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Overview of the Bills

Mineral Resource Rent Tax Bills 2011

Introduction

2.1 Australia is experiencing an unprecedented mining boom with high levels of investment and profit. Mining companies generated profits of $92.8 billion to June and plan to invest $430 billion to expand their industry. The Assistant Treasurer, the Hon Bill Shorten, MP, noted that 'mining profits have jumped 262 per cent in the last decade.'[1] The Assistant Treasurer stated:

> The current arrangements fail to provide an appropriate return for these non-renewable resources to the Australian community, who owns the resources 100 per cent.[2]

2.2 The Australian Government has taken the view that the massive profits from the one-off exploitation of Australia's mineral assets by the mining sector should be more fairly taxed and the proceeds returned to all Australians now and into the future. The Mineral Resource Rent Tax (MRRT) will be a tax on mining profits. The proceeds of the tax will fund critical infrastructure, a cut in the company tax rate, and make it possible to increase the superannuation guarantee from nine to 12 per cent.

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1 The Hon Bill Shorten, MP, Assistant Treasurer, Second Reading Speech, House of Representatives Hansard, 2 November 2011, p. 1.

2 The Hon Bill Shorten, MP, Assistant Treasurer, Second Reading Speech, House of Representatives Hansard, 2 November 2011, p. 1.

Existing taxes

2.3 Currently, state and territory governments generally tax non-renewable resources by applying a royalty on production. Royalties are generally 'applied on the basis of volume or value and do not take into account how profitable a mining operation is.'[3] As profits are not taken into account, royalties are considered less effective than a mineral resource rent tax. The Explanatory Memorandum (EM) notes that 'Royalties therefore may only recover a portion of mining rents when mining profits are high, but will also tax mining operations where no economic rent is present, such as when profits are low.'

2.4 The Australian Future Tax System (AFTS) review found 'that royalty regimes applied by the states and territories were among the most distorting taxes in the Federation.'[4] The EM states:

> As a consequence of being distorting and relatively inflexible, royalties tend to be set at rates low enough for the mining industry to continue to operate in periods of low to average commodity prices. However, this means that royalties will often fail to provide an adequate return to the community when commodity prices are high.[5]

2.5 In addition to royalties, the company tax is a profits-based tax which generally applies to business and 'will tend to raise more revenue from mining operations when profits are high.'[6] However, the company tax was not considered a desirable mechanism for taxing mining operations. The EM stated:

> …the AFTS Review found that there would be benefits to the economy more broadly through lowering the company tax rate to assist in attracting internationally mobile capital investment.
>
> The AFTS Review concluded that a lower company tax rate was desirable for Australia but only if a specific profits-based tax was extended to mining operations to ensure a sufficient return to the community in periods of high commodity prices.[7]

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3 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 5.

4 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 7.

5 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 7.

6 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 7.

7 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 7.

Basic operation of the MRRT

2.6 In contrast to royalties, resource rent taxes take into account the profitability of a mining operation. One of the earliest forms of a resource rent tax was developed in 1948 by Cary Brown. Under a 'Brown tax', cash flow, after taking into account revenue and expenditure, is taxed at a constant percentage. Where there is positive cash flow, tax is charged but where there is negative cash flow, typically at the investment phase, the government provides a refund at the tax value. The EM notes that the Brown tax model, however, is difficult to implement 'because of the immediate nature of the refund.'[8]

2.7 In contrast, the Garnaut-Clunies Ross resource rent tax is similar to the Brown tax model except that there is no tax refund when there is negative cash flow. Instead, 'losses are carried forward and uplifted by an interest rate, so that they can be used as a deduction against positive cash flows in later years.'[9]

2.8 The MRRT proposed in the legislation is 'a tax on the economic rents miners make from the taxable resources (iron ore, coal and some gases) after they are extracted from the ground but before they undergo any significant processing or value add.'[10]

