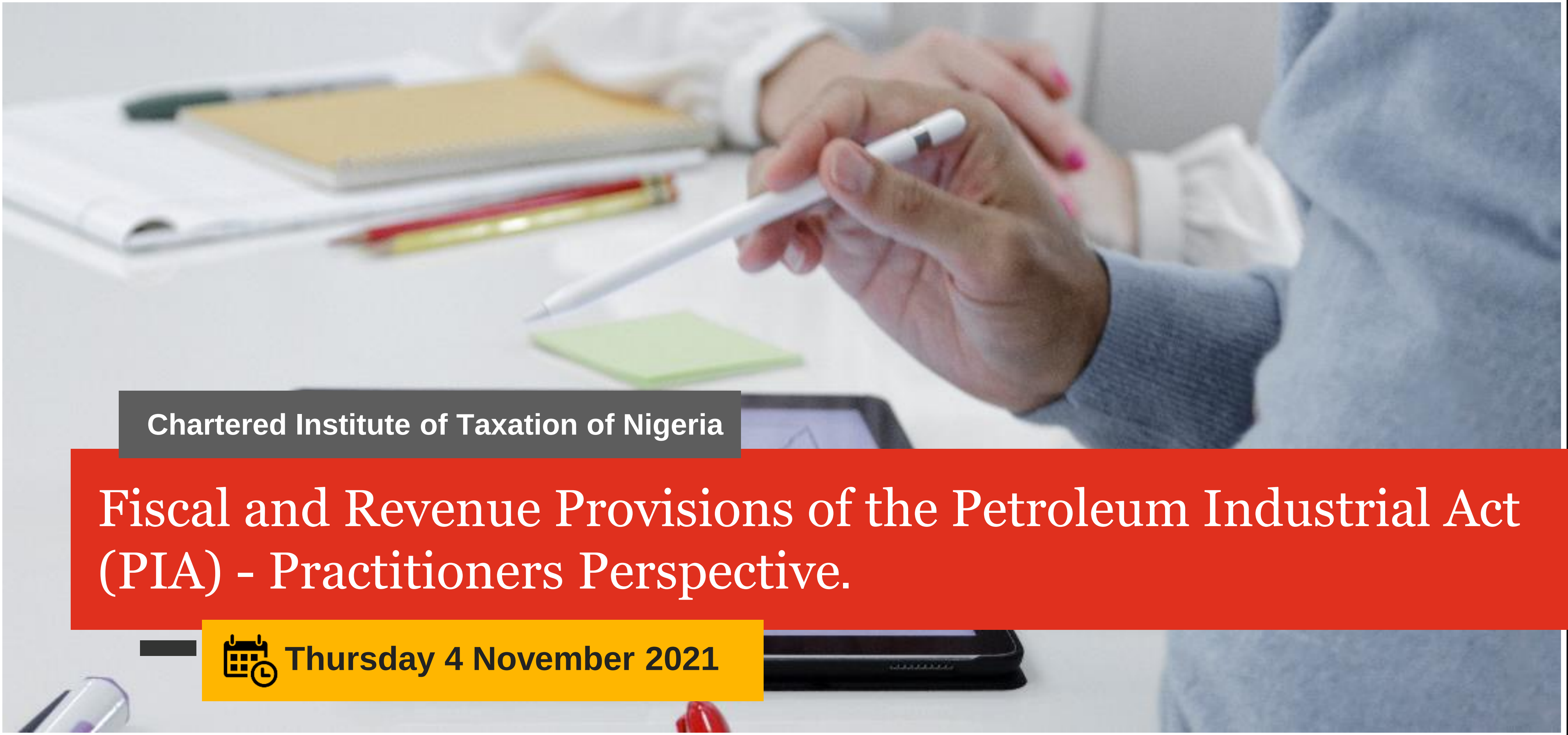

Chartered Institute of Taxation of Nigeria

Fiscal and Revenue Provisions of the Petroleum Industrial Act (PIA) - Practitioners Perspective.

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pwc

Presenter

Kenneth Erikume

Partner, PwC Nigeria

Kenneth is a partner in PwC Nigeria. He has many years of experience in dealing with the tax and regulatory issues for companies in Africa and in different industries including oil and gas, telecommunications, media and entertainment, financial services and consumer and industrial products.

His major areas of specialization involves Fiscal policy and tax administration, Tax Reporting & Strategy, International Tax, Mergers and Acquisitions Tax Advisory and Tax Due Diligence and Domestic Taxation

He is a regular facilitator for the mandatory professional education for ICAN and CITN and leads the tax thought leadership team, the tax reporting and strategy team and the Financial Services tax business development initiatives of PwC Nigeria.

