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Oil and gas taxation in South Africa

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Tax professionals of the member firms of Deloitte Touche Tohmatsu Limited have created the Deloitte International Oil and Gas Tax Guides, an online series that provides information on tax regimes specific to the oil and gas industry. The Guides are intended to be a supplement to the Deloitte Taxation and Investment Guides, which can be found at **www.deloitte.com/taxguides**.

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1.0 Overview

The Republic of South Africa ("South Africa") is a state in southern Africa. It is a parliamentary republic comprised of nine provinces and is located at the Southern tip of Africa. South Africa is a constitutional democracy in the form of a parliamentary republic. It has a two-chamber parliament and an indirectly elected executive president. The National Assembly is elected by proportional representation; the National Council of Provinces consists of indirectly elected representatives of provinces.

South Africa is ranked as an upper-middle income economy and is considered to be a newly industrialised country. It's economy is the second largest in Africa and 28th largest in the world. Poverty and inequality remain widespread, with a quarter of the population unemployed.

South Africa has a wealth of natural resources (including coal, platinum, gold, iron ore, manganese, nickel, uranium and chromium) and it has been enjoying increased attention from international exploration companies, particularly in the oil and gas sector.

South Africa has a relatively open economy. Most exports to industrialised countries consist of primary and intermediate commodities. A large proportion consists of unprocessed raw material; the mining industry contributes the most to the country's total exports. The country is a major exporter of coal, gold, diamonds, platinum, wool, sugar, manganese, and chrome ores.

1.1 Key facts

Population: 52.98 million (2013 estimate)

Median age: 25.7 years (2014 estimate)

Currency (code): Rand (ZAR)

Exchange rate at 1 March 2015: South African Rand ZAR 11.65 = US $1

Exchange controls: Maintains exchange control regulations that restrict free flow of capital in and out of the country.

GDP (purchasing power parity): $683.1 billion (2013 estimate)

GDP per head of population: $12,700 (2014 estimate)

GDP growth: 1.4% (2014 estimate)

Principal industries: Mining (world's largest producer of platinum, gold, chromium), automobile assembly, metalworking, machinery, textiles, iron and steel, chemicals, fertilizer, foodstuffs, commercial ship repair.

Official languages: IsiZulu, IsiXhosa, Afrikaans, English, Sepedi, Setswana, Sesotho, Xitsonga, siSwati, Tshivenda, isiNdebele.

Unemployment rate: 25% (2014 estimate)

Legal system: Mixed legal system or Roman-Dutch law, English common law and customary law.

Head of State: President Jacob Zuma

Head of Government: President Jacob Zuma

Transparency International corruption perception index 2013: 42 (placed 72 out of 177 countries)

1.2 Industry overview

South Africa is ranked between fourth and eighth for shale gas exploration potential with an estimated 390 Trillion Cubic feet (“Tcf”) of recoverable resource.

Apart from shale, South Africa has limited oil and gas reserves but relies on a large coal mining industry in order to meet most of its energy needs. In 2015, 71% of South Africa's total primary energy consumption came from coal, followed by oil (23%), natural gas (3%), nuclear (3%), and renewables (less than 1%, primarily from hydropower), according to the BP Statistical Review of Energy 2015.

South African state-owned company, Petroleum Oil and Gas Corporation of South Africa (“PetroSA”) dominates the upstream oil and gas sector in South Africa, with South African company Sasol also playing a key role both nationally and internationally. Whereas the downstream oil sector is more varied and includes companies from Europe, North America and Asia. BP, Shell, Chevron, Total and Engen are the main players in the downstream oil and petrochemical industry.

Other major players in the South African oil and gas industry include Forest Oil, BHP Billiton, Anschutz, Anglo American, Exxon Mobil, Falcon Oil & Gas, Anadarko, Kinetiko Energy, Cairn India, Sasol, Sunbird Energy, Thombo Petroleum and Sungu Sungu Petroleum.

Historically, offshore exploration has been limited, however recent improvements in exploration technology, combined with South Africa’s need to diversify its energy mix has seen increased interest in exploration activity off South Africa's coast, with 20 exploration licences issued. Additionally, the South African government has expressed an intention to issue licences for the exploration of shale gas in the Karoo Basin, the largest potential reserve.

