

Oil and Gas Industry – Exploration, Discovery and Development

Social Service Tax Act

Are you involved in geophysical surveying?

Do you know if you qualify for machinery or equipment exemptions?

This bulletin provides specific tax information for those involved in the exploration, discovery, and development of oil and natural gas. It explains how the social service tax, also called the provincial sales tax (PST), applies to their businesses.

This bulletin focuses on exploration, discovery and development, which includes the initial extraction phase and the production testing phase. For purposes of the production machinery and equipment (PM&E) exemption, exploration stops when the completion process begins. The completion process readies a viable well for production.

For general PST information that applies to all businesses, such as who needs to register, when general exemptions apply, and how to charge and collect the PST, please read our [Small Business Guide to Provincial Sales Tax \(PST\)](#).

You will find specific tax information for other sectors of the oil and gas industry in the following bulletins:

Bulletin SST 055, *Oil and Gas Industry—Producers and Processors*

Bulletin SST 126, *Oil and Gas Industry—Service Providers and Contractors*

Table of Contents

Qualifying for the PM&E Exemption.....	2
Qualifying PM&E.....	3
Geophysical Surveying Exemptions	4
Parts for Exempt Machinery or Equipment	6
Claiming Exemptions	7
Change of Use.....	8
Taxable Goods	9
Goods Brought Into the Province for Temporary Use....	12
Taxable Services	14
Bundled Goods and Services.....	15
Other Exemptions	15
Improvements to Real Property	15

Qualifying for the PM&E Exemption

You may be eligible to purchase or lease production machinery and equipment tax-exempt if:

- you regularly engage, for commercial purposes, in the exploration, discovery or development of petroleum and natural gas deposits, and
- the machinery or equipment is used exclusively for such activities.

For information on the categories of production machinery and equipment that qualify for the exemption, see the section below, Qualifying PM&E.

Regularly means that you undertake the activity on a routine basis. This could be full-time, seasonally or on some other part-time basis.

Used exclusively means that the machinery or equipment is used over 90% in the exploration, discovery or development of petroleum and natural gas deposits.

You may measure exclusively in a number of different ways. It depends on the nature of the machinery or equipment. You may measure it in time, volume or some other measurement that is appropriate for that particular type of equipment.

In some cases, you may use the machinery or equipment seasonally or during specific phases in the exploration, discovery or development process. When this happens, the time when the machinery or equipment is idle or in storage is not considered use.

For example, a natural gas drilling rig may be operated only during the winter drilling season and is stored during the off-season period. The total use of that drilling rig will be based only on the time that it is actually being operated. During the actual drilling period, if that rig is used over 90% to drill for petroleum or natural gas, then the drilling rig qualifies for PST exemption.

Qualifying PM&E

If you are eligible, you may purchase or lease qualifying machinery or equipment tax-exempt, provided you use it exclusively in the exploration, discovery or development of petroleum and natural gas.

The following categories of machinery or equipment are exempt if all the conditions are met. Included within each category are examples of tax-exempt equipment.

- Petroleum and natural gas drilling rigs, such as:
 - derricks, substructures, support mats and foundations,
 - circulating systems (mud tanks, mud mixers, discharge and return lines, and separators) and pumps,
 - cementing equipment and engines or power plants that are part of a drilling rig, but not transport trucks, vehicles or the automotive units transporting the rig, and
 - mobile or fixed dog houses and “support buildings” used with drilling rigs as protective covering for items, such as electrical generators and blow-out preventor controls.