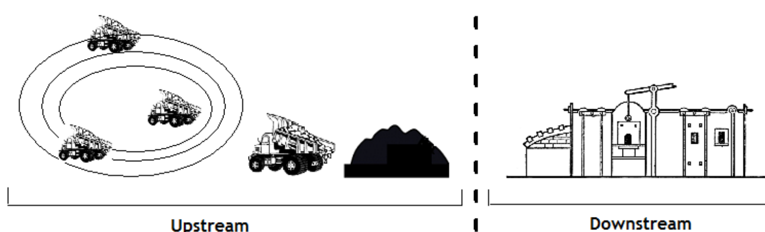
2.9 The MRRT is a project-based tax, so a liability is worked out separately for each project the miner has at the end of each MRRT year. The EM notes that 'the tax is imposed on a miner's mining profit, less its MRRT allowances, at a rate of 22.5 per cent (that is, at a nominal rate of 30 per cent, less a one-quarter extraction allowance to recognise the miner's employment of specialist skills).'[11]

2.10 A project's mining profit is mining revenue less its mining expenditure. The EM notes that 'mining revenue is, in general, the part of what the miner sells its taxable resources for that is attributable to the resources in the condition and location they were in just after extraction (the 'valuation point')'.[12] Mining expenditure is the cost the miner incurs in bringing the taxable resources to the ***valuation point***.

8 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 6.
9 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 6.
10 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 3.
11 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 3.
12 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 3.

2.11 The EM notes that 'the ***valuation point*** is typically just before the taxable resource leaves the run-of mine stockpile (also called the ROM stockpile or ROM pad). Diagram 2.1 shows the valuation point in the mining phase.

Diagram 2.1 The Valuation Point



In this diagram, the dashed line represents the valuation point at the run-of-mine stockpile. Upstream and downstream mining operations are illustrated.

Source Explanatory Memorandum, p. 13

2.12 As shown in diagram 2.1, mining operations that occur before the valuation point are **upstream mining operations** and those that occur later are **downstream mining operations**. In determining the mining revenue amount, the EM states:

> The MRRT is a tax on proceeds from selling a taxable resource (or on the proceeds which would have been realised if the resources had been sold instead of exported or sold) but only on that part of those proceeds that is reasonably attributable to the condition and location of the resource when it was at the valuation point. That amount must be attributed using the most appropriate and reliable method having regard to the miner's circumstances, the available information and certain statutory assumptions (to the extent to which they are relevant in applying a particular method). The statutory assumptions are that the downstream operations are carried on by a separate entity who has no interest in the resource and who deals independently with the miner in a competitive market.[13]

2.13 The MRRT takes into account the majority of upstream costs incurred by the miner in extracting the mine deposit. The EM states:

> Upstream costs are called ***mining expenditure*** if they are necessarily incurred by the miner in carrying on the upstream mining operations. Mining expenditure includes costs related to

13 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 13.

construction of the mining operation, blasting and digging, infrastructure, and capital assets used to transport the non-renewable resource to the valuation point (such as dump trucks and conveyor belts).[14]

2.14 Certain 'mining allowances' will reduce each project's mining profit. The EM notes that the most significant of the allowances is for mining royalties the miner pays to the states and territories' which ensures 'that the royalties and the MRRT do not double tax the mining profit.'[15]

2.15 Other allowances can include losses the project made in earlier years and losses transferred from other projects.

2.16 The Assistant Treasurer noted that 'unlike royalties, the MRRT recognises the massive investment that miners make.'[16]

What resources are covered by the MRRT

2.17 The EM notes that the MRRT applies to certain profits from iron and coal, and also applies to profits from gas extracted as a necessary incident of coal mining and gas produced by the in situ combustion of coal.

Date of effect and financial impact

2.18 The MRRT will apply from 1 July 2012. Table 2.1 shows the revenue implications of the MRRT.

Table 2.1 The financial impact of the MRRT

2011-12	2012-13	2013-14	2014-15
Nil	$3.7 billion	$4 billion	$3.4 billion

Source Explanatory Memorandum, p.4

Consequential Bills

2.19 The MRRT is imposed by the following three imposition Bills:

- Minerals Resource Rent Tax (Imposition—General) Bill 2011;
- Minerals Resource Rent Tax (Imposition—Customs) Bill 2011; and

14 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 14.

