DEPARTMENT CIRCULAR DC NO. ________

GRANT OF SPECIAL ALLOWANCES FOR PETROLEUM SERVICE CONTRACTORS

WHEREAS, Section 2, Article XII of the 1987 Constitution provides that *"xxx The exploration, development, and utilization of natural resources shall be under the full control and supervision of the State"* and *"(t)he President may enter into agreements with foreign-owned corporations involving either technical or financial assistance for large-scale exploration, development, and utilization of minerals, petroleum, and other mineral oils according to the general terms and conditions provided by law, based on real contributions to the economic growth and general welfare of the country. In such agreements, the State shall promote the development and use of local scientific and technical resources;"*

WHEREAS, Republic Act (RA) No. 7638, as amended, otherwise known as *"The Department* of *Energy (DOE) Act of* 1992", mandates the DOE to prepare, integrate, coordinate, supervise, and control all plans, programs, projects, and activities of the Government relative to energy exploration, development, utilization, distribution, and conservation;

WHEREAS, Section 5(f) of RA No 7638, as amended by Section 37(k) of RA 9136, otherwise known as the *"Electric Power Industry Reform Act of 2001 (EPIRA),"* further mandates the DOE to *"assess the requirements of, determine priorities for, provide direction to, and disseminate information resulting from energy research and development programs for the optimal development of various forms of energy production and utilization technologies;"*

WHEREAS, Section 2, Presidential Decree (PD) No. 87, as amended, otherwise known as the *"Oil Exploration and Development Act of 1972,"* declared it to be the policy of the State *"to hasten the discovery and production of indigenous petroleum through the utilization of government and/or private resources, local and foreign, under the arrangements embodied in this Act xxx"* and provides in Section 4 thereof that *"the Government may directly explore for and produce indigenous petroleum. It may also indirectly undertake the same under service contracts as hereinafter provided."*

WHEREAS, Section 18 (b) of PD 87 provides, as among the functions of the Petroleum Board (now the DOE), to "*(e)nter into contracts herein authorized with such terms and conditions as may be appropriate under the circumstances including the grant of special allowance: Provided, however, That no depletion allowance shall be granted: xxx"*

WHEREAS, PD No. 1459 authorized the Secretary of Energy to enter into and conclude service contracts, or re-negotiate and modify existing contracts, subject to the following limitations, thus: "*(a) (t)he share of the Government, including all taxes, shall not be less than sixty percent of the difference between the gross income and the sum of operating expenses and such allowances as the Secretary of Energy may deem proper to grant; (b) (t)he service contractor must be technically competent and financially capable to undertake the petroleum operations required in the contract,* *and (c) (t)he Secretary of Finance shall be consulted on all matters involving revenue."*

WHEREAS, the DOE is continuously adopting new mechanisms and strategies to effectively carry out its plans and programs as mandated under PD 87, as amended, including its implementing rules and regulations;

WHEREAS, the current state of the oil and gas exploration in the country shows low-level investments due to the attendant high risk in petroleum operations;

WHEREAS, there is a need to offer improved fiscal terms to service contractors to complement the other Government initiatives in attracting more exploration and production companies to spur exploration activities leading to the discovery of more oil and gas fields in the country;

WHEREAS, providing special allowances that allow for maximum benefits to the country and at the same time provide reasonable returns to private companies that render financial and technical services and assume all the risk of petroleum exploration will make the Philippine service contract regime more attractive to investments and will improve the state of the oil and gas exploration in the country;

WHEREAS, the grant of special allowance will induce the inflow of foreign investment capital that would have a significant potential contribution to the country's balance of payment;

WHEREAS, there is a need to attract more investments to accelerate the exploration, development, and utilization of indigenous petroleum resources in order to attain the goals embodied in the Philippine Development Plan (PDP) and Philippine Energy Plan (PEP) - to contribute to the country's energy security, create jobs, and generate wealth;

NOW, THEREFORE, in consideration of the foregoing premises, the following policies and guidelines are hereby adopted and promulgated:

Section 1. Policy on the Grant of Special Allowances. Petroleum service contractors shall be entitled to the special allowances granted under this Circular, which shall be applied by deducting the applicable special allowance/s from the gross proceeds. *Provided* further, that in no case shall the share of the Government be less than sixty percent (60%) of the difference between the gross income and the sum of operating expense, the Filipino participation incentive under Section 28 of PD 87, if applicable, and the special allowance/s granted herein. *Provided* finally, the reimbursement of all operating expenses shall not exceed seventy percent (70%) of the gross proceeds from production in any year.

Section 2. Special Allowance on Cost Recovery. To spur exploration activities and encourage producing service contractors to invest in other exploration service contracts, a special allowance for the cost recovery of exploration expenses from an exploration contract from its existing service contract with production is hereby granted, subject to the following:

2.1 The producing service contract has not fully utilized the seventy percent (70%) allowable reimbursement of all operating expenses from production in any year. The balance of which shall be deemed to be the special allowance granted under this section;

2.2 The special allowance on cost recovery shall be computed proportionately to the service contractor's participating interest in the producing service contract; and,

2.3 If the exploration service contract converts to production, the operating expenses recovered under this special allowance shall no longer be recovered from the converted exploration service contract.

Section 3. Special Allowance on Marginal Petroleum Operations. To enable petroleum service contractors to maintain or continue operations in marginal petroleum fields and when the annual operating expenses exceed the cost recovery allowance of seventy percent (70%), a special allowance shall be granted as follows:

Percent of Operating Expenses vs. Gross Proceeds	Percentage of Gross Proceeds as Special Allowance
Below 70%	0%
More than 70% - but less than 75%	6%
75% - but less than 80%	9%
80% - and above	12%

Section 4. Special Allowance on New Plays. To encourage the discovery of new petroleum sources in untested geologic plays in productive basins, a special allowance of Seven and One Half percent (7.5%) of the Gross Proceeds is hereby granted. This special allowance shall be granted only to the first commercial development of such new geologic play in the basin.

Section 5. Special Allowance for Gas Development in Remote or Frontier Areas. To encourage the development of new gas fields discovered in a remote or frontier area with more than 200km from the identified delivery market, a special allowance shall be granted as follows:

Distance to Market Delivery Point	Percentage of Gross Proceeds as Special Allowance
Less than 200km	0.0%

200km but less than 400km	2.5%
400km but less than 800km	5.0%
800km and above	10.0%

This special allowance shall be granted only to first or foundational development in the remote or frontier area.

Section 6. Special Allowance on Gas Production in Remote or Frontier Areas. To encourage the development of facilities and the production of indigenous natural gas in remote or frontier areas, a special allowance of Thirty percent (30%) of the Gross Proceeds less any FPIA, cost recovery, and other special allowances, is hereby granted. This special allowance shall be granted only to the first or foundational project in the remote or frontier area.

Section 7. Separability Clause. If, for any reason, any provision of this Circular is declared unconstitutional or invalid, such part or parts not affected shall remain in full force and effect.

Section 8. Repealing Clause. All circulars, orders, letters of instructions or issuances contrary to, or inconsistent with this Circular are hereby repealed, modified or amended accordingly.

Section 9. Effectivity. This Circular shall take into effect immediately upon its publication in at least two (2) newspapers of general circulation. Copies of this Circular shall be filed with the University of the Philippines Law Center – Office of National *Administrative Register.*

Issued this ____________________ 2024 at the Energy Center, Rizal Drive, Bonifacio Global City, Taguig City.

RAPHAEL P. M. LOTILLA
Secretary