



GOVERNMENT REGULATIONS

COST RECOVERY AND INCOME TAX TREATMENT IN THE UPSTREAM OIL AND NATURAL GAS BUSINESS FIELD

(Government Regulation Number 79 Year 2010 dated December 20, 2010)

BY GRACE OF GOD THE ALMIGHTY

THE PRESIDENT OF THE REPUBLIC OF INDONESIA,

Considering:

- a. that pursuant to the provision of Article 6 paragraph (1) of Law Number 22 Year 2001 on Oil and Natural Gas, upstream business activities are executed and controlled through production sharing contracts;
- b. that in the implementation of the production sharing contracts as meant in letter a, capital borne by business entities or permanent establishments constitutes operational cost which may be reimbursed by the government of the Republic of Indonesia when the upstream oil and natural gas business activities yield commercial production;
- c. that having regards to letters a and b, as well as in order to implement the provision of Article 31 D of Law Number 7 Year 1983 on Income Tax as already amended several times and the latest by Law Number 36 Year 2008 concerning the Fourth Amendment to Law Number 7 Year 1983 on Income Tax, it is necessary to stipulate a government regulation on cost recovery and income tax treatment in the upstream oil and natural gas business field;

In view of:

1. Article 5 paragraph (2) of the Constitution of 1945;
2. Law Number 7 Year 1983 on Income (Statute Book of the Republic of Indonesia Year 1983 Number 50, Supplement to Statute Book of the Republic of Indonesia Number 3263) as already amended several times and the latest by Law Number 36 Year 2008 concerning the Fourth Amendment to Law Number 7 Year 1983 on Income Tax (Statute Book of the Republic of Indonesia Year 2008 Number 133, Supplement to Statute Book of the Republic of Indonesia Number 4893);
3. Law Number 22 Year 2001 on Petroleum and Natural Gas (Statute Book of the Republic of Indonesia Year 2001 Number 136, Supplement to Statute Book of the Republic of Indonesia Number 4152);

D E C I D E S

To stipulate:

THE GOVERNMENT REGULATION ON COST RECOVERY AND INCOME TAX TREATMENT IN THE UPSTREAM OIL AND NATURAL GAS BUSINESS FIELD.

CHAPTER I

GENERAL

Article 1

Referred to in this regulation as:

2A

1. Petroleum, natural gas, oil and natural gas, exploration, exploitation, production sharing contracts, executive board, work area, Indonesian mining jurisdiction and upstream business activities shall be as meant in Law Number 22 Year 2001 regarding Oil and Natural Gas.
2. Contractor shall be a business entity or permanent establishment stipulated to conduct exploration and exploitation in a work area on the basis of a production sharing contract with the executive board.
3. Operator shall be contractor or in the case of contractor consisting of holders of participating interest, any of the holders of participating interest appointed as representative of the other participating interest holders in accordance with production sharing contract.
4. Oil Operation shall be activity covering exploration, exploitation, hauling, plug and abandonment of well, as well as oil and natural gas site restoration.
5. Lifting shall be a specified quantity of crude oil and/or natural which is sold or shared in custody transfer point.
6. First Tranche Petroleum hereinafter abbreviated to FTP shall be a specified quantity of crude oil and/or natural gas production of a work area in one calendar year, which may be taken or received by the executive board and/or contractor in every calendar year before cost recovery and own use are subtracted.
7. Investment Credit hereinafter called Investment incentive shall be additional capital cost recovery in a specified amount, directly related to production facilities, which is granted as incentive to the development of certain oil and/or natural gas fields.
8. Equity to be Split shall be a result of production available for split (lifting) between the executive board and contractor after FTP; investment incentive (if any) and operational cost recovery are subtracted.
9. Non capital cost shall be the costs spent in the current year operational activities, which has a benefit period less than one year, including survey and intangible drilling costs.
10. Capital cost shall be an expenditure on equipment or goods having benefit period over one year, which is burdened in the current year through amortization.
11. Work Plan and Budget shall be the planning of activities and the spending of annual budget by contractor for upstream oil and natural gas business activity in a work area.
12. Production sharing contract shall be a model of joint cooperation contract in upstream business activities on the basis of production sharing principle.
13. Service Contract shall be a model of joint cooperation contract to exploit oil and natural gas on the basis of the principle of compensation for the yielded production.
14. Participating Interest shall be right and obligation as production sharing contractor, directly or indirectly in a work area.
15. Uplift shall be a compensation received by contractor with respects to the provision of bailout for the financing of operation of production sharing contract, which should constitute participating obligation of other contractors, existing in a production sharing contract in the financing.
16. Domestic Market Obligation hereinafter abbreviated to DMO shall be an obligation to hand over right of contractor in the form of oil and/or natural gas to fulfill the domestic need.
17. Compensation

17. Compensation for DMO shall be a compensation paid by the government to contractors with respects to the delivery of oil and/or natural gas to fulfill the domestic need by using the price stipulated by the Minister in charge of oil and natural gas business activities.
18. Government shall be the Central Government.
19. Minister shall be the minister in charge of oil and natural gas business activities.

Article 2

The provisions governed in this government regulation shall apply to production sharing contracts and service contracts in the upstream oil and natural gas business field.

Article 3

- (1) Contractors shall be obliged to carry capital and technology as well as bear operational risks in the framework of the implementation of oil operation based on production sharing contract in a work area.
- (2) The implementation of oil operation as meant in paragraph (1) shall be done on the basis of effective and efficient, rational principles as well as norms of good business and technical practices.

Article 4

- (1) The whole goods and equipment purchased by contractors in the framework of oil operation shall become state property, which is fostered by the government and managed by the executive board.
- (2) The goods and equipment as meant in paragraph (1) may not be re-valuated in the framework of cost recovery.

