companies engaged in the exploration and production of oil and gas:

- Petroleum profits tax (PPT) — 50% of taxable profits (petroleum operations in deepwater blocks: 35%)
- Unemployment levy (UL) — 5% of taxable profits
- Supplemental petroleum Tax (SPT) — the applicable rate of tax is based on the weighted average crude price and is applied to the gross income from the disposal of crude oil, less certain incentives (see Section B); not applicable on gas sales
- Petroleum production levy (PPL) — lower of 4% of income from crude oil or the share of the subsidy prescribed by the Ministry of Energy and Energy Industries (MOEEI) for producers of more than 3,500 barrels of oil per day (BOPD) or proportionate share of local petroleum subsidy
- Petroleum impost (PI) — proportionate share to defray expenses of the MOEEI
- Royalties — 12.5% of crude oil and natural gas won and saved from the licensed or contract area (see Section B)
- Green fund levy (GFL) — 0.3% of gross revenue[1]
- Capital allowances — D, U[2]
- Investment incentives — L[3]

B. Fiscal regime

Upstream

Generally, companies engaged in business activities in T&T are subject to corporation tax at a rate of 30% on chargeable profits.[4] Companies engaged in the business of manufacturing petrochemicals, liquefying natural gas and transmission of natural gas are subject to corporation tax at the rate of 35%.

1 *Effective 21 January 2016.*
2 *D: accelerated depreciation; U: capital uplift or credit.*
3 *L: losses can be carried forward indefinitely (only with regard to PPT).*
4 *Effective income year 2018.*

Companies engaged in upstream operations in T&T are subject to a special fiscal regime, principally governed by the PTA.

An entity engaged in the business of exploring for, and the winning of, petroleum in its natural state from the underground reservoir in T&T, on land or in a marine area, must do so either under an exploration and production license (license) or a production sharing contract (PSC).

Companies engaged in upstream petroleum operations are subject to various taxes, levies and imposts, of which the most significant are PPT of 35%/50%, UL of 5% and SPT at rates based on the weighted average crude oil price.

Generally, businesses operating under a license may be consolidated for tax purposes; however, those conducted under a PSC are ring-fenced (with the exception of the 2006 PSC, also referred to as the tax-paying PSC).

PSCs, with the exception of tax-paying PSCs, mandate that the Government of Trinidad and Tobago (GOTT) settle the T&T tax liabilities of the operations out of the GOTT's share of profit oil or profit gas. The tax-paying PSCs require the operator to settle its own tax liabilities out of its share of profit oil or profit gas.

Petroleum profits tax

The PTA provides that PPT is payable each financial year on the profits or gains (or amounts deemed to be profits or gains) of any person accruing in or derived from T&T or elsewhere, whether received in T&T or not, in respect of, among other things, "production business."

The PTA defines "production business" as the business of exploring for and winning petroleum in its natural state from an underground reservoir. For these purposes, petroleum is defined as any mixture of naturally occurring hydrocarbons and hydrocarbon compounds. The definition of "production business" includes the physical separation of liquids from a natural gas stream and natural gas processing from a natural gas stream, produced by the production business of a person engaged in separation or processing activities. It does not include the liquefaction of natural gas.

PPT is charged at a rate of 50% on the taxable profits of any person in respect of a production or refining business. "Refining business" is defined as the business of the manufacture from petroleum or petroleum products of partly finished or finished petroleum products and petrochemicals by a refining process. PPT is charged at a reduced rate of 35% on petroleum operations in deepwater blocks. A deepwater block is a block where at least half of the acreage therein is more than 400 meters below sea level.

PPT is assessed on an annual basis, and the PPT return is due on or before 30 April of the year following the year of income. Taxes are due and payable quarterly (i.e., 31 March, 30 June, 30 September and 31 December each year).

Expenses that are wholly and exclusively incurred in the production of taxable income are deductible in arriving at the taxable profits for PPT purposes, except where specific provisions govern the treatment of expenditures.

Restrictions or limitations apply to the deductibility of certain expenses. For instance, the deductibility of management charges paid to nonresidents of T&T is restricted to the lesser of the management charges or 2% of the tax-deductible outgoings and expenses, exclusive of special allowances and such management charges.

In arriving at the taxable profits for PPT purposes, in addition to expenses wholly and exclusively incurred in the production of income, certain allowances and accumulated tax losses are also available (see Sections C and D, respectively).

Unemployment levy

The UL is charged at a rate of 5% on taxable profits as calculated for PPT purposes. In contrast to PPT, carried-forward losses cannot be carried forward for UL purposes. The UL is not deductible in the calculation of taxable profits; it is assessed on an annual basis and is payable in quarterly installments.

Supplemental petroleum tax

SPT is imposed on windfall profits, calculated on gross income from the sale of crude oil (including condensate). Income from the disposal of natural gas is not subject to SPT. The tax is charged on the gross income of marine and land operations at varying rates based on the weighted average annual crude oil price.

The rates of SPT are as follows:[5,6,7]

Weighted average crude oil prices US$	A Marine	B New field development[5]	C Land and deepwater block
0.00–50.00	0%	0%	0%
50.01–90.00	33%	25%	18%
90.01–200.00	SPT rate = base SPT rate[6]+ 0.2% (P[7] - US$90)		
200.01 and over	55%	47%	40%

In calculating the SPT liability, the following deductions, discounts and credits are allowed:

- Deduction of royalties and the overriding royalties paid from crude disposals assessed to SPT
- Sustainability incentive, which is a discount of 20% on the rate of SPT for either:
  - Mature marine oil fields[8]
  - Small marine oil fields[9]

The MOEEI must certify mature marine oil fields and small marine oil fields.

- Investment tax credit of 20% of qualifying capital expenditure incurred in either:
  - Approved development activity in mature marine oil fields and mature land oil fields
  - Acquisition of machinery and plant for use in approved enhanced oil recovery projects
- The MOEEI must certify all development activities carried out in mature marine and land oil fields and enhanced oil recovery projects.

SPT returns and applicable taxes are due on a quarterly basis.

PSCs are subject to SPT on disposals of crude oil, unless the contract expressly exempts the contractor.

5 *New fields in shallow marine areas shall be approved and certified for development by the MOEEI. "New field" means an area within the license, sublicense or contract area, consisting of a petroleum reservoir or multiple petroleum reservoirs, all grouped on or related to the same individual geological structural feature or stratigraphic conditions from which petroleum may be produced and where the total recoverable reserves are not more than 50 million barrels of oil equivalent, that comes into production after 1 January 2013, and where recoverable reserves are certified by the MOEEI before the commencement of production and the beginning of each financial year.*

6 *Base SPT rate is equal to the SPT rate applicable at the crude price range of US$50.01 to US$90.00.*

7 *P = weighted average crude oil price in US$.*

8 *Mature land oil fields or mature marine oil fields are oil fields that are 25 years or older from the date of first commercial production.*

9 *Small marine oil fields mean a field that has production levels of 1,500 barrels or less of oil equivalent per day.*

Petroleum production levy

The PPL applies to a production business only if the business produces petroleum at a daily average rate in excess of 3,500 barrels and the person is beneficially entitled to receive the proceeds of the sale of the petroleum. Petroleum for these purposes does not include petroleum in the gaseous state.

PPL is calculated as the lesser of either 4% of the income from the crude oil disposed or the share of the subsidy prescribed by the MOEEI. It is payable monthly. No deductions are available in calculating PPL.

Petroleum impost

Every licensee and party to a PSC are liable for PI in respect of all crude oil and natural gas won and saved. PI rates are determined by the MOEEI and published in the *Official Gazette.* The tax is imposed to defray the administrative cost of the MOEEI and is payable annually.

Royalties

Royalties are applicable at the rate of 12.5% of crude oil and natural gas won.[10]

The value of crude oil and natural gas for the purposes of payments of royalties shall be the net volume of crude oil and natural gas won and saves at the fair market value from the licensed or contract area.

Green fund levy

The GFL is a tax imposed at the rate of 0.3% of the gross sales or receipts of the company. It is payable on a quarterly basis.

GFL is not deductible in arriving at the taxable profits for PPT and UL purposes.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Allowances

In arriving at the taxable profit for PPT and UL purposes, the following are the allowances available.

Signature bonuses

Signature bonuses may be capitalized and written off over five years on a straight-line basis.

Production bonuses

Production bonuses are deductible when paid.

Supplemental petroleum tax

SPT is deductible when paid.

Royalties

Royalties are deductible when paid.

Work-over allowance

This allowance provides for the deduction of costs, both tangible and intangible, incurred for work overs, maintenance or repair works on completed wells and qualifying sidetracks. These costs must be approved by the MOEEI.

Dry-hole allowance

Dry-hole allowance applies to all expenditures, both tangible and intangible, incurred on a development dry hole and a dry hole.

The allowance is available in the financial year in which such development dry hole or dry hole is plugged and abandoned and certified by the MOEEI and is limited to the difference between the expenditure and capital allowances already claimed under tangible and intangible costs.

10 *Effective 1 January 2018.*

Tangible drilling costs[11]

All expenditure of a tangible nature incurred in respect of the production business carried on by any person must be capitalized, and the applicable capital allowance must be claimed. Tangible costs include costs incurred in respect of plant and machinery, related costs, import duty and installation costs. Tangible allowances are available from the year of expenditure as follows:

- Initial allowance: 50% (of costs in year one)
- Annual allowance 30% (of costs in year two); 20% (of costs in year three)

Intangible drilling and development costs[12]

All expenditure of an intangible nature incurred in respect of production business must be capitalized, and the applicable capital allowance must be claimed. Intangible drilling and development costs include all expenditure incurred in exploration operations and exclude all tangible drilling costs and acquisitions for rights. In addition, they include costs incurred in connection with working the oil wells or searching for, discovery of and winning access to deposits. The allowances granted with regard to intangible cost are as follows:

- Initial allowance: 50% (of costs in year one)
- Annual allowance 30% (of costs in year two); 20% (of costs in year three)

Exploration costs

For the period 1 January 2014 to 31 December 2017, an allowance of 100% of exploration costs was available to be claimed by the company. Where such allowance was claimed, the following could not be claimed:

- Initial/annual allowance
- Deepwater uplift
- Deep horizon uplift

From 1 January 2018, the aforementioned rates of capital allowances for intangible drilling and development costs would be applicable on such exploration costs.

Deep horizon uplift

In computing the taxable profits of a company that incurred, from 1 January 2013 to 31 December 2017, capital expenditure for the drilling of exploration wells in deep horizon[13] on land or in a shallow marine area, that company shall be granted capital allowances on its exploration expenditure calculated by reference to an amount equal to 140% of such expenditure,[14] but shall not apply to expenditure incurred for an exploration dry-hole or for finance, administrative and other indirect costs.

Deepwater allowance

The PTA provides that in computing the taxable profits of a company that incurs, on or after 1 January 2006, capital expenditure on drilling exploration wells in a deepwater block, the company is granted a capital allowance related to exploration expenditure and is computed by reference to an amount equal to 140% of the expenditure. It should be noted that the PTA defines deep water as classified by the MOEEI as that part of the submarine area that has a water depth of more than 400 meters. In addition, a deepwater block is defined as one where 50% or more of a licensed area or contract area lies in deep water.

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11 *Unrelieved allowances (prior to 1 January 2014) will continue to be claimed in the manner in which it was calculated prior to 1 January 2014.*

12 *Unrelieved allowances (in which a person has an unrelieved balance of expenditure as of 1 January 2014) shall be calculated on a 20% straight-line basis.*

13 *"Exploration wells in deep horizon" means any exploration wells drilled at and beyond a true vertical depth (TVD) of 8,000 feet on land or 12,000 feet in shallow marine areas.*

14 *Exploration work for the drilling of the wells in deep horizon shall be certified in writing by the MOEEI.*

Heavy oil allowance

This allowance is for all costs incurred on heavy oil projects (i.e., oil 18 degrees API or lower) and includes tangible and intangible drilling and development costs, as follows:

- Year one — 60% of costs
- Years two to six — 18% of costs

It should be noted that when an election is made to claim a heavy oil allowance, no additional claim may be made for tangible and intangible drilling and development costs in computing the taxable profits and tax credits in computing SPT.

Capital gains

The taxation of capital gains is not specifically addressed under the provisions of the PTA. However, other principal pieces of legislation, such as the Income Tax Act (ITA) and the Corporation Tax Act (CTA), impose tax at specified rates on "short-term capital gains." Short-term capital gains are defined as gains arising on the disposal of assets within 12 months from the date of acquisition.

D. Incentives

PPT losses

Tax losses that cannot be wholly offset against income for the same year may be carried forward and offset against income from succeeding years, without restriction. No loss carrybacks are allowed. Carried-forward losses can be carried forward only for PPT purposes.

E. Withholding taxes

Withholding tax (WHT) is levied at the source on distributions and on payments made to nonresidents (if the person or company is not engaged in trade or business in T&T).

The term "payment" is defined as a payment without any deductions whatsoever, other than a distribution, with respect to interest, discounts, annuities or other annual or periodic sums, rentals, royalties, management charges, or charges for the provision of personal services and technical and managerial skills, premiums (other than premiums paid to insurance companies and contributions to pension funds and schemes), commissions, fees and licenses, and any other such payments as may from time to time be prescribed.

In summary, WHT is levied if all of the following conditions are met:

- A payment, as defined in the ITA, is made.
- The payment is made to a nonresident of T&T.
- The nonresident is not engaged in trade or business in T&T.
- The payment is deemed to arise in T&T.

The applicable rate of WHT with regard to payments is 15%. The applicable rate of WHT on distributions made is 10%, but if the distribution is made to a parent company, the rate is 5%. However, if there is a double taxation agreement in force, the rate of WHT is the lower rate provided in the treaty, if applicable.

Branch operations

In addition to the taxes outlined above, an external company (i.e., branch of a nonresident company) that carries on a trade or business in T&T is liable for WHT at the rate of 5% on the deemed distribution of profits to its head office.

Double tax relief

If it is established that WHT applies under domestic legislation, the provisions of an applicable double tax treaty may provide relief from the domestic provision. The GOTT has successfully negotiated various double tax arrangements that seek to provide, among other things, relief from T&T tax.

The GOTT has entered into tax treaties with Brazil, Canada, China, Denmark, France, Germany, India, Italy, Luxembourg, Norway, Spain, Sweden, Switzerland, the UK, the US and Venezuela.

In addition to the above, a multilateral arrangement (the CARICOM Treaty) has also been entered into with the following members of CARICOM: Antigua and Barbuda, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines.

Unilateral relief

A credit is available to residents for foreign taxes paid on foreign-sourced income. The credit may not exceed the T&T tax payable on the underlying foreign-sourced income.

F. Financing considerations

Investment income

Interest received on bank deposits and certificates of deposits held at financial institutions in T&T, as well as interest on bonds and similar instruments, is taxable.

Dividends received from nonresident companies paid from profits not derived from or accruing in T&T are subject to tax. Dividends received by resident companies from other resident companies are tax-exempt.

Foreign-exchange controls

T&T has a floating exchange rate regime. Commercial banks and licensed foreign-exchange dealers set the exchange rate. Residents may hold foreign currencies for their own account. Profits may be repatriated without the approval of the Central Bank of T&T.

Debt-to-equity rules (thin capitalization)

In general, no thin capitalization rules apply in T&T. However, if a local company pays or accrues interest on securities issued to a nonresident company and if the local company is a subsidiary of, or a fellow subsidiary in relation to, the nonresident company, the interest is treated as a distribution and may not be claimed as a deduction against the profits of the local company.

G. Indirect taxes

VAT

Value-added tax (VAT) is taxable on the entry of goods imported into T&T and on the commercial supply within T&T of goods or prescribed services by a registered person.

The tax rate is 12.5%[15] except in the case of an entry or a supply that is zero-rated. It should be noted that natural gas, crude oil, and specified vessels and rigs used in offshore drilling and exploration are zero-rated goods and, therefore, are subject to VAT at the rate of 0%.

Companies and other businesses are required to register for VAT if their turnover exceeds TT$500,000 a year.[16]A company that is registered for VAT may recover any VAT incurred in relation to its operations.

H. Property tax

Property Tax = Annual Taxable Value (ATV) × Prescribed Rate for the Property Class

Please note the following definitions:

- Annual Rental Value (ARV) = Annual rent that particular land is likely to attract with regard to the purpose for which the land is actually used, occupied or tenanted, or where it is not actually used, occupied or tenanted, with regard to the purpose for which it is reasonably suitable
- Annual Taxable Value (ATV) = ARV less deductions and allowances
- Capital value means the sum that the fee simple (i.e., freehold interest) might be expected to realize if offered for sale on such reasonable terms and conditions as a bona fide seller would require

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15 *Effective 1 February 2016.*

16 *Effective 1 January 2016.*

The table hereunder summarizes the applicable rates for the respective Property Classes to compute Property Tax:[17]

Property class	ATV	ATV — vacant land	Rate of tax
Industrial	6% of the value of plant and machinery housed in a building[17] In the case of plant and machinery not housed in a building, the ARV is determined to be 3% of the value of such plant and machinery (value to be determined). The ATV will be determined by deducting any applicable deductions and allowances from the ARV	5% of its capital value (ARV) less any applicable deductions and allowances	6% of ATV (plant and machinery housed in a building) 3% of ATV (plant and machinery not housed in a building)
Commercial	ARV less 10%	5% of its capital value (ARV) less any applicable deductions and allowances	5% of ATV
Residential	ARV less 10%	3.5% of its capital value (ARV) less any applicable deductions and allowances	3% of ATV
Agricultural	2% of the open market capital value of the property	2% of the open market capital value of the property	1% of ATV

The Property Tax Act, 2009 was assented to by the President on 31 December 2009 and was expected to come into operation on 1 January 2010. Taxpayers have, however, benefitted from a moratorium on the payment of the tax since inception.

The moratorium on the payment of Property Taxes expired on 31 December 2015, and therefore the collection of Property Tax should have commenced from 1 January 2016 under the Property Taxes Act. Please note that at the time of publication, the Property Tax (Amendment) Bill, 2018 has been introduced in Parliament and, among other things, provides for an extension on the moratorium on the payment of Property Tax to 30 September 2017 or such later date as the Minister may declare notice. The aforementioned Bill may be subject to change during the legislative process and will become law only on assent by the President.

17 *We note that the 6% valuation methodology for plant and machinery housed in a building is based on guidance from the Ministry of Finance and is not prescribed in the relevant legislation.*

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Tunisian oil and gas tax legislation is mainly governed by the Hydrocarbons Code (HC). This is one of the main legal frameworks for oil and gas prospecting, exploration and exploitation in Tunisia.

The HC was promulgated by Law 99-93 dated 17 August 1999 and has been amended several times by the following acts:

- Law 2002-23, dated 14 February 2002
- Law 2004-62, dated 27 July 2004
- Law 2006-80, dated 18 December 2006
- Law 2008-15, dated 18 February 2008

The HC has also been amended by several decrees enacted by the State to clarify the applicability of the HC's provisions.

Prior to the promulgation of the HC, oil and gas activities were governed by Law 85-9, dated 14 September 1985. Moreover, prior to the promulgation of the HC and Law 85-9, each license had its own convention, comprising the sole legal and tax framework governing the related activities. In this respect, exploitation concessions awarded and developed prior to the effective date of the HC are excluded from the application of the provisions of the HC and the regulations issued for its implementation.

In this way, Tunisian legislation has promoted stabilization of the tax framework governing investment in the oil and gas industry. In fact, according to Article 3 of the HC and from its effective date, holders of valid prospecting or exploration permits and/or exploitation concessions granted but not yet developed are entitled to opt, with regard to such permits and concessions, for the application of the provisions of the HC and the regulations issued for its implementation. The exercise of the aforementioned option shall be subject to written notification, stamped and signed by the holder of the permit and/or exploitation concession and addressed to the authority in charge of hydrocarbons no later than six months after the effective date of the HC.

Nevertheless, the provisions of the HC are applicable to hydrocarbon licenses awarded after the promulgation of the code.

Because of the particularity of each permit or exploitation concession agreement, the following sections detail only the applicable tax rules in accordance with the HC. In this respect, the HC has defined two types of tax regimes:

- The concession regime
- Production sharing contracts (PSCs)

The main taxes applicable in this sector are:

- Corporate tax
- Royalties on production
- Registration duties
- Turnover taxes
- Local taxes

B. Fiscal regime

The fiscal regime that applies to the petroleum industry in Tunisia consists of a combination of royalties (MET), corporate profits tax and an export duty on crude oil, oil products and natural gas. Each is described below.

Royalties (MET)

An oil and gas entity is subject to the disbursement of a portion of its production, commonly referred to as royalties in respect of oil production. Generally, for gas, the royalty due is paid in cash.

The royalties production percentage should vary according to the R-factor, determined as following:

$$R = \frac{\text{Total accumulated revenues}}{\text{Total accumulated expenditures}}$$

"Total accumulated revenues" is equivalent to the total turnover for all fiscal years prior to the considered fiscal year, reduced by the sum of tax charges due or paid for all fiscal years preceding the considered fiscal year. "Total accumulated expenditures" is equivalent to the total amount of prospecting and production expenses, research and development costs and administrative costs.

All depreciation and tax charges due or paid must be excluded from the calculation of the total accumulated expenditures.

The royalties production percentage used should vary according to the nature of the hydrocarbons as follows:

For liquid hydrocarbons	
2%	R ≤ 0.5
5%	0.5 < R ≤ 0.8
7%	0.8 < R ≤ 1.1
10%	1.1 < R ≤ 1.5
12%	1.5 < R ≤ 2
14%	2 < R ≤ 2.5
15%	R > 2.5

For gaseous hydrocarbons	
2%	R ≤ 0.5
4%	0.5 < R ≤ 0.8
6%	0.8 < R ≤ 1.1
8%	1.1 < R ≤ 1.5
9%	1.5 < R ≤ 2
10%	2 < R ≤ 2.5
11%	2.5 < R ≤ 3
13%	3 < R ≤ 3.5
15%	R > 3.5

However, in the case of nonparticipation by the national oil company, ETAP, in an exploitation concession, the rate of the proportional royalty applicable to the said concession may not be less than 10% for liquid hydrocarbons and 8% for gaseous hydrocarbons.

Corporate income tax

According to Article 107.2 of the HC, for oil and gas entities, the taxable income is determined for corporate income tax (CIT) purposes in accordance with the rules set out by the Individual and Corporate Income Tax Code (ICITC).

For hydrocarbon activities, the determination of taxable income is calculated separately by the holder from its other activities in Tunisia, in accordance with Article 106 of the HC.

Enterprises and corporates subject to the CIT are subject to the social contribution of solidarity for the profit of social funds.

The social contribution of solidarity is equal to the difference between:

- The due CIT according to the legislation in force
- The due CIT according to the rates provided by the legislation in force increased with one point

The social contribution of solidarity is paid within the same deadlines and according to the same modalities prescribed for the payment of the CIT and, where appropriate, the withholding tax (WHT).

The social contribution of solidarity is applicable to incomes and profits realized starting from 1 January 2018.

Ring fencing

Tunisia applies the ring-fencing principle in determining an entity's corporate tax liability in relation to its oil and gas activities. In this respect, hydrocarbon income tax is determined separately for each concession.

Profits tax levied on taxable profit

A concession holder should maintain Tunisian tax records of its hydrocarbon activities in TND currency and in accordance with the local legislation for each concession.

Taxable profit is equivalent to nonexempt income less deductions. Nonexempt income includes sales income (determined with reference to accounting data for sales) and non-sale income (certain items are specifically mentioned in the Tax Code). Deductions include expenses to the extent that they are economically justified and documented in accordance with Tunisian legislation.

The income tax from hydrocarbon activities should be determined using a variable rate based on the R-factor, according to Article 101.3 of the HC.

The CIT rate used will vary according to the nature of the hydrocarbons as follows:

For liquid hydrocarbons	
50%	$R \leq 1.5$
55%	$1.5 < R \leq 2$
60%	$2 < R \leq 2.5$
65%	$2.5 < R \leq 3.0$
70%	$3.0 < R \leq 3.5$
75%	$R > 3.5$

For gaseous hydrocarbons	
50%	$R \leq 2.5$
55%	$2.5 < R \leq 3.0$
60%	$3.0 < R \leq 3.5$
65%	$R > 3.5$

However, in the case of participation by ETAP in an exploitation concession at a rate equal or greater than 40%, the CIT rate applicable to the profits generated from said concession is set to 50%.

During the prospecting and exploration stage, oil and gas companies will not generate any hydrocarbon activities profit.

Exploration costs incurred can be treated at the choice of the holder, either as deductible expenses in the fiscal year during which they were incurred, or capitalized and depreciated from the first fiscal year of production at a maximum rate of 30%. In general, most oil and gas companies operating in Tunisia use the capitalization method.

Development costs are deductible through the depreciation of constructed fixed assets. This is discussed in Section C below.

Export duty

Export duty (also known as Customs Service Duty, or RPD) is determined based on the price fixed every month by the Directorate General of Energy.

However, any amount paid for the RPD levied on the export of hydrocarbons produced by a company or on its behalf is considered as an advance of CIT due by the entity for the fiscal year during which the said amount was paid, or, otherwise, for subsequent fiscal years.

Production sharing contracts

Exploration permits as well as any resulting exploitation concessions are granted by the State to ETAP, within the PSC framework, as the holder of the concession for which the production will be carried out.

For its activities of exploration and exploitation of hydrocarbons, ETAP is entitled to enter into a PSC with private contractors that are able to demonstrate the necessary financial and technical potential to conduct exploration and production activities. The contractor finances at its sole risk the entirety of the prospecting, exploration and exploitation activities on behalf and under the supervision of ETAP.

In the case of production of hydrocarbons, ETAP will have to assign to the contractor a quantity of the said production within the limit of a percentage specified in the PSC to enable the contractor to recover the expenses incurred under the contract with ETAP, including expenditures incurred relating to PSC the prospecting permit (recovery oil).

In addition, and as remuneration, the ETAP assigns to the contractor a percentage of the remaining production agreed upon under the PSC (profit oil/gas). The profit oil/gas allocated to the contractor should be adjusted according to the R-factor, increased over the time the contractor has recovered all the incurred prospecting, research and appraisal, development and exploitation expenditures.

According to Article 114.1 of the HC, in consideration of the share of the production made available to ETAP after deduction of the recovery oil and profit oil/gas, the contractor shall be deemed to have paid the CIT (i.e., the contractor tax will be paid by ETAP). Such tax is set for every fiscal year to the value of the production quantities taken by the contactor as profit oil/gas.

According to the HC, the CIT due will be directly settled by ETAP on behalf of the contractor. The amount should be credited to the contractor's CIT account with the revenue authorities.

C. Capital allowances

Depreciation

For tax purposes, "depreciable assets" include assets that have a limited useful life and that decrease in value over time. In this respect, expenditures that should be capitalized consist of the following:

- Geological and geophysics studies
- Drilling costs
- Charges incurred for the installation of equipment

According to Article 111 of the HC, the annual rate of amortization should not exceed 30%.

However, for an asset retirement obligation (ARO), the holder of the exploitation concession is entitled to an allowance on the site abandonment and restoration costs. In order to be deducted from taxable income, the ARO should be provided for during only:

- The last three years for sites located onshore
- The last five years for sites located offshore

Special allowances

According to Article 109 of the HC, subject to the holder's election, the following expenses incurred may be treated either as expenses deductible from the taxable income, or capitalized and amortized annually:

- Prospecting and exploration expenses
- Dry-hole costs
- Well abandonment costs
- Drilling costs for wells producing hydrocarbons in noncommercial quantities
- Preliminary setup costs related to the startup activities of exploration and exploitation incurred in compliance with the relevant convention

D. Incentives

An oil and gas entity is entitled to build up a deductible reinvestment reserve within the limit of 20% of its taxable income to finance the following:

- Prospecting and/or exploration expenditures on the same permit and/or other prospecting or exploration permits held by the holder; however, the financing rate of the reserve may not exceed 30% of the expenditure amount
- Prospecting and/or exploration expenditures incurred in addition to initial contractual commitments on the same permit or other permits held by the holder; however, the financing rate of the reserve may not exceed 50% of the additional prospecting and/or exploration expenditure
- Expenditure for the construction of pipelines for the transportation of hydrocarbons

In this respect, the concession holder should use the reinvestment reserve to finance one of the projects realized by it, and related to one of its permits/concessions as described above.

Any reserve built up during a given fiscal year that has not been reinvested in whole or in part during the three fiscal years following the year of its buildup is subject to income tax at the rate applicable to the income from which it was built up, increased by late-payment penalties.

E. Withholding taxes

Oil and gas entities should withhold tax on payments made locally or to nonresidents. The entity should withhold tax according to the following domestic rates:

i. Payments to residents

- 1.5% on payments in consideration of goods and services, when their amounts exceed TND1,000; the rate is reduced to 0.5% for some cases (starting from 1 April 2017)
- 15% on payments in consideration of rent, fees and royalties for individuals, and 5% on fees due to entities and individuals subject to personal and corporate tax
- 10% on dividends paid to individuals (0% for resident companies)
- 20% on interest and on attendance fee
- WHT on salary determined based on the annual salary, including premiums, indemnities and other advantages in kind after deduction of 10% for professional expenses (capped to TND2,000); the income tax charge due on the annual income should be determined according to the following scale's table (applicable starting from 1 January 2017):

Annual salary (TND)	Tax rate	Effective tax rate at the upper limit
0–5,000	0%	0%
5,001–20,000	26%	19.50%
20,001–30,000	28%	22.33%
30,001–50,000	32%	26.20%
> 50,000	35%	

In this respect, the annual income tax charge should be divided by 12 to determine the monthly WHT charge.

