Tax Issues Raised by LNG Projects
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Overview

- The purpose of this presentation is to -
  - provide an introduction to some of the principal types of taxes that may be applicable to an LNG project,
  - give practical guidance on how to plan and structure an LNG project to minimize taxes, and
  - give examples of how certain types of taxes can be allocated in an LNG SPA (using as an example the AIPN Master SPA)
Two Basic Points about Taxes

1. Taxes can represent a significant cost of an LNG project. Therefore, an objective of any company making an investment in an LNG project will be to minimize taxes imposed in connection with the project.

2. Tax planning can be complex and time consuming, so think about taxes early and often.
Income or Profit Taxes

- What most people think of when they hear "taxes"
- A sponsor of an LNG project may be subject to income or profit taxes in one or more jurisdictions as a result of -
  - sales of LNG,
  - the performance of liquefaction services, regasification services, LNG storage, or gas storage,
  - the transportation of LNG, and/or
  - the receipt of distributions on equity investment or interest on loans to the project entity
Income or Profit Taxes

- Income taxes may not represent a substantial additional cost to sponsors that are subject to a "foreign tax credit" regime in their home country.
- However, the sponsor may not have the practical ability to benefit from foreign tax credits if the sponsor:
  - is a tax resident of a jurisdiction where tax rates are lower than rates applicable to the LNG project,
  - has a home country tax loss carryforward,
  - does not plan to distribute earnings from the LNG project to its home country, or
  - is a foreign governmental entity that is not subject to tax in its home country.
Income or Profit Taxes

- **Seller's income from LNG sales**
  - May be subject to tax in the jurisdiction in which the Purchaser's receiving terminal is located (the receiving jurisdiction)
  - The applicability of these taxes will depend on -
    - the domestic tax laws of the receiving jurisdiction and
    - the ability of the Seller to utilize tax treaties to which the receiving jurisdiction is a party
Income or Profit Taxes

- **Seller's income from LNG sales (continued)**
  - The domestic tax laws of the receiving jurisdiction may provide that income from an LNG sale is attributable to (and thus potentially subject to tax in) the receiving jurisdiction because of the passage of title or risk of loss with respect to the LNG in that jurisdiction.

- **Tax Planning Point** -- Make sure that, under the LNG SPA, title and risk of loss to LNG cargoes pass from the Seller to the Purchaser outside of the receiving jurisdiction (e.g., on the high seas).
Income or Profit Taxes

- **Seller's income from LNG sales (continued)**
  - The Seller may also be subject to tax in the receiving jurisdiction if the sales income is attributable to the Seller's taxable presence or (if a tax treaty applies) permanent establishment (PE) in the receiving jurisdiction.
  - Potential causes of a taxable presence or PE include:
    - maintaining a marketing office in the receiving jurisdiction,
    - negotiating the terms of an SPA at one or more locations in the receiving jurisdiction, and
    - arranging for shipping, scheduling, or other significant services in the receiving jurisdiction.
- **Tax Planning Point** -- Minimize the Seller's contacts (whether through its own employees or through certain dependent agents) with the receiving jurisdiction.
- **AIPN Master SPA**
Income or Profit Taxes

- **Income from Liquefaction or Regasification Operations**
  - May be subject to tax in the jurisdiction in which the liquefaction or regasification facility is located
  - Different jurisdictions may characterize income from such operations differently, depending on whether the operations are structured as -
    - the provision of tolling services,
    - purchases and sales of natural gas or LNG, or
    - sales of plant capacity
Income or Profit Taxes

- **Income from Transporting LNG**
  - The Seller may be subject to tax on income attributable to transportation of LNG if the Seller is obligated to deliver the LNG to the Purchaser subsequent to the passage of title

- **Tax Planning Point** -- The Seller may qualify for an exemption from transportation tax under -
  - the domestic tax law of the receiving jurisdiction,
  - a tax treaty, or
  - another international agreement such as a bilateral shipping agreement

- **AIPN Master SPA**
Income or Profit Taxes

- Withholding Taxes
  - May apply to -
    - payments of interest to a foreign lender pursuant to a financing agreement to construct a liquefaction or regasification facility, and
    - charter hire received by a seller of LNG
  - Tax Planning Point -- A tax treaty may exempt such payments from withholding taxes
  - AIPN Master SPA
Value Added Tax (VAT)

- VAT is imposed in many jurisdictions as a percentage of the price paid for certain goods and services and a percentage of the value of imported goods and services.
- VAT may represent a significant cost in the start-up phase of a project because it may be imposed on amounts payable to the engineering, procurement, and construction (EPC) contractor and the cost of materials used in the construction of the project.
Value Added Tax (VAT)

- In many jurisdictions, the cost of "input" VAT (paid by the recipient or importer of goods and services) may be recoverable out of "output" VAT (collected by the recipient or importer from persons to which it sells LNG or natural gas)
  - Many countries provide for refunds of unrecovered VAT, but such refunds may take a long time to recover (usually without interest)
- The tax laws in some jurisdictions provide that certain sales of production are "exempt" from VAT
  - **Tax Planning Point** -- "Exemption" vs. "exemption with credit"
- AIPN Master SPA
Customs Duties

- May be imposed by the jurisdiction in which the liquefaction or regasification facility is located as a percentage of the value of equipment, materials, or supplies that are imported to construct the facility
- May also be imposed on the export of LNG, based on a percentage of the value of the LNG
- Customs duties are not recoverable, but some jurisdictions provide an exemption for goods that are only temporarily located in the jurisdiction (e.g., construction equipment)

**AIPN Master SPA**
Property Taxes

- May be imposed by a jurisdiction as a percentage of the value of any real or personal property situated within the jurisdiction as of a testing date (e.g., December 31 of each year)

- **Tax Planning Point** -- Property taxes are often applied in a mechanical way, which may present opportunities to minimize property taxes imposed on mobile assets such as LNG and LNG tankers

- AIPN Master SPA
Port Charges

- May be imposed when a vessel uses a port for purposes of loading or unloading cargoes, based on the quantity of LNG that is loaded or unloaded
- Collected and administered by the port owner, which may or may not be a governmental authority
- **AIPN Master SPA**
For More Information

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