Article 5

- (1) In executing oil operation, contractors shall be obliged to formulate work plan and budget in accordance with norms of good business and technical practices as well as the rationality principle.
- (2) The work plan and budget as meant in paragraph (1) shall consist of:
 - a. routine expenditure; and
 - b. project expenditure.
- (3) The work plan and budget as meant in paragraph (2) shall secure approval from the Head of the Executive Board.
- (4) The approval of the Head of the Executive Board as meant in paragraph (3) shall constitute a basis for contractors to undertake oil operation.

Article 6

The project expenditure as meant in Article 5 paragraph (2) letter b shall secure authorization approval of financial spending from the Head of the Executive Board before the expenditure is realized.

Article 7

- (1) Contractors shall regain operational cost in accordance with the work plan and budget approved by the Head of the Executive Board after the work area yields commercial production.
- (2) The status of the commercial production as meant in paragraph (1) shall be stipulated through ministerial approval of plan of development of field which is to be produced for the first time.
- (3) In the case of the work area as meant in paragraph (1) not yielding commercial production, the whole

operational costs already spent shall become risk and burden of the contractor fully.

Article 8

- (1) The Minister shall stipulate the minimum quantity of state right in a work area linked to lifting in the approval of plan of development of field as meant in Article 7 paragraph (2).
- (2) The minimum quantity of the state right as meant in paragraph (1) shall be stipulated on the basis of guidance set forth by the Minister.

CHAPTER II

GROSS INCOME

AND DEDUCTIBLE INCOME OF CONTRACTOR

Part One

Gross Income of Contractor

Article 9

- (1) Gross income of contractor shall consist of:
 - a. income in the framework of production sharing contract; or
 - b. income in the framework of service contract; and
 - c. other income outside production sharing contract.
- (2) Income Tax on income in the framework of the production sharing contract as meant in paragraph (1) letter a shall be calculated on the basis of the value of oil and/or natural gas lifting becoming right of contractor, which results from equity share and FTP share, supplemented by oil and/or natural gas resulting from cost recovery plus additional oil and/or natural gas resulting from the granting of incentive or other considerations, subtracted by the value of the realized DMO

of oil and/or natural gas plus compensation for DMO and price variant of lifting.

- (3) Income tax on income in the framework of the service contract as meant in paragraph (1) letter b shall be counted on the basis of compensation received by the government plus the value of the realized sales of oil and/or natural gas resulting from cost recovery.
- (4) The other income outside joint cooperation contract as meant in paragraph (1) letter c shall consist of:
 - a. uplift or other compensation of the same kind; and/or
 - b. income from the transfer of participating interest.

Article 10

- (1) The Minister shall stipulate the percentage and sharing of FTP in order to assure state revenue.
- (2) In order to boost the development of work areas, the Minister may stipulate model and amount of investment incentive.

Part Two

Operational Cost

Article 11

- (1) The operational cost shall consist of:
 - a. exploration cost;
 - b. exploitation cost; and
 - c. miscellaneous cost.
- (2) The exploration cost as meant in paragraph (1) letter a shall consist of:
 - a. drilling cost, composed of:
 1. drilling cost of exploration; and
 2. drilling cost of development;
 - b. geological and geophysics cost, composed of:

1. geological

1. geological research cost; and
 2. geophysics research cost;
 - c. overhead costs in exploration; and
 - d. amortization cost
- (3) The exploitation cost as meant in paragraph (1) letter b shall consist of:
- a. direct production cost of:
 1. petroleum; and
 2. natural gas.
 - b. natural gas processing cost;
 - c. utility cost, composed of:
 1. cost of production apparatuses and equipment maintenance; and
 2. cost of steam, water and electricity;
 - d. overhead costs in exploitation; and
 - e. amortization cost.
- (4) The overhead cost of the exploration and exploitation as meant in paragraph (2) letter c and paragraph (3) letter d shall consist of:
- a. administrative and financial cost;
 - b. personnel expense;
 - c. cost of material service;
 - d. transportation cost;
 - e. overhead cost of office; and
 - f. indirect taxes, regional taxes and regional levies.
- (5) The miscellaneous cost as meant in paragraph (1) letter c shall consist of:
- a. cost needed for the transfer of gas from production point to delivery point; and
 - b. post-operation cost of upstream business activity.
- a. spent for obtaining, collecting and preserving income in accordance with the provision of legislation and related directly to activities of oil operation in work areas of the said contractors in Indonesia;
 - b. using rational price not influenced by the special relations as meant in the income tax law;
 - c. having oil operation in accordance with norms of good business and technical practices;
 - d. having activities of oil operation in accordance with work plan and budget already approved by the Head of the Executive Board as meant in Article 5 dan Article 6.
- (2) The spent costs directly related to oil operation as meant in paragraph (1) letter a shall meet requirements:
- a. in the case of amortization cost, only designated to goods and equipment used for oil operation, which becomes state property;
 - b. in the case of the direct cost of head office, charged to projects in Indonesia, which comes from other countries, only designated to activities:
 1. which cannot be executed by institutions/agencies in the country;
 2. which cannot be executed by Indonesian manpower; and
 3. which are not routine;
 - c. In the case of the granting of compensation with respects to work to employee /workers in the form of enjoyment nature, executed in accordance with the provision of taxation legislation;
 - d. In the case of the granting of natural disaster donation on behalf of the government, executed in accordance with the provision of taxation legislation;

Article 12

- (1) The operational costs which may be reimbursable in the calculation of production sharing and income tax shall comply with requirements:

- d. In the case of the granting of natural disaster donation on behalf of the government, executed in accordance with the provision of taxation legislation;

e. in the case of expenditure on community and environmental development, only in the exploration period;

f. in the case of expenditure on the allocation of indirect cost of head office with the provision as follows:

1. used for supporting business or activity in Indonesia;
2. contractors submit consolidated financial statement of head office, already audited, and allocation basis thereof; and
3. not exceeding the limit stipulated by a regulation of the Minister of Finance after securing consideration from the Minister.

(3) The maximum limit of cost related to remuneration of expatriates shall be stipulated by a regulation of the Minister of Finance after securing consideration from the Minister.