1.3 Regulatory environment

South Africa has a number of government agencies and companies involved in the coal, natural gas and oil sectors. The Petroleum Agency of South Africa (“PASA”) regulates oil and natural gas exploration and production and provides public data on exploration and production. The National Energy Regulator of South Africa (“NERSA”) regulates the electricity sector, natural pipeline industries, and petroleum pipeline industries. NERSA regulates electricity prices and encourages private sector participation by promoting investment by independent power producers (“IPPs”), and off-grid technologies to meet rural energy needs. State-owned electricity company, Eskom, produces roughly 95% of South Africa's electricity and owns and operates the national electricity grid.

2.0 General

Oil and gas companies in South Africa ("SA") are generally subject to ordinary tax rules in the same way as other companies that fall within the ambit of the SA tax system. However, certain specific tax concessions exist in the Income Tax Act which are aimed at incentivizing investment in exploration and post-exploration activities. 'Exploration activities' include all activities up to and including the appraisal phase and 'Post-exploration activities' comprise those carried out after completion of the appraisal phase, including the separation of oil and gas condensates, the drying of gas and the removal of non-carbon constituents, to the extent that the activities are the preliminary to refining.These specific tax concessions also offer fiscal stability for investment in the industry. Royalties are payable by upstream oil and gas companies under the terms set out in the Mineral and Petroleum Resources Royalty Act.

The principal taxes applicable to companies in the oil and gas industry are currently as follows:

• Corporate income tax	
– Oil and gas income	28%
– Other income	28%
– Capital gains not included in oil and gas income	18.65%
• Withholding tax*	
– Dividends	
– Paid out of amounts attributable to oil and gas income	0%
– Paid out of amounts attributable to other income	15%
– Branch remittance tax	None
– Royalties**	15%
– Interest***	15%
– Paid in respect of loans applied to fund capital expenditure in respect of exploration or post-exploration	0%
– Paid in respect of other loans	15%
– Services****	15%
• Value-Added Tax ("VAT")	14%
• Royalties	Note
• Securities Transfer Tax ("STT")	0.25%

* The rate of withholding tax is subject to reduction under an applicable double tax treaty

** The rate of withholding tax on royalties increased from 12% to 15% with effect from 1 January 2015

*** Withholding tax on interest at a rate of 15% was introduced with effect from 1 March 2015

**** No withholding tax on service fees currently applies, but it is proposed to be introduced with effect from 1 January 2017

Note: Royalties are payable on the 'transfer' (e.g. disposal) of a 'mineral resource' that has been 'extracted' from within SA. The royalty amount is determined with reference to value rather than volume of the mineral resource, and comprises gross sales (tax base) multiplied by a variable percentage rate that is calculated with reference to profitability of operations (earnings before interest and taxes, divided by gross sales, multiplied by a defined factor), with a minimum rate of 0.5% and a maximum rate of up to 5% in certain circumstances.

3.0 Corporate income tax

3.1 In general

SA resident companies are subject to corporate income tax on worldwide taxable income and capital gains (subject to various exemptions and the application of double taxation agreements). Non-resident companies are only taxed on income that is from a SA source and on capital gains relating to the disposal of certain assets in SA (subject to the application of double taxation agreements). For these purposes, SA includes the exclusive economic zone of the surrounding waters (200 nautical miles).

A company will be a resident of SA for tax purposes if it is incorporated, established or formed in SA, or if it has its place of effective management in SA.

The Income Tax Act provides that the taxable income of any 'oil and gas company' will be determined in accordance with the Income Tax Act, subject to specific provisions contained in the Tenth Schedule to that Act. In other words, ordinary tax principles apply, but are supplemented by special rules in the Tenth Schedule.

The provisions of the Tenth Schedule regulate the taxation of 'oil and gas income' derived by an oil and gas company, which comprises receipts and accruals derived from exploration or post-exploration in terms of any oil and gas right, or the leasing or disposal of such right. All other income derived by an oil and gas company is subject to tax in terms of the ordinary tax rules.

3.2 Rates

The current corporate tax rate applicable in SA is 28%. The Tenth Schedule rules provide that the rate of tax on taxable income attributable to the oil and gas income of any oil and gas company shall not exceed 28%.

