Indonesian Production Sharing Contract

~ Fiscal Terms ~

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Outline

- Introduction
- Basic Concepts
- Sharing Variables
- Sharing Mechanism
- Fiscal Terms

Introduction - General

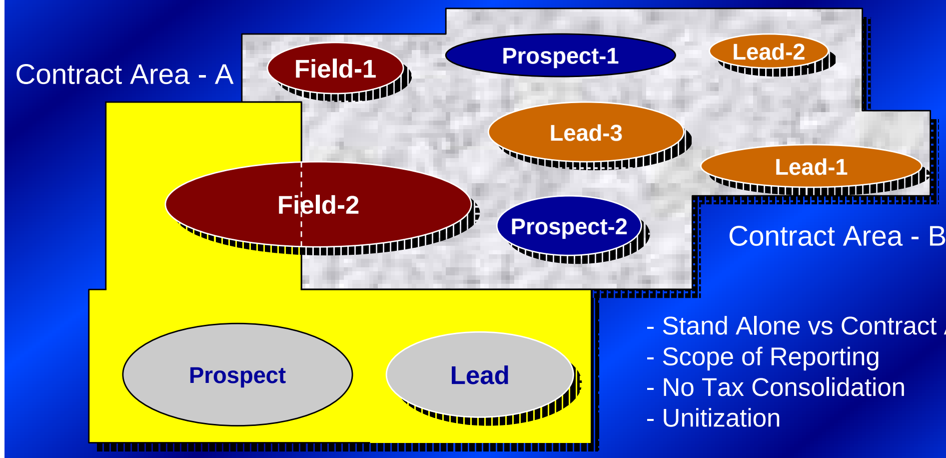
- All mineral oil and gas existing within the statutory mining territory of Indonesia are national richest controlled by the State.
- The government holds 'exclusive authority to mine'.
- The government established the 'Executive Agency for Upstream Oil & Gas Business Activities' (BPMIGAS).
- Business entities conduct oil and gas business based on cooperation contracts with BPMIGAS, mostly in the form of Production Sharing Contract (PSC).
- The PSC contracting parties are 'Contractor' and 'BPMIGAS'.
- The PSC shall prevent the government from any liability arising from the oil & gas business.

Introduction - Terms and commitments

- The contract term is 30 years to conduct exploration, development and production activities; extendable up to 20 more years.
- Normally the contract cannot be terminated during the first 2 or 3 years, except it is caused by a major breach of contract.
- The exploration period is the first 6 years of a contract term and extendable up to 4 more years.
- Typically, every 2 years of exploratory activities, a portion of contract area shall be surrendered, and finally leaving a sufficient size and shape to conduct petroleum operations.
- Normally it includes commitments of activities or expenditures to be spent for the succeeding years.

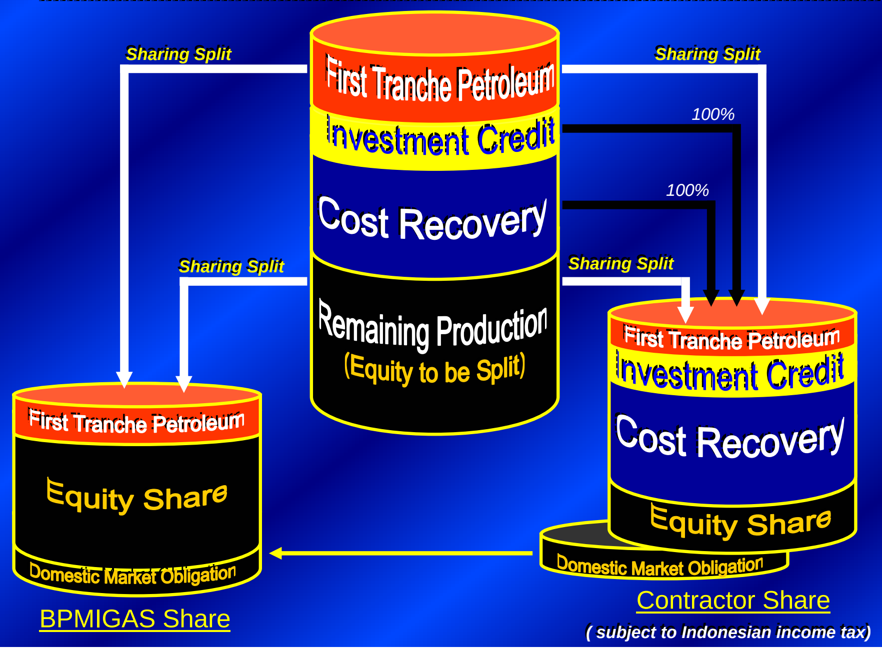
Basic Concept - Ringfencing

- A business entity operates only one contract area;
- When an oil company holds ownerships on several contract areas, a separate legal entity has to be established for each contract area.



