

## THE FIFTH SCHEDULE

(See Section 100)

### PART I

#### RULES FOR THE COMPUTATION OF THE PROFITS AND GAINS FROM THE EXPLORATION AND PRODUCTION OF PETROLEUM

##### Exploration and Production of Petroleum a Separate Business

1. Where any person carries on, or is treated as carrying on, under an agreement with the Federal Government, any business which consists of, or includes, the exploration or production of petroleum in Pakistan or setting up refineries at Dhodak and Bobi fields, income of exploration and production companies from pipeline operations, and manufacture and sale of liquified petroleum gas or compressed natural gas, such business or part thereof, as the case may be, shall be, for the purposes of this Ordinance, treated as a separate business undertaking (hereinafter referred to as "such undertaking") and the profits and gains of such undertaking shall be computed separately from the income, profits, or gains from any other business, if any, carried on by the person.

##### Computation of Profits

2. (1) Subject to the provisions of this Part, the profits and gains of such undertaking are computed in the manner applicable to income, profits and gains chargeable under the head "Income from Business".
  - (2) Where such person incurs any expenditure on searching for or discovering and testing a petroleum deposit or winning access thereto but the search, exploration, enquiry upon which the expenditure is incurred is given up before the commencement of commercial production, the expenditure allocable to a surrendered area or to the drilling of a dry-hole shall be treated as lost at the time of the surrender of the area or the completion of the dry-hole, as the case may be.
  - (3) Where the agreement provides that any portion of the expenditure is treated as lost under sub-rule (2) (hereinafter referred to as the "said loss") and is allowed against any income of such undertaking, it shall be allowed in either of the following ways as may be provided for in the agreement, namely:—
    - (a) The said loss in any year shall be set off against the income of that year chargeable under the head "Income from Business" or any income (other than income from dividends) chargeable under any other head and where the loss cannot be wholly set off in this manner the portion not so set off shall be carried forward to the following year and set off in the same manner and so on, but no loss shall be carried forward for more than six years; or

- (b) the said loss in any year shall be set off against the income of such undertaking of the tax year in which commercial production has commenced and where the loss cannot be wholly set off against the income of such undertaking of that year, the portion not set off against the income, if any, of such undertaking of that year, and if it cannot be wholly so set off the amount of loss not so set off shall be carried forward to the following year, and so on, but no loss shall be carried forward for more than ten years.
- (4) After the commencement of commercial production, all expenditure incurred prior thereto and not deemed to be lost under sub-rule (2) and not represented by physical assets in use at the time the commercial production shall be allowed as a deduction, so, however, that the portion of such deduction to be so allowed in any year shall be such amount not exceeding ten per cent of the aggregate amount deductible in respect of inshore areas, and not exceeding twenty five per cent for offshore areas, as may be selected by the taxpayer.
- (5) Any expenditure, including a royalty paid to the Federal Government by an onshore petroleum exploration and production undertaking on, or after, the first day of July 2001 (not being in the nature of capital expenditure or personal expenses of the taxpayer) laid out or expended after the commencement of commercial production wholly and exclusively for the purpose of the business of production and exploration of petroleum carried on by such undertaking shall be allowed as a deduction, provided that –
  - (a) no deduction shall be allowed in respect of such expenditure incurred in the acquisition of depreciable assets to which section 22 applies or in the acquisition of an intangible to which section 24 applies;
  - (b) sections 22, 23 and 24 apply in respect of assets referred to in clause (a);
  - (c) a depreciation deduction shall also be allowed under section 22 in respect of such expenditure incurred on the acquisition of the physical assets acquired before the commencement of commercial production and were being used by such undertaking on and after that date, as if such assets had been acquired at the time of the commencement of commercial production at their original cost, as reduced by the amount of depreciation deduction, if any, previously allowed to be deducted under this Ordinance.
- (6) If, in any year, the deductions allowed Part IV of Chapter III and sub-rules (3) and (4) exceed the gross receipts from the sale of petroleum produced in Pakistan, such excess shall be set off against other income (not being dividends) and carried forward in the manner and subject to the limitations in section 57, so however that no portion of such excess shall be carried forward for more than six years.

- (7) The limitation of six years specified in sub-section (6) shall not apply to depreciation allowed to a person carrying on the business of offshore petroleum exploration and production, in respect of any machinery, plant or other equipment used in such exploration or production.
- (8) For the purposes of section 22, where any asset used by a person in the exploration and production of petroleum is exported or transferred out of Pakistan, the person shall be treated as having made a disposal of the asset for a consideration received equal to the cost of the asset as reduced by any depreciation deductions allowed under this Ordinance (other than an initial allowance under section 23).

