

Peculiarities of Managing the Investment Assets of Oil Companies in The Implementation of The Tax for Additional Income

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Abstract - For many years, the discussion about the fair level of the tax burden on resource companies has not ceased. Both the state and the management of enterprises recognize the dependence of the level of budget financing and the profitability of investment assets on the applied approach to taxation. The article presents the results of a study of the features of evaluating the effectiveness of investment asset management and offers recommendations for optimizing the distribution of cash flows.

Keywords: Mineral extraction tax, additional income tax, taxation of oil production, investment assets, efficiency assessment.

1. INTRODUCTION

At the moment, an economic model has developed in Uzbekistan, in which hydrocarbon production is the basis of the state budget. The state budget is extremely interested in the development of new fields and the implementation of new large oil and gas projects, which promise significant fiscal payments in the long term. However, due to the gradual depletion of well flow rates, there is a need to provide such tax conditions that will make it possible to increase the profitability of investment assets with current low efficiency.

The concept of additional income tax (ATD) was proposed as early as in Uzbekistan and was introduced on January 1, 1992. Initially it was 30%, in 1993-1994 it was 25%, and since 1998 it has been 20%. However, as of October 1, 2019, the VAT rate has been reduced from 20% to 15%. The rise in oil prices at the beginning of the millennium prompted the abandonment of the AIT and the implementation of the mineral extraction tax (MET). The gradual depletion of oil and gas fields requires a transition from taxation of production volume to taxation of economic results.

An alternative to the current taxation system (DST) suggests the possibility of influencing the level of tax payments through a competent redistribution of funds between the investment assets of an oil company.

In recent years, especially with the emergence and development of the coronavirus pandemic, not only world oil and gas prices, but also their consumption volumes have undergone significant fluctuations. This situation has led to increased attention to the issue of choosing the best tax planning tools for financing investment assets.

The purpose of the article is to study the impact of the application of the tax on additional income in oil production on the procedure for assessing the effectiveness of investment asset management and to develop recommendations for optimizing the distribution of cash flows.

2. LITERATURE REVIEW

The taxation of natural resources has always been and remains a two-sided problem. On the one hand, natural resources should belong to the entire state and its people, so the income from their use is directed to finance the budget. On the other hand, the purpose of the activity of extractive organizations is undoubtedly to make a profit. Achieving the necessary balance is the goal of an effective tax policy of the country.

Over the past decade, this issue has been the subject of many studies by both national and foreign scientists.

Most authors (Hiorth, A., Osmundsen, P., 2020; Issabayev, M., Rizvanoghlu, I., 2019; Provornaya, I.V., Filimonova, I.V., Nemov, V.Y. etc., 2020; Snow, N., 2011; Kashani, H.A., 2012; Sikhimbaeva, D.R., Esimseitova, K.A., Esimseitov, M.S., 2014; Lund, D., 2014; Tang, B.-J., Song, X.-T., Cao, H., 2018; Osmundsen, P., Løvås, K., 2013), as a result of studying the experience of relations between oil companies and the state, they agree that the oil industry is very dependent on the taxation system and is quite sensitive and responsive to any changes. This is especially noticeable with sharp fluctuations in world oil prices.

The studies of Privalov, N.G., Privalova, S.G. are devoted to the issues of the need to make changes to the current MET. (2017), Reimer, M.N., Guettabi, M., Tanaka, A.-L. (2017), Smirnova, N.V., Rudenko, G.V. (2016), Rabe, B.G., Hampton, R.L. (2015), Khafizova, A.R., Fassakhov, I.A. (2015), Cherniavsky, A. (2012).

The advantages and disadvantages of introducing a tax maneuver in Russia were analyzed by Fjaertoft D., Lunden L.P. (2015), Gorbunova E. (2020), Katysheva E. (2016), Ponkratov V.V. (2014, 2016) and others. The flexibility of this tool and the ambiguity of the impact on budget revenues, as well as the stimulation of the development of fields with low efficiency, are noted.

