



The asia-pacific energy and natural resources tax forum

20 November, 2008

TAX

Panel

- Rod Henderson, KPMG in Australia – Moderator
- Jean Li, KPMG in China
- Vikram Doshi, KPMG in India
- Ward Jones, KPMG in Kazakhstan
- Chinguan Khoo, KPMG in Malaysia
- Siew Moon Chung, KPMG in Singapore

Agenda

- **Country Updates**
- **Lifecycle of typical global Resource Project**
- **International Holding Structures for Resource Project**
- **Structuring Exploration Activities into a New Country**
- **Funding the Development of Resource Projects**
- **Holding and Developing a New Mine or Oil Well**
- **Marketing the Output from the Resource Project**

Australia

Rod Henderson

Australia – Corporate Tax

- Corporate tax rate 30 percent
- Tax Consolidation
- Dividend imputation system
- Tax depreciation based on effective life with some capped lives for assets in oil & gas, gas distribution and LNG industries
- Immediate exploration deduction of 100 percent
- Research & Development concessions at 125 percent/175 percent

Australia – Indirect Tax

- GST rate of 10 percent
- Registration for ABN/GST
- Foreign contractor withholding tax of 5 percent for works in Australia
- State stamp duties on property transfers
- Petroleum Resource Rent Tax rate of 40 percent (offshore waters)

Australia – Operating Globally

- 45 Tax Treaties
- Flow through holding company regime, with participation exemption
- Non-resident CGT exemption for non-Taxable Australian Property
- Simplified CFC regime
- Thin capitalization safe harbor of 75 percent of book value of assets less non-debt liabilities (comparable to 3:1 Debt/Equity ratio)

Australia – Tax Developments

- Australian's Future Tax System Review, including:
 - Examination of taxation of the resources industry and the Federal income tax/State royalty regime mix
 - Corporate and individual tax rate reduction
 - Review of capital allowances and tax incentives
- Carbon Pollution Reduction Scheme (ETS) to start from 2010 with special income tax regime
- Ramped up Tax Risk Review program by the ATO

Australia – Transfer Pricing

- Transfer pricing continues to be one of the top tax risks in ATO's Annual Compliance program, 2008/9
- Transfer pricing focus
 - Structures impacting tax, marketing arrangements, risk stripping, financial returns vs. industry, transfer of profits to low tax jurisdictions, interest and guarantee fees, licensing of IP, service fees, transfer pricing documentation!
- SMEs new ATO target
- ATO hot topics – financing arrangements, business restructures

