THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2022

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 to the nearest month and in appropriate monetary currency, unless otherwise stated.
- As you are using the online 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.
- 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. Many countries apply a tax and concession regime to upstream oil and gas operations.

   You are required to discuss the characteristics and structures of the tax and concession regime, and differentiate it from both production sharing agreements and service contracts. (25)

2. When deciding whether or not to make an investment in a specific jurisdiction, oil and gas companies consider various tax and cost issues in order to ascertain the possible rate of return on the investment.

   The tax regime to which any future profits will be subject is an important factor in this analysis, and any future changes to this regime during the period of investment will significantly affect the calculated return. However, there are solutions that may be used to prevent or discourage countries from introducing new windfall taxes or changing the tax regime for existing contracts.

   You are required to discuss how governments may change applicable tax regimes and impact upon the calculated return on an oil and gas project, and explain, using specific examples of past cases, what solutions are available to the oil and gas companies to protect their investment against such changes. (25)

PART B

You are required to answer ONE question from this Part.

3. Carbon taxes are designed to incentivise businesses and industries to reduce their greenhouse gas emissions, and to reflect the true cost to the environment and society of burning carbon-based fuels.

   You are required to:

   1) Discuss the advantages and disadvantages of carbon taxes. (12)

   2) Differentiate between carbon taxes and emission trading schemes. (8)

   Total (20)

4. The licence holders of oil and gas projects require the help of several different service companies to carry out the various operations that are necessary during the lifespan of an exploration, development and production project.

   These contracting service companies will be required to operate in several different regions and sometimes for short periods of time (in some cases, less than three months). As a result, it is common for service companies to use representation offices and permanent establishment (PE) structures to carry out these works while using equipment, such as vessels and rigs, which may affect their tax position.

   You are required to discuss the concept of a PE, and the related tax considerations for service companies that provide these oil and gas project services. (20)

PART C

You are required to answer TWO questions from this Part.

5. Lucky Oil is a company based in the United Kingdom and operating in an oil producing host country in the Middle East. In 2021, the oil production from its three fields totalled 4.6 million barrels and was valued at £200 million.

   Lucky Oil operates under a production sharing agreement which has the following tax structure:

   - A royalty at 10%;
   - A corporate tax rate of 40%;
   - Annual allowable development costs of £60 million; and
   - An oil profit split of 60% to the host government and 40% to Lucky Oil, with allowable costs to be capped at 50% of gross oil income with excess costs carried forward to the next two years.

   You are required to:

   1) Calculate the value of each of the host government's and Lucky Oil's corresponding shares of the profit. (10)

   2) Determine how the profit share would change if the host government were to pay corporate tax on Lucky Oil's behalf. (5)

   Total (15)

6.
   1) The decommissioning of oil and gas assets involves removing topside installations, well plugging, decking concrete caissons, and the removal of pipelines and sub-sea equipment, and incurs considerable cost.

      You are required to discuss the tax implications related to decommissioning costs. (8)

   2) Leasing is primarily a source of financing in which a company does not have to provide immediate funds to acquire the asset. Under a finance lease, the lessee will eventually obtain ownership of the asset. Under an operating lease, the lessee merely rents the asset for the period of the lease.

      You are required to discuss the tax implications of operating and finance leases for upstream oil and gas companies. (7)

   Total (15)

7. The possible limitation of interest deductions through legislation in different jurisdictions is a factor that oil and gas companies should consider before deciding on how an oil and gas project is to be funded. The treatment of interest deductions may significantly influence any decision regarding the optimisation of interest expenses.

   You are required to discuss the different ways in which thin capitalisation rules may affect the tax deduction of interest expenses, and the alternative options that may be available to companies. (15)

8. Oil and gas exploration requires an extensive amount of upfront capital and investment before any return on investment is likely to be achieved. There are likely to be significant amounts of exploration losses in the project's jurisdiction, requiring careful analysis and planning by the oil and gas companies involved to ensure that these losses can be recovered as the project evolves into its production stage.

   You are required to:

   1) Discuss how planning for an appropriate structure can optimise the recovery of losses. (9)

   2) Provide three distinct examples of country regimes, in relation to the recovery of losses by oil and gas companies. (6)

   Total (15)