- Stand Alone vs Contract Area
- Scope of Reporting
- No Tax Consolidation
- Unitization

Basic Concept – Sharing of Production



Sharing Variables

1. **Price / ICP (Indonesian Crude Price)**
2. **Production**
3. **Cost Recoverables**

Notes:

The PSC sharing mechanism is applied annually based on the gregorian's calendar year; therefore:

- The price used is the weighted average price of all crudes/gases produced and sold from the contract area;
- Production is the petroleum sold (lifting) during the calendar year;
- Cost Recoverables are items/costs which are recoverables during the calendar year;

Oil and gas sharing are applied separately, due to the difference in sharing splits and investment credit rates for oil and gas.

Variable-1 Price – Indonesian Crude Price (ICP)

CRUDE OIL
(Nature : develop the fields then find the market)

QUOTED CRUDES : SLC, Senipah, Widuri, Cinta, Arjuna, Attaka, Duri

Current ICP Formula : 20% APPI + 40% Platt's + 40% RIM

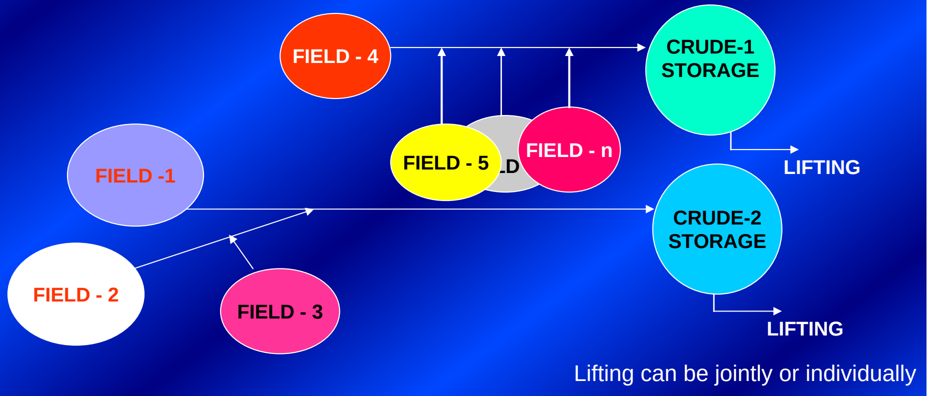
UNQUOTED CRUDES : related to a Quoted Crude

Example : Bula = Duri - $0.50

GAS
(Nature : typically the field developed after the market has been determined and it often involves external financing)
- **Long-term contract**
- **Varies ('negotiable', economically feasible)**
- **LNG Price formula mostly relates to crude oil export price**

