Oil and gas tax needs tweaks, not overhaul, says Davis Tax Committee

By Linda Ensor

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No major changes to the existing fiscal regime for the oil and gas industry have been proposed by the Davis Tax Committee.

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The committee released its report on the oil and gas sector on Monday, saying that current legislative regime was - subject to minor refinements - "appropriate to attracting oil and gas investors in an environment of geological uncertainty".

It noted that the major deterrents to investment in SA were posed by factors outside the tax system.

"The proposed amendments to the Mineral and Petroleum Resources Development Act (MPRDA) with regard to state participation have created additional policy-induced uncertainty for international investors, discouraging the further progression and uptake of oil and gas rights in SA," the committee said.

It urged that the mechanics for state participation be clarified in the act, and be clearly articulated in the exploration and production rights issued by the Department of Mineral Resources.

The report noted that in the event of a significant commercial discovery of oil or gas, new taxes could be considered.

The South African oil and gas industry is still in a nascent stage of development with considerable uncertainty over its size and the commercial recoverability of oil and gas reserves both offshore (deep-water) and onshore (shale gas).

The committee recommended that the government create fiscal stability for the "first-mover" companies that face the greatest risks, and deal with the transition to any new tax dispensation by enforcing the relinquishment provisions under the MPRDA. These compel the size of a block or field to shrink as the oil and gas project moves through its life stages (for example, the conversion of an exploration right into a production right).

"Any new tax dispensation will apply prospectively to all new rights issued, including the acreage that is released through the relinquishment process. This provides predictability to the 'frontier' investor, confronted by huge geological and commercial risk, which is difficult to quantify ex-ante, but still allows policy flexibility to government once the extent of commercially viable resources can be more accurately scoped."

The committee recommended replacing the variable royalty rate formula applicable to the sector with a flat rate royalty of 5% for oil and gas.

"The variable rate formula in the oil and gas industry introduces unnecessary complexity and should therefore be simplified," it said.

The report noted that even if attracting investment in the oil and gas sector did not yield significant tax revenue for the fiscus, the multiplier effect of such an investment provided the platform for job creation.

Source: *BDpro*