- The engines of pump trucks and truck-mounted well service drilling rigs qualify for the PM&E exemption if the engines are used over 90% for exploration, discovery and/or development activities. For example, if the engine is used less than 10% to transport the vehicle to a site and over 90% to drill, or pump mud or cement, then the engines are exempt.
- Truck-mounted well service rigs, including:
 - all parts and equipment integrated into the rig. For example, the drawworks is an integral piece of a service rig and is therefore exempt.
- Hardware used during the drilling process, such as:
 - drill bits (e.g. tricones or PDCs), drill collars, drill pipes, blowout preventors, casing, tubing, fittings, couplings and thread protectors, and
 - snubbing units, for example blowout stack preventors, hydraulic jacks, and the power units to run the hydraulics.
- Equipment used for well logging and drill stem testing, including instrumentation.
- Cementing and fracturing equipment, but not the vehicle or trailer on which the equipment is mounted.
- Machinery and equipment used during the production testing phase, such as:
 - separator vessels, dehydrators and heaters, pressure piping system and its components, flare stacks, pumps and motors.
- Generators located at the well head (includes mobile generators).

Well head means the actual well. It does not include the total area of the well site. The well head exemption applies to the machinery and equipment in and on the well. For example, valves, chokes, pressure gauges and similar items located at or adjacent to the well that make it possible to regulate well production are exempt. Pipelines are taxable as part of the transportation system.

Geophysical Surveying Exemptions

As petroleum or natural gas exploration and development are not site specific, the machinery and equipment exemptions for geophysical surveying are linked to the types of equipment used.

To receive this exemption, you must regularly engage in exploration for petroleum or natural gas, or the development of petroleum or natural gas deposits. You must use the machinery or equipment exclusively in those pursuits. For details on “regularly” and “exclusively”, see the section above, Qualifying for the PM&E Exemption.

Eligible equipment and machinery include the following items.

- Magnetometers, gradiometers and magnetic susceptibility meters.
- Instruments designed to measure the elements, variations and distortions of the natural gravitational force, including
 - gravity meters
- Field potentiometers, meggers, non-polarizing electrodes and electrical equipment for making measurements in drill holes.
- Equipment for electrical and electromagnetic surveying, including
 - self-potential meters
 - resistivity survey equipment
 - time and frequency domain induced polarization equipment and/or electromagnetic surveying equipment
 - inductive conductivity probes
- Ground penetrating radar equipment and side looking aperture radar.
- Equipment for remote sensing, including
 - ultraviolet lamps and reflectance spectrometers – infrared and hyperspectral
- Instruments and equipment for seismic prospecting, including
 - the recording system
 - seismic instrumentation
 - geophones
 - cables
 - data processing units
 - global positioning and navigation systems
 - recorder box, recorder power generators
 - blasting system

- blaster and controller
 - seismic drilling equipment
 - heli-drills
 - enviro-drills
 - vibrators
 - integrated navigation systems
- Scintillometers, spectral gamma-gamma density and geiger muller counters, gamma-ray spectrometers, potassium gradiometers and other instruments for radioactive methods of geophysical prospecting.
 - Acoustical survey equipment, including
 - sonar
 - side-scanning sonar
 - full wave form sonic loggers
 - Electrical and electronic amplifying devices and electrical thermostats designed to be used with any of the machinery or equipment described above.

Note: ATVs and snowmobiles are taxable even when used to transport personnel and equipment to surveying sites.

For further information on taxable and non-taxable items for geophysical surveying, please see our website www.sbr.gov.bc.ca/ctb/OilandGas.htm

Parts for Exempt Machinery or Equipment

Effective February 22, 2006, if you are eligible for the machinery and equipment exemptions, you do not pay PST on parts purchased or leased that you use to assemble qualifying machinery or equipment. This does not include materials used to make parts (see the section below, Materials Used to Make Parts).

Effective February 20, 2002, if you are eligible for the machinery and equipment exemptions, you do not pay PST on parts leased or purchased that you use on exempt machinery or equipment.

Between July 31, 2001 and February 20, 2002, only parts that by design would likely be used as replacement parts for industrial machinery and equipment were exempt. Generic parts were always taxable prior to February 20, 2002. There is no refund for tax paid parts held in inventory.

For information on what is not exempt as a part, see the section below, Taxable Goods.