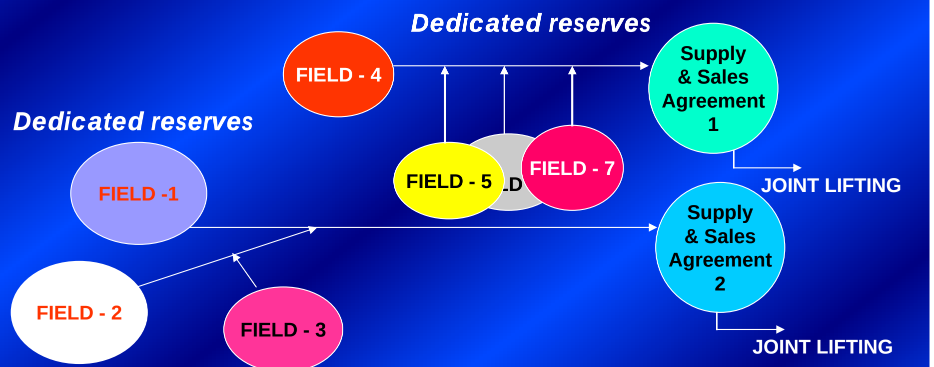
Variable-2 Production/Lifting - Oil

- Production from several different fields
- Grouped as per type of crude

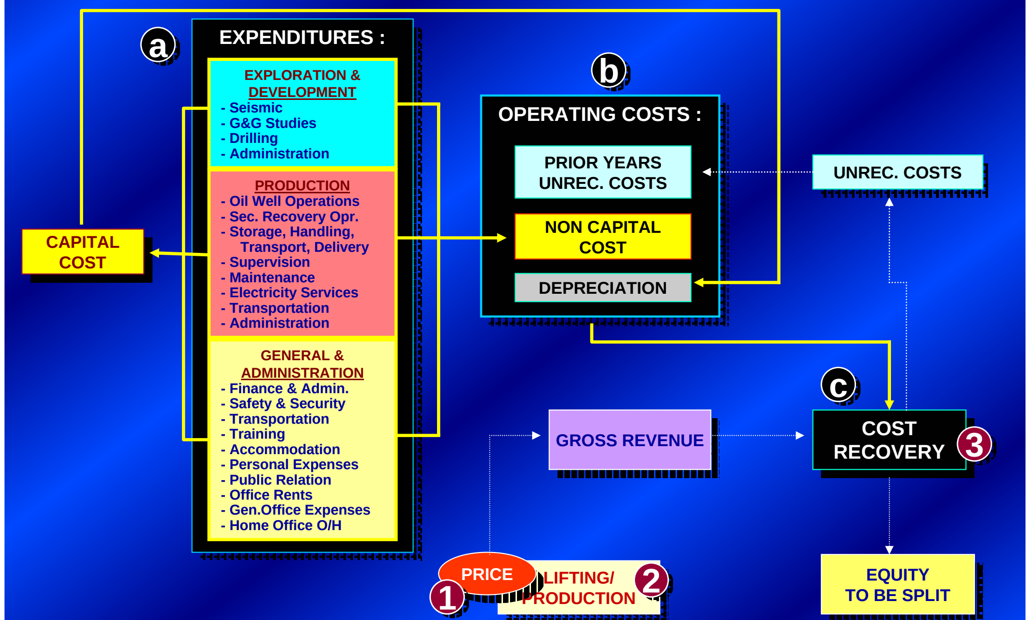


Variable-2 Production/Lifting - Gas

- Production from several different fields
- Grouped as per sales agreement, calculated as per PSC block



Variable-3 Cost Recovery - Put Together



Cost Recovery (1)

PSC ACCOUNTING PROCEDURES

For any Year in which commercial production occurs, Operating costs consist of

(a) current Year non-capital costs,
(b) current Year's depreciation for Capital Costs, and
(c) current Year's allowed recovery of prior year's unrecovered Operating Costs.

Cost Recovery is recovered operating costs from Gross Revenue. Cost Recovery is one element of the contractor's revenue.

Cost Recovery (2)

Oil & Gas Costs shall be separated due to the difference in sharing splits applicable for oil and gas.

- Oil Costs
- Gas Costs
- Common Costs : allocated based on relative revenue
- Common Support Costs : allocated based on equitable basis agreed by both parties.

Recovery from Oil/Gas Costs:

- If after commencement of production, the Natural Gas revenues do not permit full recovery of Natural gas costs, the excess shall be recovered from Oil revenues or vice versa.
- If production of either Gas or Oil has commenced while other has not, costs allocated in an equitable manner.

Expenditures – Non Capital

1. **Exploratory Survey:**
   Labor, materials & services used in aerial, geological, topographical, geophysical & seismic surveys, and core hole drilling
2. **Exploratory Drilling**
   Labor, materials & services used in drilling exploratory wells
3. **Other Exploratory Expenditures:**
   Temporary facilities used in exploration and purchase of G&G information
4. **Development Drilling:**
   Intangible development drilling, including access road and canals to wells
5. **Production Operations:**
   Labor, materials & services used in well operations, field production facilities, secondary recovery operations, storage, handling, transportation and delivery operations, repairs & maintenance, etc.
6. **Office Service and General Administration:**
   General Services incl. Technical services & related services, material services, transportation, rental of heavy engineering equipment, site rental & other rentals of services & property, personnel expenses, public relations, and other expenses abroad.

Expenditures – Other Non Capital

Overhead Allocation/Home Office charges:
Direct charges : identifiable
Overhead : determined by a detailed study approved by BPMIGAS, applied consistently and subject to review by Pertamina and Contractor.

