



Petroleum Tax Guide

April 2018
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Preface

The Petroleum Tax Guide, 1999 ("Guide") pertains to the Exploration and Production ("E&P") operators in the upstream sector. The endeavour was to update the Guide in a way that it becomes useful to operators operating under the extant Hydrocarbon Exploration and Licensing Policy ("HELP") which is based on the concept of revenue sharing and the erstwhile New Exploration Licensing Policy ("NELP") which is based on the concept of production sharing. Further, the Guide summarises the relevant provisions applicable to the petroleum sector under the income-tax and indirect tax laws. Implications under any other laws applicable to the petroleum sector would need to be verified independently. It also includes the provisions related to Royalty, which have been taken from the Model Revenue Sharing Agreement and Model Production Sharing Contract . These provision would need to be verified independently.

THE PETROLEUM TAX GUIDE 2018

A handbook of tax provisions and incentives for exploration and production of Petroleum¹

[A Guide which compiles the specific provisions of the laws relating to income tax, customs duty, central excise, cess, royalties and licence/lease fees as applicable to activities connected with the prospecting for or extraction or production of petroleum in the upstream sector under Contracts entered in terms of the Hydrocarbon Exploration and Licensing Policy (HELP)² and the earlier New Exploration Licensing Policy (NELP).]

¹ The provisions listed are as amended by Finance Act, 2017 and applicable for financial year 2017-18.

² HELP is a policy adopted by Government of India on March 10, 2016 indicating the new contractual and fiscal model for award of hydrocarbon acreages towards exploration and production (E&P). HELP is applicable for all future contracts to be awarded and replaces the erstwhile policy regime for exploration and production of oil and gas, known as NELP, which has been in existence for 18 years.

1. Title and Application

- 1.1. This Guide may be called the Petroleum Tax Guide, 2018.
- 1.2. The Guide compiles the specific provisions of the laws relating to income tax, customs duty, central excise, cess, royalties and licence/lease fees, in relation to all or any of the under mentioned activities in the whole of India including the continental shelf of India and the exclusive economic zone of India
 - a) The prospecting for or extraction or production of Petroleum in relation to which the Government of India has entered into a Contract under HELP or NELP with any person for the association or participation of the Government of India or any person authorised by it;
 - b) The provision of any services or facilities or supply of any ship, aircraft, machinery or plant (whether by way of sale or hire) to any person in connection with the prospecting for or extraction or production of Petroleum referred to in (a);
 - c) The rendering of services as an employee of any person engaged in any of the activities referred to in (a) or (b).

2. Background and Compilation

The Government of India adopted the HELP on March 10, 2016 outlining a new contractual and fiscal model for award of hydrocarbon acreage for Exploration and Production (E&P) of hydrocarbons. HELP envisages award of licenses to E&P operators to explore and extract hydrocarbon resources awarded under a contract. HELP replaces the earlier NELP which has been in place for 18 years. This guide outlines the fiscal provisions and incentives applicable to contracts awarded under HELP as well as those awarded under the erstwhile NELP.

The fiscal provisions compiled are those in force under the enactments and rules mentioned below and / or the notifications issued thereunder in relation to the prospecting for or extraction or production of Petroleum in the upstream sector under Contracts entered under HELP or NELP:

- a) The Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act (Act No.80 of 1976)
- b) The Income-Tax Act (Act No.43 of 1961)
- c) The Income-Tax Rules, 1962
- d) The Central Excise Act, 1944 (Act No.1 of 1944)
- e) The Central Excise Tariff Act, 1985 (Act No.5 of 1986)
- f) The Oil Industry (Development) Act, 1974 (Act No.47 of 1974)
- g) The Customs Act, 1962 (Act No.52 of 1962)
- h) The Customs Tariff Act, 1975 (Act No. 51 of 1975)
- i) The Oil fields (Regulation & Development) Act, 1948 (Act No.53 of 1948)
- j) The Petroleum and Natural Gas Rules, 1959

In the event of any inconsistency as between this Guide and any enactment and or any rule prescribed or notification issued thereunder, the relevant act or rule or notification, as the case may be, shall apply.

3. Definitions

- a) "Commercial Production" in relation to Revenue Sharing Contract (RSC) or Production Sharing Contract (PSC) means production of Petroleum (excluding any production for testing purposes) from a field and delivery of the same at the relevant delivery point under a programme of regular production and sale. The date of commencement of commercial production will be the date when commercial production commences from a field and the date of commencement of commercial production shall be intimated by the contractor to the Government of India in writing.

