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Uganda's Upstream Oil and Gas Customs Duty Regime

Navigating the Complexities

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1. Introduction

It is the policy aspiration of the Government of Uganda ("GoU") and its peers in the East African Community ("EAC") to exempt both the licensed petroleum companies ("IOCs") and their contractors from duty at the importation of inputs and machinery for use in upstream oil and gas operations though premised on a strict interpretation of the law there is still susceptibility to disputes especially on whether the contractors are also entitled to the exemption from customs duty.

In this article, we discuss the EAC general customs duty regime but with emphasis on the special rules, processes and procedures for Uganda's upstream oil and gas sector. This article does not cover the customs duty regime for the EACOP project that will be addressed in a separate publication.

2. Overview of Uganda's general customs duty regime

Uganda is a member of the EAC bloc alongside Burundi, Rwanda, Kenya, Tanzania, South Sudan and the Democratic Republic of Congo that constitute a single customs territory under the 2004 EAC Customs Union Protocol.

The East African Community Customs Management Act 2004 ("EACCMA") and the Common External Tariff ("CET") provide the substantive legislation for the management of customs affairs in the bloc. The EACCMA considers the supervision and administration of customs affairs while the CET sets out the import duty rates.

Each member state of the EAC bloc independently administers the customs affairs of its territory in accordance with the EACCMA and CET. The Uganda Revenue Authority ("URA") Customs Department oversees customs affairs in Uganda. It collects taxes and levies due at importation that ordinarily comprise import duty, excise duty, import VAT, withholding tax, infrastructure development levy and the environmental levy to the extent applicable.

Unless exempt, there is a four tariffs band for goods imported into the bloc. The 0% rate is for raw materials and capital goods, 10% for intermediate goods, 25% for finished goods and 35% for goods including but not limited to textiles and garments, cotton, leather products, iron and steel, furniture, meat and dairy products, paints, ceramic products and head gear. Goods on the sensitive products list may attract import duty at higher rates over 35%.

Excise duty at diverse rates may also be charged at importation. Unless exempted, zero rated or deferred, VAT is payable at the rate of 18% for goods imported into Uganda. This is in addition to withholding tax ("WHT") at the rate of 6% unless the importer is exempted. This WHT is creditable against year-end tax liability or refundable subject to a URA audit. An infrastructure development levy of 1.5% computed on the cost insurance and freight value of the import is also applicable. Environmental levies are also potentially chargeable depending on the product imported.

There is also the pre-export verification of conformity ("PVoC") overseen by the Uganda National Bureau of Standards ("UNBS"). Specific goods imported into Uganda require PVoC to ensure quality of products, health and safety and environmental protection in accordance with UNBS standards.

All goods that are subject to PVoC must obtain a Certificate of Conformity. The inspection is carried out by appointed agents in the country of origin before shipment. Such products include used motor vehicles, motor vehicle parts, steel products, various electronic and mechanical equipment. Where goods are subject to pre-shipment inspection requirements and arrive into the country prior to inspection, they may be inspected locally but with a penalty imposed. The PVoC fees per item imported are on a scale of the Free on Board value subject to minimum and maximum charges of United States Dollars ("USD") 235 and 3,000 respectively.

3. Uganda's upstream oil and gas import duty regime

With the objective of lowering petroleum exploration and development project costs, EAC member states amended the EACCMA in 2009 exempting inputs and machinery earmarked for upstream oil and gas activities from import duty. Paragraph 30 (a), Part B of the Fifth Schedule provides for the exemption from import duty of:

"Machinery and inputs, but not including motor vehicles, imported by a licensed company for direct and exclusive use in oil, gas or geothermal exploration and development upon recommendation by a competent authority of a Partner State."

This amendment operationalized provisions in Oil and Gas Production Sharing Agreements("PSAs") that exempt the oil companies and their contractors from import duty on inputs and machinery for upstream petroleum operations. It is the position of Courts in Uganda that tax incentives or exemptions in the PSAs are ineffectual unless replicated in domestic legislation.

Since the amendment, it has been a contentious question whether based on a strict reading of the

EACCMA, the exemption from import duty for the IOCs also extends to the contractors. Though the EAC Secretariat guided the GoU vide an opinion dated 2nd June 2015 confirming that the contractors too could qualify for the exemption if they were licensed by the Competent Authority, there are still lingering questions on this. It is not clear how the contractors or subcontractors to the IOCs can be licensed for purposes of this exemption. Only the IOCs are licensed by the respective governments to undertake petroleum operations.

