



***TR 2010/D5 - Petroleum resource rent tax: excluded expenditure under paragraphs 44(j) and 44(k) of the Petroleum Resource Rent Tax Assessment Act 1987 - administrative, accounting, wages, salary, other work costs, and overhead expenditure; land or buildings for use in accounting or administration not adjacent to the operations site***

 This cover sheet is provided for information only. It does not form part of *TR 2010/D5 - Petroleum resource rent tax: excluded expenditure under paragraphs 44(j) and 44(k) of the Petroleum Resource Rent Tax Assessment Act 1987 - administrative, accounting, wages, salary, other work costs, and overhead expenditure; land or buildings for use in accounting or administration not adjacent to the operations site*

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There is a [Withdrawal notice](#) for this document.

 This ruling is being reviewed as a result of a recent court/tribunal decision. Refer to Decision Impact Statement: [Esso Australia Resources Pty Ltd v Commissioner of Taxation \(Published 5 October 2012\)](#).



## Draft Taxation Ruling

Petroleum resource rent tax: excluded expenditure under paragraphs 44(j) and 44(k) of the *Petroleum Resource Rent Tax Assessment Act 1987* – administrative, accounting, wages, salary, other work costs, and overhead expenditure; land or buildings for use in accounting or administration not adjacent to the operations site

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## What this Ruling is about

1. This draft Ruling explains aspects of deductibility of certain expenditure under the *Petroleum Resource Rent Tax Assessment Act 1987* (PRRTAA). Expenditure incurred by a person may be eligible real expenditure under sections 37, 38 and 39 of the PRRTAA provided it is not excluded expenditure as defined in section 44 of the PRRTAA. Excluded expenditure under paragraphs 44(j) and 44(k) of the PRRTAA covers certain types of administrative, accounting and overhead expenditure and is considered in this draft Ruling. Excluded expenditure cannot give rise to deductible expenditure or transferred expenditure, which reduces assessable receipts in calculating the taxable profit of a taxpayer for a year of tax in relation to a petroleum project and so the amount of petroleum resource rent tax (PRRT).

2. All references to legislation in this draft Ruling are to the PRRTAA unless otherwise indicated. A reference in this draft Ruling to a taxpayer is a reference to a person with an interest in the assessable receipts of a petroleum project.

## Background

3. PRRT is essentially a tax on a person with 'assessable receipts' from a petroleum project. The PRRTAA taxes the excess of their project 'assessable receipts' over their project 'deductible expenditure' and the expenditure transferred to that project from another project of the person or of the company group of which the person is a member. It allows expenditure on such a project and expenditure eligible to be transferred to the project, each whether of a capital or a revenue nature to be fully recovered, after compounding augmentation, from 'assessable receipts' of the petroleum project before PRRT is payable on any excess, the 'taxable profit'. PRRT is a petroleum project tax not an enterprise tax. A person may be involved in a wider enterprise than the petroleum project, and even in relation to the petroleum project may incur expenditure and derive income for income tax purposes (or may include accounting assets and liabilities for accounting purposes) that do not relate to deductible expenditure or assessable receipts under the PRRTAA.

4. To be deductible expenditure or transferred expenditure, expenditure must derive from amounts liable to be paid in carrying on or providing particular operations, facilities and other things (such as things specified as making up the petroleum project or otherwise specified in the PRRTAA), and the expenditure must not be 'excluded expenditure'. In some circumstances exploration expenditure can and so must be transferred to another petroleum project of the same taxpayer or a petroleum project of a member of the same company group as the taxpayer.

5. Draft Taxation Ruling TR 2010/D4 Petroleum resource rent tax: general pre-conditions common to deductibility of expenditure of a kind referred to in sections 37, 38 and 39 of the *Petroleum Resource Rent Tax Assessment Act 1987*, states certain pre-conditions to there being eligible real expenditure, whether by way of exploration expenditure, general project expenditure or closing-down expenditure, from which any deductible expenditure or transferred expenditure taken into account in determining the amount of PRRT must derive. TR 2010/D4 identifies three general pre-conditions common to and prerequisite to any eligible real expenditure under the PRRTAA. These are that the expenditure must:

- (a) be incurred by the person in relation to a 'petroleum project', as defined;
- (b) be incurred in carrying on or providing operations, facilities or other things of a kind referred to in sections 37, 38 or 39; and
- (c) not be 'excluded expenditure' under section 44.

6. In relation to the third pre-condition to deductibility of expenditure, section 44 defines excluded expenditure by listing the kinds of such expenditure. Specifically excluded from PRRT deductibility are interest payments; repayments of principal; other borrowing costs; dividend payments; share issue costs; private override royalties; equity capital repayments; income tax payments; fringe benefits tax payments incurred before 1 July 2006; GST payments; payments to get (other than by grant) or to buy into permits, leases, licences or authorities; payments to acquire interests in petroleum project profits, receipts or expenditures; and certain other expenditure referred to in paragraphs 44(j) and 44(k).

7. This draft Ruling is concerned with payments referred to in paragraphs 44(j) and 44(k). These are:

- (j) payments of administrative or accounting costs, or of wages, salary or other work costs, incurred indirectly in carrying on or providing operations, facilities or other things of a kind referred to in sections 37, 38 and 39; or
- (k) payments in respect of land or buildings for use in connection with administrative or accounting activities in respect of the carrying on or provision of other operations, facilities or things of a kind referred to in sections 37, 38 and 39, not being land or buildings located at or adjacent to the site or sites at which those other operations, facilities or things are carried on or provided.

8. This draft Ruling concerns some circumstances when payments of administrative or accounting costs, or of wages, salary or other work costs, and payments in respect of land or buildings for use in connection with administrative or accounting activities, will be eligible real expenditure giving rise to deductible expenditure or to transferred expenditure and when they will constitute excluded expenditure identified by paragraphs 44(j) and 44(k).

9. A reference to 'eligible real expenditure' is a reference to all exploration expenditure, general project expenditure or closing-down expenditure pursuant to sections 37, 38 and 39 respectively (section 2).<sup>1</sup> Deductible expenditure and transferred expenditure, deducted from assessable receipts in working out PRRT liability, can only derive from eligible real expenditure of some kind.

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<sup>1</sup> Deductible expenditure arising from bad debts of amounts included in assessable receipts (section 40) is also classified as exploration expenditure, general project expenditure or closing-down expenditure depending on when the debt is written off. For the purposes of this draft Ruling, deductible expenditure arising from bad debts has been ignored.

## Ruling

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### **Paragraph 44(j) – administrative and accounting costs and wages, salary and other work costs**

10. Administrative or accounting costs or wages, salary and other work costs are incurred indirectly in carrying on or providing petroleum project operations, facilities and other things of the kinds referred to in sections 37, 38 or 39 only so far as they are not directly incurred for such operations, facilities or other things or are not for work performed directly in carrying on or providing such operations, facilities or other things. Such costs are excluded expenditure and cannot be eligible real expenditure giving rise to deductible expenditure or to transferred expenditure.

11. Any payment of administrative or accounting costs that is incurred indirectly, and any payment of wages, salary or other work costs that is incurred indirectly, are excluded expenditure under paragraph 44(j). In other words, paragraph 44(j) excludes an item of expenditure if that item is incurred indirectly and it is:

- a payment of an administrative or accounting cost; or
- a payment of wages, salary or other work cost.

### ***Indirectly incurred***

12. Expenditure is indirectly incurred unless it is directly ascertainable and directly attributable in some way only to carrying on or providing the operations, facilities and other things of a kind referred to in sections 37, 38 or 39. This requires attribution in some specific rather than some general or notional way. Expenditure which serves two or more objects indifferently is incurred only indirectly for any of those objects. If any of those objects is other than carrying on or providing those operations, facilities and other things, the expenditure is incurred only indirectly in carrying on or providing such things (if all objects served indifferently are themselves in carrying on or providing such things, then the expenditure is incurred directly in carrying on or providing such things though only indirectly incurred in relation to any particular one among them).

13. If one part of an administrative or accounting cost or of a wage, salary or other work cost is incurred indirectly, and another part of the cost is incurred directly, only the part that is incurred indirectly is excluded expenditure under paragraph 44(j). However, so far as a cost is both in carrying on or providing operations, facilities or other things of a kind referred to in sections 37, 38 or 39 and also for other purposes, so that it is incurred indifferently for each, that cost is incurred only indirectly in carrying on or providing the petroleum project operations, facilities or other things that it is for in combination with the other things. To that extent, the cost is excluded expenditure and cannot be eligible real expenditure which can give rise to deductible expenditure or transferred expenditure.

***Administrative and accounting costs***

14. Administrative costs related to a petroleum project include costs attributable to the management or direction of an office or employment connected with the petroleum project and costs attributable to the control and management of the project itself. Such costs include costs of the administrative framework for controlling and resourcing the carrying on and providing of project operations, facilities or other things. Accounting costs include costs of accounting for any aspect of project operations, facilities or other things. So far as accounting or administration are for other things, such as income tax liability, profit reporting to shareholders, or capital raising (whether by way of debt or equity), the accounting or administration is not for things of kinds referred to in sections 37, 38 or 39 and cannot be included in eligible real expenditure in any event.

15. Administrative costs include such costs as insurance costs (including premiums), external audit and compliance verification costs, and bank charges, as well as such costs as joint venture agreement management, internal audit and control, postage, telephone and publications, computer software and hardware, and general strategic and business planning and management.

***Wages, salary and other work costs***

16. Wages, salary and other work costs include costs of the provision of work by contract of service. They also include costs of services under contracts for services, including payments made to contractors for results of work done, if the principal contribution of the contractor in providing the service is by way of the provision of labour and of skills applied.

17. The 'other work costs' also include on-costs incurred in relation to the supply of labour and skills. For example, payroll tax, payment of superannuation, performance and end of contract bonuses, payment of wages or salary for a period when an employee is on leave, the cost of providing fringe benefits to an employee and the fringe benefits tax payable on them are all 'other work costs'.

18. If leave according to a period of service is taken, it relates directly to the work of the employee over the relevant period of service. So far as there are times in that period when the employee worked only in carrying on or providing relevant petroleum project operations, facilities or other things, the leave will not be incurred indirectly in doing so to that extent. If the leave does not exhaust entitlement for a period of past service, the period of service may be considered as a whole, or a sufficient part of the period may be determined consistently for all employees (such as 'first in first out', 'last in first out', or a combined period taking account of the past service of all members of a relevant group on the basis that all leave by those who are not members of that group will be regarded as incurred only indirectly).

19. Payroll tax is incurred directly (that is, not incurred indirectly) so far as the payroll tax base was expenditure for work done solely in carrying on or providing the relevant petroleum project operations, facilities or other things. Any applicable payroll tax threshold or lower rate step, where this does not apply only to payroll for particular activities, does not affect the identification of the part of the payroll tax that is incurred directly.

## **Paragraph 44(k) – land or buildings for use in connection with administrative or accounting activities**

20. Payments in respect of land or buildings for use in connection with administrative or accounting activities in respect of the carrying on or provision of operations, facilities or other things of a kind referred to in sections 37, 38 or 39 for the petroleum project may give rise to eligible real expenditure so far as those operations, facilities or other things are carried on or provided at or adjacent to the site of the land or buildings. So far as the operations, facilities or other things, the subject of the administrative or accounting activities in connection with which the land or buildings are provided, are not at or adjacent to the land or buildings, payments in respect of the land or buildings are excluded expenditure under paragraph 44(k).