### **Depletion Allowance**

3. In determining the income of such undertaking for any year ending after the date on which commercial production has commenced, an allowance for depletion shall be made equal to fifteen per cent of the gross receipts representing the well-head value of the production, but not exceeding fifty per cent of the profits or gains of such undertaking before the deduction of such allowance.

### **Limitation on Payment to Federal Government and Taxes**

4. (1) The aggregate of the taxes on income and other payments excluding a royalty as specified in the Pakistan Petroleum (Production) Rules, 1949 or the Pakistan Petroleum (Exploration and Production) Rules, 1986 and paid by an onshore petroleum and production undertaking on, or after, the first day of July 2001 to the Government in respect of the profits or gains derived from such undertaking for a tax year shall not exceed the limits provided for in the agreement, provided the aggregate is not less than fifty per cent of the profits or gains derived by an onshore petroleum exploration and production undertaking and forty per cent of the profits or gains derived by an offshore petroleum exploration and production undertaking, before deduction of the payment to the Federal Government.
- (2) In respect of any tax year commencing on, or after, the first day of July, 2002, the aggregate referred to in sub-clause (1) shall not be less than forty per cent of the profit or gains derived by an onshore petroleum exploration and production undertaking before the deduction of payment excluding royalty paid by an onshore company to the Federal Government.
- (3) If, in respect of any tax year, the aggregate of the taxes on income and payments to the Federal Government is greater or less than the amount provided for in the agreement, an additional tax shall be payable by the taxpayer, or an abatement of tax shall be allowed to the taxpayer, as the case may be, so as to make the aggregate of the taxes on income and payments to the Federal Government equal to the amount provided for in the agreement.

- (4) If, in respect of any year, the payments to the Federal Government exceed the amount provided for in the agreement, so much of the excess as consists of any tax or levy referred to in sub-clause (b) of clause (3) of rule 6 shall be carried forward and treated, for the purposes of this rule, as payments to the Federal Government for the succeeding year, provided that the whole of the payments to the Federal Government exceeding the amount provided for in such agreement may be carried forward if so provided for in any agreement with a taxpayer made before the first day of 1970.

### **Provision Relating to Rules**

5. The Central Board of Revenue may make rules for the purposes of any matter connected with, or incidental to the operation of this Part.

### **Definitions**

6. In this Part, –
  - (1) “agreement” means an agreement entered into between the Federal Government and a taxpayer for the exploration and production of petroleum in Pakistan;
  - (2) “commercial production” means production as determined by the Federal Government;
  - (3) “payments to the Federal Government” means amounts payable to the Federal Government or to any Federal Governmental authority in Pakistan –
    - (a) in respect of royalties as specified in the Pakistan Petroleum (Production) Rules, 1949, or the Pakistan Petroleum (Exploration and Production) Rules, 1986; and
    - (b) in respect of any tax or levy imposed in Pakistan peculiarly applicable to oil production or to extractive industries or any of them and not generally imposed upon all industrial and commercial activities;
  - (4) “petroleum” means crude oil, natural gas, and case-head petroleum spirits as defined in the Pakistan Petroleum (Production) Rules, 1949, or the Pakistan Petroleum (Exploration and Production) Rules, 1986, but does not include refined petroleum products;
  - (5) “surrender” means the termination of rights with respect to an area including the expiration of rights according to the terms of an agreement;
  - (6) “surrendered area” means an area with respect to which the rights of the person have terminated by surrender or by assignment or by termination of the business;

- (7) "Taxes on income" and "tax" includes income tax, but does not include payments to the Federal Government; and
- (8) "well-head value" shall have the meaning assigned to it in the agreement between the Federal Government and the taxpayer, and in the absence of any such definition in the agreement, the meaning assigned to it in the Pakistan Petroleum (Production) Rules, 1949, or the Pakistan Petroleum (Exploration and Production) Rules, 1986.

*(Section 100)*

**OIL, NATURAL GAS AND OTHER MINERAL DEPOSITS**

**Special provisions relating to the production of oil and natural gas, and exploration and extraction of other mineral deposits.-**

- (1) Subject to sub-section (2), the profits and gains from –
  - (a) the exploration and production of petroleum including natural gas and from refineries set up at the Dhodak and Bobi fields;
  - (b) the pipeline operations of exploration and production companies; or
  - (c) the manufacture and sale of liquified petroleum gas or compressed natural gas,

and the tax payable thereon shall be computed in accordance with the rules in Part I of the Fifth Schedule.

- (2) Sub-section (1) shall not apply to the profits and gains attributable to the production of petroleum including natural gas discovered before the 24th day of September, 1954.
- (3) The profits and gains of any business which consists of, or includes, the exploration and extraction of such mineral deposits of a wasting nature (not being petroleum or natural gas) as may be specified in this behalf by the Federal Government carried on by a person in Pakistan shall be computed in accordance with the rules in Part II of the Fifth Schedule.