



**MINERALS
COUNCIL**
OF AUSTRALIA

24 May 2002

Mr Richard Warburton
Chairman, The Board of Taxation
C/- The Treasury
Langton Crescent
PARKES ACT 2600

Dear Mr Warburton 

**SUBMISSION BY THE MINERALS COUNCIL OF AUSTRALIA – TAX VALUE
METHOD (TVM) DEMONSTRATION LEGISLATION PROTOTYPE 4**

I am writing in response to the Board of Taxation's request for written submissions to assist it in evaluating the feasibility of the introduction of the Tax Value Method of determining business income for the purposes of taxation into the Australian tax law.

The Minerals Council of Australia represents companies involved in mineral exploration, mining and processing of minerals. Its activities are funded entirely by its member companies that, between them, produce around 90 per cent of Australia's mineral output. The Council is a founding member of the Business Coalition for Tax Reform (BCTR).

The Council appreciates the Board's decision to extend the deadline for submissions to allow the Council and other members of the BCTR to form a view on the detailed demonstration legislation, explanatory memorandum and information paper that have been released for public comment by the Board.

Minerals Council Position on the Tax Value Method

The Minerals Council supports the BCTR's submission to the Board and, in particular, its key recommendations that:

- *ongoing reforms are needed to reduce the complexity, instability, uncertainty and costs of compliance associated with Australia's business income tax system; and*
- *after a careful and considered assessment over an extensive period, the BCTR does not support the continuation of the TVM project.*

There are two further matters which we wish to put before the Board - the extension of the consultation process that has been undertaken by the Board to other taxation policy issues and the need to address the remaining non-deductible business expenditure or "black hole" problems in the tax law.

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Consultation Process

As you would expect, the Minerals Council has not taken the decision on TVM lightly. And, in doing so recognises and commends the Board of Taxation for the open consultation process it has undertaken on the TVM process over the past two year.

The Minerals Council would like to commend the Board of Taxation for the open consultation process it has undertaken in relation to the TVM project. This includes the public exposure of prototype legislation and explanatory material, co-design with the assistance of the TVM Working Group, conferences and presentations on the TVM concept and engagement of private sector secondees to the TVM Legislative Group. This consultation process has enabled the Council, either directly or through the BCTR, to have input into and involvement with vital stages in the development of the TVM concept.

The Council acknowledges, with appreciation, the time and effort that Mr Andrew England and his team have given to assist its representatives and other members of the BCTR's TVM sub-committee to understand various technical aspects of the demonstration legislation. The Council has twice participated in discussions with officials to workshop the robustness of the TVM proposals against commonly used contractual arrangements in the minerals sector. Indeed, the Minerals Council was one of only two bodies to workshop Prototypes 1 and 2 with ATO and Treasury officials and initiated a further workshop discussion on Prototype 4 involving representatives from the Business Council, Corporate Tax Association, Minerals Council and National Farmers' Federation.

Given the successful rigour and effectiveness of this consultative process, the MCA recommends that a similar approach be taken in the development and evaluation of changes to Australia's taxation arrangements. More specifically, we strongly recommend such a process in meeting the Government's and industry's objectives in the review of international taxation arrangements by the Board of Taxation.

Non-deductible Business Expenditures ("Blackholes")

One of the long held principles of business taxation by both the Minerals Council and the Business Coalition for Tax Reform is that "The taxation system should avoid the double taxation of business income *and provide relief for all business expenses.*" The Ralph Review of Business Taxation's final report supported this view on non-deductible business expenditure.

Following consideration of the Ralph Report, the Federal Government announced on 11 November 1999 that all blackhole expenditure was to be appropriately addressed.

The Minerals Council welcomed the reconfirmation of the Government's commitment "to giving recognition in the tax law to 'blackhole' expenditure" declared in the Treasurer's Press Release of 22 March 2001. This statement advised that while the new capital allowance system commences the process of recognising these expenditures "other blackholes will be considered through a comprehensive treatment under the tax value method ... [and] where other blackholes are identified, they will be considered on a case-by-case basis". This position was reiterated on 14 May in the Budget. [Ref: Paper No 2 at page 22].