21. Payments are in respect of land or buildings whether they are of a revenue or a capital nature. The land or buildings are for use in connection with administrative or accounting activities whether these occur when the payments are made or are expected or contemplated, whether immediately or after an intervening period.

22. In the context of paragraph 44(k), 'adjacent' should be taken to mean the nearest practicable location for land or buildings where administrative or accounting activities in relation to the operations, facilities or other things administered or accounted for may be carried on or provided (land or buildings further away cannot be adjacent, if other land or buildings could practicably be closer to the operations, facilities or other things administered or accounted for). That nearest practical location may be on a floating platform, an island or mainland Australia depending on the characteristics of the operations, facilities or other things subject to the administrative or accounting activities. So what is the location, or the nearest practical location, must be worked out having regard to the characteristics of the particular petroleum project.

23. For payments in respect of land or buildings that are on or adjacent to the site of the operations, facilities or other things and that are in connection with administration or accounting so that they are not excluded expenditure under paragraph 44(k), to constitute eligible real expenditure in relation to a petroleum project, they must also satisfy the other conditions for deductibility. Those other conditions for deductibility include the requirement under paragraph 44(j) that the payments are directly incurred in carrying on or providing the operations, facilities or other things of a kind referred to in sections 37, 38 and 39.

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## Examples

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### **Example 1 – Other work costs of employees engaged on a petroleum project**

24. A company provides board and lodgings to employees and their families at a petroleum project operations site. The lodgings include entertainment facilities such as television, DVD player and access to the internet and Pay-TV. Do the costs of providing the entertainment facilities give rise to eligible real expenditure of the petroleum project?

25. For a cost incurred by the company to give rise to eligible real expenditure, it must be incurred by the company (or deemed to have been incurred by the company by the application of section 41) in carrying on or providing operations, facilities or other things referred to in sections 37, 38 or 39 and its payment must not be excluded expenditure under section 44. The costs incurred in providing entertainment facilities for the employees and their families at the operations site may give rise to eligible real expenditure of the petroleum project as these facilities may constitute employee amenities as defined in section 2; and providing such employee amenities is part of the operations, facilities or other things which comprise the petroleum project (subparagraph 19(4)(b)(v)). If the costs of the entertainment facilities are administrative or work costs, they are still incurred directly in providing employee amenities because they are entertainment facilities included in those employee amenities themselves.

26. Compare the cost of similar entertainment facilities provided, not in the lodgings, but in a general community facility available alike to community members not working on the petroleum project and to any petroleum project employees and their families boarded in the lodgings who choose to go to the community facility. In that case some of the benefit of the entertainment facilities may be to employees and their families, and in that sense the cost of the entertainment facilities is incurred in providing employee amenities. But the costs are incurred only indirectly in doing so. The costs are incurred in relation to the petroleum project employees only to the indirect extent that the facilities are actually made use of by employees and their families. Therefore, these costs are excluded expenditure under paragraph 44(j).

### **Example 2 – Computer hardware and software**

27. A company has incurred expenditure on upgrading computer hardware and software at its operations sites, site offices and the head office. Can the expenditure be excluded expenditure and if so to what extent?



28. Hardware and software may be used for carrying on or providing the operations, facilities and other things that comprise the petroleum project, or that are otherwise within sections 37, 38 or 39. Its cost may give rise to eligible real expenditure only to that extent.

29. If hardware or software is used for administrative or accounting purposes in connection with the petroleum project, then to that extent its cost is administrative or accounting expenditure and if the cost is incurred indirectly it is excluded expenditure under paragraph 44(j). If such hardware or software is only for purposes that serve several objectives indifferently, only some of which are in carrying on or providing petroleum project things listed in sections 37, 38 or 39, then to that extent the expenditure cannot give rise to eligible real expenditure as there is no identifiable part of the expenditure that is incurred solely in carrying on or providing those petroleum project things and so the expenditure is administrative expenditure incurred indirectly and is excluded expenditure under paragraph 44(j).

### **Example 3 – Sole enterprise costs**

30. A company holds an interest only in one petroleum project and the project is generating assessable petroleum receipts for the company in the year of tax. The company incurred expenditure including the following:

- (a) fees paid for external audit of financial accounts;
- (b) salary and wages for time spent by staff on corporate reporting requirements;
- (c) membership fee of an association of petroleum industry companies;
- (d) fees paid for the directors of the company to attend meetings of the industry association and payment for the purchase of general publications from the association;
- (e) directors' fees for meetings of the company's board of directors;
- (f) newspapers and magazines purchased for the head office;
- (g) reimbursements made to directors for costs incurred by them in attending board meetings and expenditure on meals provided to those attending such meetings;
- (h) audit fees to external auditors for ensuring that the company complies with the Sarbanes-Oxley legislation (a concern because its parent company is incorporated in the United States of America);

- (i) accounting fees for the preparation of income tax, fringe benefits tax, and superannuation guarantee statements and returns including Business Activity Statements (BAS) and annual returns and statements; and
- (j) accounting fees for the preparation of PRRT instalment statements and PRRT annual return.

31. The company's operations, and so all the expenditures listed in paragraph 30 of this draft Ruling, are related in some way to its petroleum project interest, which generates the assessable receipts for PRRT purposes and also the gross income for income tax and for accounting purposes. Are the above expenditures therefore eligible real expenditure?

32. The excluded expenditure provisions of paragraph 44(j) apply to each of the particular expenditures so that they are precluded from being eligible real expenditure to any extent. The more general requirements discussed in TR 2010/D4 may mean that particular expenditures listed in paragraph 30 of this draft Ruling are not (or are to some extent not) in any event capable of being part of eligible real expenditure from which deductible expenditure and transferred expenditure derive.

33. All of the above expenditure is excluded expenditure so far as it might otherwise be eligible real expenditure. All of the above expenditure is of one or another kind to which paragraph 44(j) applies. All of the above expenditure, even if incurred in carrying on or providing operations, facilities or other things of a kind referred to in sections 37, 38 or 39, is incurred only indirectly. None was incurred directly in carrying on or providing the operations, facilities or other things comprising the petroleum project.

34. External audit of financial accounts, audit fees for Sarbanes-Oxley compliance and assurance, fees for income tax, fringe benefit tax (FBT) and superannuation requirements, and fees for PRRT instalment statements and annual returns are each 'payments of ... accounting costs ... incurred indirectly'. These costs cannot ordinarily be directly identified to any extent with any particular operations, facilities or other things of a kind referred to in sections 37, 38 or 39 that are carried on or provided. They would otherwise be excluded expenditure under paragraph 44(j).

35. Corporate reporting requirements are for administrative processes that are mandated by corporations law. Their cost is an administrative cost which cannot be directly identified to any extent solely with any particular operations, facilities or other things of a kind referred to in sections 37, 38 or 39 that are carried on or provided. So their costs are 'payments of administrative ... costs ... incurred indirectly' and they are excluded expenditure under paragraph 44(j).

36. The costs of association membership, association meetings and association publications, and the costs of head office newspapers and magazines, are for administrative benefits chosen by the company. Their cost is an administrative cost which cannot be directly identified to any extent as solely in any particular operations, facilities or other things of a kind referred to in sections 37, 38 or 39 that are carried on or provided. So the costs are 'payments of administrative ... costs ... incurred indirectly' and they are excluded expenditure under paragraph 44(j).

37. The costs of board meetings and of directors' board meeting expenses and board meeting meals are administrative costs of the general administration and accounting of the company. Some things must be done by directors in a properly constituted meeting; board meetings are a proper way of constituting required meetings for such things, and also provide an appropriate way of making decisions for which a board meeting is not the only possible administrative option too. The costs are administrative or accounting costs which cannot be directly identified to any extent solely with any particular operations, facilities or other things of a kind referred to in sections 37, 38 or 39 that are carried on or provided. So the costs are 'payments of administrative or accounting costs ... incurred indirectly' and they are excluded expenditure under paragraph 44(j).

#### **Example 4 – Insurance premium for workers' compensation insurance**

38. A company shares in product from three production licences, gets assessable receipts from the product and maintains one workers' compensation insurance policy for all staff working across the three petroleum projects. Can the company apportion the insurance premium among the three petroleum projects as in part eligible real expenditure on one or another of them?

39. To the extent that payments for the insurance premium are incurred in carrying on or providing the operations, facilities and other things the cost of which is eligible real expenditure for a particular petroleum project, they may be eligible real expenditure which will give rise to deductible expenditure of that petroleum project.

40. So far as they are administrative or work costs incurred indirectly, the payments would be excluded expenditure. The proportion of the insurance premium that is incurred indirectly in relation to a petroleum project will usually depend on the basis on which the premium is charged. This reflects the variables used by the insurance company to evaluate the risk. For example, suppose the insurance premium for workers' compensation is calculated on the annual payroll of the company, irrespective of the job description or age of any particular employee, and without a differential rate for different projects. The part of the insurance premium that is incurred directly on each petroleum project can be identified by identifying the part of the payroll on which the premium is solely based that is eligible real expenditure as salary and wages for work in carrying on or providing relevant operations, facilities or other things for each petroleum project as a proportion of the total salary and wages expenditure which is the basis of the premium. That part of the insurance premium is directly incurred and is eligible real expenditure of each petroleum project.

41. Workers' compensation premiums are both administrative costs and other work costs. If there is no reasonable basis for establishing directly a part of the insurance premium that is solely for such work, there may be no way to identify any part of the premium as incurred directly (that is, not incurred indirectly) in carrying on or providing operations, facilities or other things of a kind referred to in sections 37, 38 or 39 for one or another petroleum project.

#### **Example 5 – Christmas function at petroleum project site**

42. A company incurs a cost of holding a Christmas function at the petroleum project operations site. The function is attended by a mix of staff, some wholly and some partly engaged in carrying on the operations, facilities and other things comprising the petroleum project, and some staff not engaged on the petroleum project at all. To what extent can the expenditure incurred on the Christmas function give rise to eligible real expenditure?

43. As a staff work-cost, a proportion of the Christmas function cost is directly incurred in carrying on or providing the operations, facilities and other things the staff carry on or provide and may give rise to eligible real expenditure in proportion to the share of staff work time spent in carrying on or providing operations, facilities or other things the cost of which is eligible real expenditure of the petroleum project. The Commissioner will accept a reasonable part of the Christmas function cost accordingly.<sup>2</sup>

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<sup>2</sup> For example, the taxpayer might work out the part of the cost based on the part of employee time spent in carrying on or providing such things for the petroleum project for a reasonable period preceding the Christmas function. In some circumstances, the taxpayer might identify the way employee time is to be spent following the Christmas function, such as in relation to staff joining the petroleum project at or around the time of the function.

44. The Christmas function cost is both an administrative cost and other work cost. If the time of staff spent solely in carrying on or providing relevant petroleum project operations, facilities or other things cannot be ascertained, the cost of the function is incurred only indirectly. The cost cannot be identified as incurred directly in carrying on or providing any particular petroleum project operations, facilities or other things of kinds identified in sections 37, 38 or 39. The cost is therefore administrative expenditure incurred only indirectly. So the cost of the Christmas function is 'administrative costs ... incurred indirectly', is excluded expenditure under paragraph 44(j), and cannot constitute eligible real expenditure giving rise to deductible expenditure or to transferred expenditure.

