

**Esq**  
LEGAL PRACTICE

*Seminars*

Aluko & Oyebo

**AN OVERVIEW OF THE FISCAL  
PROVISIONS OF THE PETROLEUM  
INDUSTRY BILL**

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## INTRODUCTION

- Nigeria is the 11<sup>th</sup> largest oil producing state in the world (6<sup>th</sup> in OPEC) with an average daily production of 2, 356, 000 (bpd) as at 2011.
- The oil sector contributed 12.59% to Gross Domestic Product (GDP) in 2012.
- In total crude oil exports accounted for over 63% of the nation's total export earnings in 2011 according to figures released by the National Bureau of Statistics.





## INTRODUCTION (CONT'D)

- According to the Federal Inland Revenue Service's (FIRS) annual report for 2012 overall proceeds accruing from Petroleum Profits Tax amounted to 67.71% of the total revenue accruing to the Federation Account in 2012.

## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

### *The Nigerian Hydrocarbon Tax (NHT):*

- NHT will replace the Petroleum Profit Tax (PPT).
- NHT is to be computed on the chargeable profits of the relevant accounting period at the rate of 50% for onshore and shallow water areas and 25% for bitumen, frontier and deep water acreages.



## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

### *Production Allowance (PA):*

- PA to replace the ITC/ITA (applicable to Product Sharing Contracts under the current regime) and PIA (applicable to all other companies liable to PPT).
- Companies in Joint Venture arrangements at the time the PIB comes into force will not benefit from PA.
- PA allowance thresholds to be fixed on the total production per PML aggregated at company level.
- Claims by a PSC contractor or a supplier of gas solely to the domestic market shall be ring-fenced.
- Where a shareholder holds at least 10% of the shares either directly or indirectly in several companies, the companies shall be treated as one for the purposes of computing PA.

## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

- While the ITC and ITA are calculated as a percentage of QCE and available throughout the period of petroleum operations, PA is to be calculated as follows:
  - For onshore operations: the lower of US\$30 per barrel or 30% of the official selling price (OSP) up to a cumulative maximum of 10 million barrels and the lower of US\$10 per barrel or 30% of OSP for volumes exceeding 10 million barrels up to a cumulative maximum of 75 million barrels and then no more.
  - For operations in the shallow water areas: the lower of US\$30 per barrel or 30% of the OSP up to a cumulative maximum of 20 million barrels and the lower of US\$10 per barrel or 30% of the OSP for volumes exceeding 20 million barrels up to a cumulative maximum of 150 million barrels and then no more.



## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

- For operations in areas with bitumen deposits, frontier acreages and deep water areas: the lower of US\$15 per barrel or 30% of the OSP up to a cumulative maximum of 250 million barrels per Petroleum Mining Lease and the lower of US\$5 per barrel or 10% of the OSP for volumes exceeding 250 million barrels.
- For companies currently in a PSC with NNPC but which are not currently claiming either ITC or ITA: US\$5 per barrel or 10% of the OSP for all production volumes.

## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

### *Capital Allowance (CA):*

- The PIB proposes provisions which put it beyond doubt that a PS Contractor which finances the acquisition of a capital asset is entitled to claim CA on the capital asset. Para 5 of the 4<sup>th</sup> Schedule to the PIB provides that:

*“Where the production sharing contract between the national oil company and a contractor provides for the contractor to finance the cost of equipment and for such equipment to become the property of the national oil company, the contractor shall be deemed to be the owner of the qualifying expenditure thereon, for the purpose of the claim of capital allowances”.*

- Restriction on the total CA that can be claimed in an accounting period has been removed.



## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

- Allowable deductions:
  - PIB proposes a *reasonability* criterion
  - Interest incurred on capital employed for upstream operations is tax deductible *except interest incurred in upstream petroleum operators under a PSC.*
  - Contributions to a pension, provident or other society, scheme or fund in line with the provisions of the Pensions Reform Act. There is no longer a requirement that approval be obtained from relevant authorities.
  - Sums set aside in a fund as decommissioning and abandonment expenditure.
  - Contributions to PHC Fund.

## **AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)**

- Deductions that are not allowed:
  - expenditure for the purpose of paying a penalty or fee for gas flaring or breach of domestic gas supply obligations
  - signature bonuses, production bonuses or other bonuses due on a lease or on the renewal of a lease
  - all general, administrative and overhead expenses incurred outside Nigeria in excess of one percent of the total annual capex
  - twenty percent of any expense (other than one percent offshore administrative and overhead expense) incurred outside Nigeria except where such expenditure relates to the procurement of goods or services which are not available in the required quantity and quality in Nigeria and subject to the approval of the Nigerian Content Development and Monitoring Board.



