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INFORMATION CIRCULAR

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Subject: CLARIFICATION ON TAXATION OF PRODUCTION SHARING CONTRACT (PSC) AND INCORPORATED JOINT VENTURE COMPANIES (IJVC) OPERATIONS UNDER THE PETROLEUM INDUSTRY ACT

This information circular is issued in line with Section 8 of the Federal Inland Revenue Service (Establishment) Act, 2007 (as amended), Section 304(1) of the Petroleum Industry Act, 2021 and other relevant tax laws for the information and guidance of the general public, taxpayers, tax officials, and tax practitioners on the provisions of Petroleum Industry Act, 2021. This circular should be read and applied together with other related circulars issued by the Service pursuant to the Petroleum Industry Act.

1.0 Introduction

The Petroleum Industry Act (the Act) requires that all companies in the petroleum industry eventually transit to the full provisions of the Act. This requirement raises conversion, transition, compliance, sundry issues and related matters.

2.0 Scope

This information circular aims at providing clarification on issues relating to the taxation of Production Sharing Contracts (PSC) and Incorporated Joint Venture Companies (IJVCs) Operations under the Petroleum Industry Act and provide direction on related matters.

3.0 Taxation of Model Production Sharing Contract

The revenue and costs of transited companies in production sharing contracts and those who enter into production sharing contract under the Act are to be determined for tax as below:

3.1 Rules for determination of Revenue and Costs chargeable to tax under a PSC

The basis of determination of cost and revenue for tax purposes for each of the contractors in the PSCs will be as follows:

a. Revenue

- i. Contractors (Companies) in PSCs** - The value of crude oil/gas lifted in the ratio of their working interest will be fiscalised for each of the contractors.
- ii. NNPC Limited and Holder of licence/lease** - The value of crude oil/gas lifted for royalty and the proportion of its profit oil/gas will be fiscalised.

b. Cost

- i. Contractors (Companies) in PSCs** - The costs incurred in the proportion of their working interest ratio and other sole costs will be deductible for the purpose of determining the assessable tax. Royalty is not claimable except if it is incurred from other PMLs that is not in PSC's.
- ii. NNPC Limited and Holder of licence/leases** - The recovery value of royalty oil lifted and other incurred sole costs. Also, royalties and the value of profit oil delivered in kind or cash from all fields to the Federation Account shall be deductible for the purposes of determining the assessable tax.

3.2 Returns Filing

Each company having interest in the PML is liable to file its tax returns with the Service and will be responsible for the Companies Income Tax liability and other relevant taxes.

3.3 Agent of Collection Role

The obligation for the deduction of all transaction taxes on the operations of a Licence or Lease is that of the company making payments to vendors.

3.4 Tax payable on Deep Offshore Production Sharing Contract

Companies Income Tax to be consolidated across terrain at 30% tax rate

3.5 Tax payable on Onshore and Shallow Water Production Sharing Contract

- a. Hydrocarbon Tax at 30% for PMLs
- b. Hydrocarbon Tax at 15% for PPLs
- c. Companies Income Tax at 30% to be consolidated across terrain and licences/leases.

4.0 ILLUSTRATIONS

4.1 Illustration 1: Single Contractor in a PML PSC for Onshore/Shallow Water

WYZ Ltd, the concessionaire of **PML OK1** is engaged in Production Sharing Contracts with Alpha Ltd-the contractor in the Onshore and Shallow water

terrain. The participating interest of the parties are 75% Alpha Ltd and 25% WYZ Ltd.

Extracted below are data of the PSCs for 20XX accounting period.

DESCRIPTION	DATA	WYZ LTD	APLHA LTD
Total Production	120,000/BBL		
Price/bbl	USD10		
Royalty Rate	10%		
Tax Rates	HT-30%, CIT-30%		
Costs:			
Opex	USD225,000		
Capital Allowance	USD75,000		
Production Allowances	USD 240,000		
Sole Costs:		USD20,000	USD30,000
Participating Interest/ Profit Ratio		25%	75%
Total Profit	USD730,000	USD182,500	USD547,500

Required: Show how revenue, costs and capital allowance will be claimable by parties and compute:

- Hydrocarbon Tax payable by WYZ LTD & APLHA LTD
- Companies Income Tax payable by WYZ LTD & APLHA LTD using same data.