### **Example 6 – Redundancy costs**

45. A company that is in the process of closing-down a petroleum project has offered redundancy payments to staff engaged in that project. Do the redundancy payments give rise to eligible real expenditure in relation to that project?

46. Redundancy costs are expenditure that is generally incurred indifferently in carrying on operations, facilities and other things comprising the petroleum project and on other non-project activities. However, the Commissioner will allow redundancy costs to be treated as giving rise to eligible real expenditure to the extent that they are for the employees for whom they are payable being engaged in carrying on or providing petroleum project operations, facilities or other things of a kind referred to in sections 37, 38 or 39. There must be an ascertainable and direct basis to attribute a proportion of the redundancy payments to the extent an employee is at least partly engaged in carrying on such operations, facilities and other things.

47. To the extent that an employee's work to that time has been directly in carrying on or providing operations, facilities or other things in relation to the petroleum project the cost of which is eligible real expenditure, the corresponding share of redundancy costs may be deductible on the same basis. It is among 'work costs' but it is incurred directly (that is, not incurred indirectly) and so is not excluded expenditure under paragraph 44(j) to that extent.

### **Example 7 – Relocation costs**

48. A company with two petroleum projects in different locations is closing-down one project. Staff are offered employment in the second petroleum project of the company and the company reimburses their relocation costs up to a certain limit. Does the reimbursement give rise to eligible real expenditure? If relocation costs do give rise to eligible real expenditure, against which petroleum project are they eligible real expenditure?

49. The treatment of relocation costs is similar to the treatment of redundancy costs. As in Example 6 of this draft Ruling, the Commissioner will allow relocation costs to be treated as giving rise to eligible real expenditure to the extent they can be attributed as direct costs to the carrying on the petroleum project. The basis on which relocation costs may be paid varies widely. Suppose relocation costs are paid on the basis that the employee is to work on the second petroleum project. Suppose there are other features relating the costs to work actually carried out on the second project: for instance, repayment or part repayment if the employee stops working on the second project within a period. In such circumstances, even if relocation is offered only to employees on the second project who had been employed on the first, the cost of relocation is only for employees on the second project. To the extent that such an employee's work is to be directly in carrying on or providing operations, facilities or other things in relation to the second project the cost of which is eligible real expenditure, that share of the relocation costs may be incurred directly in carrying on or providing the operations, facilities or other things which the employee is engaged in carrying on or providing over the relevant repayment period, and be eligible real expenditure on the same basis.

50. Relocation costs that are not paid according to a period of intended work, by way of a minimum qualifying period or otherwise, may arise in such a way that even if they are for relocation to work on the second petroleum project they are work costs incurred only indirectly in relation to that project. The particular circumstances and arrangements need to be considered. The question is whether and to what extent, in the circumstances, relocation costs are paid as a direct part of having a relocated employee work on carrying on or providing second project operations, facilities or other things of a kind referred to in sections 37, 38 or 39. If the basis of the payment is such that there is no clear expectation of a period within which the share of work on such things could then be examined, or if the expectation is of work in an overall enterprise but not to any particular extent of work in carrying on or providing such things, there may be no basis on which any part of the relocation costs could be taken to be incurred directly in the second petroleum project.

51. Suppose instead that relocation costs are to be paid in relation to employees who move for work, whether the work to which they move is with the same company or not. In such circumstances, even if relocation costs are paid in relation to an employee who is to work on the second petroleum project, the costs have no relationship to that project any more than to any other work the employee could have moved to take up. The costs then relate rather to the first petroleum project, to the extent that the work done by the employee in carrying on or providing first project operations, facilities or other things of a kind referred to in sections 37, 38 or 39 was part of the work by which eligibility for the relocation costs arose. The relocation costs would be directly incurred so far as they were based on employment directly in carrying on or providing such things.

## **Example 8 – Relocation cost of a new employee**

52. A company has agreed to pay the relocation costs to Australia of an engineer it has engaged to work. That work will be to some extent on a petroleum project. Do the relocation costs give rise to eligible real expenditure?

53. As in Example 7 of this draft Ruling, relocation costs give rise to eligible real expenditure to the extent they are incurred directly as a cost of the part of the work time spent directly by the employee in carrying on the operations, facilities or other things for the petroleum project of kinds referred to in sections 37, 38 or 39. There must be an ascertainable and correct basis to attribute directly a proportion of the relocation payments if the employee is not to be wholly and directly engaged in carrying on or providing such operations, facilities and other things of the petroleum project. If there is an ascertainable basis to directly attribute a proportion of the payment to carrying on or providing the operations, facilities or other things of the project, that proportion will constitute eligible real expenditure.

## **Example 9 – Expenditure incurred in carrying on the petroleum project as well as other things**

54. A joint venture owns and operates an eligible production licence from the area of which petroleum is recovered. The company also owns and operates the processing facilities for the production of liquefied natural gas (LNG) from the petroleum recovered from the production licence area. Expenditure is incurred on administrative activities which relate to all joint venture processes from recovery of petroleum to its processing into marketable petroleum commodities (MPC) including sales gas, liquefaction of the sales gas into petroleum products including LNG, and their loading and shipping to purchasers. Does any part of the administrative expenditure constitute eligible real expenditure of the joint venture members?

55. Once sales gas (an MPC) becomes an excluded commodity after being produced by being sent for further processing in the joint venture's liquefaction operations, all of the further costs of liquefying the sales gas and producing the LNG (the downstream activities) are not part of the eligible real expenditure of the petroleum project for PRRT purposes, and the value added by those downstream activities does not give rise to assessable receipts for PRRT purposes either.

56. For the administrative expenses to constitute eligible real expenditure of the petroleum project, they must not be indirectly incurred in carrying on or providing those operations, facilities or other things for the petroleum project the cost of which is eligible real expenditure of a kind identified by sections 37, 38 or 39. If the part of the administrative expenditure that was incurred directly in carrying on or providing such activities for the petroleum project is able to be ascertained (for example, by identifying the underlying part of what is administered that itself is in carrying on or providing such things and identifying the part of the administration that is solely in relation to it) that part of the administrative expenditure will not be indirectly incurred in carrying on or providing those things. Only that part of the administrative expenditure will be eligible real expenditure.

57. If no part of the expenditure can be identified as incurred directly, because there is no basis on which the part of the administrative expenditure that is solely for other activities themselves in carrying on or providing the relevant things can be identified, the expenditure will be 'administrative ... costs ... incurred indirectly' and will be excluded expenditure under paragraph 44(j).

#### **Example 10 – Visits by parent company officers/visits to parent company office**

58. An Australian company is a subsidiary of an overseas parent company. From time to time senior officials and technical officers from the parent company visit Australia to oversee the operations of the Australian company, discuss the running of the business and the current and proposed petroleum projects of the Australian company, review exploration activities being conducted by the company and meet government officials to discuss the proposed activities of the company. The directors, the Chief Executive Officer and technical officers of the Australian company also go overseas from time to time to brief parent company officers on current and proposed activities as well as to negotiate with overseas vendors, buyers and governments regarding possible future dealings with them. The Australian company bears all the costs associated with the travel of the parent company officers to Australia and the travel of its own officers. Can the Australian company apportion the cost of travel by its parent company's officers to Australia or by its own officers among its current petroleum projects?

59. The travel costs are clearly administrative costs to the Australian company and subject to paragraph 44(j). They are incurred both in carrying on or providing such operations, facilities or other things for the petroleum project and also for other purposes (the circumstances of which may not be to any extent incurred in carrying on or providing those operations, facilities or other things; consider in this respect TR 2010/D4), and to this extent they are incurred indifferently for each; therefore the costs are incurred only indirectly in carrying on or providing the petroleum project operations, facilities or other things.



60. At most, the travel costs are excluded expenditure pursuant to paragraph 44(j) and cannot be eligible real expenditure. The travel costs are ‘administrative ... costs ... incurred indirectly’ so far as they are ‘in carrying on or providing operations, facilities or other things of a kind referred to in sections 37, 38 and 39’. Consequently, no part of the travel costs is eligible real expenditure.

#### **Example 11 – Overhead expenditure of a ‘one petroleum project’ company**

61. A company that holds an interest in only one petroleum project maintains a head office in a capital city. The head office employees identify the work time they spend directly in carrying on or providing operations, facilities or other things for the project the cost of which is eligible real expenditure. What of overhead costs?

62. Overhead costs of the head office such as electricity and water charges are incurred indifferently in maintaining the petroleum project and on other corporate matters. They are not costs which relate directly to the work time spent by head office employees and so employee time spent in carrying on or providing different operations, facilities or other things does not identify how much of these overhead costs is incurred directly (that is, not incurred indirectly) for those different operations, facilities or other things.

63. The overhead costs are excluded expenditure (under paragraph 44(j)). If they are incurred at all in carrying on or providing petroleum project operations, facilities or other things of kinds referred to in sections 37, 38 or 39, they are ‘administrative ... costs ... incurred indirectly’ for the purposes of that paragraph. There is no basis on which any part of those costs can be identified as solely in carrying on or providing those things and so the costs are incurred only indirectly. They are administrative costs, being costs of the provision of the general administrative services of the company.

#### **Example 12 – Administration building expenditure**

64. A company with an interest in assessable receipts of a petroleum project does not maintain an administration office at or adjacent to any location at which the petroleum project operations, facilities or other things of the kinds referred to in sections 37, 38 or 39 are carried on. All administration is carried on at the administration building of the company located in the nearest capital city. The company incurs expenditure in respect of that administration building. Does the expenditure incurred in relation to the administration building give rise to eligible real expenditure?

65. The expenditure does not give rise to eligible real expenditure as the administration building is neither on the site nor adjacent to the site where the petroleum project’s operations, facilities and other things administered are being carried on or provided. The expenditure is excluded expenditure under paragraph 44(k).

**Example 13 – Time spent on recruitment of staff**

66. The duties of a Human Resource Manager of a company with an interest in assessable receipts of a petroleum project include selecting candidates to work on the project drilling rig and include attending to the human resource needs of employees while they are engaged on the drilling rig. Is the manager's salary incurred directly in carrying on or providing the operations, facilities or other things comprising the petroleum project?

67. The manager's salary is excluded expenditure to the extent that it is not incurred directly in carrying on or providing operations, facilities and other things of a kind referred to in sections 37, 38 and 39. So far as the Human Resource Manager's work is generally on all human resource issues, without differentiation between workers on the petroleum project drilling rig and non-project staff, the manager's salary will be excluded expenditure. So far as part of the manager's time is spent solely attending to the needs of workers on the project drilling rig, and so far as the workers themselves are carrying on or providing relevant operations, facilities or other things for the petroleum project, the manager's salary is directly incurred in carrying on or providing those operations, facilities or other things.

68. What of recruitment? Only so far as the manager's salary is spent in actually recruiting the particular workers who are to work on the petroleum project drilling rig and to the extent to which they are to work on the rig (or otherwise on things that are referred to in sections 37, 38 or 39) rather than on other things could the manager's salary for recruitment work be in carrying on or providing the operations, facilities or other things those workers will provide by working on the rig. But time spent generally on recruitment and in selecting possible recruits is not incurred directly in carrying on or providing what recruits carry on or provide. Only so far as recruitment activities are solely for particular recruits, and so far as those recruits carry on or provide the relevant activities for the petroleum project, is the manager's salary for recruitment work incurred directly (that is, not incurred indirectly) in carrying on or providing those things. Such recruitment costs are administrative costs and if incurred indirectly are excluded from being eligible real expenditure.