Salary is also subject to the social contribution of solidarity for the profit of social funds. The social contribution of solidarity is equal to the difference between:

- The PIT determined based on the PIT progressive scale.
- The PIT based on a modified PIT progressive scale, by increasing with one point the tax rates applicable to each income bracket

The social contribution of solidarity is paid within the same deadlines and according to the same modalities prescribed for the payment of the PIT, where appropriate, the WHT.

ii. Payments to nonresidents

- 10% on dividends
- 20% on interest or attendance fee paid to individuals or entities
- 20% on salaries paid to nonresident employees who spent less than six months in Tunisia for occasional work
- 10% on interest paid on loans obtained from nonresident banks
- 15% for payments to unregistered permanent establishment of nonresident companies (applicable from 1 January 2016)
- 15% on other payments
    - For technical assistance; however, parent company of the holder is exempt from the WHT due for the studies and technical assistance rendered to the holder
    - For capital gains the WHT is equal to 25% (starting from 1 January 2014) of the capital gain realized, but the capital gains tax may not exceed 5% of the sales price; for nonresident individuals, the capital gains tax is 10% of the capital gain realized, but the capital gains tax may not exceed 2.5% of the sales price
- Nonresidents established in Tunisia, and exercising their activity for a period not exceeding six months, are subject to income tax or to CIT through WHT for amounts due to them under the following rates:
    - 5% of gross revenue for construction
    - 10% of gross revenues for assembly operations
    - 15% of gross revenues or gross revenue for other services

The WHT domestic rates mentioned above could be decreased by a double-taxation agreement.

The applicable rate is 25% when the beneficiary is a resident of a tax haven.

Listed by a decree, the tax havens identified are as follows: Delaware (United States); Anguilla (UK); Bermuda (UK); Cayman Islands (UK); Gibraltar (UK); Montserrat (UK); Turks and Caicos Islands (UK); British Virgin Islands (UK); Guernsey (UK); Jersey (UK); Saint-Martin (France); Saint-Martin (Netherlands); Netherlands Antilles (Netherlands); Curacao (Netherlands); Cook Islands (New Zealand); Niue (New Zealand); Antigua and Barbuda; Aruba; Barbados; Belize; Costa Rica; Dominique; Granada; Liberia; Marshall Islands; Nauru; Panama; Philippines; Saint Kitts and Nevis; Saint Vincent and the Grenadines; St. Lucia; Samoa; Uruguay; and Vanuatu.

In case the Tunisian entity (i.e., oil and gas entity) has not performed the WHT on the payment made to a nonresident, the WHT due by the Tunisian entity is calculated based on the "taken in charge" tax formula, as follows: 100 x t/100 - t (where "t" is the WHT rate due to the common regime).

F. Branch tax on the profit transfer

Tunisian permanent establishments of foreign companies (including oil and gas Tunisian permanent establishments) should pay tax of 10% on profits realized in Tunisia (such profits are assumed to be distributed for the benefit of the head offices residing outside Tunisia).

The WHT is due at the rate of 25% for establishments whose head-offices are located in tax havens. Please refer to Section E for the full list of tax havens.

The branch tax is paid in conformity with the provisions of applicable double tax treaties (which could exempt the Tunisian permanent establishment from branch tax).

The branch tax shall not be applied to private contractors under the PSC as well as to holders of concessions that are governed by the provisions of their particular agreements or contracts.

G. Financing considerations

Interest charged on loans and/or credit amounts not exceeding 70% of these investments shall be deductible only if the loans or credit amounts pertain to development investments. Interest charged on loans and/or credit amounts pertaining to prospecting and exploration investments are not considered deductible expenses.

H. Transactions

Asset disposals

The transfer of a license, in whole or in part, should not trigger any tax consequences.

According to Article 105.1 of the HC, in the case of a transfer in whole or in part of the rights and obligations resulting from a prospecting permit, an exploration permit or an exploitation concession, such transfer shall not be subject to any tax, duty or levy of any nature existing at that date or that may subsequently be created.

Moreover, according to Article 110.1.c of the HC, in the case of a transfer in whole or in part of the rights and obligations resulting from a prospecting permit, an exploration permit or an exploitation concession of hydrocarbons, the transferee may depreciate only the expenditure incurred by the transferor that has not yet been recovered or depreciated.

I. Indirect taxes

VAT

According to Article 7 of the Tunisian value-added tax (VAT) code, most goods and services are subject to VAT at a standard rate of 19%. Other services are subject to the same tax whether at a rate of 13% or at a rate of 7%, depending on the nature of the service rendered.

Oil and gas companies are, however, eligible for VAT suspension pursuant to Article 100 of the HC. This VAT suspension will only be applicable if the entity obtains a valid VAT suspension certificate provided by the local tax authority, in order to be exempted from VAT.

Import duties

Oil and gas entities are entitled to import the following goods free of duties and any other taxes, rights and levies due on imports of goods, including VAT, with the sole exception of the RPD and the royalty for electronic data processing:

- All apparatus, tools, equipment, materials and vehicles to be effectively used in prospecting and exploration activities
- Vehicles used for company transportation

This exemption is not applicable to merchandise and goods available in Tunisia of a similar quality and of a comparable price to those goods being imported.

Export duties

Please refer to Section B for export duties on hydrocarbons.

Stamp duty

Stamp duty is generally capped at an insignificant amount.

Registration fees

Oil and gas entities are subject to a fixed registration tax for the hydrocarbon exploration and exploitation convention and appendices and for the associated amendments, additional acts, particular agreements or production sharing agreements concluded pursuant to the said convention.

However, goods and services supply contracts associated with all the activities of the concession holder exercised within the framework of the said particular conventions, and dealing with the exploration and exploitation of hydrocarbons, are subject to registered fees at the rate of 0.5% of the contract value.

J. Other

Foreign-exchange controls

According to Article 127 of the HC, a concession holder or contractor (oil and gas entity) can undertake its activities as residents or as nonresidents. The holder or the contractor established under Tunisian law is deemed to be a nonresident where its share capital is held by nonresidents and subscribed to by means of importing convertible currencies for at least 66% of the share capital.

Moreover, according to the same article, subsidiaries created in Tunisia by legal entities having their registered office abroad shall be considered nonresidents with regard to exchange regulations. The said subsidiaries shall be financed through the import of convertible currencies.

During a production phase, the nonresident holder or the contractor is allowed to retain foreign sales proceeds from the export of hydrocarbons. However, if the concession holder or contractor does not have the necessary funds available in Tunisia, it will be required to repatriate to Tunisia on a monthly basis a sum equal to the amount due to the Tunisian State and in lieu of local operating expenditure.

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Tax regime applied to this country

☐ **Concession** ☐ Royalties ☐ Profit-based special taxes ☐ Corporate income tax	■ **Production sharing contracts** ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies to the petroleum industry in Uganda consists of a combination of income tax, value-added tax (VAT), Stamps Act (for transfer taxes), excise duties and production sharing agreements (PSAs).

The Petroleum (Exploration, Development and Production) Act 2013 and Petroleum (Refining, Conversion, Transmission and Midstream Storage) Act 2013 are the main laws governing petroleum operations.

The Petroleum (Exploration, Development and Production) Act 2013 provides for the following:

- Regulation of petroleum exploration, development and production activities in Uganda
- Establishment of the Petroleum Authority of Uganda to monitor and regulate exploration, development and production activities
- Establishment of the National Oil Company to manage the state's financial interests in the petroleum subsector, including the management of state participation in the sector, marketing of the country's share of petroleum received in-kind and managing the business aspects of state participation
- Regulation of licensing and participation of commercial entities in petroleum activities.
- An open, transparent and competitive process of licensing, although the act also empowers the responsible government minister to receive direct applications if the following circumstances occur:
  - No applications are received in response to the invitation for bids.
  - The application is in respect of a reservoir within a licensed block that extends into an unlicensed block.
  - Uganda's national interest would be promoted.
- Creation of a conducive environment for the promotion of exploration, development and production in relation to Uganda's petroleum potential
- Rules for efficient and safe conduct of petroleum activities — for instance, no flaring of gas is allowed beyond what is necessary for normal operation safety without approval of the minister

- Rules for the cessation of petroleum activities and the decommissioning of infrastructure:
  - Contractors will be required to prepare and submit decommissioning plans to the petroleum authority before the expiry of a petroleum production license, detailing how the affected areas will be restored.
  - Contractors will also be required to make regular payments into the decommissioning fund to enable implementation of the decommissioning plan.
  - Payments into the decommissioning fund are recoverable by the contractor as operating costs under the relevant PSA.

The major elements of the fiscal regime applicable to the petroleum industry in Uganda are as follows:

- Royalties:
  - Percentages are provided in each PSA and depend on barrels of oil per day (BOPD).
- Bonuses:
  - Most contractors are required to pay a signature bonus.
- PSA:
  - In addition to issuing licenses to licensees, the Petroleum (Exploration, Development and Production) Act 2013 provides for the entry into a PSA by licensees and the Government.
  - The PSA details specific obligations and requirements of the parties to the agreement.
  - These include work programs and financial obligations; health, safety and environment (HSE) requirements; and other data and reporting obligations.
  - Details of the various PSAs are kept confidential.
- Income tax rate — 30%:
  - Ascertaining chargeable income from petroleum operations is done on a block-by-block basis. There is no consolidation.
- Resource rent tax:
  - There is a provision for surface rentals in most PSAs.

B. Fiscal regime

Corporate income tax

A licensee and its contractors are subject to corporate income tax on their nonexempt worldwide taxable income at a rate of 30%. "Taxable income" amounts to gross income less deductions. The gross income of a licensee is the sum of its cost oil and share of profit oil and any other proceeds and credits earned from petroleum operations.

Limitation on deductions

A licensee is allowed a deduction for expenses incurred in relation to petroleum operations undertaken in a contract area in a year of income, but this amount should not exceed the cost oil derived by the licensee from those operations in the contract area for that year.

Where in a year of income the total allowable deductions exceed the cost oil arising from the operations in a contract area, the excess is carried forward to the next year of income and is deducted in that year of income against the cost oil until fully deducted, or the petroleum operations in the contract area cease.

If a licensee has a loss carried forward for more than one year of income, the loss of the earliest year shall be allowed first as a deduction.

Petroleum exploration expenditure

If the cost of acquiring a depreciable asset is treated as petroleum exploration expenditure, a person is allowed a deduction for the depreciable asset (Wear & Tear deduction) under Section 27 of the Income Tax Act. The asset is treated as belonging to a separate pool of depreciable assets, and the depreciation rate applicable to the pool is 100%.

If the cost of acquiring an intangible asset is treated as petroleum exploration expenditure, Section 31 of the Income Tax Act that provides for deductions of intangible asset expense applies to the asset on the basis that the intangible asset is amortized at the same rate as the assets of the petroleum exploration.

Other than being allowed to receive the foregoing deductions, a licensee shall be allowed other deductions for petroleum exploration expenditure in the year of income in which the expenditure is incurred.

Petroleum development expenditure

If a depreciable asset for use in petroleum development operations is acquired or constructed by a licensee before the commencement of commercial production, Section 27 of the Income Tax Act that deals with depreciation allowance deductions shall apply to the asset as if the asset were acquired or constructed at the time of commencement of the commercial production.

If petroleum development expenditure is incurred before the commencement of commercial production, deductions shall apply to the expenditure as if the expenditure were incurred at the time of commencement of the commercial production.

The amount of the deduction under the above circumstances is computed in accordance with the prescribed formula in Section 89GC (5) of the Income Tax Act.

If the cost of acquiring an intangible asset is petroleum development expenditure, the useful life of the asset is the lesser of the expected life or six years.

In any other circumstances, a licensee shall be allowed a deduction on a straight-line basis for petroleum development expenditure over the lesser of the expected life or six years.

Decommissioning expenditure

The contribution made by a licensee to a decommissioning fund in accordance with an approved decommissioning plan for petroleum operations during a fiscal year is deductible in that year. Note, the decommissioning plan must be approved under a petroleum contract.

Decommissioning expenditure in a year of income is deductible in that year of income provided that the work is not paid for, directly or indirectly, from money made available out of the licensee's decommissioning fund for the petroleum operations.

An amount accumulated in or withdrawn from a decommissioning fund to meet expenditure incurred under an approved decommissioning plan shall be exempt income. However, the following amounts in relation to decommissioning are included in the gross income of a licensee:

- An amount withdrawn from a decommissioning/rehabilitation fund and returned to the licensee
- Any surplus in a decommissioning/rehabilitation fund of a licensee at the time of completion of decommissioning/rehabilitation

Indirect transfers of interest

If there is a change in the underlying ownership of a licensee, the licensee shall immediately notify the Tax Commissioner, in writing, of the change.

If the person disposing of the interest is a nonresident person, the licensee shall be liable, as agent for the nonresident person, for any tax payable under the Income Tax Act by the non-resident person for the disposal.

Further note that the interest referred to above is a business asset for the purposes of the Income Tax Act, which would therefore have capital gains tax implications.

Tax accounting principles

A licensee must account on an accrual basis.

Except as may be otherwise agreed in writing between the Government and a licensee, and subject to the provisions of Section 89L of the Income Tax Act, all transactions shall be accounted for at arm's-length prices, and a licensee shall disclose all non-arm's-length transactions in return for a specified period, if required to do so by the Tax Commissioner.

A licensee shall, for purposes of taxation:

- Maintain accounts for a contract area in Uganda shillings (UGX) and in United States dollars (US$), and, in the case of any conflict, use the, accounts maintained in US$
- Use the exchange rates prescribed for conversion of currencies as follows:
  - The Government or a licensee shall not experience an exchange gain or loss at the expense of, or to the benefit of, the other, and any gain or loss resulting from the exchange of currency will be credited or charged to the accounts.
  - Amounts received and costs and expenditures made in UGX, US$ or any other currency shall be converted into UGX or US$, as the case may be, on the basis of the average of the buying and selling exchange rates between the currencies in question, as published by the Bank of Uganda, prevailing on the last business day of the calendar month preceding the calendar month in which the amounts are received and costs and expenditures paid.
  - In the event of an increase or decrease, one time or accumulative, of 10% or more in the rates of exchange between UGX, US$ or the currency in question during any given calendar month, the following rates will be used:
    - For the period from the first of the calendar month to the day when the increase or decrease is first reached, the average of the official buying and selling exchange rates between US$, UGX or the currency in question, as issued on the last day of the previous calendar month.
    - For the period from the day on which the increase or decrease is first reached to the end of the calendar month, the average of the official buying and selling exchange rates between US$, UGX or the currency in question, as issued on the day on which the increase or decrease is reached.

A prescribed licensee shall maintain a record of the exchange rates used in converting UGX, US$ or any other currency.

Allocation of costs and expenses

Any exploration, development or production expenditure associated with a unit development involving a discovery area that extends into a neighboring country is allocated on the basis of the petroleum reserves attributable to that portion of the discovery area located in Uganda or license or both.

Valuation and measurement of petroleum

For the purposes of determining the value of petroleum derived from petroleum operations from a contract area, the petroleum shall be valued and measured in accordance with the provisions of regulations to be presented by the minister, which shall be laid before Parliament.

Petroleum revenue returns

"Petroleum revenues" means tax charged on income derived by a person from petroleum operations, government share of production, signature bonus, surface rentals, royalties, proceeds from sale of a government share of production, and any other duties or fees payable to the Government from contract revenues under the terms of a petroleum agreement.

The procedures relating to furnishing a return of income, cases where a return of income is not required and extension of time to furnish a return of income all apply to a licensee, subject to the following modifications:

- A licensee must furnish a return for a year of income not later than one month after the end of the year.
- A licensee must furnish a return not later than seven days after the end of every month in respect of the provisional payments required under collection and recovery provisions of the law (Section 89P(B)).
- Not less than 30 days before the beginning of a year of income, a licensee must furnish a return including particulars for each calendar quarter of the year, estimated to the best of the licensee's judgment, and shall furnish updates of the return within seven days after the end of each of the first three calendar quarters in the year.
- The Tax Commissioner may require any person, whether taxable or not, to furnish a return on the licensee's behalf or as an agent or trustee of the licensee.
- In addition to a return furnished on a licensee's own behalf, the Tax Commissioner may require a licensee acting as an operator in a contract area to furnish a return in respect to that area on behalf of all licensees with an interest in the petroleum agreement.
- A return must include particulars of government petroleum revenues and other taxes prescribed by the Tax Commissioner.
- A return required for any period must be furnished whether or not government petroleum revenues or other taxes are payable for the period.
- The Tax Commissioner may make provision permitting or requiring a licensee to submit returns electronically.

In addition to a return of income, a contractor must file an annual consolidated petroleum revenue return with the Tax Commissioner at the end of each year of income, not later than 90 days after expiry of the year of income.

Application of Income Tax Act provisions dealing with assessments, self-assessments and additional assessments

The above provisions apply to a licensee subject to the following modifications:

- An assessment made by the Tax Commissioner on a licensee may relate to petroleum revenues and not just to chargeable income.

Objections and appeals relating to petroleum revenues are determined in accordance with Part VII of the Tax Procedures Code Act.

Collection of other revenues

The provisions of the Income Tax Act and the Tax Procedure Code Act relating to collection, recovery and refund of tax apply to licensees with the following modifications:

- Petroleum revenues and other taxes charged in any assessment are payable within seven days after the due date for furnishing a return.
- A licensee must, in each calendar quarter, make a provisional payment consisting of:
  - In the case of income tax, one-quarter of the licensee's estimated income tax for the year
  - In the case of petroleum revenues other than income tax, the amounts payable for the quarter under the petroleum agreement
- Unless otherwise agreed between the Government and a licensee, all payments or refunds of petroleum revenues, other than those payable in-kind, and other taxes, shall be made in US$.
- A licensee must pay petroleum revenues to the Uganda Revenue Authority (URA).
- Subject to the late payment paragraph below, "refunds" applies to refunds of petroleum revenues and other taxes payable to the Government.

- Late payment, for refunds of government petroleum revenues and other taxes payable to the Government, will bear interest for each day on which the sums are overdue during any month, compounded daily at an annual rate equal to the average rates published by the Bank of Uganda plus five percentage points.
- Where a licensee has paid government petroleum revenues in-kind and the amount payable subsequently needs to be adjusted, the adjustment will be made in cash unless otherwise agreed between the Government and a licensee.
- A payment of petroleum revenues made by a licensee will be allocated by the Tax Commissioner against amounts payable in the order in which they become due and in such a way as to minimize any interest or penalties payable by a licensee.

Failure to furnish returns

A licensee who fails to furnish a return or any other document within the time prescribed by the Income Tax Act is liable to a fine of not less than US$50,000 but not more than US$500,000.

Where a licensee convicted of an offense under the previous paragraph fails to furnish the return or document to which the offense relates within a period specified by the court, or furnishes false or inaccurate returns, that licensee is liable to a fine not more than US$100,000.

Making false or misleading statements

A licensee or person who makes a statement to an officer of the URA that is false or misleading in a material particular, or omits from a statement made to an officer of the URA any matter or thing without which the statement is misleading in a material particular, commits an offense and is liable on conviction:

- Where the statement or omission was made knowingly or recklessly, to a fine not less than US$1 million or imprisonment for a term not more than five years, or both
- In any other case, to a fine not less than US$50,000 and not more than US$500,000

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Withholding taxes

The rate of tax applicable to a participation dividend paid by a resident licensee or resident contractor to a nonresident company is 15%. The rate of "nonresident contractor" tax payable by a nonresident contactor who derives a fee for provision of services to a licensee is 10%.

A licensee is also required to withhold tax at 6% for payments aggregating to UGX1 million or more that are made to a resident subcontractor.

Withholding taxes on international payments

An entity is required to withhold 15% from a payment it makes to another entity if the payment is regarding a dividend, interest, royalty, rent, natural resource payment or management charge from sources in Uganda.

The tax payable by a nonresident person is calculated by applying the 15% rate to the gross amount of the dividend, interest, royalty, natural resource payment or management charge derived by the nonresident person.

Interest paid by a resident company regarding debentures is exempt from withholding tax (WHT) under the Uganda Income Tax Act if the following conditions are satisfied:

- The debentures were issued by the company outside Uganda for the purpose of raising a loan outside Uganda.
- The debentures were widely issued for the purpose of raising funds for use by the company in a business carried on in Uganda.

- The interest is paid to a bank or a financial institution of a public character.
- The interest is paid outside Uganda.

Uganda WHT relating to the oil and gas industry can be summarized according to the table below.

	Residents*	Nonresidents
Dividends	15%	15%
Interest	15%	15%
Royalties	6%	15%
Management and technical fees	6%	15%
Natural resource payment	6%	15%
Lease of equipment	6%	15%
Payment by government entities	6%	15%
Professional fees	6%	15%
Service fee	6%	10%

* *Licensees are designated withholding agents and required to withhold 6% tax on payments for goods or services exceeding in aggregate UGX1 million to any resident person.*

WHT on sales of assets to Uganda residents

A resident person who purchases an asset from a nonresident person shall withhold 10% tax on the gross payment for the asset.

Branch remittance tax

In Uganda, tax is chargeable on every nonresident company that carries on a business in Uganda through a branch that has repatriated income for the relevant year of income. The tax payable by a nonresident company is calculated by applying a 15% WHT to the repatriated income of the branch for the year of income. If a downstream oil and gas entity is a branch of an overseas company, it is affected by this clause, in addition to the other relevant tax clauses.

D. Indirect taxes

VAT

A VAT regime applies in Uganda. All taxable transactions (i.e., those that are not exempt) are subject to VAT. The VAT is applied at rates of either 0% or 18%.

Goods and materials imported into Uganda are generally charged for VAT at the rate of 18%. However, the VAT paid at importation is reclaimable if the Uganda entity is VAT registered. A Uganda resident entity should register for VAT and charge 18% VAT on fees for contract work, but it can recover any tax paid (input VAT) against VAT charged (output VAT). It pays the difference to the tax authorities (or can claim the difference if the input VAT exceeds the output VAT).

The VAT registration threshold is UGX150 million (equivalent to about US$75,000). However, entities trading below this threshold can choose to register voluntarily for VAT. However, under the VAT Amendment Act, 2015, notwithstanding the registration threshold requirements, a contractor undertaking petroleum operation and a person undertaking the construction of a petroleum refinery or petroleum pipeline can apply to the Commissioner General to be registered for VAT in Uganda.

Further, the tax payable on a supply made by a contractor to a licensee to undertake petroleum operations is deemed to have been paid by the licensee to the contractor provided the supply is for use by the licensee solely and exclusively for petroleum operations.

While the contractor is computing the tax payable by the licensee for the tax period, the total credit allowed to the taxable person in the tax period does not include the amount of tax that the licensee is deemed to have paid to the contractor.

A credit is allowed to the taxable person for the tax payable in respect of all *import of services made by a licensee* during the tax period.

A nonresident entity may also be required to apply for registration to comply with taxes or else comply through a tax representative. A tax representative is responsible for performing any duty or obligation imposed by a tax law on the taxpayer, including the submission of tax returns and payment of tax. In the case of a nonresident entity, tax representative means the individual controlling the person's affairs in Uganda, including a manager of a business of that person or any representative appointed by the person in Uganda. Common transactions and arrangements that have VAT implications include:

- Be a person ordinarily residing in Uganda
- Have the responsibility for doing all things required of the nonresident under the VAT act
- Be jointly and severally liable for the payment of all taxes, fines, penalties and interest imposed on the nonresident under the VAT act

Common transactions and arrangements that have VAT implications include:

- Importation of equipment and vessels
- Sale or lease of equipment in Uganda
- Sale of products in Uganda
- Asset disposals

No VAT is charged if products are exported. Thus, no VAT is charged on either crude oil or refined petroleum products that are exported from Uganda, because all exports are zero-rated for VAT purposes. To qualify as VAT-free, exports must be supported by evidence that the goods have actually left Uganda.

According to Ugandan VAT law, the supply of refined petroleum fuels, including motor spirit, kerosene and gas oil, spirit-type jet fuel and kerosene-type jet fuel, is exempt from VAT but is subject to excise duty. The supply of liquefied petroleum gas is also exempt from VAT. The supply of crude oil is, however, subject to VAT at the standard rate of 18%.

The VAT registration threshold is UGX150 million (equivalent to about US$75,000). However, entities trading below this threshold can choose to register voluntarily for VAT.

E. Customs duties

On 2 July 2009, the East African Community (EAC) *Gazette* was issued to amend the Fifth Schedule (Exemption Regime) of the EAC Customs Management Act 2004, exempting machinery, spares and inputs (but not including motor vehicles) imported by a licensed company for direct and exclusive use in oil, gas or geothermal exploration and development, upon recommendation by a competent authority of a partner state. This notice came into force on 1 July 2009.

Some imports of heavy machinery are exempt from import duties under other legislation.

Otherwise, the general rate of customs duty applied to the customs value of imported goods varies from 0% to 25%, depending on several factors, including the type of commodity and its end use, constituent material, and country of origin. Import duties apply to most imports at a maximum rate of 25% if the imports originate outside East Africa.

A WHT of 6% also applies to nonexempt imports, but this WHT may be offset against the final income tax of the importer (i.e., as an advance corporation tax). VAT at 18% is also charged on every import of goods other than an exempt import and on the supply of imported services other than an exempt service.

F. Export duties

With the exception of hides and skins and raw tobacco, there are no duties applied to goods exported from Uganda.

G. Excise duties

Excise duties are applied to some goods manufactured in Uganda, as well as petroleum products, alcohol and tobacco. Excise duties on most refined petroleum products vary between UGX200 and UGX850 per liter. Excise duty is not generally levied on goods bound for export.

H. Stamp duties

Stamp duty is charged on various legal documents and agreements (e.g., share transfers and issues). The rate of duty ranges between 0.5% and 1%, although a fixed amount of UGX5,000 may apply, depending on the subject matter.

Generally, stamp duties are imposed under different heads of duty, the most significant of which are duties on the transfer of property (e.g., land, tenements and certain rights, including rights to extract and goodwill). Plant and equipment may also be subject to duty if conveyed with other dutiable property.

A transfer of shares in a company that predominantly holds land interests may also be subject to stamp duty on the underlying land interests.

The so-called "investment trader facility," which enabled investors, upon execution of insurance performance bonds, to claim input VAT incurred before they start actual production of taxable supplies has been scrapped. Companies can register for VAT purposes, at the earliest, only three months before the expected date of production of taxable supplies and can claim input VAT incurred in only the previous six months.

The Stamp Duty on insurance performance bonds is UGX50,000 as per the Stamp Duty Act, 2014.

Payroll and social taxes

Employment income includes an employee's wages, salary, leave pay, payment in lieu of leave, overtime pay, fees, commission, gratuity and bonus, and the amount of any traveling, entertainment, utilities, cost of living, housing, medical or other allowance. The employer must deduct income tax under the Pay As You Earn (PAYE) system on a monthly basis, and it must be remitted to the URA by the 15th day of the month following the month of deduction.

The combined employer and employee contribution by a member to the National Social Security Fund (NSSF) is 15% of the total employee cash emoluments. Five percent is deducted from the employee's salary, and 10% is contributed by the employer. Employees' contributions to the NSSF are not deductible for PAYE purposes. Payments to the NSSF must be made by the 15th day of the month following the month of deduction.

I. Capital gains tax

Refer to "Indirect transfers of interest" in Section B.

J. Financing considerations

Uganda's income tax system contains significant rules regarding the classification of debt and equity instruments and, depending on the level of funding, rules that have an impact on the deductibility of interest. These rules can have a significant impact on decisions made regarding financing oil and gas projects.

Thin capitalization

Thin capitalization measures apply to the total foreign debt of Ugandan operations of multinational groups (including foreign related-party debt and third-party debt). The measures apply to Ugandan entities that are foreign controlled and to foreign entities that either invest directly into Uganda or operate a business through a Ugandan branch.

The measures provide for a safe harbor foreign-debt-to-foreign-equity ratio of 1.5:1.0. Deductions are denied for interest payments on the portion of the company's debt exceeding the safe harbor ratio.

The debt or equity classification of financial instruments for tax purposes is subject to prescribed tests under the law. These measures focus on economic substance rather than on legal form. If the debt test contained in the new measures is satisfied, a financing arrangement is generally treated as debt, even if the arrangement could satisfy the test for equity.

K. Transactions

Selling shares in a company (consequences for resident and nonresident shareholders)

A share disposal is generally subject to the capital gains test (CGT) regime if the shares are a business asset. If the transaction involves a Uganda-resident company disposing of shares at a gain, tax applies at the rate of 30%. The Income Tax Amendment Act 2010 subjects disposal of shares in a private company to capital gains under general clauses of the Income Tax Act, which also covers petroleum transactions.

Similarly, Uganda's income tax law imposes a tax on a gain derived by either a resident or a nonresident from the disposal of shares in a company whose property principally consists directly or indirectly of an interest or interests in immovable property located in Uganda.

L. National Content

There are National Content regulations in place that require licensees, contractors and subcontractors to give preference to goods and services provided by duly approved Ugandan citizens and Ugandan companies as defined within the regulations.

M. Other

Uganda Investment Authority

The Government monitors investment into Uganda through the Uganda Investment Authority (UIA). The Government's policy is generally to encourage foreign investment, and there has been a recent trend toward relaxing controls on the purchase of real estate by investors. Incentives are granted for certain levels of investment.

Domestic production requirements

Exploration entities must comply with other domestic production requirements provided for by other regulatory bodies such as the National Environmental Management Authority (NEMA), the Ministry of Energy and Mineral Development, the National Oil Company, and its proposed regulatory bodies that are yet to be set up.

Licensing oil exploration contracts

In Uganda, the Petroleum (Exploration, Development and Production) Act, 2013 provides the framework for regulating oil exploration.

An entity is required to obtain a petroleum exploration license or a petroleum production license, or both, as the context requires. The application for a license is made to the Ministry of Energy and Mineral Development. The Minister may require other information about the controlling power over the company, especially if the company is controlled by individuals resident outside Uganda. The petroleum exploration license is usually granted for four years and is renewable for two years.

If petroleum has been discovered in the contract area, the person who has made a discovery may apply for a petroleum production license over any block or blocks in that area that can be shown to contain a petroleum reservoir or part of a petroleum reservoir.

An application for a production license must be accompanied by a report on the petroleum reservoir, a development plan and any other relevant information. A petroleum production license is first granted for 25 years and is renewable thereafter.

An annual charge is made in respect of the license. The annual charge is payable upon grant of the license and thereafter on the anniversary of the grant, until termination of the license. The holder of a license is also required to pay a royalty in accordance with the license.

The Petroleum (Exploration and Production) (Conduct of Exploration Operations) Regulations S.I.150-1 sets out guidelines for offshore operations, pollution prevention and control, use of explosives, and health and safety.

The guiding principles in relation to expenditures incurred during exploration and subsequent production are governed by the PSA with the Government, represented by the Ministry of Energy and Mineral Development. An expenditure incurred during exploration is allowed, but only against production of oil. Uganda is in the process of rolling out a national policy, but the discussions have not yet been concluded.

