**TOR**

**Terms of Reference for Financial Settlement**

**Background:**

According to the Amu Darya Basin EPSC contract, when the contract expires or is terminated, financial settlement is required to finalize all related legal, financial, and accounting matters. This TOR provides a principled, technical, and documented framework for the full, transparent, and legal implementation of financial settlement, so that the rights and responsibilities of both parties (the Ministry and the contractor) are clarified and guaranteed.

**Objectives:**

* Settlement of all financial accounts upon termination of the contract.
* Determination and settlement of government rights (Royalty, Tax, Fees) according to the contract.
* Recoverable Costs and settlement of remaining rights of the government company according to the contract.
* Calculation and agreement of the government's environmental remediation costs according to the contract.
* Preparation of a formal and final financial agreement (Final Settlement Agreement) between both parties.

**Legal and contractual basis:**

|  |  |
| --- | --- |
| Source | Detail |
| Amu Darya Basin EPSC contract | acts 7.1(m), 10.1(b), 13, 14, 16, 25.6 |
| Hydrocarbon Law (2009) | Principles of taxes, royalties, fees |
| Afghanistan Tax law (2009) | Revenue and Customs Duties Principles |
| International standards | IFRS، ISO 55000، EITI، WB Guidelines |

**Principles of Financial Settlement**

|  |  |
| --- | --- |
| **Original** | **Detail** |
| Transparency | Transparency of all documents, reports, and accounts. |
| Accountability | Documenting all monies spent and revenues received by the contracting company. |
| Legal notice | Compliance with Afghanistan's tax, royalty, and fee laws. |
| Confirmation of both parties | The financial settlement documents will be effective upon agreement by both parties. |

**Types of Financial Settlement:**

Outstanding accounts under the contract:

* Ministry's share in Royalty as per Article 10.1(b) of the Contract.
* Taxes, According to Article 16 of the contract and the Tax Law.
* Surface Rental Fees: According to Article 14 of the Contract
* Custom Duties: According to Article 17
* Other fees such as Administrative Fees, Training Fees, Social Obligations

**Settlement of expenses of the contracting company: (Cost Recovery):**

* Operating expenses for exploration, development and production.
* Capital expenditure (Capex).
* Account for unclaimed or unspent funds of the contracting company.
* Reform and environmental cleanup costs

**Cost Recovery of the Contractor Company:**

* Operating expenses including exploration, development, production.
* Capital expenditure (Capex).
* Account for unclaimed or unspent funds of the contracting company.
* Reform and environmental cleanup costs

**Settlement of environmental costs:**

* Site cleanup and restoration costs (Decommissioning, Abandonment).
* Compensation for Environmental Damages.

**Financial Settlement Process:**

Documentation & Review

* Receive all expenses, income, and reports
* Analysis of achievements and obligations according to the contract materials
* Bank documents, payment documents, customs documents, tax certificates.

**Account Reconciliation:**

* All income received and paid by the company should be assessed.
* Implementation and settlement of government rights (Taxes, Royalty, Fees).
* Approval of company expenses.
* Rejection of non-recoverable costs.

**Environmental Cost Review:**

* Documentation of improvement plans.
* Verification and settlement of rectification costs.
* Environmental damage compensation analysis.

**Preparation of the Final Financial Report:**

* Detailed report of all settled accounts.
* Government revenue.
* Company receivables.
* Details of outstanding expenses and liabilities

**Final Settlement Agreement:**

* Signature by both parties.
* Approval from the bank, tax authorities, and relevant government bodies.