**Example 14 – Long service leave after transfer**

69. An employee whose work for eight years was directly in operations to process petroleum from a petroleum project into an MPC is transferred to a similar position in another petroleum project of the company. The employee took all of their accumulated long service leave only after working on the second project for four years.

- (a) Can the long service leave payment made to the employee be entirely regarded as eligible real expenditure of the second petroleum project in which the employee is currently employed?

- (b) Is the deductibility of the payment affected if the employee was not directly engaged in carrying on a petroleum project in the first two years of employment with the company?

70. To the extent that payments for long service leave are incurred directly in carrying on or providing the operations, facilities and other things comprising a petroleum project, they give rise to eligible real expenditure of that petroleum project. As the employee worked directly for four years on the second petroleum project and accumulated the leave over 12 years of service, one third of the payment is in relation to the petroleum project in which the employee is currently employed. The remaining amount is incurred in relation to the petroleum project in which the employee was formerly engaged and (if case (b) applies) to the two years of non-project employment.

71. If the employee was not engaged directly in carrying on a petroleum project for some part of the period over which the leave accrued, a proportional amount of payment for the leave cannot constitute eligible real expenditure of any petroleum project.

72. This analysis depends on the usual features of long service leave: that is, that it is taken according to current salary at the time it is taken and by reference to the total period of employment over which it accrued.

## **Example 15 – Direct and indirect salary and wage expenditure**

73. The salary cost of a project design engineer who is stationed at the head office of a company with interests in assessable receipts from several petroleum projects is incurred in carrying on operations, facilities and other things for several petroleum projects. Does the engineer's salary cost fully give rise to eligible real expenditure?

74. The proportion of the engineer's salary that is incurred directly in carrying on or providing the operations, facilities and other things for a particular petroleum project and of a kind referred to in sections 37, 38 or 39 is eligible real expenditure of that petroleum project. That proportion can be determined, for instance, by identifying those parts of the engineer's time spent solely on each relevant project. So far as the time is shown to be spent on particular project things for one particular project rather than another or others, such as by appropriate 'time writing', this will identify the part of the salary incurred directly (that is, not incurred indirectly) for things for eligible petroleum projects. Any balance will not be eligible real expenditure of any of the petroleum projects.

**Example 16 – Employee engaged in activities to support other employees working at the petroleum project site office for two petroleum projects**

75. An employee is stationed at a site office that services the remote operations of two petroleum projects. The duties of the employee are:

- to maintain time keeping records for employees performing petroleum project operations at the project sites of the two projects;
- to send time keeping information in relation to the project site employees to the payroll section;
- to implement the occupational health and safety policy and measures at the project sites; and
- to maintain employee amenities at the project sites.

76. The employee is providing these services in relation to the employees engaged on both petroleum projects. How are the salary and wage costs of the employee to be apportioned between the two petroleum projects?

77. For a part of the employee's salary and wage costs to constitute eligible real expenditure of either particular petroleum project, it is necessary to determine the part of the employee's time attributable solely to activities the employee supports that are in carrying on or providing relevant operations, facilities or other things for that petroleum project. This is likely to depend on the identification of the time so spent on that project by the staff served by the site office employee, and on the identification of the time spent solely on the staff by the site office employee, as the time keeping and employee identification for payroll, the occupational health and safety management, and the employee amenities will all relate to the staff served by the site office employee.

78. Because it is a site office supporting remote work for the two petroleum projects, relatively little additional information may be needed to show that the staff who are served by the site office work wholly in carrying on or providing relevant operations, facilities or other things for the two projects. Even for such a site office, though, the extent to which the staff served work on one project rather than the other may need clarification, because of the likelihood that staff with particular skills or experience may find those skills and that experience needed for particular purposes of both projects and so may be employed in part to carry on or provide things for one project and in part for the other. So far as the time of site office staff solely for one or solely for the other petroleum project can not be identified, their salary and wage costs are administrative expenditure (or wage, salary or other work costs) incurred only indirectly and so may be excluded expenditure under paragraph 44(j). The salary and wage costs of the site office staff are 'administrative ... costs', because they are for support staff whose work is of an entirely administrative character, as well as being wages, salary or other work costs of the site office staff. Those costs are 'incurred indirectly' so far as the work they pay for cannot be identified as carried out directly in support of staff directly carrying on or providing relevant things for one rather than the other petroleum project.

#### **Example 17 – Membership of golf club**

79. A company pays for the golf club membership of certain employees engaged in carrying on the operations, facilities and other things comprising the petroleum project. Can the cost of a golf club membership give rise to eligible real expenditure?

80. If the golf club membership fee is incurred as part of an employee's salary package, the proportion that may give rise to eligible real expenditure is determined by the proportion of the time spent by the employee that gives rise to eligible real expenditure, as with any other component of the salary package. That will be to the extent that the employee's time is spent directly in carrying on or providing the operations, facilities and other things for a particular petroleum project the cost of which gives rise to eligible real expenditure.

81. If none of the employee's time is attributable to such activities the cost of a golf club membership is not incurred in carrying on or providing any of those operations, facilities or other things for a petroleum project and is not eligible real expenditure of the petroleum project. The cost of membership is an 'other work cost' which is excluded expenditure under paragraph 44(j) as it is incurred indirectly.

**Example 18 – Reimbursement of membership fee for a professional association**

82. A company reimburses its employees for the annual fees paid by the employees for their membership of a professional association that is relevant to the duties being performed by the employees. Can the reimbursement of the fees give rise to eligible real expenditure?

83. No operations, facilities or other things of a kind referred to in sections 37, 38 or 39 are provided directly by the reimbursement, except through the work of the employees reimbursed. So the reimbursement may be included in eligible real expenditure only as a cost of the work those staff perform. As a work cost, however, the reimbursement is excluded expenditure under paragraph 44(j) if it is incurred indirectly even in carrying on or providing the relevant operations, facilities or other things.

84. Whether the reimbursement is incurred indirectly depends on the extent to which the employee's work time is spent solely in carrying on or providing the operations, facilities or other things for the petroleum project the cost of which is eligible real expenditure. To the extent that identifying this portion of the employee's work time is not possible, the work cost is incurred only indirectly and so it is excluded expenditure under paragraph 44(j).

**Example 19 – Costs of maintaining an administration building at the operations site**

85. Costs are incurred in maintaining an administration building, which is located adjacent to sites where the operations and activities of recovering petroleum from two petroleum projects and processing of that petroleum into MPCs are being carried on. Do the costs give rise to eligible real expenditure?

86. To the extent that the administration building is located at or adjacent to either site where the petroleum project operations are being carried on and the proportion of direct use of the building attributable to either particular petroleum project is able to be ascertained, that proportion of payments in respect of the administration building is eligible real expenditure of that project. So far as the administration building is neither at nor adjacent to either project, payments in respect of it are excluded expenditure under paragraph 44(k).

87. Because payments in relation to an administration building are themselves administrative costs, they are excluded expenditure so far as they are incurred indirectly (under paragraph 44(j)) even if the building is at or adjacent to either project site. Some areas of the building may be dedicated to (such as by directly and exclusively supporting) carrying on or providing relevant operations, facilities or other things of kinds referred to in sections 37, 38 or 39 for one petroleum project or the other. To that extent the payments in relation to the administration building are incurred directly; the part of the payments which is not excluded may often be worked out on the basis of proportion of the total floor space area exclusively used for a particular petroleum project. However, if the administration activities are undertaken indifferently for both projects or indifferently both for carrying on or providing operations, facilities or other things of relevant kinds for either project and for other purposes, there may be no reasonable basis for identification of any component of the administration building costs as eligible real expenditure of either petroleum project.

#### **Example 20 – Equipment used for deductible and non-deductible purposes**

88. A company uses a helicopter primarily to transport staff between the town where its petroleum project site office is located and the petroleum project's drilling rig. However, on some occasions, the helicopter is used for ferrying people to a tourist destination. What method can be used by the company to calculate the component of the expenditure on the helicopter that gives rise to eligible real expenditure?

89. The component of the expenditure that is directly incurred in carrying on the activities which make up the petroleum project can be determined by maintaining a flight log and other relevant records that identify the proportion of flying time spent directly on eligible flights. As aircraft expenditures are generally closely proportionate to flying time, share of flying time will appropriately identify directly the shares of such expenditures directly attributable to one or another activity. Finance costs for an aircraft may not be proportionate to flying time, but as such costs are entirely excluded expenditure in any event under paragraphs 44(a) or 44(b), the extent to which they are directly incurred need not be worked out.

**Example 21 – Head office administration staff costs**

90. Administration staff working from the head office of a company maintain the accounting records of the business related to a petroleum project, compile the PRRT returns of the petroleum project and prepare statements on the performance of the business related to the petroleum project for corporate shareholders. Are the administration staff costs incurred in carrying on or providing any of the operations, facilities or other things for the petroleum project, the cost of which is eligible real expenditure which gives rise to deductible expenditure or transferred expenditure?

91. Not all of the administration staff costs are incurred in carrying on or providing such operations, facilities or other things for the petroleum project. The costs of maintaining accounting records of the deductible expenditures and assessable receipts of the petroleum project itself, as defined, may give rise to deductible expenditure. Those costs will extend to petroleum project records, such as records of petroleum recovered, of production of and movement of MPCs up to the point at which they become excluded commodities, and of deductible expenditure and assessable receipts of the petroleum project.

92. However, the costs of preparing the PRRT return (even though based on those records) and of compiling business performance information for corporate purposes are not incurred in carrying on or providing any of the operations, facilities or other things for the petroleum project of kinds referred to in sections 37, 38 or 39. If no part of the administration employees' salary, wages and other work costs can be identified directly with carrying on or providing particular operations, facilities or other things for the petroleum project, the administration employees' costs are administrative or accounting costs (that being the nature of their work) or are wages, salary or other work costs (that being the nature of the cost in relation to those employees) 'incurred indirectly' and so are excluded expenditure under paragraph 44(j) that cannot be eligible real expenditure.

**Date of effect**

93. It is proposed that when the final Ruling is issued, it will apply both before and after its date of issue. However, the Ruling will not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).



## Appendix 1 – Explanation

**❶** *This Appendix is provided as information to help you understand how the Commissioner's preliminary view has been reached. It does not form part of the proposed binding public ruling.*

### Paragraph 44(j)

94. The Explanatory Memorandum to the Petroleum Resource Rent Tax Assessment Bill 1987 (the Explanatory Memorandum) provides the following example of the application of paragraph 44(j):

... general administrative costs incurred in the head office of a company with diverse interests including a petroleum project would therefore be excluded expenditure and not deductible ...

95. The policy intention behind paragraph 44(j), which is supported by the Explanatory Memorandum, is consistent with what was earlier outlined in the joint statement by the Treasurer and the Minister for Resources and Energy on 27 June 1984 (the Treasurer's Statement) where it was said:<sup>3</sup>

.... expenses not directly related to the project will be excluded. For example where an entity has diverse interests, only one of which is a project assessable for RRT, only those costs incurred at its head office which are solely attributable to the RRT project will be deductible for RRT purposes. Clearly identified expenditures, such as project engineering design costs carried out in the head office therefore would be deductible, even though this might involve an apportionment of some employees' wage costs between time spent on that activity and the remainder spent on other activities not directly associated with an RRT project. General overhead costs incurred at head office would not, however, be deductible.

