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Generating Extractive Industry Revenues

Kenya's Economic Successes, Prospects and Challenges

National Treasury, Central Bank of Kenya, IMF

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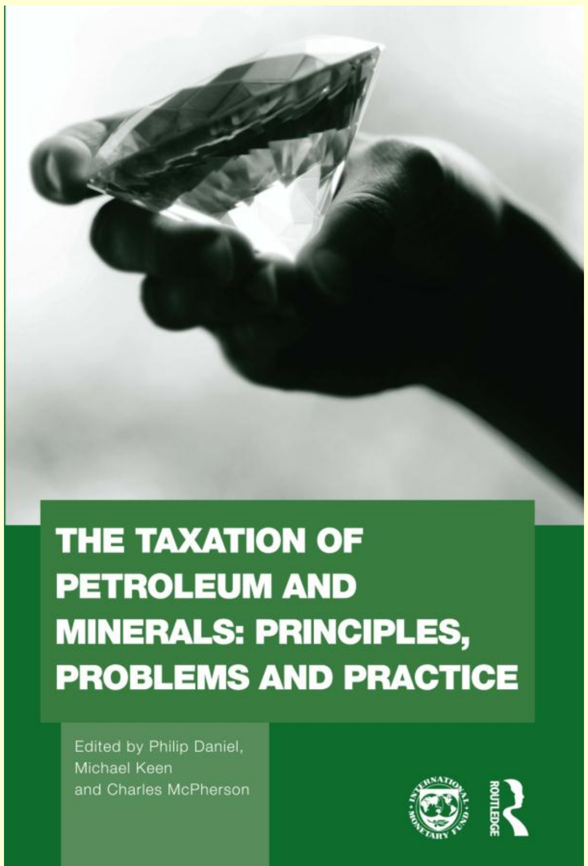
IMF (FAD) TA actively engaged and research-based



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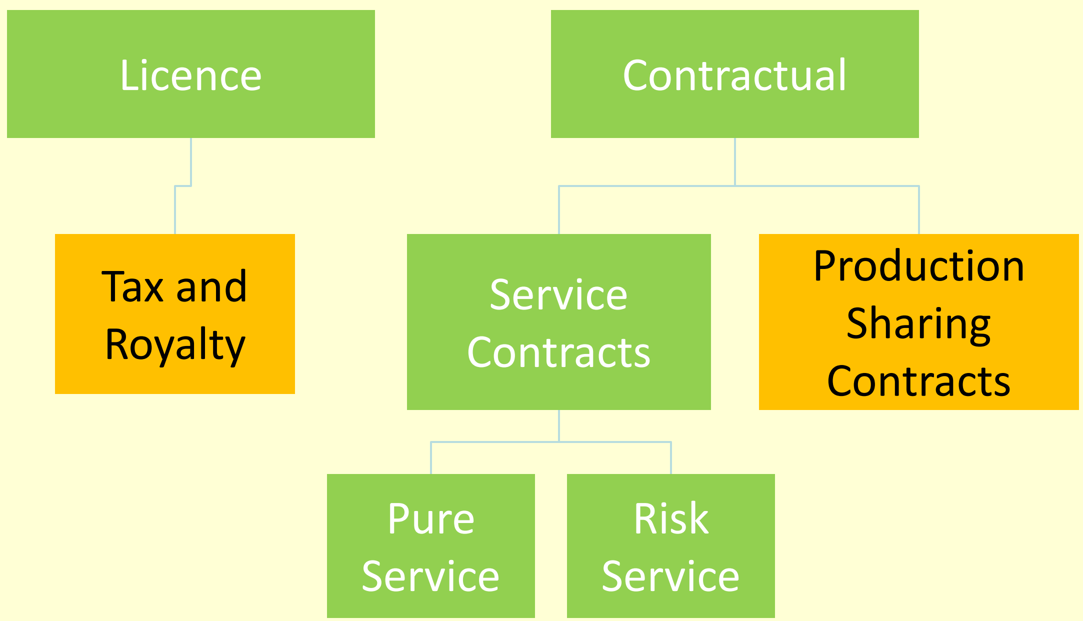
Central objectives

- Maximize PV of net government revenues
- Timing of receipts
- “Progressivity”
- Ease of administration (for authorities) and compliance (for taxpayers)

Types of Fiscal Regime



Government usually owns minerals in the ground

Licence:

- Investor has rights to 100% of production

PSC:

- Contractor has rights to a share of production

- Petroleum – Tax&Royalty and PSC systems most common
- Mining - Tax&Royalty; PSC uncommon
- Mechanics different, but economics can be equivalent
- Most countries have an "hybrid" system

Three main fiscal schemes (sometimes blended)…

- Contractual, including production sharing or service contracts
- Tax and royalty, with licensing of areas
- State ownership or participation
  - These can be made fiscally equivalent
  - Staff advice works within all three
    - Design to achieve efficiency and transparency in each case

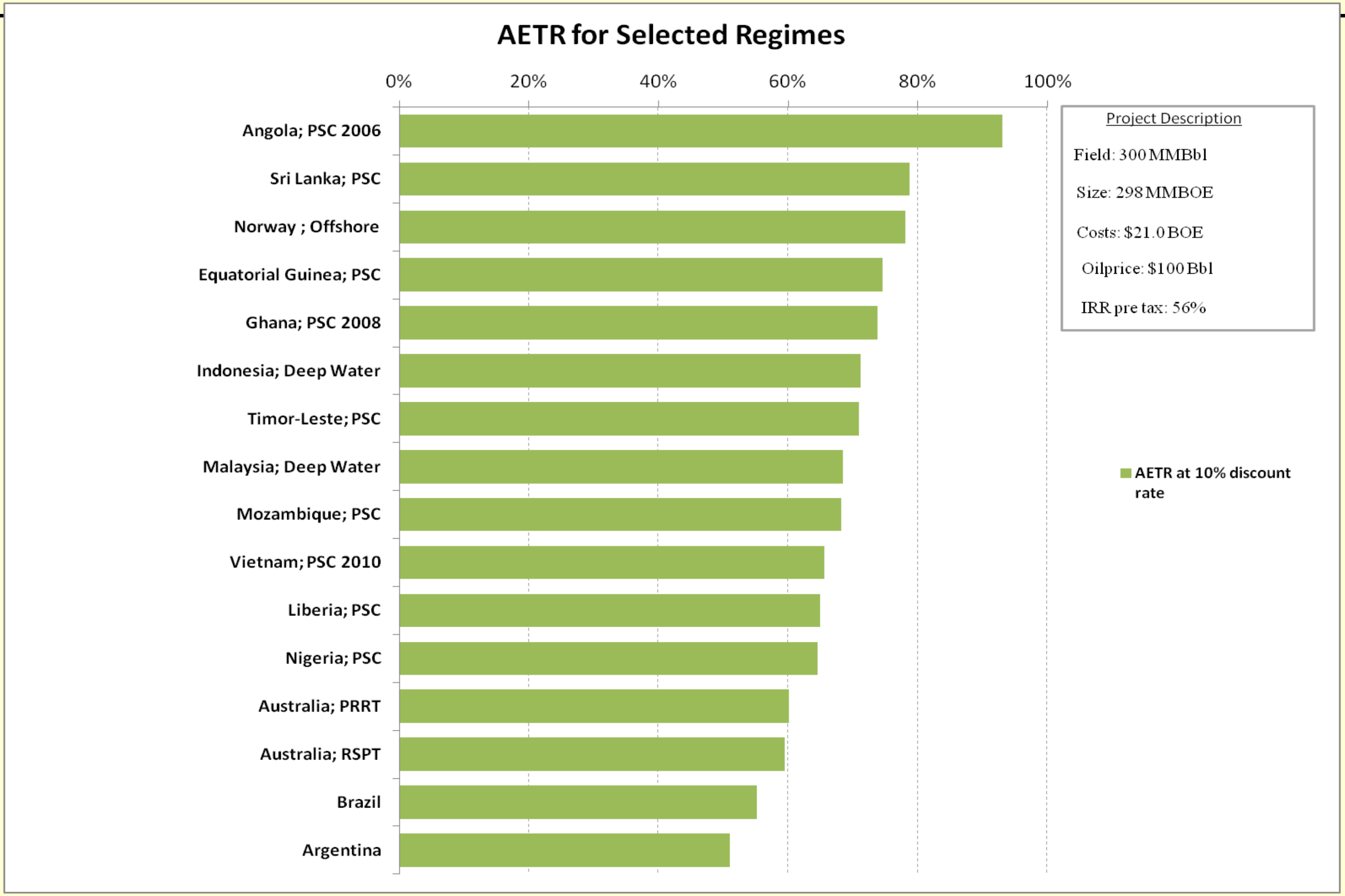
Fiscal Instruments for EI

- Bonuses (with bidding)
- Royalty
- Corporate income tax
- Explicit rent taxes
- State participation

