

# Timor-Leste (formerly East Timor) Tax and Investment Guide 2009



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PRICEWATERHOUSECOOPERS 

## A Summary of Timor-Leste Taxation and Investment

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The information in this booklet is based on current taxation and investment rules and practices including legislative proposals and measures as at 30 June 2009.

This booklet is intended as a general guide and not as specific advice to any party. Where specific transactions are being contemplated, definitive advice should be sought.

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# Overview



# Snapshot

Population	1.06m (2007)
Capital	Dili
Geography - size	18,900 km <sup>2</sup> (approx), Located in the Eastern portion of the Indonesian archipelago.
Official Currency	US Dollar
GDP per capita (Non-oil)	\$US 378 (2007)
Total GDP (Non-oil)	\$US 395.5m (2007)
GDP Growth (Annual)	7.8% (2007)
Consumer Price Index	8.9% (2006/07 est.)
Total Government Non-Oil Revenues	\$US 40.5m (2006/07)
Total Government Oil Revenues	\$US 993.1m (2006/07)
Total Government Expenditure (Cash Basis)	\$US 180.5m (2006/07)
Imports:	\$US 370m (2007 est.)
Exports:	\$US 43m (2007 est.)
Key Industries (Non-oil) Income	<ul style="list-style-type: none"><li>- Agriculture, forestry, and fishery (\$US 124.7 m)</li><li>- Industry and services (\$US 126.8 m)</li><li>- Public sector (\$US 201.8m). (2007 est.)</li></ul>
Oil & Gas Income	\$US 1,309m (2007 est.)
Official Languages:	Portuguese and Tetum (over 30 different languages or dialects are spoken by Timor-Leste's various cultural groups). English and Indonesian are also used in government and business.
Ethnicity:	Eastern Tetum (Belu) (45%), Mambai (Damata) 11%, Galolo (7%), Timorese (Vaikino) 7%, others (30%).
Religions:	Roman Catholics (98%), Islam (1%), and Protestant (1%)

Sources: World Development Indicators database, The World Bank; International Monetary Fund Country Report No.08/2003

# Overview

In recent times, Timor-Leste has undergone significant political and social change. Since the production of our previous Timor-Leste Tax Book 2005 the taxation and investment environment has evolved considerably. To understand the investment and taxation regimes applicable to Timor-Leste today it is important to understand some of this evolutionary process.

## Political and Social

### Historical

Beginning with Portuguese and Dutch traders in the early 16th Century, the island state of Timor-Leste (until recently known as East Timor) has been under various forms of foreign influence until its recent transformation to an independent democratic republic commencing in 1999 (see below).

From around 1515 until the Second World War, Timor-Leste was a Portuguese colony. Japan assumed control of the island region from 1942 – 1945. Portugal however reassumed control over Timor-Leste at the end of WWII, until a coup in Lisbon in April 1974, led to the break-up of many Portuguese colonial territories.

Independence movements gained momentum and on 11 August 1975, conservative parties launched a coup in Dili to prevent the ascendancy of the left-wing Frente Revolucionária do Timor-Leste Independente (Fretilin). On 28 November 1975, Fretilin declared Timor-Leste an independent republic. However, on 7 December 1975, Indonesia assumed control of Timor-Leste.

### Indonesian era

From 1975 to 1997 Timor-Leste's economic progress was largely unknown (although during the period from 1983 – 1997 annual growth was reported to be an estimated 6%).

The late 1990's saw the onset of the Asian financial crises and the resignation of Indonesia's President Suharto. On 27 January 1999, the new President of Indonesia Dr BJ Habibie announced a Plebiscite on East Timorese independence. In May 1999, an agreement was reached under the auspices of the UN to begin the process towards such a vote. On 30 August 1999, the East Timorese voted in favor of independence with a 78% majority.

## Timor-Leste Independence

With the 30 August 1999 Plebiscite, Timor-Leste elected to “begin a process of transition towards independence”. On 25 October 1999, the United Nations’ Security Council issued Resolution 1272 pursuant to which effective authority for the administrative of Timor-Leste was transferred to the “United Nations’ Transitional Administration in East Timor” (“UNTAET”) headed by “the Special Representative of the Secretary General”. This transfer included all legislative, judicial and executive authority.

On 30 August 2001, elections for Timor-Leste’s first “Constituent Assembly” took place. Fretilin won 55 of the 85 available seats. Timor-Leste adopted a unicameral system of parliament with key executive authority resting with the Prime Minister. Whilst the President retains certain powers of veto, the role is largely ceremonial.

On 14 April 2002, elections for Timor-Leste’s first President took place. Xanana Gusmão was elected with an 85% majority and on 20 May 2002 was sworn in as Timor-Leste’s first President. Full administrative authority also passed from the UNTAET to the newly established Timor-Leste Government led by Mari Alkatiri as Prime Minister. On the same day, a new Timor Sea Treaty was agreed between Timor-Leste and Australia (see below).

The post 2002 period however included periods of civil disturbance. In May 2006, the government requested Australian led peacekeepers to enter the country to help restore order.

On 26 June 2006, Mari Alkatiri resigned as Prime Minister and was replaced by his then Foreign Minister, Josè Ramos-Horta on 10 July 2006.

In the lead-up to the 2007 elections, President Gusmão announced that he would not seek a second term as President. Josè Ramos-Horta resigned as Prime Minister to run as a Presidential candidate. On May 20, 2007 Josè Ramos-Horta was elected as Timor-Leste’s second President.

Estanislau da Silva succeeded Josè Ramos-Horta as interim Prime Minister in the lead up to the subsequent parliamentary elections.

On 30 June 2007, Parliamentary elections took place and whilst Fretilin won the most seats no individual party could form government. On 6 August 2007, President Ramos-Horta asked Xanana Gusmão to lead a coalition (the Alliance with a Parliamentary Majority or AMP) to form a government. Xanana Gusmão was sworn in as Prime Minister on 8 August 2007. He remained as Prime Minister as at the date of this publication.

On 11 February 2008, Ramos-Horta was injured when he was shot during an assassination attempt. After a successful recovery he remained as President as at the date of this publication.

## Legal and Taxation

**IMPORTANT:** Whilst Timor-Leste has recently embarked upon a process of taxation reform, four separately distinguishable taxation regimes exists for Timor-Leste's sovereign territory and areas identified in the Timor Sea Treaty. Please refer to Appendix B – "Tax Regime Matrix" for a summary on the application of each regime.

From a taxation point of view, Timor-Leste fell under the umbrella of Indonesia's tax regime from 1975.

On 27 November 1999, UNTAET issued Regulation 1999/1. Regulation 1999/1 provided that all laws applying in Timor-Leste prior to 25 October 1999 (i.e. Indonesian Law) should continue to apply until replaced by the UNTAET or subsequently established democratic institutions. Regulation 1999/1 had application from 25 October 1999.

On 8 March 2000, UNTAET issued Regulation 2000/12 entitled a "Provisional Tax and Customs' Regime for East Timor". Regulation 2000/12 was transitional in nature and levied an excise on the import, domestic production and the export of certain goods. Regulation 2000/12 had application from 8 March 2000.

On 20 December 2000, UNTAET issued Regulation 2000/18 entitled "A Revenue System for East Timor". Regulation 2000/18 (as amended by the Revenue System Amendment Act 2002) provided the basis for Timor-Leste's first comprehensive taxation regime (other than for the area covered by the Timor Sea Treaty-see Part B). Particularly in regard to Income Tax, Regulation

2000/18 largely adopted the Indonesian Tax Law then in place, but with specified modifications. Regulation 2000/18 had general application from 1 July 2000, although certain Income Tax amendments applied from 25 October 1999.

## Current taxation regime

On 25 June 2008, the Timor-Leste parliament passed the Taxes and Duties Act (Law No.: 8/2008) (the “TDA”). The TDA has effect from 1 January 2008 for annual taxes and from 1 July 2008 for all other taxes. The TDA applies to the territory of Timor-Leste including the JPDA (except for the Bayu-Undan and Greater Sunrise areas).

The TDA repealed UNTAET Regulation 2000/18, UNTAET Directive No. 2001/2 (and the Petroleum Tax Act) to provide a single framework for the imposition of tax in Timor-Leste (subject to the overlay of the Timor Sea Treaty). However, the TDA did not repeal the legal regime applicable for the collection and recovery of tax, for tax offences and for sanctions.

Significant features of the TDA include:

- i) a reduction in the tax rate for legal persons and for non-resident persons from 30% to 10%;
- ii) a reduction in the maximum Wage Income Tax rate for resident natural persons from 30% to 10%;
- iii) the removal of the “minimum income tax” for business enterprises;
- iv) the removal of the entitlement to interest deductibility (unless incurred by a financial institution);
- v) the upfront deductibility of business inputs. This extends to all capital items including buildings (but excluding land) and trading stock which may be depreciated at 100% during the year of acquisition;
- vi) the indefinite carry forward of tax losses;
- vii) reductions in the rates of Import Duty (from 6% to 2.5%); and
- viii) reductions in the rates of Sales Tax on imported goods (from 6% to 2.5%).

# Oil & Gas Activities

## Timor Sea - Historical

The Timor Sea area has been known to be rich in hydrocarbon deposits for many years. Rights in regard to the exploration and exploitation of these hydrocarbons have been the subject of contention between Australia and, depending upon the era, Indonesia, Timor-Leste or even Portugal, as the case may be. The contention has largely related to the delineation of the seabed boundary between Australia to the South and the relevant state to the North.

An initial Treaty was concluded between Australia and Indonesia in 1972. However the legality of this treaty was challenged at the time, particularly by Portugal who had issued competing exploration permits.

In 1989 Australia and Indonesia agreed to jointly share in the exploitation of the disputed geographical area known as Zone A (i.e. “Zone of Cooperation – A” or “ZOCA”). The so-called Timor Gap Treaty was thereby signed on 11 December 1989 and became operative from 9 February 1991. Essentially, the Timor Gap Treaty provided as follows:

- i) that “ZOCA” shall fall under the joint control of both Indonesia and Australia with equal sharing in the associated petroleum resources. This control was exercised by a “Joint Authority” containing representation from both countries;
- ii) that exploration and exploitation activities in ZOCA were to be carried out pursuant to “production sharing contracts” (“PSC”) entered into between the Joint Authority and the oil company in question;
- iii) that ZOCA should be considered to be within the taxation jurisdictions of both Indonesia and Australia;
- iv) that the business profits or losses of an entity carrying on business in ZOCA shall be taxable in both Indonesia and Australia, after being reduced by 50%. This effectively meant that the respective tax rates of Indonesia and Australia were halved; and
- v) that the remuneration income of an individual resident in Indonesia or Australia, arising from activities in ZOCA, shall be taxable only in the country of residence. Remuneration of third country nationals was taxable in both Indonesia and Australia with an entitlement to a 50% rebate in each country.

With the formal transfer of administration of Timor-Leste to the UNTAET on

25 October 1999 an exchange of notes took place between the UNTAET and Australia on 10 February 2000. Under the notes, the UNTAET assumed all rights and obligations under the Timor Gap Treaty on behalf of Timor-Leste, but only until the date of Timor-Leste's full independence.