The works of the presented authors served as the basis for further research on the impact of the application of an additional income tax on the efficiency of investment assets.

3. ANALYSIS AND RESULTS

An investment asset is a field or a group of fields, united by territorial, administrative or other criteria, having a common infrastructure for the transportation and / or treatment of oil and gas, which require financing of the preparatory stage for an extended period.

Each investment asset has its own time frame. The moment in time when only the first idea about an asset occurs can be called the moment when the idea of an investment asset was born. Also, the moment of implementation can be considered the moment of commencement of financing. The end of an asset can be an event such as the end of funding, the merger of an asset with another asset, retooling and a major revision of the asset.

The life cycle of an investment asset is the time interval between the idea of an investment asset and its final liquidation. The life cycle includes three main life stages:

- pre-investment stage;
- implementation stage (investment stage);
- post-investment stage (stage of exploitation).

The criteria by which the effectiveness of any investment asset is assessed are based on the following principles:

- changes in the value of cash over time;
- possibility of changes during implementation;
- Accounting for inflation in the model economy;
- accounting for alternative cost options;
- accounting and forecasting of risks associated with the sale of an asset;
- forecasting cash flows formed on the basis of all receipts and payments;
- control throughout its implementation;
- comparability of macroeconomic parameters of assets sold in one time period;
- taking into account the impact on related areas (society, ecology, etc.);
- step-by-step structure of asset performance evaluation.

The main purpose of an investment asset is to obtain economic profit. Within an asset, cash flows provide such profits. The cash flows that are generated by an investment asset are the totality of all outflows and receipts of cash at all stages of the asset.

The static indicators will include:

- coefficient of efficiency of investments;
- simple payback period of the project.

Dynamic indicators of investment performance include:

- net present value (NPV);
- return on investment index (PI);
- internal rate of return (IRR);
- payback period calculated on discounted cash flows (DPP).

Most often, to minimize the risks of investment inefficiency, a set of economic efficiency indicators is used. Such a variety of indicators helps to have a more holistic and broader picture of the effectiveness of an investment project. Of course, economic efficiency is only one point when deciding on the implementation of an investment project. In addition, the investor evaluates many non-economic weighty factors, for example, the impact of the project on the company's reputation or the environmental situation in the region where the project is being implemented, and the coverage of new sales markets.

In an oil and gas company, cash inflows are generated from proceeds from the sale of oil and associated gas. The latter can be taken into account in the project by agreement. The use of proceeds from the sale of associated gas in calculations is allowed if, based on the results of the project, a change in the volume of associated gas production with its subsequent sale is predicted. GOR and gas utilization indicators are used to determine gas volumes.

Outflows comprise production costs for the following elements:

- investments;
- variable production costs;
- costs of well stock maintenance;
- other expenses.

The calculation of the amount of MET is made in accordance with the rates adjusted as part of the macro

parameters. When determining the amount of MET, the approved standards for oil losses during infield transportation and preparation are taken into account. For fields with an MET exemption, the amount of MET is determined taking into account the exemption. The MET rate for natural and associated gas, payments for APG flaring are determined in accordance with the Tax Code of the Russian Federation.

It can be noted that taxes have an impact when calculating performance indicators. The adoption of such an important decision as the transition to a new tax regime will reduce the base of the tax on the profits of oil companies, otherwise the current procedure for calculating corporate profits tax will remain.

The new system involves the introduction of taxation of additional income (ATD), as well as a reduction in the total value of the MET and the customs duty on oil, which depend on gross indicators. The new tax system involves a reduction in the total amount of fiscal payments that depend on gross production indicators (mineral extraction tax and export duty), and the introduction of taxation of the estimated cash flow from hydrocarbon production.

A distinctive feature of AIT is that when calculating the tax base, cash flows from an investment asset generated throughout the entire life cycle are taken into account. It is also important that the amount of tax payments is related to the profitability of each individual license area, which, in turn, depends on the conditions of production. Consequently, the tax burden will be diversified, which will improve the economic performance of fields with low profitability, including hard-to-recover reserves.

