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Analysis of Oman's 2015 Budget

8 January 2015

Oman's 2015 budget at a glance

5% Economic Growth Budgeted

4.4% Increase in Expenditure

	2015			2014	
Revenues	RO (million)	Percentage of Total	Percentage Change from 2014	RO (million)	Percentage of Total
Oil Revenues	7,700	66	(6)	8,150	70
Gas Revenues	1,460	13	(3)	1,500	12
Oil & Gas Revenues	9,160	79	(5)	9,650	82
Taxes & Fees	1,334	12	29	1,038	9
Other Non-Tax Revenues	981	8	7	913	8
Others	125	1	26	99	1
Other Current & Capital Revenues	2,440	21	19	2,050	18
Total revenues	11,600		(1)	11,700	
Expenditure					
Defence & Security	(3,800)	27	3	(3,700)	27
Oil & Gas Production	(2,080)	15	14	(1,822)	13
Development Expenditure for Civil Ministries	(1,650)	12	(8)	(1,800)	13
Current & Capital Expenditure for Civil Ministries:					
Education	(1,806)	13	27	(1,422)	11
Health	(684)	5	17	(587)	4
Social Security & Welfare	(564)	4	17	(483)	4
Housing	(568)	4	10	(518)	4
Public Services	(592)	4	10	(537)	4
Others	(996)	7	2	(978)	7
	(5,210)	37	15	(4,525)	34
Participation in Domestic, Regional & International Institutions	(200)	1	(5)	(211)	2
Others	(1,160)	8	(20)	(1,442)	11
Total Expenditure	(14,100)		4	(13,500)	
Deficit	(2,500)		39	(1,800)	
Deficit as Percentage of Total Revenue:	22%			15%	
Deficit Financed by:					
Grants	200				
Borrowings	600			400	
Reserves	700			400	
Use of Previous Years' Surplus	1,000			1,000	
	2,500			1,800	

Source of the Newsletter: Royal Decree Nos. 1/2015, 1/2014, and the press statement of the Ministry of Finance issued on 1 January 2015

A budget for driving growth

The 2015 budget comes amidst a strong reduction in global oil prices but a commitment from the Oman Government that critical projects will remain on track and that projects intended to diversify the economy, and stimulate economic growth, will continue to be supported.

This includes continuing investment at Duqm, as well as commencement of the Sohar – Al Buraimi section of the national railway project, and several major road projects. The budget also provides for several significant tourism projects, including a number of hotel developments and the Oman Convention & Exhibition Centre, in Muscat. Falling interest rates are expected to encourage investment activity. Falling global commodity prices are expected to reduce inflation to 2.0% for 2015 (2014: 2.2%; 2013: 3.1%).

It is expected that real growth for 2014 will hit 4.4% and will increase to 5% in 2015. This includes a budgeted 5.5% growth in non-oil activities.

While taxes and fees have been used as one means to plug the gap caused by falling oil and gas revenues, the Ministry of Finance acknowledges a number of options to fund the deficit, namely privatisation of several State-owned companies, through 2015 to 2017, and borrowings, including the potential issue of Islamic bonds.

Total revenues to reduce by 0.9 percent

Despite the sharp downturn in oil prices at the end of 2014, the total estimated revenues for 2015 are only expected to reduce by RO 100 million (or 0.9%), to RO 11.6 billion (2014: RO 11.7 billion). Actual revenues for 2014 are expected to total approximately RO 13.9 billion, mainly due to a higher than budgeted oil price for a significant part of the year.

Oil and gas revenues are expected to reduce by around 5% but, at RO 9.2 billion, still constitute 79% of total revenues (2014: RO 9.7 billion and 83%). The 2014 budget was based on an average oil price of US$ 85 per barrel. The 2015 budget does not disclose the budget price per barrel.

If we assume the cost of production remains roughly constant, the 2015 budget would reflect a price in the region of US$ 80, based on indicated production of 980,000 barrels per day (2014: 945,000 barrels per day).