Foreign-exchange controls

There are no foreign-exchange controls in Uganda.

Business presence

Forms of business presence in Uganda include locally incorporated companies, foreign branches and joint ventures (incorporated and unincorporated). In addition to commercial considerations, the tax consequences of each business should be taken into account when setting up a business in Uganda. Unincorporated joint ventures are commonly used by companies in the exploration and development of oil and gas projects.

Ukraine

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Tax regime applied to this country

■ **Concession**	■ **Production sharing contracts**
■ Royalties	□ **Service contract**
□ Profit-based special taxes	
■ Corporate income tax	

A. At a glance

The fiscal regime that applies to the oil and gas industry in Ukraine consists of a combination of corporate profit tax (CPT) and royalties. In addition, the following apply:

- Export duty — no duty for oil; and UAH400 per 1,000m³/metric ton (tonne) for natural gas, or 35% of the customs value if it exceeds UAH400 per 1,000m³/tonne (not levied on exports to Energy Community states)
- Bonuses — oil and gas exploration and production (E&P) permits are generally purchased at an auction. The starting bidding price of each subsoil use permit is calculated by the state, case by case, based on the amount and value of the deposit's resources. It may not be lower than 2% of the projected total net profit of a well or deposit, excluding capital investments. In certain cases (e.g., prior exploration and evaluation of deposits at the bidder's cost, the production sharing agreement (PSA) regime, or gas or oil production by joint stock companies in which 100% of shares are state-owned), there is no auction; here, the E&P permit price is the starting bidding price and, in case of PSAs, 1% of the starting bidding price calculated as stated above
- PSA — available
- CPT rate — 18%
- Domestic supply obligations — these apply to companies with 50% or larger state participation; companies in which more than 50% of the shares are contributed to the capital of other state-controlled companies, their branches and subsidiaries; and, in some cases, the parties to "joint activity" with the above entities. These entities must sell oil and gas condensate that they produce as well as liquefied gas at specialized auctions. Currently, as per the temporary Cabinet of Minister's decision, natural gas produced by the entity 100% directly or indirectly owned by the state (PJSC *Ukrgasvydobuvannia*) should be sold to a state entity, Naftogaz Ukrayiny (NAK). The requirement is valid until 1 April 2018 and may be further extended
- National oil company (NOC) — no mandatory NOC participation rules apply
- Royalties:[1]
  - Crude oil — 14% or 29%
  - Condensate — 21% or 45% (14% or 29% since 1 January 2019)
  - Natural gas — 6%–70%

1 *Adjustment coefficients may apply to the royalties' rates. Additional amounts of hydrocarbons extracted under investment projects approved by the Cabinet of Ministers that envisage an increase of extraction of mineral resources on depleted fields are taxed at 2% of the value of additional amounts of hydrocarbons.*

- Capital allowances — PD[2]
- Investment incentives — AC[3]

B. Fiscal regime

The fiscal regime that applies in Ukraine to the oil and gas industry consists of a combination of CPT, royalties, excise tax, export and import duty, value-added tax (VAT) and other taxes generally applicable to Ukrainian taxpayers.

Corporate profit tax

Ukrainian resident companies are subject to CPT on their worldwide profit at a rate of 18%. The same rate applies to profit from oil and gas activities.

There are no special tax accounting rules for oil and gas exploration and production expenses (see Section C for more details).

The profit of the companies received from business activity with coal bed methane and with derivative feedstock of coal bed methane is exempt from CPT taxation until 1 January 2020. The exempted amounts should be linked to re-equipment of the material and technical base, introduction of new technologies for extraction, degassing and use of coal bed methane and derivative feedstock of coal bed methane.

Ring fencing

Ukraine does not generally apply ring-fencing in determining a company's CPT liability in relation to oil and gas activities. Profit from one project can be offset against losses from another project held by the same Ukrainian legal entity; similarly, profit and losses from upstream activities can be offset against downstream activities undertaken by the same Ukrainian entity. Branches of foreign companies are generally taxed as separate entities for CPT purposes.

However, PSAs are ring-fenced for tax purposes.

Ukraine does not have tax consolidation or grouping rules for different legal entities.

CPT basis

CPT basis is defined as pretax financial result calculated in accordance with Ukrainian generally accepted accounting principles (GAAP)/International Financial Reporting Standards (IFRS), subject to several tax adjustments (e.g., in relation to deductions of interest, royalties, depreciation, transfer pricing).

The rules regarding recognition of oil and gas E&P expenses are not always clear and in some cases are contradictory. Depending on the types of cost, they could be capitalized and recognized for tax purposes via depreciation, treated as a tax-deductible cost of sales when oil or gas is sold, or treated as a tax-deductible cost if the project is liquidated (see below).

Under Ukrainian GAAP, oil and gas exploration costs are generally capitalized as an intangible asset in financial accounting and amortized after commercial viability of the project is determined.

Oil and gas exploration costs may also be deductible under the following circumstances:

- They are incurred prior to obtaining exploration license for a block.
- Further exploration of a block is not foreseen.

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2 *PD: partial deductibility — capital expenses may be recognized as deductible or depreciable in the same manner as in financial accounting. However, there is continuing uncertainty over treatment of certain capital expenses. Depreciation of non-production fixed assets is not deductible.*

3 *AC: decreasing adjusting coefficients to royalties are applicable to qualifying entities. Reduced royalty rates of 6%–12% are available for production of natural gas from new wells, and there is a five-year ban for raising or revoking them. Tax treatment of expenses for pilot production/further exploration at production stage is unclear.*

- Production of determined reserves is not technically possible and/or economically viable.
- The term of a license has expired and will not be extended.

Expenses for drilling dry holes are deductible. Depreciable costs are discussed in Section C below.

Transfer pricing

Ukrainian transfer pricing rules are largely in line with Organisation for Economic Co-operation and Development approach and guidelines. The arm's-length principle is applied to determine profits in the controlled transactions. The "controlled transactions" include:

- Commercial transactions with nonresident related parties
- Commercial transactions for sale of goods through nonresident commissioners
- Commercial transactions with nonresidents registered in low-tax or nontransparent jurisdictions from the list approved by the Government
- Transactions with nonresidents who do not pay corporate profit tax or are exempt from this tax and/or are not tax residents of the country where they are registered as legal entities (the list of legal forms of such nonresidents per countries shall be approved by the Government)
- Transactions between related parties that involve intermediaries that are unrelated to such parties and do not undertake significant functions, use significant assets or assume significant risk are considered as controlled for transfer pricing purposes
- Commercial transactions between a nonresident and its permanent establishment in Ukraine

The transaction is deemed to be controlled (except transactions between a nonresident and its permanent establishment) if the total annual revenue of a taxpayer exceeds UAH150 million (approximately US$5.65 million) and total annual volume of such transactions between the taxpayer and each counterparty exceeds UAH10 million (approximately US$377,000). The transaction between a nonresident and its permanent establishment is deemed to be controlled if total annual volume of such transactions exceeds UAH10 million (approximately US$377,000).

Special rules apply to the export or import of quoted goods.

Transactions with state-regulated prices, transactions where appraisal is mandatory, transactions where auction (public bidding) is mandatory, and the forced sales of collaterals are all deemed to be at arm's length.

Five methods — compared uncontrolled price, resale minus, cost plus, transactional net margin and profit split — are used for determining the arm's-length profit derived from controlled transactions.

A transfer pricing report must be filed by 1 October of the year following the reporting year. Transfer pricing documentation should be provided to the tax authorities within one month upon their request.

Production royalties

Rent payments for the use of subsoil resources for production of minerals (royalties) are payable by all subsoil users producing mineral resources in Ukraine (including during the exploration stage). Royalties on hydrocarbons are calculated as a percentage of the value of produced hydrocarbons.

The value of produced gas is determined as the average customs value of imported natural gas in the reporting period calculated by the State Fiscal Service. The value of produced oil and condensate is determined based on the average price of one barrel of Urals oil per metric ton as determined by an international reporting agency (Urals Mediterranean and Urals Rotterdam quotations). It is converted into Ukrainian hryvnia (UAH) as of the first day of the month following the reporting quarter.

The Ministry of Economy must publish the sales price of hydrocarbons determined as described above on its website by the 10th day of the month following the reporting quarter.

Royalties[4]	
Mineral resources	Rates, % of value
Oil	
Extracted from fields located entirely or partly up to 5,000 meter depth	29%
Extracted from fields located entirely below 5,000 meter depth	14%
Condensate	
Extracted from fields located entirely or partly up to 5,000 meter depth	45%
Extracted from fields located entirely below 5,000 meter depth	21%
Natural gas (any type)	
Extracted from fields located entirely or partly up to 5,000 meter depth	29%
Extracted from fields located entirely below 5,000 meter depth	14%
Extracted from offshore fields on the continental shelf or in the exclusive (sea) economic zone	11%
Extracted from fields located entirely or partly up to 5,000 meter depth and sold to the special entity authorized by the Cabinet of Ministers to accumulate natural gas for domestic consumers	29%
Extracted from fields located entirely below 5,000 meter depth and sold to the special entity authorized by the Cabinet of Ministers to accumulate natural gas for domestic consumers	14%
Extracted under the joint activity agreements (JAAs)	70%
Extracted from new wells from fields located entirely or partly up to 5,000 meter depth (except natural gas extracted under JAAs)	12%
Extracted from new wells from fields located entirely or partly below 5,000 meter depth (except natural gas extracted under	6%

Royalties are subject to adjusting coefficients as follows:

Qualifying criteria[5]	Adjusting coefficient
Extraction of off-balance-sheet gas	0.96
Extraction of off-balance-sheet oil and condensate	0.95
Extraction of mineral resources from subsidized deposits	0.01
Extraction of natural gas from fields approved by the state expert evaluation on the basis of geological explorations carried out at the taxpayer's expense	0.97

4 *Additional amounts of hydrocarbons extracted under investment projects approved by the Cabinet of Ministers that envisage an increase in extraction of mineral resources on depleted fields are taxed at 2% of value of the additional amounts of hydrocarbons (conditions apply).*

Qualifying criteria[5]	Adjusting coefficient
Extraction of oil and condensate from fields approved by the state expert evaluation on the basis of geological explorations carried out at the taxpayer's expense	0.96

Royalties for extraction of condensate will be decreased beginning on 1 January 2019 from 45% and 21% to 29% and 14%, respectively.

In addition, the Government of Ukraine introduced a ban for five years on raising royalty rates for natural gas extracted from new wells.

Recirculation gas and noncommercial coal bed methane are exempt from royalties (although conditions apply).[5]

Tax liabilities on the extraction of each type of mineral resource from one deposit during one reporting period are calculated according to the following formula:

$$\mathbf{T_l = V_{mr} \times P_{mr} \times S_r \times A_c,}$$

where $\mathbf{T}_l$ represents tax liabilities; V_{mr} stands for the amount of sales production — produced mineral resources within one reporting period (in units of weight or volume); P_{mr} stands for the value of one unit of sales production; S_r is the standard rate for royalties stipulated for oil and gas extraction activities, expressed as a percentage; and Ac is the adjusting coefficient, where applicable.

Royalties are deductible for CPT purposes.

Non-production royalties

Taxpayers that use subsoil to store oil, oil products and gas pay royalties for non-production subsoil use. For gas, the tax is calculated by applying the UAH rate to the active volume of gas that is stored in the reservoir bed. For oil, the tax is calculated by applying the UAH rate to the storage area.

Types of subsoil use	Units of measurement	Rates/per year, UAH
Use of reservoir beds for storage of natural gas and gaseous products	1,000m³ of active gas volume	0.49
Use of natural or artificial mines for storage of oil and liquid oil products	m³	

Production sharing agreements

There has been no extensive use of PSAs in Ukraine. The first PSA with a nonresident investor was concluded in 2007; three more PSAs were concluded in 2013.

Under a PSA, the state retains the title to the subsoil resources and gives the investor the right to conduct E&P of subsoil resources. Part of the oil or gas produced under the PSA is used to recover the investor's expenses (cost recovery production), and the remaining part is distributed between the state and the investor as profit production. Prior to production distribution, all extracted hydrocarbons belong to the state.

Throughout the PSA duration, the investor is subject to special tax treatment under the Tax Code. PSAs are ring-fenced for tax purposes. If the investor is engaged in business activities outside of the PSA, they are taxable under the general tax rules.

5 *More adjusting coefficients apply to the production of gas, which is sold to the special entity authorized by the Cabinet of Ministers to accumulate natural gas for the needs of consumers. Also, reductions of taxable volume of gas apply.*

Importantly, the state guarantees that the tax rules effective as of the date of signing the PSA will apply throughout its term, unless a tax is abolished or its rate decreases. In the latter cases, the new tax rules apply as they become effective. Local content rules apply to PSAs. A PSA may contain domestic supply obligations.

PSA tax registration and compliance

Both local and nonresident investors may enter into a PSA with the state (and a state-owned company if provided for under the tender conditions). Nonresidents entering into a PSA should register a representative office in Ukraine. The investor must also register the PSA as a taxpayer. A separate VAT registration is available.

If several investors participate in a PSA, they should appoint an operator for operational matters and may also appoint it responsible for tax registration, for keeping financial and tax accounting under the PSA and for accrual and discharging the taxes (except for VAT that could be administered either by operator or investors).

Taxes payable under the PSA regime

There is an exhaustive list of taxes the investor must pay under a PSA, namely:

- CPT
- VAT
- Royalties.

The investor is also obliged to administer Ukrainian payroll taxes (personal income tax (PIT) and unified social tax) and pay state duties or fees for soliciting a service or an action from government authorities or agencies. The Tax Code is ambiguous as to whether a PSA investor must pay excise tax upon the importation of goods for PSA purposes.

Payment of other taxes and duties is substituted by production sharing between the state and the investor.

The Tax Code provides for a list of events that are tax-neutral for PSA purposes, which includes (among others):

- Distribution of profit and cost recovery production or its monetary equivalent between the investor and the state; distribution of the same by the operator among investors
- Transfer of the state's share of profit production to the operator for sale
- Sale of both profit production, including the state's share, and cost recovery production (except for VAT)
- Free-of-charge use of various types of property by an investor, including money, geological and other information, data, technologies and rights granted to the investor under the law
- Transfer of the PSA-related property from the investor to the state upon expiration of the PSA or after full compensation of the property by cost recovery production; use of such property by the investor and its return to the state
- Transfer of property between the parties to the PSA and the operator when required for PSA execution
- Transfer of money/property by a foreign investor to its permanent establishment (PE) in Ukraine for PSA purposes
- Free-of-charge provision of goods, works, services or money to an investor or by an investor, including provision of fringe benefits to employees, payment of bonuses and performance of social obligations
- Relinquishment of subsoil field or its part
- Use of production for PSA purposes, including flaring, as well as loss of production as a result of PSA activities

Tax exemptions applicable to investors under a PSA do not apply to their contractors or subcontractors (except for some VAT and import/export tax incentives).

PSA taxes are paid according to special rules as outlined below.

CPT under the PSA regime

Under a PSA, CPT is payable quarterly and in cash only.

The tax basis for CPT purposes is the investor's taxable profit calculated under the following special rules:

- Taxable profit is calculated based on the value of the investor's share of profit production, less the unified social tax paid and less the investor's other expenses (including costs of works accumulated prior to the first profit production) under the PSA, provided these expenses are not subject to compensation by the cost recovery production.
- Other income from activities under the PSA is explicitly excluded from the taxable object for CPT purposes.
- The PSA parties are allowed to establish special rules for recognition of deductible expenses in the PSA. The PSA may envisage indexation of an investor's other expenses incurred prior to the first sharing of production.
- Cost recovery production may not exceed 70% of the total production under PSA within a calendar quarter. The list of expenses compensated by cost recovery production is not explicitly determined by the law; however, the cost of fixed assets, field exploration, development and production are includable as expenses that should be compensated by the cost recovery production, when incurred. The law allows cost recovery of pre-effective costs borne after the official announcement of the results of a PSA bid.
- The cost of fixed assets not covered by the cost recovery production is depreciable under general rules.
- For the investor's representative office, funds and property provided by the head office to finance the activities under the PSA are not taxable.
- If the tax basis is negative, carryforward of losses is allowed throughout the PSA duration.

Withholding tax under the PSA regime

Withholding tax (WHT) does not apply to a nonresident investor's income derived under a PSA, when remitted by its PE in Ukraine. This WHT exemption does not cover the investor's subsidiaries in Ukraine that do not qualify as investors under the PSA. Furthermore, WHT exemption does not apply to other types of Ukraine-sourced income that may be payable, i.e., to any income derived outside of the PSA.

VAT and import/export taxation under the PSA regime

The investor's/operator's sale of production derived from the PSA and of the state's share of profit production transferred to the PSA operator for sale is subject to VAT under general rules.

Importantly, the investor's VAT registration under the PSA is not subject to cancellation, regardless of the absence of supplies or purchases subject to VAT during the previous 12 calendar months.

The operator under a multiparty PSA is entitled to recognize as its VAT credit input VAT paid (accrued) by any investor or operator upon the purchase or production of goods, services or fixed assets under the PSA in accordance with approved programs and plans. The investor (operator) is entitled to an automatic VAT refund. The procedure and time frames for the VAT refund are established in the PSA.

There are several export and import tax exemptions:

- Importation of goods into the customs territory of Ukraine for PSA purposes is not subject to import taxes (except for excise tax).
- Importation of hydrocarbon raw materials, oil or gas produced under the PSA in the exclusive economic zone of Ukraine is not subject to import taxes (including VAT).
- Exportation of production acquired by the investor under the PSA is not subject to export taxes except for VAT, which is levied at a zero rate.

- Exportation by the investor of goods and other tangible assets for the performance of the PSA is not subject to export taxes except for VAT, which is levied at a zero rate (conditions apply).
- Services provided by a nonresident in the customs territory of Ukraine to the investor for the PSA purposes are not subject to VAT.

The abovementioned exemptions (except for export exemption) also apply to contractors providing goods and services for PSA purposes under contracts with the investor (conditions apply). Should the investor or contractor use the goods or services for any purpose other than the designated PSA purposes as a result of their own fault, the investor or contractor, as the case may be, will have to pay all previously saved import or export taxes.

Royalties payable under the PSA regime

The rates, payment and calculation procedure, as well as the reporting terms, of royalties are established in the PSA. However, the royalties rate may not be lower than that prescribed by the Tax Code as of the date of the PSA:

- 1.25% of the value of the extracted natural gas
- 2% of the value of the extracted oil and gas condensate

Payroll taxes under the PSA regime

Payroll taxes, namely PIT and the unified social tax, apply under the general rules of taxation. The applicability of the stability clause to payroll taxes is uncertain.

Other taxes and contributions under the PSA regime

Under PSA law and the Tax Code, the production share of the state replaces other state and local taxes.

Unconventional oil and gas

No special terms apply to unconventional oil and unconventional gas.

C. Capital allowances

Productive wells

There are no special rules for tax accounting and depreciation of productive oil and gas wells. Currently, oil and gas wells are tax-depreciable with a minimum useful life of 15 years. Since 2015, transition to these rules created various uncertainties in the treatment of wells existing before 2015.

Fixed assets acquisition and construction costs

The cost of other fixed assets is depreciable under general rules (16 groups for tangibles, with minimum depreciation terms of 2 to 20 years).

Several depreciation methods are available (straight-line, declining-balance, double-declining-balance depreciation and sum-of-the-years-digits).

Costs treated as intangibles

Certain costs (such as special license costs and geological information costs) may be treated as intangible costs and are amortized during the legally established term of use. If the title document does not provide for the term of use, the asset is amortized over 2 to 10 years, at the discretion of the taxpayer. General depreciation methods outlined above are applicable.

Successful exploration costs constitute a special type of intangibles and are amortized when production starts. As mentioned above, there is currently some uncertainty with respect to the treatment of amortization of this type of intangible asset for tax purposes.

Special allowances

There is no capital uplift or credit in Ukraine.

D. Incentives

Please refer to Sections B and H for a discussion about tax incentives — see, among others, CPT and VAT incentives for coal bed methane producers, and adjusting coefficients to royalties.

E. Withholding taxes

Interest, dividends, royalties and income from joint activity agreements and certain other kinds of Ukrainian-sourced income received by a nonresident are subject to WHT at the rate of 15%. The WHT rate on freight (or any other similar payment for carriage of goods by maritime, air, automobile or railway transport) is 6%. The tax rate on payments for advertising services provided by nonresidents is 20%, payable at the expense of the Ukrainian service recipient. There are also several WHT rates on payments for different insurance services. WHT rates can in some cases be reduced or eliminated by virtue of a double tax treaty. Certain domestic exemptions apply too.

Technical services

Technical services provided by nonresident contractors should not be subject to Ukrainian WHT, unless they fall within the definition of engineering.

If the services give rise to a PE, Ukrainian CPT will apply to a nonresident's profit under the general rules.

Branch remittance tax

There is no branch remittance tax in Ukraine. However, the law could be interpreted in a way that WHT at the general rate of 15% should apply to repatriation of Ukrainian profit of the branch to its nonresident head office.

The possibility of eliminating this tax based on a double tax treaty is uncertain.

F. Financing considerations

Thin capitalization

If taxpayer's debt to a nonresident related party exceeds taxpayer's equity by at least 3.5 times (10 times for financial and leasing companies), the interest payable to related nonresidents by such taxpayer may be deductible in an amount up to 50% of the sum of its financial result before taxation, financial expenses and depreciation according to financial accounting in the reporting year.

The remaining interest, annually reduced by 5%, may be carried forward indefinitely, subject to the same limitation.

G. Transactions

Subsoil use permit transfers

Under Ukrainian law, permits for subsoil use issued by the state to investors may not be granted, sold or otherwise transferred to any other legal entity or individual. The rights under the permit may not be contributed into charter capitals of joint ventures or into a joint activity. Thus, a sale of assets of a company does not result in the transfer of a permit for subsoil use.

However, subsidiary regulations allow changing the name of a permit holder as a result of a spin-off, resulting in a mere technical transfer of the special permit (although conditions apply).

Farm-in and farmout

Ukrainian law does not recognize farm-ins and farmouts because the permits issued by the state cannot be traded, and parts of that permit cannot be the object of any business transaction.

Historically, the most practicable way of benefiting from an existing permit held by a Ukrainian company was to enter into a "joint activity" with the permit-holding company. However, over recent years, the Ukrainian tax authorities have been threatening to invalidate joint activity agreements to which Ukrainian permit-holding companies are a party. We are not aware of cases when joint activity agreements have actually been invalidated, yet this risk should be taken into account when choosing the operating option.

A quasi farm-in may be executed via a sale of shares of the permit holder to an interested party.

Selling shares in a company

Nonresident companies that dispose of shares in a Ukrainian company are subject to Ukrainian WHT at 15% on capital gains. If the cost of shares in the hands of nonresidents is not properly confirmed, WHT could potentially apply to the entire sale proceeds. The resident buyer acts as a tax agent. WHT could be eliminated by virtue of a double tax treaty.

There is no mechanism for administering WHT where the transaction is carried out between two nonresidents with settlements outside Ukraine if no Ukrainian intermediary is involved.

Resident companies that dispose of shares in Ukrainian companies are subject to Ukrainian CPT on the margin between the share sale price and share acquisition expenses. The tax rate is 18%.

H. Indirect taxes

VAT

There is an electronic VAT administration system in Ukraine, introduced in 2015.

Domestic trading in oil and gas is subject to VAT at 20%.

Oil importation is subject to VAT at the general rate. The importer is entitled to credit input VAT for VAT paid on imports, subject to certain conditions. Exportation of oil and gas is subject to 0% VAT.

To recover VAT input incurred in connection with oil and gas E&P, an oil or gas exploration company has to be registered as a VAT payer in Ukraine. The company will be subject to mandatory VAT registration if the amount of its taxable supplies exceeds UAH1 million (approximately US$37,700). The company may voluntarily register as a VAT payer.

The oil or gas exploration company should monitor its supplies subject to VAT to maintain its VAT registration. The VAT registration can be canceled if the taxpayer's tax return does not show transactions subject to VAT during 12 calendar months (but this does not apply to parties contracted within PSAs).

Supplies of natural gas to domestic consumers, to state-funded institutions that are not registered as VAT payers and to housing companies are accounted for VAT purposes on a cash basis.

Incentives

Materials and equipment for production of alternative fuels are exempt from VAT and customs duties upon importation into Ukraine, which applies to coal bed methane as one of the alternative fuel sources. The Cabinet of Ministers of Ukraine issues the list of items that could be exempt under this rule. In addition, exemptions apply only if the importer uses these materials and equipment for its own production purposes and no identical material or equipment with similar characteristics is produced in Ukraine.

There are also a few exemptions related to the importation of equipment that operates on alternative fuels (including coal bed methane).

Import duties

Import duties on natural gas, gas condensate, and crude oil are zero-rated. However, refined products are subject to import customs duties at varying rates between 0% and 10% of their customs value.

Export duties

Ukraine imposes the export customs duties on gas exported to countries other than the members of Energy Community that are shown in the table below:

Export specification	Rate
Natural gas in a gaseous state	35% of the customs value, but not less than UAH400 per 1,000m³
Liquefied natural gas	35% of the customs value, but not less than UAH400 per tonne

Excise tax

In Ukraine, crude oil and gas are not subject to excise tax.

However, importation or first sale of locally manufactured liquefied natural gas are excisable at the rate of €3.67 per 1,000 liters, whereas importation or first sale of locally manufactured liquefied propane/propane-butane and other gases are excisable at the rate €52 per 1,000 liters.

Importation and the first sale of locally manufactured refined oil products are also excisable, at rates depending on the type of product and varying from €27 to €213.5 per 1,000 liters. Excise tax exemptions apply.

There has been an electronic fuel realization system in Ukraine since 2016.

Stamp duties

Stamp duty is levied by notaries and is generally capped at insignificant amounts, except when real estate is sold.

Registration fees

There are no significant registration fees.

I. Other significant taxes

Unified social tax

Unified social tax is levied on employees' salaries and administered by employers. The rate of employer contribution is 22%.

The tax basis for unified social tax is capped at 15 minimum wages, which from 1 January 2018 amount to UAH40,000 (approximately US$2,105).

Personal income tax and military levy

The standard PIT rate is 18% for income in the form of salary, other incentive and compensation payments, or other payments and rewards. Different rates apply in certain instances (e.g., dividends paid by CPT payers — 5%; other dividends and passive income — 18%). The employer is obliged to withhold PIT from employees' payroll and remit it to the Treasury.

The Tax Code establishes social PIT benefits that are applicable to certain categories of employees (e.g., for parents with many children, disabled people, students). Ukrainian tax residents are eligible for a tax credit if they incur certain kinds of expense during a year (e.g., expenses on mortgages, education or medical treatment). A temporary 1.5% military levy applies to the individual's income calculated in the same manner as for the PIT purposes.

Environmental tax

Ukrainian legal-entity PEs of nonresidents that perform oil and gas production activities in the customs territory of Ukraine, its continental shelf or its exclusive (sea) economic zone are subject to environmental tax if these activities cause:

- Pollution of air from stationary sources
- Pollution of water
- Waste disposal in designated places (except for recycling).

The rates vary significantly depending on the amount, nature of stationary pollutants, concentration of pollutants, object of pollution and level of hazard, etc. In 2017, tax rates for pollution of air or water, as well as waste disposal, varied from UAH0.49 to UAH3,121,217.74 per tonne of pollutant.

Property tax

Property tax is levied in the form of land tax, real estate tax (other than a land plot) and transportation tax.

Oil- and gas-producing companies are subject to property tax under general taxation rules.

Land tax rates are variable depending on the land plot, its location and its characteristics. Real estate tax is levied at up to 1.5% of the minimum monthly wage as of 1 January of the current year (approximately UAH55,85) per 1 square meter of residential and nonresidential real estate. Industrial facilities and warehouse facilities are not subject to property tax. Transportation tax is payable on the vehicles used for less than five years with average market value over 375 minimum wages established for 1 January of the reporting year (UAH1,396,126).

Royalties for special water use

Entities using water under the regime of "special water use" pay royalties for their special use of water (which includes both intake and discharge). Special use of water can be based either on a special water use permit or on an agreement. The rate of levy depends on the volume of consumed water, the water source, the region and the purpose of special water use. The levy does not apply to seawater.

Transportation royalty

Companies that manage main pipelines and provide services for transporting oil and oil products via pipelines through Ukraine pay a royalty for such transportation. This tax is mainly paid by national pipeline operators (UkrTransNafta and NAK). Royalties for transportation are calculated as a fixed rate in US$ per unit. The tax basis is the actual amount of oil and oil products transferred through the territory of Ukraine via pipelines. The tax rate is US$0.56 for transportation of one tonne of oil and oil products by pipelines. Adjusting coefficients apply to transportation royalties if the pipeline transportation tariff is changed by the Government (except for transportation of oil to Ukrainian consumers).

J. Other

Foreign-exchange controls

The official exchange rate of the hryvnia against the US dollar can be found on the website of the National Bank of Ukraine (NBU), available at www.bank.gov.ua.

The commercial exchange rate may differ from the official one. A wide variety of controls is imposed with respect to the use, circulation and transfer of foreign currency within Ukraine and abroad. These controls, which affect almost all international business transactions, include the following:

- As a general rule, transactions between Ukrainian residents and cash settlements within Ukraine may not be carried out in foreign currency. Cross-border settlements in hryvnia are allowed for a limited list of cases only.
- All statutory accounting and tax reporting, as well as tax payments, must be in Ukrainian currency.
- Wages and salaries paid to Ukrainian citizens must be in Ukrainian currency.
- Ukrainian companies must obtain an individual license (permission) from the NBU to engage in certain business transactions, including the opening of bank accounts and investing abroad.

- Ukrainian exporters must repatriate their export proceeds for goods (except intellectual property), works or transportation and insurance services within 180 days of export. Similarly, Ukrainian importers must import goods within 180 days from the moment when the payment for such goods was made. Failure to comply results in penalties. Before June 2017, this term was shortened to 120 days.
- Mandatory sale of 50% of export proceeds has been introduced as a temporary measure.

Special rules apply to PSAs.