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China

Jean Li

New Corporate Income Tax Law

Unification

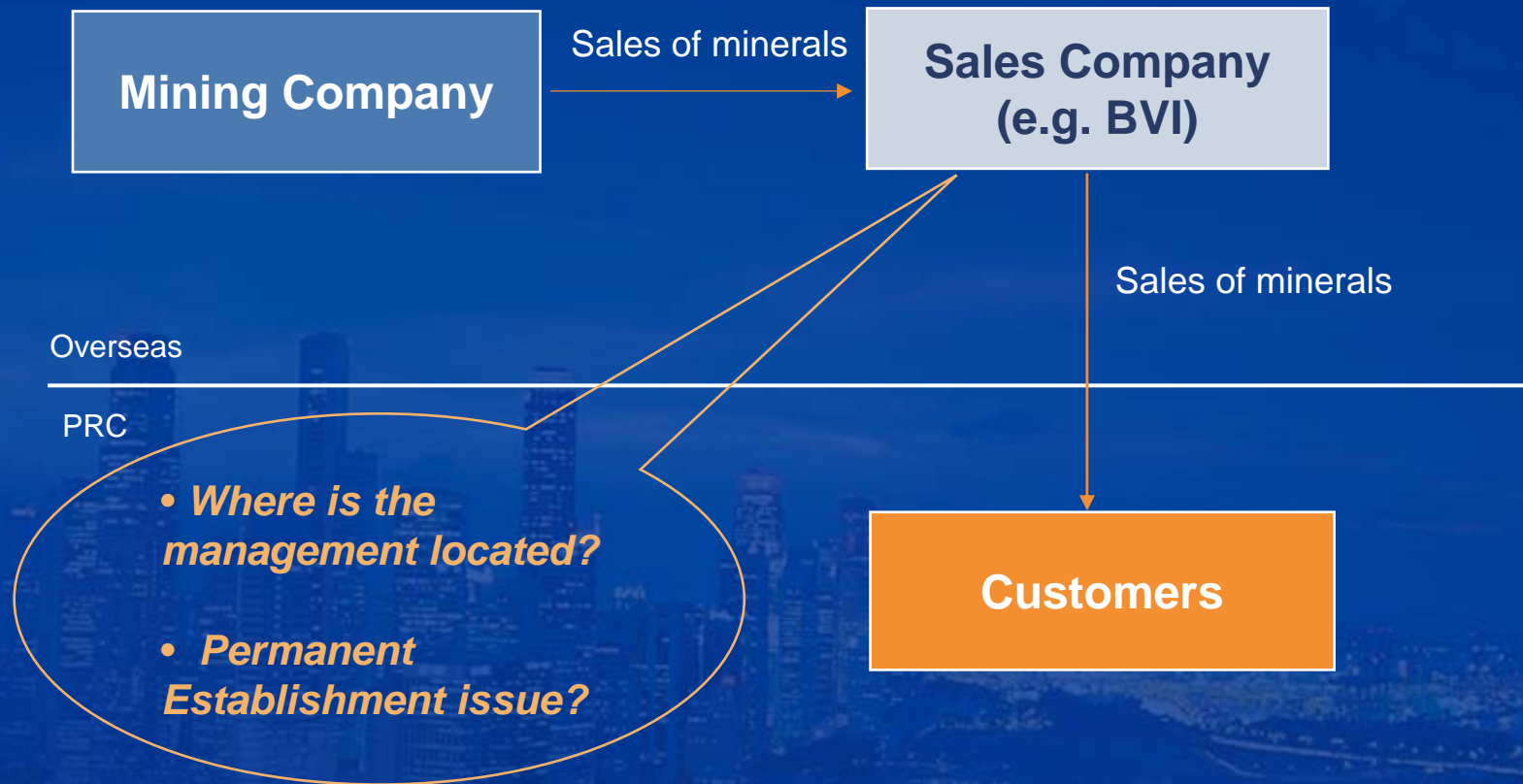
- Unified CIT Law and Implementation Rules
 - PRC Corporate Income Tax Law
 - Passed at 5th Session of the 10th NPC on 16 March 2007
 - Effective from 1 January 2008
 - The Implementation Rules of the PRC CIT Law
 - Issued through the State Council Decree No.512 in 2007
 - Effective from 1 January 2008

New Corporate Income Tax Law

Hot topics

- Taxpayer – Place of effective management
- Withholding tax rate
- Advanced and New Technology Enterprise
- Thin Capitalization
- Special treatment on expenses incurred prior to the commercial production and the depreciation of fixed assets for natural resources companies

Taxpayer – Place of Effective Management



Withholding Tax Rate

	Hong Kong (10%)	Singapore (10%)	Macau (10%)	Mauritius (10%)	Barbados (10%)	Ireland (10%)	Luxemburg (10%)
Dividends	5 ¹ or 10	5 ¹ or 10	10	5	5	5 ¹ or 10	5 ¹ or 10
Interest²	7	7 ³ or 10	7 ³ or 10	10	10	10	10
Royalties	7	6 ⁴ or 10	10	10	10	6 ⁴ or 10	6 ⁴ or 10
Gain from property	10	10	10	10	Exempt	10	10
<ul style="list-style-type: none"> ● Real Estate ● Personal Property 	Exempt ⁵	Exempt ⁵	Exempt ⁵	Exempt ⁵	Exempt	Exempt ⁵	Exempt ⁵

1: A corporate beneficial owner directly holds at least 25% of the capital of the distributing company

2: WHT exempted on interests received by government authorities or other recognised authorities

3: Interest derived by banks or other financial institutions

4: Consideration for the use of, or the right to use, industrial, commercial or scientific equipment