15 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 3.

16 The Hon Bill Shorten, MP, Assistant Treasurer, Second Reading Speech, House of Representatives Hansard, 2 November 2011, p. 1.

- Minerals Resource Rent Tax (Imposition—Excise) Bill 2011.

2.20 Each of the bills imposes the MRRT to the extent that it is a duty of customs, that it is a duty of excise and that it is a duty of neither customs or excise. The EM states:

> This reflects the constitutional requirement that laws imposing duties of customs shall deal only with duties of customs and that laws imposing duties of excise shall deal only with duties of excise (see section 55 of the Constitution). However, there is only one assessment Act.
>
> The approach of enacting a single assessment Act with multiple imposition Acts when a tax law could be a duty of customs, a duty of excise, as well as some other type of tax, complies with the Constitution. The same approach was followed for the enactment of the goods and services tax legislation.[17]

2.21 MRRT is not imposed on property belonging to a State. That ensures that the MRRT complies with section 114 of the Constitution, which prohibits the Commonwealth from imposing a tax on any kind of property of a State. In practice, this will only have an effect to the extent that a State mines its own taxable resources. In that case, the State will not be subject to MRRT.

Petroleum Resource Rent Tax Amendment Bills 2011

The extension of the Petroleum Resource Rent Tax

2.22 The Main Bill amends the PRRTAA 1987 to expand its coverage to onshore projects and the North West Shelf. From 1 July 2012, the PRRT will be extended to apply to petroleum production, including coal seam gas and shale oil, sourced from petroleum projects located onshore and in territorial waters, as well as from the North West Shelf project area. The PRRT will not apply to the Joint Petroleum Development Area in the Timor Sea.

2.23 During informal discussions with industry, it appears that the amendments to the PRRT are less significant than the other Bills in the package because:

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17 Explanatory Memorandum, Minerals Resource Rent Tax Bill 2011, p. 31.

- the PRRT is already well known to industry; and
- the North West Shelf is unlikely to pay significant amounts of PRRT because the amount of royalties and excise paid will be taken into account in calculating PRRT. These royalties and excise are sufficiently high so as to preclude the PRRT being paid for these projects.

Imposition Bills for the PRRT

2.24 The PRRT was imposed by the Petroleum Resource Rent Tax Act 1987. That Act imposes the tax in respect of the taxable profit of a person of a year from a petroleum project. The Petroleum Resource Rent Tax Act 1987 will be repealed as part of the Main Bill and replaced by the three separate imposition Bills:

- the PRRT excise imposition Bill;
- the PRRT customs imposition Bill; and
- the PRRT general imposition Bill.

2.25 The three additional imposition Bills impose the PRRT to the extent that it is a duty of customs; to the extent that it is a duty of excise; and to the extent that it is neither a duty of customs nor one of excise. All three imposition Bills set the rate with respect to the taxable profits of a person of a year of tax in relation to a petroleum project at 40 per cent, consistent with the original imposition Act.

2.26 The constitutional validity of the PRRT is not in question. However, the three imposition Bills are being introduced to avoid the possibility of constitutional irregularities arising in the future. A similar approach has been adopted for the MRRT.

2.27 The imposition Bills will apply retrospectively from 1 July 1986, consistent with the commencement of the original imposition Act. Replacing the original imposition Act does not alter the operation of the PRRT.

2.28 The approach of enacting a single assessment Bill with multiple imposition Bills when a tax law could be argued to be a duty of customs, a duty of excise, as well as some other type of tax is not unusual. The same approach was followed for the enactment of the goods and services tax (GST) legislation.

2.29 PRRT is not imposed on property belonging to a State. That ensures that the PRRT complies with section 114 of the Constitution, which prohibits the Commonwealth from imposing a tax of any kind on property of a State. In practice, this will only have an effect to the extent that a State

directly recovers its own petroleum resources. In that case, the State will not be subject to PRRT.