Interest Recovery:
Interest may be recoverable, not exceeding prevailing commercial rates, dedicated for capital investment (usually production facilities),
Details of financing plan included in annual WP&B

Expenditures - Capital Costs

CAPITAL COSTS :

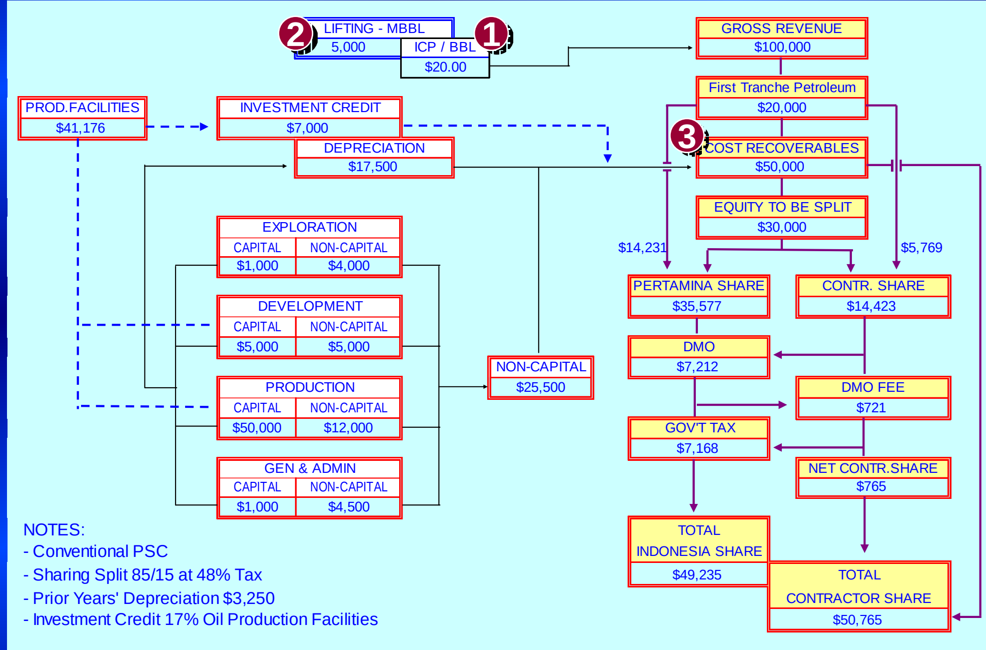
1. **Construction Utilities and Auxiliaries:**
   Workshops, power water facilities, warehouse, field roads & canals
2. **Construction Housing and Welfare:**
   Housing, recreational facilities, etc.
3. **Production Facilities;**
   Tangible development drilling, wellhead, flow lines, gathering station, treating plant & equipment, secondary recovery system, gas plants and steam system, delivery lines, storage facilities, offshore platform, jetties and anchorages
4. **Movables:**
   Drilling & production tools, equipment & instruments, barges, aircraft, automotive, construction equipment, furniture & office equipment, and miscellaneous equipment

Capital Assets Depreciation

>>> Declining Balance Method, >>>Depreciation factor - Group 1 : 50%
- Group 2 : 25%
- Group 3 : 10%

	OIL	GAS	
Group 1 :			
Automobiles	1.5 years	1.5 years	Group 1
Light Trucks and Tractor Units	2.0 years	2.0 years	Group 1
Heavy Trucks	3.0 years	3.0 years	Group 2
Buses	4.5 years		
Aircraft	3.0 years	3.0 years	Group 2
Construction Equipment	3.0 years	3.0 years	Group 2
Furniture & Office Equipment	5.0 years	5.0 years	Group 2
Group 2 :			
Construction Utilities & Auxiliaries	5.0 years	4.0 years	Group 3
Construction Housing & Welfare	10 years	10 years	Group 3
Production Facilities	5.0 years	4.0 years	Group 3
Railroad cars & Locomotives	7.5 years	7.5 years	Group 3
Water Transportation	9.0 years	9.0 years	Group 2
Drilling & Production Tools	5.0 years	4.0 years	Group 2

All Variables and Sharing Mechanism - Oil Case



Fiscal Terms

1. First Trance Petroleum
2. Tax Structure
3. Sharing Split
4. Investment Credit
5. Cost Recovery
6. Domestic Market Obligation
7. Capital & Non-Capital Expenditures

First Tranche Petroleum (FTP)

PSC - STANDARD CLAUSE :

" . . . the Parties shall be entitled to take and receive each Year 20% of all Petroleum produced and saved . . .

before any deduction for the recovery of Investment Credit and Operating Costs . . .