5: Transferor holding less than 25% of shares

Advanced and New Technology Enterprises

- Comparison of old and new recognition standards

	Old Standard	New Standard
Ownership of IP	None	Ownership of core IP
Products or services	Hi-tech areas as prescribed by the state	Hi-tech areas encouraged by the state
R&D expenses	Above 5% of total sales	3%-6% of the total sales
H-tech revenue	Above 60% of total sales	Same
Scientific personnel	Diploma degree above 30% Hi-tech R&D employees 10%	Same
Enterprise responsible person	Familiar with R&D	None
Zone	State hi-tech development zones	No restriction

Thin Capitalization

- Interest deductions are denied to the extent that the company is financed “excessively” by debt
- Applicable to loans from related parties
- Debt-equity ratio
 - Non-financial institution: 2:1
 - Financial institution: 5:1
- How the ratio interacts with arm’s length rule?

Special Treatment on Oil & Gas Companies

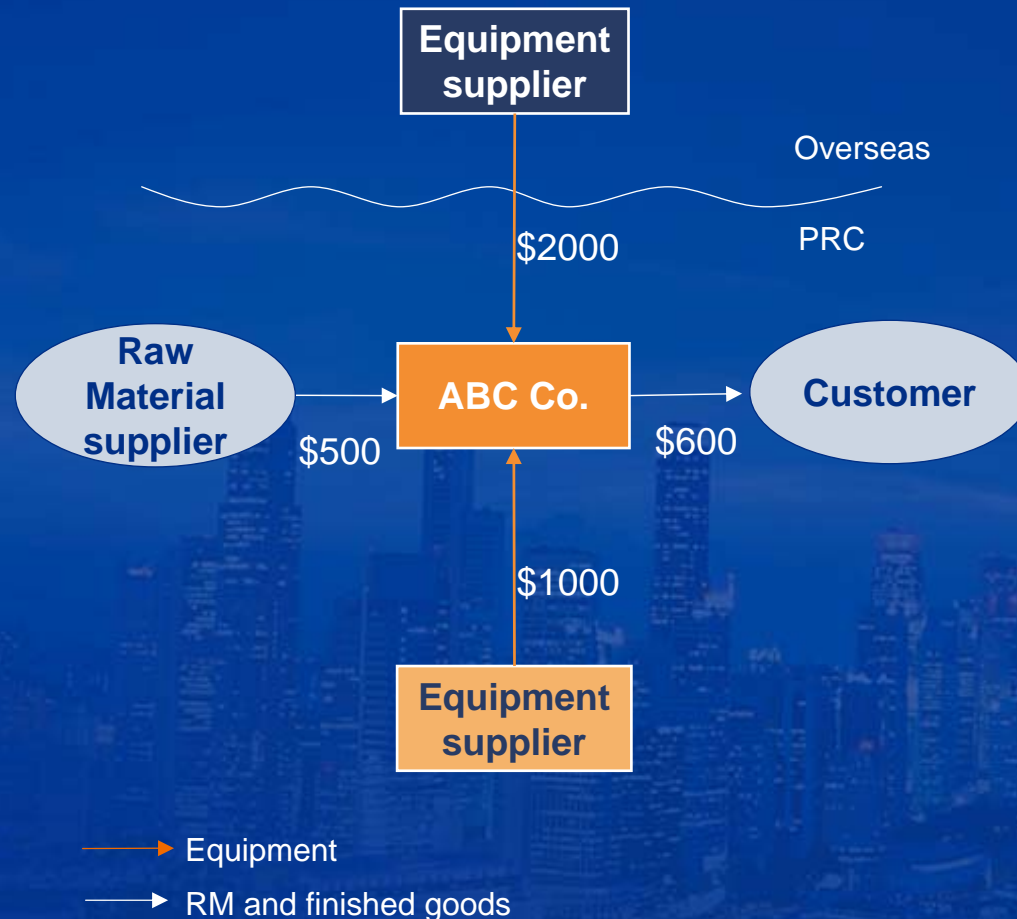
DRAFT

	Foreign Enterprise Income Tax Law	Draft Circular under CIT Law
Amortization of exploration expenses	Amortized over a period of no less than one year	Amortised over a period of no less than three years
Amortization of expenses for rights and interests of a block	Amortized as exploration expenses and development expenses	Amortised over a period of no less than three years
Depreciation of the capitalized development expenses	Depreciated over a period of not less than six years without residual value	Depreciated over a period of not less than ten years without residual value

