TAXATION OF NATURAL RESOURCES:

LEGAL FRAMEWORK CHOICES

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CONTENTS

OBJECTIVE AND INGREDIENTS OF NATURAL RESOURCES TAXATION 3

IMPERATIVE FOR EFFECTIVE TAX LAW DRAFTING SKILLS 4

INADEQUACY OF LEGAL FRAMEWORK FOR MINING AND PETROLEUM PRODUCTION TAX IN AFRICA 5

STRATEGIES FOR TAXATION OF INTER-GROUP TRANSACTIONS: IMPACT OF DOUBLE TAXATION AGREEMENTS PERMITTING FOR INVOLVEMENT OF WORLDWIDE ASSOCIATES ON THE HOST COUNTRY 6

LEGISLATING BENEFICIATION AND REFINING AS A TOOL FOR STEMMING EROSION OF MINING AND UPSTREAM PETROLEUM TAX BASE 7

REVIEW OF THE INCENTIVES REGIME FOR PETROLEUM, DOMESTIC GAS PROJECTS AND SOLID MINERALS AND THE IMPERATIVE FOR A THRESHOLD RULE 8

REFORMING MINING AND PETROLEUM TAX LAWS IN AFRICA: SELECT COUNTRY REVIEWS 9

IMPACT OF ROYALTIES ON HURDLE RATE 10

TAX CONTROVERSIES ON NIGERIA’S PETROLEUM INDUSTRY BILL 11

RECOMMENDATIONS AND CONCLUSION 12

APPRECIATION 13
The objective of solid mineral mining and petroleum taxation:

- Modulate investments
- Raise government revenue

Consideration ➔ Weight of burden on tax payer

Legislate robust tax regimes for natural resources in Africa based on the ingredients of a good tax law:

- Clarity (Simple for the tax payer to understand)
- Absence of ambiguity
- Non-Retroactivity
- Realistic
- Compliability
- Fairness
- Equity (The fiscal regime should be designed to function well at all potential levels of profitability)
Each sovereign country has the right to design and enact its own tax legislations.

The drafting of tax laws in Africa has taken a technical format.

The IMF has recommended that African countries adopt a plain language approach for the drafting of tax legislations and regulations because it enhances compliance.

African countries include tax rates for natural resources in figures, rather than in percentage. Using figures in a legislation can be affected by economic volatilities.

For example in Mozambique, there are three clear shortcomings that apply to the petroleum and mining fiscal laws:

- A lack of clarity on provisions for accelerated depreciation of capital investments;
- A lack of specificity on the rate of the capital gains tax; and
- An over-reliance on sale price rather than international benchmarks for establishing value.
INADEQUACY OF LEGAL FRAMEWORK FOR MINING AND PETROLEUM PRODUCTION TAX IN AFRICA

- Using the Nigerian example, there has been various relinquishments and transfer of onshore oil blocks by international oil companies to indigenous licensees.
- Was Nigeria’s Federal Inland Revenue Service (FIRS) aware of these transactions and did it assess these asset(s) transfers for the purpose of Capital Gains Tax (CGT)?
- If the FIRS was not aware, was it due to the absence of a legal provision making it mandatory for the Department of Petroleum Resources (DPR) to notify the FIRS of any such development prior to its processing of the asset transfer documentation for the consent of the Petroleum Minister?
- Similarly, several indigenous upstream petroleum production licensees have been benefiting from ‘Pioneer Status’ which is statutorily provided for companies involved in purely industrial processes.
- Are these indigenous upstream licensees entitled to ‘Pioneer Status’ despite:
  a. the generous tax reliefs and waivers provided by the Petroleum Profits Tax Act and the Deep Offshore and Inland Basin (Production Sharing Contracts) Act?
  b. that their oil blocks are ‘hand over’ oil / gas fields which have been de-risked?
- As a basis for continued waiving of tax obligations is there a legal provision compelling a government agency to monitor the operations of ‘Pioneer Status’?
There are a number of fiscal incentives which can effectively shore up a country’s attractiveness for foreign investments such as a guarantee of profit repatriation which may inserted as clauses in Bilateral Investment Treaties (BITs) and Double Taxation Treaties (DTTs).

Since BITs and DTTs trade off the taxing rights of a source country, they should be drafted to effectively block tax avoidance loopholes.

Branch or associate company operations can be structured on the same project to obtain DTA benefits, even when the home country of the branch or associate company has no DTA with the host country.

Tax treaties usually limit the jurisdiction of a source country to tax.

