PETROLEUM FISCAL REGIME – MALAYSIA'S EXPERIENCE

SYAKIRAH BT MD. NOR
MINISTRY OF FINANCE MALAYSIA

12 AUGUST 2015

AN OVERVIEW OF PETROLEUM ACTIVITIES IN MALAYSIA

- First commercial exploitation of crude oil began in MIRI, Sarawak in the year 1910 by Shell. Oil Production of this well lasted till 1972.
- The offshore petroleum activities in Peninsula Malaysia began in 1954 by Exxon. Commercial exploitation only began in 1964.
- Malaysia began to export crude oil from Peninsula Malaysia in the year 1974.
- The main exploration and production activities took place in the broad continental shelf offshore of the states of Sabah and Sarawak in East Malaysia, and offshore Terengganu.

AN OVERVIEW OF PETROLEUM ACTIVITIES IN MALAYSIA

Petroleum Operations in Malaysia:

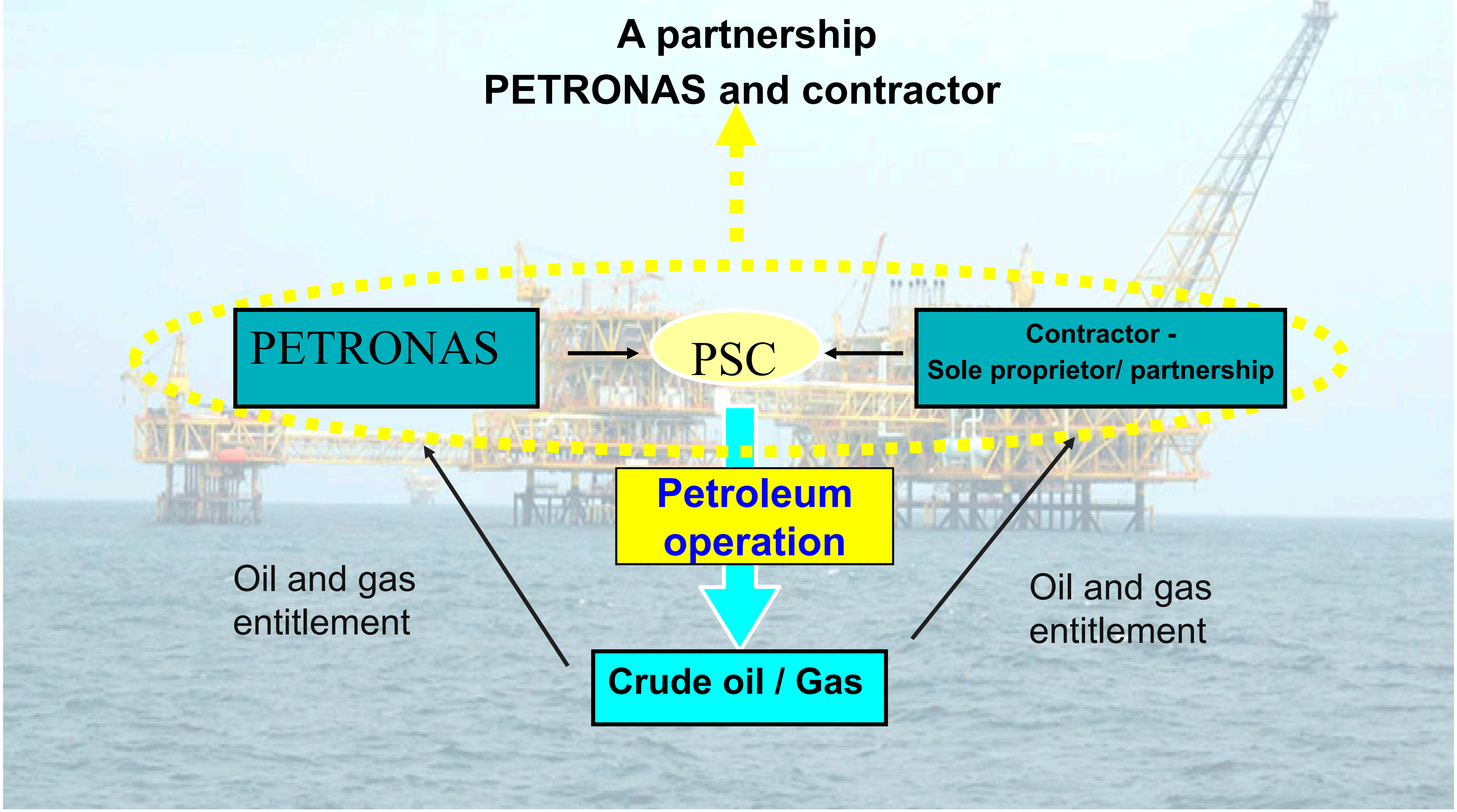
- Concession System - The State Authority awarded to companies with expertise such as Shell and Esso.
- Production Sharing Contract (PSC) - exploration, development and production of crude oil and natural gas activities are undertaken and managed through Production Sharing Contracts (PSC) with PETRONAS.

