A NEW RESOURCE TAXATION REGIME

Improved resource tax arrangements

Following extensive consultation with the industry the Australian Government has announced improved resource taxation arrangements to apply from 1 July 2012. Under the new framework:

• a Minerals Resource Rent Tax (MRRT) regime will apply to the mining of iron ore and coal in Australia; and

• the Petroleum Resource Rent Tax (PRRT) regime will be extended to all Australian onshore and offshore oil and gas projects, including the North West Shelf. This will provide certainty for oil and gas projects and ensure all oil and gas projects are treated equitably.

The new resource tax arrangements focus on our biggest and most profitable commodities: iron ore, coal, oil and gas. These represent nearly two-thirds of the value of our exports and resource operating profits and account for an even greater share of resource rents in the mining industry.

The framework will also provide certainty for some of the emerging projects being considered, such as converting Coal Seam Gas to Liquefied Natural Gas, by including all Australian onshore and offshore oil and gas projects in the PRRT. Including these major prospective projects within the existing PRRT framework will increase investor certainty in the short term. Including all oil and gas projects in the one regime will also ensure equitable tax treatment between competing projects.

To ensure the smooth implementation of the new arrangements the Government established a Policy Transition Group (PTG), led by the Minister for Resources and Energy, the Hon Martin Ferguson and Mr Don Argus, to develop the detailed technical design of the new resource tax arrangements.

The PTG provided a report on the implementation of the new MRRT and PRRT arrangements to Government in December 2010. The report made 94 recommendations on the technical design of the new resource tax arrangements.

On 24 March 2011 the Government announced its acceptance of all the recommendations of the PTG regarding the new resource taxation reforms. The PTG recommendations form the basis of the design of the MRRT draft legislation that was released for consultation on 10 June 2011. The closing date for submissions on the MRRT draft legislation is 14 July 2011. The Government will release draft PRRT legislation for consultation in the near future.

The Government also recognised the important contribution made by the PTG and has continued the engagement with industry through establishing a Resource Tax Implementation Group to support the legislative drafting stage, consistent with the PTG recommendations.

The Resource Tax Implementation Group comprises representatives of industry, the tax profession and government officials and is ensuring close consultation with the resource sector continues as legislation is developed. Legislation implementing the new resource taxation arrangements is expected to be introduced into Parliament in the second half of 2011.

The new Minerals Resource Rent Tax (MRRT) for iron ore and coal

The new MRRT will commence on 1 July 2012 and apply to all new and existing iron ore and coal projects.

The key features of the MRRT are:

• Taxpayers with small amounts of MRRT assessable profits (i.e. $50 million per annum) will be excluded from the MRRT.

• The MRRT will apply an internationally competitive rate of 30 per cent.

• New investment will be given generous treatment in the form of immediate write-off, rather than depreciation over a number of years. This allows mining projects to access the deductions immediately, and means a project will not pay any MRRT until it has made enough profit to pay off its upfront investment.

• The MRRT will carry forward unutilised losses at the government long term bond rate plus 7 per cent.

• The MRRT will provide transferability of deductions. This supports mine development because it means a taxpayer can use the deductions that flow from investments in the construction phase of a project to offset the MRRT liability from another of its projects that is in the production phase.

• The MRRT will also provide a full credit for state royalties paid by a taxpayer in respect of a mining project. Unused credits for royalties paid will be uplifted at the long term government bond rate plus 7 per cent, as per other expenses. Unused royalty credits will not be transferrable between projects or refundable.

• The MRRT will provide generous recognition of past investments through a credit that recognises the market value of that investment, written down over a period of up to 25 years. Unlike other costs, this starting base will not be uplifted.

• However, those companies that wish to use their current written down book values of the project's assets, excluding the value of the resource, will be provided with generous accelerated depreciation over 5 years. This starting base will be able to be uplifted at the government long term bond rate plus 7 per cent.

• The MRRT will recognise the particular characteristics of different commodities, by applying a taxing point close to the point of extraction, and using appropriate pricing arrangements to ensure only the value of the resources extracted is taxed.

• The MRRT will provide a 25 per cent extraction allowance to further shield from tax the important value add and capital that mining companies bring to mineral extraction.

Extension of the Petroleum Resource Rent Tax (PRRT) for all oil and gas

The Australian Government recognises that the PRRT, which has been in place since 1 July 1987, has been providing a stable and effective taxation regime for offshore oil and gas projects.

The Government has decided to extend the PRRT regime to cover all Australian oil and gas projects whether they are onshore or offshore.