The investment made in the development of the asset must be profitable, that is, efficient. To determine the profitability of efficiency, an assessment of the effectiveness of the asset is carried out. At this stage, investments are forecast for the construction of production facilities, facilities for preparing transportation, the forecast profile of oil and gas production, operating costs, and economic macro parameters.

The tax component is part of the assessment of the economic efficiency of an investment asset and is an integral element of the company's investment asset management system. Therefore, when justifying the choice of the optimal tax, it seems appropriate to include in the assessment of the effectiveness of the use of an investment asset the receipt of an additional economic effect as a result of a change in the taxation regime.

Flexibility is one of the key benefits of the new tax. If the MET is set for a produced ton of oil, then the tax on additional income is set in case of income from this ton. Accordingly, if there is no income, then there will be no tax.

Methods for adapting the investment program to the levels of limit spending on AIT can be:

- 1) acceleration or shift of investment projects with oil production;
- 2) optimization of capital costs that do not affect oil production;
- 3) optimization of operating costs without loss of oil production;
- 4) adjusting the level of oil production depending on the situation;
- 5) change in tax policy (depending on the state).

Exceeding the spending limit in the current year can only be justified by increasing the limit spending multiplier for the following years in order to increase the investment program in the license area.

NPV, PI, IRR, DPP are mandatory indicators of economic efficiency when evaluating investment assets in the oil and gas sector. In order for a project to be approved and accepted, its indicators must correspond to the level of project efficiency adopted within the oil company. In addition, in special cases, specific performance indicators can be calculated for the project.

Basic principles for assessing economic efficiency in large oil and gas companies:

- availability of certain evaluation standards;
- availability of a homogeneous competitive environment;
- centralized allocation of funds for projects;
- centralized receipt of funds from projects;
- proportionality of the depth of analysis of the materiality of the project;
- accounting for uncertainties and risks;
- analysis based on cash flows;
- accounting for the value of money in time (discounting);
- assignment to the project of expenses and incomes caused by the implementation of the project;
- accounting of past (historical) expenses and incomes;
- audit of financial models;
- standardization of financial models.

Another feature of investing in the oil and gas complex is the division into types of the most invested capital:

- capital investments;
- non-capital investments.

Large oil and gas companies have developed internal economic models for evaluating investment projects. Models are usually developed by IT departments in collaboration with the company's investment departments. All

investment models can be divided into:

- standard;
- non-standard.

Standard models are called universal models, with the help of which it is possible to evaluate the economic efficiency of a large number of homogeneous investment projects. With the help of standard models, companies usually evaluate investment projects for the development, acquisition or disposal of assets.

In the process of evaluating investment projects, there are cases when the standard performance evaluation model cannot be applied to a specific investment project. In this case, investment services resort to the use of non-standard models, which must comply with the requirements of all internal guidelines of the company, contain a detailed description of the assumptions and calculation logic. The use of non-standard models for evaluating economic efficiency is most often used in the evaluation of maintenance projects.

When evaluating the effectiveness of international projects or projects of a new type of company's business, it is possible to use non-standard netback, as well as fixed tariffs for the supply of production equipment or the provision of services.

When evaluating investment projects of oil and gas companies, it is mandatory to have an assessment of the investment risks of the project. Of the wide range of project risk assessment methods, large oil and gas companies usually resort to quantitative methods:

- sensitivity analysis;
- stress test;
- analysis of break-even points;
- modeling of random variables.