The Income Tax Act prescribes that a certain portion of a taxpayer's net capital gain for the year must be included in its taxable income. In the case of a company, 66.6% of its net capital gain is currently included in taxable income as a taxable capital gain.

3.3 Taxable income

Taxable income generally comprises gross income and certain specific inclusions, less exemptions and tax deductions provided for in the Income Tax Act.

Inclusions, exemptions and deductions that are generally applicable to other companies are also applicable to oil and gas companies. The Tenth Schedule to the Income Tax Act does however contain rules with respect to specific deductions for which oil and gas companies may qualify, as well as rules regarding the ring-fencing of any assessed losses incurred by oil and gas companies. These specific provisions have been detailed in paragraph 3.5 and 3.6 below.

3.4 Revenue

Oil and gas income

Oil and gas income means the receipts and accruals derived by an oil and gas company from exploration in terms of any oil and gas right, post-exploration in respect of any oil and gas right or the leasing or disposal of any oil and gas right. Oil and gas income may therefore include amounts of a capital nature.

As noted above, the Tenth Schedule rules provide that the rate of tax on taxable income attributable to the oil and gas income of any oil and gas company shall not exceed 28%.

Non-oil and gas income

Non-oil and gas income of oil and gas companies is taxed in terms of the normal tax rules that would apply to any other company that is subject to the Income Tax Act. Amounts included in gross income include receipts and accruals that are received by or accrued to the taxpayer in a year of assessment that are not of a capital nature. Income is deemed to form part of gross income on the earlier of date of receipt and accrual.

Non-oil and gas income of a capital nature is subject to taxation under the capital gains tax rules contained in the Eighth Schedule to the Income Tax Act, where such income arises as a result of the disposal, or deemed disposal, of an asset under those rules and the company disposing of the asset falls within the SA capital gains tax net.

3.5 Special deductions and allowances for oil and gas companies

As noted above, the Tenth Schedule to the Income Tax Act provides for specific deductions against oil and gas income which may be claimed by an oil and gas company in determining its taxable income.

Exploration and post-exploration expenditure

The Tenth Schedule provides that, in determining the taxable income of an oil and gas company, all expenditure and losses actually incurred in the tax year in respect of exploration or post-exploration, as defined, shall be allowed as tax deductions from the oil and gas income of that company.

The deduction does not however include expenditure or losses incurred in respect of the acquisition of any oil and gas right (except where specifically allowed where 'participation treatment' has been agreed between the parties – see discussion below).

In respect of expenditure that does not relate to exploration and post-exploration, a tax deduction may be available in accordance with ordinary tax rules.

Expenditure of a capital nature

In addition to claiming a tax deduction for exploration and post-exploration expenditure as detailed above, a further tax deduction may be claimed in respect of exploration and post-exploration expenditure of a capital nature incurred during the tax year. In this regard, the Tenth Schedule allows for a further deduction from oil and gas income of:

- 100% of expenditure of a capital nature actually incurred in the tax year in respect of exploration in terms of an oil and gas right; and

- 50% of expenditure of a capital nature actually incurred in the tax year in respect of post-exploration in terms of an oil and gas right.

Essentially, under the provisions applicable to expenditure of a capital nature, a taxpayer benefits from a 200% super-deduction in respect of expenditure incurred in the exploration of an oil and gas right, and a super-deduction of 150% in respect of expenditure of a capital nature incurred in respect of post-exploration in terms of an oil and gas right. No deduction may be claimed under these provisions in respect of the acquisition of an oil and gas right.

Deemed trade

If a company holds an oil and gas right, it is deemed to be carrying on a trade in respect of that oil and gas right and expenditure and losses incurred by that company in respect of the oil and gas right are deemed to be incurred in the production of income of the company. This ensures that an oil and gas company will be eligible for tax deductions under ordinary tax rules and tax losses will not lapse in circumstances such as a temporary cessation of business.

Decommissioning costs

No tax deduction is available for decommissioning provisions included in the financial statements but instead, a deduction is allowed for cash paid during any year of assessment to a qualifying closure rehabilitation trust or company.

3.6 Losses

There is no period of restriction for the carry forward of losses and in order to preserve the carried forward losses, all that is required is that a company continue its trade (see comments above under deemed trade).

