

# The Guide to the Australian Government's New Super Tax

## A simplified example of calculating the new super tax

On 2 May 2010, the Australian Government announced its proposal for a new super tax for the Australian resources sector. The tax is scheduled to take effect on 1 July 2012. It leads to a total effective statutory tax rate of 57 percent on Australian resource profits. Exhibit 1 walks through the calculation of the super tax and total tax on a typical mining operation.

## Key issues in calculating the super tax

- **Royalties.** Existing state royalties and scheduled increases must still be paid. These payments are refundable credits against the super tax.
- **Capital allowance.** The super tax allows a resource company to receive a return on past investment before calculation of the tax. This capital allowance equals the government long-term bond rate (currently 5.7 percent) multiplied by the accounting value of past investment.
- **Company tax.** Royalties and super tax payments are deducted from the company tax calculation.

### Exhibit 1: Example of a typical mining operation

Revenue and profit before tax		
Revenue		300
Operating expenses (excluding royalties)		(100)
Depreciation		(95)
Interest		(5)
<b>Profit before tax</b>		<b>100</b>

  

	Today	'Super tax'	
<b>Royalties calculation</b>			
<b>Royalty</b>	<b>(15)</b>	<b>(15)</b>	5% of 300 in revenue
<b>'Super tax' calculation</b>			
Revenue	-	300	
Operating expenses	-	(100)	
Depreciation	-	(95)	
Capital allowance <sup>1</sup>	-	(5)	
Profit before 'super tax'	-	100	
'Super tax' before royalty credit	-	(40)	40% of 100 in profit
Credit for royalties paid	-	15	
<b>'Super tax'</b>	<b>(0)</b>	<b>(25)</b>	
<b>Company tax calculation</b>			
Revenue	300	300	
Operating expenses	(100)	(100)	
Depreciation	(95)	(95)	
Interest	(5)	(5)	
Deduction for royalties paid	(15)	(15)	
Deduction for 'super tax' paid	(0)	(25)	
Profit before company tax	85	60	30% tax rate today and 28% with 'super tax'
<b>Company tax</b>	<b>(26)</b>	<b>(17)</b>	
<b>Total tax calculation</b>			
Royalty	(15)	(15)	
'Super tax'	(0)	(25)	
Company tax	(26)	(17)	
<b>Total tax</b>	<b>(41)</b>	<b>(57)</b>	
<b>Tax rates</b>			
<b>Effective cash tax rate<sup>2</sup></b>		<b>57%</b>	

1 Past investments and losses multiplied by long-term government bond rate

2 Effective cash tax rate may be higher or lower than effective statutory tax rate due to factors such as size of uplift, debt funding, and differences between accounting and tax depreciation

- **Incurred but excluded expenditures.** The super tax does not allow deductions for a number of expenditures including interest and financing

costs.<sup>1</sup> This is different to company tax, which does allow interest and other financing costs to be deducted.

1 Other excluded expenditures are payments to acquire an interest in an existing exploration, development, or production permit or licence; payments to acquire an interest in projects subject to the new tax; or payments of income tax or GST.

## What is still uncertain

The Government announcement has left a number of issues open for consultation. These include:

- **Taxing point.** The Henry Review suggests a taxing point close to the point of extraction of the resource to avoid taxing downstream activities and infrastructure such as rail and ports.
- **Assessable revenue.** Market prices may not be available at the selected taxing point. If so, an estimate of value at the taxing point will need to be calculated to separate upstream and downstream profits. For example, the PRRT applies a 50:50 split to calculate the upstream versus downstream profits of LNG.
- **Potential cap on royalty credit.** The royalty credit will be at least up to the amount of royalties imposed at 2 May 2010 and will include scheduled increases only.

### Exhibit 2: Comparison of the Government's proposed super tax on resources and the Petroleum Resource Rent Tax (PRRT)

	PRRT	Super tax (compared to PRRT)
<b>Application to existing projects</b>	▪ When introduced, applied only to new stand-alone projects (i.e., known at time of investment)	✗ ▪ Applies to existing projects (i.e., not known at time of investment)
<b>Rate</b>	▪ 40 percent	▬ ▪ 40 percent
<b>Return permitted to investors before taxing 'super profit'</b>	▪ Government long-term bond rate plus a minimum of five percent	✗ ▪ Government long-term bond rate
<b>Depreciation schedule for capex</b>	▪ Capex 100 percent deductible in year spent	✗ ▪ Capex deductible over time, not immediately
<b>Royalties</b>	▪ PRRT replaced original crude excise and royalties	✗ ▪ Existing and currently scheduled state royalties must still be paid ▪ These payments are refundable credits against super tax
<b>Transfer and recognition of losses and expenditure</b>	▪ Only exploration costs are transferrable ▪ Companies do not receive refunds if losses remain at end of project life	✓ ▪ Group companies can transfer losses including exploration ▪ Where not transferrable, companies receive partial refunds for losses remaining at end of project life (tax loss multiplied by 40 percent)

Western Australia and South Australia are reported to be planning royalty increases, and the Northern Territory has announced an increase in royalties from 18 to 20 percent. It is unclear whether all these increases can be credited against the super tax or will represent

further net increases in the total tax burden.

- **Depreciation schedules for capital expenditure.** The Government announcement states a preference for using the income tax schedule to depreciate capital expenditure of new projects.

## Frequently asked questions

**The Government announcement states that the super tax is a tax on profits after returns to investors.**

**Q: How does it allow for returns on existing investments?**

**A:** It doesn't fully. To transition existing projects into the super tax regime, the Government values them at accounting book value—typically much lower than their actual market values.

This under-compensates resource companies with an unfavourable bias against older, more depreciated assets and against companies that own their assets rather than lease.

**Q: How does the resulting effective tax rate of 57 percent compare with other countries?**

**A:** It will make Australia's taxes on its mineral resources industry the highest in the world.

**Q: What return on capital does it permit investors to receive before taxing a 'super profit'?**

**A:** Investors will receive the government long-term bond rate, which is well below the cost of capital for Australian resource companies.

**Q: What projects does the super tax apply to?**

**A:** The super tax applies to all Australian resource projects not under the Petroleum Resource Rent Tax (PRRT). Currently under the PRRT are Bass Strait, Gorgon, and Pluto among others. Projects such as North West Shelf and coal seam gas will be transitioned to the new tax system. The super tax will apply to all minerals projects. Unlike the rest of the world, under the super tax Australia will levy a higher tax burden on minerals than on oil.

**Q: How does the new super tax compare to the PRRT?**

**A:** It's worse. Exhibit 2 explains why.