**Financial Settlement Team:**

|  |  |
| --- | --- |
| **Roll** | **Responsibility** |
| Finance Specialist of the Ministry | Calculation and implementation of government rights |
| Financial specialist of the contracting company | Company expenses and staff salaries |
| Legal adviser  | Legal verification and analysis |
| Environment specialist | Environmental Cost Analysis |
| Auditor | Adjustment and settlement of accounts |

 **(Deliverables):**

|  |  |
| --- | --- |
| **documents** | **goals** |
| financial final reports  | Settlement of all accounts |
| Government and company agreement | Proof of official settlement |
| Environmental expenditure report | Documentary report of reforms and damages |
| Tax certificates  | Tax liability settlement |

**(Timeline):**

|  |  |
| --- | --- |
| **Operation** | **Duration** |
| Collection of documents | 20 days |
| Evaluation of accounts | 30 days |
| Environmental cost analysis | 15 days |
| Final report  | 10 days |
| Agreement signed | 5 days |

**(Outcome):**

1. All financial accounts are settled transparently upon termination of the contract.
2. Government rights (taxes, fees, royalties) should be received.
3. company's rights (unclaimed funds) should be settled.
4. There must be a formal agreement between both parties.
5. costs of environmental improvements should be clear and transparent.

**Steps required for financial settlement on Cash Bases Accounting:**

1. **Audit and verification of all cash accounts**
* Preparation of an accurate list of all cash receipts and expenditures.
* Collection of supporting documents (receipts, bank statements, payments order) of each expense and income.
* Recording of date, amount, purpose, and its account relation
1. **Outstanding settlements:**
* Only expenses paid in cash will be counted
* If any contract or promised money has not been paid, it will not be counted.
* Record the date, amount, purpose, and relationship with each account.
1. **Analysis and settlement of the Ministry's (Royalty, Taxes, Fees):**
* Only fees, taxes, and royalties paid in cash will be available.
* All payment receipts of Ministry must be collected and verified.
1. **Company Recoverable Costs:**
* Costs will be calculated that are paid in cash and are recoverable according to the contract.
* Compliance with the contract “R Factor Expenditure Account “recoverable cost must be verified
1. **Environmental Cost Analysis:**
* Only repairs and cleaned costs that have actually been paid for, will be counted
* Only accurate and real expenses will be counted as actual payments.
1. **Preparation of financial report and accounts:**
* Final financial report that covers all cash flow receives and paid records
* Documentation of all stages of the settlement
* Certification from both parties (Ministry and Company)
1. **Payments with Compliance to legal principles:**
* All payments must be made in US dollars (USD).
1. **Rights to Audit accounts:**
* The Ministry has the right to inspect all cash documents, receipts, and contracts.
* According to exhibit C, article III of contract, Ministry has the right to audit and inspect
1. **As a result:**
* In cash basis accounting, only the money that has been exchanged is counted for financial settlement.

**For the financial settlement it is necessary to:**

1. Collect all cash documents
2. All contracts, which cash payments has not been made, shall be set aside
3. There should be a transparent understanding between the Ministry and contracted company
4. **General Principles of Cash Basis Accounting:**

Cash Basis Accounting records only those expenses and revenues that are paid or received in cash.

However, whether these expenses are considered expenses or assets depends on the specific principles of the contract and the hydrocarbon sector.

1. **EPSC Contract and Asset Registration Principle:**

In the Amu Darya EPSC contract, the exploration, development, and production phase costs and assets are categorized as follows:

1. **Recoverable Expenses:**
* Expenses incurred by the company and permitted by the Ministry to recover them under the contract.
* Expenses are including:
* Expenses for research, survey, and drilling (Exploration & Drilling).
* **Administrative and operational expenses**
* **Environmental protection expense**
1. **Capital Assets:**
* Equipment’s, tools and machinery that have been purchased for long term operation:
* The assets which are not owned by the company, but are purchased for the government and used for production.
* Based on the contract, the recoverable assets, which the company can recover the cost of its investment.

Such as Drilling rigs

1. **If the company purchase a drilling rig:**

|  |  |
| --- | --- |
| **Standard** | **Detail** |
| **Type of property** | **Fixed asset or long term assets** |
| **In account** |  **as a Capital Expenditure**  |
| **Cash Basis**  | **The cash payment will be recorded on the date of payment, but the nature of the asset is capital** |
| **In contract** | **The asset will be recoverable cost base on contract, the company can recover its cost from production** |
| **During financial settlement** | **It will be part of the inventory assets and transferred to the ownership of the Ministry** |

## ****Summary:****

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| --- | --- | --- | --- |
| **type** | **Examples** | **Place in account** | **Status before the contract** |
| **Expense** | Administrative expenses, salaries, daily services | Cost of the year | Recoverable |
| **Asset** | Drilling rigs , machinery and other facilities | Investment record on cash bases | Recoverable and transferable assets |

## ****Important points:****

## Cash bases accounting means, that cash transactions are recorded, but this does not mean that all expenses well be considered as an expense.