Fiscal regimes for EI vary greatly

- Simulations for mining suggest government shares of 40-60 percent—but collection data suggest lower in practice
- For petroleum the simulated shares are higher: 65 to 85 percent
- Achieved shares below these ranges are cause for concern, or regret

FARI: Simulated petroleum field



Current Kenyan PSC Structure

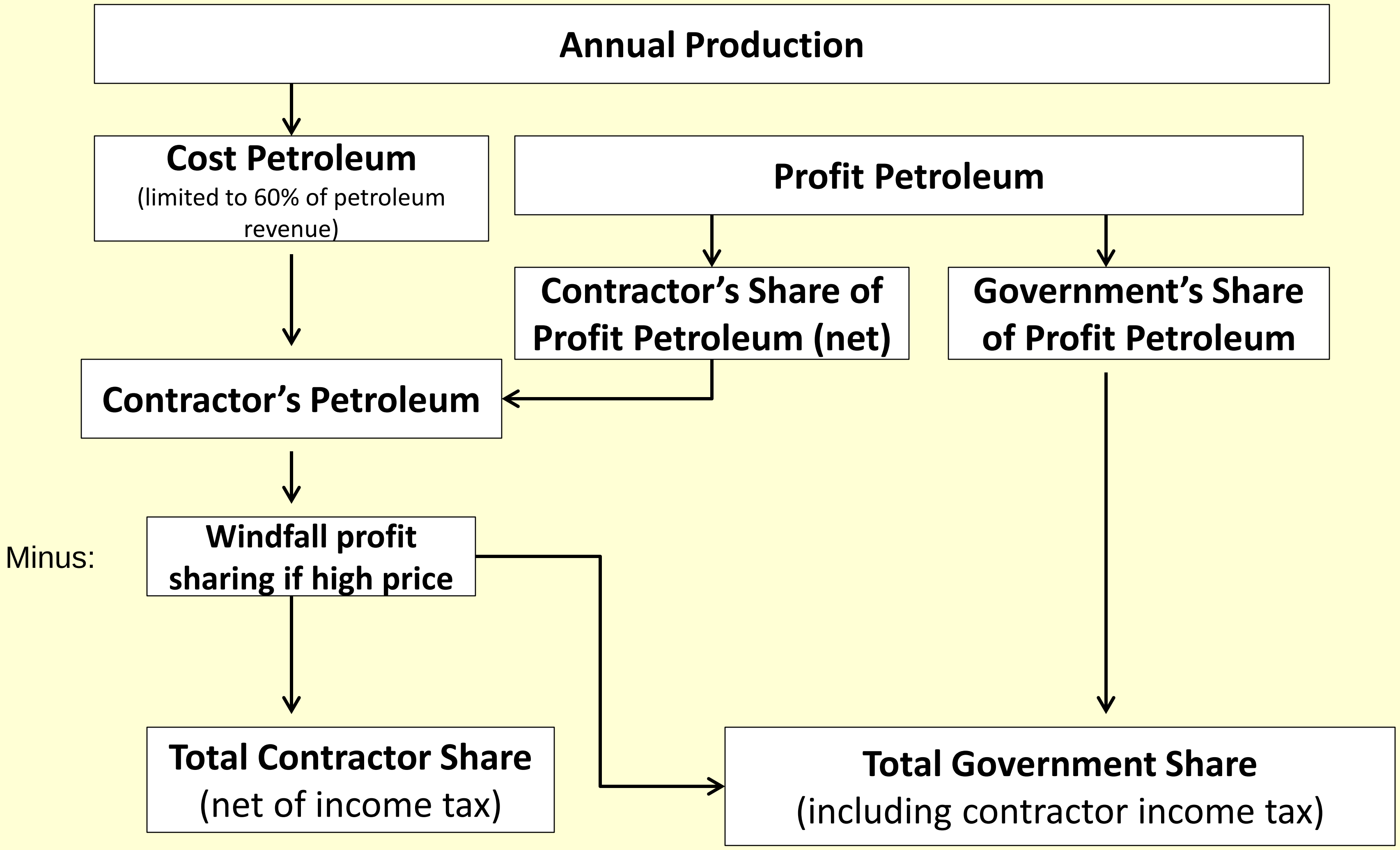
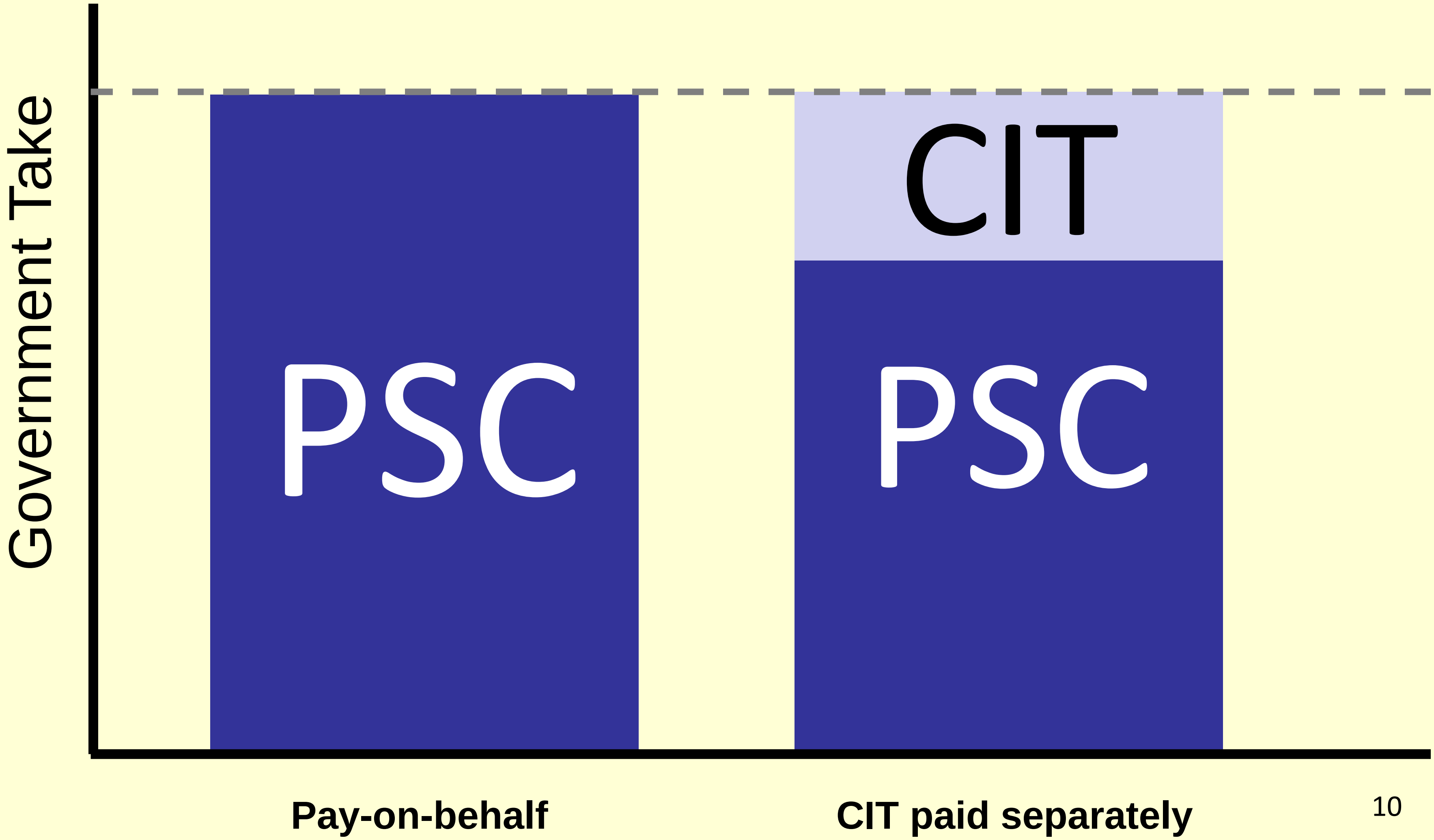
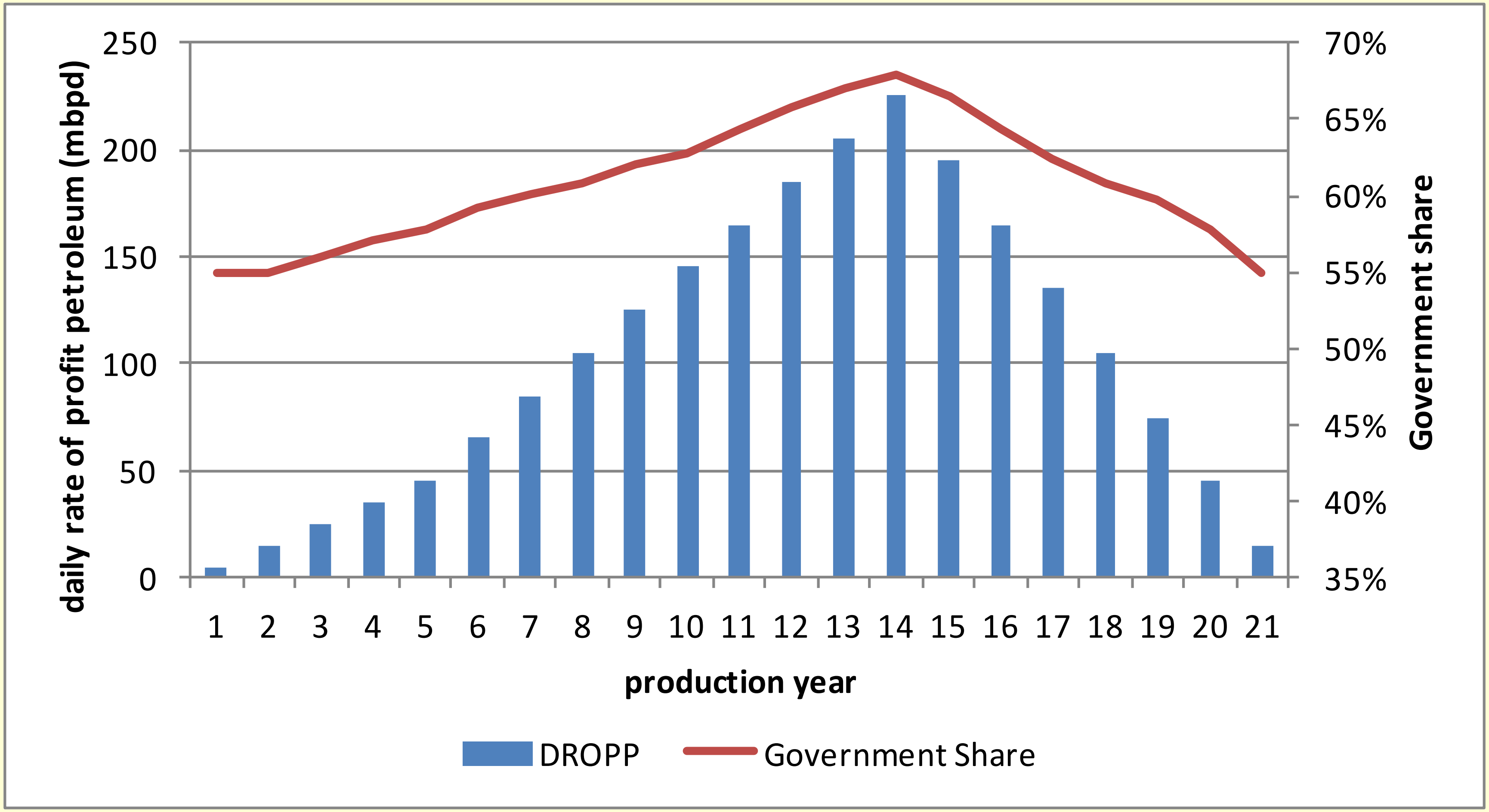