Article 13

The operational costs which cannot be reimbursed in the calculation of production sharing and income tax shall include:

- a. costs charged or spent for personal interest and/or family of workers, executives, holders of participating interest and shareholders;
- b. formation or accumulation of reserve funds, except mining closure and restoration costs saved at joint account of the executive board and contractor in account of commercial banks of the Indonesian government in Indonesia;
- c. granted assets;
- d. administrative sanction in the form of interest, fine,

and increase as well as penalty in the form of fine related to the implementation of taxation legislation as well as claims or fines arising from the mistake of contractor due to intentionality or negligence;

- e. amortization cost of goods and equipment, which are used and are not belonging to the state;
- f. incentives, payment of pension contribution and insurance premium for personal interest and/or family of expatriates, executives and shareholders.
- g. costs of expatriates not complying with the procedure for the plan to recruit expatriates (RPTKA) or not having expatriate working permit (IKTA);
- h. costs of legal consultants not related directly to oil operation in the framework of production sharing contract;
- i. cost of tax consultant;
- j. marketing cost of oil and/or natural gas becoming right of contractor, except marketing cost of natural gas already approved by the Head of the Executive Board;
- k. cost of representation, including cost of banquet in whatever name and form, unless otherwise accompanied by nominative list of beneficiaries and taxpayer code number (NPWP) of beneficiaries;
- l. cost of local environment and community development in the exploration period;
- m. cost of technical training of expatriates;
- n. cost related to merger, acquisition or cost of the transfer of participating interest;
- o. cost of interest on loan;
- p. income tax on employees, borne by contractors or paid as tax allowance and income tax which shall be withhold or collected from income tax on the third party, which is borne by contractor or grossed up;
- q. procurement

- q. procurement of other goods and services not matching the rationality principle and good technical norms, or exceeding the value of authorization approval of expenditure above 10% (ten percent) of the value of expenditure authorization;
- r. excessive material surplus attributed to mistake in the planning and purchase;
- s. book value and operational cost of assets already used, which cannot operate anymore due to negligence of contractors;
- t. transactions, which:
 - 1. inflict loss on the state;
 - 2. do not pass through tender in accordance with the provision of legislation, except in certain cases; or
 - 3. contravene legislation.
- u. bonus paid to the government;
- v. costs occurring before the signing of contract;
- w. incentive of interest recovery; and
- x. cost of commercial audit.

Article 14

Additional income obtained in the framework of the implementation of oil operation in the form of selling proceeds of by products or other forms shall be treated as offsetting account of operational cost.

Article 15

- (1) Goods having a benefit period not more than one year shall be charged as operational cost when the goods are used.
- (2) The charging as meant in paragraph (1) shall be done by average or prioritizing the first acquired goods.

Article 16

- (1) Amortization of expenditure on tangible assets having benefit period more than one year shall be done in a decreasing part during the benefit period, which is counted by means of applying the rate of amortization to the remaining book value and at the end of the benefit period, the remaining book value shall be amortized in lump sum.
- (2) The amortization shall start in month when the assets are used (placed into service).
- (3) The amortization shall be counted in accordance with category, rate and benefit period as contained in the attachment, which constitutes an integral part of this government regulation.
- (4) In the case of the tangible assets as meant in paragraph (1) being unusable anymore because of damage attributed to natural factor or force majeure, the remaining book value of the tangible assets shall continue to be amortized in accordance with the remainder of the benefit period thereof.

Article 17

- (1) The amount of reserves of mining closure and restoration costs charged for one tax year shall be counted on the basis of the estimated mining closure and restoration costs on the basis of the economic benefit period.
- (2) The reserves of the costs as meant in paragraph (1) shall be saved in joint account of the executive board and contractors at commercial banks of the Indonesian government in Indonesia.
- (3) In the case of the realized mining closure and restoration costs being smaller or bigger than the reserved

amount, the difference shall become subtrahend or enumerator of the reimbursable operational costs of the respective work areas or the said field, after securing approval from the Head of the Executive Board.

- (4) Provision on procedures for the use of reserve funds of mining closure and restoration costs shall be governed by a ministerial regulation.

Article 18

- (1) Contractors may charge contribution to severance pay of permanent employees paid to manpower severance pay management stipulated by the Minister of Finance.
- (2) Procedures for managing contribution to severance pay and the amount of severance pay shall be governed by a regulation of the Minister of Finance.

Article 19

- (1) The whole working costs shall have their charging postponed until field produces commercially in the work area as meant in Article 7 paragraph (1).
- (2) In order to secure state revenue, besides the postponement as meant in paragraph (1), the Minister may take policies related to development of field.

Article 20

- (1) The operational costs as meant in Article 12, which are reimbursable in one calendar year, shall consist of:
- current year non-capital cost;
 - amortization of current year capital cost; and
 - operational cost not yet reimbursable in the previous years.
- (2) The maximum amount of the reimbursable operational costs as meant in paragraph (1) for service contract

shall be stipulated as much as the compensation granted by the government.

- (3) The reimbursable operational cost as meant in paragraph (1), which remains uncountable in one calendar year, may be counted in the following year.
- (4) The direct cost of petroleum shall be charged into petroleum production and direct cost of natural gas shall be charged into natural gas production.
- (5) In the case of joint cost of petroleum and natural gas being available, the joint cost shall be allocated in accordance with the proportion of the relative value of production.
- (6) In the case of a file or work area already producing a kind of petroleum or natural gas, while other kinds of production have not produced, the joint cost as meant in paragraph (5) shall be allocated fairly on the basis of agreement between the executive board and contractor.
- (7) The reimbursement of operational cost of petroleum shall be applied to only petroleum lifting, while the reimbursement of operational cost of natural gas shall be applied to only the selling value of natural gas.
- (8) In the case of the reimbursement of operational cost of petroleum or natural gas being not sufficient from the production or the selling value:
- the operational cost of natural gas exceeding the production value shall be determined and the difference shall be charged into the production of petroleum;
 - the operational cost of petroleum exceeding the production value shall be determined and the difference shall be charged into the selling value of natural gas.