On 20 May 2002, full administrative authority for Timor-Leste passed from the UNTAET to the new Timor-Leste Government. On the same day, representatives of the Governments of Timor-Leste and Australia entered into the Timor Sea Treaty (as a successor to the Timor Gap Treaty). Ratification of this treaty was completed by both Governments on 2 April 2003 but with effect from 20 May 2002.

## Timor Sea Treaty

The Timor Sea Treaty provides as follows:

- i) that the Joint Petroleum Development Area ("JPDA") (formerly known as ZOCA), falls under the joint control and management of Timor-Leste and Australia. For the first three years (unless extended by mutual agreement) this should be exercised by a "designated authority" (note from 1 July 2008 this responsibility passed to the Autoridade Nacional do Petróleo ("ANP"));
- ii) that the JPDA includes all of the reserves constituting the Bayu-Undan field. However, the JPDA covers only 20.1% of the reserves making up the Greater Sunrise field (see Part D for specific regimes);
- iii) that petroleum activities, covering exploration, development, processing, transportation and marketing of hydrocarbons, are to be carried out pursuant to a contract between the designated authority and the oil company in question;
- iv) that the JPDA is considered to be within the taxation jurisdiction of both Timor-Leste and Australia;
- v) that the business profits or losses of an entity carrying on business in the JPDA are reduced by the "reduction percentage". For Timor-Leste the reduction percentage is 10% while for Australia it is 90%. This effectively means that the tax rates in Timor-Leste and Australia are at 90% and 10% of their normal levels; and
- vi) that the remuneration income of an individual resident in Timor-Leste or Australia arising from activities in the JPDA is taxable in both Timor-Leste and Australia, subject to the 10%/90% reduction percentage.

With the ratification of the Timor Sea Treaty, Timor-Leste continued to maintain geographically distinct taxation regimes. One for Timor-Leste

generally and the other covering the area now known under the Timor Sea Treaty as the JPDA (previously ZOCA).

## Bayu-Undan and Greater Sunrise areas

Annex F of the Timor Sea Treaty separately identified four Production Sharing Contracts ("PSCs") for specific fiscal treatment. These PSCs cover the discoveries known as Bayu-Undan and Greater Sunrise. The treaty preserved the taxation regime applicable to these areas to that in place immediately prior to the transfer of sovereignty to the UNTAET (i.e. 25 October 1999). Subsequent agreements and legislation have been introduced dealing with these particular fields (see Part D for details).

### Bayu-Undan

On 6 June 2003, the Timor-Leste Government issued:

- i) the Taxation of Bayu-Undan Contractors Act ("ToBUCA"); and
- ii) the Timor Sea Petroleum Development (Tax Stability) Act.

The ToBUCA relates to the taxation of petroleum contractors and subcontractors operating pursuant to the Bayu-Undan LNG project carried out within PSCs JPDA 03-12 and JPDA 03-13. The ToBUCA arrangements specifically exclude the EKKN fields.

### Greater Sunrise

Arrangements dealing with the Greater Sunrise contract area (PSCs 03-19 and 03-20) which straddles the waters of the JPDA and waters claimed exclusively by both Timor-Leste and Australia, have been the subject of controversy for a number of years (noting that only 20.1% of the field lies within the JPDA).

On 6 March 2003, Australia and Timor-Leste entered into the Unitisation of the Greater Sunrise Fields Agreement ("Sunrise IUA"). The Sunrise IUA provides for the unitisation and apportionment of petroleum production from the area 79.9% to Australia exclusively and 20.1% to the JPDA.

On 12 January 2006, the Treaty on Certain Maritime Arrangements in the Timor Sea ("CMATS") was agreed between Timor-Leste and Australia. CMATS came into force on 23 February 2007 and provides that revenues from the area shall be shared equally between Timor-Leste and Australia. CMATS does not however, disturb the taxation calculation under the Sunrise IUA (see

Part D for details on the calculation method).

Aside from the provisions for the Greater Sunrise area, CMATS also extends the duration of the Timor Sea Treaty to a maximum of 50 years (previously 30 years) and provides for a moratorium in relation to the disputed permanent maritime boundary.

## Recent Developments

Until recently, oil and gas activities in Timor-Leste have been limited to the JPDA. On 13 July 2005, Timor-Leste introduced its first sovereign laws in relation to Petroleum Operations encompassing the JPDA and its exclusive territories. These were:

- i) the Petroleum Tax Law (Law No.8/2005);
- ii) the Petroleum Act (Law No.13/2005); and
- iii) the Petroleum Fund Law (Law No.9/2005).\*

These laws provided a revised legal and taxation framework for all Petroleum Operations in Timor-Leste including the JPDA (non-Annex F – see above). As previously noted, the Petroleum Tax Act has since been repealed by the TDA. The other two legislative frameworks remain in place.

In 2006, Timor-Leste conducted an inaugural offshore bid round for its sovereign territory. A total of six PSCs were awarded - five to ENI and one PSC to Reliance Industries (please see Appendices C & D for PSC details).

\* The Timor-Leste Petroleum Fund was established to invest proceeds from Petroleum Operations in Timor-Leste for the long-term future development of the nation. As at April 2009, the Fund's estimated worth was \$US 4.5 b, adding \$US 150 – \$US 200m per month (Source: Forbes Asia, April 2009).

## Investment Overview

### Historical

From 25 October 1999 to 2004 Timor-Leste had no comprehensive commercial or investment framework (outside of the JPDA). Most investment was carried on through unincorporated arrangements or through branches of foreign entities.

During 2004 and 2005, Timor-Leste introduced the:

- i) Law on Commercial Companies (Law No. 4/2004);
- ii) the Law on Domestic Investment (Law No. 4/2005); and
- iii) the Law on External Investment (Law No. 5/2005).

## Law on Commercial Companies

The Law on Commercial Companies provides that “commercial companies” include any general partnership, limited partnership, limited liability company or joint stock company. It provides for internationally recognisable concepts such as:

- i) a distinct and separate legal personality upon the filing of a Memorandum of Association;
- ii) the requirement for ordinary and extraordinary general meetings;
- iii) paid-up capital requirements;
- iv) profit participation and voting rights of shareholders;
- v) the requirement to maintain a registered office;
- vi) requirements for directors (including the obligation for at least one director to reside in Timor-Leste) and their corresponding obligations including fiduciary duties; and
- vii) the requirement to have a company secretary and an auditing body in certain circumstances.

## Company Registration Process

In addition to the abovementioned Commercial and Investment framework, the Business Registration Code (Decree Law No. 6/2007) provides the mechanics for business registration (please see Appendix E on the requirements for establishing a Timor-Leste limited liability company):

## Law on External Investment

The Law on External Investment is aimed at promoting foreign investment in Timor-Leste\* (except in relation to petroleum activities). Key features of the Law include:

- i) a minimum investment of \$US100,000 to obtain certain concessions granted under the law;

- ii) the equal treatment of foreign and national investors including guarantees on the right to the private ownership of assets/title to property;
- iii) the right to employ foreign workers. However an external investor is also obliged to employ Timorese and promote their vocational training and technical skills;
- iv) a tax credit of \$US300 for every permanent Timorese worker during the first five years of business (and up to 15 years for projects of national interest e.g. infrastructure projects);
- v) an exemption from tax on reinvested dividends related to the periods of tax credit (as above);
- vi) import duty and tax exemptions for the import of certain capital assets;
- vii) import duty and tax exemptions for fuel (except petrol) used for the production of electric power where no public supply of power is available;
- viii) rental concessions for leases of State buildings in rural areas;
- ix) a potential special investment agreement/special legal regime for activities of national interest; and
- x) the authorisation and registration requirements for external investors to ensure investment is in accordance with the objectives of the National Development Plan.

\*Potential investors should seek professional advice on the eligibility for the abovementioned concessions.

# Part A - General Taxation Law



# Income Tax

## Background

### **IMPORTANT: SCOPE OF PART A**

This Part A focuses on the application of the TDA to non-Petroleum Operations in the exclusive territory of Timor-Leste (i.e. excluding the JPDA). Please see Part B for the taxation of Petroleum Operations, Part C for the modifications applicable to the JPDA and Part D for the Bayu-Undan and Greater Sunrise projects.

## General/Transitional

Until 24 October 1999, Timor-Leste adopted the Income Tax rules of Indonesia. From 25 October 1999 to 1 January 2008 (for annual taxes) and 1 July 2008 (for all other taxes), Regulation 2000/18 applied. Broadly, Regulation 2000/18 adopted the Indonesian Income Tax laws (subject to a number of modifications) in effect at 25 October 1999.

In 2008, the Timor-Leste government embarked upon a policy of taxation reform. The cornerstone of this reform has been the introduction of the TDA. The TDA provides for the consolidation of the taxation regimes applicable to Timor-Leste (other than for Annex F PSCs under the Timor Sea Treaty). This consolidation extended to the taxation of petroleum operations (previously governed by the Petroleum Tax Act) and the JPDA.

## Overview of the general Income Tax rules

In summary, Timor-Leste's Income Tax rules currently provide for:

- i) a top corporate tax rate of 10%, as applied to taxable income (although certain income is "final taxed" on a withholding basis-see below);
- ii) taxable income calculated according to normal accounting principles as modified by certain tax adjustments;
- iii) upfront deductibility for business inputs;
- iv) a denial of interest deductibility;
- v) the indefinite carry forward of losses;

- vi) internationally familiar concepts of residency and source; and
- vii) an extensive collection of cross-border and domestic withholding taxes.

## Scope of Taxation

Subject to certain exceptions and reduced by allowable deductions (see below) the TDA broadly seeks to levy tax on all increases in economic capacity in whatever name or form which can be used for consumption or to increase the wealth of Taxpayers.

Taxpayers include legal and natural “persons”. “Legal persons” include a wide range of entities such as companies, partnerships, trusts, governmental institutions and unincorporated associations. A “natural person” means any individual.

There is an internationally recognisable and extensive permanent establishment (“PE”) definition.

## Residency and Source

Resident “legal persons” are those incorporated, formed, organized or established in Timor-Leste, including the undivided estate of a natural person who was a resident natural person immediately before death.

Resident “natural persons” include natural persons present in Timor-Leste for more than 183 days in a 12 month period (unless that persons permanent place of abode is not in Timor-Leste); and employees of the Timor-Leste government who are posted abroad.

Timor-Leste residents are taxable on world-wide income/profits while non-residents are taxable on Timor-Leste sourced income/profits only.

Residents earning foreign sourced profits and income can receive credits for foreign taxes suffered.

## Rates of Tax

### Natural Persons

The rates of Income Tax for resident natural persons are as follows:

Annual Income	Rate
0 – \$US 6,000	0%
in excess of \$US 6,000	10%

Wages that have been correctly subject to Wage Income Tax ("WIT") (see below) are not subject to Income Tax.

For non-resident natural persons the rate of Income Tax is 10% on all Taxable Income.

