Mr Nicolaou - The research suggests that the Brown tax has not been effective in its implementation across various jurisdictions around the world.

Senator CAMERON - Where?

Senator CAMERON - Where has the Brown tax been introduced? Do you want to take that on notice?

Mr Nicolaou - I will take that on notice, but there is research. I am sure it is in the Henry review, but again I do not want to say things without the information behind me. There have been concerns around a Brown tax for many years, and that is why it has not been widely adopted throughout different jurisdictions around the world. That is not to discount a form of Brown tax in Australia, but we need to debate it.

Answer:

There are few specific examples of where a Brown tax has been implemented. There are examples of resource rent taxes (variants of a Brown tax) being implemented in overseas jurisdictions, but there is insufficient detailed information about these taxes to identify it precisely as a Brown tax. For example, the RSPT itself was based on the concept of the Brown Tax but was not exactly a Brown Tax in its operation.

There are some examples of Brown tax variants around the world.

For example, in Papua New Guinea a resource rent tax was introduced in legislation as an additional tax applying to projects for extracting metals, petroleum and gas. However, it would appear that the 'Additional Profits Tax' was only actually levied on the Bougainville copper mine project in the 1970s. In response to a sustained reduction in the country's share of global exploration investment over time, the government abolished the tax in 2003. The tax was reintroduced in 2008 for a major liquefied natural gas project[1].

According to the World Bank[2], pure economic rent-based taxes may also be in operation in the Philippines although there is little information available to gauge its success. The World Bank also notes that Ghana employs a sliding scale tax regime on mining which targets profits, although it is via a royalty mechanism based on a ratio of costs and profits, and cannot be directly identified as a Brown Tax or even a variant of it.

In the 1980s, the US imposed an oil levy, the 'crude oil windfall profit tax'[3]. Despite its name, the tax operated more like an excise tax than a profit tax - that is, it taxed each barrel of oil produced. But it had some similarities with a profit tax in that the excise on US domestic oil production taxed the difference between the market price of oil and a predetermined base price. The windfall tax was eventually repealed in 1988. The original forecast of revenues from the tax turned out to have been significantly overestimated, reflecting overestimates of crude oil prices. The tax also increased the nation's dependence on imported oil as it applied to oil produced domestically in the US and not on imported oil.

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[1] The Resource Super Profits Tax and the 2010/11 Federal Budget, How the Henry Review and 2010/11 Federal Budget will harm Australia's economic interests, Julie Novak, Research Fellow, The Institute of Public Affairs, June 2010

[2] "Mining Royalties, A Global Study of Their Impact on Investors, Government, and Civil Society", James Otto, Craig Andrews, Fred Cawood, Michael Doggett, Pietro Guj, Frank Stermole, John Stermole, and John Tilton.

[3] Historical Perspective: The Windfall Profit Tax - Career of a Concept, by Joseph J. Thorndike November 10, 2005.

Aside from these few examples, there is also evidence from academic experts that Brown taxes and their variants are currently not in use anywhere in the world. There are also concerns outlining their application in practice.

For example, according to Professor Jerry Hausman (McDonald Professor of Economics at Massachusetts Institute of Technology), there is no working model of a Brown tax anywhere in the world. According to Hausman[4]:

"I don't think it [a Brown tax] *works in the real world. It has theoretical properties but the theory of investment had moved a long way since 1948. That is not to say you could not redesign it to suit modernity. But in the real world, no one is going to do that."*

According to the Asia Tax Bulletin[5]:

"Despite this theoretical attractiveness, the RRT [resource rent tax] *can discourage exploration in practice. Investors know that they will be taxed on highly successful projects, whereas unsuccessful projects will not be compensated. Consequently the RRT reduces the expected return from exploration, and distorts exploration decisions. Also, excessive capital or a reduced rate of production will be encouraged if the RRT discount rate for cash-flow accumulation rate is set above the company's discount rate, which will vary from company to company and can never be known with certainty."*

According to RBS Morgans[6]:

"A second major contribution [of E. Carey Brown] *was the idea of the Brown Tax. Here, a tax on resource extraction is balanced by a tax deduction for exploration. The tax deduction for exploration reduces the cost of exploration. This makes resources more abundant. This means that the economic cost of developing these resources is lower. This in turn leads to a higher level of investment and to a higher level of production. These theoretical attributes of the Brown Tax may be realistic in a circumstance where capital for exploration is constrained. I can imagine there are many parts of Africa where this would be realistic. In Africa, the positive cash flow from the tax deduction would be extremely important in funding new exploration.*

This is not the case in Australia. In Australia since well before Federation, we have enjoyed a highly liquid market in the equities of mineral exploration stocks. Investors who hold blue chip shares may rationally include in their portfolios a small component of mining exploration stocks. These stocks may generate trading profits when their explorations are successful. More usually they generate trading losses when their exploration is not successful. These trading losses may generate tax losses for investors which are similar to the tax deductions provided under the Brown Tax. What this means is that the Brown Tax does not add to the funds available for exploration in Australia. In practice, the proposal won't work."

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[4] The Australian Newspaper, "Tax theory all at sea in PM's push for a fair share", by Matthew Stevens, June 18, 2010

[5] Mineral Taxation around the World: Trends and Issues, Dr J.V.M. Sarma and Dr G. Naresh, January 2001.

[6] RBS Morgans Economic Strategy Update, "When it doesn't make sense, it may not work", by Michael Knox, 11 May 2010.