The key features of the PRRT are:

• the tax rate is 40 per cent;

• there are a range of uplift allowances for unutilised losses and capital write-offs;

• immediate expensing is available for all expenditure;

• the tax value of losses can only be transferred in very limited circumstances;

• all state and federal resource taxes will be creditable against current and future PRRT liabilities from a project; and

• transition provisions will also be provided for oil and gas projects moving into the PRRT, including a generous starting base using either market value or written down book values.

A better return to the nation

The Australian Government is committed to ensuring that the Australian people receive a better return on the profits made from extracting our resources and that a strong resource sector remains sustainable into the future. These are non-renewable resources which can only be extracted once. That is why it is important that the Australian community gets a fair return for them, to put towards building a better nation.

The Government has been working with the resources industry to deliver a profits-based resource tax that works better for the industry and delivers improved returns for the community.

Improving the taxation of resources
Australia has abundant non-renewable supplies of iron ore, coal, oil and gas, which are expected to continue to command high prices driven by increased demand, particularly from China and India.

The community, through the Australian and State governments, own the rights to these resources and we have a responsibility to future generations to charge appropriately for using them. The new resource taxation framework will enable the nation to make the most of the resources boom, invest in infrastructure and jobs and give all Australians a lasting stake in our prosperity.

State governments currently tax resource projects through state royalties. These are generally based on a fixed amount per tonne of production or on a fixed percentage of the value of production. The tax generally does not vary with profits made.

Resource commodity prices have increased considerably. Since the beginning of the mining boom, prices for iron ore have increased by over 400 per cent and prices for black coal have increased over 200 per cent. However under royalties, a declining proportion of the increased profits from this price spike accrue to the community from resource charges.
A profits- based regime charges more appropriately for commodities during periods of high profits.

How the MRRT works
The following example is intended to illustrate how the MRRT will apply to iron ore and coal projects, commencing after 1 July 2012.

The example presents outcomes for a single project company with an equity financed mine that operates for 5 years. The company is assumed to invest $1 billion in the first year of the project. Over the life of the project the pre-tax rate of return (revenue less operating and investment costs) is 50 per cent.

The MRRT is levied at a rate of 30 per cent of the operating margin (revenue less operating and investment costs) less the MRRT allowance and the extraction allowance. The MRRT allowance is calculated as the value of unused losses uplifted by an allowance rate equal to the long term government bond rate plus 7 per cent. The extraction allowance provides a 25 per cent discount to the MRRT liability to focus the tax on the value of the resource rather than the value added through mining expertise.

State royalties are assumed in this example to be equal to 7.5 per cent of sales revenue and are credited against the MRRT liability to produce the net MRRT liability. Where royalty payments exceed the MRRT liability in any one year, the balance is uplifted at the allowance rate to be offset against future MRRT liabilities. The total resource charge is the sum of royalties paid in the year and the net MRRT liability.

In this example the average tax rate over the life of the project (total tax as a percentage of total profit before tax) is 42.3 per cent.

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
Resource Charge	$m	$m	$m	$m	$m	$m
Revenue	0	520	830	910	1090	1100
Operating expenses	0	130	210	230	270	280
Depreciation	1000	0	0	0	0	0
MRRT allowance @ 13 per cent	0	130	96	28	0	0
MRRT unutilised losses	0	1000	740	216	0	0
MRRT profit/loss	-1000	-740	-216	436	820	820
MRRT @ 30 per cent	0	0	0	131	246	246
Extraction allowance @ 25%	0	0	0	33	62	62
MRRT after extraction allowance	0	0	0	98	185	185
Royalty @ 7.5 per cent	0	39	62	68	82	83
Uplifted Royalty offset	0	0	44	120	102	0
Net MRRT	0	0	0	0	1	102
Total resource charge	**0**	**39**	**62**	**68**	**82**	**185**
Company tax						
Revenue	0	520	830	910	1090	1100
Operating expenses	0	130	210	230	270	280
Depreciation	0	200	200	200	200	200
Total resource charge	0	39	62	68	82	185
Company taxable income	0	151	358	412	538	436
Company tax @ 29 per cent	**0**	**44**	**104**	**119**	**156**	**126**
Profit before tax	0	190	420	480	620	620
Total tax	0	83	166	188	238	311

* Figures presented in the table above may not add due to rounding.

Next steps

On 10 June 2011 the Australian Government released the MRRT exposure draft legislation for public consultation and comment. The closing date for this public consultation period is 14 July 2011. The Government will release the PRRT exposure draft legislation for public consultation and comment in the middle of 2011.

Legislation implementing the new resource taxation arrangements is expected to be introduced into Parliament towards the end of 2011.