Senate Economics Legislation Committee

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Additional Estimates

2015 - 2016

Department/Agency: Treasury
Question: AET 41
Topic: Effective tax rates of the PRRT
Reference: Hansard page no. 71 - 10 February 2016
Senator: Whish-Wilson, Peter

Question:

Senator WHISH-WILSON: Do you agree with the analysis that effective tax rates have significantly fallen over time? I think it was estimated in 2002 they were around 24 per cent. Is it now around five per cent in terms of the actual—
Mr Hirschhorn: In terms of the effective tax rate of the PRRT?
Senator WHISH-WILSON: Yes.
Mr Hirschhorn: It is 40.
Senator WHISH-WILSON: Forty per cent is what it is set at, but after deductions, in line with the growth of value in tax, tax collection has not really improved much since it started. As I was saying earlier, gas production has ramped up quite significantly. I cannot imagine that is all due to falls in prices.
Mr Heferen: You also have to think that with the way the PRRT is designed—and I must confess I am certainly no expert in it—the PRRT, being a rent tax, is aimed at taxing the cash flow. So rather than income tax, which looks at the tax paid at the normal and the above-normal return to capital, the PRRT just tries to tax the above-normal by having a cash flow tax. The big difference is the expenditure. The idea is that money comes in, money goes out, minus one off the other and pay 40 per cent of the difference. The difference between the PRRT and a genuine cash flow tax is that a genuine cash flow tax, where it is a negative, would have that refunded. The PRRT simply uplifts it and carries it forward. So, in a situation where there is a very large project and there is a lot of expenditure on both exploration and developing, there will be a lot of losses that are then carried forward. And they are uplifted, I think, at eight per cent. I think the exploration might be uplifted at 15 but the normal—
Senator WHISH-WILSON: A rate of the bond rate plus 15 per cent—
Mr Heferen: Sorry, yes, the bond rate plus. I beg your pardon. So, where there is a project that has had significant capital works over it over a number of years, you would expect those losses to be carried forward, to be uplifted, and—
Senator WHISH-WILSON: Do you know when those rates were set and what the rationale was for setting them?
Mr Heferen: I would have to take that on notice. I assume they were part of the original design of the PRRT.
Senator WHISH-WILSON: I could not find out if they were or not, so that is genuine. I am interested if you could.
Mr Heferen: We can take that on notice and provide that.
Senator WHISH-WILSON: Thank you.

Answer: Question AET 41

The PRRT is charged at a rate of 40 per cent on the taxable profit of a petroleum project.

Taxable profit is calculated by subtracting deductible expenditure from assessable receipts.

Where this expenditure exceeds assessable receipts the balance is generally uplifted (carried over to the future with an increase in value) at either the long term bond rate (LTBR) plus 5 per cent for general project expenditure and at the LTBR plus 15 per cent for exploration expenditure.

The uplift rate applied to increase undeducted expenditure was an original design feature of the *Petroleum Resource Rent Tax Assessment Act 1987* which took effect on 15 January 1988. The rationale for the rates was to maintain the value of undeducted expenditure until sufficient income was available to absorb it.

Prior to 1 July 1990, undeducted exploration and general project expenditure incurred within 5 years of when the production licence came into force was carried forward and uplifted at the long term bond rate plus 15 percentage points. Undeducted exploration and general project expenditure incurred more than 5 years before the production licence came into force was (and continues to be) carried forward and uplifted at the lower gross domestic product deflator rate.

The *Petroleum Resources Rent Legislation Amendment Bill 1991* modified the existing carry forward arrangements for undeducted expenditures. From 1 July 1990, the uplift rate for general project expenditure incurred within five years of, or after, the production licence came into force was reduced from the long term bond rate plus 15 percentage points to the long term bond rate plus 5 percentage points. The rationale for this reduction was to take account of the introduction of the wider transferability of exploration expenditure outside of projects undertaken by a person in an individual permit area, to other projects held by that person which would otherwise have a PRRT liability.