The next feature of the oil and gas industry is the constant initiation of joint investment projects, often such projects are implemented jointly with foreign partners in the Russian Federation and abroad. An assessment of the economic efficiency of a joint project must be submitted for the project as a whole and for the share of investors in the project. When modeling cash flows in joint projects, it is necessary to take into account:

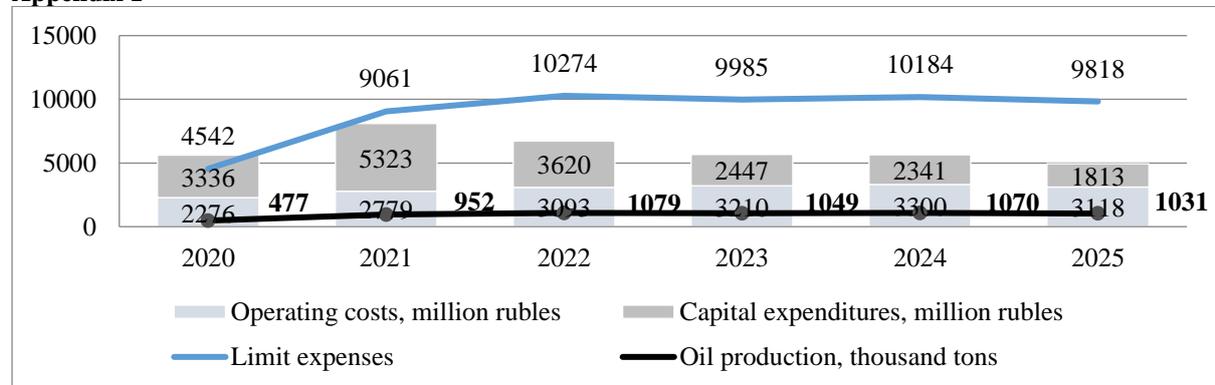
- structure of ownership and management of the joint project;
- specifics of the legislation of the country where the project is being implemented;
- terms of project financing;
- various financing options and possible cash flow optimization schemes;
- cash flows actually available after paying taxes.

Thus, when analyzing the effectiveness of an investment asset in the oil industry, a detailed analysis is required, including the issues of accounting and tax optimization within the framework of the project, including the use of various jurisdictions that allow minimizing the costs associated with financing the project and generating income from it. At the same time, it is necessary to analyze all direct tax deductions, as well as take into account benefits under double taxation treaties.

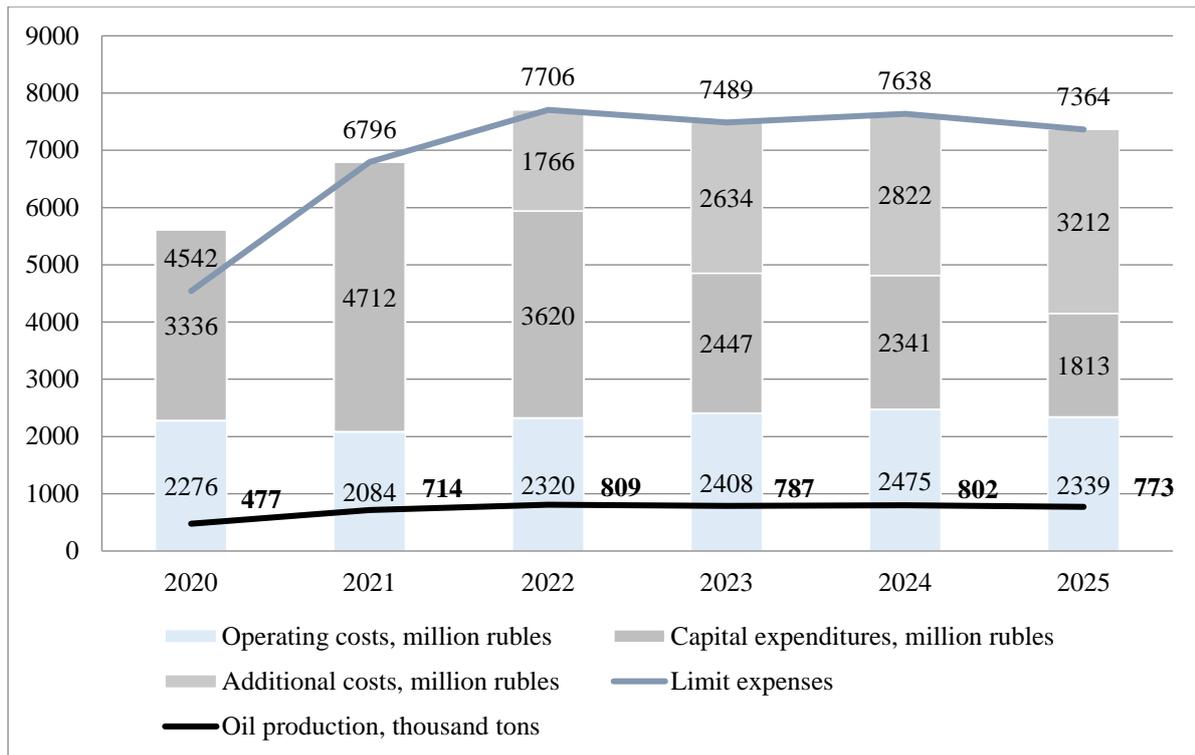
The resulting model for optimizing the investment load of an asset and operating time was tested on three investment assets ("A", "B" and "C") of an oil and gas company, which are implemented under the AIT regime.