- b) "Continental Shelf" of India comprises the sea bed and the sub soil of the submarine areas that extend beyond the limits of its territorial waters throughout the natural prolongation of its land territory to the outer edge of the continental margin or to a distance of two hundred nautical miles from the base line, referred to in section 3(2) of the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976, where the outer edge of the continental margin does not extend up to that distance.
- c) "Contract" means:
 - i. in relation to HELP, an agreement entered into by the Government of India with any person for the association or participation of the Government of India or any person authorised by it in any business consisting of the prospecting for or extraction or production of petroleum [hereinafter also referred to as 'RSC Contract(s)']; and
 - ii. in relation to NELP, an agreement entered into on or after 1st January, 1999 by the Government of India with any person for the association or participation of the Government of India or any person authorised by it in any business consisting of the prospecting for or extraction or production of petroleum [hereinafter also referred to as 'PSC Contract(s)'].
- d) "Contract Area" in relation to any RSC or PSC Contracts means the area described in the Contract entered into by that person with the Government of India or any portion of said area remaining after relinquishment or surrender from time to time pursuant to the terms of the said Contract.
 - a. "Cost Petroleum" in relation to a PSC Contract means the portion of the total volume of Petroleum (defined below) produced and saved from the Contract Area which the contractor is entitled to take from the Contract Area in a particular period for the recovery of Contract costs as provided in Article 13 of the Model PSC.
 - b. "Development Operations":
 - i. Under RSC Contracts means operations conducted in accordance with the Field Development Plan and shall include but not limited to the procurement, shipment or storage of equipment and materials used in developing Petroleum accumulations, the drilling, completion and testing of development wells, the drilling and completion of wells for injection, dewatering, the laying of gathering lines, the installation of offshore platforms and installations, the installation of separators, tankage, pumps, artificial lift, gas storage facility and other producing and injection facilities required to produce, process and transport Petroleum into main oil storage or gas processing facilities or gas storage facilities, either onshore or offshore, including the laying of pipelines within or outside the Contract Area, storage at Delivery Point(s), the installation of said storage or gas processing facilities, the installation of export and loading facilities and other facilities required for the development and production of the said Petroleum accumulations and for the delivery of Crude oil and/or Gas at the Delivery point and also including incidental operations not specifically referred to herein but required for the most efficient and economic development and production of the said Petroleum accumulations in accordance with Good International Petroleum Industry Practices (GIPIP);
 - ii. Under PSC Contracts means operations conducted in accordance with the development plan pursuant to a Contract and shall include the purchase, shipment or storage of equipment and materials used in developing Petroleum accumulations, the drilling, completion and testing of development wells, the drilling and completion of wells for gas or water injection, the laying of gathering lines, the installation of offshore platforms and installations, the installation of separators, tankage, pumps, artificial lift and other producing and injection facilities required to produce, process and transport Petroleum into main oil storage or gas processing facilities, either onshore or offshore, including the laying of pipelines within or outside the Contract Area, storage and delivery point or points, the installation of said storage or gas processing facilities, the installation of export and loading facilities and other facilities required for the development and production of the said Petroleum

accumulations and for the delivery of Petroleum at the delivery point and also including incidental operations not specifically referred to herein but required for the most efficient and economic development and production of the said Petroleum accumulations in accordance with good international petroleum industry practices.

- c. "Exclusive Economic Zone" of India is an area beyond and adjacent to the territorial waters of India, and the limit of such zone is two hundred nautical miles from the baseline referred to in section 3(2) of the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976.
- d. "Exploration Operations":
 - i. Under RSC Contracts means operations conducted in the Contract Area pursuant to the Revenue Sharing Contract in searching for Petroleum and in the course of an Appraisal Programme and shall include but not be limited to aerial, geological, geophysical, geochemical, palaeontological, palynological, topographical and Geo-scientific surveys, analysis, studies and their interpretation, investigations relating to the sub-surface geology including drilling of exploration wells and appraisal wells, testing and other related activities such as surveying, drill site preparation and all work necessarily connected therewith that is conducted in connection with Petroleum exploration;
 - ii. Under PSC Contracts means operations conducted in the Contract Area pursuant to a Production Sharing Contract in searching for Petroleum and in the course of an appraisal programme and shall include but not be limited to aerial, geological, geophysical, geochemical, palaeontological, palynological, topographical and seismic surveys, analysis, studies and their interpretation, investigations relating to the subsurface geology including structure test drilling, stratigraphic test drilling, drilling of exploration wells and appraisal wells and other related activities such as surveying, drill site preparation and all work necessarily connected therewith that is conducted in connection with Petroleum exploration.
- e) "Natural Gas":
 - i. Under RSC Contracts means wet gas, dry gas, all other gaseous hydrocarbons, and all substances contained therein, including sulphur, carbon dioxide and nitrogen but excluding extraction of helium, which are produced from oil or gas or Coal Bed Methane (CBM) wells, excluding those condensed or extracted liquid hydrocarbons that are liquid at normal temperature and pressure conditions, and including the residue gas remaining after the condensation or extraction of liquid hydrocarbons from gas;
 - ii. Under PSC Contracts means wet gas, dry gas, all other gaseous hydrocarbons, and all substances contained therein, including sulphur, carbon dioxide, nitrogen but excluding helium, which are produced from oil or gas wells, excluding liquid hydrocarbons that are condensed or extracted from gas and are liquid at normal temperature and pressure conditions, but including the residue gas remaining after the condensation or extraction of liquid hydrocarbons from gas.
- f) "Participating Interest":
 - i. Under RSC Contracts means, in respect of each RSC participant, the undivided share, expressed as a percentage, of such Party's participation in the rights and obligations under a Contract;
 - ii. Under PSC Contracts means, in respect of each PSC Participant, the undivided share, expressed as a percentage, of such participant's participation, as it may exist at any given time, in the rights and obligations under a Contract.
- g) "Petroleum":
 - i. Under RSC Contracts means naturally occurring hydrocarbons in a free state, whether in the form of natural gas and / or in a liquid, viscous and/or solid and/or Condensate form or extracted through any unconventional means or sources such as CBM, shale gas, shale oil, tight gas, and gas hydrates, but does not include helium occurring in association with petroleum, or coal, or shale, or any substance which may be extracted

from coal, shale or other rock by application of heat or by a chemical Process. For the purpose of this definition, "shale oil" means crude oil / condensate generated in-situ and retained in shale and associated fine grained rock matrix including carbonate stringers and within fractures in shales of source rock origin and obtained from through boreholes;