As indicated above, special deductions under the Tenth Schedule to the Income Tax Act are ring-fenced to oil and gas income and income from the refining of gas derived in respect of any oil and gas right held by the company.

In terms of further provisions in the Tenth Schedule, assessed losses in respect of exploration and post-exploration may only be offset against 'oil and gas income' and income from the refining of gas derived in respect of an oil and gas right held by the company, to the extent that the losses do not exceed that income. If any amount remains after offsetting the assessed loss against such income, an amount equal to 10% of the remaining assessed loss may be offset against any other income (i.e. non-oil and gas income, such as investment income). Finally, any losses remaining, after the offset of 10% against other income, must be carried forward to the succeeding year of assessment for offset against 'oil and gas income' and income from the refining of gas.

3.7 Foreign entity taxation

Non-residents are taxed in SA on income that is from a source in SA and are subject to tax on this income on the same basis as residents of SA. Non-residents are subject to capital gains tax in SA in respect of the disposal of immovable property situated in SA (or any interest or right of whatever nature to or in immovable property in SA), or in respect of any asset which is attributable to a permanent establishment of that person in SA.

For the purposes of the above, an interest in immovable property includes any equity shares held by a person in a company, the ownership or the right to ownership in any other entity, or a vested interest of a person in any assets of any trust if 80% or more of the market value of those equity shares at the time of disposal is attributable (directly or indirectly) to immovable property held otherwise than as trading stock, and that person holds (directly or indirectly) at least 20% of the equity shares in that company.

This is subject to the provisions of any applicable double tax agreement.

4.0 Other corporate income tax

4.1 Additional profits taxes

Not applicable.

4.2 State taxation

Not applicable.

5.0 Tax incentives

5.1 Income tax deductions

See Section 3.5 (Expenditure of a capital nature).

5.2 Research and development (R&D)

Under general tax rules, companies may claim a tax deduction equal to 150% in respect of expenditure actually incurred that is directly and solely in respect of research and development ("R&D") in SA if the expenditure is incurred in the production of income and in the carrying on of any trade, and for which pre-approval has been obtained from the authorities.

It should be noted that R&D does not include activities for the purpose of oil and gas exploration. It does however include research and development expenditure incurred to develop technology used for oil and gas exploration.

5.3 Other

Various other tax incentive programs, cash grants and/or other government investment incentives may be applicable, depending on the nature and location of a particular investment. These may include the learnership allowance, as well as the employment tax incentive ("ETI") which are outlined briefly below.

The ETI was implemented in January 2014 and is an incentive aimed at encouraging employers to hire young and less experienced work seekers. The incentive amount differs depending on the salary paid to each qualifying employee and whether the qualifying employee is employed during the first 12 months or second 12 months of the ETI programme.

A tax incentive for registered learnership agreements exists in the form of a learnership allowance that may be claimed as a tax deduction. A learnership agreement is a contract between a learner, an employer and a training provider granting a learner employment and training for a specific amount of time. A learnership allowance may be claimed in the year of assessment during which a recognized learnership agreement has been entered into by the employer with a learner and also where a recognized learnership agreement has been completed by a learner. The learnership allowance available is increased where the learner is a person with a disability (as defined in section 6B of the Income Tax Act).

6.0 Payments to related parties

6.1 Transfer pricing

Transfer pricing provisions contained in Section 31 of the Income Tax Act apply to oil and gas companies in the same manner that these rules apply to other companies. Section 31 requires that cross-border arrangements between connected persons (as defined for the purposes of Section 31) should be on an arm's length basis. The transfer pricing provisions may be applied to, inter alia, transactions between a non-resident and any other person that is not a resident that has a permanent establishment in SA, as well as to transactions between a resident and any other person that is a resident that has a permanent establishment outside SA.

6.2 Thin capitalization

Thin capitalization rules are applied through the application of the general transfer pricing rules and other provisions in the Income Tax Act relating to the deduction of interest (see below).