CHAPTER III

RECOGNITION AND MEASUREMENT OF INCOME

Article 21

Income of contractors for production sharing contract shall be recognized at delivery point.

Article 22

- (1) Income from joint cooperation contract in the form of petroleum sales shall be valued by using the Indonesia Crude Oil Price.
- (2) Methodology and formula of the Indonesia Crude Oil Price as meant in paragraph (1) shall be stipulated jointly by the Minister and the Minister of Finance.
- (3) Provision on procedures for stipulating methodology and formula of the Indonesia Crude Oil Price as meant in paragraph (2) shall be governed in a ministerial regulation.

Article 23

- (1) Income from joint cooperation contract in the form of natural gas sales contract shall be counted on the basis of the agreed price in the natural gas sales contract.
- (2) In the case of the sales of natural gas as meant in paragraph (1) being executed after natural gas is obtained through advanced process approved by the Minister, the recognized income shall be counted on the basis of the received selling proceeds, subtracted by components of selling cost.

CHAPTER IV

CALCULATION OF PRODUCTION SHARING

- (1) In the case of FTP and investment incentive being not

available, equity to be split shall be counted on the basis of lifting, subtracted by the reimbursable operational costs as meant in Article 20.

- (2) In the case of FTP being available but investment incentive being not available, equity to be split shall be counted on the basis of lifting, subtracted by FTP and the reimbursable operational costs.
- (3) In the case of FTP and investment incentive being available, equity to be split shall be counted on the basis of lifting, subtracted by FTP, investment incentive and the reimbursable operational costs.
- (4) In the case of FTP being not available but investment incentive being available, equity to be split shall be counted on the basis of lifting, subtracted by investment incentive and the reimbursable operational costs.
- (5) The investment incentive and the reimbursable operational costs in accordance with the provision of legislation shall be converted into:
 - a. petroleum, with the average price being the Indonesian Crude Oil Price as meant in Article 22; or
 - b. natural gas, with the price agreed in natural gas sales contract.
- (6) Right of contractors, in the case of joint cooperation contract, shall be counted on the basis of percentage of the pre-income tax right of the contractors stipulated in joint cooperation contract, which is multiplied by equity to be split.
- (7) Right of the government, in the case of joint cooperation contract, shall be counted on the basis of percentage of right of the government stipulated in the joint cooperation contract, which multiplied by equity to be split wherein income tax payable by contractors has not been included.
- (8) Contractors

- (8) Contractors shall be obliged to fulfill DMO by giving up 25% (twenty five percent) of their right from the produced petroleum and/or natural gas to fulfill the domestic need.
- (9) Contractors shall obtain a compensation for DMO with respects to the delivery of the petroleum and/or natural gas as meant in paragraph (8) with the price stipulated by the Minister.

CHAPTER V

CALCULATION OF INCOME TAX

Article 25

- (1) Taxable income of contractors, in the case of production sharing contract, for one tax year shall be counted on the basis of income in the framework of the production sharing contract as meant in Article 9 paragraph (2), subtracted by the current year non-capital cost, amortization of current year capital cost and the operational cost not yet reimbursable in the previous years.
- (2) In the case of the amount of the offsetting account as meant in paragraph (1) being bigger than the income as meant in Article 9 paragraph (2), the negative difference shall be counted in the following tax year until the contract expires.
- (3) The amount of income tax payable by contractors shall be counted on the basis of the taxable income as meant in paragraph (1), multiplied by the stipulated tax rate in accordance with the provision of taxation legislation.
- (4) The amount of income tax payable by contractors having contract signed before the enforcement of this government regulation shall be counted on the basis of the corporate tax rate or income tax when the contract is signed.
- (5) The taxable income as meant in paragraph (1), after being subtracted by the income tax as meant in paragraph (3) or paragraph (4), shall be indebted to income tax in accordance with the provision of legislation.
- (6) In the case of contractor being in the form of Indonesian legal entity, the taxable income as meant in paragraph (1), after being subtracted by the income tax as meant in paragraph (3) shall be treated as dividend provided for the payment and indebted to income tax in accordance with the provision of legislation.
- (7) Following the fulfillment of the income tax liability as meant in paragraph (3), paragraph (4), paragraph (5), and paragraph (6), income tax assessment of petroleum and natural gas shall be issued after tax audit is executed.
- (8) Before the income tax assessment of petroleum and natural gas is issued, provisional income tax assessment of petroleum and natural gas may be issued.
- (9) The provision on the issuance of income tax assessment of petroleum and natural gas as meant in paragraph (7) and provisional income tax assessment of petroleum and natural gas as meant in paragraph (8) shall be governed by a regulation of the Director General of Taxation.
- (10) Contractors shall be exempted from the collection of import duty and tax in the framework of import on goods used in oil operation in exploration and exploitation activities.
- (11) The provision on procedures for the exemption of import duty and collection of tax in the framework of

import as meant in paragraph (10) shall be governed in accordance with the provision of legislation.

Article 26

- (1) Taxable income of contractors in the framework of service contract for one tax year shall be based on the income as meant in Article 9 paragraph (3), subtracted by current year non-capital cost, amortization of current year capital cost and the whole operational costs as meant in Article 12, which have not been reimbursed.
- (2) The provision on the maximum amount of the offsetting account as meant in paragraph (1) plus the compensation granted by the government to contractors shall be governed by a ministerial regulation.
- (3) In the case of the offsetting account as meant in paragraph (1) being bigger than the income as meant in Article 9 paragraph (3), the negative difference shall be counted in the following tax years up to the expiration of contract.
- (4) The amount of income tax payable by contractors shall be based on the taxable income as meant in paragraph (1), multiplied by the rate in accordance with the provision of taxation legislation.
- (5) The taxable income as meant in paragraph (1), after being subtracted by the income tax as meant in paragraph (4) shall be treated as dividend provided for the payment and indebted to income tax in accordance with legislation.