- ii. Under PSC contracts means Crude Oil and/or Natural Gas existing in their natural condition but excluding helium occurring in association with Petroleum or shale.
- h) "Petroleum Operations" in relation to RSC or PSC Contracts means, as the context may require, Exploration Operations, Development Operations or Production Operations or any combination of two or more of such operations, including construction, operation and maintenance of all necessary facilities, plugging and abandonment of Wells, safety, environmental protection, transportation, storage, sale or disposition of Petroleum to the Delivery Point, Site Restoration and any or all other incidental operations or activities as may be necessary.
- i) "Production Operations" in relation to RSC or PSC Contracts means all operations conducted for the purpose of producing Petroleum from the Development Area after the commencement of production from the development area including the operation and maintenance of all necessary facilities therefor.
- j) "Profit Petroleum" in relation to a PSC Contract means all Petroleum produced and saved from the Contract Area in a particular period as reduced by Cost Petroleum and calculated as provided in Article 14 of the Model PSC.
- k) "RSC Participant" means a person with whom the Government of India has entered under HELP and where more than one person is a party to such Contract, the term "RSC Participants" shall mean all such persons collectively, including their respective successors and permitted assigns.
- l) "PSC Participant" means a person with whom the Government of India has entered into a Contract on or after 1st January, 1999 but does not include Contracts entered under HELP and where more than one person is a party to such Contract, the term "PSC Participants" shall mean all such persons collectively, including their respective successors and permitted assigns.

Any word or expression not defined herein shall have the meaning assigned to it in the context to which it relates in the applicable enactment, rule or notification or the Contract, as the case may be.

4. General for RSC or PSC Participants

RSC or PSC participants shall be subject to all fiscal legislation in India except where, pursuant to any authority granted under any applicable law, they are exempted wholly or partly from the application of the provisions of a particular law or as otherwise provided in Contract or in any double taxation avoidance agreement entered into by the Government of India under section 90 of the Income Tax Act, 1961.

5. Income-tax in relation to RSC or PSC Participants

1. RSC or PSC Participants shall not be assessed on their income as association of persons or body of individuals; but each RSC or PSC Participant shall be assessed in respect of his or its share of income, as the case may be, in the same Status in which that participant has entered into the Contract with the Government of India.

"Status" means the category under which a person is assessed to income tax under the Income-Tax Act, 1961, e.g., individual, company, firm, etc.

2. The profits and gains of business of a RSC or PSC Participant from Petroleum Operations shall, for the purpose of levy of income tax under the Income-Tax Act, 1961, be computed on the basis of the value, determined and revenue realised on sale of Petroleum in accordance with the Contract, of its Participating Interest share of Petroleum produced and

saved and sold, or otherwise disposed of, from the Contract Area and any other gains or receipts from Petroleum Operations, as reduced by the deductions as specified herein, and, except as herein provided, all the provisions of the Income-Tax Act, 1961, shall apply.

Expenses related to Exploration operations, Development operations, Production operations and Petroleum operations shall be allowed as per the provisions of the Income Tax Act, 1961, subject to the provisions of sections 40A and 44C of the Income-tax Act, 1961:

- a) where any expenditure is incurred in respect of which payment has been made or is to be made to any person referred to in clause (b) of section 40A(2) of the Income-Tax Act, 1961 and the Assessing Officer is of opinion that such expenditure is excessive or unreasonable having regard to the fair market value of the goods, services or facilities for which the payment is made or the legitimate needs of the business of the RSC or PSC Participant or the benefit derived by or accruing to him therefrom, so much of the expenditure as is so considered by him to be excessive or unreasonable shall not be allowed as a deduction.
- b) where any expenditure is incurred in respect of which payment is made in a sum exceeding ten thousand Indian rupees, otherwise than by a crossed cheque drawn on a bank or by an account payee bank draft or use of electronic clearing system through a bank account, such expenditure shall not be allowed as a deduction, except in such cases and under such circumstances as may be prescribed in the Income-Tax Rules, 1962.
- c) no deduction shall be allowed in respect of any provision made for the payment of gratuity to employees on their retirement or on termination of their employment for any reason, except where the provision is made for the purpose of payment of a sum by way of any contribution towards an approved gratuity fund, in which case the deduction shall be allowed on the basis of actual payment to the fund in accordance with the provisions of section 43B of the Income-tax Act, 1961, or the provision is made for the purpose of payment of any gratuity that has become payable during the year
- d) no deduction shall be allowed in respect of any sum paid by a RSC or PSC Participant as an employer towards the setting up or formation of, or as contribution to, any fund, trust, company, association of persons, body of individuals, society or other institution for any purpose except where such sum is paid by way of contribution towards a recognized provident fund, or an approved superannuation fund or an approved gratuity fund referred to in clause (iv) and clause (v) of section 36(1) of the Income-tax Act, 1961 to the extent mentioned therein
- e) in the case of a RSC or PSC Participant, being a non-resident, the deduction of head office expenditure shall be limited to -
 - i. 5 % of the adjusted total income, or
 - ii. so much of the expenditure in the nature of head office expenditure incurred by him as is attributable to the business carried on in India whichever is lower.