## **AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)**

- Deductions that are not allowed (cont'd):
  - Legal and arbitration costs incurred in prosecuting cases against the FIRS or the Government
  - Costs incurred prior to the establishment of the company in Nigeria
  - costs resulting from fraud or willful misconduct or negligence on the part of the company
  - costs incurred in obtaining and maintaining of a performance bond under a PSC

## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

The Petroleum Host Community Fund (PHCF):

- 10% of the net profits derived from upstream petroleum operations in onshore, offshore and shallow water areas is to be paid into the PHCF on a monthly basis.
- 10% of the net profits derived from upstream petroleum operations in deep water areas is to be paid into the PHC Fund for the benefit of the littoral states.
- The PHC Fund is to be “utilized for the development of the economic and social infrastructure of the communities within the petroleum providing areas”.



## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

- The monthly remittance is to be based on estimated net profits. At the end of the fiscal year companies will have to reconcile their remittances with the actual PHC Fund contributions payable, and pay the difference (if any).
- Contributions are to be set-off against a company's total fiscal rent obligation defined as:

*“the aggregation of royalty, Nigerian Hydrocarbon Tax and Companies Income Tax obligations arising from upstream operations.”*

- Cost of repair of a petroleum facility damaged by an act of vandalism, sabotage or civil unrest shall be paid from the PHC Fund unless it is established that no member of the community is responsible.

## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

### *Penalty for Gas Flaring:*

- No flaring after the “flare-out” date to be set by regulations to be made by the Minister.
- Minister can grant flaring permits after the flare-out date in certain limited circumstances.
- Flaring of gas without Ministerial approval attracts “*a fine which shall not be less than the value of the gas flared*”.
- Gas flaming penalty is not deductible for tax purposes.



## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

### *Renewal Bonus:*

- A renewal bonus is to be paid at the time of renewing a PML.
- The terms and conditions that shall apply to a renewal shall be the prevailing terms and conditions for the grant of new PMLs at the time of renewal.
- A renewal bonus is not a deductible allowance for NHT purposes.
- Query: does a renewal bonus qualify as capital expenditure incurred on *the acquisition of, or of rights in or over petroleum deposits* in respect of which CA can be claimed?

## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

### *Royalties:*

- To be fixed by regulations made by the Minister pursuant to the PIB.
- Existing rates of royalties to apply until new regulations are made by the Minister.



## AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

### *Dividends:*

- Dividends paid out of profits that have been subjected to NHT will not be liable to WHT or any other tax.

### *Procedural matters:*

- A company dissatisfied with any tax imposed upon it by the FIRS or which has any other grievance against the FIRS or government agency may seek redress in respect thereof at the Federal High Court.
- Contrast with S. 59 and the 5<sup>th</sup> Schedule of the Federal Inland Revenue Service Act, 2007 which provide for appeals to the Tax Appeal Tribunal. Query: could the proposed provision in the PIB (for redress to be sought directly at the FHC) be in response to the decisions of the Court in *Stabilini Vision v FBIR (2009) 12 NWLR (Part 1157) 200* and *Cadbury v FIBR 2 TLRN 16*

## A N OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)

*Procedural matters (cont'd):*

- An action for redress has to be filed within 30 days.
- Where redress has not been sought within 30 days, it could be done within a further period of 60 days if good cause is shown.
- *Query: does this mean that the right to seek redress is permanently lost after 90 days?*
- PSC contractors shall be responsible for reporting their upstream operations profits, outgoings, expenses, and for paying the tax chargeable on their upstream operators – s.317