VAT reform in China

- New VAT Provisional Regulations:
 - Promulgated on 13 November 2008
 - Effective from 1 January 2009
- VAT rate for mining products: from 13 percent to 17 percent
- From production-type scheme to consumption-type scheme
 - Input tax for fixed assets: deductible
- For “Encouraged” projects:
 - Import VAT exemption for equipment: revoked
 - VAT refund for domestically purchased equipment: revoked
- Import VAT exemption for equipment of PSCs?

Example – Impact of VAT reform on “Encouraged” project

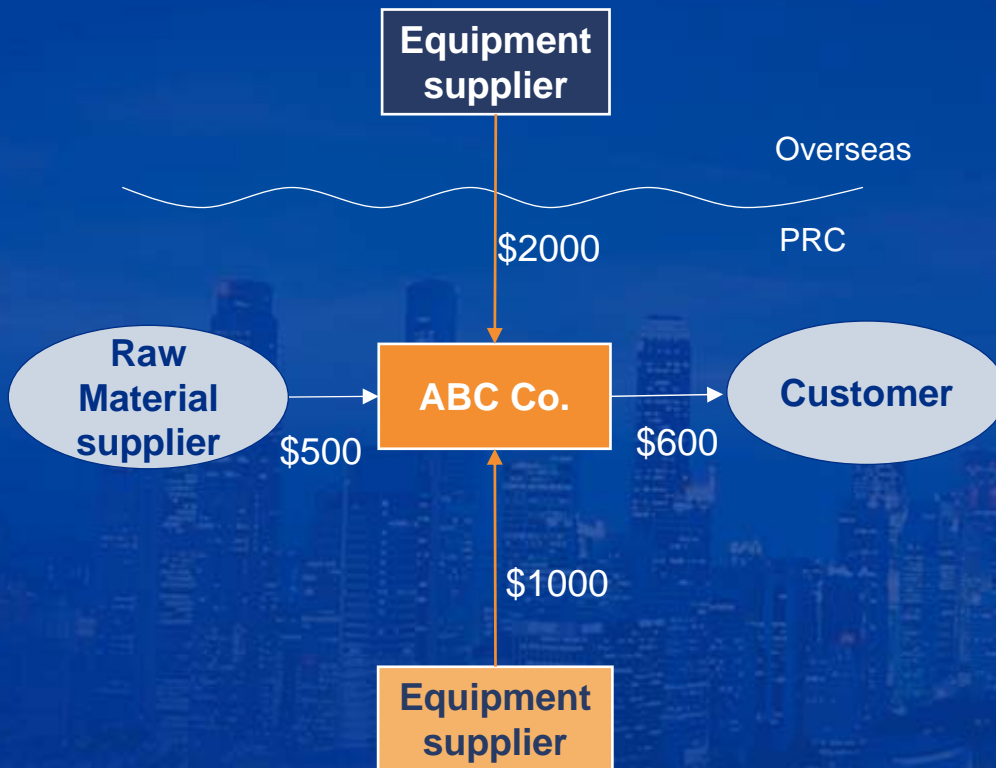


- Assumption:
 - “Encouraged” project
 - Entitled to import VAT exemption and VAT refund for domestically purchased equipment before 1 January 2009
 - VAT rate: 17%
- Cost of equipment remain unchanged
- Cash flow problem after 1 January 2009 due to additional input tax on equipment

Example – Impact of VAT reform on other project

Assumption:

- No “Encouraged” project
- VAT rate of 17%



- Equipment
- RM and finished goods

Before

	B/S
VAT payable	
– sales	102
– cost of goods sold	<u>(85)</u>
Subtotal	17
Cost of equipment	
– import	2340
– domestic purchase	<u>1170</u>
Subtotal	3510

Input tax capitalized

After

VAT payable	
– sales	102
– cost of goods sold	(85)
– equipment	<u>(510)</u>
Subtotal	(493)
Cost of equipment	
– import	2000
– domestic purchase	<u>1000</u>
Subtotal	3000