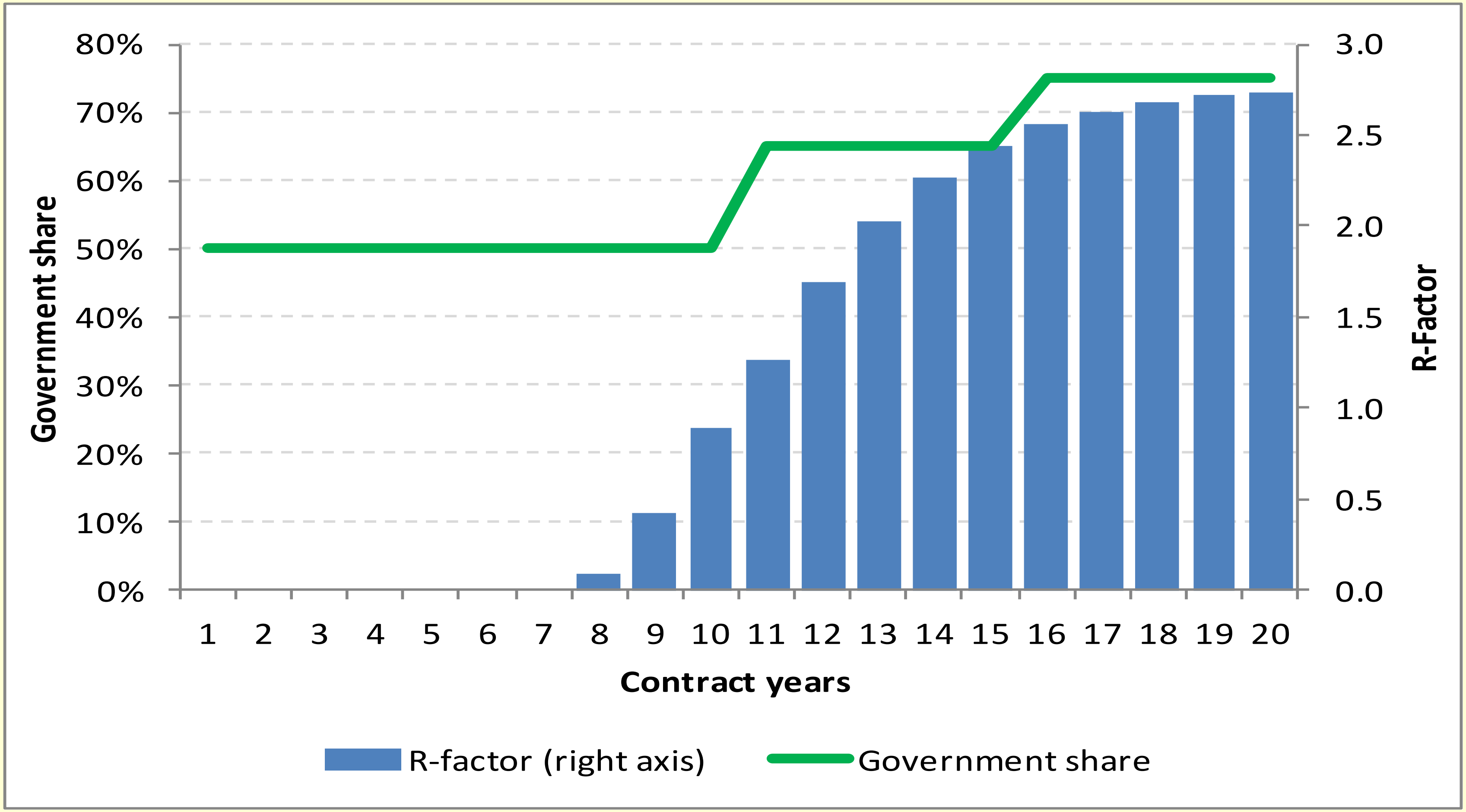
Illustration of Government Take under POB and Separate Payment of CIT