### Legal Persons

The rate of Income Tax for Legal Persons is a flat rate of 10% on Taxable Income. However, a number of business activities will be subject to a "final" Income Tax to be withheld by the payer (see Withholding Taxes below).

## Business Profits

Taxable business profits are computed on the basis of net profit determined under International Financial Reporting Standards subject to certain modifications. Broadly, income is assessable when "receivable" while expenses are deductible when "payable". A taxpayer with turnover of less than \$100,000 may however, elect to pay tax on a cash basis.

## Calculation of Taxable Income

For Timor-Leste residents, taxable income is essentially the difference between "gross income", whether domestic or foreign sourced, and "allowable deductions".

Gross income is defined widely to mean "any realised increase in economic capacity in whatever name or form which can be used for consumption or to increase the wealth of the taxpayer, other than wages that are subject to WIT." Gross income specifically includes:

- i) business income (including gains from business activities and the alienation of assets or the discharge of indebtedness);
- ii) property income (including dividends, royalties, interest and rent);
- iii) lottery prizes or awards; and
- iv) a refund of a tax payment previously deducted as an expense.

Where certain types of income are subject to withholding tax which is final, such income is excluded from taxable income (see withholding taxes below).

## Exempt Income

Whilst the definition of gross income is broad there are a number of categories of exempt income. These include:

- i) amounts received as aid or donations, provided that the donor and donee do not have any business, ownership or control relationship;
- ii) gifts received by relatives within one degree of direct lineage, or by a religious, educational, or charitable organisation, or a co-operative, provided that the donor or donee does not have any business, ownership, or control relationship;
- iii) inheritances;
- iv) assets (including cash) received by a legal person in exchange for shares or a capital contribution;
- v) amounts paid by an insurance company to a natural person in connection with health, accident, life, or education insurance;
- vi) dividends;
- vii) any contribution paid by an employer or employee to an approved pension fund;
- viii) income derived by an approved pension fund; and
- ix) remuneration financed out of the Trust Fund for East Timor.

## Allowable Deductions

With the exception of interest the TDA provides for a wide range of allowable deductions (see also Depreciation below). Specifically, the TDA provides that the following are deductible:

- i) expenditure and losses to the extent incurred on the alienation of assets or the discharge of indebtedness in the conduct of a taxable business activity;
- ii) expenditure incurred in deriving any other amounts included in gross income;

- iii) any loss on disposal of an asset other than assets held on personal account;
- iv) contributions to an approved pension fund; and
- v) bad and doubtful debts (subject to various tests).

## Depreciation/Amortisation

The TDA provides for the depreciation of “depreciable assets” and “business buildings” and for the amortisation of “intangible assets”.

“Depreciable assets” include any tangible movable property that has a useful life exceeding one year; is likely to lose value as a result of wear and tear, exploitation or obsolescence; and is wholly or partly used in the conduct of taxable business activities.

“Intangible assets” include all other property, other than tangible movable property or immovable property, that has a useful life exceeding one year and is used in the conduct of taxable business activities.

There are provisions for the election of either straight line or diminishing value methods, the pooling of assets and di minimus exceptions.

The rate of tax depreciation/amortisation for non-Petroleum Operations is however set at 100%, meaning taxpayers are in effect entitled to a full and upfront deduction. In circumstances where the asset is only partly used for the conduct of taxable business activities, the deduction is reduced by the proportion of its non-taxable business use.

## Non-Allowable or Conditional Deductions

Each of the following expenditure is specifically not deductible:

- i) the distribution of profit, in whatever name or form, such as dividends and including dividends paid by an insurance company to a policy holder or any distribution of surplus by a co-operative;
- ii) expenses charged or incurred for the personal benefit of shareholders, partners, or members;
- iii) reserves, other than as provided for under the TDA;
- iv) premiums for health, accident, life, or education insurance paid by a natural person, except if the premiums are paid by an employer in respect of an employee and the premium is treated as income of the employee;
- v) excessive pay or compensation paid by a legal person to a member of

the legal person, or paid between associates, as consideration for work performed;

- vi) gifts, aid, donations or inheritances if exempt from Income Tax in the hands of the recipient;
- vii) Timor-Leste or foreign income tax;
- viii) costs incurred for the personal benefit of an income taxpayer or the taxpayer's dependents;
- ix) salaries paid to a partner in a partnership;
- x) late payment interest, penalties and fines imposed for non-compliance with the TDA;
- xi) interest expense unless incurred by a financial institution;
- xii) a fine or other monetary penalty imposed for violation of any law, rule, or regulation;
- xiii) a bribe or any similar payment; and
- xiv) expenditure or losses incurred to the extent recoverable under a policy of insurance or contract of indemnity.

## Losses

Previously, losses could be carried forward for a maximum of 5 years. The TDA now provides that losses incurred post 1 January 2008 may be carried forward indefinitely (with pre-2008 losses still limited to five years). The carry-back of losses is not permitted. There is no provision for any form of consolidated filing or group loss relief.

## Transfer Pricing

Whilst there is a definition of "associates", the TDA does not contain specific provisions for related party transactions or a general transfer pricing regime for non-Petroleum Operations.

## Administration

Income Tax returns are to be filed annually by the 15<sup>th</sup> of the third month following year end. The standard tax year is the calendar year although different accounting year-ends can be granted upon application. Any Income Tax payable is also due by the 15<sup>th</sup> day of the third month.

Businesses with an annual turnover of \$1m or more in the previous fiscal year are required to pay monthly Income Tax installments (at 0.5% of monthly turnover). Businesses with an annual turnover of less than \$1m are required to make quarterly installments.

## Withholding Tax

### Historical

Until 24 October 1999, the WHT rules were as set out in Indonesia's Income Tax Law. For the period 25 October to 31 December 1999 all income was exempt from Income Tax meaning no withholding obligation existed. Effective 1 January to 31 December 2000 all WHT rates were reduced to zero. The income was still however subject to tax in the hands of the recipient at the standard tax rates (maximum of 30%). From 1 January 2001 to 30 June 2008 WHT was applied at rates ranging between 2% and 15% for residents, and 20% for non-residents (final and non-final).

### Post 30 June 2008

WHT arrangements have been simplified under the TDA. The payments caught from 1 July 2008 are as follows:

		Rate	Final Tax
<b>A. Payment by residents to a resident for:</b>			
1	Royalties	10%	N
2	Rent (Land & Buildings)	10%	N
3	Prizes and Winnings	10%	Y
4	Construction/Building Activities	2%	Y/N*
5	Construction Consulting Services	4%	Y/N*
6	Air or Sea Transportation	2.64%	Y/N*
7	Mining & Mining Support Services	4.5%	Y/N*

	Rate	Final Tax
<b>B. Payment by residents to a non-resident</b>	10%**	Y

\* The Default position is that such amounts will be final taxed. The income recipient can elect to have these payments for services not subject to final tax by submitting a notification letter to the Timor-Leste Revenue Service.

\*\* applies to all payments of Timor-Leste source income to non-residents, other than those to which points 4-7 apply or payments to a PE of a non-resident.

Where WHT is applied as a final tax, the income is not included in the income recipients' calculation of taxable income for income tax purposes. Correspondingly, expenses incurred in deriving income which is subject to final tax are not deductible for income tax purposes.

## Administration

Withheld Income Tax is required to be remitted and reported (in a monthly return) by the income payer on a monthly basis by the 15<sup>th</sup> day of the month following the relevant withholding. There is no annual return or reconciliation for WHT.

## Services Tax

### Historical

Services Tax was originally due under Regulation 2000/18 from 20 March 2000 to 30 June 2008. Please see our 2005 Tax Guide for details.

### General/Transitional

From 1 July 2008, Services Tax is imposed on the gross consideration received by a person for the provision of "designated services".

"Gross consideration" includes all amounts received for the provision of the designated services. The TDA has removed a number of designated services to which Services Tax would apply (e.g. rental services). Services Tax does not apply to services performed in the JPDA.

Designated services, and the Service Tax Rates, are as follows:

Service	Service Tax Rate*
hotel services;	0% or 5%
restaurant and bar services; and	0% or 5%
telecommunication services	0% or 5%

\*5% rate applies where monthly turnover  $\geq$  \$US 500

## Administration

Providers of "designated services" must complete a monthly Services Tax form and make monthly remittances. The forms and remittances are due by the 15<sup>th</sup> day of the month following the provision of the relevant service.

## Excise Tax

### Historical

Excise Tax was originally due under Regulation 2000/8 from 20 March 2000 to 30 June 2008. Please see our 2005 Tax Guide for details.

### General

From 1 July 2008, excise Tax is imposed on the import or domestic production (but not both) of certain goods.

### Rates of Tax

The list of goods subject to Excise Tax is extensive. Selected goods and rates of Excise Tax are as follows:

General Description of Goods	Rates
Beer	\$US 1.90 per litre
Wine, vermouth, and other fermented beverages (for example, cider, perry)	\$US 2.50 per litre

General Description of Goods	Rates
Ethyl alcohol (other than denatured) and other alcoholic beverages	\$US 8.90 per litre
Tobacco and tobacco products	\$US 19.00 per kg
Gasoline, diesel fuel, and other petroleum products	\$US 6¢ per litre
Small passenger vehicles with an excise value exceeding \$US 70,000	35% of the excise value above \$US 70,000
Arms and ammunition	200% of the excise value
Cigarette lighters	12% of the excise value
Smoking pipes	12% of the excise value
Pleasure boats and private aircraft	20% of the excise value

Note: the excise value of excisable goods imported into Timor-Leste is the total of the customs value and any import duty imposed. The excise value of excisable goods manufactured in Timor-Leste is their fair market value at the time of removal from the manufacturers warehouse.

## Basis of Taxation

For imported goods the taxpayer is the importer. For goods produced domestically, the taxpayer is the producer. A good is considered produced at the earlier of the time it is available for sale/consumption, or is actually sold.

Goods are exempt from Excise Tax if they exported from Timor-Leste within 28 days of production and exempt from Import Duty; or relate to the JPDA.

## Administration

For imports, Excise Tax is payable at the time of import. For domestic production the taxpayer must complete an Excise Tax form and make a monthly remittance. The returns and remittances are due by the 15<sup>th</sup> day of the month following the relevant import or production event.

# Import/Export Duty

## Historical

Import/Export Duty was initially due under Regulation 2000/8 from 20 March 2000 to 30 June 2008. Please see our 2005 Tax Guide for details.

## General

From 1 July 2008, Import Duty is imposed on the import of all goods (except specifically exempted goods) at a rate of 2.5% the “customs value” of the goods.

“Customs’ value” is the fair market value of the goods including cost, insurance and freight (“CIF”) per GATT rules.

The liability to Import Duty rests with the importer. There are a number of exemptions including for goods:

- i) which accompany an individual upon arrival into Timor-Leste (limits apply);
- ii) being re-imported after export;
- iii) imported on a temporary basis;
- iv) constituting certain infant and female hygiene products; and
- v) which fall under the Timor Sea Treaty.