Gas to liquids

There is no special regime for gas-to-liquids conversion. Ukraine imposes only excise tax and export duties on liquefied gas. Refer to Section H for more detailed information.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

The tax regime applied in the United Arab Emirates (UAE) for oil and gas enterprises can be summarized as follows:

- Concessions:
  - Royalties
  - Corporate income tax (CIT) — see Section B for details
- Capital gains tax (CGT) rate — see Section B for details
- Branch tax rate — not levied by the federal UAE Government nor the individual Emirates
- Withholding tax — not levied by the federal UAE Government nor the individual Emirates.

B. Taxes on corporate income

Although there is currently no federal UAE taxation, each of the individual Emirates (Abu Dhabi, Dubai, Sharjah, Ajman, Umm al Quwain, Ras al Khaimah and Fujairah) has issued corporate tax decrees that theoretically apply to all businesses established in the UAE. However, in practice, these laws have not been uniformly applied. Taxes are currently imposed at the Emirate level on companies involved in the upstream sector in the UAE (actual production of oil and gas in the UAE) in accordance with specific (but confidential) concession agreements.

The concession agreements will also stipulate whether there should be any royalties on production. Tax rates are agreed on a case-by-case basis. The tax deductibility of costs and expenses relating to oil and gas exploration, development and production, and business losses will be stipulated in the specific concession agreement. Tax payment and compliance obligations should also be included in the concession agreements.

Note that this is merely how the practice has evolved in the UAE. There is no general exemption in the law. Anyone investing in the UAE should be aware of the risk that the law may be more generally applied in the future and of the remote risk that it may be applied retroactively.

The income tax decrees that have been enacted in each Emirate provide for tax to be imposed on the taxable income of all corporate bodies, wherever incorporated, and their branches that carry on trade or business, at any time during the taxable year, through a permanent establishment in the relevant Emirate. Corporate bodies are taxed if they carry on trade or business directly in the Emirate or indirectly through the agency of another body corporate.

In 2015, the UAE Ministry of Finance (MoF) announced the potential introduction of corporate tax in the UAE. No further details have been provided with respect to the proposed tax rate or timeline. The MoF stated that after an announcement has been made that the draft law has been finalized, it will be at least 12 months before businesses will be required to fulfill their UAE corporate tax obligations. This will allow businesses to prepare for the implementation of the corporate tax.

Tax incentives

Some of the Emirates have free zones that cater to the oil and gas sector (non-production), which offer tax and business incentives. The incentives usually include tax exemptions at the Emirate level or a 0% tax rate for a guaranteed period, the possibility of 100% foreign ownership, absence of customs duty within the free zone and a "one-stop shop" for administrative services. The free zones across the Emirates include, but are not limited to, Masdar City (in Abu Dhabi), the Dubai Multi Commodities Centre (DMCC), the Dubai Airport Free Zone (DAFZ), Dubai World Central (DWC) Dubai International Financial Centre (DIFC), Dubai Internet City (DIC), Dubai Media City (DMC), Dubai Studio City (DSC) and Jebel Ali Free Zone (JAFZ). Approximately 30 free zones are located in the Emirate of Dubai alone.

Unconventional oil and gas

No unconventional oil and gas fields are currently developed in the UAE.

C. VAT

The UAE is a signatory to the 'Common Value Added Tax ('VAT') Agreement of the States of the Gulf Cooperation Council'. The UAE Government under the Federal Tax Authority ('FTA') implemented VAT with effect from 1 January 2018 and is governed by the Federal Decree-Law No. (8) of 2017 on Value Added Tax.

VAT applies on the supply of most goods and services in the UAE and on the import of goods and services. The standard rate of VAT is 5%, however there is a zero rate of VAT as well an exemption from VAT for certain supplies. The zero rate of VAT applies to certain supplies, including exported goods and services and the supply of crude oil and natural gas. The supply of refined petroleum products is subject to VAT at standard rate.

Businesses and individuals should register for VAT if their taxable turnover exceeds the threshold as specified in the Cabinet Decision No. (52) of 2017 on the Executive Regulations of the Federal Decree-Law No (8) of 2017 on Value Added Tax. The mandatory VAT registration threshold is AED 375,000 (approximately USD100,000).

D. Customs duty

The UAE is a member of the GCC Customs Union, which is based on the principle of a single entry point upon which customs duty on foreign imported goods is collected, and therefore, goods moving between the GCC Member States should not be subject to customs duty. Goods considered to be of GCC origin for customs duty purposes are treated as "national products" and should also not be subject to customs duty when moved within the GCC Member States.

Under the GCC Customs Law, most foreign imports are subject to customs duty of 5% of the cost, insurance and freight (CIF) value of imported goods. There is no customs duty on the export of either foreign or national goods from the GCC Customs Union.

UAE free zones are generally seen as foreign territories for customs duty purposes (i.e., are not considered within the scope of the GCC Customs Union). Therefore, goods manufactured within a UAE free zone are not considered to be GCC national products for GCC customs duty purposes. Goods should not incur customs duty on import into a free zone, and there is no export duty applied on goods removed from a free zone. However, if goods leave a free zone for a destination within the GCC Member States, customs duty will be levied on the import at the first point of entry into the GCC Customs Union.

Concession agreements may set out a general exemption from customs duty for goods imported into the UAE for petroleum operations.

E. Foreign-exchange controls

Neither the federal Government of the UAE nor the individual Emirates impose foreign-exchange controls.

F. Tax treaties

The UAE has the following treaties currently in force with the following jurisdictions: Albania, Algeria, Armenia, Austria, Azerbaijan, Bangladesh, Belarus, Belgium, Bosnia Herzegovina, Brunei, Bulgaria, Canada, China (mainland), Cyprus, Czech Republic, Egypt, Estonia, Fiji, Finland, France, Georgia, Germany, Guinea, Greece, Hungary, Hong Kong SAR, India, Indonesia, Ireland, Italy, Japan, Kazakhstan, Korea (South), Kyrgyzstan, Latvia, Lebanon, Lithuania, Luxembourg, Macedonia, Malaysia, Malta, Mauritius, Mexico, Montenegro, Morocco, Mozambique, Netherlands, New Zealand, Pakistan, Panama, Philippines, Poland, Portugal, Romania, Russia (limited), Serbia, Seychelles, Singapore, Slovenia, South Africa, Spain, Sri Lanka, Sudan, Switzerland, Syria, Tajikistan, Thailand, Tunisia, Turkey, Turkmenistan, Ukraine, UK, Uruguay, Uzbekistan, Venezuela, Vietnam and Yemen.

In addition, treaties with the following jurisdictions are in various stages of negotiation, renegotiation, signature, ratification, translation or entry into force: Andorra, Argentina, Barbados, Belize, Benin, Comoro Islands, Croatia, Ecuador, Ethiopia, Gambia, Guernsey, Jersey, Jordan, Kenya, Libya, Liechtenstein, Malawi, Maldives, Mauritania, Moldova, Nepal, Nigeria, Palestine, Paraguay, Peru, Senegal, Slovak Republic and Uganda.

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

The fiscal regime that applies in the United Kingdom (UK) to the oil and gas industry consists of a combination of corporation tax, supplementary charge and petroleum revenue tax. In certain circumstances, diverted profits tax could also apply.

- Corporation tax rate — 30% ring-fence (19% non-ring-fence[1]) — profits from oil and gas exploration and production are subject to the ring-fence rate
- Supplementary charge rate — 10%
- Petroleum revenue tax rate — 0%[2] (for fields that received development consent before 16 March 1993)
- Diverted profits tax — 55%, where the diverted profits would otherwise be ring-fence profits
- Capital allowances — D, E[3]
- Investment incentives — L, RD[4]

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1 *Reduced to 19% on 1 April 2017 and reducing to 17% on 1 April 2020.*

2 *While reduced to 0% from 50% with effect from 1 January 2016, refunds can still arise, e.g., on carryback of any losses arising upon end of field life decommissioning.*

3 *D: accelerated depreciation; E: immediate write-off for exploration costs.*

4 *L: losses can be carried forward indefinitely; RD: R&D incentive.*

B. Fiscal regime

Corporation tax

UK tax-resident companies are subject to corporation tax on their worldwide profits, including chargeable gains, with credit for any creditable foreign taxes.

However, exemptions apply to certain dividends, profits or losses from overseas branches and gains or losses on disposals of substantial shareholdings. The taxable profits of a UK company are based on its accounting profits as adjusted for a number of statutory provisions.

Non-UK tax-resident companies are subject to corporation tax only if they carry on a trade in the UK through a permanent establishment (PE). In general, the UK for these purposes includes UK land and territorial waters only. However, the taxing jurisdiction of the UK is extended to include income from exploration or exploitation of the natural resources of the seabed and subsoil of the UK continental shelf.

As a result, a non-UK tax-resident company that undertakes exploration or exploitation activities on the UK continental shelf is deemed to have a UK PE. The taxable profits of a UK PE are computed on the assumption that the PE is a separate entity dealing wholly independently with the nonresident company of which it is a PE.

The existence of a UK PE of a non-UK tax-resident company is subject to the application of any double tax treaty between the UK and the country of residence of the company, although the UK's double tax treaties normally preserve the UK's taxing rights in respect of exploration or exploitation activities.

A company is "UK tax-resident" if it is either incorporated in the UK or its central management and control is located in the UK. However, companies that are regarded as resident under domestic law, but as nonresident under the "tie breaker" clause of a double tax treaty, are regarded as nonresident for most tax purposes.

The current rate of corporation tax is 30% for ring-fence profits (see below) and 19% for non-ring-fence profits.

Ring fencing

For corporation tax purposes, UK exploration and production activities (both onshore and offshore) are treated as a separate ring-fence trade from other trading activities, such as refining and marketing. As a result, a company's ring-fence trading profits are calculated separately from its profits from any non-ring-fence trade. The main consequence of the ring-fence is that non-ring-fence losses may not be offset against the profits from a ring-fence trade. However, losses from a ring-fence trade can be offset against non-ring-fence profits.

Similar rules apply for capital gains purposes (i.e., non-ring-fence capital losses cannot be offset against ring-fence capital gains, but ring-fence capital losses can be offset against non-ring-fence capital gains, provided that a timely election is made).

Timing of corporation tax payments

Large ring-fence companies are required to pay corporation tax on their ring-fence profits in three equal installments based on the estimated liability for the year. For a ring-fence company with a calendar year-end, installment payments are due on 14 July and 14 October during the year and on 14 January following the year-end.

Large companies are required to pay corporation tax on their non-ring-fence profits in four equal installments, again based on the estimated liability for the year. For a large company with a calendar year-end, installments are due on 14 July and 14 October during the year and on 14 January and 14 April following the year-end.

The UK Government has announced that from 1 April 2019, the date on which "very large companies" (defined as those with annual taxable profits exceeding £20m) are required to make installment payments will be brought forward by four months. Therefore, under these revised rules, a very large company with a calendar year-end will have installments due on 14 March, 14 June, 14 September and 14 December of the accounting period to which the liability relates.

Taxation of income

Strict rules determine whether sales of oil and gas are considered to be arm's length or non-arm's length. Arm's-length sales are taxable based on the actual price realized, whereas non-arm's-length sales are taxable based on the market value of the oil or gas sold. Specific valuation rules apply in determining the market value of non-arm's-length sales, and the UK tax authorities, i.e., HM Revenue & Customs (HMRC), maintain a database of statutory values for certain common crude oil types.

Nomination scheme

Anti-avoidance provisions exist to help prevent manipulation of the tax rate differential between exploration and production activities, and other activities, by the allocation of oil sales to lower-priced sales contracts, using hindsight (a process known as "tax spinning"). In particular, in certain circumstances, these provisions require the taxpayer to "nominate" oil sales contracts within two hours of agreeing to the contract price.

Tariff receipts

In general, tariff receipts are taxed as part of a company's ring-fence trading profits for corporation tax purposes.[5]

Relief for expenditures

To be deductible for corporation tax purposes, trading expenditure must be incurred wholly and exclusively for the purposes of the company's ring-fence or non-ring-fence trade. In addition, no relief is available for qualifying trading expenditure until the company has actually commenced trading, which, in the case of ring-fence activities, is generally considered to be when a decision has been taken to develop a field. It is not considered that exploration, or the sale of a small quantity of oil as the result of unsuccessful exploration, constitutes the commencement of a trade. Most trading expenditure incurred prior to the commencement of a trade will typically qualify for relief in the period when the trade commences.

In addition, the corporation tax treatment of expenditure depends on whether it is capital or revenue in nature; this distinction depends on, among other things, the life cycle of the related fields. In particular, the exploration stage of a field mainly involves capital expenditure, including expenditure on intangible assets, such as oil licenses and drilling exploration and appraisal wells, whereas the production phase may involve a mixture of revenue and capital expenditure. At the end of the field's life, decommissioning expenditure is treated as capital in nature.

In general, revenue expenditure incurred wholly and exclusively for the purposes of the company's ring-fence trade is deductible as it is accrued, whereas relief is available for capital expenditures only to the extent that capital allowances are available (see Section C below for further details).

5 *Recent technical ambiguity had arisen as to whether all tariff receipts earned by ring-fence companies were subject to ring-fence corporation tax and supplementary charge, particularly in respect of tariff receipts arising from assets outside the scope of petroleum revenue tax. Legislation is to be introduced as part of the 2017 Winter Finance Bill [UPDATE THIS TEXT?] to amend the definition of tariff receipts to ensure no such ambiguity is possible, and all tariff receipts will be within the ring fence irrespective of whether they are charged to petroleum revenue tax.*

Targeted tax anti-avoidance legislation exists such that in certain circumstances, payments made by ring-fence oil companies on the lease of a drilling vessel, or accommodation vessel, that is employed directly or in connection with exploration or exploitation of the seabed or subsoil of the UK territorial sea or the UK continental shelf can be restricted.

Losses

The UK loss rules distinguish between different types of losses, including trading losses, finance losses and capital losses.

Trading losses can be utilized by a company against its taxable profits (of any type) in the period when the losses arose, or the losses may be carried back one year against any profits. In addition, trading losses can be surrendered to other companies in the same group to offset their profits arising in the same period. If trading losses are not used by the company in its current or prior period or surrendered to another company, they are automatically carried forward to offset future profits of that company arising from the same trade.

Additional flexibilities have been introduced for the use of trading losses arising on or after 1 April 2017 against non-ring-fence profits together with additional restrictions in the ability to use carried forward trading losses (whether arising before or after 1 April 2017) against non-ring-fence profits. In particular, Finance (No. 2) Act 2017, which received royal assent on 16 November 2017, contains provisions that allow carried forward non-ring-fence trading losses and carried forward non-decommissioning ring-fence trading losses arising on or after 1 April 2017 to be surrendered against non-ring-fence profits of other companies in the same group. At the same time, the offset of carried forward trading losses (whether arising before or after 1 April 2017) against non-ring-fence trading profits has been limited to the first £5m (on a group basis) plus 50% of the remainder. Importantly, however, these new loss relief rules do not apply to the offset of ring-fence trading losses against ring-fence trading profits.

In certain circumstances, the one-year carryback period is extended. In particular, under current legislation, losses arising in the year of cessation of trade or losses that arise from capital allowances for decommissioning expenditure (see Section C) can be carried back to 17 April 2002 for losses incurred in accounting periods beginning on or after 11 March 2008 (previously, the carryback period was restricted to three years).

Finance losses

Finance losses resulting from loan relationships can be utilized against profits in a number of ways. They can either be offset against profits of the same accounting period or non-trading profits of an earlier period or a subsequent period, or they can be surrendered to other companies in the same group in the same period by way of group relief. However, Finance (No. 2) Act 2017, which received royal assent on 16 November 2017, contains similar provisions for finance losses to that described above under the "Losses" heading, that apply from 1 April 2017. Financing costs are not generally deductible for supplementary charge or petroleum revenue tax purposes.

Capital losses

Capital losses may be offset against any chargeable gains arising in the same accounting period and, to the extent they are not fully utilized, may then be carried forward to be offset against future chargeable gains. Capital losses cannot be used to reduce trading profits or any income other than chargeable gains.

An election can be made to transfer a chargeable gain or allowable loss to another company in the same group. However, no election can be made to transfer a ring-fence chargeable gain accruing on or after 6 December 2011 to a company not carrying on a ring-fence trade.

For members joining a group, special rules exist that prevent losses from being offset against gains in certain circumstances. In addition, special rules exist for ring-fencing, as noted above.

Currency issues

A company's taxable profits are generally calculated by reference to the functional currency of the company for accounting purposes. However, capital gains are generally calculated by reference to sterling (British pounds, GBP) except for gains on ships, aircraft, shares or an interest in shares, which are computed by reference to the company's functional or designated currency as appropriate.

Transfer pricing

The UK transfer pricing regime aims to ensure that, for corporation tax purposes, transactions between connected parties take place on arm's-length terms. If arm's-length terms are not used, these terms are imposed for tax purposes. Several methods for determining the arm's-length price are available, and there are strict documentation requirements to support the method chosen and the prices reached. This is particularly relevant to the sale of oil and gas (see above), the provision of intercompany services, intercompany funding arrangements (see below), and bareboat and time charter leases in respect of vessels, such as rigs and floating production, storage and offloading units (FPSOs).

In addition to transactions between a UK tax-resident company and a non-UK tax-resident company, the UK's transfer pricing regime also applies to transactions between two UK tax-resident companies and to transactions between a ring-fenced trade and a non-ring-fenced trade within the same company. For example, the appropriation of crude oil from the exploration and production business of a company to its refining business would be subject to the rules.

The treatment of dividends

The UK adopted a dividend exemption system in respect of dividends received on or after 1 July 2009. Generally, the UK dividend exemption provides for a full exemption from UK corporation tax in respect of distributions that are not of a capital nature from either UK or foreign companies. If distributions do not meet the exemption, they will be subject to UK corporation tax.

Generally, a dividend will be treated as an exempt distribution if:

- The recipient company controls the company paying the dividend.
- The dividend is in respect of non-redeemable ordinary shares.
- The dividend is in respect of a portfolio holding (i.e., the recipient owns >10% of the issued share capital of the payor).
- The dividend is from a transaction not designed to reduce tax.
- The dividend is in respect of shares accounted for as liabilities.

Targeted anti-avoidance rules exist to prevent abuse of the exemption system.

Treatment of foreign branches

Companies resident in the UK are taxed on their worldwide profits, including the profits from their foreign branches. UK tax relief may be available for overseas taxes suffered by way of double taxation relief. Any excess foreign tax credits can be carried back three years or carried forward indefinitely against profits from the same branch. From 19 July 2011, each company subject to UK corporation tax has been able to make an irrevocable election to exempt the future profits and gains of all its foreign branches. The election takes effect from the start of the next accounting period after it is made.

Supplementary charge

"Supplementary charge" is an additional tax (currently levied at 10%) on UK exploration and production activities. Taxable profits for supplementary charge purposes are calculated in the same manner as for ring-fence trading profits but without any deduction for finance costs. Finance costs are defined very broadly for this purpose and include the finance element of lease rentals and any costs associated with financing transactions for accounts purposes.

The due date for payment of supplementary charge is the same as that for ring-fence corporation tax.

Supplementary charge is not deductible for corporation tax purposes.

Field allowance/investment allowance

Historically, the UK has provided a range of "new field allowances" to incentivize the development of certain new offshore fields and the so-called "brownfield allowance" to encourage investment in older existing fields and infrastructure.

The new field allowances and the brownfield allowance were replaced by the investment allowance with effect from 1 April 2015. The investment allowance is a cost-based basin-wide allowance and operates by translating "qualifying expenditure" incurred on or after 1 April 2015 into the investment allowance by applying 62.5% to such expenditure. "Qualifying expenditure" for these purposes is capital expenditure as determined under tax statute and case law and certain specified discretionary operating expenditure. Similar to the operation of the older allowances, the resulting investment allowance is then activated when revenue is earned from the relevant oil field and then once activated is deducted from adjusted ring-fence profits, which are liable to supplementary charge.

Complex transitional rules aim to have the effect of ensuring that a company holding an unactivated new field allowance or brownfield allowance as at 1 April 2015 is no worse off on transition into the current regime, but at the same time, companies are not able to benefit from both investment allowance and new field allowance and brownfield allowance in relation to the same oil field.

In addition to the investment allowance, the onshore allowance (which reduces profits subject to supplementary charge by an amount equal to 75% of the capital expenditure incurred on that project on or after 5 December 2013) and the cluster allowance (which reduces profits subject to supplementary charge by an amount equal to 62.5% of qualifying capital expenditure incurred from 3 December 2014 in relation to a determined cluster) remain in place.

Petroleum revenue tax

Petroleum revenue tax, levied at a rate of 0% from 1 January 2016, previously 50% (for fields that received development consent before 16 March 1993), is charged on a field-by-field basis rather than an entity-by-entity basis, and it applies only to fields that received development consent before 16 March 1993. Petroleum revenue tax is charged in six-month periods ending 30 June and 31 December and is based on profits calculated in accordance with specific statutory provisions rather than on accounting profits. Income and expenditure are dealt with separately for petroleum revenue tax purposes. In particular, each participant is required to file returns in respect of its share of the oil and gas won and saved in each chargeable period, together with any other chargeable receipts such as tariff and disposal receipts.

However, expenditure must be claimed separately and does not become allowable until HMRC gives formal notice (which may be after the period when the expenditure is incurred).

Income

As with corporation tax, strict rules apply to determine whether sales of oil and gas are considered to be at arm's length (and taxable based on the actual price realized) or non-arm's length (and taxable based on statutory values).

Hedging

As petroleum revenue tax is a tax on oil won and saved, only physical hedging contracts with third parties result in a tax-effective hedge for petroleum revenue tax purposes (e.g., a physical forward sale to a third party).

Tariff receipts

Petroleum revenue tax is also chargeable on tariff and disposal receipts (e.g., rentals for the use of infrastructure) received by the participant for the use, or in connection with the use, of a qualifying asset on a taxable UK field. However, the taxable receipts may be subject to specific exclusions and exemptions.

Expenditure

Expenditure incurred in finding, developing and decommissioning a field, together with the costs of extracting and transporting the oil, is generally allowable for petroleum revenue tax purposes. There is no distinction made between capital and revenue expenditure for petroleum revenue tax purposes; however, certain types of expenditure are specifically prohibited, such as interest, production-related payments, subsidized expenditure or the cost of acquiring land and buildings. A supplement of 35% is available for certain types of expenditure incurred in any period, up to and including the period when the participant reaches a break-even position in respect of the relevant field.

Expenditure on assets that are used to earn tariff income is an allowable expense for petroleum revenue tax purposes, to the extent that the tariff income is subject to petroleum revenue tax.

Losses

If a loss accrues to a participant in a chargeable period, it can be carried back against profits from the same field in preceding chargeable periods (on a last-in, first-out basis) or, if no carryback claim is made, the loss is carried forward automatically against profits from the same field in future chargeable periods. Losses are offset against profits before any oil allowance is made (see below). Profits in this context include profits irrespective of the fact that they may have been subject to a 0% petroleum revenue tax.

The carryback and carryforward of losses are indefinite. In certain circumstances, any losses from an abandoned field that cannot be relieved against the profits of that field can be claimed against the profits of another field.

Oil allowance

Oil allowance is a relief designed to prevent petroleum revenue tax from being an undue burden on more marginal fields, and it allows a certain amount of production to be earned free of petroleum revenue tax for at least the first 10 years of a field's life. The allowance is given after all other expenditure and allowances, with the exception of safeguard (see below).

The amount of oil allowance varies depending on the location of the field and the timing of the development consent. It is 125,000, 250,000 or 500,000 metric tons per chargeable period, which equates to 2.5 million, 5 million or 10 million metric tons, respectively, over the life of the field. The oil allowance is converted into a cash equivalent in each chargeable period based on the company's taxable income in the chargeable period. If the oil allowance due has not been fully used in a chargeable period, the excess remains available for future use, subject to the maximum allowance available for the field.

Safeguard

Similar to oil allowance, safeguard is also a relief designed to prevent petroleum revenue tax from being an undue burden on more marginal fields, and it allows a company to earn a specific return on its capital before being subject to petroleum revenue tax. Safeguard applies after all expenditure and other reliefs have been taken into account; it applies for only a certain number of periods and is now largely historical.

Opt-out of petroleum revenue tax

An election is available to take a specific field out of the charge to petroleum revenue tax (provided that all of the field participants agree to the election). The election to opt out of petroleum revenue tax should be successful if either no profits subject to petroleum revenue tax will accrue or, more specifically, given petroleum revenue tax is now levied at 0%, it is not expected to generate a petroleum revenue tax repayment in the future. At present this election is irrevocable.

Diverted profits tax

From 1 April 2015, a new diverted profits tax may in certain circumstances apply. This tax is aimed at perceived abuse involving payments by a UK taxpayer to entities with insufficient economic substance or the avoidance of a UK taxable presence. The general rate is currently set at 25%, but the rate is set at 55% where the diverted profits would otherwise be ring-fence profits.

C. Capital allowances for corporation tax and supplementary charge

Expenditure on assets used in a ring-fence trade

A 100% first-year allowance (FYA) is available on most capital expenditure incurred for the purposes of a company's ring-fence trading, including expenditure on plant and machinery, together with expenditure on exploration, appraisal and development. A number of exclusions to the FYA regime apply, including expenditure on ships and plant and machinery for leasing.

For asset acquisitions, it is important to note that the amount of the purchase consideration that qualifies for capital allowances cannot generally exceed the amount of costs that qualified for relief in the hands of the seller. This means that relief is not available for premium paid-for license acquisitions.

FYAs are given only if the assets are used wholly and exclusively for the purposes of ring-fence trade; thus, an FYA can be withdrawn if the asset is sold or if it is no longer used in a ring-fence trade within five years of incurring the expenditure.

If an FYA is not claimed in the year when the expenditure is regarded as being incurred, it is not available in subsequent years, and the expenditure instead attracts writing-down allowances of 25% a year for most intangible expenditures, 25% a year for plant and machinery, or 10% a year for expenditure on long-life assets or mineral extraction assets on a reducing-balance basis.

Expenditure on assets used in a non-ring-fence trade

Capital allowances of 18% per year on a reducing-balance basis are available on most expenditure on plant and machinery used in a non-ring-fence trade. However, assets purchased on or after 26 November 1996, with a useful economic life of 25 years or more, attract capital allowances at a reduced rate of 8% per year.

Decommissioning

Most decommissioning expenditure is considered to be capital in nature for tax purposes and qualifies for a special 100% capital allowance. This includes expenditure on demolition, preservation pending reuse or demolition, and preparing or arranging for reuse (including removal). Specifically, this may include mothballing installations, plugging wells, dumping or toppling rigs, and restoring sites.

A special 100% capital allowance may be claimed in respect of ring-fence trades for pre-cessation decommissioning expenditure, subject to a number of conditions.

While the rate of relief for decommissioning expenditure for supplementary charge purposes is restricted to 20% for decommissioning carried out on or after 21 March 2012 given the now lower rate of supplementary charge with effect from 1 January 2016, this rate is now 10%.

The UK Government has the power to enter into deeds with ring-fence companies guaranteeing the amount of tax relief available on decommissioning expenditure (both in a default and non-default scenario) based on the tax legislation in operation at the time of enactment of the Finance Act 2013.

Asset disposals

The disposal of an asset that attracted capital allowances may give rise to a balancing charge or an allowance for capital allowance purposes. This is generally calculated by comparing the sale proceeds received to the remaining capital allowances available in respect of the asset.

D. Incentives

Ring-Fence Expenditure Supplement

If a company has a ring-fence loss in a particular period but it, or other companies in its group, does not have ring-fenced taxable profits against which the losses can be offset, the company can claim the Ring-Fence Expenditure Supplement (RFES). This increases the ring-fence losses the company is able to carry forward to the next period by 10% (6% for periods commencing prior to 1 January 2012). Historically, it could be claimed for a maximum of 6 years, but this is now extended to 10 years (these years do not have to be consecutive). However, claims for years 7 to 10 would be available only for losses incurred/supplement generated after 5 December 2013.

Tax holidays

The UK does not have a tax holiday regime.

R&D allowances

Exploration and appraisal expenditure incurred before a field is considered as commercial qualifies for 100% R&D allowances for corporation tax and supplementary charge purposes.

In addition, a company can elect to receive a taxable pre-tax credit of 49% for ring-fence companies, or 11%[6] for non-ring-fence companies calculated in respect to qualifying R&D expenditure. In certain circumstances, if a company is in an overall loss position, then the pretax credit can result in a payment to the company or a credit against the tax liabilities of other group companies.

E. Withholding taxes

In general, withholding tax (WHT) applies at 20% on both interest payments and royalties, subject to any relief provided under an applicable double tax treaty.

The UK has an extensive network of double taxation agreements with overseas jurisdictions. Treaty relief for WHT on royalties can be claimed automatically. However, a nonresident recipient of interest must make a claim for repayment or an application for relief at source to the UK Centre for Nonresidents to benefit from treaty relief. In addition, there are a number of exemptions in respect of interest WHT, including exemptions for payments to other companies charged to UK corporation tax and payments to qualifying banks.

The UK does not levy WHT on dividend payments, and it has no branch remittance tax.

6 *It should be noted that as part of the 2017 Winter Finance Bill, it was announced that the RDEC headline rate has been increased from 11% to 12% from 1 January 2018. The Winter Finance Bill is expected to receive Royal Assent on 15 March 2018.*

F. Financing considerations

Finance costs are generally deductible for corporation tax purposes but not for supplementary charge or petroleum revenue tax purposes. In addition, deductions for finance costs in computing the profits of a ring-fenced trade are permitted only if the money borrowed has been used to meet expenditure incurred in carrying on oil extraction activities or on acquiring a license from a third party.

If borrowing is from a connected party or is guaranteed by another group company, the UK's transfer pricing regime, which includes thin capitalization provisions, may apply. The effect may be to restrict deductions for finance costs to those that would have been available if the loan had been from an unconnected third party. This involves consideration of both the amount of the loan and the terms of the loan that could otherwise have been obtained from a third party.

In response to Action 4 of the Organisation for Economic Co-operation and Development's Base Erosion Profit Shifting plan (Limiting Base Erosion Involving Interest Deductions and Other Financial Payments), Finance (No. 2) Act 2017, which received royal assent on 16 November 2017, contains provisions that restrict deductions for net UK interest expense from 1 April 2017 onward to 30% of tax-EBITDA (earnings before interest, tax, depreciation and amortization) unless the wider group's debt position is such that a higher ratio applies under the group ratio rule. This restriction does not apply to finance costs that are deductible against ring-fence profits.