Kenneth is a member of the Chartered Institute of Taxation of Nigeria (CITN) and also an indirect tax faculty member of the CITN. He is also a member of the Institute of Chartered Accountants of Nigeria (ICAN) and has a Certificate in International Treasury Management from the Association of Corporate Treasurers (ACT), UK.

Course Outline

01 The Nigerian economy with a focus on the Fiscal environment

02 The Petroleum Industry and the Nigerian economy

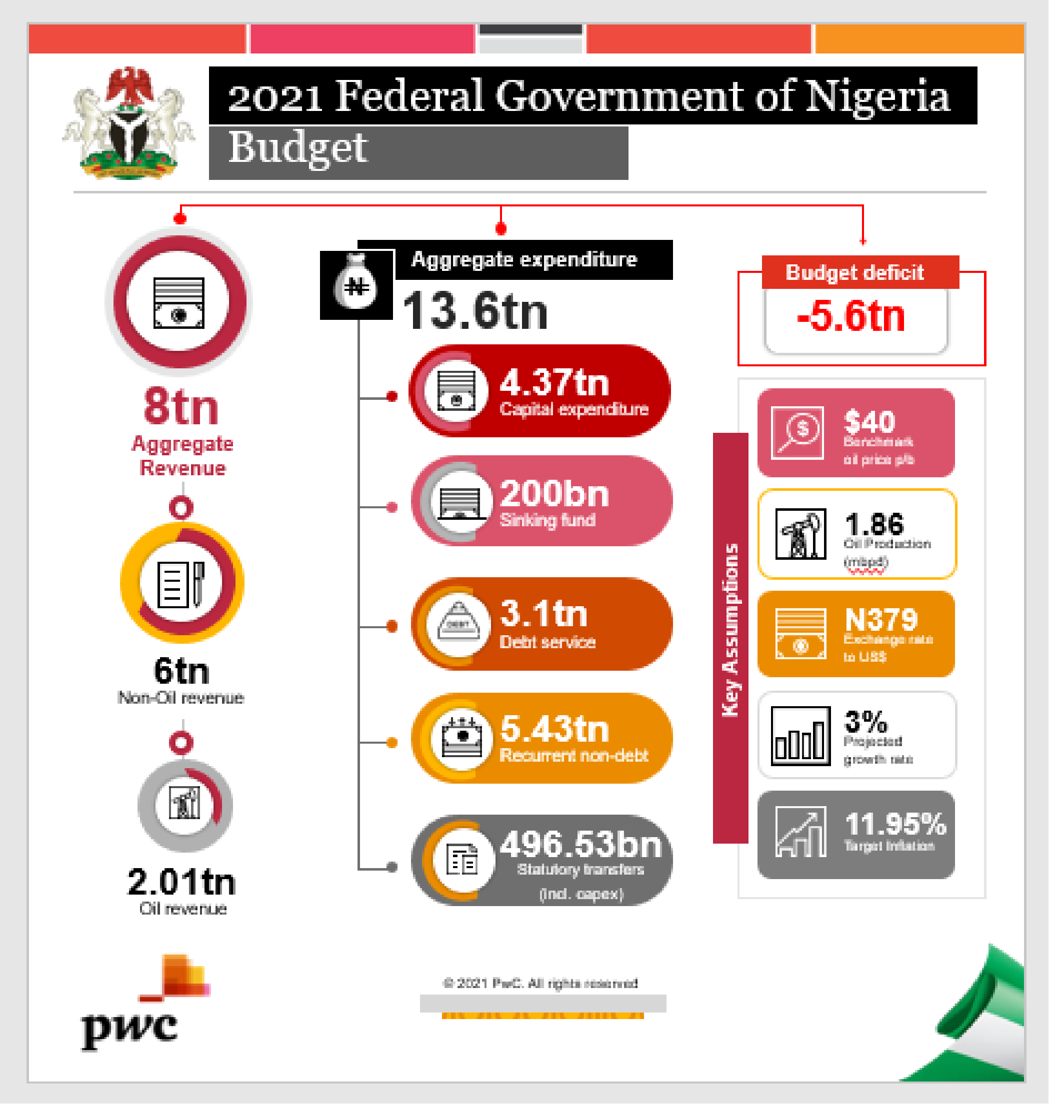