Such First Tranche Petroleum shall be shared between BPMIGAS and CONTRACTOR in accordance with sharing splits . . ."

FTP DIFFERS FROM ROYALTY :

- FTP is shared between the Parties.
- FTP has no impact when financial operation runs normally.
- FTP is designed to ensure the minimum income for the State.

Note:
For the PSC signed in 2002&2003, the whole FTP goes to BPMIGAS (Gov't)

Case on First Tranche Petroleum

US Dollars

Cost to be recovered	with FTP 10,000	No FTP 10,000	with FTP 20,000	No FTP 20,000
1 Lifting - mbbl	1,000	1,000	1,000	1,000
2 Price per bbl - $/bbl	20.00	20.00	20.00	20.00
3 Gross Revenue	20,000	20,000	20,000	20,000
4 First Tranche Petroleum	4,000	0	4,000	0
5 Gross Revenue after FTP	16,000	20,000	16,000	20,000
6 Investment Credit	500	500	0	0
7 Cost Recovery	10,000	10,000	16,000	20,000
8 Equity To Be Split	5,500	9,500	0	0
9 CONTRACTOR SHARE:				
FTP Share	1,154	0	1,154	0
Equity Share	1,587	2,740	0	0
D M O	(1,442)	(1,442)	0	0
D M O Fee (New Oil)	1,442	1,442	0	0
Taxable Share	3,240	3,240	0	0
10 Gov't Tax Entitlement	(1,555)	(1,555)	0	0
11 Net Contractor Share	1,685	1,685	1,154	0
12 Total Share	11,685	11,685	17,154	20,000
13 Unrecovered Costs	0	0	4,000	0
14 Indonesia Share	8,315	8,315	2,846	0

Tax Structure

- Contractor shall pay the income tax to GOI
- Excluded other taxes and levies

INCOME TAX STRUCTURE	1994	1984	Prior to 1984
Corporate Tax (CT)	30%	35%	45%
Dividend Tax (DT)	20%	20%	20%

Taxable Income 100%			
Corporate Tax	30%	35%	45%
Dividend Tax: *DT(100%-CT)*	14%	13%	11%
Effective Tax Rate	44%	48%	56%

Note: Dividend Tax subject to tax treaty, and affects the tax rates

Sharing Split

- Sharing Splits include tax component
- Sharing Split is applicable to First Tranche Petroleum, Equity to be Split and Domestic Market Obligation (DMO)

Standard Sharing Splits

After Tax Split	Tax Rate	Contractor Split (before tax)	BPMIGAS Split (before tax)
85/15	56%	15/(100 - 56) = 34.0909%	65.0909%
	48%	15/(100 - 48) = 28.8462%	71.1538%
	44%	15/(100 - 44) = 26.7867%	73.2133%
70/30	56%	30/(100 - 56) = 68.1818%	31.8282%
	48%	30/(100 - 48) = 57.6923%	42.3077%
	44%	30/(100 - 44) = 53.5714%	46.4286%

Investment Credit

PSC - STANDARD CLAUSE :

"Contractor may recover an investment credit amounting to 17% of the capital investment costs directly required for developing Crude Oil production facilities . . . of each new field out of deduction from gross production before recovering operating costs, commencing in the earliest production Year or Years before tax deduction (to be paid in advance in such production Year when taken).

The Investment Credit may be applied to new secondary recovery and tertiary recovery EOR projects but is not applicable to "interim production schemes" or further investment to enhance production and reservoir drainage in excess of what was contemplated in the original project as approved by BPMIGAS".

Case on Investment Credit

	Costs to be Recovered	No I/C 10,000	with I/C 10,000	No I/C 20,000	with I/C *) 20,000
1	Lifting - mbbl	1,000	1,000	1,000	1,000
2	Price per bbl - $/bbl	20.00	20.00	20.00	20.00
3	Gross Revenue	20,000	20,000	20,000	20,000
4	First Tranche Petroleum	4,000	4,000	4,000	4,000
5	Gross Revenue after FTP	16,000	16,000	16,000	16,000
6	Investment Credit	0	2,000	0	100
7	Cost Recovery	10,000	10,000	16,000	15,900
8	Total Recoverables	10,000	12,000	16,000	16,000
9	Equity To Be Split	6,000	4,000	0	0
10	CONTRACTOR SHARE :				
	FTP Share	1,154	1,154	1,154	1,154
	Equity Share	1,731	1,154	0	0
	D M O	0	1,442	0	0
	D M O Fee (New Oil)	0	(1,442)	0	0
	Taxable Share	2,885	4,308	0	100
11	Gov't Tax Entitlement	(1,385)	(2,068)	0	(48)
12	Net Contractor Share	1,500	240	1,154	1,106
13	Total Contractor Share	11,500	12,240	17,154	17,106
14	Unrecovered Costs	0	0	4,000	4,100
15	Indonesia Share	8,500	7,760	2,846	2,894