As I am sure you are aware, a number of "blackhole" expenditure problem areas for corporates remain. Particularly:

1. The **Uniform Capital Allowances regime** – this was developed to be consistent with the TVM approach (should it go ahead) but capable of enactment without TVM. This has addressed a range of blackhole problem areas, following detailed consultation with industry – particularly the minerals industry.

S40-880 of the *New Business Tax System (Capital Allowances) Act 2001* refers to business cessation expenditure costs being deductible over five years. However the wording of this provision raises some uncertainty as to its scope. One might expect such a provision to encompass all costs arising from a decision to cease a business, including necessary costs of dismantling and removing existing plant, etc. The Explanatory Memorandum gives little guidance on this matter.

- We also suggest that some of the items in S40-880(1) could be better phrased. For instance paragraph 40-880(1)(d) could be rewritten as "(d) expenditure incurred by the company subject to the bid in relation to or in response to a take-over offer". This would address problems with the current wording such as what is meant by "defend".

2. **Certain native title costs** – The Government advised it would address some of these concerns in the Treasurer's and Attorney-General's Joint Press Release of 13 February 1998.

The Council understands from the Treasurer's Press Release of 11 November 1999 that all business blackhole expenditure was to be appropriately addressed. Whilst the Uniform Capital Allowance legislation does give significant relief in some areas of blackhole expenditure, it does not go as far as we understood the Government's intention to be.

Unless and until the Government takes additional action to remedy anomalies, Australian companies will continue to pay tax based on a distorted assessment of their trading results. The additional tax impost creates yet another competitive disadvantage for Australian companies operating in the global market.

Recommendations

In consideration of these matters, the Minerals Council recommends:

- there be a consultation process to address all non-deductible business expenditures pursuant to the Government's commitment.
- a workable comprehensive solution to blackhole expenditure be developed consistent with the Government's commitment to address non-deductible business expenditures **irrespective of the introduction of TVM.**

Uniform Capital Allowance Regime

The Minerals Council considers that a similar comprehensive treatment afforded under TVM can be achieved within the existing legislative structure. This could involve:

- an appropriate replacement measure to paragraph 40-840(2)(d) of the *Income Tax Assessment Act 1997* (ITAA1997). This would ensure deductibility of all expenditure not otherwise deductible on the basis that it is "capital" in nature and that it is connected with a project a taxpayer carries on for a taxable purpose. If for policy reasons certain types of expenditure are desired not to be afforded tax relief (e.g. purchased goodwill), these could be specifically excluded from S40-840(2).

The above replacement measure would leave some expenditure not related to a project "carried on for a taxable purpose" exposed, as it is either "too early" or "too late" in the income producing process to have the required nexus. A possible solution to this problem is:

- to have an ancillary provision to S40-840 allowing deductibility for expenditure incurred relating to a project associated with a business carried on, previously carried on, or a potential business that may be carried on for a taxable purpose. This should include costs such as:
 - demolition costs; and
 - unsuccessful feasibility studies in relation to a new business venture.

In addition, there may be other categories of costs to be added to Section 40-880 and, as noted above, there needs to be some amendment to this section to address problems with the current wording.

Certain Native Title Costs

Through a continuation of the consultative process strongly supported by the Minerals Council, the Board of Taxation could develop an appropriate treatment for the costs associated with certain native title expenditures pursuant to the Government's commitments announced in the Treasurer's and Attorney-General's Joint Press Release of 13 February 1998.

Should you or your officers wish to discuss these matters raised here further or any related matters, please do not hesitate to contact me directly or Peter Morris, Director – Economics and Commerce, who has carriage of this portfolio in the Secretariat, on (02) 6279 3600.

Yours sincerely



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CHIEF EXECUTIVE