03 The Petroleum Industry Act 2021

04 Implementation of the PIA

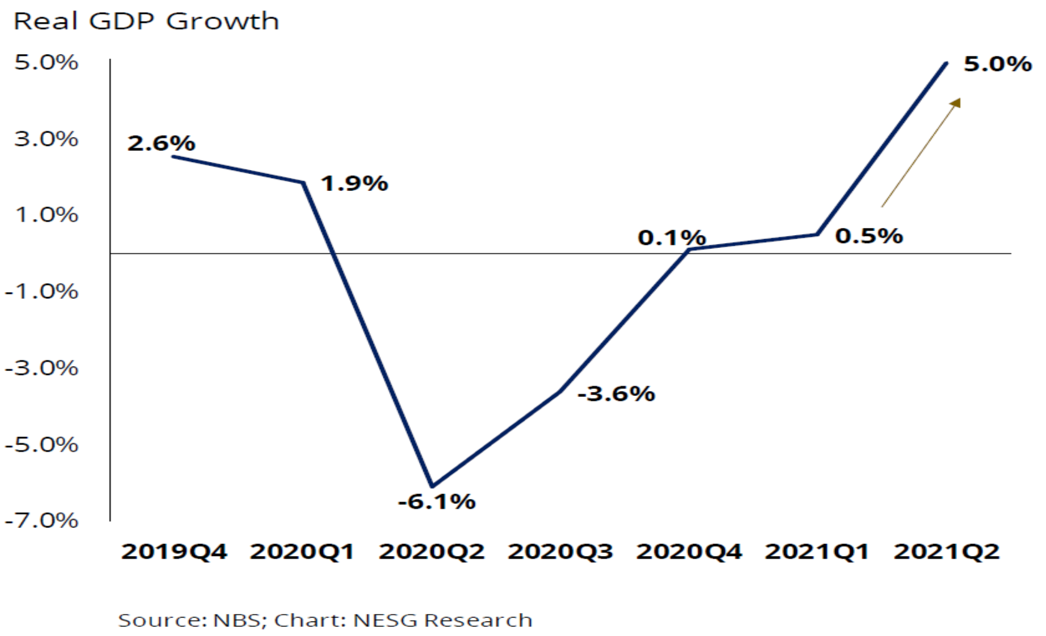
The Nigerian economy with a focus on the Fiscal environment

01

The current state of the Nigerian economy



Gross Domestic Product (GDP) – Quarter 2 (2021)



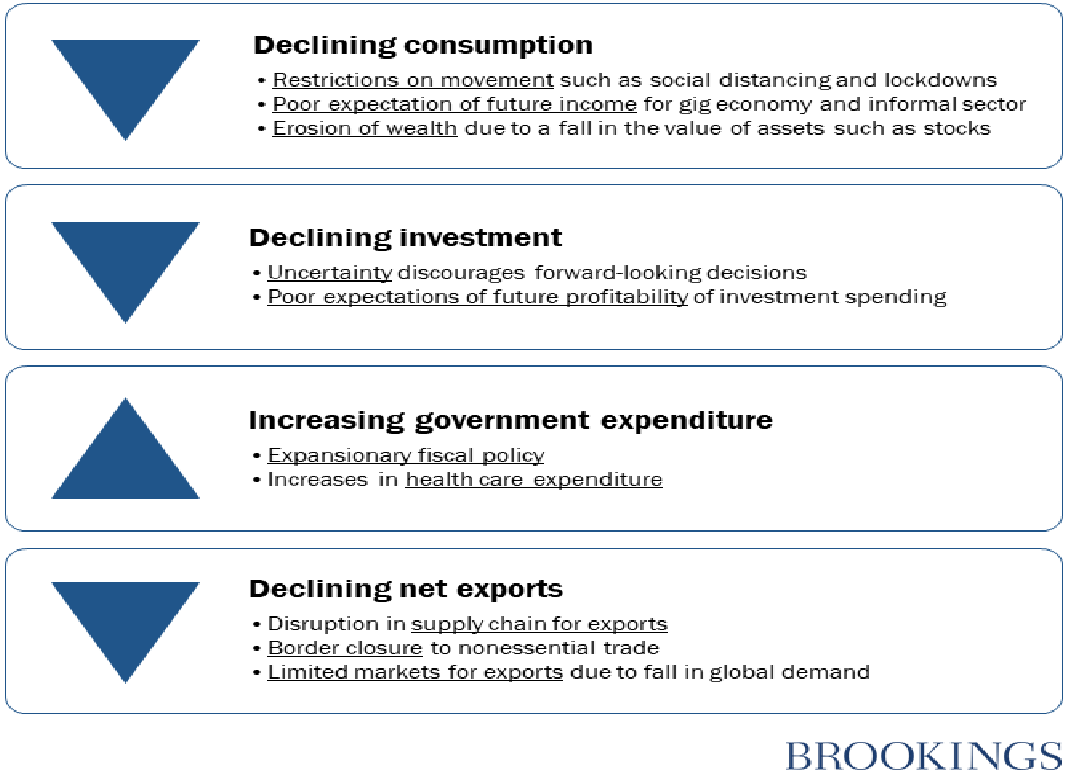
2021 National Budget – The enactment of the budget on 31 December 2020 allowed for increase in effectiveness and efficiency in the implementation of the budget.