# Wage Income Tax

## Historical

For the period 25 October to 31 December 1999, employment related income was exempt from all taxes. Effective 1 January to 31 December 2000, the salary related withholding tax rate was reduced to zero although the income was still taxable directly at the top Income Tax rate of 30%. For wages received on or after 1 January 2001, WIT due under Regulation 2000/18, rather than Income Tax, was imposed.

## General/Transitional

From 1 July 2008 the TDA reduces WIT to a maximum of 10% in line with the reduced Income Tax rate (please note that a tax rate of 30% will apply to employees who do not supply a Tax Identification Number to their employer – see “Registration” below).

## Scope of Taxation

WIT applies to both cash salary and “fringe benefits” i.e. both constitute “taxable wages” and are taxable to the employee.

WIT is due on wages paid to a person who is “in employment in Timor-Leste”, where employment in Timor-Leste means services performed in Timor-Leste or services performed by an employee of the government whether performed in Timor-Leste or elsewhere.

Taxable wages constitutes “wages” received by an employee other than exempt wages. Exempt wages include:

- i) wages received for official duties that are exempt from taxation under the law;
- ii) wages of an employee who is a citizen of a foreign country received in the employee’s capacity as a public servant of the government of a foreign country provided that the wages are subject to Income Tax in that country;
- iii) wages of an employee who is an employee of the United Nations or its specialized agencies; and
- iv) remuneration received by any individual if the remuneration is financed out of the Trust Fund for East Timor.

## WIT Rates

The rates of WIT are as follows:

- a) If the employee is a resident natural person:

Monthly taxable wages	Rate
\$US0-\$US500	0%
Above \$US500	10% of the amount of wages above \$US 500

- b) If the employee is a non-resident natural person, 10% of the taxable wages received by the employee.

If an employee receives taxable wages for a period of less than one month, the rates of WIT are imposed in a pro rata basis.

In all cases, WIT is withheld and remitted by the employer. Where WIT has been correctly withheld, no further tax is due on those wages.

## Administration

Employers are required to withhold WIT from wages. Employers must also complete monthly returns and remittances. The monthly returns and remittances are due by the 15<sup>th</sup> day of the month following the relevant wage payment. An annual return is due by the last day of the February following the end of the relevant tax year. Information on WIT withheld must also be provided to each employee on an annual basis or on termination of employment.

## Fiscal Administration

As previously mentioned, the TDA does not contain tax administration provisions. The TDA also does not repeal the previous law in respect of the administration and collection of tax and the provisions relating to tax offences and sanctions as applied under UNTAET No. 2000/18.

## General

Pursuant to Resolution 1272 of 25 October 1999, UNTAET was established with overall administrative responsibility over Timor-Leste. Pursuant to UNTAET Regulation 2000/1, UNTAET established the Central Fiscal Authority ("CFA"). Post the election of Timor-Leste's first parliament, the CFA's role was replaced by the Minister for Planning and Finance (now the Minister of Finance - "MoF"). The MoF is responsible for (amongst other things):

- i) the overall financial budget;
- ii) the overall fiscal strategy; and
- iii) the operation of the Timor-Leste Revenue Service ("TLRS").

The TLRS is headed by a Commissioner. The Commissioner's obligations include enforcement of Regulations in relation to the collection of taxes, duties & fees. These obligations may be delegated.

## Registration

Most persons liable to tax are required to obtain a unique Tax Identification Number (“TIN”). Businesses are required to register for a TIN in addition to the requirement to register with the Business Registration Unit of the Department of Economic Affairs. If an employee does not supply a TIN to their employer, employers are required to deduct WIT at 30%. A register of TIN’s is maintained by the Commissioner.

## Assessments

Assessments may occur as follows:

- i) upon the delivery of a tax return form and payment;
- ii) after receipt of a return where the Commissioner believes a return is incorrect; and
- iii) where a taxpayer fails to file a return.

Assessments may be amended:

- i) by the taxpayer upon delivery to the Commissioner of an amended assessment;
- ii) via a taxpayer request to the Commissioner; and
- iii) via specific amendment by the Commissioner.

Amendments resulting in tax refunds are to be applied first against any other outstanding taxes (this includes interest on such amounts). The Commissioner has 5 years from the date the return was due in order to assess or amend. However, if deliberate evasion or fraud is involved there is no time limit.

Where tax is not paid on time the Commissioner may take action in the Courts. Unpaid tax also creates a lien over taxpayer property. This can extend to property controlled by an agent or partners. Directors may be exposed if they caused the company not to pay.

## Books and Records

Taxpayers are required to create records showing the calculation of their tax liability. The records must be kept in an official language, and for a period of 5 years after the relevant tax year.

The Commissioner has wide powers to review, make copies, seize or retain such records. The Commissioner also has powers allowing for the collection of information in regard to a taxpayer’s affairs from third parties.

## Rulings

The Commissioner is entitled to issue rulings on the Commissioner's interpretation of the law. The rulings are binding on the Commissioner.

The Commissioner is entitled to issue a private ruling to a particular taxpayer. A private ruling is also binding on the Commissioner.

## Appeals

It is intended that the Commissioner will establish an Appeals Office within the TLRS. Taxpayers may then make appeals to the Appeals Office within 60 days of the date of receipt of any assessment in dispute. A decision of the Appeals Office is binding on the Commissioner.

Taxpayers may appeal a decision of the Appeals Office to the Board of Trade and Customs within 60 days of receiving the notice of decision.

The commencement of action in the Appeals Office or the Board of Trade and Customs does not extinguish a liability to pay the tax in dispute.

## Double Taxation Agreements

At the time of writing, Timor-Leste had not negotiated any double taxation agreements (other than for the JPDA-see Part C).

There is a question as to whether Timor-Leste effectively adopted Indonesia's tax treaties from 25 October 1999. While this remains unclear, Regulation 2000/18 removed any possible application with effect from 1 July 2001.

## International Agreements

At the time of writing Timor-Leste had not entered into any Investment Promotion and Trade Agreements.

# Part B - Taxation of Petroleum Operations



# Taxation of Petroleum Operations

## Background

### **IMPORTANT: SCOPE OF PART B**

This Part B outlines the taxation arrangements for oil and gas activities in Timor-Leste's exclusive area of sovereignty (i.e. excluding activities falling within the JPDA which includes the Annex F PSCs covering the Bayu-Undan and Greater Sunrise projects).

In respect of activities carried out in the (non-Annex F) JPDA area, this Part B is relevant but only in conjunction with Part C which outlines the underlying Indonesian tax principles and overlying application of the Timor Sea Treaty. This Part B has no application to Annex F PSCs which are covered exclusively by Part D.

A historical outline of Timor-Leste's taxation of oil and gas activities is provided earlier in this guide (see the "Overview" section). This outline noted the existence of a number of tax regimes for oil and gas activities according to whether the activities take place in Timor-Leste or the JPDA. For oil and gas activities taking place solely within Timor-Leste's exclusive area of sovereignty the tax regime is as outlined below and is essentially based upon the TDA.

## TDA Regime – Chapter IX

The TDA consolidates the regimes imposing tax in Timor-Leste (including in the oil and gas sector) and applies as follows:

- i) from 1 January 2008 (for annual taxes); and
- ii) from 1 July 2008 (for all other taxes).

Chapter IX of the TDA contains special provisions for the taxation of "Petroleum Operations" for the territory of Timor-Leste (note the TDA extends to the JPDA but for JPDA activities this Part B should be read in conjunction with Part C). The TDA also repealed the Petroleum Tax Act (which had effect from 1 January 2005).

Petroleum Operations are defined in Chapter IX of the TDA to include authorised activities under a Petroleum Agreement (e.g. a PSC, or other agreement made pursuant to the Petroleum Act except a Seepage Use

Authorisation). Specific provisions for the taxation of Petroleum Operations include:

- i) a corporate tax rate for Contractors (see definition below) of 30% on taxable income (although certain income is “final taxed” on a withholding basis);
- ii) no tax due on branch profit remittances;
- iii) where “net receipts” exceed specified levels, a Supplemental Petroleum Tax applies;
- iv) the “ring-fencing” of income and expenditure within the Contract Area;
- v) modified deductibility rules, including the deductibility of interest for Contractors and a modified depreciation regime; and
- vi) a specific WHT regime.

## Scope of taxation

The TDA applies to all activities carried out within Timor-Leste’s sovereign territory. Chapter IX however operates to modify the taxes outlined in the TDA in respect of Petroleum Activities. The Chapter IX modifications apply to Contractors, Subcontractors and any person (legal or natural) receiving an amount for goods or services supplied to a Contractor or Subcontractor.

Contractors are defined as persons who have an interest in a Petroleum Agreement with the Designated Authority in Timor-Leste. A Subcontractor includes any person supplying goods or services directly or indirectly to a Contractor in respect of Petroleum Operations.

## Income Tax/WIT

Chapter IX includes specific modifications in respect of the Income Tax and WIT rules as set at Chapters VI and VII of the TDA. The modifications include an adjustment to the respective rates as follows:

### Contractors

- i) taxed at a flat rate of 30%;

## Employees of Contractors

- i) If the employee is a resident natural person\* and has (or is deemed to have) provided their tax identification number:

Monthly taxable wages	Rate
\$US 0 – \$US 550	10%
Above \$US 550	\$US 55 + 30% of the amount of wages above \$US 550

- ii) If the employee is a non-resident natural person, the rate is a flat 20%;  
iii) In any other case, the rate is 30%.

\* If the employee is a resident natural person, they are entitled to a \$10 tax credit per month against the WIT payable for the month.

No further Income Tax liability exists on income for Contractors or their employees under the TDA.

## Subcontractors

Subcontractors will generally be taxed on a final withholding basis at a rate of 6% (see “WHT” below).

## Allowable Deductions

Subject to the limitations outlined below, all expenditure incurred by a Contractor in respect of Petroleum Operations is deductible, including interest, financing charges and amounts of Timor-Leste Income Tax (prior to the calculation of Supplemental Petroleum Tax). Specific rules on allowable deductions for Petroleum Operations include:

- i) *ring fencing* - expenditure incurred by a Contractor is only deductible against the Gross Income of such Petroleum Operations in the Contract Area in that year. The Contract Area is defined as the area originally granted under a Petroleum Agreement (but includes any subsequently relinquished area);

- ii) *indefinite carry forward of excess deductions (excluding interest)* – if in any year total deductions in a Contract Area exceed the the total gross income arising from Petroleum Operations in that Contract Area, the excess can be carried forward and deducted in the following year until such excess is fully deducted or the Petroleum Operations cease;
- iii) *interest deductibility* – unlike the general taxation provisions, Contractors enjoy a limited deduction for interest expenditure. Interest deductibility is limited to the amount of interest income a Contractor has derived during a year and 25% of “net non-interest income” derived by the Contractor during the year. “Net non-interest income” is defined as gross income, less interest income, less deductions other than interest deductions. Any amount that is not deducted as a result of the limitation mentioned above may be carried forward and deducted as an interest expense for 5 years;
- iv) *head office expenditure of a PE* – a deduction for head office expenditure where not exceeding 2% of total deductible expenditures (excluding depreciation and head office expenditure deductions);
- v) *decommissioning Costs* – specific deductibility provisions enabling Contractors to claim a deduction for amounts carried to a decommissioning reserve. An amount is first deductible in the year when estimates of decommissioning costs are first charged as a recoverable cost under a Petroleum Agreement; and
- vi) *cost of acquiring an interest in Petroleum Operations* – any amount incurred as consideration for acquiring an interest in Petroleum Operations is non-deductible.