Let's consider the schedule (Appendix 1, a) of the current forecast of the investment program for the investment asset "A" and the level of limit expenses.

Appendix 1



(a). Current forecast and level of limit expenses of the investment program for the investment asset "A" until 2025



(b). Proposal to adjust the production program of the investment asset "A" until 2025

It is worth noting that 2020 is overloaded with investment projects related to oil production (development drilling, sidetracking, etc.). High future production from these projects is not supported by the required level of investment activity of the company in this license area.

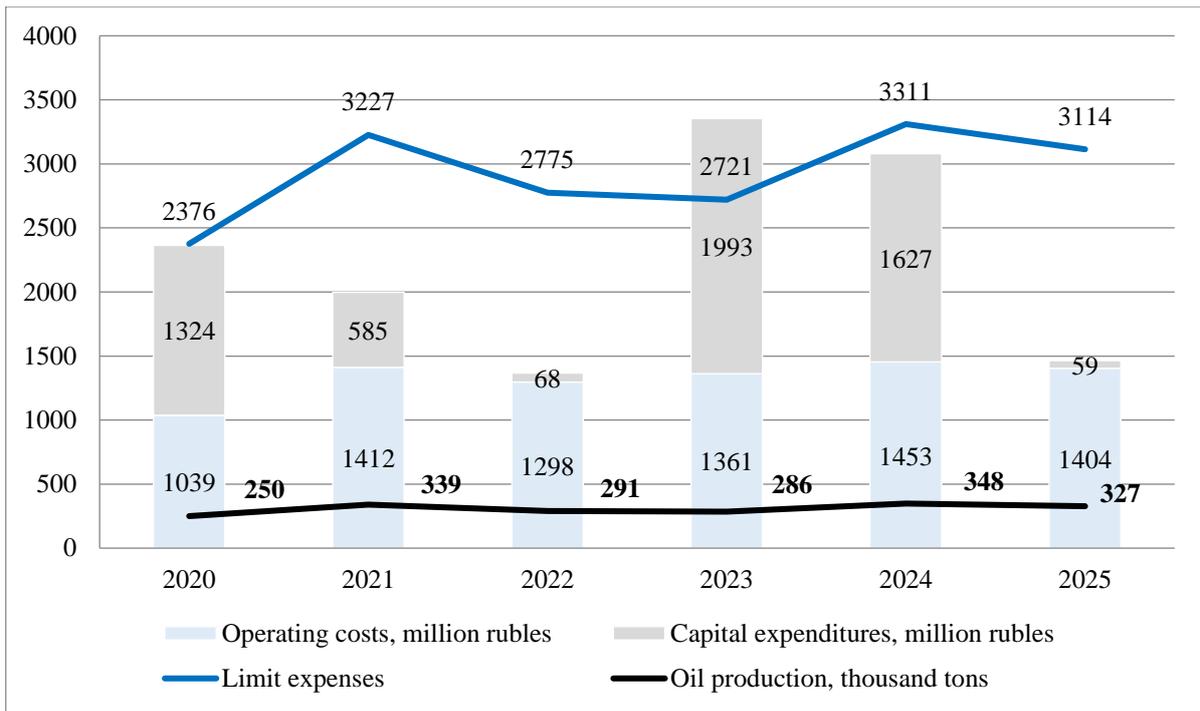
As the analysis showed, in order to achieve a positive effect on the investment asset "A", it is necessary to reduce the investment burden in 2021 by 11% (Appendix 1, c), the consequence of this decision will be a decrease in oil production for all subsequent years. From the decline in production levels, indicators of limit costs will be adjusted, to achieve which it will be enough to load the investment program for subsequent years. As a result, inefficient overpayment of AIT will be reduced.