“adjusted total income” means total income computed in accordance with the Income-tax Act, 1961, as modified herein, but before any deduction for carried forward unabsorbed depreciation, carried forward family planning expenses under section 36(1)(ix), any losses carried forward under section 72(1), or section 73(2) or section 74(1) or section 74(3) or section 74A(3) or deduction under section 80IB of the Income-tax Act, 1961.

“head office expenditure” means executive and general administration expenditure incurred by the RSC or PSC Participant outside India, including expenditure incurred in respect of -

- a) rent, rates, taxes, repairs or insurance of any premises outside India used for the purposes of the business;
- b) salary, wages, annuity, pension, fees, bonus, commission, gratuity, perquisites or profits in lieu of or in addition to salary, whether paid or allowed to any employee or other person employed in, or managing the affairs of, any office outside India;

- c) travelling by any employee or other person employed in, or managing the affairs of, any office outside India; and
 - d) such other matters connected with executive and general administration as the government of India may prescribe for the purpose of section 44C of the Income-Tax Act, 1961.
3. All expenditure incurred by an RSC Participant on exploration, development and production under an RSC Contract³ shall be allowed as deduction under section 42(1) of the Income Tax Act, 1961. In respect of PSC Participants, PSC Contracts read with Section 42(1) of the Income-tax Act, 1961 provided for specific provisions in respect of PSC Participants. These have been listed in **Annexure A**. The said deductions would be available only for such RSC or PSC Contracts which have been laid on the Table of each House of Parliament.
4. A RSC or PSC Participant shall be entitled to deduct, while computing the profits and gains of business from Petroleum Operations, for the purpose of income tax, any amount deposited by him in the Site Restoration Fund, in accordance with and for the purposes specified in, the Site Restoration Fund Scheme, 1999 notified by the Ministry of Petroleum and Natural Gas, Government of India, in the year in which such amount is deposited, upto a maximum of 20% of such profits. Interest reinvested in accordance with the Scheme shall also qualify for deduction within this limit.
5. As regards the tax treatment of assignment or transfer of participating interest by a RSC or PSC Participant under the Contract, following provisions of section 42 (2) of the Income Tax Act shall apply:-

"Where the business of the assessee consisting of the prospecting for or extraction or production of petroleum and natural gas is transferred wholly or partly or any interest in such business is transferred in accordance with the agreement refer to in sub-section (1), subject to the provisions of the said agreement and where the proceeds of the transfer (so far as they consist of capital sums) –

- a) are less than the expenditure incurred remaining unallowed, a deduction equal to such expenditure remaining unallowed, as reduced by the proceeds of transfer, shall be allowed in respect of the previous year in which such business or interest as the case may be, is transferred;
- b) exceed the amount of the expenditure incurred remaining unallowed so much of the excess as does not exceed the difference between the expenditure incurred in connection with the business or to obtain interest therein and the amount of such expenditure remaining unallowed shall be chargeable to income tax as profits and gains of the business in the previous year in which the business or interest therein, whether wholly or partly has been transferred; Provided that in a case where the provisions of this clause do not apply, the deduction to be allowed for expenditure incurred remaining unallowed shall be arrived at by subtracting the proceeds of transfer (so far as they consist of capital sums) from the expenditure remaining unallowed.

Explanation:

Where the business or interest in such business is transferred in a previous year in which such business carried on by the assessee is no longer in existence, the provisions of this clause shall apply as if the business is in existence in that previous year.

- c) are not less than the amount of the expenditure incurred remaining unallowed, no deduction for such expenditure shall be allowed in respect of the previous year in which the business or interest in such business is transferred or in respect of any subsequent year or years;

³ Refer Article 16 of the Model RSC Contract - http://online.dghindia.org/oalp/Content/pdf/MRSC_booklet_02.pdf

Provided that in a scheme of amalgamation of the amalgamating company sells or otherwise transfers the business to the amalgamated company being an Indian company, the provisions of this sub-section:

- i) shall not apply in the case of amalgamating company; and
 - ii) shall, as far as may be, apply to the amalgamated company as they would have applied to the amalgamated company if the later had not transferred the business or interest in the business.
6. Any capital expenditure, other than those qualifying for 100% allowance (as prescribed in the RSC Contract or PSC Contract), in the nature of buildings, machinery, plant or furniture owned by the RSC or PSC Participant and used for the Petroleum Operations, shall be eligible for depreciation allowance on the written down value of the block of assets in accordance with section 32 of the Income-Tax Act, 1961, at the rates prescribed in
 7. Appendix I of the Income-Tax Rules, 1962.
 8. Set off, or carry forward and set off of losses, if any, shall be in accordance with the provisions of the Income-Tax Act, 1961.
 9. The provisions of section 115JB of the Income-Tax Act, 1961 shall apply to a RSC or PSC Participant in respect of profits and gains derived from a Contract.
 10. The income-tax payable by the RSC or PSC Participant on his total income shall be the amount of income-tax calculated on such total income at the rate of income-tax in force as applicable to him.
 11. In terms of section 10(15) of the Income-Tax Act, 1961, the following interest shall be exempt from income-tax in the hands of the payee.

