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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

Treasury Laws Amendment (Measures for Consultation) Bill 2023: PRRT deductions cap

EXPOSURE DRAFT EXPLANATORY MATERIALS

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# Glossary

This Explanatory Memorandum uses the following abbreviations and acronyms.

|  |  |
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| Abbreviation | Definition |
| ATO | Australian Taxation Office |
| ITAA 1997 | *Income Tax Assessment Act 1997* |
| LNG | Liquefied Natural Gas |
| PRRT | Petroleum Resource Rent Tax |
| PRRTA Act | *Petroleum Resource Rent Tax Assessment Act 1987* |
| TAA 1953 | *Taxation Administration Act 1953* |

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1. PRRT Deductions Cap

## Outline of chapter

* 1. Schedule # to the Bill amends the PRRTA Act to cap the availability of deductible expenditure incurred by a person in relation to a petroleum project for a year of tax. The changes will mean the offshore LNG industry pays more tax sooner.
  2. A person to whom the deductions cap applies will be taken to have a taxable profit of 10 per cent of their assessable receipts derived in relation to the project and the year of tax, with PRRT being payable on this amount of deemed taxable profit. That person will incur denied deductible expenditure in the next financial year.
  3. This Schedule partially implements the Petroleum Resource Rent Tax – Government Response to the Review of the PRRT Gas Transfer Pricing arrangements measure announced in the 2023‑24 Budget.

## Context of amendments

* 1. On 2 November 2018, the former Government announced its final response to the PRRT Review conducted by Michael Callaghan AM PSM (Callaghan Review) in 2017. As part of its response, the former Government asked Treasury to lead a review of the GTP arrangements (Treasury Review), which determine the value of gas for PRRT purposes in integrated LNG projects.
  2. Schedule # implements Recommendation 1c of the Treasury Review to introduce a deductions cap by limiting deductible expenditure to the value of 90 per cent of PRRT assessable receipts in respect of each LNG project in the relevant years of tax.
  3. Currently, PRRT is imposed on the taxable profit of a person in relation to a petroleum project and year of tax. The taxable profit is the amount by which assessable receipts exceed deductible expenditure and transferable exploration expenditure.
  4. The amendments cap the amount of deductible expenditure available in relation to an LNG project and a year of tax to offset assessable receipts derived in respect of that project and year of tax. The effect of the deductions cap is to bring forward PRRT collections from LNG projects, delivering both a timely and fairer return to the Australian public from their natural resources. The measure will provide industry and investors policy certainty to allow the sufficient supply of domestic gas, and will ensure Australia remains a reliable international energy supplier and investment partner.

## Summary of new law

* 1. The deductions cap applies to a person in relation to a petroleum project and a year of tax if:
* the person derives assessable receipts;
* the person has no taxable profit;
* sales gas is produced from the petroleum recovered from the project; and
* the person regularly or consistently enters into arrangements, as a result of which it is intended that the sales gas be wholly or primarily produced into LNG.
  1. Projects are excluded from the deductions cap:
* in the first year of production, or in any of the subsequent seven financial years;
* if a person incurs resource tax or starting base expenditure in the year of tax in relation to the project; and
* if a person has exhausted their deductible expenditure in relation to the project.
  1. When the deductions cap applies, the person will be taken to have a taxable profit of 10 per cent of the assessable receipts they derived in relation to the project and the year of tax (the denied deduction amount). A person has an alternative taxable profit calculation if they have an interest in a Greater Sunrise project.
  2. If, in relation to a petroleum project and a year of tax, the deductible expenditure incurred by a person exceeds the assessable receipts derived by the person in relation to the project and year of tax, that person will be taken to incur an augmented denied deductible expenditure amount in relation to the project on the first day of the next financial year.
  3. The denied deduction amount will be 10 per cent of the assessable receipts derived by the person in relation to the project in the financial year, uplifted by the Government long-term bond rate. Augmented denied deductible expenditure can be carried forward indefinitely.
  4. From 1 July 2024, the deductions cap will apply to a person in relation to a project or a Greater Sunrise project as part of the PRRT instalment regime.