96. In the Attachment to the Treasurer's Statement it was further stated that:

... no part of head office expenses such as accounting and auditing fees, pay-roll preparation costs, and the costs of maintaining the head office motor vehicle fleet, will be deductible for RRT purposes.

97. The report to the Parliament in November 1992 on the operation of the PRRTAA stated as follows in relation to the industry submissions on the meaning of indirect expenditure:<sup>4</sup>

The PRRT is a project tax, not an enterprise tax. As such, all expenditures incurred indirectly are specifically excluded from eligible deductions. This distinguishes the PRRT from general income tax provisions.

<sup>3</sup> Keating, P (Treasurer) and Walsh, P (Minister for Resources and Energy) 1984, RESOURCE RENT TAX ON 'GREENFIELDS' OFFSHORE PETROLEUM PROJECTS, media release, Canberra, 27 June 1984.

<sup>4</sup> *Report on the Operation of the Petroleum Resources Rent Tax Assessment Act 1987*, November 1992, Department of Primary Industries and Energy (Commonwealth).

98. These statements outline that the policy intention of paragraph 44(j) was that payments of administrative or accounting costs, or of wages, salary or other work costs, incurred only indirectly in carrying on or providing operations, facilities or other things comprising a petroleum project are not deductible when determining the taxable profit of a year of tax in relation to the petroleum project (a reference to a petroleum project in this draft Ruling is a reference to a petroleum project, as defined in the PRRTAA; this topic has been discussed in TR 2010/D4). However, the Commissioner considers that consistently with the policy intention and the terms of the law there are circumstances when certain payments of administrative or accounting costs, or of wages, salary or other work costs that are head office costs, will qualify as eligible real expenditure. These are circumstances where some elements of paragraph 44(j) do not apply. To understand the application of paragraph 44(j) and to determine whether an item of expenditure may be eligible real expenditure or whether it is excluded expenditure, it is necessary to consider the elements of the provision more closely.

***The meaning of ‘administrative or accounting costs’***

99. The words ‘administrative costs’ and ‘accounting costs’ are not defined within the PRRTAA. In interpreting paragraph 44(j), the ordinary meaning of these words in their context must be applied.

100. The word ‘administration’ generally connotes the control and management of what is administered and so includes activities by way of that control and management. The Macquarie Dictionary<sup>5</sup> defines ‘administration’ as ‘the management or direction of any office or employment’. The Commissioner considers, therefore, that administrative costs related to a petroleum project will include costs attributable to managing or directing an office or employment connected with the petroleum project and to controlling, directing and managing the project itself, which is an employment in terms of the dictionary definition (as it employs the resources of the taxpayer for the purposes of the project).

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<sup>5</sup> [Multimedia], Version 5.0.0, 1/10/01.

101. The Macquarie Dictionary<sup>6</sup> defines ‘accounting’ as ‘the theory and system of setting up, maintaining, and auditing the books of a firm; the art of analysing the financial position and operating results of a business firm from a study of its sales, purchases, overheads etc’. In the context of paragraph 44(j), accounting costs related to a petroleum project will be costs or expenditure attributable to the setting up, maintaining, and auditing of the books attributable to the running of the petroleum project, and analysing the financial position and operating results of the petroleum project. The books include all records relevant to understanding the petroleum recovered, its movement and storage, the MPCs produced, their movement and storage up to the point at which they become excluded commodities, and the activities by which they are produced, as well as records relevant to employee amenities, to support services, and to any of the other operations, facilities or other things referred to in sections 37, 38 or 39.

102. Administrative and accounting costs include a wide variety of expenditure and it is not possible to provide an exhaustive or comprehensive list of all such expenditure. As a general guide, the payments that would normally be disclosed as ‘general and administrative expenses’ in the financial statements of a business will be included in payments of administrative and accounting costs. Examples of such costs are costs incurred for insurance, office supplies, general selling expenses, motor vehicles, preparing financial statements, head office project management costs and salary and wages paid to office staff, managers and directors (refer to Examples 3 to 11 of this draft Ruling).

103. Administrative costs also include expenditure in respect of land or buildings in connection with administrative or accounting activities. Such expenditure includes various expenditures, for instance building lease fees and land rates. The deductibility of this type of expenditure is also considered in paragraphs 180 to 188 of this draft Ruling.

### ***The meaning of ‘wages, salary or other work costs’***

104. The PRRTAA does not provide a statutory definition of wages, salary or other work costs. Therefore, wages and salaries maintain their ordinary dictionary meaning as payment for work and services. In other words, they are payments for the labour and skills supplied by a worker. The breadth of the expression is not limited to payments under contracts of service, including payments made to contractors whose main contribution is by way of labour and skills applied. In this context, ‘other work costs’ include costs of the provision of work and services under contracts for services, including payments made to contractors for results of work done under such contracts.

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<sup>6</sup> [Multimedia], Version 5.0.0, 1/10/01.

105. 'Wages, salary and other work costs' includes the on-costs incurred in relation to the supply of labour and skills. For example, payroll tax, payment of superannuation, performance and end of contract bonuses, payment of wages or salary for the period when an employee is on leave, the cost of providing fringe benefits to an employee as well as the fringe benefits tax payable on them are as much within the expression as the wages or salary themselves (refer to Examples 14, 17 and 18 of this draft Ruling).

106. Some taxpayers have contended that only wages, salary and other work costs that themselves relate to the administrative or accounting function can be excluded expenditure under paragraph 44(j). This is not consistent with the legislation. The wording used in paragraph 44(j) is 'payments of administrative or accounting costs, or of wages, salary and other work costs, incurred indirectly'. In other words, any payment of administrative or accounting costs that is incurred indirectly, and any payment of wages, salary or other work costs that is incurred indirectly, will alike be excluded expenditure under paragraph 44(j). Paragraph 44(j) denies a deduction if an item of expenditure has been incurred indirectly and it is:

- a payment of an administrative or accounting cost, whether or not it is also wages, salary or another work cost; or
- a payment of wages, salary or other work cost, whether or not it is also an administrative or accounting cost.

***The meaning of 'incurred indirectly'***

107. Administrative, accounting, wages, salary or other work costs, are not eligible real expenditure giving rise to deductible expenditure or to transferred expenditure so far as they are incurred indirectly in carrying on or providing the operations, facilities or other things of a kind referred to in sections 37, 38 or 39, by operation of paragraph 44(j). The meanings of 'incurred' and 'in carrying on or providing' have been discussed in TR 2010/D4.

108. The Commissioner does not regard paragraph 44(j) as prescribing an absolute exclusion of every administrative, accounting, wages, salary or other work cost. It is implicit from the language used in the provision that there may be some administrative, accounting, wages, salary or other work costs paid, which may be costs that have been incurred directly in carrying on or providing relevant operations, facilities or other things in the course of carrying on a petroleum project. Paragraph 44(j) only rules out administrative or accounting costs, and rules out wages, salary and other work costs, where they are incurred indirectly in carrying on the petroleum project.

109. It is therefore necessary under the PRRTAA to distinguish between administrative, accounting, wages, salary and other work costs so far as they are indirectly incurred in carrying on or providing relevant operations, facilities or other things and other administrative, accounting, wages, salary and other work costs that have been incurred directly in the course of carrying on or providing such operations, facilities or other things for the petroleum project or otherwise. If costs are not incurred in carrying on or providing relevant operations, facilities or other things the question whether they are administrative, accounting, wages or other work costs, and the question whether they have been incurred directly need not be considered: they are not capable of being eligible real expenditure in any event.

110. The meaning of the words ‘directly’ and ‘indirectly’ was considered in *Federal Commissioner of Taxation v. Dixon* (1952) 86 CLR 540 at pages 553-554 in the context of former paragraph 26(e) of the *Income Tax Assessment Act 1936* (ITAA 1936). In a joint judgment, Dixon CJ and Williams J stated:

A direct relation may be regarded as one where the employment is the proximate cause of the payment, an indirect relation as one where the employment is a cause less proximate, or, indeed, only one contributory cause.

111. The above judgment does not mean that a taxpayer can contend that if carrying on or providing the operations, facilities and other things were the predominant but not the only cause for the payment of head office accounting, administration, wages, salary or work costs, that predominant cause would be sufficient to identify such costs as directly incurred expenditure.

112. The clause note to paragraph 44(j) in the Explanatory Memorandum at page 77 provides the following example of a circumstance in which costs would be incurred indirectly for the purposes of the provision:

...general administrative costs incurred in the head office of a company with diverse interests including a petroleum project would therefore be excluded expenditure and not deductible...

113. Consistent with the approach to the provision as read in the Explanatory Memorandum, the term ‘incurred indirectly’ does not mean that all administrative type costs are incurred directly in carrying on or providing relevant operations, facilities or other things for the petroleum project unless they are directly related to something other than the petroleum project.

114. Expenditure relating to some extent to carrying on or providing the relevant petroleum project operations, facilities or other things is incurred indirectly if no ascertainable distinct part of it could be identified as incurred only in carrying on or providing those operations, facilities or other things. Expenditure is indirectly incurred (certainly so far as it is not petroleum project specific) if the way it is incurred is such that an arbitrary or indirect allocation of the cost (or of some part of it) to carrying on or providing such things must be made. For example, allocating salary and wage costs of an employee working on two petroleum projects, on the basis of assessable receipts of the two projects when those costs are not directly proportional to the assessable receipts generated by each project.

115. Expenditure, albeit project specific, is also incurred only indirectly if it was directed not at paying for the carrying on or providing of those relevant operations, facilities or other things for the petroleum project but at meeting other concerns of the taxpayer, even if those concerns arise because of the taxpayer's interest in the petroleum project or because of other operations, facilities or other things relating in some way to the petroleum project. Administrative costs which are indirectly incurred in this way include, for example, costs in managing the PRRT and income tax treatment of profits from the petroleum project, costs of managing joint venture relationships, and the costs of central management of a taxpayer's corporation (such costs may also not be incurred in carrying on or providing any relevant petroleum project operations, facilities or other things; but if they are so incurred they are incurred only indirectly).

116. For expenditure to be incurred directly (that is, not incurred indirectly), it must have a clear and direct identification of that part of the expenditure only with carrying on or providing operations, facilities or other things for the petroleum project, as listed in sections 37, 38 or 39. Such expenditure must be directly ascertainable and directly attributable in some way to carrying on or providing those operations, facilities and other things in some specific rather than some general or notional way.

117. If an administrative, accounting, wages, salary or other work expenditure has been incurred in order to receive more than one benefit only one of which is carried on or provided for deductible expenditure purposes, only that part of the expenditure which can be clearly identified as a direct cost only of carrying on or providing the operations, facilities and other things comprising the petroleum project will be deductible. Parts of such expenditure cannot be allocated in an arbitrary or general manner and only that portion that is only and directly attributable to the carrying on or providing the operations, facilities and other things of a kind referred to in sections 37, 38 and 39 will not be excluded under paragraph 44(j).

118. For income tax purposes, in *Ronpibon Tin NL v. Federal Commissioner of Taxation* (1949) 78 CLR 47 the High Court explained the different ways that apportionment of losses and outgoings into income tax deductible parts should proceed under former subsection 51(1) of the ITAA 1936. The Court considered that there were two kinds of expenditure that would require apportionment. The two types of expenditure considered by the Court were:

- (a) An undivided item of expenditure in respect of things or services of which several and distinct parts are devoted to gaining or producing assessable income and distinct and several parts to some other cause.
- (b) Expenditure involving a single outlay or charge which serves two objects indifferently. Of this directors' fees were given as an example (and the way in which directors' fees serve more than one object indifferently is common to many other kinds of expenditure).