Parts Inventory

If you have a parts inventory of mixed taxable and exempt items, you may make a reasonable estimate of the portion used on exempt machinery or equipment and purchase that portion without paying PST. Reconcile this estimate to your actual usage. If the reconciliation shows you used more parts for taxable purposes than estimated, you pay the PST owing on the parts you purchased exempt, but used for taxable purposes.

If you have a PST registration number, send in this additional amount with your regular tax return. If you do not have a PST registration number, you self-assess the PST due using the *Return of Tax Due on Taxable Tangible Personal Property by a Purchaser/Seller not Registered under the Social Service Tax Act* form (FIN 428).

Claiming Exemptions

You give the supplier a completed *Certificate of Exemption—Production Machinery and Equipment* form (FIN 453/M) when you purchase or lease:

- exempt production machinery or equipment, or
- parts or taxable services for exempt machinery or equipment.

This requirement applies whether you are registered or not registered as a vendor. There is an option of using an alternative approved certification (see below in this section.)

You complete all parts of the certificate. Where a description of the items purchased or leased is required, you list each type of machinery or equipment. It is not enough to simply state “production machinery and equipment”.

For example, if you are purchasing drill bits, regulators or coiled tubing, you list each as a specific item on the form. If you are purchasing parts for eligible machinery, include what piece of exempt equipment the part is attached to. For example, state “filters or seals used on a circulating system” on the certificate not only “filters or seals”.

When you purchase or lease a large quantity of machinery or equipment, you may attach an itemized list or a copy of the sales invoice to the completed certificate. The invoice must clearly describe the machinery or equipment being purchased or leased and it must indicate which is exempt.

When you are making purchases or leases (rentals) frequently from the same supplier, you may provide one completed certificate to your supplier along with a list of items that you are claiming an exemption for. You can make future exempt purchases/leases of the same items from that supplier based on this same certificate.

You use the *Certificate of Exemption—Production Machinery and Equipment* form (FIN 453/M) only for claiming exemption on production machinery, equipment, and related parts and taxable services. It does not replace the *Certificate of Exemption* (FIN 453) used to purchase goods for resale, etc.

As an alternative to using the *Certificate of Exemption—Production Machinery and Equipment* form (FIN 453/M), you may claim an exemption by stamping or printing a certification on the purchase order.

The purchase order must clearly indicate the purchaser/lessee's name, address, registration number where applicable, and the goods or services being acquired. Stamp or pre-print on the form a certification using the following wording:

Production Machinery and Equipment Exemption:

We certify that the goods and services purchased are eligible for exemption from social service tax under Section 76(1)(k) of the *Social Service Tax Act*, Division 13 of the regulations to the Act.

You may also write to us with suggested alternative wording. We must approve the suggested wording before you use it.

Change of Use

If you purchase an item exempt and later use that item for a taxable purpose, PST applies from the moment the use changes. You calculate and self-assess PST on the greater of the depreciated value or 50% of the original purchase price.

For information on depreciation rates, please see our website at www.sbr.gov.bc.ca/ctb/DepreciationRates.htm

Taxable Goods

Unless exempt, your purchase of machinery, equipment or other goods purchased in the province are taxable. You pay PST on the full purchase price at the time of purchase. If the items are leased, you pay PST on each lease payment either when the lease payment is paid or when the lease payment becomes due under the terms of the lease agreement, whichever is earlier.

Interest charges under a conditional sale contract are not subject to tax if:

- the interest charges are separately stated on the invoice or bill of sale, or billed to the purchaser, and
- the interest charges are payable over the term of the contract.

What is Included in the Purchase Price

When you purchase goods within British Columbia, the purchase price includes charges for transportation and installation, interest, finance, service, customs, and excise when these charges happen at or before the time that the title passes to the purchaser. Include fuel surcharges for delivery but do not include the goods and services tax (GST). The charges remain part of the purchase price even if the charges are separated on either the invoice or on the seller's books.

If the charges occur after the purchaser receives title to the goods, they are not taxable when the charges are separately listed on the invoice. They do not form part of the original purchase price.

For information on goods purchased from out-of-province, see the section below, Purchases from Out-of-Province Suppliers.