6.3 Interest deductibility

The deductibility of interest is subject to the normal provisions of the Income Tax Act. New rules came into effect on 1 January 2015 which provide a limitation on the level of interest that can be claimed as a deduction for tax purposes in certain circumstances (for example, in respect of debts owed to persons who are not subject to tax in SA). The interest limitation is essentially 40% of earnings before interest, taxes, depreciation and amortization ("EBITDA"), after taking into account interest received or accrued by the debtor, 40% of the debtors 'adjusted taxable income' and any interest incurred by the debtor not subject to section 23M. 'Adjusted taxable income' is determined before interest income and expenditure, capital allowances, claw-backs and any losses carried forward from the previous year.

7.0 Transactions

7.1 Capital gains

Oil and gas companies are subject to tax on capital gains in the same manner as other companies, however special rules contained in the Tenth Schedule govern the disposal of oil and gas rights. These specific rules are detailed in paragraph 7.2 below.

7.2 Asset disposals

Under provisions in the Tenth Schedule dealing with the disposal of an "oil and gas right", the parties to the disposal may agree in writing that "rollover treatment" or "participation treatment" will apply.

Rollover treatment

This treatment may apply if an oil and gas company disposes of any oil and gas right to another company where the market value of the right exceeds its tax value. If the parties agree to rollover treatment, the selling company is deemed to have sold the right for an amount equal to its tax value. Essentially, under rollover treatment, any tax gain for the selling company at the time of disposal is eliminated and the company acquiring the right is deemed to have acquired it at the selling company's tax value.

Participation treatment

This treatment may apply if an oil and gas company disposes of any oil and gas right to another company where the market value of the right exceeds its tax value. If the parties agree to participation treatment, the selling company effectively treat all gains on the disposal of the oil and gas right as ordinary revenue (regardless of whether the right was held as trading stock or as a capital asset), and will include any gain in its gross income. The company acquiring the oil and gas right may deduct from its oil and gas income an amount equal to the sum included in the seller's gross income. The effect of electing into the participation treatment is that losses arising from oil and gas activities may be effectively transferred from the seller to the purchaser.

8.0 Withholding taxes

8.1 Dividends

The rate of dividends tax on any dividend that is paid by an oil and gas company out of amounts attributable to its oil and gas income is nil. Any dividends paid by an oil and gas company out of amounts attributable to income other than oil and gas income, will be subject to dividends tax at the standard rate (currently 15%). The rate is subject to reduction under any applicable double taxation agreement.

8.2 Interest

From 1 March 2015, withholding taxes on cross-border interest payments came into effect at the rate of 15%. This rate is subject to reduction under any applicable double tax agreement and is nil in respect of interest paid on loans applied to fund capital expenditure in respect of exploration or post-exploration.

8.3 Royalties

The Income Tax Act provides that withholding tax at the rate of 15% is applicable to any royalties paid to non-residents in respect of intellectual property used in SA. As noted above, the rate of withholding tax on royalties, which is subject to reduction under any applicable double tax agreement, increased to 15% from 12% with effect from 1 January 2015.

8.4 Services

Currently, no withholding taxes exist with regard to cross-border service fees, but it is proposed to come into effect at the rate of 15% with effect from 1 January 2017. This rate will be subject to reduction under any applicable double tax agreement.

8.5 Other

A withholding tax is levied on amounts payable to non-resident sellers of immovable property (which may include an oil and gas right, or shares in a company that holds an oil and gas right). This withholding tax is levied at the rate of 7.5% where the seller is a company, and constitutes an advance payment in respect of the seller's liability for normal tax in SA. The provisions of a double tax treaty may apply.

8.6 Tax treaties

SA has an extensive network of double tax treaties with other jurisdictions which determine the circumstances in which SA has taxing rights, and allow for a reduction in withholding tax rates in many cases. Certain treaties have specific clauses dealing with oil and gas activities.

9.0 Indirect taxes

9.1 Value-added tax

VAT issues relating to oil and gas companies are relatively complex and the following is a brief overview of some key features.

Subject to certain exemptions and provisions for the zero-rating of certain supplies, VAT is levied at a rate of 14% on the value of the supply of goods or services by a vendor in the course of an enterprise carried on by that vendor.

VAT is levied on the importation of goods, subject to certain exceptions, such as the exemption from VAT of imported petroleum oil and crude oil imported for the purposes of being refined. An exemption from VAT on importation also applies in respect of the importation of goods for use in petroleum exploration and production activities.