## Based on the contract assets and expenses would be separated.

1. Assets purchased for long-term use (such as drilling rigs, machinery) are considered capital, have a recoverable cost, and are part of the asset list during financial settlement.
2. During the processes, these assets will be transferred to the Ministry and the contractor will have the right to recover its costs.

## Result:

* Drilling rigs and other similar equipment are not considered consumables, but rather assets.
* These assets are recoverable according to the contract, meaning the company will get the money back.
* Cash Basis will be recorded only at the time of cash payment, but will be calculated and transferred to capital during accounting and settlement.

## ✅1****. Contractor Subcontractor:****

When a main contractor offers its operations (such as drilling, surveying, logistics, construction work), to subcontractor

these contracts are generally as follows:

|  |  |
| --- | --- |
| **operations** | **details** |
|  **(Pure Services)** | the subsidiary company only provides the service (drilling, surveying), owns the equipment, and then takes it back |
|  **(Services with Equipment)** | The subsidiary not only provides the service, but also uses its own equipment (such as drilling rigs, machinery, vehicles) to provide this service. |

## ✅2. ****(EPSC) contract from the prospective view of property:****

 If the equipment is owned by a subsidiary and has provided only service to the parent company:

* Only the service will be considered a recoverable expense of the original company under the contract.
* The tools and equipment used by the subsidiary do not become the property of the ministry.
* It means that The ministry only pays for the service, not the ownership of the equipment.

### ****Important principle of contract:****

"Assets which are purchased directly by the Contractor for use in Petroleum Operations and whose cost is recoverable, shall be transferred to the Ministry upon contract termination, Based on the contract.

* The target here is the equipment purchased by the parent company, not those brought in by the subsidiary.
* That is, if the equipment is not owned by the original company and is only part of the service, it is not transferred to the ministry.

## ✅ ****3. (International Best Practices):****

|  |  |  |  |
| --- | --- | --- | --- |
| **condition** | **Condition of vehicles** | **Operation condition** | **Ministry property** |
|  (Service Only) | Subcontractor property | Only service | No, it will not be transferred to the ministry |
|  (Service + Purchased Equipment) | If the equipment is purchased by the main company | Service and equipment both | yes, it will be transferred to the ministry |
|  (Service with Contractor-Owned Equipment) | Equipment owned by subcontractor | service | No, only service counts |

## ✅ ****4. Detail of properties and functions based on the EPSC****

**Recoverable Costs:**

* the costs (such as drilling services) that the ministry will reimburse.

**Transferred Assets:**

* the assets (equipment, facilities) that the original company purchased and that become the property of the ministry according to the contract.
* if the equipment was not purchased by the parent company, but was used in services by a subsidiary, it does not become the property of the ministry.

✅ 5. **The Ministry's position during financial settlement:**

1. Only those assets (equipment, equipment, facilities) that the parent company has purchased are owned by the ministry.
2. Service contracts (such as drilling, surveying) if the subsidiary's equipment is used, only the service is counted, the equipment is not transferred.
3. The Ministry should request a complete list of purchased equipment from the original company.
4. The Subcontractor equipment must be separated from services.

## ✅6****. Result and example:****

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| --- | --- |
| **condition** | **result** |
| The subcontractor has drilled; its equipment is its own. | Only services, equipment not transferred to the ministry |
| The parent company purchased the equipment (not from the subsidiary, but for its own project). | yes, the equipment is being transferred to the ministry. |
| The subcontractor provided the equipment, bought the parent company and became part of the operation. | yes, the equipment is being transferred to the ministry as per the contract. |

## ✅7****. summary:****

* Equipment used by the subsidiary solely for services is not considered the property of the Ministry.
* Only assets that the parent company has purchased and used for operations are transferred to the ministry.
* Services are considered separate, assets are considered separate
* distinction should be made clear during financial settlement.