Interest payable by a RSC or PSC Participant -

- a) on moneys borrowed under a loan agreement with such financial institution in a foreign country as may be approved in this behalf by the Central Government by a general or special order
 - b) on moneys borrowed or debt incurred by it in a foreign country in respect of the purchase outside India of raw materials or components or capital plant and machinery, to the extent to which such interest does not exceed the amount of interest calculated at the rate approved by the Central Government in this behalf, having regard to the terms of the loan or debt and its repayment
- Explanation** - For the purpose of this item, "purchase of capital plant and machinery" includes the purchase of such capital plant and machinery under a hire-purchase agreement or a lease agreement with an option to purchase such plant and machinery.
- c) on moneys borrowed by it in foreign currency from sources outside India under a loan agreement approved by the Central Government having regard to the need for industrial development in India, to the extent to which such interest does not exceed the amount of interest calculated at the rate approved by the Central Government in this behalf, having regard to the terms of the loan and its repayment.

6. Income-Tax in relation to service providers and suppliers

1. Subject to the provisions of the applicable double taxation avoidance agreement entered into by India under section 90 of the Income-Tax Act, 1961, in the case of a person being a non-resident, engaged in the business of providing services or facilities in connection with, or supplying plant and machinery on hire used, or to be used, in the prospecting for or extraction or production of Petroleum and/or Natural Gas, a sum equal to 10% of the aggregate amount specified in (a) and b) below shall be deemed to be the profits and gains of such business, which shall be taxed at the normal tax rate applicable to the business income of such non-resident

- a) the amount paid or payable (whether in or out of India) to the person or to any other person on his behalf on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of Petroleum in India; and
- b) the amount received or deemed to be received in India by or on behalf of the person on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of Petroleum outside India.

“Plant” includes ships, aircraft, vehicles, drilling units, scientific apparatus and equipment, used for the purpose of the said business.

The provisions of section 115JB of the Income Tax Act, 1961 shall not apply to a non-resident referred above, provided its total income comprises solely of profit and gains from business referred to in section 44BB of the Income Tax Act, 1961⁴.

2. The income-tax liability, if any, of a non-resident from transactions involving sale of plant and machinery in connection with the prospecting for or extraction or production of Petroleum, shall be in accordance with the provisions of the Income-Tax Act, 1961 or the applicable double taxation avoidance agreement entered into by India under section 90 of the Income-Tax Act, 1961, whichever is more beneficial to the non-resident.
3. Residents providing any services or facilities or supplying any ship, aircraft, machinery or plant (whether by way of sale or hire) in connection with any business consisting of the prospecting for or extraction or production of Petroleum and/or Natural Gas, will be liable to income-tax in accordance with the normal provisions of the Income-Tax Act, 1961.

7. Customs Duty

Prior to introduction of Goods and Services Tax (GST), effective customs duty on import of goods comprised of Basic Customs Duty, Counter Veiling Duty, Customs Cess and Special Additional Customs Duty. However, with enactment of GST with effect from July 1, 2017, effective customs duty comprises of Basic Customs Duty (BCD), Surcharge Cess and Integrated Goods & Service Tax (IGST).

The following tax exemptions are available for upstream sector for the aforesaid component:

a. Basic Customs Duty and Surcharge Cess

Import of goods by the RSC or PSC Participant or any of its sub-contractor shall be exempt from payment of BCD and surcharge Cess provided following key conditions stand satisfied:

- i. The goods being imported fall within the list given in **Annexure B**
- ii. Such goods should be required in connection with petroleum operations undertaken under RSC or PSC Contract
- iii. An essentiality certificate is issued by Director General Hydrocarbons
- iv. A certificate, in the case of a contract entered into by the Government of India and a Foreign Company or Companies or the Government of India and a consortium of an Indian Company or Companies and a Foreign Company or Companies that no foreign exchange remittance is to be made for the import of such goods undertaken by the Foreign Company or Companies.

In case where any of such conditions are not satisfied or stands violated post importation without payment of duty, the importer shall be liable to pay customs duties at applicable rate along with interest and penalty.

Such goods shall also be exempt from export duties or other charges on re-exportation in accordance with applicable legislation.

⁴ Explanation 4A to section 115JB(1) proposed to be inserted by Finance Bill, 2018.

b. Integrated GST at 5% on permanent imports

In addition to levy of BCD and surcharge cess, import of goods into India attracts levy of IGST. However, similar to exemption granted for levy of BCD, the government of India has provided benefit for upstream sector by levying concessional rate of 5% IGST on the value of imported goods, as required in connection with petroleum operations undertaken under RSC or PSC Contract subject to the same conditions, as mentioned above for exemption from BCD.