## Depreciation/Amortisation

Subject to the modifications outlined below, Contractors are entitled to depreciate all “depreciable assets” and amortise all “intangibles” in accordance with the general provisions of the TDA (see definitions above) from the commencement of commercial production.

Exploration Expenditure and Development Expenditure incurred under a Petroleum Agreement is treated as intangible expenditure and amortised on a straight-line basis in accordance with the following useful life criteria:

- i) *exploration expenditure* – the lesser of the expected life of the Petroleum Operations under a Petroleum Agreement or 5 years;
- ii) *development expenditure* - the lesser of the expected life of the Petroleum Operations under a Petroleum Agreement or 10 years.

## Depreciation/Amortisation rates

The depreciation rates and useful lives of “depreciable assets” and “business buildings” is as follows:

Items	Useful Life	Depreciation Rate	
		Straight Line	Double Declining
Buildings – permanent	20 years	5%	N/A
Buildings – non permanent	10 years	10%	N/A
Assets	1 – 4 years	25%	50%
Assets	5 – 8 years	12.5%	25%
Assets	More than 9 years	6.25%	12.5%

The amortisation rates for “intangible assets” (including Development and Exploration Expenditure) is as follows:

Items	Useful Life	Straight Line Depreciation Rate
Intangible assets	1 – 4 years	25%
Intangible assets	5 – 8 years	12.5%
Intangible assets	9 – 16 years	6.25%
Intangible assets	16 – 20 years	5%

Where an interest in a Petroleum Agreement is transferred, the transferee must continue to amortise any Exploration or Development Expenditure on the same basis as the original Contractor and the provisions of the TDA apply to all other depreciable or intangible assets.

There are specialised provisions for “small field depreciation” (where an approved Development Plan estimates 80% or more of the reserves will be developed within five years of the commencement of “commercial production”).

## Value of Petroleum

Petroleum is valued “free on board” (“f.o.b”) at the Field Export Point (the point at which the Petroleum leaves the Contract Area, or such an earlier point where it is loaded onto any form of transportation or pipeline).

Crude oil is essentially valued at the f.o.b price paid under an arm’s length transaction at the Field Export Point.

The value of Natural Gas is the price paid under an Approved Contract or as provided for under a Development Plan or Petroleum Agreement.

## Installments of Income Tax

Contractors are subject to monthly instalments calculated at 1/12<sup>th</sup> of the Contractor’s income tax liability of the preceding tax year (subject to various adjustments). Any “excess” payments are credited against subsequent instalments. If the total amount of instalments paid exceeds the Contractor’s Income Tax liability for the year, the excess is not refunded but is credited against the Contractor’s instalments of tax due for the next tax year.

The instalments of Income Tax should be paid by the 15<sup>th</sup> day of the following month.

## Supplemental Petroleum Tax

### Background

SPT is applied where a Contractor has a positive amount of accumulated net receipts for the Petroleum Operations for a tax year.

SPT is applied in addition to the Income Tax imposed on the Contractor for the year. However, SPT paid by a Contractor is deductible in the calculation of taxable income of the Contractor in the year in which the SPT is paid.

### Calculation of SPT

The SPT is calculated according to the following formula:

$$\text{ANR} \times 22.5\% / (1-r)$$

where:

ANR is the “accumulated net receipts” of the Contractor for the Petroleum Operations for the year (see below); and

r is the rate of corporate Income Tax (30% currently).

The ANR of a Contractor for Petroleum Operations for a tax year is calculated according to the following formula:

$$((A \times 116.5\%) - (I \times (1-r))) + B$$

where:

A is the Contractor’s accumulated net receipts for the Petroleum Operations at the end of the previous tax year (entered as a negative to denote a loss), and is deemed to be nil if APT was payable in the previous year of tax;

B is the Contractor’s “net receipts” for the Petroleum Operations for the current tax year;

“Net receipts” of a Contractor for a tax year is the “gross receipts” of the Contractor for the year, less the total deductible expenditure of the Contractor for the Petroleum Operations for that year (this may be negative).

The definition of “gross receipts” of a Contractor is extremely broad and includes (amongst other items) the gross income accrued for Income Tax purposes as well as other amounts and forms of consideration, but specifically excludes interest income and amounts received or accrued in consideration for the transfer of an interest in the Petroleum Operations.

I is the interest expense and other financial charges paid by the Contractor in respect of the Petroleum Operations in the current tax year and is entered in the formula as a negative number; and

r is the rate of corporate Income Tax (30% currently).

It is understood that in practice, the TLRS administers the taxation law on the basis that, in the ANR formula above, if component  $(A \times 116.5\%)$  is negative for a tax year, that component cannot be offset by  $(I \times (1-r))$ , such that the result of  $((A \times 116.5\%) - (I \times (1-r)))$ , in absolute terms, is lesser than A, in absolute terms.

The computation of SPT can be complicated when a Contractor moves from a taxable loss to a taxable income position, and the above formulae/definitions will need to be applied with care.

## **Payment and Reporting Procedure for SPT**

The due date for the SPT payment and SPT return submission is the same as annual Income Tax.

As with Income Tax, Contractors are required to remit instalments of SPT. The instalment is calculated at 1/12<sup>th</sup> of the Contractor's estimated SPT to be due for the tax year.

The instalments of SPT Tax should be paid by the 15<sup>th</sup> day of the following month.

## **Transfers of interests in Petroleum Operations**

Where an interest in Petroleum Operations is transferred to another Contractor, the transferee is treated as having the same gross receipts and deductible expenditures in respect of the interest as the transferor had immediately before the transfer. For the purposes of calculating the transferee's accumulated net receipts, the transferee inherits the transferor's accumulated net receipts at the end of the previous tax year.

Where part of an interest is transferred, the gross receipts, deductible expenditure and accumulated net receipts are proportionally allocated.

## **Withholding Tax**

Payments by all Timor-Leste residents and PE's for services acquired for Petroleum Operations (other than services as an employee) are subject to 6% WHT (final) on the gross amount.

## **Indirect taxes**

### **Services Tax**

Other than in the JPDA, Services Tax is applied on "designated services" (hotel, restaurant, bar and telecommunications services) at a rate of 12% (see Part A for details).

## **Sales Tax**

Other than in the JPDA, Sales Tax at a rate of 6% applies on the import of goods by a Contractor in relation to Petroleum Operations (see Part A for details).

## **Value Added Tax**

VAT does not apply to Petroleum Operations in Timor-Leste sovereign territory (however see Part's C and D for modifications in relation to the JPDA).

## **Import Duty**

Under Chapter IX, other than in the JPDA, Import Duty at a rate of 6% is payable on the import of goods by a Contractor. Subcontractors will generally be subject to the general import duty provisions (see Part A for details).

# Part C - Modifications for the JPDA



# Income Tax

## Background

### **IMPORTANT: SCOPE OF PART C**

This Part C deals with tax arrangements for oil and gas activities connected with the JPDA (other than Annex F PSCs). These tax arrangements are largely as outlined in Part B of this publication but as modified by the Indonesian tax laws of 25 October 1999 and the Timor Sea Treaty. This Part C only considers Timor-Leste's taxing rights (i.e. on Timor-Leste's 90% share of income) and so does not consider the Australian taxation implications for activities connected with the JPDA.

## General/Transitional

As outlined in the earlier "Overview" section of this publication, Timor-Leste originally adopted the Indonesian Tax laws in place as at 25 October 1999. These laws were then progressively modified by UNTAET Regulation 2000/18, the Petroleum Tax Act (see below) and (most recently) the TDA (see Part A & B of this publication).

Regulation 2000/18 however had no application to activities carried out in the JPDA (at least in regard to Income Tax). This position was followed by the Petroleum Tax Act. Instead, Timor-Leste's tax rules applying in the JPDA continued to be sourced entirely out of the Indonesian tax rules as at 25 October 1999 (which extends to Indonesia's "uniformity principle" - see below) until modified by Chapter IX of the TDA.

The tax regime covered in this Part C is therefore potentially quite complex.

## Taxation of oil and gas

### Indonesian Legacy - Uniformity Principle

Income Tax levied on PSC contractors in Indonesia was traditionally determined according to the "uniformity principle" (i.e. the principle that cost recoverable and tax deductible expenditure should be identical). The Indonesian experience is that, cost recovery has been limited to exploration, development and production related spending as formally approved for cost recovery purposes by the relevant Government Agency (BP Migas but formerly Pertamina). The adoption of the "uniformity principle" also meant

that upstream activities, even in Indonesia, were not actually subject to Income Tax as technically outlined pursuant to the Income Tax laws in place at 25 October 1999.

A historical perspective on Indonesia's uniformity principle is worth noting. From the early 1960's, contractors in Indonesia were entitled to take their share of production on a "net of tax" basis. In the late 1970's this was changed to a "gross of tax" basis, to accommodate US foreign tax credit rules. This change led to a calculation of taxable income being necessary and an actual payment of Income Tax by the contractors.

However, the change from a "net of tax" to a "gross of tax" sharing basis was not meant to disturb the desired after-tax take. It therefore became necessary to adopt the "uniformity principle" in relation to the calculation of taxable income, so that the treatment of income and expenditure items for cost recovery and tax deductibility purposes became identical.

Uniformity therefore meant that tax deductibility followed the rules of cost recovery as set out in the relevant PSC, rather than the rules set out in the actual Indonesian Income Tax Law. Uniformity also meant that the Income Tax rate was set for the life of the PSC, and so continued to apply irrespective of any changes in that rate under the general tax law.

## Transition to Timor-Leste rules (1 January 2005 – 2008)

From 1 January 2005 until the introduction of the TDA the Petroleum Taxation Act applied to Petroleum Operations carried out in the JPDA. The PTA however preserved the linkage to Indonesia's 25 October 1999 tax laws for both Income Tax and VAT.

## Current Tax Rules (Timor-Leste 90% share)

From 1 January 2008 (for annual taxes) and 1 July 2008 (for all other taxes) the TDA "consolidates" the taxation regime applicable to Timor-Leste including for Petroleum Operations in the JPDA (but excluding Annex F PSCs – see Part D).

However, there are a number of important modifications made to the TDA's application in the JPDA. In effect, whilst the TDA does apply to the JPDA, the following taxes appear to be excluded from application in the JPDA:

- Services Tax
- Excise Tax
- Sales Tax

- Input Duty; and
- Wage Income Tax.