When analyzing the situation for the investment asset "B" (Appendix 2, a) in the medium-term forecast, one can single out a very significant uneven distribution of investments over the years: the investment program for 2021-2022 is significantly lower than for 2023-2024.

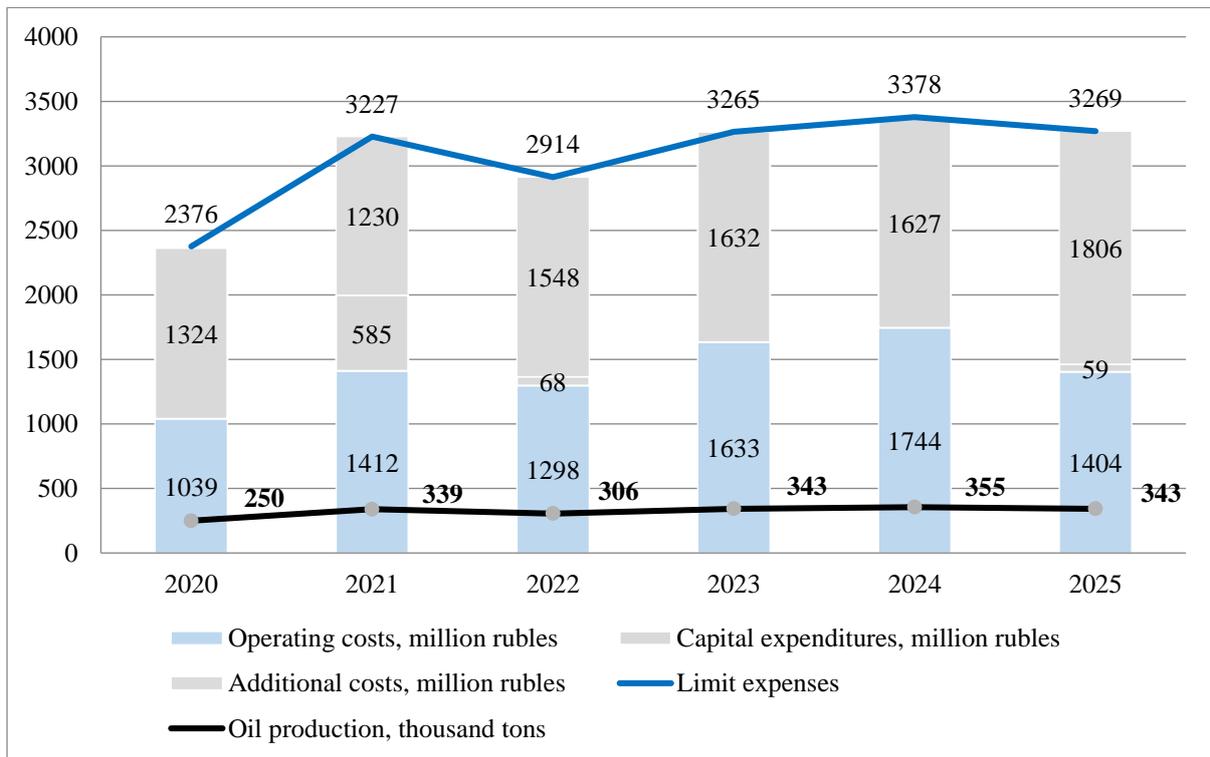
In this area, it seems logical to accelerate the implementation of the most "confident" investment projects for drilling and sidetracking for the period 2021-2022 (Appendix 2, c).