## **AN OVERVIEW OF THE FISCAL PROVISIONS OF THE PETROLEUM INDUSTRY BILL (PIB)**

### *Companies Income Tax (CIT):*

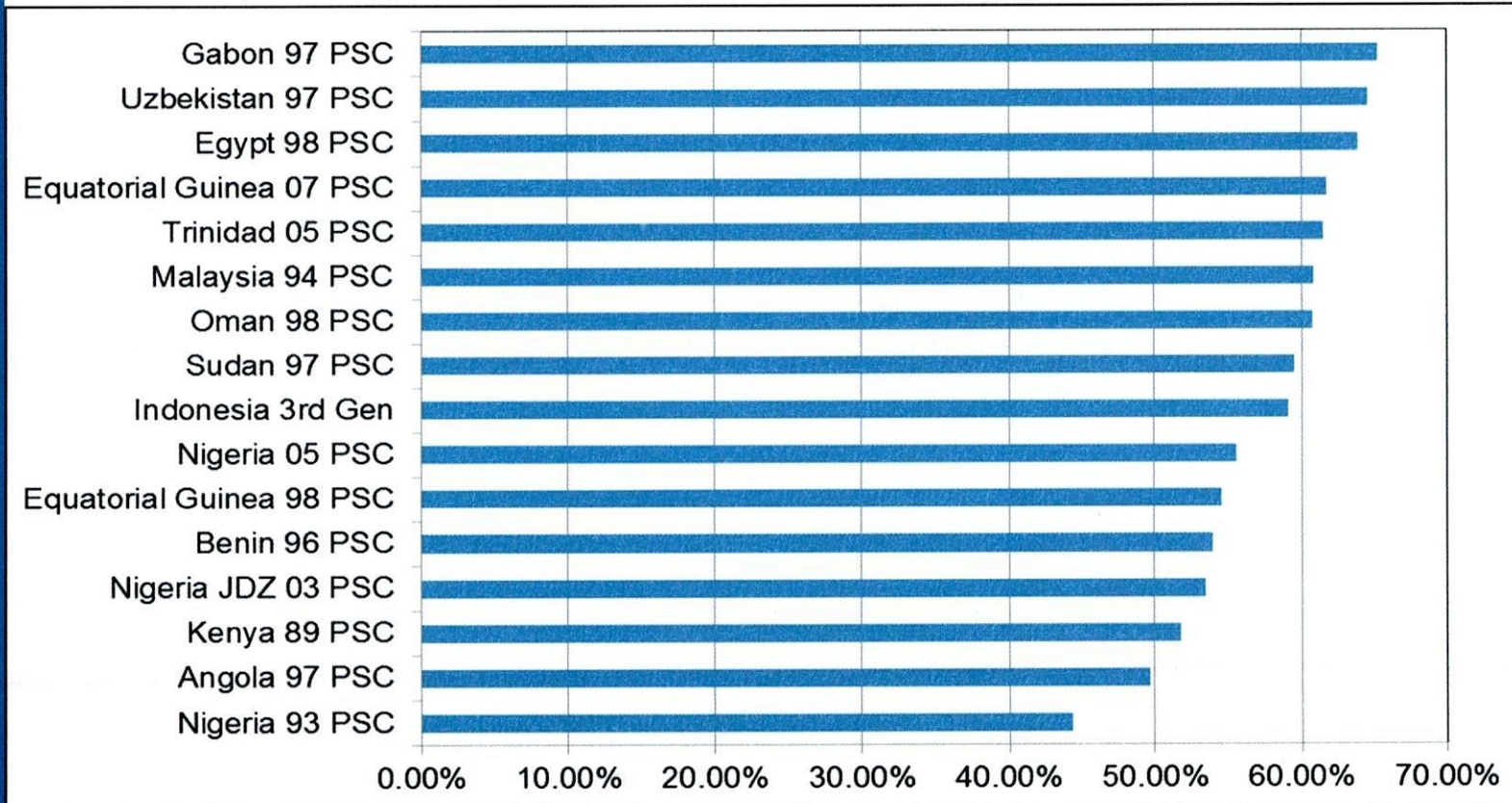
- CIT payable by upstream petroleum companies in addition to NHT.
- NHT is not tax deductible for CIT purposes.
- Upstream companies to pay CIT on an actual year basis.
- Rate of CIT remains 30%.
- Companies involved in both upstream and downstream petroleum operations are to compute CIT separately for upstream operations and downstream operations.

**WILL THE FISCAL PROVISIONS IN THE PIB  
RESULT IN AN INCREASE OF THE EFFECTIVE  
TAX RATE FOR UPSTREAM COMPANIES?**

- Product Sharing Contractors pay PPT at the rate of 50% under the current regime.
- Under the fiscal regime proposed under the PIB, they will pay 55% (i.e. 25% WHT plus 30% CIT)
- PA and GPA will replace the more beneficial ITC/ITA
- JV companies that are yet to fully amortise their capitalised pre-production costs currently pay PPT at the rate of 65.75%. Under the PIB they will pay NHT and CIT at a combined rate of 80%
- Other JV companies currently pay PPT at the rate of 85%. Under the PIB they will be liable to NHT and CIT at a combined rate of 80%. However, while they enjoy PIA under the current regime they will not be entitled to claim PA or GPA under the PIB.