119. For the first type of expenditure the Court considered it possible to divide the expenditure in accordance with the applications which have been made of the things or services. Each part of the expenditure is incurred directly for each separate cause. With the second kind of expenditure, the Court considered that there must be some fair and reasonable assessment of the extent of the relation of the outlay to assessable income for income tax purposes, as the income tax provision expressly allowed for deduction from assessable income 'to the extent that' expenditure was incurred in certain ways. Expenditure serving multiple objects indifferently is incurred only indirectly for any of those objects. No comparable wording of the PRRTAA identifies deductible expenditure 'to the extent that' it is for a purpose, and the PRRTAA provisions identify payments liable to be made only 'in carrying on or providing' particular petroleum project operations, facilities or other things rather than the income tax context of gaining or producing assessable income or of carrying on a business for the purpose of doing so. The PRRTAA does not allow the 'fair and reasonable' identification of indirectly incurred administrative, accounting, wages, salary or other work expenditure for the purposes of the PRRT. Such expenditure is excluded expenditure because it is incurred indirectly.

120. For PRRT purposes, administrative, accounting, wages, salary or other work expenditure of the first kind may have a part that is directly and only attributable to carrying on or providing operations, facilities or other things of relevant kinds for the petroleum project, which part can be identified. However, expenditure of the second kind, which serves two or more objects indifferently, is incurred only indirectly for any of those objects. If any of those objects is other than carrying on or providing those operations, facilities and other things of a kind referred to in sections 37, 38 or 39, the expenditure is incurred only indirectly in carrying on or providing such things (if all objects served were themselves in carrying on or providing such things, then the expenditure would be incurred directly in carrying on or providing such things though only indirectly incurred in relation to any particular one among them). In such cases, no part of the expenditure of the second kind is incurred directly in carrying on or providing such matters. All the expenditure is incurred indirectly to that extent and that part of the expenditure is excluded in total under paragraph 44(j). The clause note to paragraph 44(j) in the Explanatory Memorandum referred to at paragraph 112 of this draft Ruling supports this interpretation of the provision.

### ***Apportionment***

121. Administrative, accounting, wages, salary and other work costs, in some circumstances, may be apportioned to establish that part of the expenditure that has not been incurred indirectly and which is not excluded expenditure by paragraph 44(j) (refer to Examples 19 to 21 of this draft Ruling).

*Employee salary, wages and other work costs including fringe benefit costs*

122. If salary, wages and other work costs are incurred partly for work in carrying on or providing the relevant petroleum project operations, facilities or other things and partly for work on other things, any part of the expenditure which can be identified only indirectly as a cost of carrying on or providing particular operations, facilities and other things of kinds referred to in sections 37, 38 or 39 for the petroleum project will not be eligible real expenditure giving rise to deductible expenditure or to transferred expenditure. What is indifferently a cost of such things and of other things is 'incurred indirectly' for the purposes of paragraph 44(j). And what cannot be identified directly with the carrying on or providing of such things is 'incurred indirectly' for the purposes of paragraph 44(j). So, even if it is otherwise in carrying on or providing such operations, facilities or other things (taking account of issues such as the pre-conditions considered in TR 2010/D4), that part of any cost will be excluded expenditure and cannot be eligible real expenditure giving rise to deductible expenditure or to transferred expenditure.

123. Suppose salary, wages and other work costs are based on time spent or on particular work done, and records are so kept as to show what work time was spent or what work was done directly in carrying on or providing relevant operations, facilities or other things for the petroleum project. In that case, the records may show what part of the salary, wages or other work costs was incurred directly (that is, not incurred indirectly) in carrying on or providing those things. However, the taxpayer records must be adequate in the circumstances to establish the time spent and what that time was spent on, or the work done and what was paid for it, so as to explain directly how the expenditure was incurred. Time writing that does not identify in the circumstances (which may include in light of other records or information) what operations, facilities or other things were being carried on or provided and the actual extent to which the relevant time was spent or work was done directly in carrying on or providing them does not identify the part of any payment that was not indirectly incurred.

124. Some work costs are themselves related to time spent or to particular work done in such a way that they are directly incurred in carrying on or providing what the time was spent on or what work was done. For instance, the cost of travel payable to have particular work attended to is a cost only of that work; if the work to be carried out is of more than one character, a time basis of payment for the work may allow identification of the part of the travel cost that is directly on work of one kind and directly on work of another kind, so far as the time working at the destination is spent working on only one or another kind of work (refer to Example 10 of this draft Ruling).



125. To support a claim for deductibility of expenditure, reliable records are needed. Such records ordinarily need to be created reasonably contemporaneously. If an employee or contractor is engaged partly in carrying on or providing the operations, facilities and other things, expenditure on which is eligible real expenditure and partly for other reasons, the records must be such as to establish that the expenditure was based on time spent and how the employee or contractor's time was spent for the purposes of identifying what part of the wages, salary or other work costs of the employee or contractor was directly incurred in carrying on or providing the relevant operations, facilities or other things. If expenditure was not in relation to time spent, the records must be such as to establish the basis on which the expenditure was incurred and how that directly distinguishes between work only in carrying on or providing the relevant petroleum project operations, facilities or things and other work; otherwise the expenditure will be incurred only indirectly in carrying on or providing those things.

126. Employees and contractors engaged on the petroleum project but also in carrying on or providing things, expenditure on which is not eligible real expenditure, cannot generally show how their time was spent by records kept just for a sample period. This is because a sampling approach must establish that the sample is a reliable one – that is, that the proportion of time spent is consistent over the rest of the period. Showing that the sample is reliable will generally require records for the whole period, other than in unusual circumstances.

127. Expenditure for the work of an employee or contractor is directly incurred and time writing is not required if the evidence shows that during the year of tax the employee or contractor is engaged only in carrying on or providing operations, facilities and other things for the petroleum project that are of a nature giving rise to eligible real expenditure. For such employees and contractors, it is then unnecessary to establish that they are paid for their time (rather than for particular work outcomes) either.

128. If expenditure on an employee or contractor is not based on their time spent or for work done over an identifiable period of time, a direct allocation of the expenditure requires some other form of direct identification of the expenditure with the work carried on or provided. For example, an employee or contractor could be paid on the basis of completion of particular work. In such a case, if particular work is the subject of particular expenditure, and if that work is wholly in carrying on or providing operations, facilities or other things for the petroleum project that are of a kind giving rise to eligible real expenditure, the particular expenditure may then be incurred directly in carrying on or providing those things and will not be excluded under paragraph 44(j).

129. The cost of providing fringe benefits and the fringe benefits tax payable for a year of tax may be treated as part of the salary or wage cost of a person for that year of tax and included in the salary or wage cost identified as expenditure incurred directly in the same way as other parts of salary or wage costs. It should be noted, however, that payments of tax under the *Fringe Benefits Tax Assessment Act 1986* that were incurred up to the end of the year of tax ended 30 June 2006 were specifically treated as excluded expenditure pursuant to former paragraph 44(h) and are, therefore, never deductible.

130. Time writing is not an acceptable basis on which to identify other than indirectly a part of expenditure that is not incurred on a time basis (for instance, some head office overhead expenditure is likely not to be incurred on a time basis or to be proportionate to time spent by employees in carrying on or providing particular operations, facilities or other things). In relation to such expenditure, there may be other bases by which the part of the expenditure can be identified other than indirectly as incurred in carrying on or providing the operations, facilities and other things of a kind referred to in sections 37, 38 and 39. Any such method depends on the basis on which the expenditure is incurred and the identification of a part of the expenditure as only in carrying on or providing relevant operations, facilities or other things in the particular circumstances in light of that basis.

#### *On-costs*

131. Ancillary costs (the kind of costs generally referred to as on-costs) that are related other than indirectly to eligible real expenditure may also be eligible real expenditure incurred in carrying on or providing the operations, facilities or other things for the petroleum project. These are on-costs that are directly incurred in doing something in respect of which the expenditure constitutes eligible real expenditure. For example, although the administrative costs incurred by a taxpayer in keeping records of the time worked by the employees on the petroleum project and in making payments of salary and wages to the employees are not activities that themselves comprise a petroleum project, the Commissioner accepts that to the extent that the costs can be attributed other than indirectly to the eligible real expenditure of the petroleum project, they may give rise to deductible expenditure (refer to Examples 16 and 19 of this draft Ruling).

#### *Employee leave, relocation and redundancy entitlements*

132. Whether employee leave, relocation and redundancy entitlement costs are incurred indirectly depends upon the factual position concerning the reason for the entitlement.

133. As only payments liable to be made can be eligible real expenditure, they do not include a provision for accrued leave entitlements or for any other amounts not yet liable to be paid, as confirmed by the following extract from the Explanatory Memorandum:

Expenditure for which provision is made but for which liability has not yet arisen (for example, accruing leave entitlements of employees and provision for contingent costs) will not be deductible.<sup>7</sup>

134. Such provisions arise before any amount is liable to be paid, generally because the occasion for payment has not arisen (for instance because leave has not been requested) and often at a time when the liability cannot be accurately known (for instance because leave is to be taken at the then current salary of the employee and not at the salary applying at the time of service according to which the period of leave entitlement is worked out).

135. Employee salary and wages and other work costs for a period when the employee is on leave are not necessarily directly incurred in carrying on or providing relevant operations, facilities and other things for the petroleum project merely because that is what the employee was doing immediately before taking the leave. There are several ways in which a part of them may be identified as incurred directly (that is, not incurred indirectly), all depending on the basis of the entitlement to leave.

136. Periodic leave (such as annual leave and long service leave) is generally taken on the basis of an entitlement according to a period of service. So leave taken is incurred in what was done over that period of service. To identify the part of the leave costs that is incurred directly in carrying on or providing petroleum project operations, facilities or other things of kinds referred to in sections 37, 38 or 39 requires identification of the work done over the period for which the entitlement to leave arose and of the proportion of that work that was directly in carrying on or providing such operations, facilities or other things.

137. If leave according to a period of service is taken and satisfies all the employee's entitlement to such leave, it relates directly to the work of the employee over that period of service. So far as there are times in that period when the employee worked only in carrying on or providing relevant petroleum project operations, facilities or other things, the leave will not be incurred indirectly in doing so to that extent.

138. If leave according to a period of service is taken and satisfies only part of the employee's entitlement to such leave, there are several ways in which the relevant period of service for the leave could be identified. If a method of identifying that relevant period of service were applied consistently to all staff taking such leave, then, so far as there are times in the relevant period of service identified for any particular employee when the employee worked only in carrying on or providing relevant petroleum project operations, facilities or other things, the leave will not be incurred indirectly in doing so to that extent.

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<sup>7</sup> Explanatory Memorandum, Petroleum Resource Rent Tax Assessment Bill 1987, Main Features, Deductible Expenditure at pp 9-10.

139. One method, consistent with the terms of many leave arrangements which require leave to be taken within a set period of entitlement arising, is 'first in first out' (FIFO). In applying this method, a taxpayer would identify the relevant period of service as the earliest part of the overall period of service for which part there is a sufficient entitlement to leave to cover the leave taken. Within this period, time worked solely in carrying on or providing relevant petroleum project operations, facilities or other things would mean that the corresponding part of the leave taken was incurred directly (that is, not incurred indirectly) in carrying on or providing those things.