*) I/C (Investment Credit) is partially claimed starting in the first years of production

Domestic Market Obligation

PSC - STANDARD CLAUSE :
after commercial production commences, . . . Contractor agrees to sell and deliver a portion of the share of Crude oil to which it is entitled pursuant to Section 6.1.3 and 6.3.1 *(6.1.3 = Equity share; 6.3.1 = FTP share)* . . .

Effective Formula for DMO :
25% x Sharing Split x Production

DMO Fee:
US$0.20, 10%, 15% or 25% the price, as stated in the contract.

When a portion of operating costs remains unrecovered, contractor shall be relieved from the obligation.

Case on Domestic Market Obligation

	Case-1	Case-2	Case-3
Data at year end			
Price/bbl	25.00	20.00	23.00
Total Lifting - mbbl	1,000	1,000	1,000
Investment Credit - $	0	0	0
Cost Recovery - $	18,000	18,000	18,000
Computation:			
Total Lifting	1,000	1,000	1,000
FTP	200	200	200
Investment Credit	0	0	0
Cost Recovery [1]	720	800	783
Equity	80	0	17
Contr.FTP Share [2]	58	58	58
Contr.Equity Share [3]	23	0	5
Total	81	58	63
DMO (normal)	72	72	72
DMO Delivered	72	0	63

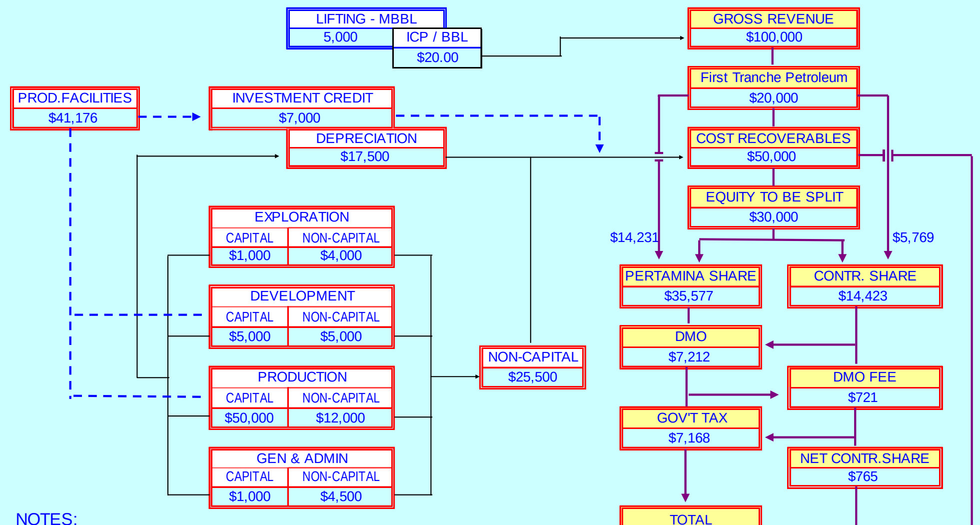
Notes:

1) Cost recovery - $ / Price/bbl

2) 28.85% x FTP

3) 28.85% x Equity

Summary - Sharing Mechanism (Oil)



NOTES:
- Conventional PSC
- Sharing Split 85/15 at 48% Tax
- Prior Years' Depreciation $3,250
- Investment Credit 17% Oil Production Facilities

Summary - Contractor Cashflow

Simple Equation **:**

PROCEED (Cash – in) **–** **OUTLAYS** (Cash – Out) **=** **NET CASHFLOW** (After Tax)

PROCEED (Cash – in):

1. Lifting
   - Joint Lifting
   - Individual Lifting
2. DMO Fee
   - Monthly billings
3. Under Lifting Settlement
   - after year end

OUTLAYS (Cash – Out):

1. Expenditures
   - Exploration
   - Development
   - Production
   - Supporting
2. Income Tax
3. Over Lifting Settlement
4. Non-PSC Costs

Thank You