Input tax deductible

Resource Tax Reform

- Current tax calculation basis
 - Tax on quantum method
 - Rates
 - Coal: RMB0.3-8 / ton
 - Other non-metallic mineral ore: RMB0.5-20 / ton or cubic meter
 - Ferrous metallic mineral ore: RMB2-30 / ton
 - Non-ferrous metallic ore: RMB0.4-30 / ton
 - Resource Tax of 2007: **0.53 percent** of the total tax revenue
- Proposed calculation basis
 - Quantum method -> Valorem method
 - Based on sales volume -> extraction volume
 - Time schedule not determined

Forthcoming TP Documentation Rules

- Currently, there is no contemporaneous documentation in China. However, State Administration of Taxation (SAT) is expected to issued TP “contemporaneous documentation” rules by the end of 2008
- Likely to be effective from 1 January 2008
 - Possible first year of documentation: 2008
 - However, the results for each of three preceding year (i.e., 2006-2008) may also be analyzed
 - Possible due Date: 1 June 2009
- Information required likely to cover
 - Overview of business operations
 - Functional and risk analysis for each associated enterprise
 - Comparability analysis
 - Selection of TP method

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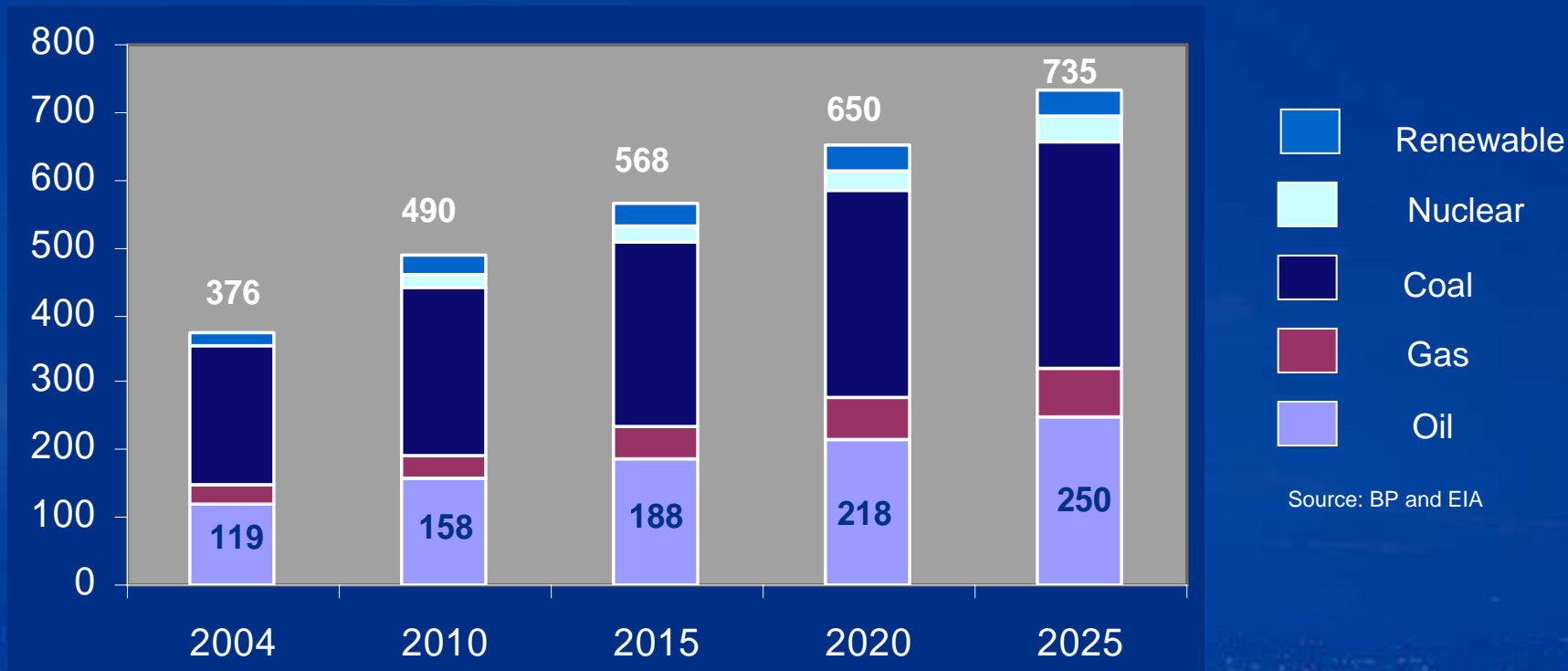
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India

Vikram Doshi

India's Energy Mix and Outlook for Oil

Trends in Primary Energy Demand



Demand for oil is expected to grow at 3.6% p.a.