Goods for Own Use

You pay PST on the purchase or lease of new or used goods that you use in your business, such as:

- stationery, furniture and office equipment,
- computer hardware and software (unless custom software), and
- cleaning cloths, paper towels and cleaning supplies.

If the supplier does not charge you PST on the above items, you self-assess and record the PST due at Step 3 of your next tax return.

If you take items from your resale inventory for business or personal use, you self-assess PST on your cost of the items.

If you have a PST registration number, you send in the tax due on your next tax return. If you do not have a PST registration number, you self-assess the PST due using the *Return of Tax Due on Taxable Tangible Personal Property by a Purchaser/Seller not Registered under the Social Service Tax Act* form ([FIN 428](#)).

Materials Used to Make Parts

Materials you use to make parts are not exempt from PST as parts. If you need to modify materials before you are able to use them, **they are not** parts; they are taxable materials, therefore you pay PST on them.

A part is a pre-manufactured good designed to replace an integral piece of machinery or equipment that no longer functions and that needs only minimal adjustments for installation.

An example of minimal adjustment is when a specified, predetermined cut length of belting needs lacing or adhesive agents, but not fitting (e.g. trimming) or processing before installation. It then qualifies as a part, not as material used to make parts.

Where any modification or manufacturing before use occurs, you are using materials, not exempt parts.

Consumables

Industry often calls consumables, “supplies”. A good consumed or used up in the operation or maintenance of machinery or equipment is a consumable, even if it is necessary for that item’s operation or maintenance.

The following are some examples of consumables.

- Hydraulic fluid in a cylinder is a consumable as it is not attached to or part of the cylinder. The hydraulic fluid retains its separate identity.
- Consumables may be materials or substances actually used or consumed in the process of servicing test wells. An example is KCL fluid added to drilling mud to control pressure.
- Diesel or gasoline not used in an internal combustion engine. Examples are gasoline used as a cleaning agent or diesel used as a lubricant.
- Oxygen or acetylene gas and pipe dope.
- Additives for raw petroleum or natural gas.

Consumables are taxable unless they qualify for another exemption under the Act. Two examples of exempt consumables are water, which is exempt to everyone, or an additive to raw petroleum or natural gas that is a catalyst or direct agent.

For detailed lists of taxable and non-taxable items for the oil and gas industry, please see our website at www.sbr.gov.bc.ca/ctb/OilandGas.htm

Examples of Taxable Goods

The following are taxable machinery, equipment or goods used in the exploration, discovery, and development of petroleum and natural gas:

- vehicles designed for public highway use, such as transport trucks or other vehicles or units on which well servicing equipment (e.g. mobile welders) or cementing and fracturing equipment is mounted, but not a truck-mounted well service rig,
- pipes, valves, fittings, pumps, compressors, regulators and equipment ancillary to any machinery and equipment that is used in transporting or distributing petroleum or natural gas from the well head to the processing plant or refinery or between processing plants, or is used in transporting a marketable product,
- furnishings, camp equipment, machinery or equipment related to the use of a building, and machinery and equipment used in construction,
- materials used or consumed in the drilling process, such as oil, lubricants, drilling mud, fracturing or stimulating fluids, and
- general and administrative equipment and supplies, for example, cell phones, pagers and computers.

For additional examples of taxable and non-taxable items used in the oil and gas industry, please see our website www.rev.gov.bc.ca/ctb/OilandGas.htm

Purchases from Out-of-Province Suppliers

If you purchase or lease taxable goods from an out-of-province supplier, you pay PST on the total amount that you pay to bring the goods into British Columbia, including charges for transportation, customs, excise, and any other costs. You do not include GST, or other provinces' or countries' retail sales tax.

If you have a PST registration number and the supplier does not charge you PST, you self-assess and record the PST due at Step 3 of your next tax return.

If you do not have a PST registration number and the supplier does not charge PST at the time of the sale, you self-assess the PST due using the *Return of Tax Due on Taxable Tangible Personal Property by a Purchaser/Seller not Registered under the Social Service Tax Act* form ([FIN 428](#)). Do this at the time you bring or ship the goods into British Columbia.