Do African countries need to trade - off their taxing rights over oil, gas and mining transactions – What are the quid proco for Africa?
Legislating Beneficiation and Refining as a Tool for Stemming Erosion of Mining and Upstream Petroleum Tax Base

- There is need for a provision in African tax legislations that would drive beneficiation of solid minerals and refining of a significant percentage of crude oil prior to export, with deterrent penalty clauses. This can be achieved through:
  
  - increased custom duties for export of solid minerals and crude oil in their unprocessed stage;
  
  - elimination of Pioneer Status relief for mining and petroleum producing companies and ASMs who have not demonstrated any corporate plan/capacity to locally beneficiate and refine their natural resources; and
  
  - who are not selling their products to their home country industrial and manufacturing sector in instances where such natural resources are required as by-products for other products that are a significant component for their home country’s industrial growth.
African countries have addressed the question of tax holidays for petroleum and solid mineral upstream activities from different perspectives:

- Zimbabwe, Tanzania and Ghana do not have tax holidays for the sector;
- Cote D'Ivoire, Burkina Faso and Nigeria have tax holidays for the two sectors.

Legislations in several African countries provide that a new company engaged in petroleum production or mining is entitled to fiscal incentives such as to be exempted from tax for a statutorily stipulated number of years of its operation.

Legislations have also allowed mining and E & P companies to recover their investments and break-even within statutorily stipulated years. However:

- There is no statutory provision to cater for companies who may break-even earlier than the stipulated years' period.
- A better alternative to this “Period Rule” would be to set a “Threshold Rule” for the evaluation of the profitability of new mining and E & P companies so they can be assessed, for tax incentive evaluation purposes, at six months periodic intervals and de-listed as ‘in mature’ rather than at the expiration of the three years stipulated.

Should fiscal incentives replace infrastructure development by Government?
Tax is not a profit centre for the government.

It should not be pigeon holed in a silo.

The essence of mining or E & P taxation is not to put the taxpayer out of business.

The formulators of tax legislations should therefore have a good understanding of corporate planning and of the business of the sector being taxed.

What are the cumulative effects that taxes and royalties would have on the economics of a mining or an E & P project?

The tax legislation should take cognisance of the prevailing and projected hurdle rate for taxable mining and E & P projects as well as their internal rate of return (IRR).
Nigeria’s National Assembly first received the PIB in 2008 as an Executive Bill which seeks to reform her oil and gas industry. With the end of Nigeria’s sixth National Assembly, the PIB is yet to become law after a second submission to parliament in 2012.

The PIB seeks to repeal all the 13 existing oil and gas legislations, including the Petroleum Profits Tax Act and the Deep Offshore and Inland Basin (Production Sharing Contracts) Act (DOIBA) and re-enact as well as amend most of the provisions of the legislations into a single legislation.

Under the prevailing legislative framework companies that are assessed for Petroleum Profits Tax (PPT) are statutorily extricated from Companies Income Tax (CIT).

PIB’s fiscal rates on production in the deep offshore have completely changed DOIBA’s rates.

Under the PIB, if passed into law, petroleum production companies will be expected to pay CIT as well as ‘Nigeria Hydrocarbon Tax’ (‘NHT’) which has replaced the PPT.

International oil companies (IOCs) and other operators view PIB’s fiscal provisions as an attempt at multiple taxation.

IOCs and other operators also view the rates in the various taxes and royalties that the PIB intends to impose on them as capable of eroding the prospects of any profit by them.

Should the fiscal provisions in the PPTA be in the PIB or be in a stand – alone legislation outside PIB?
REFORMING MINING AND PETROLEUM TAX LAWS IN AFRICA: SELECT COUNTRY REVIEWS

- **NIGERIA**
  - Is it elegant to have the tax law embedded into a general legislation like the PIB?
  - Need for coherence in tax adjudication - *Federal High Court vs TAT*
  - Regulating tax deductibility of Decommissioning, Restoration and Abandonment

- **UGANDA**
  - Impact of Stabilisation Clauses for Tax Rates in Petroleum Production Contracts

- **TANZANIA**
  - Ring-fencing rules to protect potential mining tax revenues

- **ZAMBIA**
  - Replaced the profit based tax system with a simple mineral royalty based regime

- **GHANA**
  - New legislative provision on non-Ring Fencing of natural resources
The National Tax Policy of several African countries such as Nigeria seek to grow the mining and upstream petroleum sectors into major profit centres for the countries.

There is need for a provision in their respective tax legislations that shall accelerate beneficiation of African sourced solid minerals and refining of African sourced crude oil prior to export through:

- increased custom duties for export of solid minerals and crude oil in their unprocessed stage and the elimination of Pioneer Status relief for mining and petroleum production companies

In order to hide their transactions from the tax authority, some companies have mining, petroleum production as well as manufacturing as part of their object clauses:

- Such companies file their tax returns claiming to be engaged solely in manufacturing and to have had a bad financial year owing to the absence of electricity and other critical infrastructure.
- There is thus need to ensure that such companies do not benefit from the fiscal incentives earmarked for the mining sector; and
- There should be a provision in the mining and petroleum legislations that companies applying for licence should be companies incorporated with sector specific object clauses.
In am appreciative to the Management of the IBFD Knowledge Centre for inviting me to make this presentation.

Thank you for listening.