Domestic production from existing developed reserves expected to grow at approximately 2.5%

Regulatory Environment

- Foreign investment policy
 - 100 percent foreign investment permitted under the automatic route in exploration, pipelines, petroleum refining and petroleum product refining
 - 49 percent foreign investment permitted subject to government approval in case of PSU refining
- New Exploration Licensing Policy (NELP) is in place since 1999, to facilitate Private Sector participation in Oil & Gas exploration
- Under NELP VII round, 57 blocks were offered by the government
- Partial open acreage system being discussed

Tax Environment – Corporate Tax

- Indian companies taxable at 33.99 percent on net income (AMT at 11.33 percent)
- Foreign companies taxable at 42.23 percent on net income (AMT at 10.56 percent)
- Presumptive taxation for Non residents providing services in the oil and gas sector at 4.223 percent of revenues (i.e., 42.23 percent of 10 percent of revenues)
- Dividend distribution tax at 16.995 percent

Tax Environment – Corporate Tax

- Production sharing contract with government may provide additional tax incentives
- All exploratory and drilling expenditure tax deductible
- 100 percent tax holiday for production or refining of mineral oil for 7 years from the date of commercial production – subject to MAT
- 100 percent tax holiday for natural gas distribution infrastructure for 10 years
- No ring fencing – setoff of expenditure from one contract area against another

Corporate Tax – Developments and Hot Topics

- Tax holiday for ‘natural gas’ exploration and production
- Applicability of presumptive taxation for certain services e.g., seismic studies
- Fringe benefit tax where operator incurs expenditure on behalf of consortium
- Ability of PSC to grant additional federal and state tax incentives
- Date of commencement (for tax holiday purposes) for different wells within same block
- Complex farm in and farm outs (especially involving carried interest) – no clear taxation principles

Tax Environment – Indirect Tax

Customs duty

- Goods imported for E&P under NELP eligible for exemptions from Customs duty – subject to actual user condition
- Goods imported for setting up of pipelines eligible for Project Import benefits and attract a concessional Basic Customs ('BCD') duty rate of 5 percent
- Concessional rate of BCD at 5 percent available for goods imported for setting-up refineries

Cenvat

- Manufacture of petroleum products chargeable to Excise duty
- Most contracted services with regard to upstream and midstream operations are liable to Service tax at the rate of 12.36 percent
- Set-off of input Service tax / Excise duty available to a contractor / sub-contractor against its output Service tax liability

VAT

- Goods procured locally are chargeable to VAT at the rate of either 4 percent or 12.5 percent, which may be a cost
- Sale of petroleum products chargeable to VAT, however VAT credit restricted on purchase of certain key products such as MS, HSD, etc

Tax Environment – Indirect Tax

Hot Topics

- Levy of Service tax on upstream operations constitute a significant cost due to the inability of owners to utilize input credit
- Procurement chain planning - varied VAT rates for same products in different states require procurement chains to be carefully planned
- Management of tax credits – efficient management of tax credits can positively impact working capital

Major Developments

- Constant evolution of Service tax laws to tax sophisticated transactions/ service arrangements. For example; introduction of new taxable category of 'supply of goods for use' has led to re-evaluation of equipment hiring contracts
- Convergence of Customs duty and Transfer Pricing regime – Synergy between different Revenue departments require businesses to be cautious and thorough with regard to international transactions
- Introduction of GST in 2010 – Positive impact on businesses due to unification of levies, availability of cross credits between Central & State levies, etc