Thin capitalization

There are no statutory or non-statutory safe harbor rules in the UK in respect of thin capitalization. Instead, the UK relies purely on the arm's-length test for connected-party debt. The arm's-length test can be a source of uncertainty, as neither UK legislation nor the Organisation for Economic Co-operation and Development (OECD) guidelines offer practical assistance as to how to evaluate arm's-length debt. HMRC is often willing to enter into discussions or provide advance clearance on potential thin capitalization issues when relevant funding arrangements are being put in place, in order to give some certainty as to the tax treatment likely to apply in specific circumstances.

G. Transactions

Capital gains

Capital gains realized by a UK tax-resident company on the sale of a chargeable asset are subject to corporation tax (19%[7] for non-ring-fence gains and 30% for ring-fence gains). There has historically been some uncertainty as to whether a ring-fence gain is subject to the supplementary charge. However, the Finance Act 2012 provided that ring-fence chargeable gains accruing on or after 6 December 2011 will be subject to the supplementary charge. A capital gain is usually calculated as the excess of sales proceeds less any qualifying capital expenditure. In addition, up to 1 January 2018,[8] an allowance is available for inflation; the amount of the reduction is based on the increase in the retail price index (RPI).

A non-UK tax resident is not normally subject to UK tax on its capital gains. However, if a non-UK tax resident realizes a gain from disposal of UK exploration or exploitation rights or assets (or a company's unquoted shares that derive the greater part of their value from such rights or assets), this gain is subject to UK tax.

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7 *Reduced to 19% on 1 April 2017 and reducing to 17% on 1 April 2020.*

8 *It should be noted that as part of the 2017 Winter Finance Bill, it was announced that the indexation allowance will be frozen with effect from 1 January 2018. The Winter Finance Bill is expected to receive Royal Assent on 15 March 2018.*

Any unpaid tax can be assessed against the licensees of the fields owned by the company sold. Gains on the sale of assets situated in and used in a trade carried on by a UK tax-resident company or a PE in the UK are subject to corporation tax.

Farm-in and farmout

If a license interest is farmed out for noncash consideration (such as subordinated interests, development carry, license swaps or work obligation), the consideration must be valued. It is important that the farmer agrees to the value of any rights-based consideration to avoid a possible future challenge from HMRC. If all or part of the consideration given cannot be valued, the disposal is deemed to be for a consideration, equal to the market value of the asset.

Farmouts of license interests relating to undeveloped areas (i.e., areas for which no development consent has been granted and no program of development has been served or approved) are deemed to be for zero consideration to the extent that the consideration consists of an exploration or appraisal work program. Otherwise, these proceeds are taxable.

Swaps

Swaps of license interests in undeveloped areas are also deemed to take place for zero consideration, to the extent that the consideration is in the form of another license relating to an undeveloped area.

Swaps of license interests in developed areas are deemed to take place for such consideration as gives rise to no gain or no loss.

Allowable base costs deducted from consideration received on disposal

Consideration given to acquire an asset can be deducted when computing a chargeable gain, as can incidental costs of acquisition and disposal and expenditures to enhance the value of the asset. However, any expenditure allowed as a deduction against profits in calculating corporation tax is not allowable.

Complex rules apply that may "waste" the base cost deduction over the life of the license, thus reducing the base cost.

Ring-fence rules

Gains or losses arising on the disposal of an interest in an oilfield or assets used in connection with the field (but only if the assets are disposed of as part of a license transfer) are ring-fenced. Gains on disposals of shares, field assets disposed of outside a license transfer and disposals of licenses that do not have determined fields are not ring-fenced. Ring-fence gains cannot be offset by non-ring-fence losses. Ring-fence losses can be offset against ring-fence gains, but they can be offset against non-ring-fence gains only to the extent that a claim is made within two years for the loss to be treated as non-ring-fence.

Reinvestment relief can be claimed if the proceeds of a disposal that fall within the ring-fence rules are reinvested in certain "oil assets," including disposals made on or after 24 March 2010 and reinvestment in intangible drilling expenditure.

Substantial shareholding exemption

The substantial shareholding exemption (SSE) applies if a shareholding of more than 10% of a trading company's share capital is disposed of, subject to certain conditions being met. If SSE applies, then any chargeable gain is exempt from corporation tax. Finance (No. 2) Act 2017, which received royal assent on 16 November 2017, contained a number of potential simplifications to the SSE rules which apply to disposals made on or after 1 April 2017. In particular, this includes removal of the investing company condition, removal of the post-disposal investee trading condition and extension of the period in which the 12 month holding requirement needs to be satisfied from two years to six years.

Transferable tax history for oil and gas companies

As part of the Autumn Budget 2017, it was announced that transferable tax history (TTH) will be introduced for deals where the license transfer is approved by the UK Oil & Gas Authority on or after 1 November 2018.[9]

In essence, TTH will enable the buyer of an interest in a field to acquire some of the corporation tax history of the seller, thus enabling the buyer to be in broadly the same corporation tax position as the seller when it comes to achieving relief for decommissioning expenditure in relation to that field. A key design principle will be that the exchequer is not exposed to a greater share of the cost of decommissioning.

The corporation tax system currently discriminates against new or recent entrants to the UK continental shelf when bidding for mature assets due to their lack of corporation tax history. TTH is intended to neutralize this effect, ensuring it does not act as a barrier to transactions involving late-life assets.

H. Indirect taxes

VAT

The standard rate of value-added tax (VAT) in the UK is 20%, with reduced rates of 5% and 0%. VAT is potentially chargeable on all supplies of goods and services made in the UK and its territorial waters. UK resident companies may be required to register for UK VAT if supplies exceed the VAT threshold or if there is an intention to make future taxable supplies. As of 1 December 2012, the VAT threshold for nonresident companies has been removed, meaning all nonresident companies making taxable supplies in the UK must register for UK VAT. A nonresident company that is required to register for UK VAT can register directly with the UK tax authorities; there is no requirement to appoint a VAT or fiscal representative. VAT incurred by an entity that is VAT registered in the UK is normally recoverable on its periodic VAT returns provided it makes sales of goods located in the UK or provides services related to land or general services on a business-to-consumer basis.

A specified area is licensed for both onshore and offshore oil and gas exploration or exploitation purposes, often to a consortium of companies. One of the participating companies in a consortium usually acts as the "operating member" (the OM) under a joint operating agreement. In this situation, the OM incurs UK VAT on the supplies it receives for the consortium, so it is essential that it registers for UK VAT to obtain credit for the VAT charged. In addition, it is important for the "participating members" of the consortium to register for VAT to recover input VAT.

In the UK, the VAT treatment of the sale of hydrocarbon products produced as a result of a successful exploration and production program depends on the product itself, where it is sold and to whom it is sold. Natural gas and associated products imported into the UK (via a gas pipeline) from a field outside the UK territorial waters are subject to formal customs import procedures — although from 1 January 2011, the importation of natural gas has been exempt from import VAT.

Excise duty

Excise duty is payable on certain hydrocarbon products in the UK if these products are removed from an excise warehouse for "home use" (i.e., they are removed for domestic use). Products stored in an excise warehouse are afforded duty suspension. The rate of excise duty payable in respect of hydrocarbon products is based on the classification of the product.

9 *A technical consultation on the precise mechanics will be published in spring 2018, with a view to legislation being included in Finance Bill 2019.*

Customs duty

All goods imported into the UK from outside the European Union are potentially liable to customs duty. The rate of customs duty is based on the classification of the goods and whether the goods qualify for preferential rates. However, customs relief and regimes may allow goods to be imported at a reduced or zero rate of duty, provided the goods are used for a prescribed use under customs control, within a specified time limit. Normally, a business must seek prior authorization from HMRC to utilize any customs relief or regimes.

Insurance premium tax

Insurance premium tax (IPT) is a tax on premiums received under taxable insurance contracts. Two rates of IPT apply:

- A standard rate of 6%
- A higher rate of 20% for insurance supplied with selected goods and services

All types of insurance risk located in the UK are taxable, unless they are specifically exempt.

In respect of the oil and gas industry, onshore installations in the UK and those within the 12-mile limit are liable to IPT. However, IPT does not apply to installations located outside UK territorial waters. The Isle of Man and the Channel Islands are also outside the UK for IPT purposes.

Appropriate allocations must be made when certain insurance policies cover both UK and non-UK risks, to determine the proportion of the premium that will be subject to IPT.

Stamp taxes

Stamp duty applies in the UK at a rate of 0.5% on the consideration of the sale of shares, and stamp duty land tax applies up to a rate of 5% on the consideration on the sale of an interest in nonresidential UK land and buildings. The tax is generally payable by the purchaser. Relief is available for transfers between group companies and some other forms of reorganization. However, this relief is hedged around with anti-avoidance rules, so it is essential to seek specific advice before relying on the availability of a relief. In the case of land transfers to a company connected with the transferor, the market value is substituted for the consideration if it is higher.

A license may be an interest in land, but stamp taxes do not apply to licenses situated in territorial waters because, for these purposes, the territory of the UK ends at the low-water mark. Offshore structures fixed to the seabed may amount to an interest in UK land if they are connected to land above the low-water mark (e.g., a pier or jetty). It is generally considered that the section of an undersea pipeline on the seaward side of the low-water mark does not give rise to an interest in land, although this is not completely certain. The owner of the landward section, including any termination equipment and associated structures, generally possesses an interest in the land. On a sale, it is sometimes difficult to allocate the consideration between the interest in the land and buildings and any equipment, which may not be regarded as technically part of the land and buildings.

As part of the Government's agreed devolution of some tax raising powers to Scotland, from 1 April 2015, the land and buildings transactions tax was introduced in Scotland and replaced the UK stamp duty land tax. The land and buildings transaction tax applies up to a rate of 4.5% on nonresidential property transactions. Stamp duty will continue to be administered across the whole of the UK.

I. Other

Forms of business presence

Forms of business presence in the UK typically include companies, foreign branches and joint ventures (incorporated and unincorporated). In addition to commercial considerations, it is important to consider the tax consequences of each type of entity when setting up a business in the UK. Unincorporated joint ventures are commonly used by companies in the exploration and development of oil and gas projects.

Foreign-exchange controls

There are no foreign-exchange restrictions on inward or outward investments.

Anti-avoidance legislation

The UK's tax law contains several anti-avoidance provisions, which apply in certain areas (such as financing) where a transaction is not carried out for genuine commercial reasons. In addition, a general anti-abuse rule also exists, which is intended to counteract tax advantages arising from tax arrangements that are considered to be abusive.

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Tax Cuts and Jobs Act of 2017

On 22 December 2017, the United States (US) Congress enacted broad and sweeping changes to the US federal income tax system, most notably by reducing the corporate income tax rate, changing the taxation of foreign earnings, and introducing full expensing of depreciable assets, among others. While certain key US federal oil and gas tax provisions were left unchanged by the legislation, the ripple effects of the enacted provisions will have a lasting and profound impact on the oil and gas industry. While a detailed description of each legislative change is beyond the scope of this guide, such changes should be considered on an entity-by-entity basis.

Fiscal regime

The fiscal regime that applies to the petroleum industry in the US consists of a combination of corporate income tax (CIT), severance tax and royalty payments. In summary:

- Royalties:
  - Onshore[1] — 12.5% to 30%, negotiated or bid with the mineral interest owner

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1 *Onshore mineral interests can be held by the federal government (managed by the Department of the Interior's Bureau of Land Management and the Department of Agriculture's U.S. Forest Service), states, Indian reservations (managed by the Bureau of Indian Affairs and the Bureau of Land Management), individuals, corporations and trusts.*

  - Offshore[2] — 18.75% effective for 19 March 2008 auction, 16.667% in certain previous lease auctions and 12.50% for older leases
- Bonuses:
  - Onshore — negotiated or bid with the mineral interest owner
  - Offshore — competitive bid process
- CIT rate — 21%[3]
- Severance tax — Severance tax is payable to the US state where the product is extracted, including onshore and offshore state waters. The tax rates and the tax base vary by state; for example, states calculate the tax based on a flat amount per volume produced or as a percentage of gross receipts. Additionally, it is common for different tax rates to apply for different types of products produced.
- Capital allowances[4] — D, E[5]
- Investment incentives — L, RD[6]

B. Fiscal regime

The fiscal regime that applies to the petroleum industry in the US consists of a combination of CIT, severance tax and royalty payments.

Corporate tax

US resident corporations are subject to income tax on income (as modified by the recent legislation — see discussion below), including, in many cases, income of foreign branches and certain foreign entities (subject to the application of foreign tax credits (FTCs) in certain circumstances), at a rate of 21%, effective for tax years beginning after 2017 (a blended rate applies for fiscal-year corporate taxpayers with a fiscal year that includes 1 January 2018). Income of nonresident corporations from US sources that is not subject to withholding tax (WHT) or treaty protection is also subject to the 21% CIT rate. The 21% CIT rate applies to oil and gas activities and to non-oil and gas activities.

The US does not apply ring-fencing in the determination of CIT liability. Profit from one project can offset losses from another project held by the same tax entity, and, similarly, profits and losses from upstream activities can offset downstream activities or any other activities undertaken by the same entity. The US tax law allows related US corporations with a US parent — in which the parent owns, directly or indirectly through one or more chains, 80% of the total voting power and value of the stock of each US subsidiary — to file consolidated tax returns and be treated as a single taxable entity for US federal income tax purposes.

US corporate tax is levied on taxable income. Taxable income equals gross income less allowable deductions. Gross income includes all taxable ordinary and capital income (determined under tax law). Deductions include expenses to the extent that they are incurred in producing gross income or are necessary in carrying on a business for the purpose of producing gross income.

Capital expenditures incurred by taxpayers in the oil and gas industry are recovered through deductions available for intangible drilling and development costs (IDCs), cost or percentage depletion for leasehold cost basis, or accelerated methods of depreciating tangible assets (or immediate expensing,

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2 *Offshore mineral interests (Alaska, Gulf of Mexico and Pacific) are owned by the US Government and are managed by the Bureau of Ocean Energy Management (BOEM), a bureau of the U.S. Department of the Interior.*

3 *US federal rate (effective for tax years beginning after 2017; however, a blended rate applies for fiscal-year taxpayers with a fiscal year that includes 1 January 2018); individual state tax regimes vary and include income, franchise, production and property taxes.*

4 *Capital allowances vary depending on the type of taxpayer and the nature of assets (see later discussion on integrated and independent producers).*

5 *D: accelerated depreciation; E: accelerated write-off for intangible drilling costs.*

6 *L: losses from 2018 and later can be carried forward for indefinitely and offset 80% of taxable income; RD: R&D incentive.*

if available, see Section C). Additionally, there may be deductions available for other types of capital expenditures — for example, expenditures incurred to establish an initial business structure (organizational or startup costs are "generally" capitalized (subject to certain exceptions) and amortized over 15 years). Taxpayers in the oil and gas industry may elect to use the unit-of-production (UoP) method of cost recovery for certain tangible, depreciable property. Taxpayers may also elect to capitalize and amortize, or deplete, domestic IDCs (certain rules exist for non-US IDCs).

An overriding principle in the US taxation of the oil and gas industry is that almost all calculations involving assets are calculated on a unit-of-property (tax property) basis; this includes property basis, gain or loss on disposal, abandonment and property-related deductions (depletion, depreciation and amortization). Although the concept and actual determination of a unit of property (i.e., separate property) can be very complicated, in practice, a unit of property can be equated to a lease or a particular oil and gas well.

Additional deductions are allowed against gross income, including, in limited circumstances, percentage depletion. Further, the US imposes a strict limitation on the current deductibility of interest expense through Section 163(j) of the Internal Revenue Code (IRC). Effective for tax years after 2017, IRC Section 163(j) limits the net interest expense deduction to 30% of the business's adjusted taxable income (which is generally determined to be earnings before interest, taxes, depreciation and amortization (EBITDA) through 2021, and EBIT thereafter). Certain limitations and exceptions apply.

Prior to the tax reform legislation of 2017, the USA taxed all income earned worldwide. However, as part of the aforementioned legislation, the US federal income tax system was converted to a modified territorial regime. This system allows for a 100% exemption for foreign dividends made by certain foreign corporations if owned at least 10% by a US corporation. This allows income earned outside of the US and distributed back to the US parent to be removed from taxable income (subject to numerous restrictions and limitations). In 2018, the US will impose a one-time transition tax on accumulated foreign earnings (see foreign entity taxation below). The US also several base erosion measures including the base erosion and anti-abuse tax (BEAT) and global intangible low-taxed income (GILTI) provisions, which impose US federal income tax obligations on payments or structures designed to shift income out of the US (see foreign entity taxation below).

Alternative minimum tax regime

Prior to 2018, the US tax system imposed an "alternative minimum tax" (AMT) on corporations, in amount by which the tentative minimum tax exceeded the regular US federal income tax for the applicable tax year, resulting in a separate and parallel tax system. As part of the recently enacted legislation, effective for tax years beginning after 2017, the corporate AMT was repealed, allowing corporate taxpayers with an AMT credit to use the credit to offset regular tax liability (as well as the potential for certain refund opportunities related to remaining credits). For corporate taxpayers with a fiscal tax year that includes 1 January 2018, a blended rate applies. While the corporate AMT has been repealed on a prospective basis, the AMT regime still applies to individuals (with certain modifications).

Under prior law (for tax years before 2018), the AMT rate for corporate taxpayers was 20% when AMT liability exceeded regular taxable income. AMT starts with regular taxable income and is increased or reduced by additional preferences and adjustments. The AMT regime often affected oil and gas companies because they are subject to the IDC preference item. Consequently, if a corporation had large IDC deductions, especially in years with low taxable income due to IDC deductions, loss carryforwards or low commodity prices, the corporation may have an AMT liability. AMT taxpayers are allowed credits against regular tax liability in years when they are not subject to the AMT. A full overview of the US AMT regime is beyond the scope of this chapter and will not be described in detail herein.

The following are common AMT preferences and adjustment items that apply to the oil and gas industry:

- The depreciation deduction is recalculated using a slower method.
- The IDC deduction is recalculated by capitalizing and amortizing the current-year IDC using either the 10-year straight-line (SL) or the UoP ratio for AMT preference purposes. Additional computations (not detailed here) are required to determine the final amount of the AMT IDC preference. AMT IDC amortization is not allowed on any prior-year IDC expenditures.
- For independent producers, the treatment of IDC as a tax preference was repealed. However, the benefit of the repeal was limited. Therefore, an independent producer must still determine the amount of preference IDC to be added back for AMT purposes, if any.
- For integrated producers (see Section C below) only, the adjusted current earnings (ACE) IDC adjustment is the excess of the IDC deducted for regular tax over the amount allowed for ACE IDC amortization, less the amount already added back as an AMT IDC preference. The ACE IDC amortization is calculated based on capitalizing all of the IDC and amortizing it over 60 months. The taxpayer may continue to amortize the IDC capitalized for ACE purposes until it is fully amortized, even if this causes the taxpayer to have a negative ACE IDC adjustment.
- The last-in, first-out (LIFO) method is not allowed for ACE purposes.

State and local taxes

In the US, state and local taxes can be a significant cost of doing business onshore or in state waters. Each state has its own tax statute. The details of the various state requirements are numerous, and they are not included in detail in this chapter.

State income tax

Most states impose a tax based on the income of companies doing business within the state. Generally, state corporate taxable income is calculated by making certain state-specific additions and subtractions to federal taxable income. Alternatively, some states calculate state taxable income based on gross receipts, subject to state-specific definitions and modifications.

State taxable income is apportioned to an individual state based on a factor that generally compares the property, payroll or sales activity within the state to those same factors within and outside the state. Apportioned income is multiplied by the state income tax rate to determine the tax due. State income tax rates typically range from 0% to 12%.

State franchise tax

Many states impose a franchise tax on any company that is:

- Organized in the state
- Qualified to do business, or doing business, in the state
- Exercising or continuing the corporate charter within the state
- Owning or using any of the corporate capital, plant or other property in the state

Generally, the franchise tax rate is calculated by multiplying the value of the apportioned assets, capital stock or net worth employed in the state by the franchise tax rate. Franchise tax rates typically range from 0.15% to 1.0% of the taxable base.

Foreign entity taxation

The tax issues associated with inbound investment into the US for oil and gas ventures bring into play unique rules and regulations specific to the oil and gas area. Similarly, inbound investment,[7] in general, has a defined set of tax rules

7 *Any reference to "inbound investment" refers to an investment into the US by a nonresident foreign person, including a multinational foreign corporation.*

and regulations governing the taxation of a foreign multinational, regardless of the industry.

Taking the rules for inbound investment into the US first, a foreign multinational is generally subject to US tax on its US-sourced income under US domestic tax principles, unless a bilateral income tax treaty applies that supplants the ability of the US to tax certain types of income. For example, certain activities that take place in the US may give rise to a taxable trade or business under US domestic tax principles; while under an applicable income tax treaty, the activity may be exempt from US tax by agreement of the treaty parties. An example of this treatment may be rental of equipment to a US party on a net basis, whereby the lessee takes on most of the risks and costs associated with leasing the asset from the foreign party.

Further, regardless of whether a foreign multinational is attempting to apply an applicable income tax treaty or not, certain domestic tax provisions may apply, such as IRC Section 163(j), which governs the amount of interest expense that is deductible in the US against US taxable income. Until 2022, such amount is generally limited to a percentage of EBITDA; whereas, after 2021, such amount is generally limited to a percentage of EBIT. Similar issues for inbound financing of US operations will entail debt/equity characterization, the conduit financing regulations and thin capital considerations.

Another area of the US federal income tax provisions that may be applicable to foreign multinationals investing in the US is set forth in IRC Section 897. This section was included in the Foreign Investment in Real Property Tax Act (FIRPTA) and sets forth the tax rules for determining whether an investment in the US constitutes an investment in a "US real property interest" (USRPI). If an investment is a USRPI, there are specific provisions that are meant to preserve the ability of the US to tax any built-in gain or appreciation that may arise while the foreign multinational owns the USRPI and subsequently disposes of it. The gain-triggering rules encompass sale transactions and can also include transactions that would otherwise qualify for tax-free restructuring of the FIRPTA property owner.

The USA also imposes several base-erosion measures, including the BEAT and GILTI provisions. BEAT generally applies to corporations (other than RICs, REITs, or S corporations) that are subject to US net income tax with average annual gross receipts of at least US$500 million and that have made related-party deductible payments totaling 3% (2% for banks and certain security dealers) or more of the corporation's total deductions for the year. A corporation subject to the tax generally determines the amount of tax owed under the provision (if any) by adding back to its adjusted taxable income for the year all deductible payments made to a foreign affiliate (base erosion payments) for the year (the modified taxable income). The amount owed is the excess of 10% (5% for one tax year for base erosion payments paid or accrued in tax years beginning after 31 December 2017) of the corporation's modified taxable income over its regular tax liability for the year (net of an adjusted amount of tax credits allowed).

GILTI is gross income in excess of extraordinary returns from tangible depreciable assets, excluding effectively connected income (ECI), subpart F income, high-taxed income, dividends from related parties, and foreign oil and gas extraction income. It should be noted that foreign oil and gas related income (FORI) is not excluded from GILTI and will have to be tracked and defined by taxpayers. Generally, FORI is income derived from the processing, transportation or distribution of oil and gas, and may include certain related services. The extraordinary return base equals 10% of the controlled foreign corporation's aggregate adjusted basis in depreciable tangible property. Only 80% of the foreign taxes paid on the income is allowed as a foreign tax credit. For tax years beginning after 31 December 2017, and before 1 January 2026, the highest effective tax rate on GILTI is 10.5%.

In 2018, the US will impose a one-time transition tax on a US 10% shareholder's pro rata share of the foreign corporation's post-1986 tax-deferred earnings, at the rate of either 15.5% (for accumulated earnings held in cash, cash equivalents or certain other short-term assets) or 8% (for accumulated earnings invested in illiquid assets (e.g., property, plant and equipment)). A foreign corporation's post-1986 tax-deferred earnings is the greater of the earnings as of 2 November 2017, or 31 December 2017. The portion of post-1986 earning and profits subject to the transition tax does not include earnings and profits that were accumulated by a foreign company before attaining its status as a specified foreign corporation. The transition tax provision allows post-1986 accumulated earnings deficits of any foreign corporation to offset tax-deferred earnings of other foreign corporations. Additionally, the transition tax provision generally allows netting among affiliated group members. The US shareholder may elect to pay the transition tax over eight years or less.

As discussed above, the US federal income tax system contains rules and regulations with respect to non-US entities that are owned directly or indirectly by US taxpayers. A detailed review and summary of rules and regulations is beyond the scope of this chapter and will not be discussed in detail herein.

Additionally, there is a whole host of special US federal income tax provisions (and state tax provisions), not discussed herein, which are applicable to foreign multinationals investing in US oil and gas extraction activity.

Capital gains

Gains and losses resulting from the sale of capital assets by corporate taxpayers are subject to US federal income tax at the ordinary corporate tax rate of 21% (effective for tax years after 2017). Capital gains or losses are determined by deducting the adjusted basis of an asset from the proceeds (money received or receivable and the market value of any property received or receivable).

Assets held for one year or less and inventory or assets held for sale in the ordinary course of business are treated as non-capital assets and generate ordinary income or loss upon their sale.

Non-inventory assets that are used in the taxpayer's trade or business for more than one year are considered trade or business assets. The disposition of trade or business assets generates ordinary losses or so-called "IRC Section 1231" gains that may (subject to certain limitations) be treated as capital gains. However, the US tax authorities require that certain previously claimed ordinary deductions be recaptured as ordinary income at the time of sale if the property is sold for a gain. For example, if tangible assets are sold at a gain, the depreciation deducted must be recaptured up to the amount of the gain. Upon the sale of a leasehold interest, the taxpayer is required to recapture all IDC and depletion taken that reduced the tax basis, up to the amount of the gain realized on the property, if that property was placed in service after 31 December 1986. There are different recapture rules for property that was placed in service prior to 1 January 1987.

Although the tax rate is the same for ordinary income and capital transactions for corporations, capital losses are deductible only against capital gains and not against ordinary income. Net capital losses can be carried back three years and carried forward five years. Trade or business losses incurred in the ordinary course of business are deductible against taxable income.

Oil and gas leases held for more than one year generally result in trade or business gains and losses upon sale, subject to recapture as discussed above. Gains or losses on the disposition of property must be calculated for each tax property (i.e., property by property, not in total). Recapture is also calculated on a property-by-property basis.

Capital gains or losses derived by a US resident company on the disposal of shares in a foreign company are generally treated as US-sourced capital gains or losses. However, if the stock in the foreign corporation constitutes stock in a controlled foreign corporation when sold, or at any time during the five years prior to the date of sale, certain rules can apply to, in effect, re-source the income as foreign-sourced dividend income, to the extent of the selling shareholder's share of the accumulated earnings and profits of the foreign corporation. In addition, the selling shareholder may be entitled to a foreign tax credit on such earnings.

US companies with foreign branch active businesses (including oil- and gas-producing assets, in most cases) have capital gains or losses on disposal of foreign branch assets, which could be foreign-sourced or US-sourced depending on the facts. Moreover, even if the sale of a foreign branch asset, such as equipment, is classed as foreign under the sourcing provisions, additional rules could apply that recapture, as US-sourced income, a portion of the gain equal to the amount of depreciation taken in the US in prior tax years related to the foreign branch asset.

Functional currency

Under the US income tax law, taxpayers are required to calculate their taxable income using the US dollar.

Transfer pricing

US tax law includes measures to ensure that the US taxable income base associated with cross-border transactions is based on arm's-length prices. Several methods for determining the arm's-length price are available, and there are strict documentation requirements to support the method chosen and the prices reached. This is particularly relevant to the sale of commodities, intercompany services, intercompany funding arrangements, and bareboat and time charter leases.

Dividends

Dividends paid by US resident companies are taxable, unless the recipient is eligible for a dividend-received deduction (DRD) or is covered by an applicable income tax treaty at a reduced tax rate.

For US resident corporate shareholders, all dividends received are included in the gross income. Under prior law, C corporations that received dividends from certain taxable domestic corporations were entitled to a 100% dividend received deduction if the recipient C corporation owned more than 80% of the US corporate payor. Further, C corporations that received dividends from certain taxable domestic corporations were entitled to receive either an 80% deduction (if it owned more than 20% but less than 80% of the dividend payor) or a 70% deduction (if it owned less than 20% of the dividend payor) on the dividends received. Effective for tax years beginning after 2017, however, the 80% dividend received deduction was lowered to 65%, and the 70% dividend received deduction was lowered to 50%. The dividends paid by certain foreign corporations are eligible for a 100% exemption if the US corporate recipient owns 10% or more of the foreign payor.

For corporate nonresident shareholders, dividends paid or credited to nonresident shareholders are subject to a 30% WHT (unless the rate is reduced by an applicable income tax treaty). The WHT is deducted by the payor on the gross amount of the dividend.

Royalty payments

Onshore leases

Petroleum royalties are paid to mineral owners, which for onshore leases can be the state or federal government, individuals, Indian reservations, corporations, partnerships or any other entity. Royalty payments are excluded from gross income of the working interest owner.

For onshore projects, wellhead royalties are paid to the mineral owner. Wellhead royalties are generally levied at a rate of 12.5% to 30% (based on the lease or contract) of the gross wellhead value for all of the petroleum produced.

Gross wellhead value is generally the posted spot price for the production location, or the actual revenue received, less any costs. The types of costs allowable are those for processing, storing and transporting the petroleum to the point of sale.

Offshore leases

For offshore projects, wellhead royalties are paid to the federal government via the Office of Natural Resources Revenue (ONRR) but are shared with the appropriate state if the well is located in state waters. The royalty is based on the percentage set at the time of the auction. As discussed above, this royalty is paid on the gross wellhead value of production.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas. And under the current US federal income tax rules, no specific special terms or provisions apply to treat unconventional oil or gas differently from conventional oil or gas for tax purposes.

C. Capital allowances

The oil and gas industry is capital-intensive. For US federal income tax purposes, costs associated with the acquisition of a lease (project), costs to develop a lease and production-related costs (operating expenses) have various treatments. Production-related costs are generally deductible in the year they are paid or accrued for tax purposes. Acquisition and development costs are generally capitalized expenditures for both book and tax purposes. It should be noted that there are exceptions that allow for deducting some of these capitalized expenditures, based on specific statutory authority.