A feature of the situation with the investment asset "C" for the period 2021-2023 is the growth of specific operating costs for oil production (Appendix 3, a). For this investment asset, it is necessary to carry out a large audit work (Appendix 3, b) in terms of the formation of operating costs, to propose ways to reduce them. It is also necessary to adjust the capital expenditure program without losing oil production.

Appendix 2

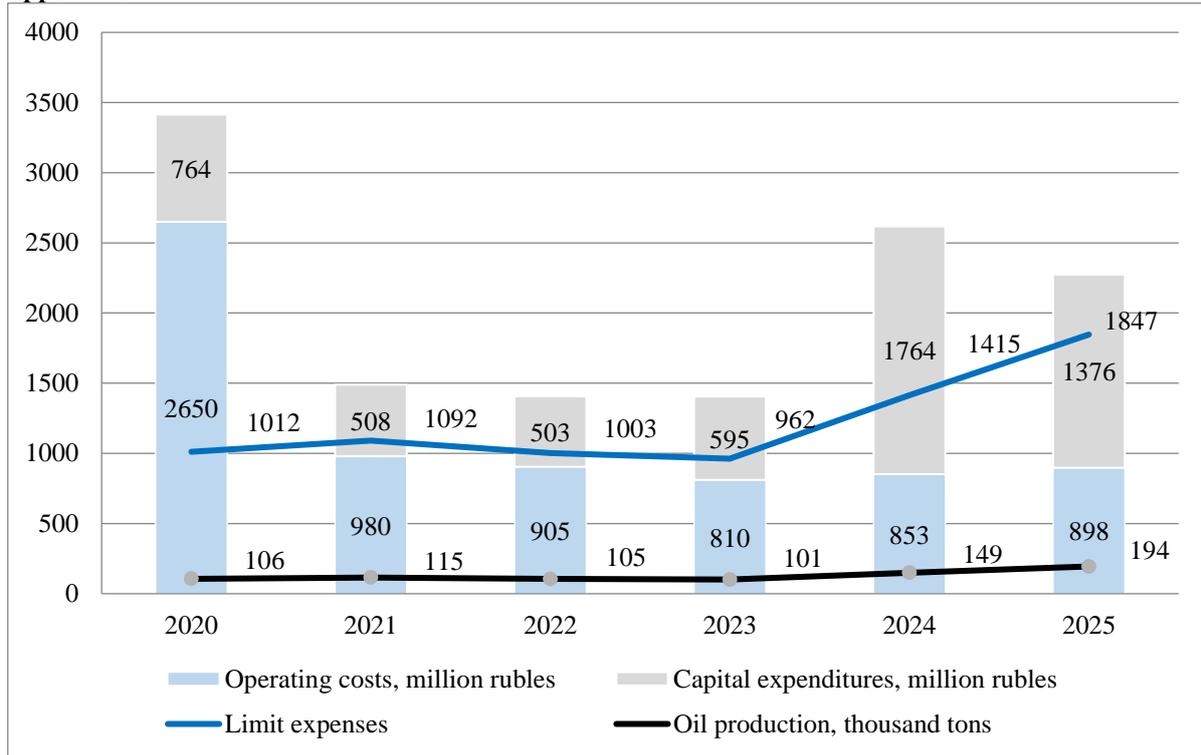


(A). Current forecast and level of limit expenses of the investment program for the investment asset "B" until 2025