Further, such IGST of 5% is available as input tax credit for sub-contractors, who supply the same imported goods or services to operators. Hence, while such IGST paid by sub-contractor or vendor down the line on import of goods does not result into any incremental cost for exploration business, it would add to the cost of business in case where operators themselves import such goods.

c. Integrated Goods & Service Tax on temporary imports

Levy of 5% on value of imported goods resulted into adverse cash flow or incremental cost in case of temporary imports except for admissible drawback at the time of re-export.

Resultantly, the government has exempted IGST on temporary import of goods [other than motor vehicles] including vessels, ships under lease arrangement subject to key conditions enumerated below:-

- i. Such goods being imported temporarily should be covered under lease arrangement
- ii. Importer undertakes to pay IGST on lease rentals being paid
- iii. Importer should undertake not to sell or part with the goods so imported under lease arrangement, without the prior permission of the customs authorities at the port of importation
- iv. Importer would be required to re-export such temporarily imported goods within three months from completion of lease agreement
- v. Such exemption from IGST on temporary imports has immensely resulted into relief for all importers engaged in exploration of petroleum products.

d. Maintenance of records

- The Government of India shall have the right to inspect the records and documents of the physical item or items for which an exemption has been provided pursuant to (1) to determine that such item or items are being or have been imported solely and exclusively for the purpose for which the exemption was granted.
- The Government shall also be entitled to inspect such physical goods so as to ensure that goods so imported by claiming benefit of exemption from BCD and concessional rate of IGST are being used for the said petroleum operations.
- RSC or PSC Participant, its sub-contractors and their sub-contractors, who have imported goods by claiming exemption from customs duty, may sell or otherwise transfer such imported goods on payment of applicable customs duty as computed in accordance with the provisions captured in the Notification.

8. Excise Duty and Cess

While excise duty is not applicable on production and sale of petroleum products explored under the RSC or PSC Contract, Cess stands payable on crude and natural gas produced from the field.

The generic rate of Cess payable on production of crude and natural gas is 20% ad valorem. However, such rate of Cess payable varies basis the RSC or PSC Contract executed.

9. GST

1. GST, the biggest indirect tax reform in India, has been introduced from July 1, 2017 to subsume various central and state indirect taxes such as service tax, excise, CST, VAT and entry tax etc.
2. GST regime consists of central GST and a state GST, which is concurrently levied by the central government as well as state government. However, presently, following petroleum products are kept out of the ambit of GST until a date to be determined by the GST Council:
 - i. Crude
 - ii. High Speed Diesel
 - iii. Petrol
 - iv. Natural Gas
 - v. Aviation Turbine Fuel

Given this implication of GST is mostly on the procurement side as sale of Natural Gas and Crude emerging from petroleum operations are outside the ambit of GST.

3. Considering above, presently, production of crude and natural gas does not attract GST since both of them are outside the ambit of GST until that date to be decided by GST council. Sale of crude and natural gas would continue to attract state specific VAT / CST.
4. Domestic procurement of Goods:

Local procurement of goods mentioned vide **Annexure B**, as required for petroleum operations, would attract GST of 5% subject to conditions mentioned above, as applicable for importation without payment of BCD.

5. Procurement of Services:
 - a) The generic rate of GST on supply of services is 18%. Given such increased rate of non-recoverable GST on services, as compared to service tax of 15%, there has been a view across industry that cost of exploration, development and production of crude and natural gas would envisage higher investment as compared to pre-GST regime.
 - b) Transfer of right to use goods would attract GST at the rate, as applicable on the supply of the underlying goods.
 - c) Time charter / voyage charter of vessels for transportation shall attract GST of 5% subject to condition that input tax credit of GST charged on procurement of inputs is not availed.
 - d) Works Contract –
 - i. Any transaction envisaging transfer of ownership in respect of material during execution of work, thereby resulting into addition or erection of immovable property would qualify as 'works contract'.
 - ii. Such works contract services rendered within 12 nautical miles and beyond 12 NM from the nearest point of the appropriate base line would attract GST of 18% and 12% respectively.
 - iii. Rate of GST for offshore works contract is pegged at 12% in order to ensure that the effective cost / investment to be made in offshore fields remain the same as pre-GST regime.
 - e) Exploration, mining or drilling services :

While the rate of GST on services of exploration, mining and drilling of petroleum crude or natural gas or both has been kept at 12%, support services to mining, electricity, gas and water distribution other than (ii) above would continue to attract GST of 18%.
 - f) GST implications on royalty to be paid to Government:
 - g) Royalty is slated to be consideration for services being undertaken by government in the nature of licensing contractors to explore the fields. Hence, RSC or PSC Participants would be required to pay GST under reverse charge mechanism on royalty paid to government.

- h) The Government has clarified its stand in order to avoid ambiguity that cost petroleum is not the consideration for supply of services. Hence, GST should not be applicable on cost petroleum though one needs to assess facts of each case before concluding on the said aspect.
- i) The Government has exempted profit petroleum from levy of GST and service tax.