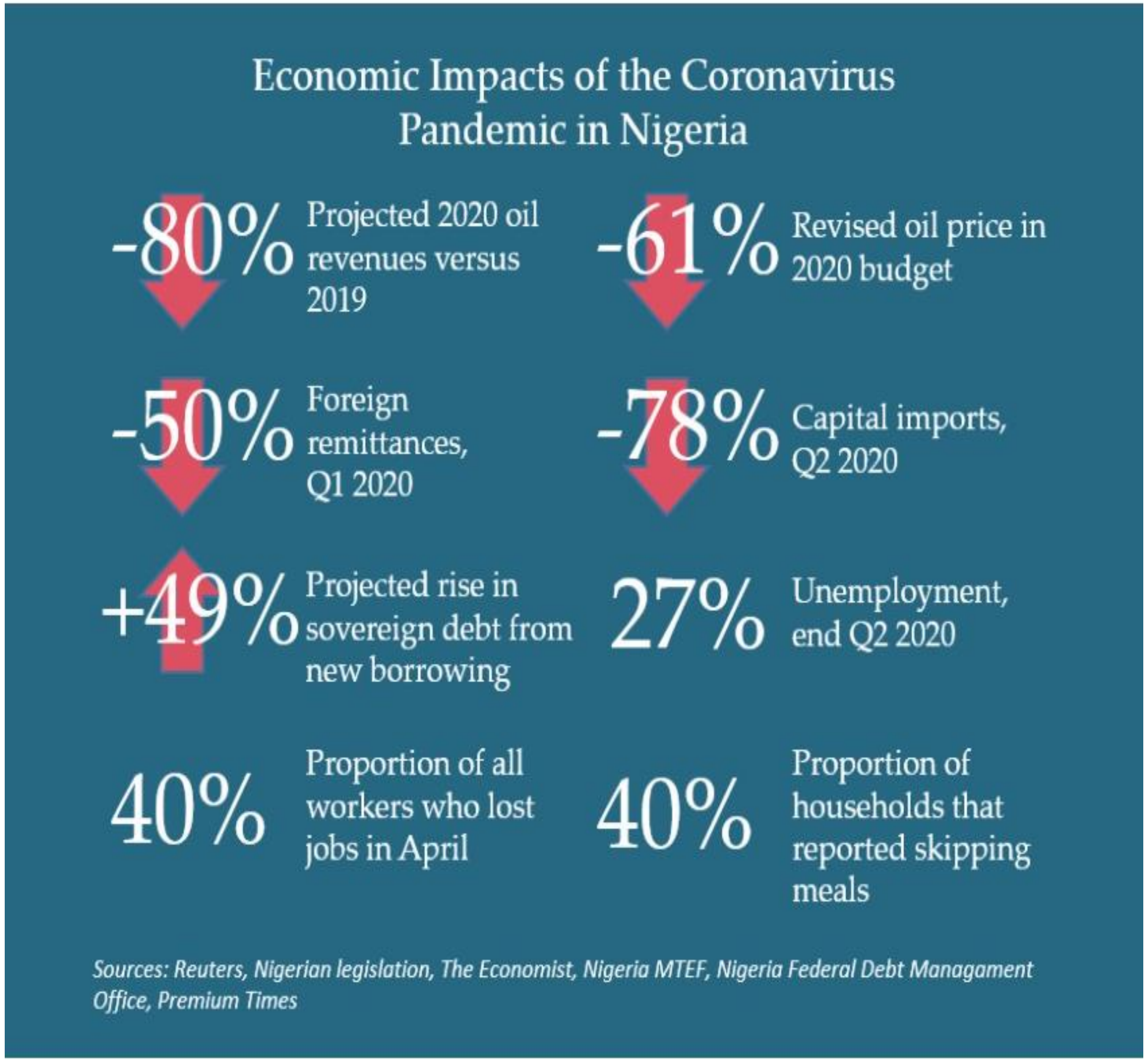
GDP – The economy exited recession in Q4 2020 and achieved a year on year GDP increase of 5% in Q2 2021 due to the base effect.