Income Tax does continue to apply in the JPDA. However the Income Tax regime for upstream activities appears to consist of the arrangements set out in Chapter IX (as covered in Part C of this publication) but with a possible variation of being based upon Indonesian's 25 October 1999 tax laws (with the uniformity principle, etc) rather than the other Chapters of the TDA.

## Timor Sea Treaty

A further variation is the JPDA's 90:10 revenue split as set out in the Timor Sea Treaty. As a result, the tax levied in the JPDA is at 90% of the rates set out under the TDA.

The Timor Sea Treaty also includes a tax code (Annex G) for the avoidance of double taxation. Similar to a conventional tax treaty, Annex G contains specific provisions on matters including (but not limited to) residency, business profits, dividends, interest and royalties connected with the JPDA.

## Value Added Tax

Given the continued JPDA reliance on Indonesia's tax laws as at 25 October 1999, the JPDA continues to allow for a broad-based VAT at the rate of 10% (or 9% after the Timor Sea Treaty reduction). This is notwithstanding that there is no VAT applying in Timor-Leste outside of the JPDA.

The legislative framework in regard to VAT is however unclear. Based upon a TLRS draft discussion paper of 14 October 2001, VAT is generally administered as follows:

- i) *imports of goods*: the Timor Sea Treaty appears to allow Timor-Leste the option to levy VAT;
- ii) *imports of services*: likely to be subject to VAT on a self-assessed basis, at least where dealing with "first tier" contractors (i.e. PSC interest holders or contractors);
- iii) *second tier contractors/sub contractors*: appear to be not required to register for VAT.

Up to date advice on the VAT position should however be sought before executing binding agreements.

# Part D - Bayu-Undan and Greater Sunrise (Annex F PSCs)



# Background

## Legislative/Political

Prior to the signing of the Timor Sea Treaty on 20 May 2002, PSCs had been granted over two significant hydrocarbon discoveries in the JPDA. Annex F of the Timor Sea Treaty provides that, for these existing contracts (known as the “Annex F PSCs”) interest holders would be offered JPDA PSCs on essentially the same terms that existed prior to the Timor Sea Treaty. This stability extended to the fiscal regime applicable to the PSCs.

The Annex F PSCs constitute:

- PSCs 03-12 and 03-13 (including the Elang/Elang Kakatua/Kakatua North (“EKKN”) fields) which have been unitised and are operated by a ConocoPhillips entity (Bayu-Undan); and
- PSCs 03-19 and 03-20 which have been unitised and are operated by a Woodside entity (Greater Sunrise). The Greater Sunrise field unitisation is itself complicated in that the field straddles the JPDA (approximately 20.1%) and waters that are claimed exclusively by Timor-Leste and Australia.

See Appendix D for the geographic location of each project.

The foundation tax laws for the Annex F PSCs are those adopted into Timor-Leste under UNTAET regulation 1999/1 (i.e. the Indonesian tax laws as at 25 October 1999).

UNTAET Regulation 1999/1 provided that these Indonesian laws were to continue to apply in Timor-Leste until being replaced by UNTAET regulation or Timor-Leste law. With regard to Income Tax the subsequent introduction of UNTAET 2000/18, the Petroleum Tax Act and the TDA specifically excluded their application to Annex F PSCs (and so also prevented the introduction of Timor-Leste’s own taxes such as the Services, Excise, Sales and Import Taxes).

Accordingly, whilst both Bayu-Undan and Greater Sunrise each have distinct unitisation and taxation overlays (discussed below), the 25 October 1999 tax laws (including potentially the “uniformity principle” – see part C) remain relevant to activities in these areas.

## Summary of Annex F regimes

The applicable regime for each Annex F PSC is as follows:

### Timor Sea Treaty (for Timor-Leste's 90% share)

<b>Bayu-Undan (excluding EKKN)</b>	i) Indonesian Tax Laws at 25 October 1999; ii) ToBUCA
<b>Greater Sunrise</b>	i) Indonesian Tax Laws at 25 October 1999 ii) Sunrise IUA iii) Certain Maritime Agreements Treaty
<b>EKKN</b>	i) Indonesian Tax Laws at 25 October 1999

For a geographical representation of these areas, please see Appendix D. For a comparative table of each area, please see Appendix B.

## The Law on Income Tax

### Overview

The Law on Income Tax (i.e. Indonesian tax law as at 25 October 1999) provides for:

- i) a top corporate tax rate of 30%, as applied to taxable income (although certain income is “final taxed” on a withholding basis - see below);
- ii) taxable income calculated according to normal accounting principles as modified by certain tax adjustments (noting in particular the potential operation of the “uniformity principle” as outlined in Part C);
- iii) internationally familiar concepts of residency and source; and
- iv) an extensive collection of cross-border and domestic withholding taxes.

## Scope of Taxation

The Law on Income Tax seeks to tax business profits and “designated passive” income. Business profits can include capital gains. Passive income includes interest, royalty, rental and dividend income (although see comments on WHT below). Employment related income is also subject to Income Tax (i.e. not the separate Wage Income Tax as set out in Parts A & B of this booklet).

Various taxpayer “entities” are recognised including companies, partnerships and individuals. There is an internationally recognisable, and extensive PE definition. There are also “force of attraction” principles requiring the aggregation of PE and non-PE activities.

## Residency and Source

For non-individuals, a Timor-Leste resident includes a “body established or domiciled in Timor-Leste”. A body includes a limited company, limited partnership, state owned enterprise and “other forms of business”.

For individuals, a resident includes a person “residing in Timor-Leste or being present in Timor-Leste, for more than 182 days in a calendar year”.

Timor-Leste residents are taxable on world-wide income/profits while non-residents are taxable on Timor-Leste sourced income/profits only. Residents earning foreign sourced profits and income can receive credits for foreign taxes suffered.

## Rates of Tax

The standard income tax rates for resident companies and individuals is as follows:

	<b>Annual Taxable Income</b>	<b>Rate</b>	<b>Tax</b>
	<b>\$US</b>		<b>\$US</b>
on the first	3,368	10%	337
on the next	3,368	15%	505
over	6,737	30%	-

A significant number of business activities will be subject to a “final” tax withheld by the payer (see Withholding Taxes below).

## Business Profits

Taxable business profits are generally computed on an accruals basis. Under the accruals basis, income is assessable when “receivable” while expenses are deductible when “payable”.

## Calculation of Taxable Income

Taxable income is essentially the difference between total revenue attributable to the PE, and “allowable expenses” paid or incurred to carry on the business. Certain income and expenditure of the PE’s head office can also be forcibly attracted to the PE.

Income is defined widely to mean “any increase in economic capacity received or accrued”. Specifically it includes:

- i) profits from business;
- ii) gains from the sale or transfer of property;
- iii) refunds of deductible tax payments;
- iv) interest, premiums, discounts and compensation from loan repayments guarantees;
- v) dividends;
- vi) royalties;
- vii) rent;
- viii) gains from the cancellation of indebtedness;
- ix) gains from the fluctuation in foreign currencies;
- x) gains from the revaluation of property; and
- xi) insurance premiums.

## Allowable Deductions/Uniformity Principle

For a PSC Contractor, the following comments on deductibility are subject to any special rules relevant to the calculation of Income Tax due on liftings. As was outlined in Part C, Indonesia had adopted the “uniformity principle” in respect of tax due on liftings earned under an Indonesian PSC. The uniformity principle itself is not however well set out in Indonesia law. The extent therefore

to which the “uniformity principle” may have been incorporated into the Law on Income Tax as adopted by Timor-Leste on 25 October 1999 is not clear.

“Uniformity principle” issues aside, Timor-Leste’s tax rules contain a general deductibility provision under which all expenditure first falls for consideration as a deduction. Any expenditure satisfying the general criteria will be fully deductible in that year unless specific provisions apply. Such expenditure specially includes:

- i) losses suffered on the sale of property;
- ii) losses arising from fluctuations in foreign exchange; and
- iii) expenditure on tangible property with a useful life of more than 1 year – depreciable at designated rates as follows:

Items (useful life)	Depreciation rate	
	Straight line	Dim. Value
Buildings – permanent	5%	N/A
Buildings – non-permanent	10%	N/A
Property (4 years)	25%	50%
Property (5-8 years)	12.5%	25%
Property (9-16 years)	6.25%	12.5%
Property (17 years +)	5%	10%

- iv) expenditure on intangible property (including pre-commencement costs) with a useful life of more than 1 year-amortizable at designated rates as follows:

Items (useful life)	Straight line depreciation rate
Property (4 years)	25%
Property (5-8 years)	12.5%
Property (9-16 years)	6.25%
Property (17 years +)	5%

## Non-Allowable or Conditional Deductions

These include:

- i) private expenses;
- ii) non-business gifts and aid;
- iii) general provisions/reserves;
- iv) Income Tax payments;
- v) penalties, fines etc.; and
- vi) expenses relating to income taxed on a “final-taxed” basis (see Withholding Taxes section below).

## Losses

Taxpayers may carry forward their losses for five years. The carry-back of losses is not permitted. There is no provision for any form of consolidated filing or group loss relief.

## Transfer Pricing

The Law on Income Tax provides wide powers for the Timor-Leste authorities to redistribute income and deductions between parties under “a special relationship”. A Special Relationship will exist at a relatively low 25% common ownership level.

## Withholding Tax

### Payments/Rates

The following WHT apply on certain payments. The rates mentioned below are before the reduction factor of 10% under the Timor Sea Treaty (i.e. Timor-Leste’s is only entitled to tax 90%):

**“Article 21” WHT (payment from a resident (including a PE), to a resident)**

Type	Rate* (Max.)	Final Tax (Y/N)
On salaries/wages	30%	N
Severance payments	15%	N

Pension payments	30%	N
Fees paid to independent, individual professionals	6%	N

\* before JPDA reduction factor of 10%

### “Article 23” Withholding Taxes (payment by resident to resident, or PE to PE)

Type	On gross amount/Est. net Income (ENI)?	ENI percentage	WHT rate	Actual WHT rate* (%of gross amount)	WHT rate with 10% reduction percentage applied	Final Tax (Y/N)
Interest	Gross	-	15%	-	13.50%	N
Royalties	Gross	-	15%	-	13.50%	N
Drilling and support services in mining	ENI	30%	15%	4.50%	4.05%	N
Prizes and awards	Gross	%	15%	15%	13.50%	N
Rent (other than land and building)	ENI	40%	15%	6%	5.40%	N
Technical and management services	ENI	40%	15%	6%	5.40%	N
Architecture, interior, and landscape design	ENI	40%	15%	6%	5.40%	N
Accounting and bookkeeping	ENI	40%	15%	6%	5.40%	N
Timber cutting	ENI	40%	15%	6%	5.40%	N
Pest control and cleaning services	ENI	10%	15%	1.50%	1.35%	N
Intermediary	ENI	60%	15%	9%	8.10%	N
Appraisal	ENI	40%	15%	6%	5.60%	N
Actuary	ENI	40%	15%	6%	5.40%	N
Film dubbing/mixing	ENI	40%	15%	6%	5.40%	N
Other services which payments are borne by Government Budgets	ENI	10%	15%	1.50%	1.35%	N

\* before JPDA reduction factors of 10%. May be an additional tax on branch profits if earned by a PE.