AN OVERVIEW OF PETROLEUM ACTIVITIES IN MALAYSIA

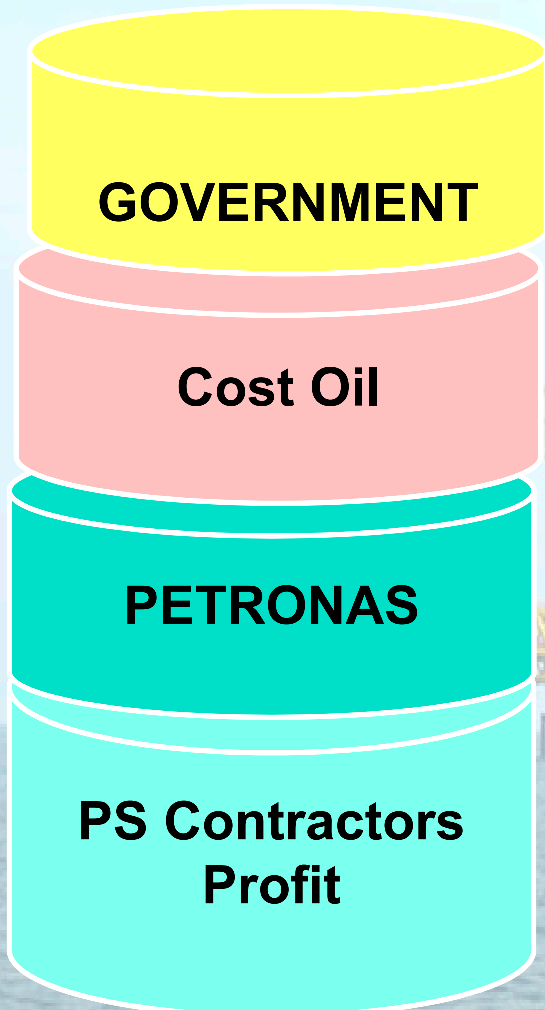
- Malaysian Government enacted the Petroleum Development Act in 1974 (PDA), and established its national oil company, PETRONAS.
- PETRONAS has exclusive ownership right to the oil and gas resources in Malaysia, and makes it the main regulatory body for upstream oil and gas activities.
- Upstream activities, which are exploration, development and production of resources, are carried out through the production sharing contract (PSC).

- The promulgation of the PDA in 1974 is to ensure that the nation's petroleum resources could be developed in line with the needs and aspirations of the nation.
- The Act vests the entire ownership and control of petroleum resources in PETRONAS.
- The upstream activities are subjected under the "Production Sharing Contract" (PSC) agreement with PETRONAS.
- PERTONAS is actively engaged in the exploration, development and production of crude oil and natural gas both at home and abroad.
- At the same time managing the upstream activities through Production Sharing Contract (PSC) - 1 April 1975