TREATMENT-1

COMPUTATION OF HYDROCARBON TAX FOR 20XX ACCOUNTING PERIOD

DESCRIPTION	ALPHA LTD (CONTRACTOR)	WYZ LTD (CONCESSIONAIRE)	Total-PML OK1
	USD	USD	USD
Revenue	877,500	322,500	1,200,000
Less: Royalty	-	120,000	120,000
Opex	225,000	-	225,000
Sole Costs	30,000	20,000	50,000
Assesable Profit	622,500	182,500	805,000
Production Allowances	175,500	64,500	240,000
Capital Allowances	75,000	-	75,000
Chargeable Profit	372,000	118,000	490,000
Hydrocarbon Tax @30%	<u>111,600</u>	<u>35,400</u>	<u>147,000</u>

COMPUTATION OF COMPANIES INCOME TAX FOR 20XX ACCOUNTING PERIOD

DESCRIPTION	ALPHA LTD (CONTRACTOR)	WYZ LTD (CONCESSIONAIRE)	Total-PML 00X
	USD	USD	USD
Revenue	877,500	322,500	1,200,000
Less: Royalty	-	120,000	120,000
Opex	225,000	-	225,000
Sole Costs	30,000	20,000	50,000
Assesable Profit	622,500	182,500	805,000
Capital Allowances	75,000	-	75,000
Total Profit	547,500	182,500	730,000
Companies Income Tax @30%	<u>164,250</u>	<u>54,750</u>	<u>219,000</u>
Education Tax @ 2.5% of Assessable Profit	<u>15,562.50</u>	<u>4,562.50</u>	<u>20,125</u>

SUMMARY OF TAXES PAYABLE BY PARTIES IN PML OK1

SUMMARY OF TAXES PAYABLE BY PARTIES		
DESCRIPTION	ALPHA LTD	WYZ LTD
	USD	USD
Hydrocarbon Tax	111,600	35,400
Companies Income Tax	164,250	54,750
Education Tax	15,563	4,563
Total Taxes Payable	<u>291,413</u>	<u>94,713</u>

4.2 Illustration 2: More than one Contractor in a Deep offshore water PSC for a single PML

Alpha Ltd and Beta Ltd are into Production Sharing Contract with WYZ Ltd the concessionaire of **PML OK2** in the deep offshore terrain. Assume the PSC is funded by Alpha and Beta at a working interest ratio of 80% and 20%.

DESCRIPTION	DATA	WYZ LTD	BETA LTD	APLHA LTD
Total Production	100,000/BBL			
Price/bbl	USD20			
Royalty Rate	10%			
Tax Rates	CIT-30%			
Costs:				
Opex	USD300,000			
Capital Allowance	USD150,000			
Production Allowances	USD 250,000			
Sole Costs:	USD 135,000	USD40,000	USD50,000	USD45,000
Participating Interest/ Profit Ratio		20%	18%	62%
Total Profit	USD1,215,000	USD243,000	USD218,700	USD753,300

Extracted below are data of the PSCs for 20XX accounting period.

Required: Compute the taxes payable by each of the parties in the **PML OK2** for 20XX Accounting period.

TREATMENT-2

COMPUTATION OF COMPANIES INCOME TAX FOR 20XX ACCOUNTING PERIOD

DESCRIPTION	ALPHA LTD (CONTRACTOR) USD	BETA LTD (CONTRACTOR) USD	WYZ LTD (CONCESSIONAIRE) USD	TOTAL-PML OK2 USD
Revenue	1,158,300	358,700	483,000	2,000,000
Less: Royalty	-	-	200,000	200,000
Opex	240,000	60,000	-	300,000
Sole Costs	45,000	50,000	40,000	50,000
Assesable Profit	873,300	248,700	243,000	1,450,000
Capital Allowances	120,000	30,000	-	150,000
Total Profit	753,300	218,700	243,000	1,215,000
Companies Income Tax @30%	225,990	65,610	72,900	364,500
Education Tax @ 2.5% of Assessable Profit	21,833	6,218	6,075	34,125