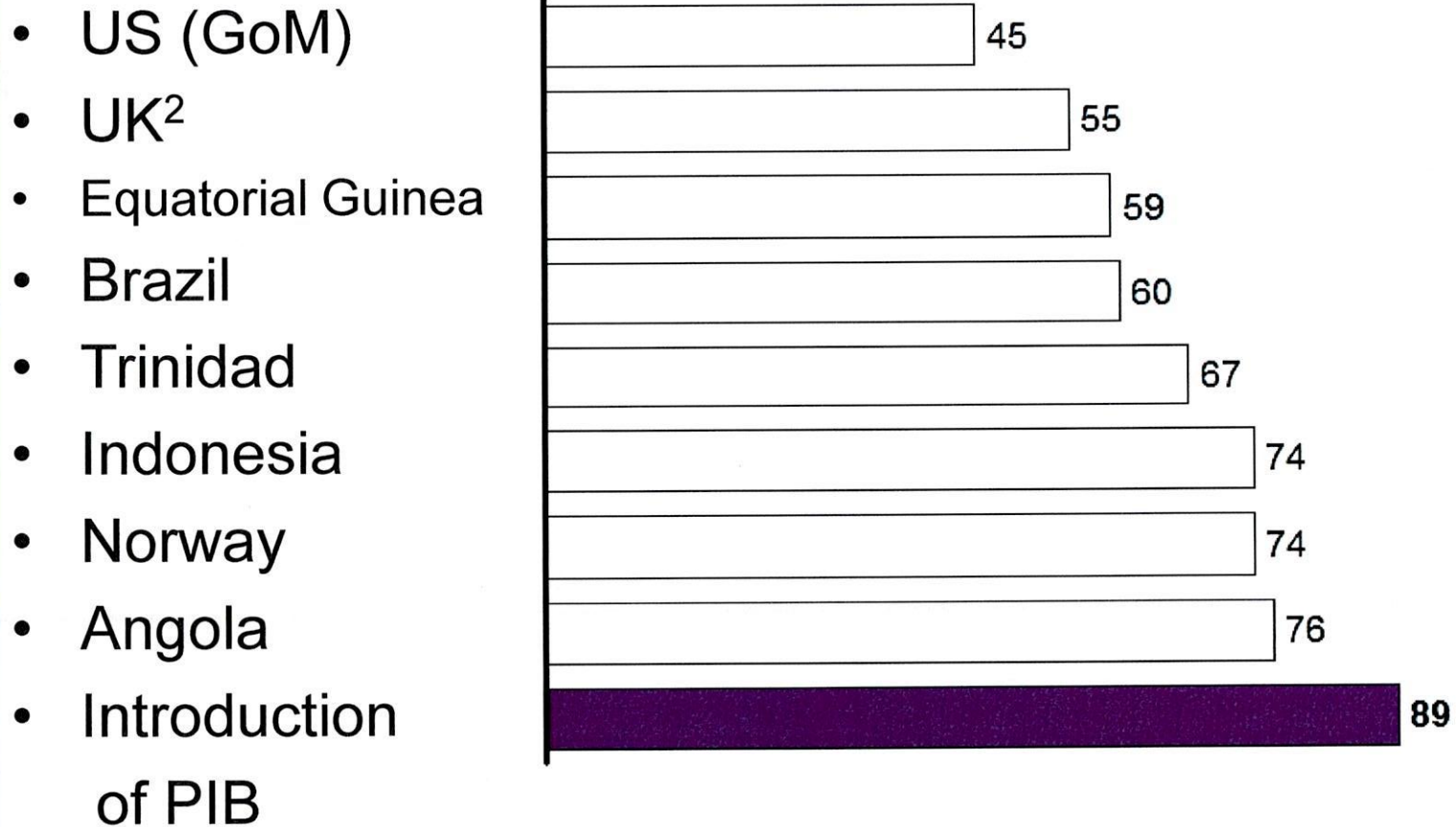


## VARIOUS GOVERNMENTS' TAKES (THE NIGERIAN GOVERNMENT'S POSITION)





**VARIOUS GOVERNMENTS' TAKES OF REMAINING PORTFOLIO VALUE  
AT OIL PRICE 60 US\$/BBL UNDER THE PSC REGIME (THE IOC'S  
PERSPECTIVE**



- According to a survey by the United States Accountability Office in 2007 the fiscal revenue derived from petroleum exploration activities are as follows:

Fiscal System	Government Take%	
	2002	2006
• United States	- 41.20%	38% - 42%
• United Kingdom	- 40.77%	
• Venezuela	- 88% - 93%	
• Norway	- 74.74%	
• Angola	- 74.11%	80.40%
• Trinidad & Tobago	- 69%	

## **VARIOUS GOVERNMENTS' TAKES: AN INDEPENDENT VIEW (CONT'D)**

- Nigeria (onshore) - 87.21%
- Nigeria (deepwater) - 64.62%
- Nigeria (shelf) - 87.44%



## POTENTIAL DISPUTES FROM THE ALTERATION OF EXISTING FISCAL ARRANGEMENTS

- Contractual arrangements are made under existing legal framework
- Governments are always free to change their laws
- Such changes may adversely impact on the rights and benefits of the non-government party under existing contracts
- In the context of international investment law, certain mechanisms have been put in place for addressing these issues. They include:
  - *Stabilization clauses*
  - *BIT arbitration*
  - *Statutes that make a general offer of arbitration to foreign investors (for example the NIPC Act).*
- In the event that the fiscal provisions of the PIB are applied to existing contracts in such a way that they impact adversely on existing contractual rights, a dispute may arise which can be resolved using any one of the mechanisms above.