Note: WHT = withholding tax

**“Article 26” Withholding Taxes (payments by resident – (incl. PE), to non-resident)**

Type	On gross amount/Est. net Income (ENI)?	ENI percentage	WHT rate	Actual WHT rate* (%of gross amount)	WHT rate with 10% reduction percentage applied	Final Tax (Y/N)
Dividends	Gross		20%	20%	18%	Y
Interest, including premiums, discounts, and guarantee fees	Gross		20%	20%	18%	Y
Royalties	Gross		20%	20%	18%	Y
Rental and payments for the use of assets	Gross		20%	20%	18%	Y
Fees for services, work, and activities	Gross		20%	20%	18%	Y
Prizes and awards	Gross		20%	20%	18%	Y
Pensions and any other periodical payments	Gross		20%	20%	18%	Y
National annual distributions of after-tax profits of a branch (or so-called “PE”)	Gross		20%	20%	18%	Y
Insurance premium paid by:						
- by the insured	ENI	50%	20%	10.00%	9%	Y
- by Indonesian insurance companies	ENI	10%	20%	2%	2%	Y
- by Indonesian reinsurance companies	ENI	5%	20%	1%	1%	Y

\* before JPDA reduction factors of 10%.

## Specifically regulated payments of income

Type	On gross amount/ Est. Net Income (ENI)?	Rate*	WHT rate with 10% reduction percentage applied	Final Tax (Y/N)
<b>- Payment from resident to resident:</b>				
Rentals of land and buildings:				
- if the lessor (i.e. the owner) is a corporate taxpayer	Gross	6%	5.4%	Y
- if the lessor (i.e. the owner) is an individual taxpayer	Gross	10%	9%	Y
- if the lessor is a corporate taxpayer but the owner is an individual taxpayer	Gross	10%	9%	Y
Fees for construction and consulting services:				
- construction contracting	Gross	2%	1.8%	Y
- construction planning	Gross	4%	3.6%	Y
- construction supervision	Gross	4%	3.6%	Y
- consulting services (other than tax and legal)	Gross	4%	3.6%	Y
Payment of interest from banks	Gross	15%	13.5%	Y
Payment to resident shipping/airlines companies	Gross	1.2%	1.08%	Y
Payment to non-resident shipping/airlines companies (with PE)	Gross	2.64%	2.376%	Y

\* May be an additional tax on branch profits if earned by a PE.

# Value Added Tax

As previously mentioned, Indonesia's tax laws as at 25 October 1999 included a broad-based VAT levied at the rate of 10%. This VAT continues to apply in areas covered by Annex F PSCs (see Part C for details).

## Bayu-Undan (excluding EKKN)

### Taxation of Bayu-Undan Contractors Act

In June 2003, Timor-Leste passed the ToBUCA. ToBUCA was introduced in an attempt to provide specific tax related concessions and obligations (relevant to the Indonesian Income Tax Law as at 25 October 1999) considered necessary to help ensure the early development of the Bayu-Undan LNG project. The underlying intention was to encourage the Bayu-Undan contractors to proceed with the gas phase of the project. These changes were effective from 1 January 2002.

ToBUCA specifically excludes the EKKN fields which remain subject to the Law on Income Tax as outlined above.

### Summary of the changes

Summarised below is an outline of the changes. It should be noted that ToBUCA applies to contractors and subcontractors supplying goods or services in respect of JPDA PSCs 03-12 (previously 91-12) (excluding the Elang Kakatua Kakatua North area) and JPDA PSCs 03-13 (previously 91-13).

ToBUCA changes to the Law on Income Tax	Description of Change
Taxes Covered	Income Tax (including associated withholdings), VAT, Sales Tax.
Activities Covered	Petroleum activities in relation Bayu Undan, other than EKKN.

ToBUCA changes to the Law on Income Tax	Description of Change
Activities Exempted	Income and activities connected to the Bayu-Undan export pipeline.
Branch Profits Tax	General elimination of tax on branch profit remittances for “first tier” contractors (i.e. PSC entities) and sub-contractors.
Withholding Taxes	General reduction in WHT rates on a wide range of service charges (see below for further detail).
Additional Profit Tax	Introduction of an Additional Profit Tax ("APT") on significant oil and gas profits. APT is calculated in the same manner and method as SPT (see p. 38 for details).
Decommissioning Costs Reserve	Introduction of an entitlement to progressively accrue qualifying decommissioning costs. Accrual is tax deductible.
Depreciation/Amortisation	Acceleration of tax depreciation and amortization rates for Bayu-Undan assets.

## New Withholding Tax Rates

Summarised below are the main rate changes arising from ToBUCA:

Type of activity	Pre-ToBUCA		Post-ToBUCA		
	Actual WHT on gross amount	10% reduction % applied rate	Post ToBUCA rate (reduction % not applied)	10% Reduction % applied	Final Tax (Y/N)
Drilling Services (by a PE)*	4.5%	4.05	1.8%	1.62%	Y
Drilling Support	4.5%	4.05	1.8%	1.62%	N
Construction Services	2.0%	1.8%	0.8%	0.72%	Y

Type of activity	Pre-ToBUCA		Post-ToBUCA		
	Actual WHT on gross amount	10% reduction % applied rate	Post ToBUCA rate (reduction % not applied)	10% Reduction % applied	Final Tax (Y/N)
Construction Consulting Services	4.0%	3.6%	1.6%	1.44%	Y
Royalties – to residents (or PE)	15.0%	13.5%	6.0%	5.4%	N
Royalties – to non residents	20.0%	18.0%	8.0%	7.2%	Y
Shipping and Air Charter Service (by a PE)	2.64%	2.376%	0.72	0.648%	Y
Payments for (most) services to residents (or PE)	6.0%	5.4%	2.4%	2.16%	N
Payments for services to non-residents	20.0%	18.0%	8.0%	7.2%	Y

## Greater Sunrise Field

The Sunrise and Troubadour fields (collectively known as “Greater Sunrise”) are estimated to contain some 8 trillion cubic feet of gas, and 300 million barrels of condensate. Greater Sunrise straddles waters falling within the JPDA (approximately 20.1 %) and waters that are claimed exclusively by both Australia and Timor-Leste.

In respect of the disputed areas, the Timor Sea Treaty (Annex E) and the Sunrise International Unitisation Agreement (“IUA”) acknowledged that production from the Greater Sunrise fields would be distributed on the basis that 20.1% would be attributable to the JPDA and 79.9% would be attributed to Australia. Effectively, this gives Timor-Leste the right to tax 90% of the

portion of the Greater Sunrise area which lies in the JPDA (i.e.  $90\% \times 20.1\% = 18.09\%$ ). Australia's taxable portion is therefore 79.9% plus its entitlement to 10% of the area which lies in the JPDA ( $10\% \text{ of } 20.1\% = 2.01\%$ ).

Annex E to the Timor Sea Treaty, also provided for the renegotiation of the unitisation for the hydrocarbon reserves contained in Greater Sunrise. On 12 January 2006, Timor-Leste and Australia concluded negotiations on this matter, with the signing of the Certain Maritime Agreements in the Timor Sea ("CMATS") Treaty.

CMATS came into force on 23 February 2007 and extends for a period of 50 years or the earlier of certain events including the cessation of petroleum exploitation. It provides for a moratorium on claims by either party in relation to their sovereign rights, jurisdiction and maritime boundary for the period of the agreement.

The key feature of CMATS is that Timor-Leste and Australia shall share equally in the revenue derived directly from the production of petroleum in Greater Sunrise insofar as it relates to the upstream exploitation of that petroleum. The value of such petroleum is to be determined on the basis of arm's length principles. It is important to note that the mechanism for sharing revenue equally between the two nations does not disturb the calculation of tax under the Timor Sea Treaty and Sunrise IUA (i.e. the 79.9% Australia / 20.1% JPDA calculation above).

# Regulations/Documents of Relevance

## UNTAET Regulations

- UNTAET Regulation 1999/1.
- UNTAET Regulation 2000/12.
- UNTAET Regulation 2000/18 of July 2002 (as amended).

## Timor-Leste Sovereign Law

- Taxation of Bayu-Undan Contractors Act – Law No. 3/2003.
- Law on Commercial Companies – Law No. 4/2004.
- Law on External Investment – Law No. 5/2005.
- Petroleum Taxation Act – Law No. 8/2005.
- Petroleum Fund Law – Law No.9/2005.
- Petroleum Law – Law No. 13/2005.
- Taxes and Duties Act – Law No. 8/2008.
- Code of Business Registration – Decree Law No. 6/2007.

## International Agreements

- Timor Sea Treaty between Australia and Timor-Leste signed on 20 may 2002.
- Sunrise International Unitisation Agreement between Australia and Timor-Leste signed on 6 March 2003.
- Certain Maritime Agreements in the Timor Sea Treaty between Australia and Timor-Leste signed on 12 January 2006.

## **Rulings**

- ETRS Public Rulings 2001/1 to 2001/11.

## **Indonesian Law (at 25 October 1999)**

- The Law on Income Tax - Law No. 10/1994. The Amendment of Law No. 7/1983 on Income Tax as amended by Law No. 7/1994.
- The Law of Value Added Tax - Law No. 11/1994. The Amendment of Law No. 8/1983.

## Appendix B

# Tax Regime Matrix

	Part A	Part B	Part C
	Non-JPDA – 100% Timor-Leste		
	Non-PSC	Non-Annex F PSCs	
	Non-Oil and Gas (general tax regime)	Oil and Gas (non-JPDA)	JPDA (non-Annex F)
Foundation Laws:	TDA (excluding Chapter IX).	TDA (Specifically modified by Chapter IX).	TDA (Chapter IX only).
Comments:	The TDA provides the framework for the general taxation regime in Timor-Leste. However, it does not provide a tax administration, offences, sanctions or collection framework (UNTAET 2000/18 continues in this regard).	The TDA repeals the previous Petroleum Tax Act. UNTAET 2000/18 continues for tax administration.	The TST (including Tax Code -Annex G) applies, meaning tax levied in the JPDA is at 90% of the rates set out under the TDA. Indonesian VAT at 25/10/99 continues to apply. UNTAET 2000/18 continues for tax administration.
<b>Main Features</b>			
Effective taxable Portion	100%	100%	90%
Income tax rate - PSC Contractor	N/A	30%	30%
- Sub-contractor	N/A	10%	N/A (but will generally be subject to WHT)
- Other corporate/PE	10%	10%	Progressive rates
- Individual	0% if < \$6k p.a. 10% if >\$6k p.a. No income tax on wages subject to WIT.	Different rates for employees of Contractors and non-Contractors	Different rates for employees of Contractors and non-Contractors
Wage Income Tax -Payment to resident	0% if < \$6k p.a. 10% if >\$6k p.a.	Various rates (0%-30%)	Various rates
-Payment to non-resident	10% (final)	20% (final)	20% (final)
Branch profit tax	N/A	N/A	N/A
WHT on Services -payment to resident/PE	Various rates	12% (final) or 6% (final)	6% (final)
-payment to non-resident	10% (final)	6% (final)	6% (final)
Supplemental petroleum tax	N/A	Applicable for Contractor	Applicable for Contractor
VAT	N/A	N/A	10%
Interest deductibility	No longer deductible	Contractor only – equal to interest income + 25% of net non-interest income	Contractor only – equal to interest income + 25% of net non-interest income

### NOTES:

- The TDA consolidates the tax regimes applicable to Timor-Leste, other than the Law on the Taxation of Buyu-Undan Contractors (Section 4). This includes the taxation of Oil and Gas (Chapter IX) which was previously governed by the Petroleum Tax Act.
- At present, the TDA preserves the previous tax administration, collection, offences and sanctions as provided under UNTAET 2000/18.