140. Another method is 'last in first out' (LIFO). In applying this method, a taxpayer would identify the relevant period of service as the latest part of the overall period of service for which part there is a sufficient entitlement to leave to cover the leave taken. Within this period, time worked solely in carrying on or providing relevant petroleum project operations, facilities or other things would mean that the corresponding part of the leave taken was incurred directly (that is, not incurred indirectly) in carrying on or providing those things.

141. As a practical matter, the Commissioner will also accept that a proportion of the payments for leave according to a period of service taken during a year by members of a group will give rise to eligible real expenditure if that proportion is based upon a substantial group of employees including all those whose work over the last year has been substantially in carrying on or providing relevant petroleum project operations, facilities or other things. In that case, the proportion of time worked by the whole group solely in carrying on or providing relevant petroleum project operations, facilities or other things might be treated as the proportion applicable to each member of the group taking leave. The corresponding part of the group member employee's leave costs for leave taken in the year of tax would be taken not to be indirectly incurred in carrying on or providing those operations, facilities and other things. This treatment allows working out a proportion on a single consistent basis for a substantial group of employees for the whole year, but entails regarding any part of leave according to a period of service taken by other employees not working included in the group as being incurred only indirectly and so as being excluded expenditure.

142. For example, an employee spends part of their time on activities that give rise to eligible real expenditure. If the employee is taking their available annual leave regularly on a yearly basis, it would be appropriate to apportion the leave payment for a particular year on the basis of the proportion of the employee's work time applicable to that particular year that was spent solely in carrying on or providing relevant petroleum project operations, facilities and other things, as determined by reasonable evidence such as contemporaneous 'time writing'.

143. Correspondingly, suppose a substantial group of staff are engaged during a year on, or largely on, activities that give rise to eligible real expenditure. Annual leave payments to members of the group for leave taken in the year may not need to be identified with petroleum project activities of the individual staff member over the whole period over which their entitlement to leave arose – it may be practicable instead simply to regard all leave in this group in the year as part of the eligible real expenditure in the same proportion as the work of the group, and correspondingly to disregard all leave taken by staff outside the group not working on activities giving rise to eligible real expenditure in that year. However, the smaller the number of staff, the fewer the number of leave payments, and the longer the period over which the entitlement to leave payments made has accumulated, the less readily any part of the leave payments may be identified directly as in carrying on or providing operations, facilities or other things expenditure on which is deductible without analysis of the work of the individual staff member over the whole period over which their entitlement to leave arose.

144. Leave payments according to an extended period of service, such as long service leave, made to an employee who has solely been engaged in carrying on the operations, facilities and other things comprising the particular petroleum project for the whole period during which the entitlement was accrued will be directly incurred in carrying on or providing those things and will not be excluded expenditure. However, extended leave payments accrued over a number of years of tax for only part of which the employee was engaged solely in carrying on the operations, facilities and other things comprising the petroleum project and partly on other matters are indirectly incurred in carrying on or providing the operations, facilities and other things that comprise the petroleum project except to the extent that the proportions of the leave payments that are directly attributable to the particular project are able to be ascertained (also refer to Example 14 of this draft Ruling).

*Redundancy and relocation costs*

145. Redundancy and relocation costs paid to an employee for past work who was solely engaged in carrying on or providing the petroleum project operations, facilities and other things will not be incurred indirectly. Redundancy and relocation costs paid to an employee because of past work whose work did not at all relate to the particular petroleum project are not deductible. For a proportion of the costs to be deductible if only part of the employee's work time was engaged in carrying on or providing the operations, facilities or other things that comprise the petroleum project, there must be an ascertainable and correct basis to attribute a proportion of the redundancy or relocation payments directly to the work of the employee in carrying on or providing the operations, facilities or other things of the particular project expenditure on which is deductible.

146. The basis of relocation costs depends on the facts of the particular case. Some relocation costs are paid only for future work, as part of getting the employee to take up particular work in the new location. These costs are incurred only indirectly so far as the work in the new location is not solely in carrying on or providing relevant petroleum project operations, facilities or other things. Other relocation costs are paid on a basis that does not permit any identification of the costs with any particular work past or future; all such costs are incurred only indirectly (refer to Examples 6, 7 and 8 of this draft Ruling).

147. Redundancy costs always relate to past work of the employee. So only the share of those costs in proportion to the share of past work spent solely in carrying on or providing relevant petroleum project operations, facilities or other things is incurred directly (that is, not incurred indirectly) in that respect, and the whole period of past work must be considered in working out that share.

*Travel expenses*

148. A person may travel for only one objective or for more than one objective. If the travel is only incurred to carry on or provide the operations, facilities or other things of kinds referred to in sections 37, 38 or 39 for the petroleum project, the travel costs will be eligible real expenditure. For example, an engineer who normally works at the head office travels to the operations site to carry out repairs to equipment for recovering project petroleum, or for producing an MPC as part of the petroleum project.

149. However, travel (especially by senior officers) is frequently undertaken to serve more than one objective. In that event, only that direct component of the travel cost that has been incurred in carrying on the activities which comprise the petroleum project may give rise to eligible real expenditure. If the travel is for more than one objective, only one objective being for eligible purposes related to the petroleum project, there may be no reasonable basis to apportion the travel costs directly between the various objectives and if there is not then no eligible real expenditure will arise. The travel expenses are work costs of the work for which the travel is done, and so far as the expenses are not attributable directly to a part of that work that is solely in carrying on or providing operations, facilities or other things of kinds referred to in sections 37, 38 or 39 for the petroleum project, the expenses will be work costs that are incurred indirectly and are excluded expenditure under paragraph 44(j) (refer to Example 10 of this draft Ruling).

#### *Payroll tax*

150. Although payroll tax is in a sense only ever incurred indirectly and is in a sense administrative expenditure in relation to the costs which form part of the payroll on which the tax is calculated, the Commissioner considers payroll tax to be 'other work costs' directly incurred, and so not excluded expenditure, in proportion to the part of the salary and wages payroll tax base that itself constitutes eligible real expenditure. This is the part of the salary and wages payroll tax base that is for work done solely in carrying on or providing relevant petroleum project operations, facilities or other things.

151. Because payroll tax may apply only after a threshold, and may then apply according to stepped rates of tax, it could be thought that the threshold or step might be regarded as attributable preferentially to, or preferentially against, the relevant part of the payroll tax base that is for work done solely in carrying on or providing those things. Ordinarily neither preferential allocation would be appropriate, as the threshold or step does not ordinarily apply other than on the basis of the total amount of the payroll tax base in a period. If such a threshold or step applies, the taxpayer really has an effective average rate of payroll tax across the whole base. It is the part of that base liable to be paid only in carrying on or providing the relevant petroleum project operations, facilities or other things that would identify the part of the payroll tax that is correspondingly directly incurred in carrying on or providing the operations, facilities or other things of kinds referred to in sections 37, 38 or 39 for the petroleum project.

*Joint venture participant costs*

152. Some taxpayers have contended that if there is an operator of a joint venture (whether the operator is one of the joint venturers or not), all amounts sought from the joint venture participants by the joint venture operator are deductible to the participants under sections 37, 38 and 39. There are several forms of this contention. One is that because an operator is engaged for the purposes of the joint venture involving a petroleum project every amount sought by the operator is as such an amount liable to be paid by the joint venturers in carrying on or providing the operations, facilities or other things for the petroleum project expenditure on which is eligible real expenditure. Another is that when joint venturers put the operator in funds to be able to incur expenditure on their behalf, the joint venturers have incurred expenditure then on the purpose for which the operator may incur expenditure toward which the funds were provided.

153. These contentions are not sound. In effect, each substitutes for the requirements of the law a 'but for' argument. 'But for' the petroleum project, there would be no joint venture agreement; 'but for' the joint venture agreement no amount would be sought by the operator; therefore every such amount is said to be liable to be paid in carrying on or providing the operations, facilities or other things specified under sections 37, 38 or 39 in relation to the project.

154. Some of the expenditure payable by the joint venture participants may not constitute eligible real expenditure, including for example, administrative or accounting costs, or wages, salary or other work costs, incurred indirectly in carrying on or providing the operations, facilities or other things that comprise the petroleum project (as this is excluded expenditure under paragraph 44(j)). An item of expenditure that would not be eligible real expenditure if incurred by a person for themselves would not become eligible real expenditure merely because it has been incurred by the joint venture operator on their behalf. As discussed in TR 2010/D4, if the joint venture agreement provides that the joint venture operator is to incur costs and the venturer participant is to be liable for a part of those costs, a cost invoiced to the joint venture participant by the joint venture operator would not be deductible if the cost incurred by the operator is in the nature of expenditure that would not constitute eligible real expenditure, for example, excluded expenditure under section 44.



155. If a person, including a joint venture operator, carries on or provides relevant operations, facilities or other things of the petroleum project for the taxpayer joint venture participant, the amounts the joint venture participant is liable to pay for having the provider carry on or provide those things will be treated as expenditure by that taxpayer in carrying on or providing those things for themselves (under section 41). The operation of this provision is considered specifically in the draft Taxation Ruling TR 2010/D6 Petroleum resource rent tax: deductibility of expenditure to procure the carrying on or providing of operations, facilities or other things by another person in relation to a petroleum project, as provided by section 41 of the *Petroleum Resource Rent Tax Assessment Act 1987*, to which this explanation is subject. So the amounts will be eligible real expenditure if, and only if, expenditure by the taxpayer on doing those things for themselves would constitute eligible real expenditure. Expenditure by way of payment to a joint venture operator by a joint venturer is subject to this principle in the same way as any other expenditure. However, to the extent that the things the taxpayer pays for are things expenditure on which would not constitute eligible real expenditure if they were done directly by the taxpayer (whether as a joint venture participant or otherwise), such as non-project specific expenditure, the amounts will not be deductible as they will not be any kind of eligible real expenditure.

156. In some cases, the agreement between joint venturers requires them to pay a specified share of all expenditure incurred by the operator on any of a range of things (perhaps there will be a 'cost plus' addition to the amount due to the operator; perhaps it will be only at cost; this aspect does not affect the analysis). In such cases, what the joint venturers are liable to pay is for what the operator incurred its expenditure on. The joint venturers in such cases are paying, not for the framework of the arrangement to have the operator carry out the joint venture or to have the operator carry out the petroleum project, but payments parts of which are to carry on or provide each of the things on which the operator has incurred its own expenditure for which the joint venturer is to pay the specified share.

157. If what the joint venturer is liable to pay is directly for the operator to arrange the carrying on or providing by the operator or others of operations, facilities or other things of kinds specified under sections 37, 38 or 39 in relation to the petroleum project, and what is paid to be carried on or provided is not of such a kind that paying for it attracts section 44, how the operator actually disburses or applies the money the operator receives will not affect the application of section 44. Accordingly, the deductible amount for the joint venturer may be applied by the operator to purposes of the operator that would make it excluded expenditure had the joint venturer been liable to pay it to have those purposes met, for example, general administration costs of the operator and a profit margin element for the operator. However, if the joint venture operator is a joint venturer in the project, its own expenditure, in effect what is unreimbursed by the other joint venturers, is itself subject to the PRRTAA including section 44.

