THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

December 2024

MODULE 3.04 – ENERGY RESOURCES 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 will **not** receive marks for any additional answers.

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 in appropriate monetary currency, unless otherwise stated. Any monetary calculations should be made to the nearest whole unit of currency. Any necessary time apportionments in your calculations should be made to the nearest whole month.
- 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.
- There is no separate reading time, so you can start typing your answers as soon as the exam begins. However, we recommend that you set aside some time to thoroughly read each question and plan each of your answers.

PART A

You are required to answer BOTH questions from this Part.

1. On 1 January 2020, the Lucky Oil Company (Lucky Oil) signed a production sharing agreement (PSA) with a host country, Country Z. The terms of the PSA were as follows:

    1. Lucky Oil will pay Country Z a £100,000 signature bonus. This payment cannot be recovered via cost oil and is not deductible for corporate tax purposes.

    2. The PSA will cover an area of 500 hectares in the southeast of Country Z, and will last for 25 years. The PSA can be extended by a further five years, upon agreement between Lucky Oil and Country Z.

    3. Lucky Oil has incurred pre-production exploration, appraisal and operational costs of £1 million. This cost is to be recovered from the cost oil.

    4. Lucky Oil incurs annual production-related operating costs of £200,000. These costs are deductible for corporate tax purposes.

    5. A royalty of 10% is to be received in kind. Royalties received in kind are not considered an allowable deduction for corporate tax purposes, and the royalty is deducted before splitting profit oil.

    6. Profit oil is to be split, with 40% going to Lucky Oil and 60% to Country Z. For cost recovery, opex is recovered first, then capex on an undepreciated, cash-incurred basis, and there is no cost oil ceiling.

    7. Lucky Oil will pay corporate tax to Country Z at a rate of 20% on its profits.

    8. Lucky Oil has installed production platforms and other fixed assets at a cost of £30 million. These are expected to last for 30 years and their value will depreciate on a straight line basis over the 30-year period. Depreciation charges are considered allowable expenses for corporate tax purposes. The depreciation charge in 2020 can be set against revenues in 2021 and subsequent years.

    9. Oil production started on 1 January 2021. Production quantities and agreed oil prices between Lucky Oil and Country Z for the period between 2021 and 2023 were as follows:

Year	Oil production (barrels)	Oil price (£ per barrel)
2021	800,000	£40
2022	900,000	£42
2023	1,000,000	£44

    You are required to:

    1) Calculate the profits after tax for Lucky Oil over the 2020-2023 period. (20)

    2) Calculate the tax and other revenues payable to Country Z over the 2020-2023 period. (5)

    Total (25)

2. **You are required to discuss the role of tax treaties in the context of the oil and gas industry. Critically evaluate how tax treaties affect the financing of extractive investments, capital gains taxation and withholding taxes, and highlight the benefits and challenges faced by investors.** (25)

PART B

You are required to answer ONE question from this Part.

3. It has been argued that carbon taxes are the most efficient and cost-effective way to curb climate change and address the problem of global warming.

   You are required to:

   1) Define 'carbon taxes' and discuss how implementing a carbon tax system may incentivise businesses to reduce their carbon emissions. (8)

   2) Identify and discuss four potential benefits of carbon taxes for climate change mitigation and sustainable development. (12)

   Total (20)

4. **You are required to explain the concept of 'contractual assurances of fiscal stability' in oil and gas agreements, with a focus on the role and function of fiscal stability clauses. Critically evaluate the types of fiscal stability assurance available to investors, such as 'frozen law' and 'agree-to-negotiate' clauses, and discuss the implications of these clauses on both the host government and investors.** (20)

PART C

You are required to answer TWO questions from this Part.

5. The merger and acquisition of oil and gas corporations presents several important tax concerns. Tax issues such as 'debt push down' involve utilising interest deductions from loans to buy assets and applying them in the country where the purchase was made.

   You are required to:

   1) Discuss the tax implications of interest deductions in the case of purchasing assets or target shares of oil and gas companies. (8)

   2) Discuss the tax implications of interest deductions in the case of this deduction being 'pushed down' to the target company's country. (7)

   Total (15)

6. The tax due diligence process is often an important factor in the context of a planned investment or deal. The objectives of tax due diligence are to recognise tax-related opportunities and risks, and to acquire fresh insights that may aid in designing the most beneficial transaction structure for the prevailing tax regulations.

   During an oil and gas acquisition, investment or deal, the purchaser must examine important details as part of the tax due diligence process. Information can be provided in either a physical or online data room, with the option for buyers to request the inclusion of additional documentation.

   You are required to outline ten key issues that should be reviewed in the tax due diligence process by the buyer's team. (15)

7. In the context of the oil and gas industry, leases and sale-leaseback agreements are commonly used as financial tools.

   You are required to:

   1) Identify and discuss the differences between finance leases and operating leases, from both accounting and tax perspectives. (11)

   2) Explain the tax implications of sale-leaseback agreements, particularly in relation to cross-border leasing operations, and outline the advantages and potential risks associated with each type of lease structure. (4)

   Total (15)

8. **You are required to critically analyse the role of royalties in the fiscal regime for extractive industries. Discuss the advantages and challenges of using royalties, as opposed to profit-based taxes, for governments seeking to maximise their revenues from natural resources, and support your analysis with appropriate examples.** (15)