<b>Part D</b>		
<b>JPDA – 90% taxed by Timor-Leste (10% Australia)</b>		
<b>Annex F PSCs</b>		
<b>Bayu Undan PSCs 03-12 and 03-13 (excluding EKKN)</b>	<b>EKKN (PSC 91-12)</b>	<b>Greater Sunrise PSCs 03-19 and 03-20</b>
Indonesian tax laws at 25/10/99, modified by ToBUCA.	Indonesian tax laws at 25/10/99.	Indonesian tax laws at 25/10/99 as modified by the Sunrise IUA.
Special regime to enable the gas re-cycle phase of Bayu Undan.  The TST (including Tax Code -Annex G) applies, meaning tax levied in the JPDA is at 90% of the rates under Indonesian tax laws at 25/10/99 as modified by ToBUCA.	Regime covering the early liquids phase of Buyu-Undan PSC 91-12.  The TST (including Tax Code -Annex G) applies, meaning tax levied in the JPDA is at 90% of the rates under Indonesian tax laws at 25/10/99.	The Sunrise IUA creates the taxation split 20.1% JPDA / 79.9% Australia. CMATS is a separate government revenue sharing mechanism (50% Australia / 50% Timor-Leste).  The TST (including Tax Code -Annex G) applies, meaning tax levied in the JPDA is at 90% of the rates under Indonesian tax laws at 25/10/99 as modified by the Sunrise IUA.
90%	90%	$90\% \times 20.1\% = 18.09\%$
30% (exemption for export pipeline)	Progressive rates	Progressive rates
Progressive rates	Progressive rates	Progressive rates
Progressive rates	Progressive rates	Progressive rates
Progressive rates	Progressive rates	Progressive rates
Various rates	Various rates	Various rates
20% (final)	20% (final)	20% (final)
N/A	20%	20%
Various (reduced) rates	Various rates	Various rates
8% (final)	20% (final)	20% (final)
Applicable for Contractor	N/A	N/A
10%	10%	10%
N/A	N/A	N/A

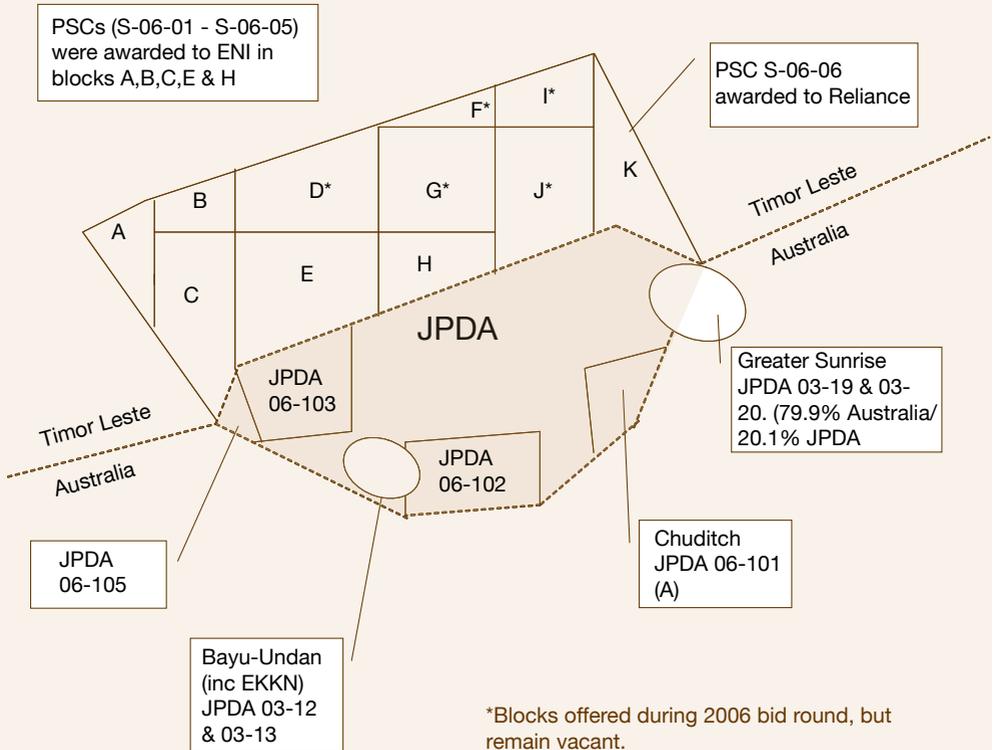
3. Indonesian Tax Law at 25/10/1999 includes Income Tax, VAT, Sales tax and the General Tax provisions.
4. Australian tax law applies on the remaining 10% of income from the JPDA.  
The Progressive rates for Income Tax purposes are 10% (on the first \$3,368), 15% (on the next \$3,368) and 30% (on income over \$6,737).

## PSC Possible Classifications

PSCs	Current Operator	Status / Project	Tax Regime Matrix	Comments
S-06-01 (Area A) S-06-02 (Area B) S-06-03 (Area C) S-06-04 (Area E) S-06-05 (Area H)	ENI Group	Exploration	B	Awarded in 2006 as part of Timor-Leste's inaugural offshore bid round for its sovereign territory.
S-06-06 (Area K)	Reliance Industries Limited	Exploration	B	Awarded in 2006 as part of Timor-Leste's inaugural offshore bid round for its sovereign territory.
JPDA 06-101(A)	Minza Oil and Gas Limited	Discovery	C	Includes the Chuditch gas field discovered in 1998.
JPDA 06-102	Petronas Group	Discovery	C	Discoveries in four wells - Coleraine-1, Fohn-1, Minotaur-1 and Naga-1.
JPDA 06-103	Oilex Group	Exploration	C	Located near the producing oil & gas fields at Laminaria, Coralina, EKKN and Bayu-Undan.
JPDA 06-105	ENI Group	Discovery	C	Includes the Jahal, Kuda Tasi and Kitan Oil field's first discovered in 1996 (formally JPDA 03-01).
JPDA 03-12	Conoco Phillips Group	LNG Production	D	Bayu-Undan Project (formally PSC 95-12). This PSC includes the EKKN area.
JPDA 03-13	Conoco Phillips Group	LNG Production	D	Bayu-Undan Project (formally PSC 95-13).
JPDA 03-19	Woodside Group	Discovery	D	Greater Sunrise Project (formally PSC 95-19).
JPDA 03-20	Woodside Group	Discovery	D	Greater Sunrise Project (formally PSC 95-20).

\* See Appendix D for a geographical representation of the above PSCs

# PSC Map



This map is not to scale. It is intended for illustrative purposes only.

# Company Registration Process

The Commercial Registry Code provides the requirements for establishing a Timor-Leste limited liability company:

Pay registration fees and deposit of minimum capital requirement at the Banco Nacional Ultramarino (BNU).	1 day
Obtain criminal record clearances from the Ministry of Justice (MIJ) for founders, shareholders, directors and management.	1 day
Verify uniqueness of company name and register at the Ministry of Tourism, Commerce and Industry (MTCI).	1 day
Obtain proof of business address (lease or title) from the Department of Land and Property.	1 day
File company statute with the MIJ (cost \$US 100)	3 days
Publish company statutes in the official gazette (in practice this is not enforced)	30 days
Apply for a Tax Identification Number (TIN) with the TLRS.	7 days
Notify labor department (not a legal requirement, but practically required)	2 days
Apply for temporary business license at the Ministry of Tourism, Commerce and Industry	35 days
Make a company seal	2 days

Source: The World Bank: Doing Business – Starting a business in Timor-Leste

## Glossary of Abbreviations

<b>Timor-Leste</b>	<b>Definition</b>
AMP	Alliance with a Parliamentary Majority
Annex F PSCs	PSCs detailed in Annex F of the Timor Sea Treaty
ANP	Autoridade Nacional do Petróleo
ANR	Accumulated Net receipts
APT	Additional Profit Tax
BNU	Banco Nacional Ultramarino
CFA	Central Fiscal Authority
CIF	Cost, Insurance and Freight
CMATS	Certain Maritime Arrangements in the Timor Sea Treaty between Australia and Timor-Leste
EKKN	Elang Kakatua-Kakatua North
ENI	Estimated Net Income
f.o.b	free on board
Fretilin	Frente Revolucionária do Timor-Leste
GATT	General Agreement on Tariffs and Trade

## Appendix F

<b>Timor-Leste</b>	<b>Definition</b>
GDP	Gross Domestic Product
Law on Income Tax	Indonesian Tax Laws as at 25 October 1999
JPDA	Joint Petroleum Development Area as provided for in the Timor Sea Treaty (previously ZOCA)
LNG	Liquefied Natural Gas
MIJ	Ministry of Justice
MoF	Minister of Finance
MTCI	Ministry of Tourism, Commerce and Industry
PE	Permanent Establishment
PSC	Production Sharing Contract
PTA	Petroleum Taxation Act
SPT	Supplemental Petroleum Tax
Sunrise IUA	International Unitisation Agreement of the Greater Sunrise Fields Agreement
TDA	Taxes and Duties Act

**Timor-Leste****Definition**

Timor Gap Treaty	Predecessor to the Timor Sea Treaty. An agreement between Australia and Indonesia to jointly share in the exploration of the disputed geographical area known as Zone A (i.e. ZOCA) signed on 11 December 1989 and operative from 9 February 1991 to 20 May 2002.
Timor Sea Treaty	The successor to the Timor Gap Treaty. An agreement between Timor-Leste and Australia entered into and effective from 20 May 2002.
TIN	Tax Identification Number
TLRS	Timor-Leste Revenue Service
ToBUCA	Taxation of Bayu-Udan Contractors Act
TST	Timor Sea Treaty
UN	United Nations
UNTAET	United Nations Transitional Administration in East Timor
VAT	Value Added Tax
WHT	Withholding Tax
WIT	Wage Income Tax
ZOCA	Zone of Cooperation – A, as provided for under the Timor Gap Treaty.

# PricewaterhouseCoopers Contacts

PricewaterhouseCoopers has extensive experience in advising on Timor-Leste as well as international tax matters.

This tax book has been prepared for the general information and assistance of those investing in Timor-Leste. It should not be used as a substitute for specific advice on a contemplated transaction.

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