10.Royalty:

a) Royalty under RSC Contracts

Blocks	Duration	Royalty rates	
		Oil	Gas
Onland	-	12.5%	10%
Shallow Water	-	7.5%	7.5%
Deep Water	First 7 years	No Royalty	No Royalty
	After 7 years	5%	5%
Ultra deep water	First 7 years	No Royalty	No Royalty
	After 7 years	2%	2%

b) Royalty under PSC Contracts

PSC Participants shall pay royalty at 10% for crude oil & natural gas in offshore areas. For onshore areas the royalty shall be at 12.5% for crude oil and at 10% for natural gas.

Provided, however, the royalty will be charged at half the rate applicable to normal off-shore area i.e. at 5% for deep water areas beyond 400 m bathymetry for the first 7 years, commencing with the year in which Commercial Production is commenced.

The valuation of Petroleum for the purpose of calculating royalty shall be as per the provisions of the Oilfields (Regulation and Development) Act, 1948 and the Petroleum and Natural Gas Rules, 1959.

The royalty amount due for any month shall be paid to the Central Government/ State Government latest by the last day of the succeeding month in accordance with the provisions of The Petroleum and Natural Gas Rules, 1959.

11.Deposits, Licence Fee, Dead Rent and Surface Rent

- 1 Before the licence is granted, the applicant for a licence shall deposit with the Central Government or where the licence is to be or has been granted by the State Government, the State Government as security for due observance of the terms, covenants and conditions of the licence, a sum of Rs. 1,00,000 (Rupees One Lac only).
- 2 The licensee shall pay yearly in advance by way of licence fee in respect of his licence a sum calculated for each square kilometre or part thereof covered by the licence at the following rates
 - a) Rs. 50 (Rupees Fifty only) for the first year of the licence
 - b) Rs. 100 (Rupees One Hundred only) for the second year of the licence
 - c) Rs. 500 (Rupees Five Hundred only) for the third year of the licence
 - d) Rs. 700 (Rupees Seven Hundred only) for the fourth year of the licence
 - e) Rs. 1,000 (Rupees One Thousand only) for the first and second years of the renewal

- 3 The applicant for a lease shall, before the lease is granted to him -
 - a) deposit with the Central or the State Government, as the case may be, as security, a sum of Rs. 2,00,000 (Rupees Two Lacs only), for due observance of the terms and conditions of the lease,
 - b) also deposit with the Central or the State Government, as the case may be, for meeting the preliminary expenses, such sum not exceeding Rs. 30,000 (Rupees Thirty thousand only), as the Central Government or the State Government with the approval of the Central Government, may determine.
- 4 On the grant of a lease, the lessee -
 - a) shall pay to the Central or the State Government, as the case may be, for every year a fixed yearly dead rent at the following rates -

Rs. 25 (Rupees Twenty Five only) per hectare or part thereof for the first 100 square kilometres and Rs. 50 (Rupees Fifty only) per hectare or part thereof for area exceeding the first 100 square kilometres provided that the lessee shall be liable to pay only the dead rent or the royalty, whichever is higher in amount but not both.
 - b) shall also pay to the State Government, for the surface area of the land actually used by him for the purpose of the operations conducted under the lease, surface rent at such rate, not exceeding the land revenue and cesses assessed or assessable on the land, as may be specified by the State Government with the approval of the Central Government.
- 5 The deposits, license fee, dead rent and surface rents are subject to change in accordance with the relevant laws and rules by the Government or State Government, as the case may be, from time to time.

12. Employees

Subject to the provisions of applicable double taxation avoidance agreements entered into by India under section 90 of the Income-Tax Act 1961, employees of RSC or PSC Participants, service providers and suppliers shall be subject to the provisions of all fiscal legislation in India.

13. Exclusion

This Guide does not take into account -

- a) charges payable by specified industries or in connection with Petroleum Operations under any other legislation;
- b) payments for purchase, lease or rental of land or land rights in connection with Petroleum Operations;
- c) taxes, fees or charges for specific services rendered on request or to the public generally;
- d) sales tax, if any, leviable on the facts and circumstances of any given case;
- e) stamp duties, registration fees, licence fees, taxes such as taxes on property or assets (not calculated by reference to income or otherwise exempted) or other levies, fees or charges of a non-discriminatory nature and generally applicable in India or in the State where Petroleum Operations are being conducted;

ANNEXURE A

Specific deductions available to PSC Participants as per the Model PSC (which has been laid on the Table of each House of Parliament) read with section 42(1) of Income-tax Act, 1961 – basis the model PSC⁵ released by the government

1. Subject to the provisions herein below, in computing the profits and gains from the business of Petroleum Operations of a RSC or PSC Participant for the purpose of income tax, there shall be allowed deductions at the rate of one hundred percent (100%) per annum for all of the following expenditures -
 - a) all expenditure incurred in respect of Exploration Operations

⁵ http://dghindia.gov.in/assets/downloads/56cee34476e1f8_MPSC_NELP_VIII.pdf

- b) all expenditure incurred in respect of drilling operations

The expenditure incurred in respect of Development Operations, other than drilling operations, and Production Operations will be allowable as per the provisions of the Income-tax Act, 1961. The expenses so incurred are subject to the following:

- 2. For any or all accumulated expenditures incurred in respect of Exploration Operations and drilling operations prior to the date of commercial production, PSC Participants shall have option to amortize such expenditures over a period of ten (10) years from the date of first commercial production.