It should also be noted that the rules that apply to foreign (non-US location) leases are different from those for US domestic leases. US domestic leases generally include leases up to the 200-nautical mile limit in the Gulf of Mexico. Usually, owners of foreign leases are required to capitalize costs and depreciate or amortize such costs over longer time frames. Leasehold costs may be recovered based on only cost depletion (i.e., percentage depletion is not allowed on foreign leases).

Additionally, tax recovery rules vary significantly based on the designation of the company as an "integrated oil company," an "independent producer" or a "major integrated oil company."

An integrated producer is defined as a company (or a 5% or more related party) that has exploration and production activity and either:

- Gross receipts in excess of US$5 million in US retail sales of oil and gas for the taxable year

  Or

- Refinery runs (located anywhere in the world) that average in excess of 75,000 barrels of throughput per day

An independent producer or royalty owner is defined as any taxpayer that is not an integrated producer.

In 2006, Congress created a subset of integrated producers called "major integrated oil companies," which is defined as producers of crude oil that have average daily worldwide production of at least 500,000 barrels, gross receipts in excess of US$1 billion for the last taxable year ended during the 2005 calendar year and at least a 15% ownership in a crude oil refinery. Currently, the rule regarding the amortization of geological and geophysical (G&G) costs is the only provision of the US federal tax law that utilizes the definition of a major integrated oil company.

Leasehold costs

Leasehold acquisition costs include costs to acquire the lease (e.g., lease bonus payments, auction bid payments, G&G costs incurred in years beginning before 9 August 2005, attorney fees and title transfer fees). These types of costs are capitalized to the property acquired and are recovered through depletion. Cost depletion attempts to match the deduction for the tax basis in the property with the rate at which the production occurs over the life of the reserves. Thus, the cost depletion rate is calculated as current year volumes sold, divided by the total volume of reserves in the ground at the beginning of the taxable year.

This ratio is then multiplied by the remaining adjusted basis of the mineral property at the end of the year. Cost depletion is allowed for all types of taxpayers and for domestic and foreign mineral properties.

Independent producers and royalty owners who own US domestic property are allowed percentage depletion based on the statutory rates and limitations. For oil and gas production, the statutory rate is 15% of gross income, limited to 100% of the net income of the property, determined on a property-by-property basis. Percentage depletion is further limited to 1,000 barrels of production a day. Percentage depletion is prorated to the eligible property based on the ratio of 1,000 barrels to the total average daily production volume. The limited percentage depletion is compared with the cost depletion on a property-by-property basis. The taxpayer is allowed a deduction equal to the higher of the cost or percentage depletion on a property-by-property basis. Lastly, the taxpayer is subject to an overall taxable income limitation such that percentage depletion cannot exceed 65% of the taxpayer's taxable income (with certain adjustments). Any depletion limited by the 65% limitation can be carried forward to future years without expiration. The actual depletion deducted in the current year return is the amount that reduces the leasehold basis for the year.

G&G costs

Costs expended for G&G have different tax treatment depending on the taxpayer's classification, the date on which the costs were incurred and whether the lease is domestic or foreign.

For taxpayers that are not defined as major integrated oil companies, G&G costs incurred in a taxable year are capitalized as an asset, separate from the leasehold cost, and amortized over 24 months beginning on the date that such expense was paid or incurred using the half-year convention.

For taxpayers defined as major integrated oil companies, G&G costs are capitalized and amortized over a period of seven years.

G&G costs incurred in relation to foreign leases are generally treated as part of the leasehold cost and recoverable via depletion deductions.

Development costs

Development expenditures include IDC and tangible property expenditures. IDC is a capitalizable cost, but the current US tax law allows taxpayers to make an election to deduct domestic IDC in the first year it is incurred. This is a taxpayer-level election, and, once it is made, it is binding for all future years. If this election is not properly made, the IDC is capitalized to the leasehold or tangible-property basis and recovered through depletion or depreciation, as appropriate.

In almost all cases, a company will want to make the initial election to deduct domestic IDC because the present value benefit of the tax deduction is generally significant. If the taxpayer is an independent producer that has made the initial election to deduct IDC, the amount of the IDC deduction is equal to 100% of the IDC incurred in the current year. If the taxpayer is an integrated producer that has made the initial election to deduct IDC, the amount of the IDC deduction is equal to 70% of the IDC incurred in the current year, with the remaining 30% capitalized and amortized over a 60-month period, beginning with the month in which the costs are paid or incurred.

If the taxpayer made a proper initial election to expense the IDC, the taxpayer may make a year-by-year election to capitalize some or all of its otherwise deductible IDC. If the IDC is capitalized under this yearly election, it is amortized over a 60-month period beginning with the month in which such expenditure was paid or incurred. Some taxpayers may want to consider this yearly election to capitalize some or all of the IDC as part of their tax planning. Two examples of when the yearly election might be beneficial are when a taxpayer is paying AMT or when a taxpayer has a large net operating loss to carry forward.

IDC on property located outside of the US is capitalized and, based on taxpayer entity election, is either amortized over 10 years or depleted as part of the leasehold-cost basis.

Tangible property is a depreciable asset. Under prior law, taxpayers were allowed to claim bonus depreciation under IRC Section 168(k) in the year in which qualified property was placed in service through 2019 (50% bonus depreciation in 2017, phased down to 40% in 2018 and 30% in 2019). Effective for qualified property acquired and placed in service after 27 September 2017 (subject to certain limitations), taxpayers may be permitted to claim 100% bonus depreciation for qualified property (phased down after 2022: 80% for property placed in service during 2023; 60% for property placed in service during 2024; 40% for property placed in service during 2025; and 20% for property placed in service during 2026). For property not covered under the newly enacted legislation, prior law (see below) may apply. Importantly, however, under current law, the definition of qualified property has been expanded to include used property (subject to numerous limitations and exceptions), among other items.

In lieu of claiming bonus depreciation, taxpayers (in many cases) may elect to depreciate tangible property placed in service during a tax year using either the UoP method or the modified accelerated cost recovery system (MACRS). The UoP method uses a similar ratio used to calculate cost depletion multiplied by the adjusted basis of the tangible equipment; thus, depreciation is calculated over the entire productive life of the property.

The MACRS is based on the class life as determined by the Internal Revenue Service (IRS) on a declining-balance method. For tangible equipment used in the US, the MACRS method is the percentage of the declining balance shown in the table below, which is based on the recovery period of the asset. For foreign assets, taxpayers may use the UoP method or the MACRS method, but they are required to use the straight-line (100%) declining balance over the longer alternative recovery period for MACRS and are not permitted to use the bonus depreciation 100% expensing. Over the years, the IRS has published revenue procedures[8] that list the recovery periods of various types of tangible property. The following table gives examples of the typical oil and gas tangible equipment MACRS recovery periods for domestic assets.[9]

Item	Kind of depreciating asset	Industry in which the asset is used	Period
1	Oil and gas transportation asset, (including trunk line, pipeline and integrated producer-related storage facilities)	Gas supply or transportation	15 years 150%
2	Petroleum and petroleum products distribution asset used for wholesale or retail sales	Marketing petroleum products	5 years 200%
3	Oil production asset (including gathering lines, related storage facilities and platforms, excluding electricity generation assets)	Oil and gas extraction	7 years 200%
4	Gas production asset (including gathering lines, related storage facilities and platforms, excluding electricity generation assets)	Oil and gas extraction	7 years 200%
5	Onshore and offshore platform	Oil and gas extraction	7 years 200%

8 *Rev. Proc 87-56;1987-2.C.B.674.*

9 *TAM 200311003.*

Item	Kind of depreciating asset	Industry in which the asset is used	Period
6	Asset (other than an electricity generation asset) used to separate condensate, crude oil, domestic gas, liquid natural gas (LNG) or liquid petroleum gas for product pipeline quality (i.e., gas processing compression or separation equipment, but not if the manufacture occurs in an oil refinery)	Gas processing (production)	7 years 200%
7	Petroleum refining (including assets used in distillation, fractionation and catalytic cracking of crude into gasoline and its other products)	Petroleum refining	10 years 200%
8	Onshore drilling equipment	Oil and gas drilling	5 years 200%
9	Offshore drilling equipment:		
	For contract drillers	Oil and gas drilling	5 years 200%
	For oil and gas producers	Oil and gas drilling	7 years 200%
10	LNG plant (including assets used in liquefaction, storage and regasification, connections, tanks, related land improvements, pipeline interconnections and marine terminal facilities)	Gas liquefaction and regasification	15 years 150%

Capital allowances for income tax purposes are not subject to credits unless they qualify as R&D costs.

D. Incentives

Exploration

IDC expenditures incurred for property located in the US are immediately deductible for income tax purposes for independent producers, and 70% is deductible for integrated producers. See also Section C.

Tax losses

Under prior law, net operating losses could be carried back two years, and carried forward 20 years (and could offset up to 100% of taxable income). Effective for losses arising in tax years after 2017, however, net operating losses may offset only 80% of the taxpayer's taxable income (determined without regard for the net operating loss). Additionally, effective for net operating losses ending after 31 December 2017, the two-year carryback provision has been repealed (with certain limited exceptions).

Regional incentives

Various state and local governments may give incentives to continue production on properties that are marginally producing, such as waiving production or property taxes, or both.

IRC Section 199 (manufacturing) deduction

Effective for tax years beginning after 31 December 2017, the deduction under IRC Section 199 has been repealed. Under prior law, IRC Section 199 allowed a deduction, which was based on the lesser of the appropriate percentage of qualified production activities income (QPAI) or taxable income, but it was limited to 50% of production wages. QPAI was calculated as the domestic production gross receipts less the cost of goods sold and other expenses and losses or deductions allocable to such receipts.

Research and development

An R&D tax credit may be available for qualifying R&D expenditures. Although the R&D credit has had a long and varied history, it was permanently extended under the Protecting Americans from Tax Hikes (Path) Act on 18 December 2015. It generally allows for two calculation methods: the company may choose the "old" method or an alternative simplified credit (ASC) method.

The ASC method is much simpler than the old method; it eliminates the base period limitations, thereby allowing more taxpayers to qualify for the credit, and it significantly simplifies the calculation. The ASC requires a company to calculate the average R&D expenditures for the three prior tax years. The R&D expenditures that qualify for credit are those in excess of 50% of the three prior years' average expenditures. Qualified small businesses may elect to apply the credit against payroll tax instead of income tax. Under certain circumstances, eligible small businesses may apply the research credit against the AMT.

The R&D credit under the ASC method is 14% if the taxpayer elects to reduce asset bases and deductions for expenditures, or 9.1% if the taxpayer elects not to reduce asset bases and deductions of qualified expenditures.

Additionally, certain states have adopted R&D credit regimes to create incentives for companies.

E. Withholding taxes

Interest, dividends and royalties

Interest, dividends, patent and know-how royalties paid to nonresidents are subject to a final US WHT of 30%, unless modified by treaty or subject to an exception provided by the internal revenue code.

Branch remittance tax

The US imposes a branch profits tax of 30%, unless modified by a treaty.

Foreign-resident WHT

In general, if nonemployee compensation is paid to a nonresident, the company must withhold tax on the payment and remit the withholding to the IRS. The withholding rate is 30%, unless it is reduced by a treaty.

F. Financing considerations

Thin capitalization and related-party debt

The US income tax system contains significant rules regarding the classification of debt and equity. These rules can have a significant impact on decisions made regarding the financing of oil and gas projects, including the following:

- Thin capitalization measures apply to re-characterize debt as equity for related-party debt if the debt-to-equity ratio is too high. No guidance is provided by the IRS, but a debt-to-equity ratio of 3:1 is generally acceptable. Interest expense on any re-characterized debt is prohibited.
- Additionally, current interest expense deductibility may be limited under IRC Section 163(j) to 30% of adjustment taxable income (as determined under applicable law).
- These thin capitalization measures apply to the total debt of US operations of multinational groups (including foreign and domestic related-party debt and third-party debt). The measures apply to all US entities and foreign entities with effectively connected income.

Effective for tax years after 2017, IRC Section 163(j) limits the net interest expense deduction to 30% of the business's adjusted taxable income (ATI). Through 2021, ATI is generally computed without regard to depreciation, amortization or depletion. Thereafter (beginning in 2022), ATI is decreased by those items, thus making the computation 30% of net interest expense exceeding EBIT. However, interest that is disallowed under this rule is carried forward indefinitely (subject to limitations).

The debt or equity classification of financial instruments for tax purposes is subject to prescribed tests under law. These measures focus on economic substance rather than on legal form. On 21 October 2016, the U.S. Department of the Treasury released final regulations under IRC Section 385[10] that attempt to clarify treatment of certain interests as debt or equity for US tax purposes. (A full description or summary of these regulations is beyond the scope of this chapter.)

The debt or equity measures are relevant to the taxation of dividends (including imputation requirements), the characterization of payments from nonresident entities, the thin capitalization regime, and the dividend and interest WHT and related measures.

The US does not impose interest quarantining. Corporate-level debt deductions may be used to offset all income derived by the borrowing entity regardless of the source or the type of income.

G. Transactions

Asset disposals

The disposal of an oil and gas property generally results in a taxable event, unless the disposal qualifies as a statutory nontaxable event (e.g., like-kind exchange and involuntary conversions — see the next subsection). Depletion, depreciation, IDC deductions and IDC amortization are subject to recapture if the proceeds received upon disposal exceed the asset's adjusted basis at the time of disposition; any amounts recaptured are included in taxable ordinary income. If the proceeds are less than the adjusted basis of the asset, a tax loss may be allowed against ordinary income (see Section B).

Like-kind exchanges and involuntary conversions

The US tax statute generally allows taxpayers that exchange certain like-kind property to defer the gain. The taxpayer may have to recognize some or all of the gain immediately if the recapture rules apply. The gain that is deferred is not to be taxed until the newly acquired property is sold. Additionally, if assets are lost or damaged through an involuntary conversion (e.g., hurricane, flood or fire), taxpayers may replace the property with like-kind property and, similarly, may qualify to defer the gain. Specific rules must be followed to take advantage of the gain deferment treatment for both like-kind exchanges and involuntary conversions.

Effective for like-kind exchanges completed after 2017, nonrecognition of gain or loss in like-kind exchange transactions is limited to those involving real property only (which may include operating interests and many nonoperating interests in oil and gas in place). Additionally, a transition rule exists with respect to like-kind exchanges that were initiated, but not completed, before 31 December 2017.

The oil and gas industry often uses these statutory provisions to exchange or replace property and defer potential gain. Gain deferral can be achieved in a variety of circumstances. For example, oil and gas mineral properties are considered to be real property for these purposes, and they can be exchanged for other mineral properties whether developed or undeveloped. Because mineral interests are considered to be real property, royalty mineral interests can be exchanged for working interests. They can also be exchanged for other non-mineral real property (e.g., ranchland). Note that IDC recapture rules may apply to these transactions.

10 T.D. 9790, 2016-45 I.R.B.

Since mineral properties generally consist of both real property (reserves in the ground) and tangible property, care must be taken in evaluating future like-kind exchanges, as nonrecognition treatment will be provided only with respect to like-kind exchanges of real property (effective for like-kind exchanges completed after 2017).

The property received in a like-kind exchange or involuntary conversion uses the carryover basis from the property exchanged. The basis must be adjusted if non-like-kind property is received or any gain is recognized on the transaction.

Abandonment

If an oil and gas property is abandoned or considered worthless for tax purposes, then the adjusted basis remaining in the property may be deducted in the current tax year as a trade or business loss and may be offset against ordinary income.

Sharing arrangements — joint development of oil and gas property

It is common in the US oil and gas industry for entities to enter into sharing arrangements under which one party pays part or all of the development costs of the other party to earn an interest in the mineral property. Two of the most common sharing arrangements are farm-ins and carried interests. If structured properly, these arrangements can be entered into with little or no current income tax implications under the "pool of capital" doctrine. The arrangements must be structured so that the investment made by both parties relates to the same oil and gas property or properties. For example, assume Taxpayer X, owner of the mineral interest, structures an arrangement whereby Company A agrees to drill and pay all the costs for the first well on a tract. If Company A receives an interest in the same property as its only consideration, the arrangement should be accorded nontaxable treatment for both parties. If either party receives cash or noncash consideration for entering into the arrangement, the "other" consideration is likely to be immediately taxable. For example, it is common for the mineral interest owner to receive cash at the time of entering into the sharing arrangement. While the sharing arrangement should be afforded nontaxable treatment, the mineral interest owner generally has a taxable event with respect to the cash received.

It is common for one party to pay a disproportionately larger share of the drilling and completion costs to earn an interest in the mineral property. These disproportionate costs, representing amounts in excess of the parties' percentage interest, may not be fully deductible currently. As a result of these limitations on deductions, it is common to structure these arrangements to be treated as partnerships under US tax law. The partnership structure currently allows the taxpayers to obtain some or all of the deductions that otherwise may be limited. The tax partnership rules are very complicated, and care should be taken because the partnership structure may affect the economic outcome of the arrangement (see the discussion in Section J regarding forms of business presence).

Selling shares in a company (consequences for resident and nonresident shareholders)

Generally, a corporate share disposal is subject to the capital gains tax (CGT) regime. Nonresidents that dispose of shares in a US company are not generally subject to US federal income tax because the domestic tax rules source the gain to the residence of the seller. However, the main exception to this rule is if the stock of a US corporation constitutes a USRPI the company is then treated as a US real property holding company. If it is determined that the stock of a US corporation constitutes a USRPI any resulting built-in stock gain is subject to tax.

Effective for sales and exchanges of partnership interests on or after 27 November 2017, the US treats gain or loss on a foreign partner's sale or exchange of a partnership interest as effectively connected with a US trade or business to the extent of the transferor's share of effectively connected gain or loss. Additionally, under the recently enacted legislation, a withholding requirement may result for the buyer and partnership in connection with such sale or exchange.

H. Indirect taxes

VAT and GST

The US does not have a value-added tax (VAT) or goods and services tax (GST) regime.

Sales and use taxes

Most states and localities (e.g., cities, counties, parishes and transportation districts) impose a sales tax on sales, except on sales for resale. These taxes generally include both tangible personal property and enumerated services. The taxable base generally includes the total amount for which the tangible personal property is sold, including any services rendered by the seller in connection with the sale. Services purchased separately are not generally taxable, unless they are specifically enumerated as taxable.

In addition, most states and localities impose a "use" tax. Use tax is a tax imposed on the storage, use or other consumption of a taxable item purchased, for which sales tax has not already been charged by the seller. Sales and use tax rates typically range from 3% to 9% of the fair value of the taxable item sold.

If a company establishes "nexus" (a presence sufficient that the state has jurisdiction to impose a tax on the company) in a state, it will generally need to obtain a sales tax permit, collect the proper taxes from customers on behalf of the state and file sales tax returns. Although each state has slightly different nexus requirements, a company generally is subject to tax collection requirements if it leases, rents or sells tangible personal property in the state, furnishes services in the state that are taxable under the statute, holds property in the state for resale, maintains a business location in the state, operates in the state through full-time or part-time resident or nonresident salespeople or agents, or maintains an inventory in the state of tangible personal property for lease, rental or delivery in a vehicle owned or operated by the seller.

Property tax

Many states, counties and cities impose ad valorem tax on real or tangible personal property located in the jurisdiction on a specified date each year. Real property and personal property are valued by assessors at fair market value, and tax is assessed as a percentage of the fair market value. Generally, property is assessed according to its status and condition on 1 January each year. The fair market value of real and personal property must be determined by the following generally recognized appraisal methods: the market approach, the cost approach or the income approach.

Severance tax

Many states impose a tax on the extraction of natural resources, such as oil, coal or gas. Returns generally must be filed by each operator or taxpayer that takes production in-kind. The operator must withhold tax from royalty and nonoperator payments. Severance taxes are typically charged based on a volumetric or valuation base for the natural resource and vary in rate from state to state.

Petroleum products tax

Many states impose a tax on petroleum products delivered within the state. Generally, any company that makes a sale of petroleum products to a purchaser in a state that is not a licensed distributor, or does not hold a direct payment certificate, pays a tax based on the gross earnings derived from the sale of the petroleum products.

Other taxes

In addition to imposing the abovementioned taxes, many states impose other state-specific taxes. For example, some states impose an inspection fee on petroleum products distributed, sold, offered or exposed for sale or use, or used or consumed in a state. The inspection fee can be imposed on fuels removed from a terminal using a terminal rack and must be collected by the owner of the inventory, or the position holder, from the person who orders the withdrawal.

Some states impose a tax based on the gross receipts of companies that transport natural gas by pipeline for hire, sale or use, in addition to all other taxes and licenses levied and assessed. Some states impose fees on underground storage tanks under the hazardous waste control law.

Import duties

All goods, equipment and materials that enter the US from overseas are subject to customs import duties. The U.S. Customs and Border Protection (the CBP) regulates imports into the US. The CBP directly processes the clearance of imported goods and enforces the customs regulations of the US. The CBP also enforces the laws of other government agencies that may require special documentation at the time of import or may impose additional obligations upon importers (such as excise tax or other collections).

The customs duty applied to the customs value of imported goods may vary depending on several factors, including the type of commodity, its end use, the constituent materials and the country of origin. Duty rates may be ad valorem (at a percentage) or a specific amount (rate per unit or quantity), or a combination of both. For example, LNG is generally "free" of duty, and greases are dutiable at 5.8% of the import value, while some petroleum products, such as motor fuel and motor fuel blending stock, attract a duty rate of US$0.525 per barrel effective to 1 January 2016. Ethanol that is denatured is subject to an ad valorem duty of 1.9%; it may be subject to an added duty if imported for fuel use and may also be subject to a specific excise tax.

In addition to customs duties, imports arriving by vessel at certain ports are subject to a Harbor Maintenance Fee of 0.125% of the value of the cargo. It is due at the same time as the duty payment.

Upon importation into the US and within 15 calendar days after arrival in US territory, the importer or its representative (a customs broker) must file an "entry" (CF-3461) for the release of the merchandise. Ten working days after the release of the merchandise, the importer is responsible for filing the "entry summary" (CF-7501) with accurate information, together with the appropriate duties, taxes and fees.

It is important to note that, under Section 484 of the Tariff Act, as amended,[11] the importer of record (IOR) is responsible for using "reasonable care" to enter, classify and value imported merchandise. The importer must also provide any other information necessary to enable the CBP to assess duties properly, collect accurate statistics and determine whether any other applicable legal requirement is met. Even when the IOR uses a customs broker to make the entries, the importer remains liable for the customs broker's acts made on its behalf, including any broker errors.

Export duties

There are no duties applied to goods exported from the US. In December 2015, the United States passed legislation lifting the nearly four-decade ban on crude oil exports.

Excise tax

The US federal excise tax is applied to some goods manufactured in the US, including petroleum products, alcohol, tobacco and some luxury products. Excise taxes are imposed on all the following fuels: gasoline (including aviation fuel and gasoline blend stocks), diesel fuel (including dyed diesel fuel), diesel-water fuel emulsion, kerosene (including dyed kerosene and kerosene used in aviation), other fuels (including alternative fuels), compressed natural gas (CNG) and fuels used in commercial transportation on inland waterways. It is important to note that some excise taxes other than fuel taxes affect the oil and gas industry, most notably environmental taxes, such as the oil spill liability tax.

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11 19 US Code §1484.

The excise tax varies depending on the product. For example, the 2017 excise tax on gasoline is US$0.183 per gallon, and on aviation gasoline, it is US$0.193 per gallon. The excise tax on diesel fuel and kerosene is US$0.243 per gallon, with an additional US$0.001 per gallon for the Leaking Underground Storage Tank Trust Fund.

Excise taxes may also be imposed at the state level and vary by product and state. For current information pertaining to state-level excise taxes, please consult with any of the oil and gas contacts listed for the US.

The rate of the oil spill liability tax is presently US$0.09 per barrel; this rate is scheduled to be in effect until 31 December 2017, at which point the oil spill liability tax will terminate without congressional action to extend the tax. As this rate may be modified by Congress after this publication, readers are advised to consult with any of the oil and gas contacts listed for current rates. This tax generally applies to crude oil received at a US refinery and to petroleum products entering the US for consumption, use or warehousing. The tax also applies to certain uses and the exportation of domestic crude oil. The time when the tax is imposed, as well as the entity that is liable for it, depends on the specific operations of importing or exporting.

Stamp duty

The US does not have a stamp duty regime.

Registration fees

The US does not impose registration fees at the federal level. Some states impose a transfer tax on the transfer of title of tangible or real property.

I. Preference programs

Foreign trade zones

Foreign trade zones are established to encourage and expedite US participation in international trade, to foster dealings in foreign goods imported not only for domestic consumption but also for export after combination with domestic goods, and to defer payment of duties until goods are entered into the commerce of the US.

There are two kinds of foreign trade zones:

- General purpose zones (often an industrial park or port complex whose facilities are available for use by the general public)
- Subzones (normally, single-purpose sites when operations cannot feasibly be moved to, or accommodated by, a general purpose zone)

The main financial benefits of foreign trade zones include duty deferment, duty elimination on exports, duty reduction (inverted tariff relief) and local ad valorem tax exemption. Other benefits include lower administrative costs, lower security and insurance costs, no time constraints on storage, shorter transit time and improved inventory control. There are also community benefits, such as the retention of existing jobs, attraction of new employment, investment in the local community, local improvements to infrastructure and increased local purchases of goods and services.

Duty drawback

A drawback is a refund, reduction or waiver, in whole or in part, of customs duties and certain other taxes collected upon the importation of an article or materials that are subsequently exported or used in the production of goods that are exported. Several types of drawback are authorized under Section 1313, Title 19, of the US Code: manufacturing, unused merchandise and rejected merchandise.

Specific guidelines apply for a drawback between the members of the North American Free Trade Agreement (NAFTA) (NAFTA drawback claim). Under the NAFTA drawback regime, the rule known as "the lesser of the two" is sometimes applied. There are also specific collections that cannot be refunded, waived or reduced by a NAFTA country as a condition of export.

Other significant taxes

Other significant US taxes include payroll taxes paid by employers, including social security tax at the rate of 6.2% up to the annual wage limitation (for 2018, the limit is US$128,700 per employee) and Medicare tax at the rate of 1.45% with no income limitation. Additionally, individuals with earned income of more than US$200,000 (US$250,000 for married couples filing jointly) pay an additional 0.9% in Medicare taxes.

J. Other

Foreign Investment Review Board

The US Government does not allow foreign companies to purchase offshore leases directly. Additionally, the U.S. Department of Commerce requires foreign parties to report investment in the US on a quarterly and annual basis if certain criteria are met.

Forms of business presence

Forms of business presence in the US typically include corporations, limited liability companies, foreign branches, joint ventures (incorporated and unincorporated) and partnerships (e.g., general partnerships, limited partnerships). In addition to commercial considerations, the tax consequences of each type of entity are important to consider when setting up a business in the US.

Unincorporated joint ventures are commonly used by companies for the exploration and development of oil and gas projects. Unincorporated joint ventures are treated as tax partnerships under US tax law, unless the joint venture owners elect to take production in kind and not be treated as a partnership. Partnership operations "flow through" the entity, meaning that the income and deductions are reported by the partners on their tax returns. Therefore, all US federal income tax is paid by the partners, not at the entity level. Additionally, there are very complex rules that must be followed that deal with partnership capital accounts.

There are various US reporting requirements for tax partnerships (e.g., a federal information tax return must be filed annually). In addition, if there are foreign partners, tax withholding and reporting may be required. Lastly, most states treat partnerships as flow-through entities and require information returns to be filed. But some states impose income tax at the partnership level or require the partnership to withhold, remit and file reports on partner distributions to out-of-state or foreign partners.

Uruguay

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Tax regime applied to this country

- ■ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

- Concession agreements — these apply
- Production sharing contracts — not used
- Corporate income tax (CIT) rate — 25%
- Royalties — none
- Bonuses — none
- Resource rent tax — none
- Capital allowances — see Section C
- Investment incentives — see Section D

B. Fiscal regime

According to Article 1 of Decree-Law No. 14,181, oil and natural gas reserves situated in Uruguayan territory, in any state, belong to the Uruguayan nation. Their exploration and exploitation (including research activities) may be performed only by the state.

ANCAP (*Administración Nacional de Combustibles, Alcohol y Portland*) is the state agency in charge of oil and gas activities. It is allowed to hire third parties on its behalf to perform exploration and exploitation activities, either individuals or legal entities, nationals or foreign, publicly or privately owned. Contractors' remuneration may be fixed in money or goods, and contractors may freely export oil and gas corresponding to them according to contractual clauses.

In accordance with Article 16 of Decree-Law No. 14,181, the activities of exploration, exploitation, transportation and commerce in relation to oil and natural gas have been exempted from all national taxes, except for the following:

- Any applicable CIT
- Social security contributions

These exemptions apply exclusively to ANCAP and its direct contractors.

Corporate income tax

CIT applies to Uruguayan-sourced income, derived from activities performed, goods situated, or rights economically exploited in Uruguay and obtained by resident legal entities or nonresidents operating through a permanent establishment (PE) in Uruguay. CIT is applicable at a fixed 25% rate on net taxable income (gross fiscal income minus deductible expenses).

According to the general tax regime, expenses are deductible for CIT if accrued in the fiscal year, if appropriately documented, if necessary to obtain/maintain Uruguayan-sourced income and if subject to taxation (in Uruguay or abroad). Expenses should be real, and their amount in accordance with the economic advantage obtained by the taxpayer.

All of the expense should be deductible if the counterparty taxpayer is taxed at a rate of 25% or more; if not, only part of an expense should be deducted in proportion to the rates — for example, if the expense is subject to 12% withholding tax in Uruguay, then 48% (12% out of 25%) of the expense should be deductible by the taxpayer.

Uruguayan companies should obtain certificates issued by foreign tax authorities or private audit firms abroad stating the effective income tax rate applicable to the counterparty's income, so that expenses can be deducted in proportion to effective foreign tax rates.

If the local company is a PE of a foreign entity, expenses incurred abroad may be deducted only if considered necessary to obtain and maintain Uruguayan-sourced income and if their origin and nature can be reliably determined. The same treatment should apply between a local company and its PE abroad, or between two PEs of a single entity with one located in Uruguay and another elsewhere. In any case, in order for the deduction to be allowed, these expenses should have been actually incurred or the services actually rendered, and allocated according to technically sustainable criteria. For PEs, a pro rata allocation of services is generally not allowed.

