Australian Government

# Exploration Development Incentive

Operational details for the Exploration Development Incentive

July 2014

# 1. Introduction

1. The Government has committed to introduce an Exploration Development Incentive to encourage investment in small exploration companies undertaking greenfields mineral exploration in Australia from 1 July 2014.

2. This paper provides more detail on the operation of the Exploration Development Incentive (the Incentive) to provide certainty for small mineral exploration companies and their investors ahead of the release of legislation to give effect to the measure.

3. Interested stakeholders will have an opportunity to provide further input on the design of the Incentive in public consultation on draft legislation and explanatory materials. Additional details on the operation of the measure will be explored at that stage.

4. The paper is organised consistently with the previous discussion paper and addresses:

   - which explorers will be eligible to access the Incentive;
   - how exploration credits can be provided to investors in these companies;
   - what expenditure will be eligible;
   - how the Incentive will be capped; and
   - the treatment of exploration credits.

# 2. Which explorers will be eligible

5. Companies with no taxable income in an income year will be eligible to participate in the Incentive (for that year). To ensure the scheme is confined to junior minerals explorers, the scheme will exclude companies that have commenced resources production and companies connected or affiliated with an entity that has commenced resources production. The scheme will also exclude companies with a substituted accounting period.

6. To ensure the integrity of the scheme and keep compliance costs to a minimum, the Incentive will only be available to disclosing entities under section 111AC of the *Corporations Act 2001*.

7. Consistent with the treatment of tax consolidated groups, the consolidated group will be treated as a single entity for the purposes of the Incentive. This means that eligibility is determined taking into account the activities of the whole group, and exploration credits can be provided to the shareholders of the head company based on expenditure incurred by any member of the group.

8. Participation in the Incentive will be voluntary, eligible companies do not need to participate.

# 3. How exploration credits can be provided to investors

9. Companies participating in the Incentive and providing exploration credits to shareholders will need to make an irrevocable choice whether to provide exploration credits to all shareholders, or only to holders of shares issued after 30 June 2014.

10. Providing companies with a choice to provide exploration credits to all shareholders or to restrict the availability of exploration credits to holders of shares issued after 30 June 2014 will allow them to decide which option best assists them in continuing to explore for new mineral deposits.

11. Whether a company chooses to provide exploration credits to all shareholders or only to holders of shares issued after 30 June 2014, exploration credits will be apportioned on a per share basis.

12. Note that a consequence of only providing exploration credits to holders of shares issued after 30 June 2014 would be that shares issued after 30 June 2014 would need to be traded as a separate class of shares to comply with the requirements of the corporations law.

# 4. What expenditure will be eligible

13. The Incentive will apply to eligible 'greenfields' exploration expenditure incurred in Australia from 1 July 2014.

## 4.1 What is exploration expenditure?

14. Exploration will include geological mapping, geophysical surveys, systematic search for areas containing minerals, except petroleum or quarry materials, and search for minerals by drilling or other means for such minerals within those areas.

15. Only expenditure on exploration for minerals will be eligible for the Incentive. The Incentive will not apply to exploration for:

    - quarry materials;
    - shale oil;
    - petroleum, including coal seam gas, and any naturally occurring hydrocarbon or naturally occurring mixture of hydrocarbons, whether in a gaseous, liquid or solid state; or
    - geothermal energy resources.

16. Expenditure on studies to evaluate the economic feasibility of mining minerals once they have been discovered will be excluded from the Incentive.

## 4.2 How will greenfields exploration be targeted?

17. Eligible exploration expenditure will be that incurred on activities for the purpose of determining the existence, location, extent or quality of a new mineral resource in Australia.

18. Exploration expenditure will exclude any expense related to a mineralisation that has been classified as an Inferred Mineral Resource or higher under the Joint Ore Reserves Committee (JORC) Code 2012 edition, or to a potential or actual extension of a mine.

19. Expenditure must relate to exploration within an Australian onshore exploration tenement. Exploration expenditure on any other mining tenement, including production licences and retention leases, will be excluded, as will offshore exploration expenditure.

# 5. How the Incentive will be capped

20. The cost of the scheme is capped at $100 million. Exploration credits are capped at $25 million for exploration expenditure incurred in 2014-15, $35 million for exploration expenditure incurred in 2015-16 and $40 million for exploration expenditure incurred in 2016-17. Where the cost of the Incentive is less than the cap for any given year, the caps applying to subsequent years will not be adjusted.

21. The Incentive will be capped using an ex-post modulation approach. Companies that choose to participate in the Incentive will notify the Australian Taxation Office after the expenditure year of the lesser of their exploration expenditure and their tax loss from the financial year. The ATO will then advise eligible companies of the proportion of this amount they will be entitled to provide to shareholders as exploration credits. As long as it does not exceed this amount, companies will be able to choose the tax losses to convert into exploration credits at the company tax rate. Further details on the operation of the modulation process will be determined as part of the consultation on draft legislation.

# 6. Treatment of exploration credits

22. Following modulation, a company that wishes to provide exploration credits to its shareholders will reduce its tax loss that it may carry forward by the amount it wishes to provide to shareholders. The company will then calculate the total credits by multiplying the reduction in losses by the corporate tax rate and provide these exploration credits to its shareholders. Exploration credits must be distributed by the end of the financial year in which modulation occurred.

23. Australian resident shareholders will be entitled to refundable tax offsets equal to the exploration credits they receive. These will be claimed in their tax returns for the year they receive the exploration credits. Although foreign resident shareholders will receive exploration credits, they will not be able to use them. Likewise, as with franking credits, most exempt entities that receive exploration credits will not be able to use them. In calculating the modulation factor, the ATO will not make an allowance for the exploration credits that go to

ineligible claimants as this cannot be known with certainty. Further consideration is being given to the tax treatment of these offsets.

24. Exploration credits will flow through trusts and partnerships in a manner consistent with the rules applying to franking credits. Likewise, corporate shareholders will receive similar benefits to those they obtain under the rules that apply to franking credits.