The 2015 budget doesn't disclose a breakeven price (2014 budgeted breakeven price: US$105 per barrel). However, the overall budget deficit of RO 2.5 billion represents only a slight increase on the 2014 budget deficit (of RO 1.8 billion) and oil production is expected to increase slightly in 2015 (to 980,000 barrels per day). One might assume, therefore, that the breakeven price would not increase significantly in 2015. The actual realised price for 2014 has not been disclosed (2013: US$109 per barrel).

Revenues from taxes and fees projected to increase by 28.5 percent

Revenues from taxes and fees are budgeted at RO 1.3 billion for 2015 (2014: RO 1.0 billion), representing a significant increase of 28.5%.

Revenues from income tax are expected to rise by 25%, from RO 400 million (2014) to RO 500 million (2015). This is a significant increase by comparison to previous budgets (2014: 14% budgeted increase; 2013: 3% budgeted increase).

The increase in income tax revenue will reflect income tax collections made in 2015 but relating to 2014 and previous years and there must be an expectation that part of this increase will relate to older tax years, tax assessments for which are expected to be completed in 2015. Taxpayers could therefore expect greater scrutiny of their tax returns during 2015.

While there has been some debate around the introduction of new taxes and a possible increase of the income tax rate, there have been no announcements, and any changes that are introduced during the year would only be reflected in later years' tax collections.

There is a noticeable increase in revenues from non-Omani labour licences, from RO 150 million (2014) to RO 245 million (2015). It is expected that this reflects an increase in the labour licence fee, rather than a significant increase in the number of labour licences being issued.

There is also a 22% increase in Customs duties, from RO 270 million (2014) to RO 330 million. This is consistent with the planned investment in major projects, and the increase in imports that would be expected, in order to deliver these projects.

Overall expenditure increases by 4.4 percent

Overall expenditure increases by only 4.4%, to RO 14.1 billion (2014: RO 13.5 billion).

Education expenditure increases by 27%, though, to RO 1.8 billion (2014: RO 1.4 billion), and this is consistent with the commitment to continue investment in public and university education and the higher and technical education scholarship programs.

Notable increases can also be seen in the level of health expenditure, by 16.6% to RO 684 million (2014: RO 587 million), and social security, by 16.8% to RO 564 million (2014: RO 483 million). Social security expenditure also reflects increased pension contributions of RO 286 million, an increase of 28.9% (2014: RO 222 million).

Key tax developments in 2014

1. Double tax agreements

Japan – Oman Income Tax Treaty
On 10 January 2014, the Governments of Oman and Japan signed a new double tax agreement (DTA), in Muscat. The DTA came into force on 1 September 2014 and will have effect from 1 January 2015. Under the DTA, the maximum rates of withholding tax are:

- 10% on dividends (5% in certain specific cases);
- 10% on interest, subject to exceptions; and
- 10% on royalties.

The protocol to the DTA states that the provisions of Article 7 (Business Profits) do not prevent each country from applying their own domestic tax provisions when determining the taxable income of a permanent establishment in their country. This is of some significance in Oman, where the domestic tax provisions are more restrictive concerning the head office costs that shall be treated as deductible for tax purposes.

Oman – Spain Income Tax Treaty
On 30 April 2014, the Governments of Oman and Spain signed a new DTA, in Muscat. The DTA was ratified by Oman on 19 August 2014 but has not yet been ratified by Spain and, as such, has not yet come into force.