Additionally, transfer pricing regulations have been applied in Uruguay since 2007 for CIT purposes.

Nonresidents' income tax

As a general rule, companies should pay income tax on their Uruguayan-sourced income derived from their operations.

In case no PE arises in Uruguay, then the nonresident extractive company should be subject to a 12% nonresidents' income tax (NRIT) on the Uruguayan-sourced income derived from its activities. The applicable tax rate since 1 January 2017 would be 25% on income (except for dividends) of entities resident, domiciled, incorporated or located in countries or jurisdictions with low or null taxation or that benefit from a low or null taxation regime (LONT entities) in accordance with Law No. 19,438. An additional rate of 5.25% would apply on income derived from capital gains of real estate located in Uruguay obtained by the referred entities according to Law No. 19,484. If a nonresident company is hired by a local CIT-paying client, tax should be withheld directly from the nonresident company by that client.

Services rendered inside Uruguay should be considered of Uruguayan source. Furthermore, technical assistance services rendered from abroad to corporate income taxpayers should also be considered as of Uruguayan source and thus subject to withholding tax. Starting January 2018, income from nonresident entities that render services directly through the internet, technological platforms, computer applications or similar means will be considered to be entirely Uruguayan-sourced income, for income tax purposes, when the acquirer is located in Uruguay. Income derived from mediation and intermediation in the supply and demand of services rendered through the internet, technological platforms, computer applications or similar means will be 100% Uruguayan sourced when the supplier and the acquirer of the service are located in Uruguay. The income will be 50% Uruguayan sourced if either the supplier or the acquirer of the service is located abroad. Unless otherwise proven, the law will treat the acquirer of the services as located in a Uruguayan territory when the services are paid for through electronic means managed in Uruguay, including electronic money instruments, credit or debit cards, bank accounts or other similar payment options established through regulations in the future.

If the company constitutes a PE in Uruguay, it should pay CIT on amounts of Uruguayan-sourced net taxable income at a 25% rate. As a consequence, the 12% NRIT should not apply in this case. As a PE, the company should register in

Uruguay for tax purposes by appointing a local representative (jointly liable for the nonresident's tax responsibilities in the country). In addition, the PE should maintain sufficient accounting records for tax purposes.

Net wealth tax

Net wealth tax is levied on assets located inside Uruguay at the tax year-end, valued according to tax criteria. The deduction of certain liabilities is allowed (such as average loans with local banks and accounts payable related to acquisition of goods and services, among others). The annual rate is 1.5% for legal entities. The rate applicable on the taxable equity of LONT entities that do not have a permanent establishment in Uruguay is 3%.

Group relief

Uruguay does not allow so-called group relief.

Statute of limitations

The statute of limitations in Uruguay permits a period of five years to bring a case to court, but that period may be extended to 10 years in a case of tax fraud. In force since 2016, and with respect to taxes related to benefits granted under the Uruguayan investment Law, No. 16,906, the statute of limitations will be suspended until the end of the term established either for the accomplishment of the project goals or for the utilization of the benefits (whichever term is longer).

Unconventional oil and gas

No special terms apply for unconventional oil or unconventional gas.

C. Capital allowances

For taxable income subject to a total 25% tax, investments in production facilities, pipelines and installations (tangible assets) used in extractive activities are depreciated over their estimated useful life. Urban buildings should be depreciated over a 50-year period. In general, tangible assets should be revalued according to the variation in prices measured through the national products producer price index (Spanish acronym IPPN, an inflation index), published by the National Statistics Institute of Uruguay. The National Budget Law No. 19,355 established that the consumer price index should be used for fiscal years started on or after 1 January 2016 for the actualization of fixed assets.

Intangible assets may be recognized for tax purposes if a real investment has been made and the seller has been duly identified. They cannot be revalued and should be depreciated over a five-year period. Goodwill cannot be depreciated for tax purposes. According to Decree No. 181/015, the intangible assets acquired from 1 July 2015 on should be depreciated, at a fixed quota in the number of years of expected life of these goods. In those cases in which it is not possible to determine the expected life of those goods, they shall be depreciated for 10 years.

Taxpayers will have to establish the estimated useful life when submitting the first tax return after the good's acquisition and will not be able to change it without the tax office's (*Dirección General Impositiva*) authorization. Such authorization would be granted only if the change is technically justified, and approved by the tax office. Public works concessionaires may opt to depreciate concession investments over a 10-year period or during the useful life of the actual investments. In the latter option, the depreciation period cannot exceed the duration of the contract, and "useful life" should be justified through certification by a qualified professional.

In case of the final concession awards granted as from 1 July 2015, this type of intangible asset can be depreciated in a 10-year period as long as it has been specifically included in the bid specifications.

A particular regime applies with regard to software amortization, which will be deductible only if the general deductibility requirements are met for CIT purposes. This provision includes the counterparty rule requirement by which expenses are deductible only if the counterparty is subject to income taxation (in Uruguay or abroad) of at least 25%.

D. Incentives

Tax losses

Losses may be carried forward for up to five years. Nevertheless, since 1 January 2017, companies are allowed to offset only 50% of their taxable income with net operating losses (NOLs) due to Accountability Law No. 19,438. It is compulsory to adjust the value of losses by applying the appropriate variation in the IPPN. The National Budget Law No. 19,355 established that the consumer price index should be used for fiscal years started on or after 1 January 2016 for the actualization of NOLs.

No loss carryback is allowed, nor can losses be transferred to other taxpayers through mergers or any other means.

Decree No. 68/013

Decree No. 68/013 provides terms for hydrocarbon exploration in areas offshore Uruguay under the agreements awarded as a result of so-called "Uruguay Round II." The agreements are made between ANCAP and the oil companies selected.

According to the Decree, contractors that concluded their contracts under the terms of Uruguay Round II would have:

- A tax credit for value-added tax (VAT) included in the acquisitions of goods and services required for hydrocarbon exploitation activities if the subcontractors are CIT or NRIT taxpayers.
- A right to import and re-export, free of any fee, tax, cost, right, quota, payment or any other restriction, the machinery, equipment, materials, tools, vehicles, and inputs necessary for developing hydrocarbon exploitation activities.

Additionally, subcontractors that concluded their contracts under the Uruguay Round II could enjoy the following provisions:

- Exemption from CIT or NRIT for Uruguayan-sourced income derived from hydrocarbon exploitation activities
- VAT exemption for the sale of goods and the provision of services related to hydrocarbon exploitation activities
- A tax credit for VAT included in the acquisitions of goods and services related to hydrocarbon exploitation activities if the subcontractors are CIT or NRIT taxpayers
- Exemption from net wealth tax for the goods and rights related to hydrocarbon exploitation activities
- A right to import and re-export, free of any fee, tax, cost, right, quota, payment or any other restriction, the machinery, equipment, materials, tools, vehicles and inputs necessary for developing hydrocarbon exploitation activities

This Decree became effective on 5 October 2012.

Promotion of investments

The promotion of investments has been regulated by Law No. 16,906 and, at present, by Decree No. 2/012. To qualify for tax incentives on investments, CIT-paying companies must be engaged in activities considered to be promoted (as described below).

Promotion has to be approved by the executive power, taking into consideration not only the amount of local investment but also the extent to which the activities to be performed are aimed at achieving the following goals of increasing:

- Employment in the country
- Improvement in geographical decentralization
- Exports
- Use of environment-friendly technologies (such as wind energy)
- Research, development and innovation
- Specific indicators

Regarding CIT, the amount of the exemption depends on the total amount of investment, and can vary up to 100% of the investment, although the exemption may not exceed 60% of tax payable at fiscal year-end.

The benefits to be derived from the Government's promotion of investments scheme are granted for a period of time, determined by taking into account the amount of investment and, after certain conditions have been met, to be considered as a promoted investment.

If promotion is granted, in general, the executive power also grants the following additional benefits:

- Net wealth tax exemption on movable assets and real estate (the latter for a period of 8–10 years)
- Import taxation exemption (VAT, customs duties and others); this exemption should apply only to goods that do not compete with national industries, and prior authorization by the Ministry of Industry must be obtained
- VAT on local acquisitions of goods and services related to real estate may be recovered through certificates of credit

According to the National Budget Law No. 19,355, if the company applied the benefits of this regime, the limitation period of five years would be extended until the finalization of the deadlines granted to comply with the conditions that required the exemption are met, or until the end of the time limit established for the utilization of the fiscal benefits. If the conditions are breached, the limitation period of the right to collect taxes that would have been wrongly exonerated would be interrupted by notification of a resolution that revokes all or part of the benefits granted or from a resolution of the application committee that would state the non-fulfillment of the commitments made and the reassessment of taxes.

Free trade zones

Law No. 15,921 declared of national interest the promotion and development of free trade zones (FZs), which were created to promote investments, to expand exports, to use the Uruguayan workforce and to encourage international economic integration.

Companies established in an FZ may not carry on industrial or commercial activities or render services in Uruguayan territory (other than an FZ). Notwithstanding of this, Law No. 19,566 of 2017 (in force starting March 2018), allows services that are rendered to third countries from the FZ to also be rendered from the FZ to corporate income taxpayers inside Uruguayan, non-FZ, territory. Retail trading is also forbidden inside an FZ; however, the new law allows retail activities between FZ users and providers and between users. Commercial and service activities to final consumers who are employees of the FZ will be allowed as well.

At least 75% of an FZ company's personnel must be Uruguayan nationals. The abovementioned new Law states that this minimum requirement could be reduced with authorization of the Executive Power, under certain circumstances. When granting the authorization, the Executive Power could additionally require the users to implement training programs with the purpose of reaching the minimum quota of Uruguayan citizens. For service activities, the Executive Power could reduce the minimum employment requirement to 50% of Uruguayan nationals, when the nature of the business deems it necessary.

FZ companies are exempt from national and local taxes related to their activities in the FZ. The exemption does not cover:

- Social security contributions
- Taxes to be paid as withholding agent (such as personal income tax or NRIT) in certain cases

In general, goods and services introduced into an FZ, as well as products manufactured in them, may be sent abroad without restrictions. However, goods introduced into an FZ lose Uruguayan certificate of origin. As a consequence, customs advantages of MERCOSUR (the economic union formed by several countries including Brazil, Argentina, Paraguay, Venezuela and Uruguay) are also lost.

Temporary admissions regime

Companies may request the local authorities to apply the "temporary admissions" regime, under which they import raw materials, subject them to an industrial process, or finished goods and then export them. The time between import and export of materials should not exceed 18 months.

Under this regime, raw materials may be imported without paying any customs duties, VAT or any other applicable taxation on imports. However, if raw materials or finished goods are not exported in due time, customs duties, VAT or other applicable taxes should be paid, with the corresponding penalties and interests.

E. Withholding taxes

Dividends and other profit distributions

Dividends paid from a Uruguayan subsidiary to nonresidents (companies, individuals or branches) or to Uruguayan tax-resident individuals are subject to a 7% withholding tax applicable on the total amount of dividends paid or accrued if the dividends are paid out of income subject to CIT. Dividends and branch remittances paid out of income not subject to CIT are exempt from tax. Dividends subject to withholding tax cannot exceed the taxable profit of the company.

For tax purposes, any capital redemptions paid or credited to NRIT taxpayers or personal income tax (PIT) taxpayers exceeding the nominal value of the shares for which redemption is being paid should be treated as dividends and thus subject to the abovementioned withholding tax regime.

As of March 2017, notional dividends withholding apply on net taxable income that is more than three years old — while certain investments could be deducted — at a 7% rate. This withholding would be creditable against the final tax for dividends effectively distributed.

Royalties

In general, royalty payments to nonresidents should be subject to a 12% withholding tax. The applicable tax rate since 1 January 2017 would be 25% for LONT entities in accordance with Law No. 19,438.

Interest

Please refer to Section F below.

Technical assistance services

In general, a 12% withholding tax should apply to the payment of services to nonresidents if the services rendered could be considered as technical assistance services. The applicable tax rate since 1 January 2017 would be 25% for LONT entities in accordance with Law No. 19,438. The effective rate could drop to 0.6% for non-LONT entities or to 1.25% for LONT entities if 90% of the local company's income is not subject to CIT.

All services performed by nonresidents inside Uruguayan territory should be subject to 12% withholding tax (whether technical or not). The applicable tax rate since 1 January 2017 would be 25% for LONT entities in accordance with Law No. 19,438.

Net wealth tax

CIT taxpayers should withhold 1.5% from the total amount of accounts payable owed to nonresident entities without permanent establishment in Uruguay at 31 December each year. The rate applicable for accounts payable with LONT entities that do not have a permanent establishment in Uruguay is 3%. An exemption should apply for liabilities arising from imports of goods and loans.

VAT

VAT withholding may apply when services are performed by nonresidents inside Uruguayan territory, at a rate of 22%. The withholding tax amount may be recovered by the local VAT payer through its own tax liquidation if the service is directly or indirectly related to VAT-applicable operations.

F. Financing considerations

Thin capitalization

Uruguay has no thin capitalization rules. However, there is an exception by which financial operations between a parent and its branch are considered as equity accounts.

Interest taxation

In general, interest paid to nonresidents should be subject to a 12% withholding tax on the total amount of interest paid.

VAT at 22% should apply on local interest. Interest derived from public or private securities, bank deposits and warrants is VAT-exempt.

G. Transactions

Asset disposals

In general, the disposal of assets is taxable, or deductible at the 25% tax rate, for Uruguayan entities or nonresident entities with permanent establishments in the country. Disposal of fixed assets offshore should not be taxable for CIT purposes.

Disposals of capital participations

Direct transfers of a participation interest in a Uruguayan subsidiary owned by individual residents or any nonresidents should be taxed at a 12% rate applicable to 20% of fair market value (FMV). A 2.4% effective rate would apply in this case. A third-party valuation should be undertaken to ascertain the FMV. Furthermore, if capital participations are transferred by LONT entities, a 25% rate would apply on 30% of the price (which should also be equal to FMV). In this sense, a 7.5% effective rate would be applicable.

In order to pay this tax, nonresidents should register in Uruguay for tax purposes and appoint a Uruguay tax resident as a representative (jointly liable for the nonresident's tax responsibilities). Sales performed by CIT taxpayers should be taxable at 25% applicable on net taxable income.

In regard to indirect transfers of participations, generally no capital gains taxation would apply in Uruguay. Nevertheless, when the share or equity participation transferred is of a LONT entity and more than 50% of that entity's assets, valued according to CIT rules, are integrated, directly or indirectly, from goods located in Uruguay, the transaction should be taxable.

Disposal of a participation interest in a foreign entity should also not be a taxable event in Uruguay.

H. Indirect taxes

VAT

In general, VAT is levied on circulations of goods and supplies of services inside Uruguayan territory, as well as on imports of certain goods. No VAT should apply for goods commercialized or services rendered abroad. The general VAT rate is 22%, although a minimum 10% rate should apply for some specific goods and transactions. On imports, VAT rates should be applied on normal customs value plus customs duty.

Advanced payments for imports may be required, as follows:

- Advanced VAT at 10% (for imports of goods taxed at 22%) or 3% (for imports of goods taxed at 10%) of total customs value plus customs duty:

    - The VAT rate applicable depends on the customs item number of the goods to be imported. Some goods may be exempted from VAT on import.
- Advanced CIT at 15% or 4% of total customs value:
    - The rate here again depends on the customs item number of the goods to be imported. Some goods may be exempted.

These advanced payments can be deducted from the company's tax liabilities.

VAT applicable on the importation of goods should be recovered by the taxpayer as input VAT. Input VAT directly or indirectly related to nontaxable operations for VAT cannot be recovered; in contrast, input VAT directly or indirectly related to taxable operations or exports can be recovered.

As long as the extracting company is VAT-registered (as a PE, subsidiary or other structure), it can recover input VAT on local purchases of goods and services. Recoverable input VAT should be exclusively those amounts directly or indirectly related to taxable VAT operations or exports.

In the case of input VAT, refunds related to exports may be obtained monthly through the request of certificates of credit from the tax authorities. These certificates of credit may be used to pay a taxpayer's own taxes or social security contributions or to pay local suppliers from which the company originally purchased those goods and services (who may in turn use these to pay for their own taxes or social security contributions).

Imports of oil into Uruguay are VAT-exempt, as well as the internal circulation of combustible materials derived from oil (except fuel oil and gas oil).

Income derived from mediation and intermediation services related to the supply and demand of services rendered through the internet, technological platforms, computer applications or other similar means will be considered as Uruguayan-sourced income and, therefore, subject to VAT at a 22% rate when both parties are located in Uruguay.

Additionally, for VAT purposes services provided directly through the internet, technological platforms, computer applications or other similar means will be considered as entirely rendered in Uruguayan territory, provided the services are used in Uruguay, and will generate Uruguayan-sourced income subject to VAT at a rate of 22%.

Unless otherwise proven, the law will treat the acquirer of the services as located in a Uruguayan territory when the services are paid for through electronic means managed in Uruguay, including electronic money instruments, credit or debit cards, bank accounts or other similar payment options established through regulations in the future.

Excise tax

Excise tax is an indirect tax levied on the first sale of certain luxury products performed within Uruguayan territory. Among its range of taxable goods is the transfer of combustible materials derived from oil, for which excise tax rates vary from 0% to 133%.

The direct sale of oil is exempted.

Stamp tax/transfer tax

There are no stamp or transfer taxes in Uruguay that should apply to petroleum extraction activities.

I. Other

Tax returns and tax assessments

Companies engaged in extraction activities must register with the Uruguayan tax authorities within 10 days before the beginning of any taxable activity. Registration is not automatic; certain information must be filed with the tax authorities.

CIT and net wealth tax returns

Year-end tax returns and tax payments for CIT and the net wealth tax must be lodged/paid within four months after the end of the relevant fiscal year. For large taxpayers, tax returns must be filed along with audited financial statements. All interim returns are not compulsory.

VAT returns

For large and medium-sized taxpayers, VAT returns should be filed monthly; for smaller taxpayers, VAT returns should be filed annually (within two months after fiscal year-end).

Withholding tax returns should be filed monthly.

Companies are also obliged to perform monthly CIT, net wealth tax and VAT advanced payments.

The deadlines for tax return filings and tax assessments are fixed by tax authorities annually.

Tax authorities may audit any tax return within the period of limitations, regardless of the date these are actually filed.

Transfer pricing reporting and documentation requirements

Transfer pricing (TP) regulations in Uruguay are contained in the CIT laws and several related executive power decrees. TP regulations were enacted in 2007 and became effective in 2009, based on the arm's-length principle, and are in many aspects consistent with the Transfer Pricing Guidelines of the Organisation for Economic Co-operation and Development (OECD). The TP regulations allow advance pricing agreements (APAs), but advance customs valuation agreements (ACVAs) are not allowed at present.

Transfer pricing has become one of the most controversial issues for multinational companies in Uruguay when facing tax authorities' audits.

Local companies are required to submit TP information on an annual basis when meeting either of the following circumstances:

- When they engage in transactions included in this system for amounts exceeding 50 million indexed units (equivalent approximately to US$6.5 million)

  Or
- When notified by the tax authorities

TP information should include:

- An informative return including a breakdown and quantification of transactions for the period that have been included in the TP system
- A copy of financial statements for the related fiscal year, when not required to be submitted under other provisions
- A TP study

TP information should be filed within nine months after fiscal year-end.

If tax adjustments for CIT purposes should result from the TP submissions, the adjustments should be included in the corresponding return within four months after fiscal year-end.

According to local regulations, TP analysis may be performed considering either the local taxpayer or the nonresident counterparty.

If a TP study is performed abroad, the local company should obtain a document certified by an independent well-known auditor (duly translated if necessary) regarding the relevant study.

Uzbekistan

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ■ Profit-based special taxes
  - ■ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

This article describes the fiscal regime in force as of 1 January 2018, which is applicable to almost all subsurface users in Uzbekistan except for those operating under production sharing agreements (PSAs) signed with the Government of Uzbekistan.

The generally applicable fiscal regime that applies in Uzbekistan to exploration and production (E&P) contracts in the oil and gas industry consists of a combination of corporate income tax (CIT), bonuses, subsurface use tax, excess profits tax (EPT) and other generally established taxes and contributions.

Bonuses

The subsurface users are subject to both a signature bonus and a commercial discovery bonus.

Subsurface use tax

Companies conducting extraction or processing of natural resources are obligated to assess and pay a subsurface use tax (similar to a royalty). The rates vary depending on the type of mineral extracted or processed.

Excess profits tax

Subsurface users extracting, producing and selling natural gas (export) and certain other products are generally subject to EPT.

Corporate income tax

CIT is applied to all companies under the general tax regime at a rate of 14%.

Investment incentives

Foreign companies engaged in exploration and prospecting for oil and gas are provided with certain tax incentives.

B. Fiscal regime

The generally applicable fiscal regime that applies in Uzbekistan to E&P activities in the oil and gas industry (except for PSAs) consists of a combination of CIT, bonuses, subsurface use tax, EPT, and other generally established taxes and contributions.

The taxes applicable to subsurface users are as set out in the table below.

Applicable taxes	
Bonuses	Variable
Subsurface use tax	2.6% to 30%
EPT	50%
CIT	14%
Excise tax	Variable
Value-added tax (VAT)	20%
Contributions on revenue	3.2% in total
Unified social payment	25% (15% for small businesses)
Property tax	5%
Land tax	Variable, depends on location and other characteristics of a land plot
Water use tax	Variable, generally immaterial
Other taxes and contributions	Variable

Bonuses

Subsurface users are generally subject to both a signature bonus and a commercial discovery bonus.

Signature bonus

The signature bonus is a one-off payment levied on subsurface users for the right to conduct prospecting and exploration for mineral resources.

Depending on the type of the mineral resource, the amount to be paid to the Government varies from 100 to 10,000 times the minimum monthly wage (MMW), while for hydrocarbons, it is 10,000 MMW. One MMW is set at UZS172,240 (approximately US$21) as of 1 January 2018.

Commercial discovery bonus

The commercial discovery bonus is a fixed payment by subsurface users when a commercial discovery is made on the contract territory.

The base for calculation of the commercial discovery bonus is generally defined as the world market value of the extractable minerals duly approved by the competent state authorities (while for certain subsurface users having a market share dominance, an established value is used, and in certain cases a cost plus formula is used). The rate of the commercial discovery bonus is fixed at 0.1% of the value of approved extractable resources.

Subsurface use tax

The taxpayers of subsurface use tax are defined as legal entities conducting the extraction or processing of minerals. The taxable base is generally the average actual sales value of extracted (processed) minerals. The rates differ depending on the type of minerals extracted or processed (30% for natural gas, 20% for crude oil and gas condensate).

Excess profits tax

Subsurface users extracting, producing and selling natural gas (export), cathode copper, polyethylene granules, cement and clinker are generally subject to EPT (excluding white cement, and excluding cement and clinker produced using coal as alternative fuel). In general, the taxable base is the difference between the selling price and the cut-off price set by legislation, as well as certain taxes.

Currently, the established tax rate is 50% for all the above products. EPT for natural gas is generally calculated as follows:

Product	Taxable base (cut-off price)	Tax rate
Natural gas	Selling price above US$160 per 1,000 cubic meters	50%

Taxpayers are also obliged to transfer excess profit remaining after taxation to a special investment account at the time when the EPT payment is due. These special-purpose funds are disbursed only with the approval of the Ministry of Economics and the Ministry of Finance of the Republic of Uzbekistan for financing investment projects and for modernization and technical upgrading of main production, among other things. In other words, these funds are set aside from normal operations for specific purposes that are controlled by the Government.

Subsurface users operating under PSAs are not subject to EPT.

Corporate income tax

CIT is applied to all companies under the general tax regime at the rate of 14% in respect of taxable income. "Taxable income" is calculated as the difference between aggregate annual income (after certain adjustments) and statutory deductions. The following items are generally not deductible for tax purposes:

- Non-business expenses
- Entertainment, business travel and certain voluntary insurance expenses in excess of established statutory limits
- Interest on overdue and deferred loans (in excess of normal loan interest rate)
- Losses resulting from misappropriations of funds or assets
- Charitable donations
- Litigation expenses
- Fines and other monetary penalties

Special deductions

Taxable profits may be reduced by certain special deductions, including the following:

- Amounts reinvested in main production in the form of purchases of new technological equipment, new construction, and reconstruction of buildings and facilities used for production needs (less current depreciation), up to 30% of taxable profits, over a five-year period
- Charitable donations of up to 2% of taxable profits
- Net excess profit if subject to EPT

Depreciation

The applicable depreciation rates in Uzbekistan are given in the following table:

Assets	Rate (%)
Buildings and structures	5
Trains, ships, airplanes, pipelines, communication equipment, and electric power lines and equipment	8
Certain special transport, plants	10
Production machinery and equipment	15
Cars, computers and office equipment	20
Other assets	15

Intangible assets are amortized for tax purposes over the useful life of the asset, the life of the company, or five years (if useful life cannot be determined), whichever is the least.

Relief for losses

Tax losses can be carried forward for five years. However, the amount of losses carried forward that may be deducted each year is subject to a limit of 50% of taxable profits for the year. Losses incurred during a CIT exemption period (i.e., a period during which a company might have been on a CIT holiday (where exemption is granted for certain period of time) as a result of a special incentive) cannot be carried forward.

Groups of companies

The tax law does not allow offsetting profits and losses among members of a tax group.

Capital gains

Capital gains are generally included in taxable profits and are subject to tax at the regular CIT rate. Capital gains received by a nonresident from the sale of shares or participation interest in an Uzbek-resident legal entity are subject to withholding tax (WHT) at a rate of 20%. This rate may be reduced or eliminated by virtue of a double tax treaty between Uzbekistan and the country of residence of the income recipient.

Unconventional oil and gas

No special tax terms apply to unconventional oil or unconventional gas.

C. Investment incentives

In accordance with the Presidential Decree dated 28 April 2000 (as amended), "On measures of attraction of direct foreign investments into prospecting and exploration of oil and gas," foreign companies engaged in exploration and prospecting for oil and gas are supported by certain tax incentives, including, in part, the following:

- Exemption from all taxes and mandatory contributions for the period of exploration and prospecting
- Exemption from customs payments (including import customs duties, import excise tax and import VAT, but excluding a customs processing fee) on imported equipment and technical resources necessary for conducting prospecting and exploration

In accordance with the Presidential Decree, joint ventures involved in the production of oil and gas, established with the participation of foreign companies that were engaged in exploration and prospecting for oil and gas, are exempt from CIT for seven years from the commencement of oil and gas production.

By a special resolution of the government (or investment agreement), a company with foreign investments may potentially be granted additional tax exemptions and other benefits, depending on the importance of the company's project to the Government, the volume of the investment to be made and other factors.

D. Withholding taxes

In the absence of a permanent establishment (PE) in Uzbekistan of a nonresident company, Uzbek WHT applies to a nonresident's income derived from Uzbekistan sources. The general WHT rate is 20% (dividends, interest, insurance premiums — 10%; international communications and freight — 6%). Double tax treaties may also provide for either exemption from Uzbek WHT or application of reduced WHT rates.

Dividends and interest paid by Uzbek companies domestically (except for interest paid to Uzbek banks) are subject to 10% domestic WHT.

E. Financing considerations

There are no thin capitalization rules in Uzbekistan.

F. Indirect taxes

Import duties

The import of goods and equipment is generally subject to import customs duties at various rates (if any) based on the established list (according to customs classification codes). There are certain exemptions provided by the legislation.

Excise tax

Companies producing or importing excisable goods in the territory of Uzbekistan are subject to excise tax. The list of excisable products with the respective tax rates is established by legislation. Natural gas and liquefied gas producing companies must assess tax on the sale or disposal of the products at the rates of 25% and 26%, respectively, including export sales (but excluding sales to the general population).

Fuel products are indexed to certain rates depending on the type of products sold or disposed of and may not be less than certain minimum tax amounts established for each fuel product. The import of distillates is subject to 5% excise tax.

VAT

VAT is imposed on the supply of all goods and services, including imports, unless they are zero-rated or exempt. Hence crude oil, natural gas and gas condensate sold in the territory of Uzbekistan are subject to 20% VAT. Export sales of certain goods, including sales of crude oil, natural gas and gas condensate, are subject to zero-rated VAT, which means that the entities may generally offset respective input VAT against other taxes and contributions or recover it (based on certain administrative procedures and limitations). Imports of goods and equipment are generally subject to 20% import VAT.

Place-of-supply rule

The applicability of Uzbek (reverse-charge) VAT on "imported" works and services purchased from nonresidents is determined based on the deemed place of supply of a given supply. It is important to note that, under the place-of-supply rules, a service may be physically performed outside Uzbekistan but deemed to be supplied in Uzbekistan for VAT purposes. Examples of services taxed in this way include a supply of a service related to immovable property located in Uzbekistan or a consulting service performed outside Uzbekistan for a customer inside Uzbekistan. If the place of supply is deemed to be outside Uzbekistan, the underlying supply is not subject to Uzbek VAT.

The rules determining the place of supply for works and services are generally as follows:

- The place where immovable property is located for works and services directly related to such property
- The place where works and services are actually carried out for works and services related to movable property
- The place of business or any other activity of the customer for the following works and services: transfer of rights to use intellectual property, consulting services, audit services, engineering services, design services, marketing services, legal services, accounting services, attorney's services, advertising services, data provision and processing services, rent of movable property (except for rent of motor vehicles), supply of personnel, and communication services
- Otherwise, the place of business or any other activity of the service provider

Stamp duties

No stamp duty currently applies in Uzbekistan.

Registration fees

Insignificant fixed fees apply.

G. Other taxes and charges

Contributions on revenue

Contributions to special State Funds are assessed on sales revenue (net of VAT and excise tax) at the total rate of 3.2%.

Property tax

Property tax is generally imposed at a rate of 5% on the average annual net book value of immovable property (and certain other assets).

Unified social payment

The unified social payment (social tax) is paid by employers at a rate of 25% (15% for small businesses) on the total payroll cost (except for certain exempt items).

Social contributions of individuals

The employer is obliged to withhold and remit a mandatory pension fund contribution from local employees at a rate of 8% from salaries and other taxable benefits. Employers also make mandatory monthly contributions to individual accumulative pension accounts of local employees at a rate of 2% of salaries and other taxable benefits of employees, and the amounts of such contributions are subtracted from accrued individual income tax.