It has therefore been the practice in Kenya, Tanzania and Uganda since 2009 for the contractors to consign their imports for use in petroleum operations in the name of the IOCs they are serving to unlock this exemption which conceivably was intended to apply to both the IOCs and the contractors notwithstanding the potential variance with the interpretation of the law. The importers of record for customs purposes in this instance are therefore the IOCs.

The Competent Authority in Uganda recommending the exemption is the Petroleum Authority of Uganda("PAU"). The IOCs share with PAU a master control list of their authorized contractors and the items proposed to be imported for petroleum operations. Once approved, URA ensures that the applicable imports are cleared under a customs procedures code ("CPC") where no taxes are payable.

4. Risks importing contractors items through the IOCs

The contractors presently consign their imports in the name of their customers, the IOCs, to benefit from the duty exemptions. This notwithstanding, there is unease in the industry premised on previous experience that future tax disputes can arise unless it is anchored in the law with clear certainty that contractors to the IOCs are also entitled to the exemption from import duty.

There is a similar provision in the EACCMA under Paragraph 30 (b), Part 2 of the Fifth Schedule extending the exemption from customs duty to licensed mining companies in the region. Around 2011 or thereabout, the Tanzania Revenue Authority ("TRA") raised an assessment against one of the mining companies in Tanzania that had consigned contractor imports through its name. The TRA contended that the exemption from taxes only extended to the licensed mining companies and not their contractors.

TRA took the consigning of the contractor imports through the mining companies as a tax avoidance scheme. Though the mining company successfully defended its position in the Tribunal, this is early warning of what can happen if the URA reconsiders its stance given the contested interpretation as has been the case recently on international transportation. In a sudden turn of events, the URA started demanding for withholding tax on international transport charges despite previously submitting to the position that taxes were not applicable. The areas where we anticipate tax disputes can arise include:

a) Risk of Post Customs Audit Liabilities

URA has up to 5 years to examine whether a taxpayer made the correct import declarations. Customs audits are very manual andonerous requiring the provision of bulky information to support each customs entry for every import made. As the importers of record, the IOCs are answerable for any anomaly that may be identified in future customs audits despite not technically being the legal owners of the goods imported.

b) Additional assessments

In the remote event that URA questions in future the practice of consigning contractors' goods in the name of the IOCs on the basis that the strict interpretation of the EACCMA does not shoulder this, all import taxes that ought to have been paid if it were not for this exemption can be demanded

c) Disposal

URA can treat the transfer of these imported goods to the contractors as a disposal by the IOCs to which all the applicable transfer taxes can be assessed.

d) Tax wear and tear

Contractors' entitlement to tax wear and tear can also be problematic. Equipment qualifies for tax capital allowances if it is recognized as part of the company assets in the financial statements which in part is premised on how the equipment is imported and who the import declaration forms document as the owner.

5. Other ways of contractors importing goods into Uganda

Other than consigning their imports through the IOCs, contractors can directly import own equipment and inputs into Uganda. This however takes away the benefit of the import duty exemptions that the contractors would enjoy if they import through the IOCs.

Equipment and other durable non consumable goods can also be imported into Uganda under the temporary importation regime. Temporary imports are assessed to all the applicable import taxes though no cash

payment is made. The importer executes a customs bond committing to pay the assessed tax if the goods are not exported out of Uganda after the expiration of the bond period that is usually for one year but can be renewed as the URA deems fit.

6. Conclusion

The expanded PVoC programme is fairly recent. It is unclear whether the economic impact of the PVoC was considered at the time of simulating the financial numbers to determine the project viability of Uganda's oil project. Whether the government would exempt the IOCs and their contractors from the PVoC requirement which is unlikely or the IOCs would invoke the economic stabilization clause to restore economic parity pre-the PVoC can only be speculated at the moment.

Cristal Advocates accepts no responsibility for any loss occasioned to any person acting or refraining from acting as a result of material contained in this publication. Further advice should be taken before relying on the contents of this publication.

Contacts for this Publication

Denis Yekoyasi Kakembo

dkakembo@cristaladvocates.com

+256 751 834 168

Denis is the Managing Partner at Cristal Advocates where he also leads the energy and tax practice. He is qualified both as a Lawyer and Chartered Accountant with vast experience serving various industries in Sub Saharan Africa. Before joining Cristal Advocates, he had worked for close to 10 years with Deloitte and Touche where he started his career and rose to senior managerial positions.

At Deloitte, he lived and worked in Uganda, Kenya, Tanzania and the United Kingdom for over 6 years and subsequently became the firm's chief of staff for the Energy and Resources Industry Group seeing him play a lead advisory role in Uganda, Kenya, Tanzania, Mozambique, South Sudan, Somalia and Ethiopia.