Provided further that, a PSC Participant may, at his option, set off any loss on account of the allowable expenses in the year such expenses are incurred against profits from any other source in accordance with and subject to the provisions of sections 70 and 71 of the Income-Tax Act, 1961.

- 3. A PSC Participant shall be entitled, for income tax purposes only, to deduct all its unsuccessful exploration costs in contract areas covered by other contracts from the aggregate value of Petroleum allocable to the PSC Participant from any Field (s) in the Contract Area in the manner as follows:
 - a) Unsuccessful exploration costs incurred in contract areas other than the Contract Area where a commercial discovery has been made up to the date of commencement of Commercial Production shall be aggregated and the PSC Participant shall be entitled to deduct such costs at the rate of one hundred per cent (100%) per annum;
 - b) Unsuccessful exploration costs incurred in contract areas other than the Contract Area where a commercial discovery has been made, after the commencement of Commercial Production, shall be deductible at the rate of one hundred per cent (100%) per annum of such costs beginning from the Year such costs are incurred.

Provided however, a PSC Participant may, at his option set off any costs mentioned in (a) or (b) above in the year in which such costs are incurred against profits from any other source in accordance with and subject to the provisions of sections 70 and 71 of the Income-Tax Act, 1961.

Annexure - B

- 1. Land Seismic Survey Equipment and accessories, requisite vehicles including those for carrying the equipment, seismic survey vessels, global positioning system and accessories, and other materials required for seismic work or other types of Geophysical and Geochemical surveys for onshore and offshore activities
- 2. All types of Drilling rigs, jackup rigs, submersible rigs, semi submersible rigs, drill ships, drilling barges, short-hole drilling rigs, mobile rigs, workover rigs consisting of various equipment and other drilling equipment required for drilling operations, snubbing units, hydraulic workover units, self elevating workover platforms, Remote Operated Vessel (ROV)
- 3. Helicopters including assemblies/parts
- 4. All types of marine vessels to support Petroleum Operations including work boats, barges, crew boats, tugs, anchor handling vessels, lay barges and supply boats; Marine ship equipment including water Maker, DP system and Diving system
- 5. All types of Equipment/units for specialised services like diving, cementing, logging, casing repairs, production testing, simulation and mud services, oil field related lab equipment, reservoir engineering, geological equipment, directional drilling Stimulation, Coil Tubing units, drill stem testing (DST), data acquisition and processing, solids control, fishing (as related to downhole retrieval in oil field operations), well control, blowout prevention (BOP), pipe inspection including Non Destructive Testing, coring, gravel pack, well completion and workover for oil/gas wells including wireline and downhole equipment
- 6. All types of casing pipes, drill pipes, production tubing, pup joints, connections, coupling, kelly, cross overs and swages, Drive Pipes

7. All types of drilling bits, including nozzles, breakers and related tools
8. All types of oil field chemicals including synthetic products used in petroleum operations, oil well cement and cement additives required for drilling, production and transportation of oil or gas
9. Process, production and well platforms for oil, gas and water injection including items forming part of the platforms and equipment required like process equipment, turbines, pumps, generators, compressors, primemovers, water makers, filters and filtering equipment Telemetry, Telecommunication, Tele-Control and other material required for platforms
10. Line pipes for flow lines and trunk pipelines including weight coating and wrapping
11. Derrick barges, Mobile and stationary cranes, trenchers, pipelay barges, cargo barges and the like required in the construction/installation of platforms and laying of pipelines
12. Single buoy mooring systems, mooring ropes, fitting like chains, shackles, couplings marine hoses and oil tankers to be used for oil storage and connected equipment; Tanks used for storage of oil, condensate, water, mud, chemicals and related materials
13. All types of fully equipped vessels and other units/equipment required for pollution control, fire prevention, fire fighting, safety items like Survival Craft, Life Raft, fire and gas detection equipment, including H2S monitoring equipment
14. Mobile and skid mounted pipe laying, pipe testing and pipe inspection equipment
15. All types of valves including high pressure valves
16. Communication equipment required for Petroleum operations including synthesized VHF Aero and VHF Marine multi channel sets
17. Non directional radio beacons, intrinsically safe walkie-talkies, directional finders, EPIRV, electronic individual security devices including electronic access control system
18. Specialized antenna system, simplex telex over radio terminals, channel micro wave systems, test and measurement equipment
19. X-band radar transponders, area surveillance system
20. Common depth point (CDP) cable, logging cable, connectors, geo-phone strings, perforation equipment and explosives
21. Wellhead and christmas trees, including valves, chokes, heads spools, hangers and actuators, flexible connections like chicksons and high pressure hoses, shut down panels
22. Cathodic Protection Systems including anodes
23. Technical drawings, maps, literature, Data tapes, Operational and Maintenance Manuals required for petroleum operations
24. Sub-assemblies, tools, accessories, stores, spares, materials, supplies, consumables for running, repairing or maintenance of the goods specified in this list



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