For more information, please see [Bulletin SST 043](#), *Goods Purchased from Out-of-Province Suppliers*.

Lease with Operator

Agreements where the person supplying the equipment also supplies a person to operate the equipment are not leases under the Act.

A lease with operator is a non-taxable service. Therefore, billings for such agreements are not taxable. However, the owner of the equipment pays PST on the purchase price of the equipment. PST does apply to equipment leased (rented) without an operator.

Goods Brought Into the Province for Temporary Use

Exempt Goods

If you are eligible for the machinery or equipment exemption, you do not pay PST on qualifying machinery and equipment when it is brought into British Columbia for temporary use in the province.

For example, if you are eligible for the exemption and you rent surface equipment—such as an electronic drilling recorder, a pit volume totalizer and submersible trash pump units—you do not pay PST on the lease (rental) as these items are exempt.

You provide a completed and signed ([FIN 453/M](#)) form to the person you rent from.

Other Goods

You pay tax on goods that do not qualify for exemption or for payment of tax on a $1/36^{\text{th}}$ or $1/3^{\text{rd}}$ formula basis (described below). The tax is due at the time you bring the property into the province for use.

For machinery and equipment that does not qualify for the exemption, you pay on the $1/3^{\text{rd}}$ formula or in limited cases, on the $1/36^{\text{th}}$ formula. The taxable value includes any manufacturing, labour, service, customs and excise, transportation or other costs incurred before use of the property in British Columbia.

Temporary Use Formulas

There are two formulas for calculating PST on temporary use: the $1/36^{\text{th}}$ and the $1/3^{\text{rd}}$ formula.

In certain cases, the equipment may be taxable under either formula. You may pay tax using the formula that produces the lesser amount.

1/36th formula

Only the following goods used for petroleum or natural gas exploration or development qualify for the 1/36th formula:

- cementing trucks,
- acid fracturing trucks, including pressure fracturing trucks that produce the same petroleum or gas flow stimulation as acid fracturing trucks, or
- vehicles with permanently mounted seismic recording or well logging equipment.

First entries into the province

If you are eligible to use the 1/36th formula, you determine the equipment's value as follows.

- New equipment purchased outside of British Columbia for temporary use in the province is taxed on 1/36th of the purchase price of the equipment. Tax is payable at the time of first entry into the province. You pay the tax for each month, or portion of a month, that the equipment is in the province.
- Equipment previously used outside the province and brought into British Columbia for temporary use is taxed on 1/36th of the depreciated value to a maximum of 50% of the purchase price. Tax is payable at the time of first entry into the province.

Your purchase price in both cases includes transportation, service, customs, excise, and any other charges you pay prior to use of the good in this province.

Subsequent entries and capital improvements

For all subsequent re-entries of the same equipment into British Columbia, you pay PST on 1/36th of the value established at the first entry of that good into the province. After 36 payments on that equipment, no further PST is due on it.

Capital additions and major repairs

Capital additions or capitalized major repairs made to tax-paid equipment are taxable.

Calculate PST on the first entry value, at the time of first entry. You do not include transportation costs on capital additions or major repairs as these costs were included as part of the purchase price at the time of first entry. There is no subsequent tax on transportation costs.

Repair or storage of equipment under the 1/36th formula

You do not pay PST on equipment that enters British Columbia for repair and storage only, and then is removed from the province.

Once use occurs in British Columbia, the equipment is taxable. You pay PST based on the total time the equipment is in the province.

Repair parts for equipment qualifying for the 1/36th formula

You pay PST on repair parts used to service equipment used in British Columbia. You do not pay PST on repair parts for equipment used only outside of British Columbia.

Equipment qualifying for 1/3rd formula

Machinery and equipment brought into the province for temporary use that does not qualify for exemption as production machinery and equipment, or for payment of tax on the 1/36th formula, may be eligible for payment of tax on the 1/3rd formula. This includes vehicles, trailers, well servicing, road building and construction equipment.