With regard to oil and gas companies, the supply of petroleum oil and crude oil for the purposes of being refined for the production of fuel levy goods constitutes a zero-rated supply. The zero-rating also applies to the supply of fuel levy goods which includes:

- Petrol as defined in Part 1 of Schedule No.1 to the Customs and Excise Act;
- Distillate fuel defined in Part 1 of Schedule No.1 to the Customs and Excise Act; and
- Biodiesel

Subject to certain exceptions, VAT incurred in respect of goods or services used by the vendor in the course of making taxable supplies may be claimed as an input tax credit.

9.2 Import, export, and customs duties

Customs duty and VAT (at 14%, 0% or exempt) is due on importation of goods into the Southern African Customs Union (“SACU”) from outside of SACU.

SACU is comprised of Botswana, Lesotho, Namibia, Swaziland and the RSA.

The following trade agreements offer preferential rates of customs duty on importation into SACU:

- European Union
- EFTA[1]
- SADC[2]

There are no customs duties on crude oil, but there is customs duty on refined products (petrol and diesel), certain blend stocks and lubricants.

Import and export permits from the Department of Energy on all petroleum products, including crude and most blend stock, are required in order to import or export these products into or out of South Africa.

A wholesale distribution license is also required from the Department of Energy to sell and distribute fuel within SA.

Rebates are in place to claim back or offset duties on refined product that has been:

- Exported outside of SACU;
- Removed to a neighbouring SACU state (all duties except customs and excise duties);
- Product marked at a licensed marking warehouse.

[1] EFTA comprises: Iceland, Liechtenstein, Norway, and Switzerland

[2] SADC 15 member states: Angola; Botswana; Democratic Republic of the Congo; Lesotho; Madagascar – membership reinstated on 30 January 2014; Malawi; Mauritius; Mozambique; Namibia; Seychelles; South Africa; Swaziland; Tanzania; Zambia and Zimbabwe

In addition, rebates on customs duty may be claimed in respect of certain goods imported by a person who explores for petroleum or produces petroleum for use in the manufacture of any equipment, installation or device, for use solely in operations in connection with the exploration for, or production of petroleum.

Export claims may only be made by licensed distributors or licensed manufacturers.

9.3 Excise and other petroleum taxes

Refined products (petrol and diesel) are subject to duties at source ("DAS"). Certain related products, such as Aviation Kerosene and Illuminating Kerosene, are strictly regulated and may be subject to DAS on non-compliance.

There is no DAS on crude oil.

DAS is levied on imports or removal from a manufacturing warehouse (refinery). Imports into licensed manufacturing warehouses may suspend payment of the DAS levies until the goods are removed from the manufacturing warehouse. At present, no import and export bond facilities exist for fuel levy goods, but the legislation does provide for import and export specific bond storage facilities.

In SA, DAS levies are administered and payable to the South African Revenue Service and comprise:

- Excise duty;
- Fuel levy; and
- Road Accident Fund levy.

Further duties payable to the Central Energy Fund on refined products include:

- Slate levy – A self-adjusting mechanism varying month to month in order to smooth out fuel prices;
- Petroleum Products levy;
- Illuminating Paraffin Tracer levy;
- Inland Incremental Recovery levy (recently repealed); and
- A demand-side levy based on high octane sales to inland retail outlets, in order to persuade inland consumers to use low octane fuels.

Illuminating kerosene (marked) or aliphatic hydrocarbon solvents (marked or sold to permit holders) do not attract any DAS levies, but are strictly regulated.

9.4 Stamp tax

Securities transfer tax ("STT") is payable at the rate of 0.25% on the transfer or cancellation of any listed or unlisted security in SA.

9.5 Employment taxes

Employment taxes comprise Pay-As-You-Earn ("PAYE"), Unemployment Insurance Fund ("UIF") contributions and Skills Development Levies ("SDL").

PAYE refers to the tax required to be deducted by an employer from an employee's remuneration, both paid and payable.