CHAPTER VI

INCOME OUTSIDE JOINT COOPERATION CONTRACT

Article 27

- (1) Other income of contractors in the form of uplift or other compensation of the same kind as meant in

Article 9 paragraph (4) letter a shall be subject to final income tax with the rate 20% (twenty percent) of the gross amount.

- (2) Income of contractors from the transfer of participating interest as meant in Article 9 paragraph (4) letter b shall be subject to final income tax with the rate:
 - a. 5% (five percent) of the gross amount, in the case of the transfer of participating interest during the exploration period; or
 - b. 7% (seven percent) of the gross amount, in the case of the transfer of participating interest during the exploitation period.
- (3) The imposition of the income tax as meant in paragraph (2) letter b shall be excluded as long as the obligation to transfer participating interest to national companies is in accordance with joint cooperation contract as contained in the joint cooperation contract.
- (4) The provision on procedures for withholding and payment of the income tax as meant in paragraph (1), paragraph (2), and paragraph (3) shall be governed by a regulation of the Minister of Finance.

Article 28

In the framework of distributing risks in the exploration period, the transfer of participating interest shall not include the income as meant in Article 9 paragraph (4) letter b if the following criteria are fulfilled:

- a. contractor does not transfer participating interest wholly;
- b. participating interest has been owned over 3 (three) years;
- c. exploration has been executed in work area (investment expenditure has been realized); and

d. the

- d. the transfer of participating interest is not intended to obtain profit .

CHAPTER VII

BOOKKEEPING OF CONTRACTOR

Article 29

- (1) Bookkeeping or recording shall be performed by regarding the good will and reflecting the actual business condition or activity.
- (2) Bookkeeping or recordings shall be executed in Indonesia by using Latin letter, Arabic figure and prepared in Indonesian language or foreign language already securing approval of the Minister of Finance.
- (3) Bookkeeping shall be performed by norm compliant principle, in accordance with financial accountancy standard and production sharing contract principle.
- (4) Bookkeeping shall consist of at least record of assets, liabilities, capital, income and cost and purchase so that the amount of tax payable can be counted.
- (5) Books, records and documents becoming the basis of bookkeeping or recording and other documents, including results of data processing of bookkeeping managed electronically or based on online application program shall be provided in Indonesia in so far as the costs as meant in Article 12 have not been reimbursed.

Article 30

- (1) In order to calculate tax, the Directorate General of Taxation shall stipulate the amount of cost in the exploration phase in every year in the upstream oil and natural gas business field after securing recommendation from the Executive Board.

- (2) Before stipulating the amount of the cost as meant in paragraph (1), government auditors on behalf of the Directorate General of Taxation shall conduct audit.
- (3) IN the case of the amount of cost recommended by the executive board as meant in paragraph (1) being different from the amount of cost resulting from audit by the government auditor as meant in paragraph (2), the government auditor and executive board shall be obliged to settle the difference.

CHAPTER VIII

OBLIGATION OF CONTRACTOR AND/OR OPERATOR

Article 31

- (1) Every contractor in a work area shall be obliged to:
 - a. register to obtain taxpayer code number;
 - b. perform bookkeeping;
 - c. submit annual income tax returns (SPT Tahunan PPh);
 - d. pay tax installment in the current year, not later than the 15th of the ensuing month in every month, and counted from the taxable income from the actual lifting in a calendar year;
 - e. fulfill other provisions in accordance with the provision of taxation legislation.
- (2) In the case of the transfer of participating interest or share, contractor shall be obliged to report the value to the Director General of Taxation.
- (3) In the case of the transfer of participating interest, taxation rights and obligations shall shift to new contractor.
- (4) Model and content of annual income tax returns (SPT Tahunan PPh) as meant in paragraph (1) letter c shall be governed by regulation of the Director General of Taxation.

Article 32

- (1) Every operator in a work area shall be obliged to:
 - a. register joint cooperation contract to secure a taxpayer code number different from the taxpayer code number as meant in Article 31 paragraph (1) letter a;
 - b. fulfill the obligation to withhold and/or collect tax;
 - c. perform bookkeeping for activities of oil operation in the work area.
- (2) In the case of operator changing, the obligation as meant in paragraph (1) shall shift to new operator.

Article 33

- (1) Petroleum and/or natural gas becoming right of the government from the production sharing contract as meant in Article 24 shall be counted on the basis of the volume of petroleum and/or natural gas.
- (2) In the case of the government needing petroleum and/or natural gas to fulfill the domestic need, income tax on contractor from the production sharing contract may be in the form of volume of petroleum and/or natural gas resulting from right of contractor.
- (3) Provision on the calculation and procedures for submitting the right of the government as meant in paragraph (1) shall be governed by a ministerial regulation.
- (4) Provision on the calculation and procedures for the payment of income tax as meant in paragraph (2) shall be governed by a regulation of the Minister of Finance.

CHAPTER IX

OBLIGATION OF EXECUTIVE BOARD

Article 34

- (1) The executive board shall be obliged to issue standards or norms, kinds, categories and amounts of costs

used in activities of oil operation in coincidence with the enforcement of this government regulation.

- (2) The executive board shall be obliged to submit bookkeeping report on the realization of reimbursement of operational cost to the Director General of Taxation and the Director General of Oil and Gas periodically every year and at any time if necessary.

CHAPTER X

MISCELLANY

Article 35

- (1) Contractors shall execute their transactions in Indonesia and settle the payment through banking system in Indonesia.
- (2) The transactions and settlement of payment as meant in paragraph (1) may only be realized outside Indonesia after securing approval from the Minister of Finance.

Article 36

- (1) The Minister of Finance in certain conditions may appoint the independent third party to conduct financial and technical verification after coordinating with the Minister.
- (2) The appointment of the third part as meant in paragraph (1) shall be executed in accordance with the provision of legislation in the field of the procurement of goods and services.

Article 37

In the case of any change in legal status and/or domicile and/or the transfer of participating interest or ownership or others from contractor thus changing the calculation of income tax, the right of the state revenue shall remain unchanged.