You cannot use the 1/3rd formula to calculate tax on parts that you bring into the province. You pay PST on the total amount that you paid to bring the goods into British Columbia, including any charges for transportation, customs, excise and any other costs, except GST.

For more information, please see [Bulletin SST 098](#), *Equipment Brought Into the Province for Temporary Use (1/3 Formula)*.

Taxable Services

Generally, you pay PST for services you receive that are related to your goods. This includes services to install, assemble, construct, dismantle, repair, adjust, restore, recondition, refinish or maintain. However, if you are eligible for the PM&E exemption, you do not pay PST on services to exempt production machinery and equipment that you purchased or leased.

For details on how to claim your exemption, see the section above, Claiming Exemptions.

Consulting services do not meet the definition of a taxable service. Therefore, no taxes apply. For example, an oilfield drilling company that sends out a consultant/supervisor to supervise, but provides no hands-on service to a drilling rig, is providing a non-taxable consulting service.

Geophysical surveying services are also not taxable. However, if the company providing the services sells seismic data in a hard copy format to a third party, PST applies to this hard copy data sale. A sale of goods occurred, therefore PST applies. If the data is sold only in an electronic version, no PST applies as no tangible goods were sold.

For more information, please see [Bulletin SST 018](#), *Taxable Services*.

Bundled Goods and Services

When a non-taxable good or service is bundled together with a taxable good or service and sold for a single price, you charge PST only on the fair market value of the taxable good or service. However, there are some exceptions if the price is \$500 or less. For details, please see [Bulletin SST 119](#), *Bundled Sales: Taxable and Non-taxable Goods or Services Sold Together for a Single Price*.

Other Exemptions

Work-Related Safety Items

You do not pay PST on work-related safety equipment designed to be worn by a worker. For example, self-contained breathing apparatus (SCBAs), hard hats and other protective clothing are exempt. There are also safety items that are exempt to everyone, such as portable fire extinguishers and refills, or gas detection monitors.

For more information, please see [Bulletin SST 002](#), *Exemption for Safety Equipment*.

Improvements to Real Property

Real property is land and any items permanently attached to land (buildings and structures). The way you structure a contract determines whether the contractor pays PST, or you pay PST on the goods that become improvements to real property on installation.

You do not pay PST on sales and leases of real property, or on services to real property. For example, you do not pay PST on the construction of a lease road associated with drilling a well. Maintenance services, such as grading are also not taxable. The labour is not taxable although the materials used are taxable. Gravel or culverts are examples of taxable materials.

For more information, please see [Bulletin SST 072](#), *Real Property Contractors*.

Need more info?

Oil and Gas website: www.sbr.gov.bc.ca/ctb/OilandGas.htm

Telephone (Vancouver): 604 660-4524

Toll-free in Canada: 1 877 388-4440

E-mail: CTBTaxQuestions@gov.bc.ca

The information in this bulletin is for your convenience and guidance and is not a replacement for the legislation. The *Social Service Tax Act* and Regulations are on our website at www.sbr.gov.bc.ca/ctb

Acknowledgments

This bulletin has been prepared in consultation with industry representatives. We wish to acknowledge and thank the *Canadian Association of Geophysical Contractors*, *Canadian Association of Oilwell Drilling Contractors*, *Canadian Association of Petroleum Producers*, *Northern Society of Oilfield Contractors and Service Firms* and the *Petroleum Services Association of Canada* for their input. By working with us, they help us better serve their members and work towards making British Columbia the best place to do business.

References: *Social Service Tax Act*, Sections 1, 5, 6, 9, 11, 12, 20(1)(a), 24, 76(1)(k), 76(5) and 77(c), and Regulations 2.10, 2.38, 2.39, 2.46(e), 3.29, 13.1, 13.4, 13.5, 13.10, 13.10.2(1), 13.10.2(2), 13.11, 13.12, 13.13 and 13.14