The Pandemic has increased the need for government revenue due to expansionary fiscal policy

COVID-19 negatively affected the economy of many countries, especially developing countries. According to Brookings, COVID-19 affected aggregate demand through-

Figure 1. How the COVID-19 pandemic affects the components of aggregate demand





The Nigerian economy – Major economic indicators

Investment

Total investment into Nigeria remains low.

Investment inflows was $875m in Q2 2021 which is the lowest quarterly inflow since Q1 2016

Trade Balance

Nigeria's trade deficit position in Q2 improved significantly.

The value of imports declined by 1.5% year on year, exports increased by 75%

Exchange Rate

Increased supply gap in the foreign exchange market.

It is expected that this will continue given the high demand including backlogs and weak foreign investment inflows

Employment

Growing labour force (estimated 69.7m) with 33% unemployed and 22.8% underemployed.

This has quadrupled over the last five years given two recessions

Key issues

Inflations remains high at 16.63%

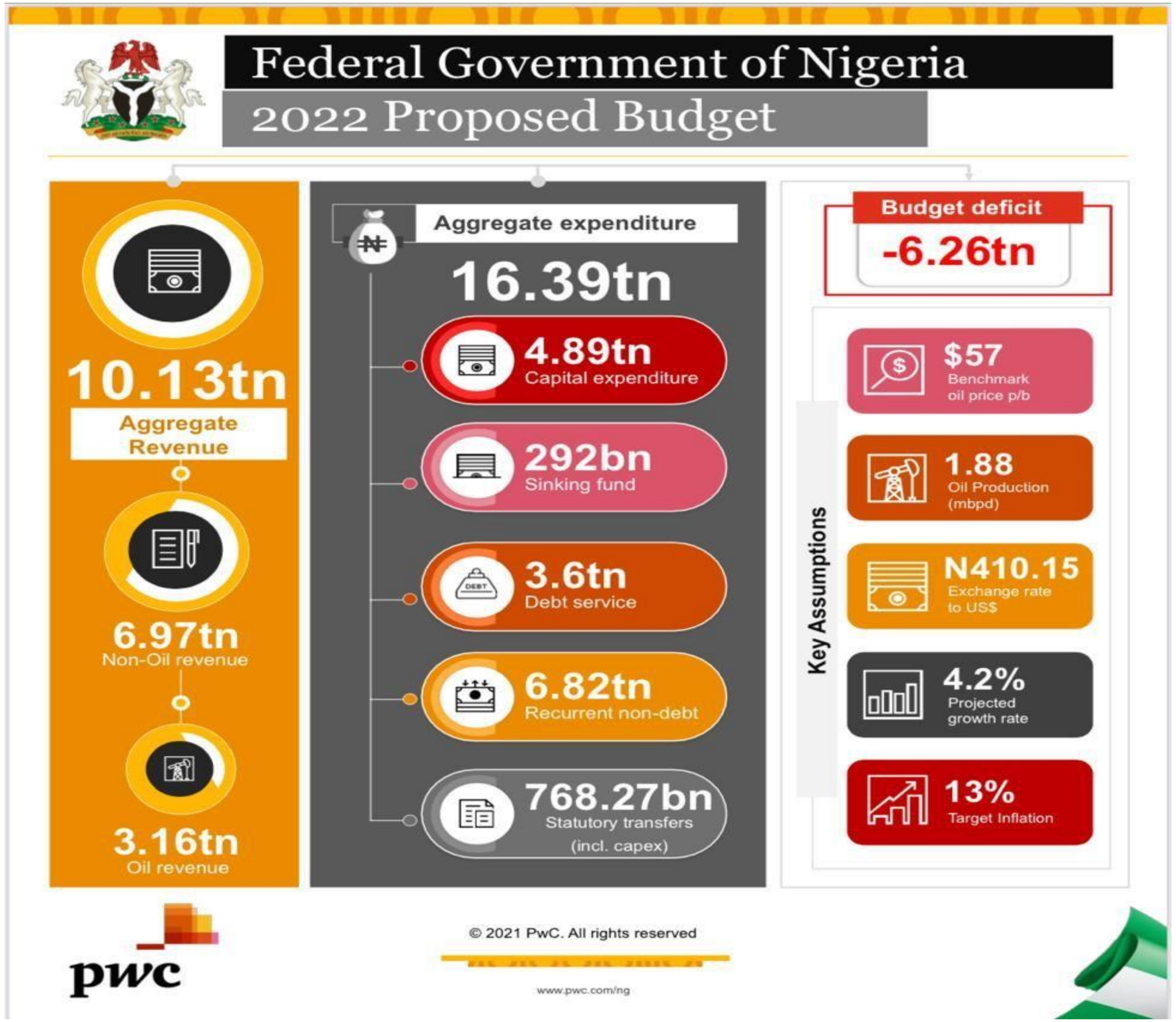
High debt to revenue ratio

Inadequate infrastructure

Insecurity

Tough business climate

The expansionary fiscal policy of the Nigerian government

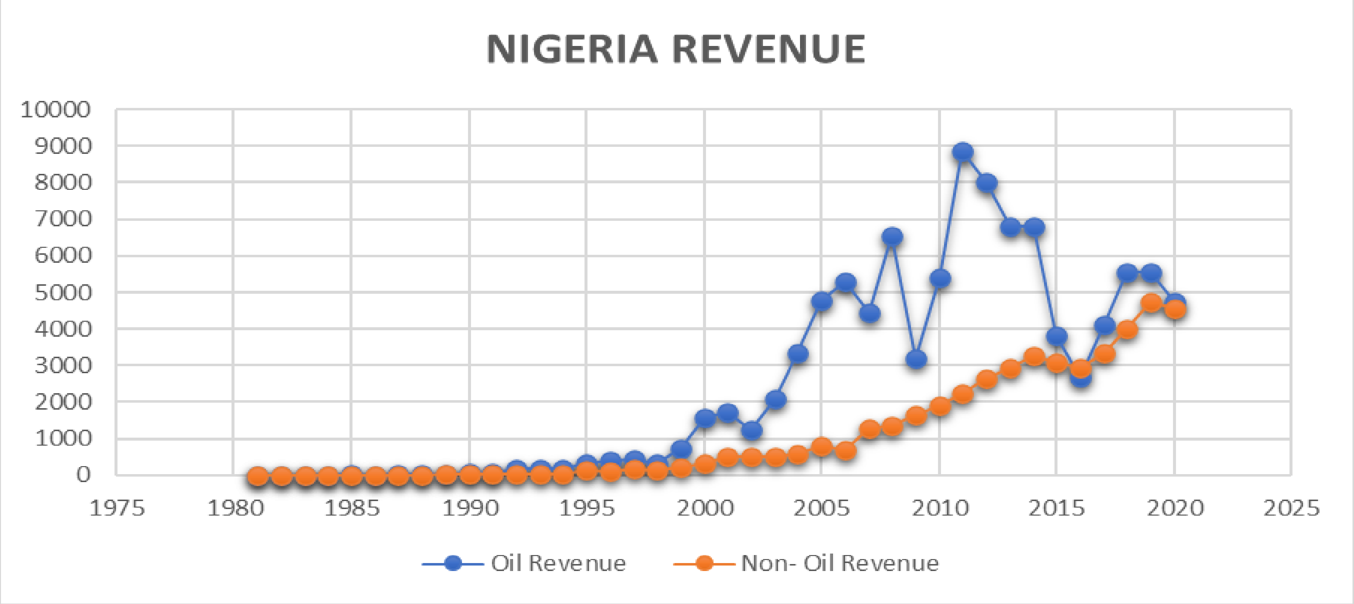


- The 2022 budget has a deficit of about N6.26tn, approximately 3.39% of GDP.
- Non-debt recurrent expenditure of N6.82tn is the largest expense item, with 60%relating to personnel costs at N4.11tn.
- The capital expenditure budget of N4.89tn represents an increase of 18% compared to 2021, and about 30% of total 2022 expenditure.
- Debt service expenditure is estimated at N3.6tn, representing about 35.6% of the projected revenue for the year.
- The President highlighted that the loans would be directed at financing critical development projects and programmes and highlighted plans to grow the revenue-to-GDP ratio from currently about 8%, to 15% by 2025.