CHAPTER XI
TRANSITIONAL PROVISION

Article 38

Following the enforcement of this government regulation:

- a. The joint cooperation contracts already signed before the promulgation of this government regulation shall be declared to remain effective until the expiry date of the contracts.
- b. Matters not yet regulated or not yet regulated sufficiently shall be regulated firmly in the joint cooperation contracts as meant in letter a for the provision related to:
 1. the amount of right of state revenue;
 2. requirements for reimbursable operational costs and operational cost charging norms;
 3. non reimbursable operational costs;
 4. appointment of the independent third party to conduct financial and technical verification;
 5. issuance of income tax assessment;
 6. exemption from import duty and tax in the framework of the import on goods in exploration and exploitation activities;
 7. income tax on contractor in the form of the volume of petroleum and/or natural gas resulting from right of contractor; and
 8. income outside joint cooperation contract in the form of uplift and/or the transfer of participating interest, in not later than 3 (three) months shall be adjusted to this government regulation.

CHAPTER XII
CONCLUSION

Article 39

The production sharing contracts in upstream oil

and natural gas business activities, which are made or extended following the enforcement of this government regulation shall abide by the provisions in this government regulation.

Article 40

The government regulation shall come into force as from the date of promulgation.

For public cognizance, the government regulation shall be promulgated by placing it in Statute Book of the Republic of Indonesia.

Stipulated in Jakarta

On December 20, 2010

THE PRESIDENT OF THE REPUBLIC OF INDONESIA,
sgd.

DR. H. SUSILO BAMBANG YUDHOYONO

Promulgated in Jakarta

On December 20, 2010

THE MINISTER OF LAW AND HUMAN RIGHTS OF THE
REPUBLIC OF INDONESIA
sgd

PATRIALIS AKBAR

STATUTE BOOK OF THE REPUBLIC OF INDONESIA
YEAR 2010 NUMBER 139

ELUCIDATION.....
(To be continued)

—==(R)==—

COST RECOVERY AND INCOME TAX TREATMENT IN THE UPSTREAM OIL AND NATURAL GAS BUSINESS FIELD

(Government Regulation Number 79 Year 2010 dated December 20, 2010)

[Continued from Business News No. 8053 pages 1A-14A]

ELUCIDATION

ON

GOVERNMENT REGULATION OF

THE REPUBLIC OF INDONESIA

NUMBER 79 YEAR 20 10

REGARDING

**COST RECOVERY AND INCOME TAX TREATMENT IN
THE UPSTREAM OIL AND NATURAL GAS BUSINESS FIELD**

I. GENERAL

Article 33 paragraph (2) and paragraph (3) of the Constitution of 1945 affirms that production fields important for the state and controlling the life of the public at large, including oil and natural gas, which constitute strategic and non-renewable natural resources are controlled by the state. Given that oil and natural gas constitute a key source of state revenue, the management thereof needs to be executed efficiently and optimally so as to be usable maximally for the prosperity and welfare of the people.

Oil and natural gas have been managed through a production sharing contract also adopted by most oil producer countries.

This government regulation better guarantees state revenue

from income of production sharing contract and other income become more optimal through, among others:

- a. costs deductible from gross income will be the same as the costs which can be reimbursed by the government;
- b. kind, requirement, allocation method and limit of the cost are to be governed properly so that the state revenue is more optimal and legal certainty is created;
- c. indirect taxes such as value added tax (VAT), import duty, land and building tax (PBB), regional taxes and regional levies which have so far been borne by the government are changed to become collective burden of the government and contractors by booking the payment of the indirect taxes as component of cost;
- d. contractors are obliged to pay directly income tax payable on income received or earned outside the joint cooperation contract scheme.

The government regulation is stipulated with a view of preventing the misapplication of double taxation avoidance agreement (P3B).

In the framework of maximizing state revenue from the existing contracts, Law Number 41 Year 2008 regarding the State Budget of Revenue and Expenditure in Fiscal Year 2009 mandates the government to issue regulation governing the reimbursement of operational costs already spent by contractors in the framework of joint cooperation contract. For the purpose, the provisions governed in this government regulation also apply to joint cooperation contracts already signed before the enforcement of this government regulation with several transitional provisions.

II. ARTICLE BY ARTICLE

Article 1

Sufficiently clear

Article 2

Sufficiently clear

Article 3

Paragraph (1)

In the case of joint cooperation contract in the upstream oil and natural gas business field, the government provides natural resources while contractors are obliged to carry capital and technology. As a consequence, the contractors are not permitted to charge interest cost and royalty cost and the like into the reimbursable operational costs.

Paragraph (2)

Sufficiently clear

Article 4

Paragraph (1)

Basically the whole expenditures on goods and equipment purchased by contractors constitute state property so that the expenditures constitute operational costs which can be reimbursed by the government to the contractors on the basis of the acquisition price.

Paragraph (2)

Sufficiently clear

Article 5

Norms of good business practices cover norms of generally effective and proper business practices in accordance with business ethic, while good technical norms include:

- a. abiding by provisions on occupational safety and health as well as environmental protection and management;
- b. producing oil and natural gas in accordance with good reservoir management norms;
- c. producing oil and natural gas wells properly;
- d. using the right advanced-level oil exploitation technology;
- e. enhancing efforts to increase capability of reservoirs to transfer fluid by a right technique; and
- f. fulfilling the provision on the required equipment standards.

Paragraph (2)

Letter a

Routine expenditure is, among others, salary payment, maintenance cost and post-mining operational cost.

Letter b.....

Letter b

Project expenditure is, among others, development of production facilities and seismic survey.

Paragraph (3)

Sufficiently clear

Paragraph (4)

Sufficiently clear

Article 6

Financial spending authorization is authorization for expenditure (AFE) .

Article 7

Sufficiently clear

Article 8

Sufficiently clear

Article 9

Paragraph (1)

Sufficiently clear

Paragraph (2)

The price variant of lifting means a price difference attributed to the difference between month Indonesia Crude Oil Price and weighted Indonesian crude Price average.