450 mm bbl Offshore Field

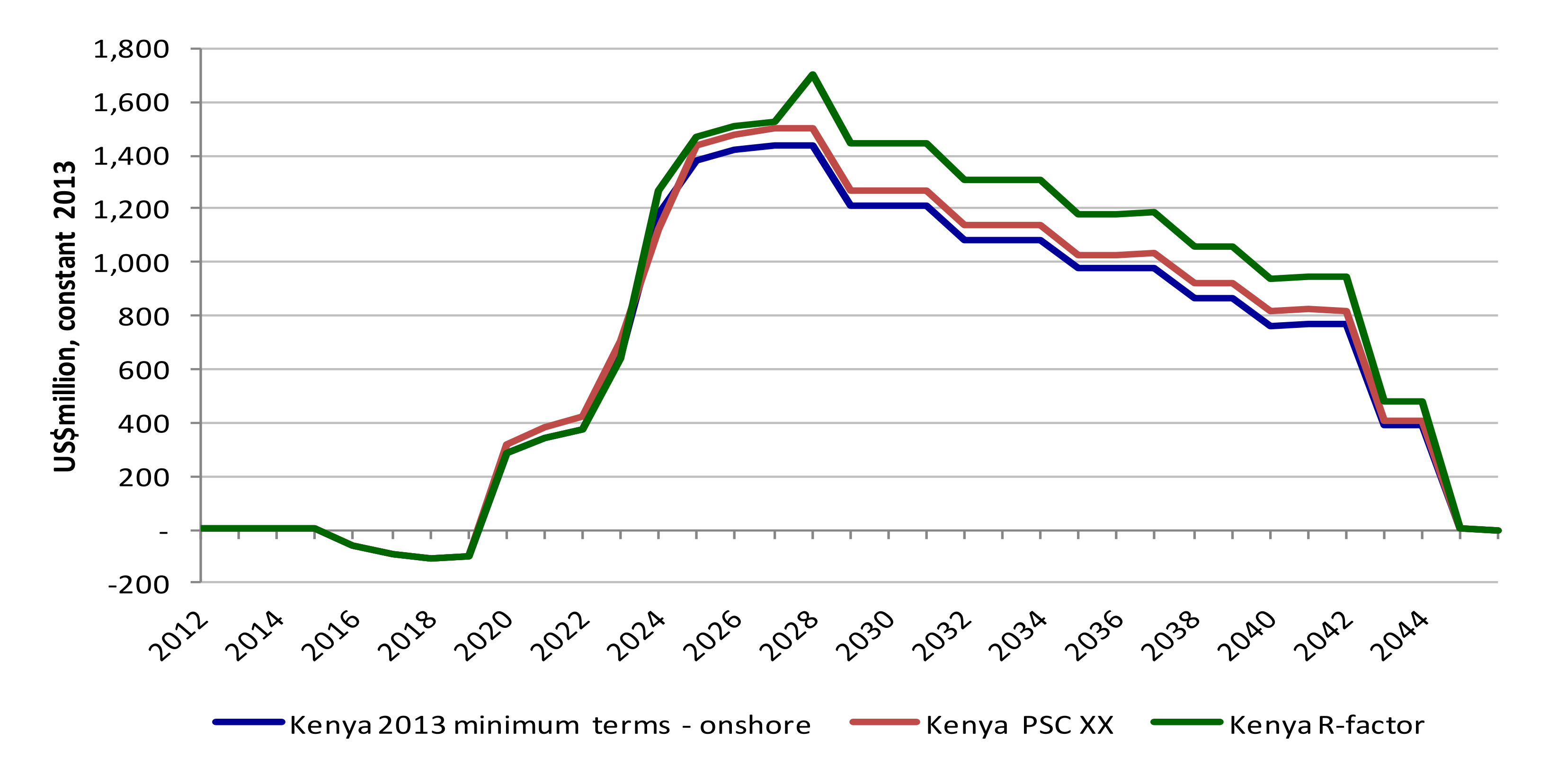


Three Tiered R-Factor Illustration



Government Revenue: R-factor vs. DROPP

Large oil field onshore (450 mmbbl), Oil Price at $90, pre-tax IRR 33%

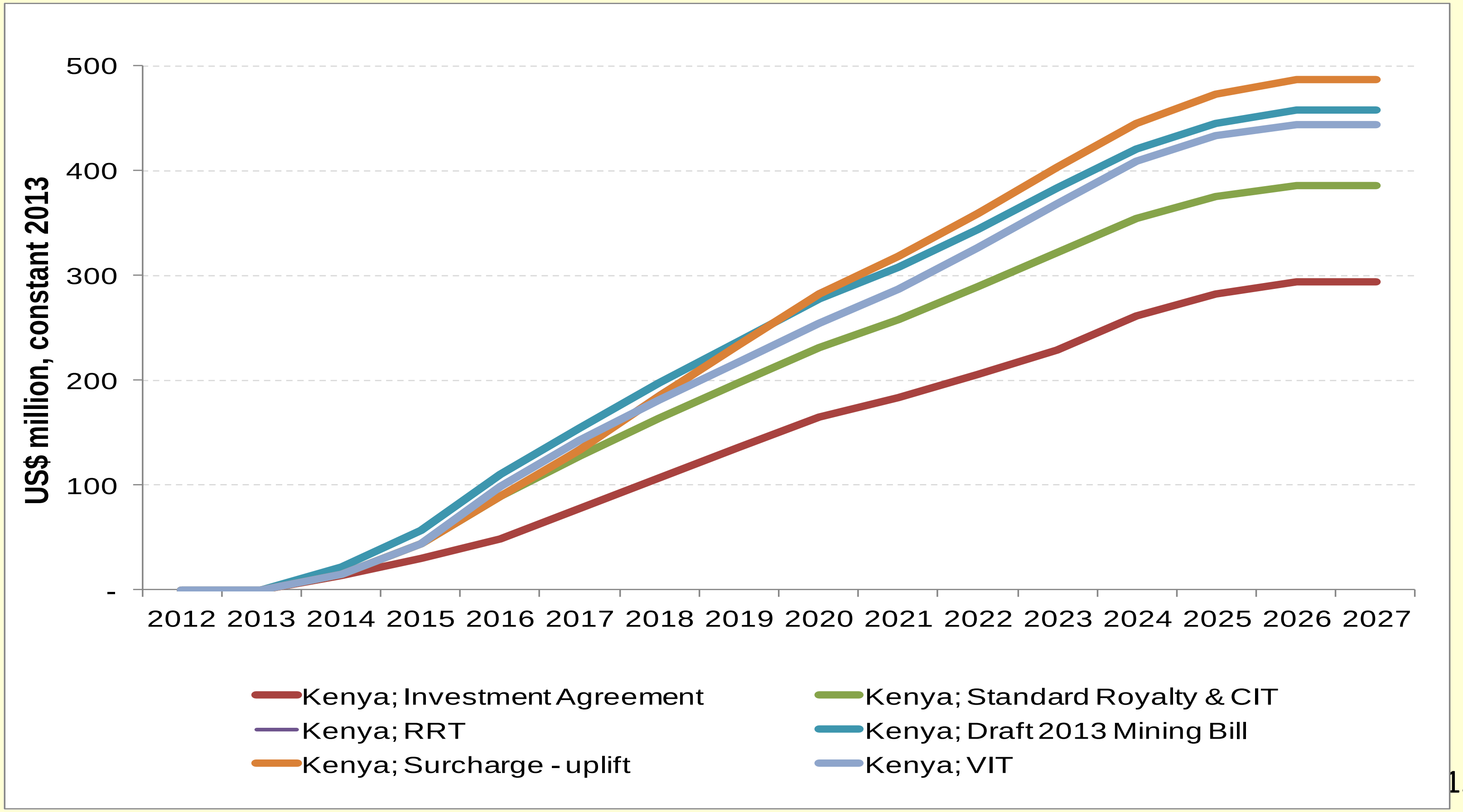


Fiscal regimes: mining

Taxes	Standard Regime	Specified Minerals	Stylized SML and Investment Agreement
Royalties	10% on diamonds; 5% on gold and precious metals; 3% on other minerals		Subject to negotiation or discretionary prescription in SMLs
CIT rate	30%		CIT reductions of up to 50% of the standard rate have been negotiated in Investment Agreements
Depreciation of capital expenditures for CIT purposes	Straight-line with 40% deduction in the first year, and 6 further annual installments of 10%	100%	Depends on whether the mineral has been defined as a "specified mineral" or not.
Withholding Taxes (subject to lower rates under DTAs)	Dividends - 10% for non-residents, 5% for residents; Interest - 15% for residents and non-residents;		Subject to negotiation or discretionary prescription in SMLs
VAT	Local sales - 16%; Export sales - zero rated		Remission of VAT may be provided under Investment Agreements
Custom duties	Machinery and spare parts used in mining imported by a licensed mining company are exempted		

Government Revenue: Different Tax Devices

Stylized Mineral Sands Project with a pre-tax IRR 33%



Where do we go?

- Develop a single fiscal regime for future mining leases, with royalties varying by mineral as at present.
- Maintain petroleum production sharing contracts, but
  - Modernize the model PSC for future contracts by introducing a petroleum profit sharing based on an economic criterion, such as the R-factor.
- Define gas terms for production sharing in existing contracts
  - By scale of profit gas?
  - By R-Factor or other means?
- Determine the preferred commercial configuration of the upstream, pipeline and LNG segments in any gas export project.
- Introduce competive bidding and new transparency measures.