Operating Globally

- Wide treaty network
- Investment structures through Mauritius, Cayman Islands, Singapore and UAE preferred
- No thin cap regulations in India – ability to structure inter company payments and capital in a tax efficient manner
- ‘Onshore’ services beyond ‘threshold’ lead to creation of permanent establishment in most cases
- Cyprus preferred for out-bound investments due to deemed credit availability
- Onerous transfer pricing regulations

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Kazakhstan

Ward Jones

Tax Environment – Corporate Tax

- Profit tax rate = 30 percent
- Branch profit tax rate = 15 percent (on net after-tax profits)
- Draft new tax law proposes to reduce Corporate Income Tax rate to 15 percent in 2009

Tax Environment – Corporate Tax

- Kazakh-source income includes income from six “tainted services”
- Gain on sale of Kazakh company is Kazakh-source income
- Gain on sale of foreign company can be Kazakh-source income
- Draft new tax law proposes to exempt gains from income tax in case of shares sold on a stock exchange

Tax Environment – Corporate Tax

- 20 percent on all other service fees, including royalties, and gains from sales of assets
- Draft new tax law proposes to eliminate tax on dividends on stakes held less than 3 years and on gains from sale of company or parts thereof, except in natural resource sector, and to reduce the tax rate on service fees and royalties to 15 percent

Tax Environment – Corporate Tax

- Excess profits tax
 - Historically triggered when project IRR exceeded 20 percent
 - Since 2004 triggered when cumulative project revenues exceed cumulative deductible project expenses by more than 20 percent
- Draft new tax law proposes to trigger excess profits tax whenever annual project revenues exceed annual deductible project expenses by more than 20 percent

Tax Environment – Corporate Tax

- Tax stability gone for most subsoil users
- Ring fencing required and no consolidated tax filings
- Transfer price issues
- Tax losses can be carried forward 7 years (10 under draft new tax law)
- Intended tax audit by tax authorities on annual basis

Tax Environment – Indirect Tax

- VAT rate of 12 percent in 2009
- Export customs duty on crude oil – flat amount per ton
- Tax on exported crude oil or gas condensate
 - Rates on a sliding scale reaching 33 percent of selling price at an oil price of USD 40 per barrel (draft new tax law reduces the tax to approximately 32 percent of selling price at USD 180 per barrel)
- Mineral extraction tax to replace current royalty
 - Royalty on a sliding scale based on annual production and reaching a 6 percent rate. MET on a sliding scaled based on annual production and reaching a 20 percent rate.

Operating Globally

Kazakhstan's tax treaties

- Armenia
- Azerbaijan
- Austria
- Belarus
- Belgium
- Bulgaria
- Canada
- China
- Czech Republic
- Estonia
- France
- Georgia
- Germany
- Hungary
- India
- Iran
- Italy
- Kyrgyzstan
- Latvia
- Lithuania
- Malaysia
- Moldova
- Mongolia
- Netherlands
- Norway
- Pakistan
- Poland
- Romania
- Russia
- Singapore
- South Korea
- Sweden
- Switzerland
- Tajikistan
- Turkey
- Turkmenistan
- United Kingdom
- Ukraine
- United States
- Uzbekistan

Tax Developments

- End of tax stability for most natural resource companies
- New tax law shifting more of overall tax burden to natural resource sector
- New export customs duty on natural resources
- New mechanism for taxing gains on nonresident's sales
- The state has a priority right to any interest offered for sale
- The government must approve any buyer purchasing an interest declined by the state

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Malaysia

Chinguan Khoo

Overview of Petroleum Income Tax in Malaysia

- Introduction
- Extent of Petroleum Income Tax Collection on Malaysian Government's Revenue
- Petroleum Income Tax Rates
- Concept of Chargeable Person
- Comparison with Income Tax Act 1967

Introduction

- Position prior to enactment of Petroleum (Income Tax) Act 1967
- Introduction of Petroleum (Income Tax) Act 1967
- Distinction between income from petroleum operations and income from non-petroleum operations

Extent of Petroleum Income Tax Collection on Malaysian Government's Revenue

Year	Petroleum Income Tax (RM Million)	% of Malaysian Government's Revenue
2003	8,466	9.14%
2004	11,479	11.55%
2005	14,566	13.70%
2006	20,674	16.73%
2007	20,453	14.62%
2008	24,511 (revised estimate)	15.17%
2009	35,826 (budget estimate)	20.33%