Tax Laws Amendment (Stronger, Fairer, Simpler and Other Measures) Bill 2011

Abolishing the entrepreneurs' tax offset

2.30 The entrepreneurs' tax offset was introduced into the *Income Tax Assessment Act 1997* (ITAA 1997) by the Tax Laws Amendment (2004 Measures No. 7) Act 2005 and applies to assessments for income years commencing on or after 1 July 2005.

2.31 The entrepreneurs' tax offset provides up to a 25 per cent tax offset on the income tax liability attributable to business income of small businesses that have an annual turnover of under $75,000. The benefit of the offset begins to phase out for small businesses with an annual turnover above $50,000 and eligibility ceases when turnover reaches $75,000. In addition, the entrepreneurs' tax offset is subject to an income test that restricts the eligibility of individuals whose income is over a threshold amount ($70,000 if they are single and $120,000 if they have a family).

2.32 The Australia's Future Tax System Review noted that removing the entrepreneurs' tax offset would reduce compliance and administration costs and provide a more equitable and neutral treatment between self-employment and employment income. The Australia's Future Tax System Review recommended (recommendation 6) the abolition of the entrepreneurs' tax offset as it is complex to administer and provides problematic incentives related to business structure.

2.33 On 8 May 2011, the Government announced as part of the small business tax reform package in the 2011-12 Budget that it would abolish the entrepreneurs' tax offset from the 2012-13 income year. It will have a positive annual Budget impact of $180 million.

Small business depreciation

2.34 Small businesses can choose to use the capital allowance arrangements in Subdivision 328-D of the ITAA 1997 to depreciate assets.

2.35 The existing capital allowance arrangements for small businesses allow low cost assets to be written off in the year the small business first started

to use the asset or had it installed ready for use. A low cost asset (except a horticultural plant) is defined in section 40-425 as one which has a cost of less than $1,000 at the end of the income year in which the asset started to be used or is installed ready for use, for a taxable purpose.

2.36 Other depreciating assets, generally those costing $1,000 or more, are allocated to one of two depreciation pools, depending on the effective life of the asset: the long life small business pool or the general small business pool. The pools are depreciated at different rates (5 per cent or 30 per cent).

2.37 Recommendation 29 of the Australia's Future Tax System Review (December 2009) proposed that the capital allowance arrangements for small business be streamlined and simplified by allowing:

- depreciating assets costing less than $10,000 to be immediately written off; and
- all other depreciating assets (except buildings) to be pooled together, with the value of the pool depreciated at a single declining balance rate.

2.38 In response to this review, the Government announced on 2 May 2010 that from the 2012-13 income year small businesses would be allowed to write off assets costing less than $5,000, and that simplified pooling arrangements would be provided for other assets.

2.39 On 10 July 2011, the Government announced that as part of the Clean Energy Future Plan the small business instant asset write-off threshold would be further increased from $5,000 to $6,500.

2.40 From the 2012-13 income year, these amendments enable small businesses that choose to use the capital allowance provisions in Subdivision 328-D to:

- write off depreciating assets costing less than $6,500 in the income year in which they start to use the asset or have it installed ready for use for a taxable purpose during or before that income year; and
- allocate depreciating assets costing $6,500 or more to the general small business pool and depreciated at a rate of 15 per cent in the year of allocation and 30 per cent in following years.

2.41 The measure will have a negative annual Budget impact of $1.1 billion.

Small business deductions for motor vehicles

2.42 Small businesses can choose to use the capital allowance arrangements in Subdivision 328-D of the ITAA 1997 to depreciate assets, including motor vehicles.

2.43 As part of the 2011-12 Budget, the Government announced that small business entities would be allowed to bring forward a deduction of up to $5,000 for any motor vehicles purchased in the 2012-13 and subsequent income years. The remainder of the purchase value of the motor vehicle is depreciated through the general small business pool at 15 per cent in the first year and 30 per cent in later years.

2.44 From the 2012-13 income year, small business entities that choose to use the capital allowance provisions in Subdivision 328-D can claim up to $5,000 as an immediate deduction for a motor vehicle in the year they start to use the motor vehicle, or have it installed ready for use, for a taxable purpose. Taking into account the amount already written off, the remainder of the purchase cost is depreciated as part of the general small business pool, at 15 per cent in the first year and 30 per cent in later years. This is an exception to the general small business capital allowance rules for depreciating assets.