Individual income tax

Employers are obliged to withhold and remit individual income tax to the government at progressive tax rates (up to 22.5%).

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Tax regime applied to this country

- ■ **Concession**
  - ■ Royalties
  - ☐ Profit-based special taxes
  - ■ Corporate income tax
- ☐ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

The fiscal regime that applies to the petroleum industry in Venezuela consists of a combination of corporate income tax (CIT), royalty tax, indirect taxes and special contributions. In summary:

- CIT rate — 50% of net profits
- Royalties — up to a maximum of 33.33% on the value of the crude oil extracted
- Tax on capital gains — 50%
- Alternative minimum tax (AMT) — 50% of gross profits

B. Fiscal regime

Oil activities in Venezuela

According to the Master Hydrocarbons Law, upstream activities are reserved for the Venezuelan state, which must perform the activities directly or through state-owned enterprises.

Upstream activities can be performed through joint venture corporations *(empresas mixtas)* in which the state owns more than 50% of the shares (qualifying the entities as state-owned enterprises). The National Assembly must approve the incorporation of any joint venture corporations and the conditions for their operation. These corporations are owned by Petróleos de Venezuela, S.A. (PDVSA).

Corporate income tax

A joint venture corporation that undertakes oil activities is subject to a 50% CIT rate on its annual net profits from Venezuelan and foreign sources of income. "Annual net profits" are determined by subtracting the costs and deductions allowed by the income tax legislation from the gross receipts of the taxpayer. For Venezuelan-sourced income, these calculations are subject to the inflation adjustment rules. For financial years initiated after 18 November 2014, the adjustment by inflation shall be calculated using the National Index of Consumer Prices (INPC). For previous financial years, the Index of Consumer Prices (IPC) shall apply.

Effective from 31 December 2015, taxpayers appointed as "special taxpayers" by the Tax Administration are excluded from the inflation adjustment set forth in the Income Tax Law. This new rule is applicable to most of the oil and gas companies in Venezuela.

Entities must determine their Venezuelan-sourced annual net profits separately from their foreign-sourced annual net profits. In the determination of the Venezuelan-sourced annual net profits, costs and expenses incurred only in Venezuela are allowed, provided the conditions established in the income tax law and regulations are met. Likewise, in the determination of foreign-sourced net annual profits, costs and expenses incurred only abroad may be deducted, provided relevant conditions are met.

Royalties

According to the latest amendment of the Master Hydrocarbons Law (August 2006), the royalty to be paid to the state is equivalent to 30% of the extracted crude; however, the royalty may be reduced to 20% if the oil field is proven to not be economically exploitable. The amendment also creates the following additional taxes:

- An extraction tax equivalent to one-third of the value of the extracted liquid hydrocarbons
- An export registration tax of 0.1% of the value of the exported liquid hydrocarbons

An additional royalty is included in the law on the terms and conditions for the incorporation and functioning of joint venture corporations. The additional royalty amounts to 3.33% of the crude oil extracted from the corresponding oilfield. The royalty tax rate is established in the mandatory bylaws of each joint venture company and is calculated on the value of the extracted crude oil delivered to PDVSA.

Furthermore, any company that develops activities related to hydrocarbons is subject to the royalty-like taxes set out next.

Superficial tax

Superficial tax applies to the superficial extension, without being exploitative, the equivalent of 100 tax units (TU, where one TU currently approximates to US$17 but is updated annually) for each square kilometer per year. This tax increases each year by 2% during the first five years and by 5% for each year following the fifth year.

Own consumption tax

The own consumption tax applies at a rate of 10% of the value of each cubic meter (m^3) from products derived from hydrocarbons produced and consumed as fuel from operations, based on the price sold to the final consumer.

General consumption tax

The general consumption tax, which is paid by the final consumers, is withheld monthly and paid to the National Treasury; the applicable rate is set annually by law. For products derived from hydrocarbons sold in internal markets, the tax is between 30% and 50% of the price paid by the final consumers.

Tax on capital gains

Internal income tax legislation provides that capital gains arising from the sale of stocks, quotas or participation by companies engaged in oil activities are subject to income tax at a 50% rate.

Tax on dividends

The portion that corresponds to each share in the profits of stock companies and other assimilated taxpayers, including those resulting from participation quotas in limited liability companies, is considered to be a dividend.

According to the Venezuelan income tax law, dividends distributed by a company for activities in the oil industry that in total value exceed the company's previously taxed net income are subject to tax at a 50% rate. For these purposes, "net income" is defined as the income approved at the shareholders' meeting, which is the basis for the distribution of dividends. "Taxed net income" is that income used for the calculation of the income tax liability. Net income from dividends is the income received as such, fully or partially paid, in money or in kind.

AMT

The AMT is the difference (if any) between 50% of the gross sales and the sum of the following taxes paid in the respective fiscal year:

- Income tax (50% of the fiscal year's net profits)
- Royalty tax (up to a maximum of 33.3% of the amount of the crude oil extracted)
- Other taxes effectively paid based on income (municipal tax, among others)
- Special contributions allowed

If the taxes paid exceed the additional tax, there is no possibility for the taxpayer to credit the excess in future fiscal years.

Relief for tax losses

Operating losses from a Venezuelan source may be carried forward for three years, but the attribution may not exceed 25% of income obtained in subsequent periods. No carryback is permitted.

Offsetting of losses against gains between different sources (foreign and local source income) is not allowed.

Income tax withholdings

Income tax withholdings in Venezuela are set out in the following table.

Payment type	Entities affected	Tax rate (%)
Interest	Resident individuals	3[1]
Interest	Resident corporations	5[2]
Interest	Nonresident individuals	34[3]
Interest	Nonresident corporations	34[4]
Royalties[5]	Non-domiciled corporations	34[6]
Royalties[5]	Nonresident individuals	34[7]
Professional fees	Resident individuals	3[1]
Professional fees	Resident corporations	5[2]

1 *Withholding tax (WHT) applies to payments of more than VEF25,000. The tax is imposed on the payment minus VEF750.*

2 *WHT applies to payments of more than VEF25.*

3 *WHT is imposed on 95% of the gross payment. Consequently, the effective WHT rate is 32.3% (95% × 34%).*

4 *In general, the WHT rate is determined at progressive rates up to a maximum of 34%. It is applied to 95% of the gross payment. Interest paid to foreign financial institutions that are not domiciled in Venezuela is subject to WHT at a flat rate of 4.95%.*

5 *Royalties paid to nonresidents are taxed on a deemed profit element, which is 90% of the gross receipt.*

6 *The WHT rate is determined at progressive rates up to a maximum of 34%. Because royalties paid to non-domiciled corporations are taxed on a deemed profit element, the maximum effective WHT rate is 30.6% (90% × 34%).*

Payment type	Entities affected	Tax rate (%)
Professional fees	Nonresident individuals and corporations	34[8]
Rent of immovable property	Resident individuals	3[1]
Rent of immovable property	Resident corporations	5[2]
Rent of immovable property	Nonresident individuals	34
Rent of immovable property	Nonresident corporations	34[9]
Rent of movable goods	Resident individuals	3[1]
Rent of movable goods	Corporations	5[2]
Rent of movable goods	Nonresident individuals	34
Rent of movable goods	Nonresident corporations	5
Technical assistance	Domiciled corporations	2[10]
Technical assistance	Resident individuals	1[7]
Technical assistance[11]	Nonresident individuals[14]	34[12]
Technical assistance[11]	Non-domiciled corporations	34[13]
Technological services	Domiciled corporations	2[7]
Technological services	Resident individuals	1[7]
Technological services	Nonresident individuals[14]	34[15]
Technological services	Non-domiciled corporations	34[16]
Sales of shares[17]	Resident individuals	3[1]
Sales of shares[17]	Corporations	5[2]
Sales of shares[17]	Nonresident individuals	34
Sales of shares[17]	Nonresident corporations	5

7 *Because royalties paid to nonresidents are taxed on a deemed profit element, the effective WHT rate is 30.6% (90% × 34%).*

8 *Professional fees paid to nonresidents are taxed on a deemed profit element, which is 90% of the gross receipts. Consequently, the effective WHT rate is 30.6% (90% × 34%).*

9 *The WHT rate is determined by applying the progressive rates up to a maximum of 34%.*

10 *Technical assistance and technological services provided from local suppliers are treated as services.*

11 *Payments to nonresidents for technical assistance are taxed on a deemed profit element, which is 30% of the gross receipts.*

12 *Because payments to nonresidents for technical assistance are taxed on a deemed profit element, the effective WHT rate is 10.2% (30% × 34%).*

13 *The WHT rate is determined at progressive rates up to a maximum of 34%. Because payments to non-domiciled corporations for technical assistance are taxed on a deemed profit element, the maximum effective WHT rate is 10.2% (30% ×34%).*

Other significant taxes

The following table summarizes other significant taxes:

Nature of tax	Rate paid
VAT — imposed on goods and services, including imports; the national executive may exempt acquisitions of goods and services from tax for up to five years; the law provides an indexation system for input VAT during the pre-operational period for enterprises engaged in certain industrial activities; input VAT generated during the pre-operational phase of industrial projects intended primarily for export is refunded	12%
Municipal tax — a business activity tax that is generally based on gross receipts or sales, where the rate varies depending on the industrial or commercial activity	0.5% to 10%
Social security contributions — charged on the monthly salary of each employee up to a maximum of five minimum salaries	Employer: 9%, 10% or 11% Employee: 4%
National Institute of Cooperative Education contributions — required if an employer has five or more employees	Employer, on total employee remuneration: 2% Employee, on profit share received, if any, from employer at year-end: 0.5%
Housing policy contributions — charged on the monthly integral salary (as defined In the Labor Law; see also below) of each employee	Employer: 2% Employee: 1%
Unemployment and training contributions — charged on the monthly salary of each employee, up to 10 minimum salaries	Employer: 2% Employee: 0.5%
Science and technology contribution	0.5% to 1% of gross income
Anti-drug contribution	1% of operating income
Endogenous development contribution	1% of financial profits
Contribution to the National Fund for Development of Sports, Physical Activities and Physical Education	1% of net income or financial profits

14 Payments to nonresidents for technological services are generally taxed on a deemed profit element, which is 50% of the gross receipts.

15 Because payments to nonresidents for technological services are taxed on a deemed profit element, the effective WHT rate is 17% (50% × 34%).

16 The WHT rate is determined by applying the progressive rates up to a maximum of 34%. Because payments to non-domiciled corporations for technological services are taxed on a deemed profit element, the maximum effective WHT rate is 17% (50% × 34%).

17 This tax applies to transfers of shares of corporations non-domiciled in Venezuela that are not traded on national stock exchanges. The WHT rates are applied to the sales price.

"Integral salary" includes any remuneration, benefit or advantage perceived by the employee in consideration for the services rendered, whatever its name or method of calculation, as long as it can be evaluated in terms of cash value, to include, among other things, commissions, bonuses, gratuities, profit sharing, overtime, vacation bonus, food and housing.

C. Financing considerations

Foreign-exchange controls

Under the foreign-exchange control system in Venezuela, the purchase and sale of currency in Venezuela are centralized by the Central Bank of Venezuela. This centralization limits foreign currency trade and other transactions in Venezuela.

Debt-to-equity rules

Venezuelan income tax legislation establishes a safe harbor method that denies the interest deduction for interest payments to related parties domiciled abroad if the average of the payor's debts (with related and unrelated parties) exceeds the amount of the average of its fiscal equity for the respective fiscal year.

D. Other tax issues

Transfer pricing

Under the transfer pricing rules, cross-border income and expense allocations concerning transactions with related parties are subject to analysis and special filings. The rules contain a list of related parties and acceptable transfer pricing methods.

Controlled foreign corporations

Under the controlled foreign corporation (CFC) rules, income derived by a CFC that is domiciled in a low-income-tax jurisdiction is taxable to its Venezuelan shareholders. The tax authorities have issued a list of low-income-tax jurisdictions and may invoke the "substance over form" rules contained in the Venezuelan Master Tax Code to challenge the form chosen by the parties.

Consequently, if a transaction is motivated solely by a desire for tax-avoidance or a reduction in tax liability, the transaction may be disregarded for tax purposes.

Provisions

Provisions for inventory obsolescence and accounts receivable are not deductible; amounts are deductible only when inventories or accounts receivable are effectively written off.

Depreciation

In general, acceptable depreciation methods are the straight-line and the unit-of-production methods; the declining-balance and accelerated-depreciation methods are not accepted. Venezuelan law does not specify depreciation rates, but if the estimated useful life of an asset is reasonable, the depreciation is accepted. Estimated useful lives ranging from 3 to 10 years are commonly used.

There is no provision related to the minimum useful lives of the business assets of the oil companies and, generally, the tax depreciation is the same as the accounting and financial depreciation.

Tax indexation

Companies must apply an annual inflationary adjustment. A company carries this out by adjusting its non-monetary assets, some of its non-monetary liabilities and its equity to reflect the change in the consumer price index from the preceding year. These adjustments affect the calculation of depreciation and the cost of goods sold. Their net effect is recorded in an inflation adjustment account and is added to taxable income or allowed as a deduction.

Effective from tax years beginning after 22 October 1999, the tax indexation rules apply to the reconciliation of only Venezuelan-sourced income; thus, foreign-sourced non-monetary assets and liabilities are not subject to tax indexation.

Windfall oil price tax

Regulations applicable to this tax were modified in 2013 through the Law of Special Contribution due to Extraordinary and Exorbitant Prices of the Hydrocarbons International Market (the Windfall Oil Price Tax), published in *Official Gazette* No. 40,114 on 20 February 2013. The modification related to the increase in the monthly threshold of the Venezuelan liquid hydrocarbons basket for extraordinary and exorbitant prices of hydrocarbons.

This law establishes a special contribution payable to companies exporting, for sale purposes, certain hydrocarbons, including liquid hydrocarbons, both natural and upgraded, and their derivatives. Mixed companies selling natural and upgraded liquid hydrocarbons and derivatives to PDVSA were expressly included.

The Law defines "extraordinary prices" as those where the monthly average of international quotes of the Venezuelan liquid hydrocarbons basket exceeds the price set out in the Annual Budget Law for the respective fiscal year, but is equal to or lower than US$80 per barrel. The Law defines "exorbitant prices" as those where the monthly average of international quotes of the Venezuelan liquid hydrocarbons basket exceeds US$80 per barrel.

In the case of extraordinary prices, when the monthly average of international quotes of the Venezuelan liquid hydrocarbons basket exceeds the price set out in the Budget Law for the respective fiscal year but is equal to or lower than US$80 per barrel, the rate will be equivalent to 20%, to be applied on the difference between both prices.

In the case of exorbitant prices, the rate of the special contribution will vary as follows:

- When exorbitant prices are greater than US$80 but less than US$100, a rate equivalent to 80% of the total amount of the difference between both prices is applied.
- When the exorbitant prices are greater than or equal to US$100 but less than US$110, a rate equivalent to 90% of the total amount of the difference between both prices is applied.
- When the exorbitant prices are greater than or equal to US$110, a rate equivalent to 95% of the total amount of the difference between both prices is applied.

This tax is settled by the Ministry of Popular Power for Energy and Petroleum and is paid on a monthly basis to the National Development Fund (FONDEN).

Where the Ministry of Popular Power for Energy and Petroleum has approved projects for either new reservoir developments or increasing the production of exploitation plans in ongoing projects, an exemption is available from these contributions, provided the total investment has not yet been recovered.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

Vietnam

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Tax regime applied to this country

- ☐ **Concession**
  - ☐ Royalties
  - ☐ Profit-based special taxes
  - ☐ Corporate income tax
- ■ **Production sharing contracts**
- ☐ **Service contract**

A. At a glance

Fiscal regime

In Vietnam, the Petroleum Law, with its guiding decree and circulars, as well as other tax regulations, covers the fiscal regime applicable to organizations and individuals (referred to as contractors) conducting exploration and exploitation of crude oil, condensate (collectively referred to as crude oil) and natural gas in Vietnam. The principal elements of the fiscal regime are as follows:

- Bonuses — defined in each production sharing contract (PSC)
- PSC — based on production volume
- Corporate income tax (CIT) — 32%–50%
- Resource tax — crude oil: 7%–29%; natural gas: 1%–10%
- Investment incentives — CIT rate of 32%; rate of recoverable expenditure up to 70%
- Export duties — crude oil: 10%
- Tax on transfer of capital in petroleum contract — 20%

The Vietnamese Government has introduced the concept of "encouraged" oil and gas projects, which receive special incentives.

B. Fiscal regime

Contractors are permitted to participate in, and operate, the exploration, development and production of petroleum resources in Vietnam by entering into a PSC with Vietnam Oil and Gas Group (Petrovietnam). The PSC will be in accordance with the model contract issued by the Vietnamese Government.

Product sharing

Production sharing for crude oil is based on the profit oil that is computed by subtracting the resource tax and cost petroleum from the actual crude oil output.[1]

The same principle is applicable to natural gas.

1 *Model PSC issued under Decree 33/2013/ND-CP dated 22 April 2013, Article 6.1.*

Bonus and commission

A bonus or commission is a lump-sum payment made, pursuant to a PSC, by foreign parties to the Government (via Petrovietnam). Such a payment is made:

- After the effective date of the PSC (signature commission)
- After declaration of the first commercial discovery
- After the first commercial production date

In addition, nonresident parties to a PSC must also pay Petrovietnam a data fee and a training fee.[2]

Resource tax[3]

Crude oil and natural gas are subject to resource tax. The payable resource tax on crude oil or natural gas amounts to the average taxable output of crude oil or natural gas per day in the tax period, multiplied by the tax rate and the number of days of exploitation of crude oil or natural gas in the tax period.

The tax rates applicable to crude oil are as set out in the table below. There is a column in the table referring to "encouraged" projects, which are defined as:

- Projects where petroleum operations are conducted in deep water and remote offshore areas
- Projects in areas where geographical and geological conditions are difficult
- Projects in other areas in accordance with the list of blocks decided by the Prime Minister
- Coal gas projects[4]

Output (barrels per day)	Encouraged investment projects	Other projects
Up to 20,000	7%	10%
20,001 to 50,000	9%	12%
50,001 to 75,000	11%	14%
75,001 to 100,000	13%	19%
100,001 to 150,000	18%	24%
More than 150,000	23%	29%

The tax rates applicable to natural gas and coal gas are shown in the following table:

Output (million cubic meters per day)	Encouraged investment projects	Other projects
Up to 5	1%	2%
6 to 10	3%	5%
More than 10	6%	10%

Additional levy imposed on shared profit oil[5]

For petroleum contracts signed or approved from 1 January 2010, petroleum contractors are required to pay a surcharge imposed on quarterly shared profit oil when the quarterly average selling price increases by more than 20% of the base price. "Profit oil" is the crude oil volume after deduction of resource tax oil

2 *Model PSC issued under Decree 33/2013/ND-CP dated 22 April 2013, Articles 9.5 and 10.1.*

3 *Resolution 1084/2015/UBTVQH13 dated 10 December 2015.*

4 *The Petroleum Law No. 18/VBHN-VPQH, Article 3.12.*

5 *Circular 22/2010/TT-BTC dated 12 December 2010.*

and recoverable expense oil. The base price is the estimated approved price of the same year. In formula terms, we have:

Additional levy = surcharge rate × (quarterly average selling price − [1.2 × base price]) × quarterly shared profit oil volume.

A surcharge rate of 30% is applicable to an encouraged oil or gas project when the quarterly average selling price increases by more than 20% of the base price. A surcharge rate of 50% is applicable to an oil or gas project when the quarterly average selling price increases from more than 20% up to 50% of the base price. A surcharge rate of 60% is applicable to an oil or gas project when the quarterly average selling price increases by more than 50% of the base price.

Corporate income tax[6]

Contractors are taxed at the rate of 32% to 50% on their taxable income according to the amended Corporate Income Tax Law, which came into effect on 1 January 2014. The specific rate is determined by the Prime Minister for each PSC. The amount of CIT payable is computed by multiplying the specified rate of tax by the taxable income.

"Taxable income" in this context is defined as revenue earned from exploration and exploitation of oil and gas in the tax period, but as reduced by deductible expenses; other incomes, such as interest income, are added to the taxable income. "Revenue earned" from exploration and exploitation of oil and gas is the total value of crude oil and gas that is actually sold under an arm's-length contract in the tax period; if this is not known, the taxable price used to calculate the revenue earned is determined on the basis of the average price in the international market.

Deductible expenses include:

- Expenses actually incurred in relation to activities of exploration and exploitation of crude oil or gas to the extent that they do not exceed expenses that are calculated as revenue earned from the sale of crude oil or gas multiplied by the rate of recoverable expenses that is agreed in the petroleum contract:
  - Under the 2000 amended Petroleum Law, the standard recovery rate is 70% for encouraged projects and 50% for other projects.[7] If the rate of recoverable expenses is not mentioned in the petroleum contract, the deemed rate of 35% will be used.[8]
- Expenses supported by legal evidence documents.

Nondeductible expenses include:

- Expenses that exceed the contractual rate of recoverable expenses
- Expenses incurred before the effectiveness of the PSC, unless otherwise agreed in the PSC or by the decision of the Prime Minister
- Commissions, documentation fees and other expenses not included in the recovered expenses under the PSC
- Loan interest from the borrowing to invest in the search, exploration and development of oilfield and extraction of oil and gas
- Penalty or compensation for damages
- Expenses that are not allowed under the prevailing regulations on CIT

Ring fences

In Vietnam, if a contractor enters into two or more petroleum contracts, it must fulfill its tax obligations for each contract separately.[9] Therefore, a ring fence may be understood as being applicable to each separate contract.

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6 *Circular 36/2016/TT-BTC dated 26 February 2016 on oil and gas taxation, Article 18.*

7 *The Petroleum Law No. 19/2000/QH10, Article 1.7.*

8 *Circular 36/2016/TT-BTC dated 26 February 2016 on oil and gas taxation, Article 17.*

9 *Ibid, Article 6.*

Capital transfer tax[10]

Any gain from transfer of a participating interest in the petroleum contract is subject to capital transfer tax (CTT) at a rate of 20%, including income earned in Vietnam by foreign enterprises from indirect capital transfer.

The payable CTT equals taxable income multiplied by the tax rate. "Taxable income" is here determined as the transfer price less the purchase price of the transferred capital less transfer expenses.

Unconventional oil and gas

No special terms apply to unconventional oil or unconventional gas.

C. Incentives

Corporate income tax

The following incentives are available for encouraged projects:

- Recoverable expenses rate up to 70%.[11]

Encouraged projects are:

- Projects where petroleum operations are conducted in deep water and remote offshore areas
- Projects in areas where geographical and geological conditions are difficult
- Projects in other areas in accordance with the list of blocks decided by the prime minister
- Coal gas projects.[12]

D. Withholding taxes[13]

Nonresident contractors that provide services to a petroleum company operating in Vietnam are subject to foreign contractor tax (FCT), which comprises value-added tax (VAT) and CIT. The applicable CIT rates are as shown in the table below.

No	Business activity/industry	Deemed CIT rate
1	Commerce: distribution, supply of goods, material, machinery and equipment distribution of goods, raw materials, supplies, machinery and equipment attached to services in Vietnam (including those provided in the form of on-the-spot-export (except for goods processed under processing contracts with foreign entities), supply of goods under Incoterms	1%
2	Services, equipment lease, insurance, oil rig lease	5%
3	Construction, installation, whether or not inclusive of raw materials, machinery and equipment	2%
4	Other business activities, transport (including sea transport and air transport)	2%
5	Lease of airplanes, plane engines, plane parts, ships	2%
6	Reinsurance abroad, reinsurance commission, transfer of securities, certificates of deposit	0.1%
7	Service in a restaurant or hotel, casino management	10%
8	Loan interest	5%
9	Royalties	10%
10	Financial derivatives services	2%

10 *Ibid, Article 22.*
11 *The Petroleum Law No. 18/VBHN-VPQH, Article 25a.*
12 *Ibid, Article 3.12.*
13 *Circular 103/2014/TT-BTC dated 2 August 2014.*

VAT[14] will be generally computed as the amount before tax multiplied by the applicable tax rate on the services or goods that the foreign contractor provided. The standard VAT rate is 10% in Vietnam.

E. Indirect taxes

Export duties[15]

Exported crude oil and gas is subject to export duties. The payable export duties are calculated as the quantity of crude oil and natural gas actually exported, multiplied by the dutiable price, multiplied by the export duty ratio. "Dutiable price" is the selling price of crude oil and natural gas under an arm's-length contract. "Export duty ratio" equals 100% less the ratio of resource tax temporarily calculated in the tax period multiplied by the export duty rates of crude oil and natural gas. The "ratio of resource tax temporarily calculated" equals the estimated payable resource tax by crude oil and natural gas divided by the estimated output of crude oil and natural gas, expressed as a percentage.

The export duty rate of crude oil is currently 10%.[16]

Import duties

The following goods imported and used for oil and gas activities will be exempt from import duties:[17]

- Imports serving petroleum activities as prescribed in Clause 15 Article 16 of the Law on Export and import duties
- Specialized vehicles exclusively used for petroleum activities as prescribed by the Ministry of Science and Technology
- Goods that cannot be domestically manufactured as prescribed by the Ministry of Planning and Investment

VAT

VAT, at the rate of 5% or 10%, is imposed on most goods and services used for business. However, the following imported goods that are not available domestically are exempt from VAT[18]:

- Machinery, equipment and material imported for scientific research and technological development
- Machinery, equipment, parts, transport means, and material imported for the exploration and development of oil and gas wells
- Oil rigs and ships imported to form fixed assets or leased from abroad and imported for business activities and for re-lease

Natural resources and minerals exported without or after further processing into products whose prime cost consists of, by at least 51%, the total value of such natural resources and minerals plus the energy cost; exports derived from natural resources and minerals whose value and the energy cost make up at least 51% of the prime cost of such exports are exempt from VAT.[19]

F. Financing considerations

According to the CIT regime, interest expenses paid on bank loans utilized to finance taxable operations are generally tax-deductible. Interest expenses paid on loans borrowed from nonfinancial institutions or noneconomic organizations are also deductible, provided that the interest rate does not exceed 150% of the rates announced by the State Bank of Vietnam.[20]

In case of medium- or long-term borrowing from overseas, the borrower must register the loan with the authority within 30 days from the signing of borrowing contract.[21]

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14 *Circular 103/2014/TT-BTC dated 2 August 2014, Article 12.3a.*

15 *Circular 36/2016/TT-BTC dated 26 February 2016 on oil and gas taxation Article 13.*

16 *Decree 125/2017/ND-CP dated 16 November 2017 — Appendix I Code 2709.0010.*

17 *Decree 134/2016/NĐ-CP dated 1 September 2016, Article 16.*

18 *Circular 219/2013/TT-BTC dated 31 December 2013 on VAT, Article 4.17.*

19 *Circular 130/2016/TT-BTC dated 12 August 2016 Article 1c.*

20 *Circular 96/2015/TT-BTC dated 22 June 2015 on CIT, Article 4.2.17.*

21 *Circular 03/2016/TT-NHNN dated 26 February 2016 on administration procedures in the State Bank of Vietnam, Article 13.*

Foreign currency

The following list sets forth the names and symbols for the currencies of the countries discussed in this book.

Country	Currency	Symbol
Algeria	Dinar	DZD
Angola	Kwanza	AOA
Argentina	Peso	ARS
Australia	Dollar	A$
Azerbaijan	Manat	AZN
Bahrain	Bahraini dinar	BHD
Benin	CFA franc	XOF
Brazil	Real	BRL
Cambodia	Khmer riel	KHR
Cameroon	CFA franc	XAF
Canada	Dollar	C$
Chad	CFA franc	XAF
Chile	Peso	CLP
China	Yuan renminbi	CNY
Colombia	Peso	COP
Côte d'Ivoire	CFA franc	XOF
Cuba	Cuban Peso	CUP
Cyprus	Euro	€
Democratic Republic of Congo	Franc	CDF
Denmark	Krone	DKK
Ecuador	US dollar	US$
Egypt	Egyptian pound	EGP
Equatorial Guinea	CFA franc	GQE
Gabon	CFA franc	XAF
Germany	Euro	€
Ghana	Cedi	GHS
Greece	Euro	€
Greenland	Danish krone	DKK
Guyana	Guyana dollar	GUD
HRK	Kuna	kn
Iceland	Krona	ISK
India	Rupee	INR
Indonesia	Rupiah	IDR
Iran	Iranian rial	IRR
Iraq	Iraqi dinars	IQD

Foreign currency

Country	Currency	Symbol
Ireland	Euro	€
Israel	New shekel	ILS
Italy	Euro	€
Kazakhstan	Tenge	KZT
Kenya	Shilling	KES
Kuwait	Kuwaiti dinar	KWD
Laos	Kip	LAK
Lebanon	Pound	LL
Libya	Dinar	LYD
Malaysia	Ringgit	MYR
Mauritania	Ouguiya	MRO
Mexico	Peso	MXN
Morocco	Dirham	MAD
Mozambique	Metical	MZN
Myanmar	Kyat	MMK
Namibia	Dollar	N$
The Netherlands	Euro	€
New Zealand	Dollar	NZ$
Nigeria	Naira	NGN
Norway	Krone	NOK
Oman	Rial	OMR
Pakistan	Rupee	PKR
Papua New Guinea	Kina	PGK
Peru	Nuevo sol	PEN
Philippines	Peso	PHP
Poland	Zloty	PLN
Qatar	Riyal	QAR
Republic of the Congo	Franc	XAF
Romania	Leu	RON
Russia	Ruble	RUB
Saudi Arabia	Saudi riyal	SAR
Senegal	CFA franc	XOF
Singapore	Dollar	S$
South Africa	Rand	ZAR
Spain	Euro	€
Sri Lanka	Sri Lanka rupee	Rs
Syria	Syrian pound	SYP

Foreign currency

Country	Currency	Symbol
Tanzania	Shilling	TZS
Thailand	Baht	THB
Trinidad and Tobago	Dollar	TT$
Tunisia	Dinar	TND
Uganda	Shilling	UGX
Ukraine	Hryvnia	UAH
United Arab Emirates	UAE dirham	AED
United Kingdom	Pound sterling	£
United States	US dollar	US$
Uruguay	Peso	$U
Uzbekistan	Uzbekistan som	UZS
Venezuela	Bolivar	VEF
Vietnam	Dong	VND

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