PETROLEUM OPERATIONS IN MALAYSIA IS A JOINT VENTURE ACTIVITY BETWEEN PETRONAS AND CONTRACTORS



PRODUCTION SHARING CONTRACTOR ENTITLEMENT



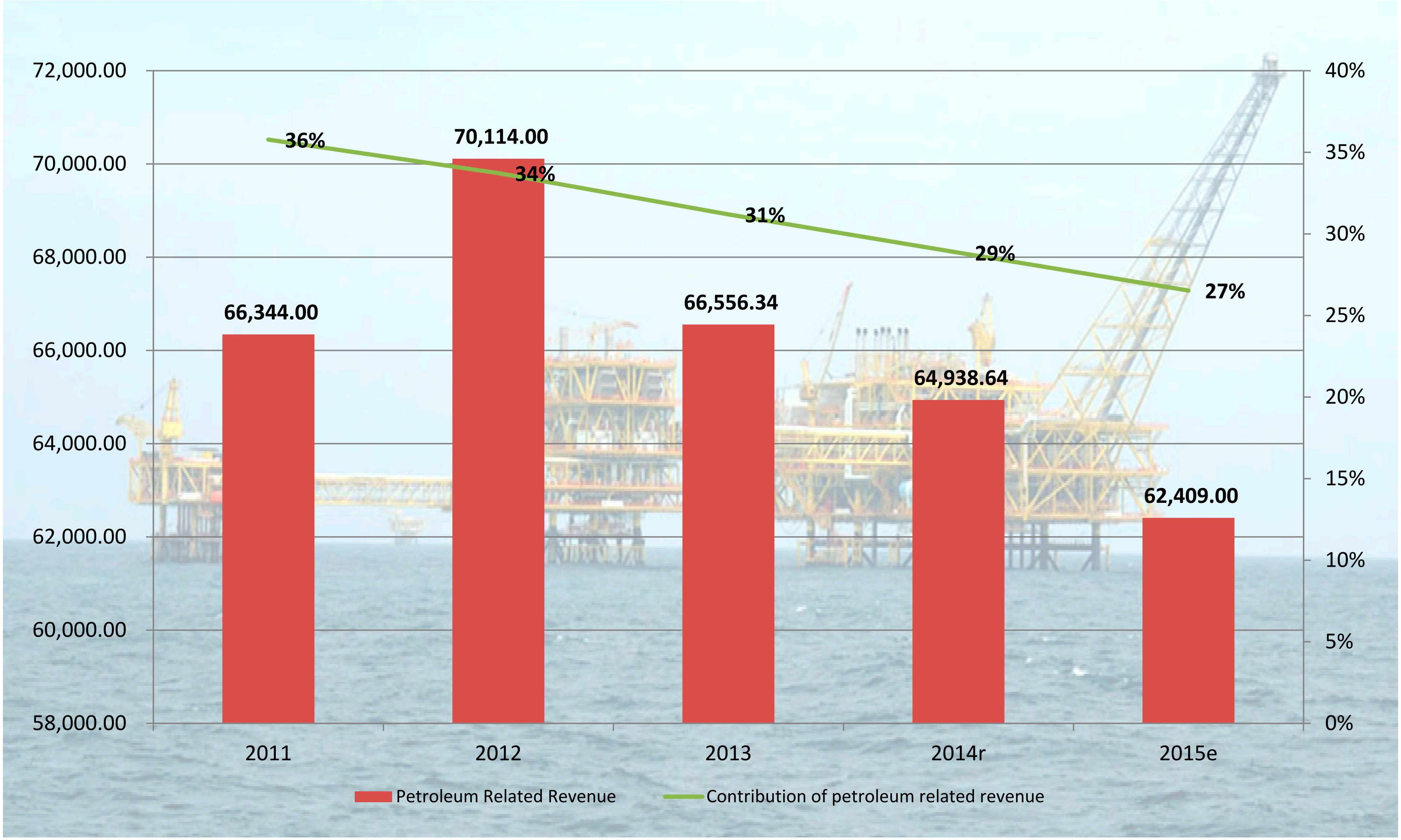
Government take

- Royalty
- Taxes From PETRONAS and PSC
- Dividend from PETRONAS

PSC

- Petronas Carigali Sdn. Bhd.
- International Oil Company

REVENUE CONTRIBUTION ON PETROLEUM



PETROLEUM INDUSTRIES MAIN SECTOR

PETROLEUM (INCOME TAX) ACT 1967

Point of sale or Export

INCOME TAX ACT 1967

Upstream

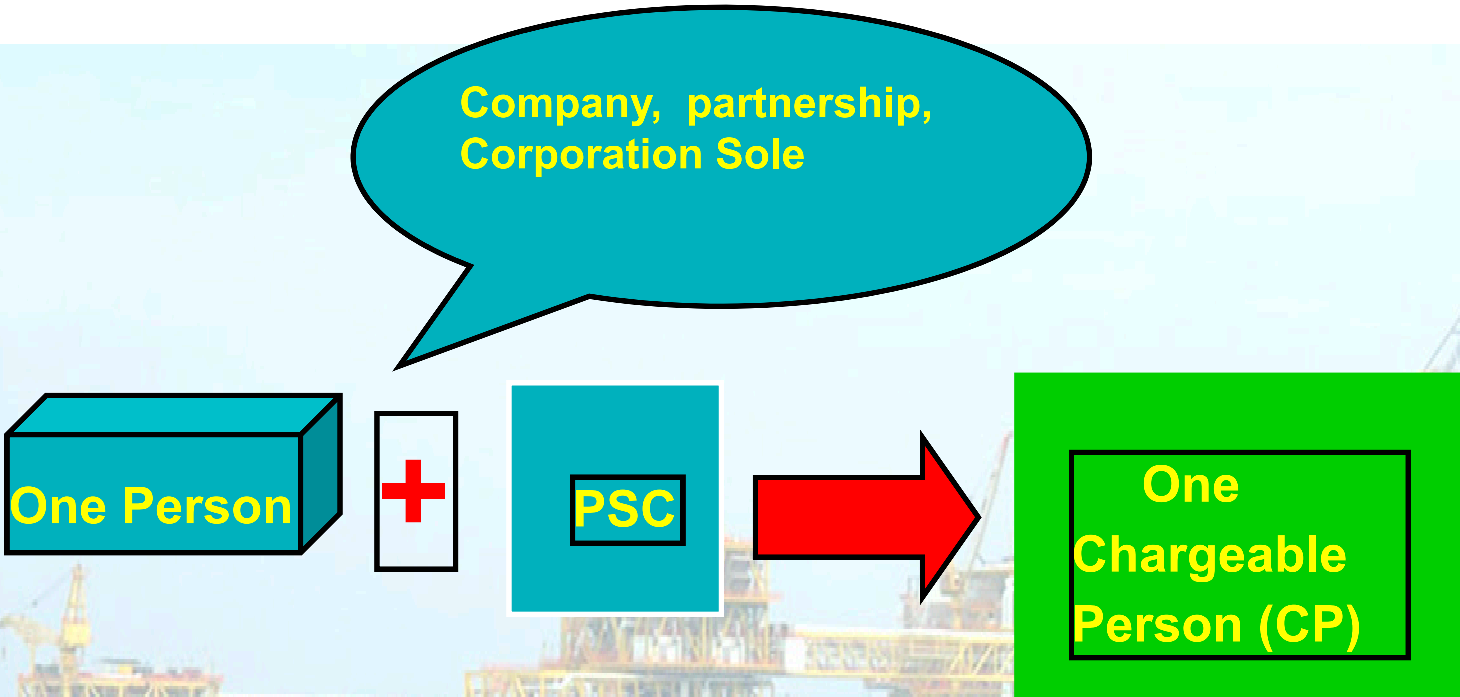
Downstream

"CHARGEABLE PERSON" UNDER PETROLEUM INCOME TAX (PITA)

Petroleum Agreement	→	Production Sharing Contract (PSC)
(PITA)		(Petroleum Industry)

- Any person carrying on petroleum operation under a petroleum agreement with PETRONAS or Malaysia Thailand Joint Authority (MTJA)
- Different "chargeable person" for each petroleum agreement.

Ring-Fencing concept



where a person other than PETRONAS or MTJA carries on petroleum operations under more than one petroleum agreement, he shall be regarded as a separate chargeable person in respect of each of those agreements

PETROLEUM INCOME TAX RATE IN MALAYSIA

Assessment Year 1976 – 1993	45%
Assessment Year 1994 – 1997	40%
Assessment Year 1998 & current	38%

Joint Development Area (JDA)-Malaysia/Thailand

First 8 years of petroleum production	0%
Next 7 years of petroleum production	10%
Subsequent years	20%

PETROLEUM INCOME TAX COMPUTATION

Sale of crude oil and gas	X	
Crude oil/gas delivered to refinery	X	
Miscellaneous receipts	X	X
Total Income		X