Paragraph (3)

Sufficiently clear

Paragraph (4)

Sufficiently clear

Article 10

Paragraph (1)

Sufficiently clear

Paragraph (2)

Development of work area in this provision covers expansion and intensification.

Article 11

Costs deductible from income are the same as the costs to be reimbursed by the government to contractors in the framework of joint cooperation contracts and vice versa. The principle is usually known as uniformity principle.

The operational costs as referred to in this provision constitute costs becoming the basis in the calculation of production sharing and taxable income.

Paragraph (1)

Sufficiently clear

Paragraph (2)

Sufficiently clear

Paragraph (3)

Letter a

Sufficiently clear

Letter b

Sufficiently clear

Letter c

Sufficiently clear

Letter d

Sufficiently clear

Letter e

The amortization costs include, among others:

1. production facility;
2. office building, warehouse, housing;
3. machine and equipment.

Paragraph (4)

Sufficiently clear

Letter a

Cost needed to transfer gas from production point to delivery point includes marketing cost.

Letter b

Sufficiently clear

Article 12

Letter a

Costs needed to obtain, collect and preserve income are called as daily costs which may be charged in the expenditure year. In order to charge the expenditure as cost, the expenditure must have direct or indirect relations with business activities or activities to obtain, collect and preserve income in activities of oil operation in commercially producing fields in the said work area in Indonesia.

Therefore, spending for obtaining, collecting and preserving income which is not tax object, in accordance with the provision of legislation in the field of income tax and/or for income subject to final income tax may be not be charged as reimbursable cost.

Letter b

Sufficiently clear

Letter c

Sufficiently clear

Letter d

Sufficiently clear

Paragraph (2)

Letter a

Sufficiently clear

Letter b

Direct costs of head office charged into the project are costs related directly to activities of oil operation in Indonesia with the provision that:

1. the activities cannot be executed by institutions/agencies in the country;
2. the activities cannot be executed by Indonesian manpower; and
3. the activities are not routine.

Letter c

Sufficiently clear

Letter d

Sufficiently clear

Letter e

Sufficiently clear

Letter f

Sufficiently clear .

Paragraph (3)

The regulation of the Minister of Finance governs at least the moment of enforcement of remuneration.

Article 13

Letter a

Sufficiently clear

Letter b

Sufficiently clear

Letter c

The granted assets may not be charged as cost because the assets constitute state property.

Letter d

Sufficiently clear

Letter e

Sufficiently clear

Letter f

Sufficiently clear

Letter g

Sufficiently clear

Letter h

Sufficiently clear

Letter i

Sufficiently clear

Letter j

Sufficiently clear

Letter k

Sufficiently clear

Letter l

Sufficiently clear

Letter m

Sufficiently clear

Letter n

Merger and acquisition related costs are, among others:

- a. personal and consultant costs related to due diligence;
- b. external cost of press release, promotion and change in corporate logo;
- c. cost related to separation program dan retention program, cost related to technology of information system (as long as the old system has not been depreciated fully), cost related to change in location of office and cost arising from change in policy on the ongoing project.

Letter o

Interest on loan is interest on loan used for financing oil operation.

Letter p

Sufficiently clear

Letter q

Sufficiently clear

Letter r

Mistake in planning means an action of contractor in formulating plan, which may be categorized as serious negligence or intentional misconduct. Serious negligence or intentional misconduct means every intentional action or carelessness committed by management or senior official of contract:

- a. having consequence ascertained or allegedly ascertained to be potential to inflict loss on people or threaten security or ownership of other people or bodies; or
- b. violating fatally standards of prudence which cause harmful consequence in the ignorance or unawareness thereof.

Letter s

Negligence of contractors means serious negligence (gross negligence) or intentional misconduct (willful misconduct).

Part of the construction cost of production facility/equipment cannot be charged into non reimbursable operational costs in the event that:

- a. It can be proven that the capacity of the production facility meets the agreed target so that the charging can only be applied proportionally to the proven capacity;
- b. it can be proven that performance of the production facility meets the stipulated criteria so that the charging can only be applied proportionally to the proven performance.
- c. the production facility, including indemnity for all risk construction insurance is improved or re-designed/replaced wholly and/or partly in the construction period;
- d. failure attributed to mistake in the fabrication of manufacturing occurs in the guarantee period so that the cost of repairing or replacement becomes responsibility of contractor supplying goods/services.

Letter t

Point 1

Transactions inflicting loss on the state mean the realized transactions do not comply with the provisions of legislation thus inflicting loss on the state, such as the procurement of goods and services not suitable to the stipulated specifications and others.

Point 2

Not passing through tender means the procurement of the whole goods and services is obliged to pass through tender in accordance with the effective need but goods and services needed for emergency need can be procured without tender.

Point 3

Sufficiently clear

Letter u

Sufficiently clear

Letter v

Sufficiently clear

Letter w

Sufficiently clear

Letter x

In the case of urgent national interests, such as continuation of production, acceleration of the increase in oil and/or natural gas production contributing maximal benefit to the state, exception may be applied to the provision.

Article 14

Additional income resulting from the selling proceeds of by products is among others income from the sales of sulfur and surplus capacity of electricity.

Article 15

Sufficiently clear

Article 16

Paragraph (1)

Sufficiently clear

Paragraph (2)

"Placed into service" means a momento when a tangible asset starts to be used and has met the requirements stipulated by the Executive Board.

Paragraph (3)

Sufficiently clear

Paragraph (4)

Sufficiently clear

Article 17

Paragraph (1)

Tax Year means calendar year.

Paragraph (2)

Sufficiently clear

Paragraph (3)

Sufficiently clear

Paragraph (4)

Sufficiently clear

Article 18

Sufficiently clear

Article 19

Paragraph (1)

Sufficiently clear

28A.

Paragraph (2)

Policy means, among others, in the framework of reimbursement of cost on the basis of scale of economy of field or several field in recommendation about plan for the development of field (POD basis) or the development of field based on scale of economy of a field (field basis) or development of field on the basis of scale of economy of a well or several wells without building personal production facility (put on production).