Denis is widely published and a regular commentator in the local, regional and international media and speaker at various forums regarding the taxation and financing of energy projects as well as the protection of large capital projects within the framework of international investment law.

He holds a Master of Laws degree in Petroleum Taxation and Finance from the University of Dundee in the United Kingdom, a Post Graduate Diploma in Legal Practice and a Bachelor of Laws degree from Makerere University. ■

Bill Page

bpage@cristaladvocates.com

Bill is a Senior Advisor with Cristal Advocates. He has concentrated on working with energy companies with a particular focus on cross border transactions and M&A since 1989 and is a leading global energy and tax practitioner with wide international experience. Between 1986 and 1998, he worked in London with the UK tax authorities and Big Four accounting firms. From 1998 to 2004, he was based in Kazakhstan working across the Caspian region with Deloitte. He was in the region at the time it was developing its infrastructure for crude oil production with international investment following the collapse of the Soviet Union.

From 2004 to 2008, he worked in Russia where he led Deloitte's oil and gas industry group and established Deloitte's office in Sakhalin. He moved to East Africa in 2009 leading Deloitte's energy and resources industry group in Uganda, Kenya, Tanzania, Rwanda, Ethiopia and Mozambique. He was initially based in Kampala, Uganda later relocating to Dar es Salaam, Tanzania. Bill returned to the UK in 2014 supporting Deloitte UK teams working on outbound projects investing in Africa and was a key member of Deloitte UK's energy and resource practice until his retirement from the firm in September, 2018.

Bill is a graduate of Oxford University and completed his inspectors' training with the UK Inland Revenue in 1989. ■

John Teira

jteira@cristaladvocates.com

+256 704 493 997

John leads the public policy and advocacy practice at the firm and combines unique public and private sector experience.

Prior to joining Cristal Advocates, he had worked as a Private Secretary to the President of the Republic of Uganda. During this time, he participated in several public and private sector engagements that included advising and coordinating activities relating to oil and gas as well as infrastructural projects of national significance. John had earlier worked with the Post Bank Uganda Limited and Shonubi Musoke and Co. Advocates.

He holds a Bachelor of Laws degree from Makerere University and a Post Graduate Diploma in Legal Practice from the Law Development Centre and various other qualifications. ■

Dickens Asiimwe Katta

dasiimwe@cristaladvocates.com

+256 772 370 021

Dickens leads the oil and gas practice at Cristal Advocates. He has an in depth appreciation of Uganda's oil and gas sector having served as the maiden Company Secretary of the Uganda National Oil Company (UNOC) and the Uganda Refinery Holding Company Limited (URHC). UNOC represents the Government of Uganda commercial interests in the oil and gas sector while URHC represents government interests in the refinery project as well as managing the petrol based industrial park.

Dickens was instrumental in UNOC's formation and initial period of operation and also served as its head of Contracts, Negotiations and Advisory until May 2018. Prior to joining UNOC, Dickens was Legal Counsel at the Petroleum Directorate of the Ministry of Energy playing key legal advisory roles on the negotiation and implementation of PSAs, Joint venture and other oil and gas agreements. He was also part of the team that shepherded the process of enacting the current Ugandan oil and gas Legislations and Regulations including the local content requirements.

He is a certified project control specialist (IFP) and holds a Master of Laws Degree in Petroleum Law and Policy from the University of Dundee in the United Kingdom, a Post Graduate Diploma in Legal Practice and a Bachelor of Laws degree from Makerere University. ■

Francis Tumwesige Ateenyi

ftumwesige@cristaladvocates.com

+256 702 540 936

Francis leads the litigation and dispute resolution practice at the firm. He is an Advocate of the High Court of Uganda with expertise in oil and gas, infrastructure and dispute resolution. He has been part of teams advising on projects in Uganda, Tanzania, Mozambique and South Africa. He specializes in regulatory compliance, national content, health and safety and dispute resolution.

He joined Cristal Advocates from Kizza, Tumwesige, and Ssemambo Advocates. He previously worked with the Advocates Coalition for Development and Environment (ACODE). He also undertook a traineeship with the oil and gas division of Webber Wetzel in Johannesburg, South Africa.

He holds a Master of Laws degree in Petroleum Law and Policy from the University of Dundee in the United Kingdom and various other qualifications. ■

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Contact us

Cristal Advocates
32 Lumumba Avenue
4th Floor, Padre Pio House
Lumumba Avenue

P.O. Box 1769 Kampala, Uganda
Tel: +256 (414) 671 274
Email; admin@cristaladvocates.com
www.cristaladvocates.com