ADIT

Chartered Institute of Taxation
Excellence in Taxation

THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2019

MODULE 3.04 – UPSTREAM OIL AND GAS OPTION

ADVANCED INTERNATIONAL TAXATION (THEMATIC)

TIME ALLOWED – 3¼ HOURS

This exam paper has **three** parts: **Part A**, **Part B** and **Part C**.

You need to answer **five** questions in total.

You must answer:

- **Both** questions in **Part A** (25 marks each)
- **One** question from **Part B** (20 marks)
- **Two** questions from **Part C** (15 marks each)

Further instructions

- All workings should be made to the nearest month and in appropriate monetary currency, unless otherwise stated.
- Start each answer on a new page and clearly indicate which question you are answering. If you are using the on-screen method to complete your exam, you must provide appropriate line breaks between each question, and clearly indicate the start of each new question using the formatting tools available.
- Marks may be allocated for clarity of presentation of your answers.
- The time you spend answering questions should correspond broadly to the number of marks available for that question. You should therefore aim to spend approximately half of your time answering Part A, and the other half answering questions in Parts B and C.
- The first 15 minutes of the exam is reading time. You will be allowed to annotate the question paper during this time; however, you will **not** be permitted to start writing or typing your answer. The Presiding Officer will inform you when you can start answering the questions.

PART A

You are required to answer BOTH questions from this Part.

1.

1) In the upstream oil and gas industry, international oil and gas companies enter into a range of contracts with host countries including concession agreements, Production Sharing Contracts (PSCs) and service contracts. The different types of contract are characterised by differing fiscal regimes.

   You are required to explain the key features of, and differences between, the types of international oil and gas agreement mentioned above. (9)

2) Oil and gas fiscal terms often include royalties, signature and production bonuses, rentals, state equity and carried interests, export duty, and other indirect taxes.

   You are required to explain what is meant by 'royalties' and 'signature and production bonuses' in this context, including appropriate examples. Your answer should cover the advantages and disadvantages of each. (16)

Total (25)

2. Oil and gas producing countries can choose to administer the taxation of oil and gas revenues in different ways, and model their tax provisions, to restrict certain aspects of cost deduction with a significant impact upon the taxation of oil and gas companies' profit and government tax revenues. Ring fencing provisions are among the ways in which countries may choose to model the tax treatment of revenues, in order to limit specific tax deductions for the oil and gas companies.

You are required to:

1) Explain the concept of ring fencing in oil and gas fiscal arrangements (and how the scope may differ), and discuss the impact of ring fencing on the taxation of both the oil and gas company and the oil producing state. (15)

2) Discuss at least four different examples of countries which have ring fencing provisions or regimes in place, and how they operate. (10)

Total (25)

PART B

You are required to answer ONE question from this Part.

3.

1) A primary issue when acquiring oil and gas assets is whether to acquire the target company by acquiring shares in that company, or alternatively to directly acquire the assets of the company.

   You are required to discuss the related acquisition and tax issues that may arise from such an international investment. (12)

2) Transfer pricing is the requirement in many countries to adopt pricing for goods and services between related companies on an arm's length basis, in other words the prices which would be paid if the parties were not related. The Organisation for Economic Cooperation and Development (OECD) has issued suggested methodologies and procedures relating to transfer pricing.

   The transfer pricing methods proposed by the OECD include the comparable uncontrolled price (CUP), resale price method (RPM), cost plus method (CPM), transactional net margin method (TNMM), and profit split method (PSM).

   You are required to explain four of the transfer pricing methods proposed by the OECD. Your answer should include examples from the oil and gas industry. (8)

Total (20)

4. Oil and gas service companies are commonly used as subcontractors by oil and gas companies to provide exploration and production works in a number of countries around the world. For offshore projects, this normally entails the use of a representation office initially and at a later stage equipment such as vessels or rigs within the territorial waters or economic exclusive zones of these countries, leading to possible tax impacts arising from the formation of a permanent establishment (PE).

   Please discuss the concept of a PE, and the PE tax considerations faced by oil and gas service companies. (20)

PART C

You are required to answer TWO questions from this Part.

5. Upstream oil and gas investments may be financed internally or externally.

   You are required to discuss the key features of intra-group financing and banking arrangements. (15)

6. Accounting practice defines decommissioning as "the process of plugging and abandoning wells, dismantlement of wellhead, production and transport facilities and restoration of producing areas in accordance with licence requirements and the relevant legislation".

   You are required to:

   1) Discuss various ways in which decommissioning costs may be treated in relation to the taxation of oil and gas activities. (10)

   2) Discuss when, in the case of the United Kingdom, a provision may be deducted in accordance with the HMRC rules. (5)

   Total (15)

7. The corporate structure used to acquire and hold and oil and gas license in a specific country can have a significant impact on the treatment of potential tax impacts or costs, in a future sale of the licence to a third party or even an affiliate or group company for restructuring purposes.

   Comment on the paragraph above, and discuss the different items that need to be considered in relation to the tax impacts on an oil and gas licence sale. (15)

8. You are requested to assist your company's board with a tax review for a new venture opportunity in an upcoming bidding round, and to give your thoughts on the financial model to be used.

   Outline your main tax concerns with regard to the opportunity, and your opinion regarding the financial model analysis. (15)