2. Assessment of prior years' Income Tax Returns

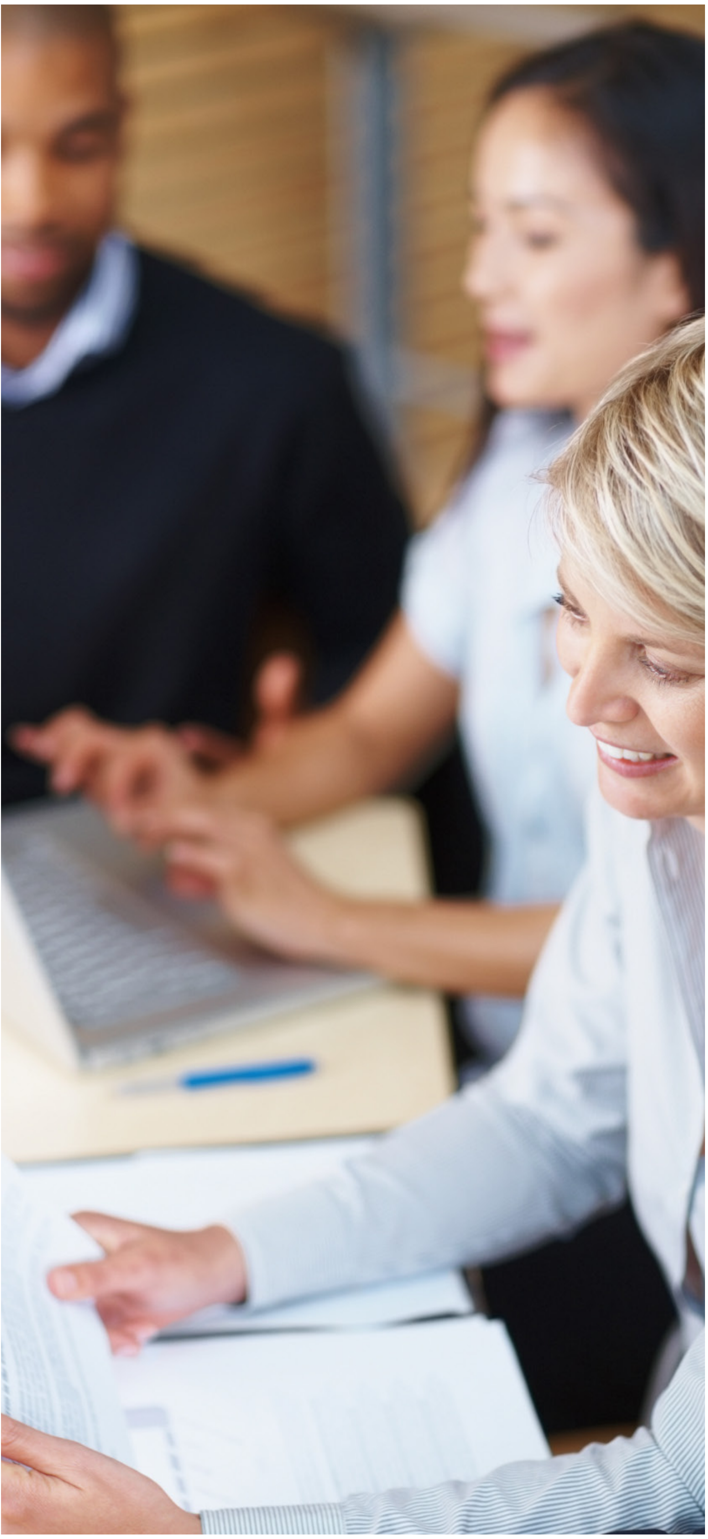
The Tax Department continues to pursue tax assessments aggressively, for open tax years, with the aim of clearing the back log in assessments and generating additional tax collections. The trend is likely to continue in 2015, particularly with the budget anticipating an increase in tax collections of 25%.

The Tax Department is scrutinizing related party transactions in greater detail, and the documentary evidence required to support such costs is increasing. Taxpayers need to pro-actively manage their assessments, and keep in close contact with the Tax Department. We often see unfavourable adjustments being made where full information is not provided, or is not provided on time.

The Tax Department now has a dedicated Large Taxpayer Unit, as well as a dedicated withholding tax team. Payments to foreign companies are being scrutinized closely, with particular focus on management fees and payments for the use or right to use computer software. This is another area where the Tax Department would expect to realise additional income tax collections in 2015.

3. EFTA-GCC Free Trade Agreement enters into force on 1 July 2014

Five years after its signing, the free trade agreement (FTA) between the EFTA States – Iceland, Liechtenstein, Norway and Switzerland – and the GCC became effective for all parties. Industrial and fish products will benefit from duty-free access to the markets of all parties, with some transitional periods and exceptions applying on the GCC side. Bilateral agreements between the GCC and individual EFTA States provide for preferential trading conditions for agricultural products and form part of the instruments establishing the free trade area.



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