The Petroleum Industry and the Nigerian economy

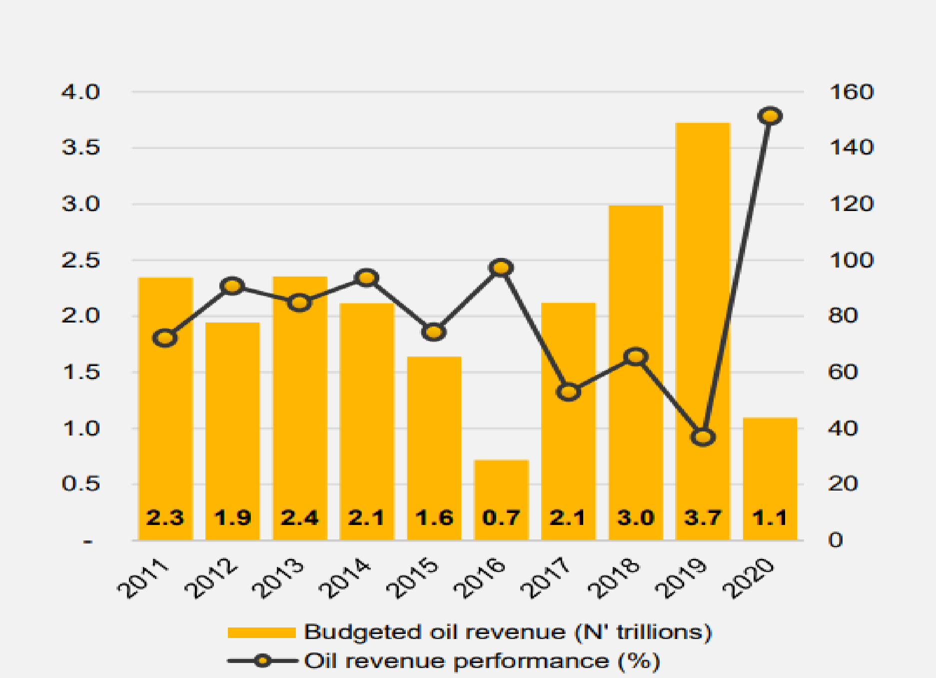
02

The Petroleum sector has accounted for majority of the Government's revenue



The sector contributes 65% of the government revenue which rises to over 90% where gas revenue is included.

Nigeria's oil revenue performance over the past 10 years



Source: Federal Ministry of Finance, Budget and National Planning (FMFBNP), Budget Office of the Federation, PwC analysis

Historically, oil revenue has had mixed performances compared to budget.

The Petroleum sector drives government policy more than any other industry

"The sector contributes over 85% of foreign exchange earnings and over 65% of government revenue. This is close to 90% if gas is included. "

Despite large Government interest, investment in the sector has been private sector led despite uncertain tax and regulatory environment.

The sector attracted 4% of the $70bn investment in Africa. Lost $50bn in investment over the past 10 years

Nigeria is the largest crude producer and has the largest proven crude oil reserves in Africa at 37 billion barrels

Largest proven reserves in Africa and 9th in the world 200 trillion tcf and 600 trillion tcf of gas reserves. Majority are unproven

NNPC is the largest player in the market i.e largest producer of petroleum, only importer of PMS, import 60% of AGO. Negligible offshore investment

Nigeria does not control the price and in recent times does not control production.

The sector is connected to the 3 subsidies we have in Nigeria i.e PMS, electricity and foreign exchange

Landmark Projects i.e NLNG, Dangote Refinery, Dangote Fertilizer

Government has gained revenue from this sector through taxes and levies

S/N	Taxes and Levies
1	Petroleum Profit Tax
2	Oil Royalty
3	Gas Royalty
4	Gas Flare Penalty
5	Concession Rentals
6	Company Income Tax (Gas)
7	Capital Gains Tax
8	Education Tax
9	Niger-Delta Development Commission (NDDC) Levy
10	NCDMB (Nigerian Content Development Fund) Levy
11	Ness (Nigerian Export Supervision Scheme) Fee
12	Value Added Tax (VAT)
13	Withholding Tax (WHT)
14	Pay As You Earn (PAYE)

S/N	Taxes and Levies
15	Government Signature Bonus
16	License Renewal Payments

The Petroleum Industry Act 2021 introduces more levies


The Petroleum Industry Act 2021
03

A fiscal framework that expands the revenue base of the FGN, while ensuring a fair return for investors;

The PIA has several objectives. This includes the Expansion of Government revenue whilst encouraging investments. This is evident from the objectives listed under Chapter 4.

Petroleum Industry Fiscal Framework

- Establish a progressive fiscal framework that encourages investment in the Nigerian Petroleum Industry, balancing rewards with risk and enhancing rewards to the Federal Government of Nigeria (FGN);
- Provide a forward-looking fiscal framework that is based on core principles of clarity, dynamism, and fiscal rules of general application;
- Establish a fiscal framework that expands the revenue base of the FGN, while ensuring a fair return for investors;
- Simplify the administration of petroleum tax; and
- Promote equity and transparency in the petroleum industry fiscal regime

The building blocks of the fiscal regime

Expands revenue base for government whilst ensuring fair returns

Grandfathering provisions

- Existing operators have the option to retain existing fiscal terms or convert prior to renewal save for marginal field operators;
- Producing marginal operators will maintain existing farm-out agreements and royalty rates;
- The conversion process will include termination clause for court/arbitration cases, relinquishment of acreages, loss of fiscal stability clauses and Investment tax credits and Investment tax allowance;