## Detailed explanation of new law

#### Taxable Profit

* 1. The deductions cap applies to a person in relation to a petroleum project and a year of tax if:
* the person derives assessable receipts;
* the person has no taxable profit;
* sales gas is produced from the petroleum recovered from the project; and
* the person regularly or consistently carries out arrangements, as a result of which it is intended that the sales gas be wholly or primarily produced into LNG.  
  ***[Schedule #, item 1, subsection 22(3) of the PRRTA Act]***
  1. Projects are excluded from the deductions cap:
* in the first year of production, or in any of the subsequent seven financial years;
* if a person incurs resource tax or starting base expenditure in the year of tax in relation to the project; and
* if a person has exhausted their deductible expenditure in relation to the project.  
  ***[Schedule #, item 1, subsection 22(5) of the PRRTA Act]***
  1. Closing-down expenditure is expenditure incurred in closing-down a petroleum project. If, in relation to a project and year of tax, a person incurs closing-down expenditure, that person will generally not derive assessable receipts. Therefore, as the deductions cap does not apply to a person who does not derive assessable receipts in relation to a petroleum project and a year of tax, the deductions cap will generally not apply to a person who incurs closing-down expenditure in relation to a project and year of tax.
  2. In relation to a project and a year of tax, if a taxpayer has no taxable profit because the deductible expenditure incurred by the person exceeds the assessable receipts derived by the person, the person is taken to have a taxable profit in relation to the project and the year of tax. This deemed taxable profit is 10 per cent of the assessable receipts derived by the person in relation to the project in the year of tax. This is the denied deduction amount. This amount is equal to the amount of deductions that are taken to have been denied in order to produce the resulting deemed taxable profit.  
     [Schedule #, item 1, paragraph 22(f)-(g) of the PRRTA Act]
  3. For a Greater Sunrise projects, an alternative calculation is required. Where a person has no taxable profit in relation to a Greater Sunrise project under the existing taxable profit calculations in a year of tax, that person is taken to have a taxable profit. This deemed taxable profit, equal to 10 per cent of the assessable receipts derived by a person from a Greater Sunrise project, is multiplied by an apportionment percentage figure. The resulting amount is the denied deduction amount. For these purposes, the apportionment percentage figure has the meaning given by section 2C of the PRRTA Act.   
     [Schedule #, item 1, subsection 22(4) of the PRRTA Act]

#### Augmented denied deductible expenditure

* 1. If, in relation to a project and a year of tax, a person has a denied deduction amount, the person is taken to incur augmented denied deductible expenditure on the first day of the next financial year.  
     [Schedule #, item 3, subsection 35F(2) of the PRRTA Act]
  2. In relation to a project and year of tax, the denied deduction amount is 10 per cent of the assessable receipts derived by the person. The denied deduction amount is uplifted by the long-term bond rate plus 1. The uplifted denied deduction amount is taken to be incurred on the first day of the next financial year as augmented denied deductible expenditure.  
     [Schedule #, items 1 and 3, subsections 22(3) and 35F(2) of the PRRTA Act]
  3. Additionally, augmented denied deductible expenditure incurred by a person in relation to a project and financial year includes amounts transferred under Division 5 of Part V of the PRRTA Act, which deals with the transfer of entitlements to assessable receipts.  
     [Schedule #, item 3, subsection 35F(1) of the PRRTA Act]
  4. In relation to a project and year of tax, if a person has a denied deduction amount, then the sum of deductible expenditure incurred by the person and transferable exploration expenditure will exceed the assessable receipts derived by the person. So much of this excess as does not exceed the sum of the augmented denied deductible expenditure and the denied deduction amount is uplifted by the long-term bond rate plus 1 and incurred as augmented denied deductible expenditure on the first day of the next financial year.  
     [Schedule #, item 3, subsection 35F(2) of the PRRTA Act]
  5. The augmented denied deductible expenditure rules operate in relation to combined projects in the same way as they do for single projects, except for the financial year in which the project combination certificate in relation to the project comes into force. For that year, denied deductible expenditure however incurred by pre-combination projects in the financial year is included in the sum of denied deductible expenditure for the combined project.  
     [Schedule #, item 3, subsection 35F(1) of the PRRTA Act]