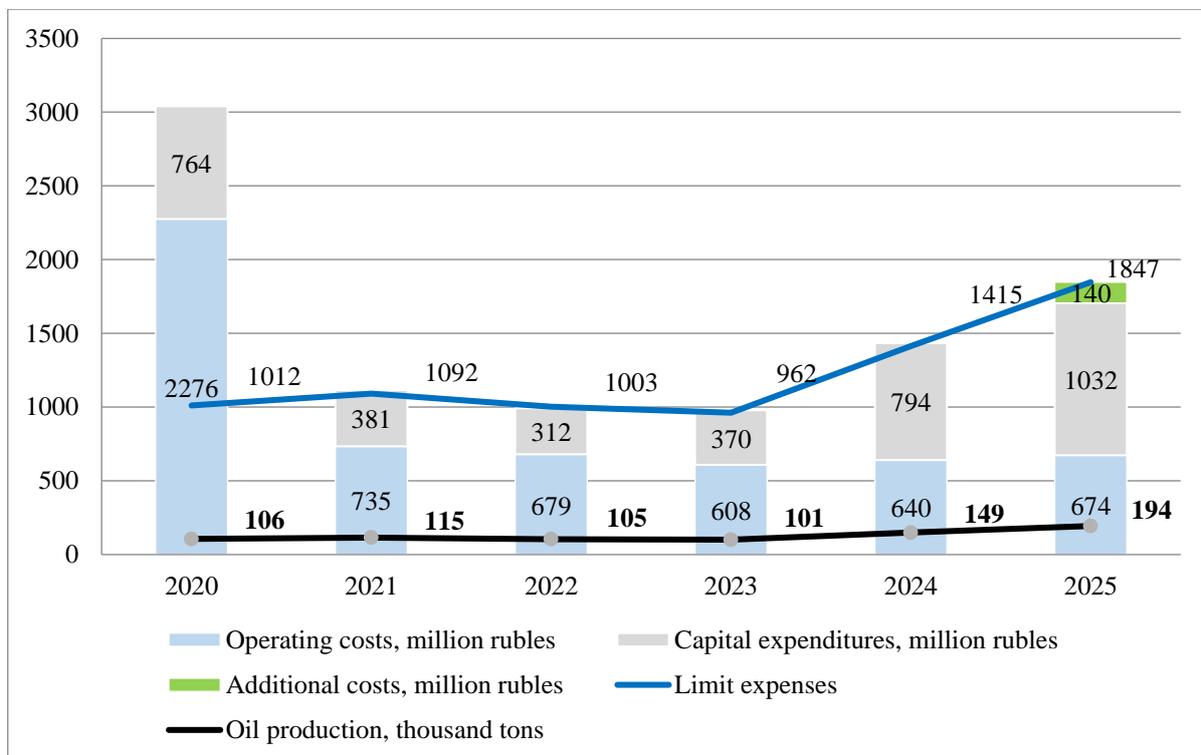


(V). Proposal to adjust the production program of Investment asset "B" until 2025

Appendix 3



(A). Current forecast and level of limit expenses of the investment program for the investment asset "C" until 2025



(V). Proposal to adjust the production program of Investment asset "C" until 2025

Thus, I would like to note that the issues of building long-term production plans for individual investment assets should be studied especially carefully. Each asset has its own characteristics, its own problem areas that need to be worked on, its own high-performance zones, the effectiveness of which does not always correlate with the efficiency of paying taxes.

4. CONCLUSIONS

The product of a painstaking analysis of each field is a large cumulative plan for the development of an oil and gas asset, in which license areas in the AIT regime will be only a part of the overall production program, which has many levers of influence and controlling.

One of the most significant problems of the current stage of development of the oil and gas complex of Uzbekistan is the high level of depletion of deposits. Rich oil reserves are discovered either at considerable depths or in areas with a harsh climate, which leads to a sharp increase in the cost of their production. Therefore, when applying the current taxation system, many investment assets were assessed as economically inefficient. The introduction of a tax on additional income, subject to its competent use, as well as high-quality planning of the distribution of investment efforts, will increase the profitability of deposits of this type and give a new impetus to the development of the industry.

Summarizing the above, it should be emphasized that the construction of a management accounting system for the investment activity of an enterprise is a creative process. The methodological approach proposed in this article to the formation of an interorganizational management accounting system will allow solving a number of tasks related to the management and control of the investment activity of an enterprise, including ensuring the efficiency of accounting. An effective management accounting system will allow at any time to assess the state of affairs in investment activities and make a decision on the further implementation or suspension of an investment project.

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