Dual Tax System

- The profits of upstream companies will be taxed under the provisions of the PIA and the Companies Income Tax Act.
- This could lead to a lot more tax disputes if the application of both laws are managed properly by taxpayers and the tax authority.
- Limitation on cost deductions i.e Cost Price Ratio, interest, bank and finance charges etc
- Timelines for filings remain the same with the old regime

Introduction of levies and funds

- 0.5% of petroleum products and natural gas sold in Nigeria to fund the Midstream and Downstream Gas Infrastructure Fund
- 0.5% of petroleum products sold in Nigeria to fund the Midstream and Downstream Petroleum Regulatory Authority
- 3% of prior year operating expenditure to the Host Community Trust Fund.
- Environmental Remediation Fund – basis of assessment is to be determined

Reduction of tax & royalty rates

- Reduction in the headline rate from 85% to 60% (HCT 30% & CIT 30%)
- HCT will not apply to deep offshore investments.HCT at 15% will apply to marginal field operators
- Royalty will be high in a higher price climate and low in a lower price climate. However the highest standard royalty rate has been reduced from 20% to 15%.
- Expansion of the gas utilisation regime to include midstream gas operations and large scale gas based industries.

Alignment with the National Tax Policy for Sustainable growth and development

Host Community Trust Fund to promote harmonious relationship between Operators and Host communities

Gas incentives to promote utilisation and infrastructure development e.g gas pipeline up to 10 years tax holiday

Midstream and Gas infrastructure fund to develop gas projects for private sector investment and promote elimination of gas flaring

Non-applicability of HCT to promote deep water upstream investments

The PIA through the lens of a tax practitioners (1 of 2)

1 PIA Assessment- Qualitative analysis of current situation vs future prospects

2 Scenario Simulation-

- Conversion within the 18 months window
- Licence renewal
- Contributions to the funds

3 Conversion Contract-

- Tax clauses
- Termination clause i.e Court/Arbitration cases
- Engagement with the stakeholders

4 Business Restructurings

- Segregation of Upstream, Midstream and Downstream into separate entities
- Incorporated Joint Venture

5 Structuring-

- Holding
- Financing and
- Operating
- Engaging the tax authorities

6 Financial Reporting

- New tax rates & deferred tax balances
- Business combinations
- Effective tax reconciliations
- IFRIC 21

The PIA through the lens of a tax practitioners (2 of 2)

7 Tax Computation-

- Taxable profit differences for HCT & CIT
- Estimated tax returns
- Automation of computations

8 Royalty Calculation

- Royalty on volume
- Royalty on price
- Reconciliation with the Nigerian Petroleum Upstream Commission

9 Tax Advisory-

- Gas utilisation incentive
- Impact on ongoing acquisition transactions
- VAT Modification Order 2021

10 Minimum Tax

Reduction of the minimum tax rate on Midstream/Downstream operations.

The fiscal environment will be dynamic in the near future

What should be done now

01

Continue to Upskill and stay abreast of development i.e Regulations are expected

02

Impact assessment of the PIA on the business or potential transactions

03

Consideration of financial reporting requirements i.e IFRIC 21

04

Consider automation of processes given the ease of compliance in a dynamic environment

Implementation of the PIA

04

Transition is moving faster than the timelines in the PIA

What to action now

6 months
Incorporation and determination of assets interest and liabilities of NNPC to be transferred to NNPC Limited. This includes existing arrangements involving the NNPC/its subsidiaries

>>>>>
Carry out an impact assessment of the PIA. This will analyse the impact of the PIA on the valuation of the Oil Assets, considerations for conversion, Incorporated Joint Venture etc

12 months
Provide to the Upstream commission all licence/lease agreements including amendments. Set up the Host Communities Development Trust (HCDT) and Submit Decommissioning, abandonment and Environmental management plans

What to keep in mind for near term

12 months
Transfer of existing host communities development projects to the HCDT. Submit gas flare elimination and monetisation plan

18 months
Midstream and Downstream licence holders are to reapply for a new licence. Producing marginal fields will convert. Timeframe for executing the conversion contract

What to expect in the coming months

18 Months
Transfer of determined assets, interest and liabilities to the NNPC Limited

Going forward
Activities of the implementation committee, commission and Authority including regulations to be issued to implement the provisions of the PIA.

Transition pitfalls

Lack of a robust and coordinated implementation plan

Poor stakeholder involvement, sensitivity and lack of a clear strategy for public communication

Lack of capabilities within the institutions and excessive political interference

Delay in issuing Regulations and Guidelines pursuant to the PIA

Thank You!