##### Exclusions

* 1. There are various projects that do not fall within the scope of the deductions cap.
  2. Projects are excluded from the operation of the deductions cap in a year of tax if that year is when the person first derives assessable petroleum receipts in relation to the project, or if it is one of the subsequent seven financial years. This exclusion is designed to minimise the impacts of the substantial upfront payments on project economics.   
     ***[Schedule #, item 1, paragraphs 22(3)(g) and 22(5)(a) of the PRRTA Act]***
  3. Projects are also excluded from the deductions cap if a person incurs resource tax expenditure or starting base expenditure in relation to the project and the year of tax.   
     [Schedule #, item 1, paragraph 22(5)(b) of the PRRTA Act]
  4. Projects are also excluded from the deductions cap once a person has exhausted their deductible expenditure. This includes where amounts have been transferred to other projects.   
     [Schedule #, item 1, paragraph 22(5)(c) of the PRRTA Act]

#### Instalments

* 1. PRRT liability taken to be incurred as a result of the deductions cap is to be paid in instalments. Such instalments apply to all persons who, in relation to a project, expect to have a taxable profit under subsections 22(3) or (4) in a year of tax.  
     [Schedule #, items 4-7, subsection 97(1BA) of the PRRTA Act]
  2. In relation to a project and instalment period, a person’s notional tax amount is calculated as the current period receipts less previous period receipts, all multiplied by 0.1   
     [Schedule #, item 5, subsection 97(1BA) of the PRRTA Act]
  3. Current period receipts, for projects that are not a Greater Sunrise project, are the assessable receipts derived by a person in relation to the project and the instalment period.  
     [Schedule #, item 5, subsection 97(1BA) of the PRRTA Act]
  4. Current period receipts for the Greater Sunrise project are the assessable receipts derived by a person in relation to the project and the instalment period multiplied by the current apportionment percentage that applied during that period.  
     [Schedule #, item 5, subsection 97(1BA) of the PRRTA Act]
  5. Previous period receipts, for projects that are not a Greater Sunrise project, are the sum assessable receipts derived by a person in relation to the project in any earlier instalment periods in that year.  
     [Schedule #, item 5, subsection 97(1BA) of the PRRTA Act]
  6. Previous period receipts for the Greater Sunrise project are the sum of assessable receipts derived by a person in relation to the project in any earlier instalment periods in that year multiplied by the current apportionment percentage that applied during that period.  
     [Schedule #, item 5, subsection 97(1BA) of the PRRTA Act]
  7. The PRRT instalment regime, as it relates to the deductions cap, will apply to a person in relation a project, or a Greater Sunrise project, and in relation to a year of tax beginning on or after 1 July 2024.   
     [Schedule #, item 16]

## Consequential amendments

* 1. Schedule # makes a number of consequential amendments to Schedule 1 to the PRRTA Act.
  2. The definition of notional taxable profit is amended to give effect to the amendments in the schedule.  
     [Schedule #, items 8-15, clauses 5, 9, 14, 19 and 27 of Schedule 1 to the PRRTA Act]
  3. The Commissioner may determine the notional tax amount of a person in an instalment period in accordance with the general formula or determination.  
     [Schedule #, item 7, subsection 97(2) of the PRRTA Act]
  4. Changes have been made to Schedule 1 so that denied deductible expenditure cannot be transferred under sections 45A or 45B.  
     [Schedule #, items 12 and 13, clause 14 of Schedule 1 to the PRRTA Act]

## Commencement, application, and transitional provisions

* 1. The amendments commence on the first 1 January, 1 April, 1 July or 1 October to occur after the day the Act receives the Royal Assent.
  2. The amendments to the PRRTA Act made by this Schedule apply in relation to assessable receipts derived by a person in relation to a project, or a Greater Sunrise project, and in relation to a year of tax beginning on or after 1 July 2023, whether or not assessable receipts were also derived by a person in relation to the project and an earlier year of tax.  
     [Schedule #, item 16]
  3. Instalment provisions, as they relate to the deductions cap, apply if a person expects to have a deemed taxable profit in relation to a project and financial year. These instalment provisions apply in relation to a petroleum project and in relation to a year of tax beginning on or after 1 July 2024.  
     [Schedule #, item 16]