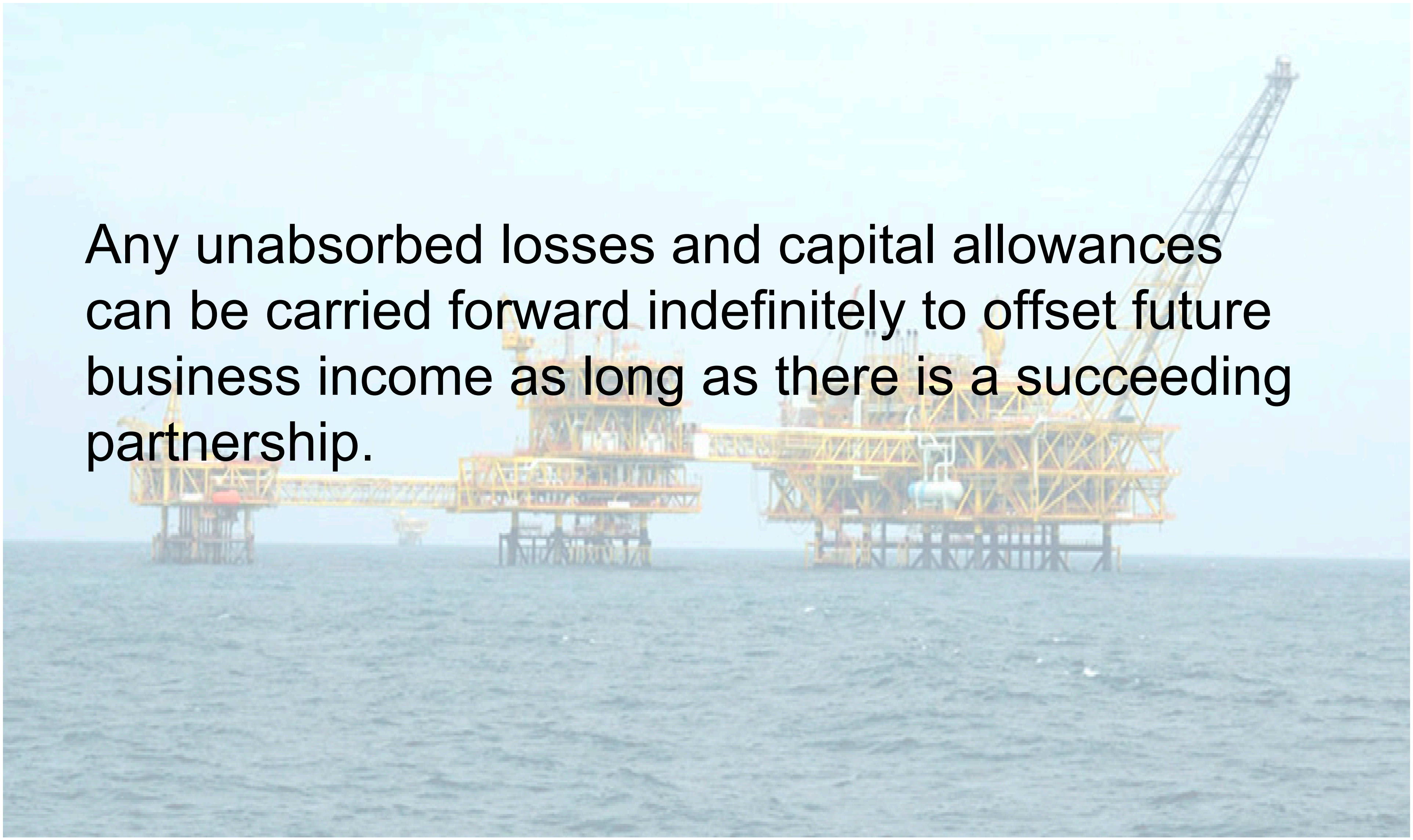
(-)	**Allowable deductions**		
	Outgoings and expenses wholly and exclusively incurred during that period in the production of the gross income Interest on loans Specific expenses • Bad debts written off • Contributions to approved fund (limited to 19%) • Intangible drilling expenses (on exploration, appraisal and development wells) • Qualifying Exploration Expenditure (Schedule 1) • Royalty payments under Petroleum Development Act • Equipment for disabled person • Expenditure incurred on services, public amenities and contributions to a charity or community project approved by the Minister • Maintenance of a child care centre • Managing a musical or cultural group • Sponsoring any arts and cultural activity • Scholarship provision • Expenditure of obtaining certification for recognized quality systems and standard • Provision of practical training • Deductions on expenditure determined by Minister of Finance • [Research Cess] • [Abandonement Cess] • Double Deductions [Insurance premium for exporters]	x x x x x x x x x x x x x x x x x x x x x x	x
	Adjusted Income		x