UIF provides short-term relief to workers when they become unemployed or are unable to work because of maternity or adoption leave or illness. An employer and employee must each contribute 1% of the employee's remuneration as does not exceed certain prescribed limits (currently South African Rand ("ZAR") 14,872 per month or ZAR178,464 annually). UIF is not payable where an employee has entered SA for the purposes of carrying out a contract of service, apprenticeship or learnership, if upon termination thereof the employer is required by law or by agreement to repatriate that person, or if the person is required to leave SA.

SDLs are imposed to promote learning and development in SA and are calculated with reference to the employer's remuneration bill (calculated as 1% of remuneration). Employers with an annual payroll (as calculated for PAYE purposes) of less than ZAR500,000 are exempt from paying SDL.

Employment taxes are generally payable on a monthly basis but other payment intervals could also potentially apply depending on the specific circumstances.

10.0 Other

10.1 Choice of business entity

The principal methods of doing business in SA are by using a:

- Company (public or private) incorporated under the Companies Act No. 71 of 2008
- Personal liability company
- Partnership
- Business Trust
- Sole Proprietorship
- External company (branch of a foreign company)

The tax consequences differ for each of the entity types listed above, however the most common form used is that of a company. Companies and personal liability companies are taxed at a corporate income tax rate of 28%, whilst partnerships and sole proprietorships are not viewed as separate legal entities for tax purposes, and the individual partners/business owners are taxed on their share of the business's taxable income on a sliding scale with a maximum marginal rate of 40%. Business trusts are taxed at a rate of 40% and branches of a foreign company are taxed at a rate of 28% of taxable income.

The legislative and administrative requirements for each of the business entities also differ, with the requirements for companies (specifically public companies) being the most onerous. External companies are exempt from certain administrative and legislative requirements in terms of the Companies Act and this often proves a popular choice for foreign companies operating in SA.

10.2 Foreign currency

In terms of the Tenth Schedule to the Income Tax Act, currency gains or losses of an oil and gas company (regardless of whether those gains or losses are realized or unrealized) must be determined solely with reference to the functional currency of that company and the translation method used by that company for financial reporting purposes (the 'functional currency' is the currency of the primary economic environment in which the business is conducted).

As a result, dollar-based oil and gas companies can use the dollar as their base currency for determining currency gains and losses for tax purposes. Furthermore, any amounts received by, or accrued to, or expenditure incurred by an oil and gas company in a currency other than that of SA, must be determined in the functional currency of the company and must be translated to the currency of SA by applying the average exchange rate for the tax year.

10.3 Fiscal stability

Under the Tenth Schedule, the Minister of Finance may enter into fiscal stability agreements with any oil and gas company in respect of an oil and gas right held by that company. The fiscal stability agreement will guarantee that the provisions of the Tenth Schedule as at the date on which the agreement was concluded will apply for the duration of the period that the right is held by the company.

The Minister of Finance may also enter into a fiscal stability agreement with any company in anticipation of an oil and gas right being acquired by that company, provided that the fiscal stability agreement will have no force or effect if the oil and gas right to which the agreement relates is not granted within one year after the agreement is concluded. The fiscal stability agreement will guarantee that the provisions of the Tenth Schedule, as at the date on which the oil and gas right is granted, will apply for the duration of the period that the right is held by the company.

Fiscal stability rights may be assigned as part of the disposal of an exploration or production right. In the case of a production right, the assignee forms part of the same group of companies as the assignor at the time the agreement is concluded. If a company holding a participating interest in an oil and gas right has concluded a fiscal stability agreement, the terms and conditions of that agreement will apply to all participating interests subsequently held by that company in that oil and gas right. Oil and gas companies are permitted to rescind a fiscal stability agreement unilaterally with effect from the commencement of the year of assessment immediately following the notification date of the termination.

10.4 Exchange Controls

Exchange control is administered by the South African Reserve Bank ("SARB") which has delegated powers to Authorized Dealers (banks licensed to deal in foreign exchange). SA does not impose exchange controls on non-residents but exercises exchange controls over residents and transactions entered into between residents and non-residents. For exchange control purposes, a "resident" is a person (natural person or legal entity) which has taken up residence, is domiciled or registered in SA and includes external companies (branches of foreign companies).

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12.0 Appendix 1

Sources:

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- Oanda (http://www.oanda.com/currency/converter/)
- US Energy Information Administration (http://www.eia.gov/countries/cab.cfm?fips=sf)

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