Source : Economic Reports, Ministry of Finance Malaysia

Petroleum Income Tax Rates

(a) Taxation of Income from Petroleum Operations in Malaysia

	Tax Rate
YA 1968 to YA 1975	50%
YA 1976 to YA 1993	45%
YA 1994 to YA 1997	40%
YA 1998 to date	38%

Petroleum Income Tax Rates

(b) Taxation of Income from Petroleum Operations in Joint Development Area (JDA)

	Tax Rate
First 8 years of production	0%
Next 7 years of production	10%
Subsequent years of production	20%

Paragraph 1(a) Article 7A Malaysia/Thailand DTA
- 50 percent reduction

Concept of Chargeable Person

- Reference to petroleum agreement
- By Definition
 - PETRONAS
 - Malaysia-Thailand Joint Authority (MTJA)
 - Any other person carrying on petroleum operations

Multiple Agreements

- Separate Chargeable Person
- Implications
 - Ring-fencing provisions
 - Manner of set-off expenses, Schedule 1 Allowances, Schedule 2 Allowances and Losses

Contiguous Agreement Areas

- Partnership carrying on petroleum operations under two or more petroleum agreements
- Areas are contiguous
- Treated as one petroleum agreement

Contiguous Agreement Areas

Position Pre 21 October 1988

- Partnership has more than one petroleum agreement
- No change in members of the partnership
- Treated as one petroleum agreement

Comparison with Income Tax Act 1967

	Petroleum Income Tax	Income Tax
Self Assessment	No	Yes
Basis of Assessment	Preceding Year	Current Year
Basis of Taxation	Generally, by reference to each petroleum agreement	At Company's level
Deadline for Filing of Accounts/Tax Return	3 months	7 months
Dividend Payment	Tax exempt (Section 84)	Section 108/Single-Tier

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Singapore Siew Moon Chung

Singapore – Corporate Tax

- Corporate tax rate of 18 percent
- Group Relief System
- One-tier dividend system
- Tax depreciation for qualifying capital expenditure
- Research & Development (R&D) Incentives
 - R&D Incentives for Start-ups (RISE)
 - R&D Allowance
 - Enhanced Deductions of 150 percent to 200 percent

Singapore – Indirect Tax

- GST rate of 7 percent
- For GST purposes, a supply can be a sale of good or services
- Standard Supplies
- Zero-Rated supplies
 - Goods that are exported
 - Services that are classified as International Services
- Exempt Supplies
 - Sale and rental of unfurnished residential property
 - Financial Services
- Out-of-Scope Supplies

Operating Globally

- 58 Comprehensive Tax Treaties
- No CFC regime
- No thin capitalization rules
- No withholding tax on dividends

Singapore Transfer Pricing (1)

- There are no transfer pricing regulations in Singapore
- Transfer Pricing Guidelines Circular issued in February 2006 with detailed guidance on
 - applying the arm's length principle;
 - using the appropriate transfer pricing method; and
 - documentation requirements
- This circular applies to both local and cross-border transactions, between a Singapore taxpayer and its related parties.
- The circular also sets out the procedures for applying for the Mutual Agreement Procedures and Advanced Pricing Arrangement facilities in order to avoid or eliminate double taxation.

Singapore Transfer Pricing (2)

- In July 2008, IRAS released a TP consultation to monitor taxpayers' compliance with TP guidelines.
- In October 2008, the IRAS has issued guidelines on the application of Advance Pricing Agreements (APA).
- A draft supplementary circular has been issued in October 2008 to obtain public feedback on the treatment of intra-group services, management fees and loans. A circular based on the feedback is expected to be released soon.

Singapore Tax Incentives

- Trading Company
 - Global Trader Program
- Shipping Operations
 - Approved International Shipping
- Headquarters Services
 - HQ incentives
 - Development and Expansion (DEI)
- Refineries
 - Pioneer Incentive/DEI

Use of Singapore as a base

- Trading Company
- Shipping Company
- Holding Company
- Headquarter
- Service Company

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