Article 20

Paragraph (1)

Letter a

Sufficiently clear

Letter b

Sufficiently clear

Letter c

Operational cost not yet reimbursable in the previous years is a part of the balance of operational cost, which have not been reimbursable early year so that it can be reimbursed in the current year in accordance with the production sharing pattern.

Paragraph (2)

Sufficiently clear

Paragraph (3)

Sufficiently clear

Paragraph (4)

Sufficiently clear

Paragraph (5)

Sufficiently clear

Paragraph (6)

Sufficiently clear

Paragraph (7)

Sufficiently clear

Paragraph (8)

Sufficiently clear

Article 21

Delivery point means a point where the title to oil and/natural gas transfers from the government to contractors.

Article 22

Paragraph (1)

Sufficiently clear

Paragraph (2)

Indonesia Crude Oil Price means the Price of crude oil stipulated periodically by the Minister.

Paragraph (3)

Sufficiently clear

Article 23

Paragraph (1)

Sufficiently clear

Paragraph (2)

Component of selling cost is cost related to advanced processing of gas up to the sales, among others, cost of loan needed for building plant, operational cost of plant and marketing cost.

Article 24

Sufficiently clear

Article 25

Paragraph (1)

Sufficiently clear

Paragraph (2)

Sufficiently clear

Paragraph (3)

The tax rate according to the provision of taxation legislation means the application of tax rate according to tax rate chosen by contractors, namely tax rate effective when the joint cooperation contract is signed or tax rate according to taxation legislation in force and subject to change.

Paragraph (4)

Sufficiently clear

Paragraph (5)

Sufficiently clear

Paragraph (6)

Sufficiently clear

Paragraph (7)

Income tax assessment of oil and natural gas is a tax assessment issued by the Director General of Taxation following audit.

Paragraph (8)

Provisional income tax assessment of oil and natural gas means a tax assessment issued by the Director General of Taxation before the usage, among other internal interest of management of head office is audited.

Paragraph (9)

Sufficiently clear

Paragraph (10)

Sufficiently clear

Paragraph (11)

Sufficiently clear

Article 26

Sufficiently clear

Article 27

Paragraph (1)

Sufficiently clear

Paragraph (2)

Sufficiently clear

Paragraph (3)

Participating interest is executed on the basis of legislation.

Paragraph (4)

Sufficiently clear

Article 28

Sufficiently clear

Article 29

Sufficiently clear

Article 30

Sufficiently clear

Article 31

Paragraph (1)

Sufficiently clear

Paragraph (2)

Sufficiently clear

Paragraph (3)

If interest in a work area is owned by Contractor A, Contractor B, and Contractor C and interest of Contractor A is later transferred to Contractor D, the taxation

liabilities to the said interest become liabilities of Contractor D as from the moment when the transfer of interest is effective.

Paragraph (4)

Sufficiently clear

Article 32

Paragraph (1)

Letter a

If Contractor A has signed joint cooperation contract of oil and natural gas with the government in work area X, Contractor A, also acting as operator, is obliged to register the work area to secure NPWP different from NPWP of the said contractor.

Letter b

Sufficiently clear

Letter c

Sufficiently clear

Paragraph (2)

If Contractor B becomes operator to replace Contractor A, the liabilities shift to Contractor B as from the moment when the transfer is effective.

Article 33

Sufficiently clear

Article 34

Paragraph (1)

Standards, norms, categories and amount of cost are qualitative and/or quantitative parameters that constitute a range of value representing the technical condition and rationality of substances of costs of goods and services used as comparator in the approval of work plan and budget as well as financial spending authorization.

The charging of operational cost is based on the realization of the spent cost on the basis of the procurement of goods and services in accordance with the provision of legislation. The standards or norms, kinds, categories and amount of cost are to be evaluated in accordance with the need.

Paragraph (2)

Sufficiently clear

Article 35

Sufficiently clear

Article 36

Paragraph (1)

Certain conditions mean disaster attributed to natural phenomenon, which are potential to cause state loss, such as decreasing revenue and/or loss in state assets in the exploration and/or exploitation of oil and/or natural gas.

Paragraph (2)

Sufficiently clear

Article 37

The provision is intended to prevent the amount of state revenue (taxes and non-tax state revenue) from changing in accordance with the amount of state revenue mentioned in joint cooperation contract.

Article 38

Letter a

Sufficiently clear

Letter b

Sufficiently clear

Article 39

Sufficiently clear

Article 40

Sufficiently clear

SUPPLEMENT TO STATUTE BOOK OF THE REPUBLIC OF

INDONESIA NUMBER 5173

ATTACHMENT TO GOVERNMENT REGULATION

NUMBER 79 YEAR 2010

GROUP OF TANGIBLE GOODS, BENEFIT PERIOD AND RATES

GROUP AND RATE	BENEFIT PERIOD
<p>GROUP I : Rate 50%</p> <ol style="list-style-type: none"> 1. Passenger Car 2. Light Truck (13,000 pounds or less) and tractor 3. Heavy Truck (above 13,000 pounds) 4. Aircraft 5. Construction equipment 	<p>1.5 years</p> <p>2 years</p> <p>3 years</p> <p>3 years</p> <p>3 years</p>
<p>GROUP II: Rate 25%</p> <ol style="list-style-type: none"> 1. Bus 2. Office and household appliance 3. Building of Supporting Facilities and Structures 4. Production Facility 5. Cabin and locomotive 6. Drilling and production equipment as well as appliance and instruments thereof 	<p>4.5 years</p> <p>5 years</p> <p>5 years</p> <p>5 years</p> <p>7.5 years</p> <p>5 years</p>
<p>GROUP III : Rate 12.5%</p> <ol style="list-style-type: none"> 1. Ships, barges, tug boats and floating instrument of the same kind 2. Office and House Building as well as Welfare 	<p>9 years</p> <p>10 years</p>

THE PRESIDENT OF THE REPUBLIC OF INDONESIA,

sgd.

DR. H. SUSILO BAMBANG YUDHOYONO

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