SUMMARY OF TAXES PAYABLE BY PARTIES			
DESCRIPTION	ALPHA LTD USD	BETA LTD USD	WYZ LTD USD
Companies Income Tax	225,990	65,610	72,900
Education Tax	21,833	6,218	6,075
Total Taxes Payable	247,823	71,828	78,975

5.0 Taxation of a Company under PSC in a Licence or Lease Granted under PIA and a Licence granted under Petroleum Act (PA)

Any company with an interest in Model PSC under The Act and PSC under the PPTA /DOIBPSCA shall compute its tax separately for both regimes.

Cost incurred for the operation of a licence granted under the PIA shall be claimed against its revenue. Similarly, cost incurred for operations under the licence granted under Petroleum Act will be claimed against revenue under the PPTA/ DOIBPSCA.

Where costs are incurred jointly for more than one PSC, the cost shall be apportioned in line with FIRS information circular on *Apportionment and Consolidation of Costs and Revenue Under the Petroleum Industry Act. No 2022/22 of 12th August, 2022.*

6.0 TAX ISSUES ON IJVCs (SECTION 54, 65 & Second schedule)

6.1 IJVC Operations

All IJVCs are required to register for tax with the Service with all relevant information required of any company for the purposes of tax registration.

All IJVCs shall compute, file returns and pay appropriate taxes applicable to their relevant operations as a company. Accordingly, the respective rates for Hydrocarbon Tax and companies' income tax shall apply to IJVCs as appropriate.

6.2 Service Contractors under IJVCs

Where the Commission has approved the appointment of another company (Service Contractor) other than the IJVC to operate any of the streams of operation of the IJVCs, the IJVCs shall continue to be responsible for the computation, filing of returns and payment of taxes while the service contractor shall be responsible for its own taxes as a company.

The IJVCs shall deduct all applicable taxes from any amount paid to the Service contractors which shall include but not limited to WHT, VAT, etc and remit to the Service.

6.3 Restructuring of Existing JV to New IJVC

Assets transferred from any existing JV to IJVC would be deemed to be transferred at Tax Written Down Value (TWDV) for the purpose of capital allowance, while subsequent merger, take over, or restructuring shall be treated in line with the provisions of Section 271 of PIA and other extant laws.

7.0 Applicable Tax Rate

The applicable income tax and Hydrocarbon Tax rate for PSCs (Deep Offshore, Onshore and Shallow Waters) as well as IJVCs shall be as stipulated in the table below.

Rates for Hydrocarbon Tax (HT) and Companies Income Tax (CIT)

S/N	Description	Area of Operations	Hydrocarbon Tax Rate	Companies Income Tax Rate
1	Oil Mining Lease (OML) converted to Petroleum Prospecting Licence (PPL)	Onshore and Shallow water	15%	30%
2	Oil Prospecting Licence (OPL) converted to Petroleum Prospecting Licence (PPL)	Onshore and Shallow water	15%	30%

3	Frontier acreages reclassified into Petroleum Prospecting Licence (PPL)	Onshore and Shallow water	15%	30%
4	Oil Mining Lease (OML) converted to Petroleum Mining Lease (PML)	Onshore and Shallow water	30%	30%
5	Oil Prospecting Licence (OPL) converted to Petroleum Mining Lease (PML)	Onshore and Shallow water	30%	30%
6	Frontier acreages reclassified into Petroleum Mining Lease (PML)	Onshore and Shallow water	30%	30%
7	Licences or leases in the Deep Offshore	Deep offshore	Not Applicable	30%
8	Unclassified Frontier Acreages	Frontier Basins	Not Applicable	30%

8.0 Amendment or Revision of the Circular

The Service may, at any time, withdraw or replace this Circular or publish an amended or updated version.

9.0 Enquiries

All Enquiries on any aspect of this publication should be directed to:

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