2.45 The measure will have a negative annual Budget impact of $200 million in 2013-14 and $150 million in 2014-15.

Low income superannuation contribution

2.46 The low income superannuation contribution is part of a suite of reforms to improve the superannuation outcomes for Australians. It is dependent on the implementation of the MRRT package of Bills. It is designed to ensure a fairer distribution of Australia's wealth in the resources boom by benefiting low income earners.

2.47 Concessional contributions are generally contributions to a superannuation fund that receive concessional tax treatment. Concessional contributions are generally before tax contributions that include an employer's superannuation guarantee (SG) contributions, contributions made under a salary sacrifice arrangement and an individual's personal contributions that are deducted

2.48 The low income superannuation contribution seeks to effectively return the tax paid on concessional contributions by a person's superannuation fund or retirement savings account (RSA) provider to a person who is a

low income earner. Low income earners are defined as individuals with an adjusted taxable income of $37,000 or less.

2.49 The maximum amount payable is $500.

2.50 The measure will have a negative annual Budget impact of up to $1 billion.

Superannuation Guarantee (Administration) Amendment Bill 2011

2.51 Under the Superannuation Guarantee (SG) scheme, all employers are required to make a prescribed minimum level of superannuation contributions to a complying superannuation fund or a retirement savings account (RSA) on behalf of their eligible employees.

2.52 The legislation gradually increases the SG with increments of 0.25 per cent on 1 July 2013 and 1 July 2014. From then increments will increase by 0.5 percentage points applying annually up to 2019-20 when the SG rate will be set at 12 per cent.

2.53 The minimum level of employer superannuation contributions is the SG 'charge percentage' applied to each eligible employee's ordinary time earnings. The current SG charge percentage is 9 per cent.

2.54 The *Superannuation Guarantee Charge Act 1992* imposes the SG charge on any employer who has an SG shortfall in respect of a quarter. Where an employer does not contribute the minimum level of required employer superannuation contributions on time, they will be liable to pay to the Australian Taxation Office (ATO) a charge on the SG shortfall. The SG shortfall for a quarter is calculated pursuant to section 17 of the *Superannuation Guarantee (Administration) Act 1992* (SGAA 1992) and consists of the total of the employer's individual SG shortfalls for that quarter, a nominal interest component, and an administration component.

2.55 Currently, the SG charge is payable by employers who do not contribute 9 per cent of ordinary time earnings on time for eligible employees under the age of 70.

Raising the superannuation guarantee age limit from 70 to 75

2.56 Under subsection 19(1) and paragraph 27(1)(a) of the SGAA 1992, salary or wages paid to an employee who is 70 or over does not count towards the calculation of the SG shortfall. Since there is no SG shortfall, this means

that employers are not required to make SG contributions for employees who are aged 70 or over.

2.57 This Bill raises the SG age limit from 70 to 75 and requires employers to contribute to complying superannuation funds of eligible mature age employees under the age of 75.

2.58 Raising the SG age limit to 75 brings the SG amendments in line with provisions of the ITAA 1997 which allow employers to claim a full deduction for all contributions to superannuation funds made on behalf of their employees up to age 75 and allow self-employed people to make deductible contributions until they turn 75.

Increasing the superannuation guarantee charge percentage to 12 per cent

2.59 In order to avoid an SG shortfall in respect of a quarter, employers currently have to pay 9 per cent of ordinary time earnings in superannuation contributions for eligible employees. In order to increase future retirement incomes for Australian workers, this Bill gradually increases the SG charge percentage each year, reaching 12 per cent in 2019-20. Future rates are detailed below.

Table 2.2 Future changes to the SG percentage

Income year	Charge percentage (%)
2013-14	9.25
2014-15	9.5
2015-16	10
2016-17	10.5
2017-18	11
2018-19	11.5
2019-20 and subsequently	12

Source Explanatory Memorandum to the Bill, p. 10.