	Adjusted Income c/f		X
(+)	Balancing Allowance Schedule 2	x	
(-)	Capital Allowance Schedule 2	x	x
	Statutory Income		X
(-)	Loss b/f		x
			X
(-)	ƒ Approved donations ƒ Gift of artifact, manuscript or painting to the Government ƒ Gift of money or contribution in kind for the provision of facilities in public places for the benefit of disabled persons ƒ Gift of money or the cost or value of medical equipment to any healthcare facility certified by the Ministry of Health not exceeding RM20,000 ƒ Gift of painting to National / State Art Gallery	x x x x x x	
	CHARGEABLE INCOME		X

Non Allowable Expenses

Deductions not allowed
• Expenses not being money wholly and exclusively laid out or expanded for the purpose of producing gross income • Capital expenditure • Payment to unapproved scheme • Rent or cost of repairs not used for the purpose of petroleum operations • Depreciation • Interest, royalty, services, technical advice, rent from which tax is deductible but has not been deducted and paid to IRB. • Any amount chargeable tax payable under PITA or CITA • Rentals of motor vehicle exceeding RM 50,000 • A sum of 50% of expenses incurred in entertainment expenses • Leave passage

Unabsorbed losses and capital allowances



Any unabsorbed losses and capital allowances can be carried forward indefinitely to offset future business income as long as there is a succeeding partnership.

Capital Allowances

Qualifying plant expenditure		
	Initial Allowance	Annual Allowance
Plant		
Secondary recovery	40%	10%
Any other case	20%	8%
Fixed, offshore platform	-	10%
Environmental protection equipment and facilities	40%	20%
Computer software and hardware	20%	40%
Building		
Secondary recovery	20%	3%
Any other case	10%	3%

Qualifying exploration expenditure (QEE)

Qualifying exploration expenditure (QEE) incurred during the exploration and development period is accumulated and carried forward until the first sale of petroleum (i.e., when commercial production begins). QEE is allowed as a deduction gradually in the form of the initial allowance and annual allowances against the gross income for each year of assessment.

- Initial allowance — 10%
- Annual allowance — the greater of:

  (a) 15% of residual expenditure; or

  (b) $$\frac{\text{Output from petroleum operations for the basis period x residual expenditure}}{\text{Output from petroleum operations for the basis period + total potential future output of the petroleum operations}}$$

Other Taxes – Indirect

- Import Duty - all equipment and materials directly used in the exploration, development and production of crude oil, including condensate and gas currently benefits from import duty exemptions.
- Export Duty - Export duty at the rate of 10% applies to petroleum crude oil exported from Malaysia.
- Goods & Services Tax (GST) – Crude oil produced for domestic consumption (downstream) are subject to 6% GST.

INCENTIVE FOR PETROLEUM SECTOR

The following incentives are given to promote upstream development and boost the commercialization of hard-to-reach oil fields:

- Reduced tax rate of 25% from 38% for marginal oil fields.
- Accelerated capital allowances of up to five years for marginal oil fields.
- Waiver of export duty on oil produced from marginal fields.
- Investment allowance (IA) for capital-intensive project.
- QEE transfer between noncontiguous petroleum agreements.

INCENTIVE FOR PETROLEUM SECTOR

These incentives are given because:

- projects undertaken are in line with the Government's policy to increase petroleum production capacity in the future;
- incentive is expected to provide long-term impact directly and positively to the country's economic position;
- provision of incentives to promote and enhance the interests of oil and gas contractor to carry out exploration and production activities mainly marginal field projects and activities which require high capital expenditure;
- project carried out in compliance with the criteria established and approved by PETRONAS as required by the subsidiary legislation and guidelines

MAIN CURRENT CHALLENGES IN PETROLEUM INDUSTRY

- Enhance Oil Recovery – new approach and technical ability.
- Marginal and Matured Field Development – production is declining.
- Deepwater – technologies, product and service delivery.
- High Pressure and High Temperature – technologies and expertise.

OTHER CHALLENGES IN PETROLEUM INDUSTRY

- Price volatility – the recent decline in oil prices gave a negative impact to the revenue.
- Production – The demand and supply issue.
- Sustainability of the petroleum industry – Oil and gas are depleting resources. Issue of how to sustain, grow and diversified.
- Alternative reserve – e.g shale oil


THANK YOU