

Understanding Tanzania's 2014/2015 National Budget

PwC insight and analysis

Finance Act 2014 Update Oil and Gas Commentary

Our “Oil and Gas – Tax Alert” circulated in July 2014 (based on provisions of the Finance Bill) highlighted a change to extend the 5% final withholding tax regime currently applied to the mining sector to the oil and gas sector. The Finance Act 2014 reflects this same amendment. Our commentary below is an expanded version of the observations made in our earlier alert.

Amendments

The relevant amendments to the Income Tax Act (“ITA”) 2004 are as follows:

- An amendment to Section 3 (“Interpretation”) so as to expand the definition of technical services as highlighted below:

*“‘technical service’ in respect of mining, **oil and gas** operations, means services in respect of earthmoving, engineering and construction and includes geological, geotechnical and metallurgical services, **seismic survey, data interpretation, drilling or any like such services**”*

- An amendment to Section 83(1)(a) (which imposes the resident withholding tax obligation on payments of technical services and management fees) to extend its application to the oil and gas sector, as a consequence of the amendments highlighted below:

*“a resident person who is conducting **mining** business **of extractive industry in mining, oil or gas** pays a service fee to another resident person in respect of management or technical services provided wholly and exclusively for the business”*

Final withholding payment

Section 86(1)(d) ITA 2004 (“Final Withholding Payment”) provides that “service fees paid to a resident person that are subject to withholding under section 83(1)(a)” are a final withholding payment. In other words, the basis for taxation for entities receiving such a payment is 5% of turnover (not 30% of profit), with the liability settled by way of withholding.

Interpretation

Whilst the change may be seen as a simple and practical way to ensure tax collection from entities whose presence on the ground is often not a particularly long term one, there are areas where further clarification on interpretation will be required:

- Scope of services covered: More clarification may be required as to the precise nature of the services that qualify as either “technical” or “management” – particularly, the latter term which is a rather general term and for which no separate definition has been provided.
- Scope of withholders covered: There is the possibility for confusion as to whether the obligation to withhold extends to entities other than oil and gas contractors. In particular, whilst there is a definition for “mining operations”¹ there is no definition provided for “oil and gas operations”. Our assumption is that the intention is to only cover payments made by a Contractor under a Production Sharing Agreement (rather than payments made by the sub-contractors working for the contractor, or by entities in the downstream oil and gas sector), but this point is not spelt out. In practice this point may be more of a concern in relation to payments for “management services” rather than “technical services” (which as defined would normally be paid by the contractor).
- Allocation and transitional issues: Where an entity provides relevant services subject to the 5% final withholding tax regime, as well as other services taxable under the normal regime, an issue that arises is the allocation of an entity’s profit between the different services. A similar issue

relates to the transitional period and in particular the allocation before/after 30 June.

Other issues

We also note that the change has not been accompanied by any adjustment to the high withholding rate (15%) applied on services supplied by non-residents – a matter of significant concern to the oil and gas sector.

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¹ “mining operations” means prospecting mining or operations connected with prospecting or mining carried out pursuant to rights granted under the Mining Act, 1998;