158. TR 2010/D6 provides further guidance on the characterisation of payments made by a person to procure services from a third party in relation to a petroleum project.

159. If by arrangement with the operator the joint venturers put the operator in funds in anticipation of significant project expenditure arising which the joint venturers are liable to pay for, putting the operator in funds is likely not to be a payment itself liable to be made in carrying on or providing any of the operations, facilities or other things identified in sections 37, 38 or 39; and it is in any event likely to be a borrowing cost under paragraph 44(a) and so excluded expenditure. By putting the operator in funds, the joint venturers are not incurring project expenditure. They are simply arranging for it to be incurred. Doing so is as much a borrowing cost as making a loan to the operator for the same purposes would be.

*Single petroleum project or multiple projects*

160. In some circumstances a petroleum project may be but one of a diverse range of projects, business activities and operations being undertaken by a taxpayer, some of which may not be subject to PRRT. The taxpayer may maintain administrative facilities and accounting functions that support all those projects, business activities and operations. The taxpayer may also make payments to a contractor to maintain administrative facilities and accounting functions that support all those projects, business activities and operations. The fact that the petroleum project has benefited from the administrative facilities and accounting support functions does not establish that any of the administrative and accounting payments are to any extent directly incurred in carrying on or providing relevant petroleum project operations, facilities or other things and so not excluded expenditure but eligible real expenditure which gives rise to deductible expenditure or transferred expenditure under the PRRTAA. Expenditure associated with the administration, accounting, wages, salary and other work costs that are not solely in carrying on or providing such things for the petroleum project, but that serve other of the taxpayer's business activities and operations in an indifferent manner, are incurred indirectly and are excluded expenditure under the PRRTAA.

161. It has been contended by some taxpayers that paragraph 44(j) has a different and more limited application to entities that hold an interest in only one petroleum project and in no unrelated business activities. This contention is not correct. Whether an item of expenditure is 'excluded expenditure' pursuant to paragraph 44(j) depends on whether the payment is a payment of administrative or accounting costs, or of wages, salary or other work costs and whether it is incurred indirectly in carrying on or providing operations, facilities or other things of kinds referred to in sections 37, 38 or 39 for the petroleum project.

162. Expenditure is not in carrying on or providing operations, facilities or other things of such kinds because the taxpayer has only one petroleum project and no other, unrelated business activities. That test does not depend on the number of enterprises that the taxpayer carries on or the number of projects in which the taxpayer holds an interest. It also does not depend on whether the taxpayer's enterprise involves only 'upstream' petroleum project activities or also includes 'downstream' post-petroleum project activities (refer to Example 3 of this draft Ruling).

163. This matter is discussed in more detail in TR 2010/D4 under the subheading *The concept of a 'petroleum project'*.

### *Depreciation*

164. Depreciation (or decline in value) is not expenditure incurred: it is not a payment liable to be made. It cannot be claimed to any extent as eligible real expenditure under the PRRTAA. The Explanatory Memorandum explains as follows:

... because outright deductions are allowable for expenditure of a capital nature, there will be no deduction for depreciation of plant or equipment used in a project.<sup>8</sup>

### *Administration, preparation of financial statements and auditing expenditures*

165. Expenditure such as corporate auditing fees and the costs of compliance with Sarbanes-Oxley, the Australian Securities Exchange listing rules and Australian Securities Investment Commission requirements is incidental to the carrying on of any business endeavour. It is not a direct or specific expense in carrying on or providing the operations, facilities or other things expenditure on which is eligible real expenditure in relation to a petroleum project. These costs (even if they might otherwise be eligible real expenditure) are administrative or accounting expenses, are incurred only indirectly, and so are excluded expenditure and not eligible real expenditure for PRRT purposes.

166. However, if administration and accounting expenses are incurred directly (that is, not incurred indirectly) in carrying on a petroleum project, the expenditure may constitute eligible real expenditure. For example, a part of general project administration and project management expenses solely associated with running a site office on and for a site solely carrying on or providing the operations, facilities or other things comprising the petroleum project will not be incurred indirectly, will be in carrying on or providing those operations, facilities or other things, will not constitute excluded expenditure and consequently may qualify as eligible real expenditure which may give rise to deductible expenditure or transferred expenditure under the PRRTAA (also refer to Examples 3, 16 and 21 of this draft Ruling).

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<sup>8</sup> Explanatory Memorandum, Petroleum Resource Rent Tax Assessment Bill 1987, Main Features, Deductible Expenditure at p 10.

*Insurance*

167. Insurance expenditure is administrative expenditure, because it arises as an incident of, and in, administration and management of the activities in relation to which the insured risk is present. For much insurance, the decision about whether and to what extent to insure against what aspects of any risk is a management decision; for some particular insurance, there is a framework requiring certain minimum insurance cover of certain prescribed risks.

168. Insurance expenditure is capable of being eligible real expenditure. The risk insured may be one that arises in carrying on or providing operations, facilities or other things for a petroleum project of kinds identified in sections 37, 38 or 39. The extent to which this is so depends on the nature of the insured risk and the way in which that risk is present in the activities of the taxpayer. Insurance premiums that are liable to be paid in connection with risks in (say) time spent by workers, or by equipment, in carrying on or providing the operations, facilities and other things comprising a petroleum project (for example, workers' compensation premiums so far as the workers are engaged in petroleum project work, or indemnity premiums on petroleum project drilling equipment so far as it is so employed) are likely to be in carrying on or providing activities or operations that qualify. Other insurance premiums so far as they are partly solely for risks, a payout on which would be an assessable receipt for PRRT purposes, would also be accepted as in carrying on or providing relevant petroleum project operations, facilities or other things and so as eligible real expenditure.

169. Insurance of an administrative nature, and covering conglomerate risks only partly arising in carrying on or providing the relevant operations, facilities or other things for the petroleum project, is an administrative expenditure incurred indirectly except so far as the part of the premium relating solely to such risks in the petroleum project can be directly ascertained in some reasonable way.

170. As a general guide, if the insurance premium is reasonably able to be apportioned into a part that is a direct cost of carrying on or providing the petroleum project operations, facilities or other things because it is solely for a risk arising in carrying on or providing those things, and into a part that is for other things, the Commissioner will accept the former cost component as incurred directly (that is, not incurred indirectly) on the operations, facilities or other things comprising the petroleum project (refer to Example 4 of this draft Ruling).

*Bank fees and charges*

171. Generally, bank fees and charges are not exclusively incurred wholly or in some particular part for banking assessable receipts from the petroleum project and to pay for the eligible real expenditure incurred in running the petroleum project. They are administrative costs, as they arise as an incident of, and in, administration and management of the activities involved in carrying on or providing the relevant petroleum project operations, facilities or other things. Consequently, as they are administrative costs that are indirectly incurred even if they are in carrying on or providing those operations, facilities or other things, they are excluded expenditure pursuant to paragraph 44(j) and not eligible real expenditure.

172. Payments of principal or interest on a loan, including a credit line or facility, and any other borrowing costs are also excluded expenditure and not deductible pursuant to paragraph 44(a). Many bank charges are of this nature and are excluded expenditure for this reason too.

*Motor vehicles*

173. Expenditure incurred in maintaining a motor vehicle fleet at the head office of the taxpayer is likely to be an indirect administrative expenditure and is normally excluded from deductibility by paragraph 44(j). If a motor vehicle is partly used directly in carrying on the petroleum project, for example, a project design engineer working from the head office of the taxpayer travels to the petroleum project site in a head office motor vehicle to conduct operations of the petroleum project, the Commissioner will accept a corresponding part of the cost of the vehicle as not indirectly incurred and as not excluded expenditure. The proper use of a log book is a method of calculating the part of expenditure that was directly incurred in carrying on or providing the operations, facilities and other things comprising the petroleum project. However, the PRRTAA does not provide for other simplified methods of calculating work related car expenses like those acceptable for income tax purposes, such as 'per kilometre' allowances, as they are proxy methods not based on the identification of the part of the actual cost of the motor vehicle that is for or in carrying on or providing particular operations, facilities or other things. In any particular case, what is required is reasonable evidence of what the actual expenditure was and of what part of it was directly incurred (and so solely) in carrying on or providing relevant operations, facilities or other things for the petroleum project.

174. For a motor vehicle used directly in carrying on or providing such things for the petroleum project on a regular basis if its pattern of usage is the same over a long period of time, the Commissioner will accept an identification of the part of the total cost of maintaining the motor vehicle that is incurred directly (that is, not incurred indirectly) in doing so on the basis of evidence from properly maintaining a log book for a continuous representative period of not less than 13 weeks.

175. If the pattern of usage of the motor vehicle changes, the taxpayer should maintain a log book for another representative sample period of not less than 13 weeks. If the pattern of usage of a motor vehicle is changeable, such as where it varies from month to month, a sample will not provide reasonable evidence of what cost is in carrying on or providing the relevant operations, facilities or other things and of what part of the cost is incurred directly (that is, not incurred indirectly). In such cases the taxpayer can still work out the part of the cost that is eligible real expenditure by maintaining appropriate records, such as a log book, of the vehicle's use for the full year of tax.

176. If a pattern of usage of a motor vehicle has been worked out by properly maintaining a log book of its use for a sample period and the motor vehicle is replaced by another motor vehicle for which the pattern of usage has not changed, the taxpayer may reasonably work out the part of cost of the replacement vehicle that is not indirectly incurred according to the sample period.

*Telephone, postage and publication expenditure*

177. In most circumstances, some portion of this expenditure would be in carrying on or providing relevant operations, facilities or other things to the petroleum project but no ascertainable part of it can be identified directly as in doing so. Such expenditure is an administrative cost and any part that cannot be identified directly is incurred indirectly. That part of the expenditure constitutes excluded expenditure and is not eligible real expenditure.

178. A taxpayer may, however, maintain various records such as a log book to record the telephone calls (including call cost, directly or by length of call correlating to phone billing rates) or postage expenses that allow direct identification of expenditures as in carrying on or providing particular operations, facilities or other things. If such a telephone call log is maintained, the Commissioner may also accept as not indirectly incurred a proportional amount of related 'fixed' costs such as telephone line rental.

*Computer hardware and software expenditure*

179. The cost of computer hardware and software is generally an administrative cost, which arises as an incident of, and in, administration and management of the activities involved in carrying on or providing the relevant petroleum project operations, facilities or other things, though some particular hardware and software may be more directly employed in carrying on or providing such things. The cost of hardware and software acquired exclusively for direct use in carrying on or providing the operations, facilities and other things that comprise the petroleum project will be eligible real expenditure. If hardware and software is used for administration or management in carrying on or providing the operations, facilities and other things that comprise the petroleum project as well as for other purposes, and no part of its use is solely in carrying on or providing such things, all of the cost of acquiring the hardware and software will be administrative costs indirectly incurred and will be excluded expenditure as the cost is incurred indifferently for the carrying on of the petroleum project and other activities (also refer to Example 2 of this draft Ruling).

**Paragraph 44(k)**

180. Paragraph 44(k) excludes from deductibility payments so far as they are in respect of land or buildings for use in connection with administrative or accounting activities, other than so far as the operations, facilities or other things of kinds referred to in sections 37, 38 or 39 for the petroleum project in respect of which the administrative or accounting activities are carried on or provided are themselves carried on or provided at, or adjacent to, the site of the land or buildings.

181. Therefore, an item of expenditure will be excluded expenditure if:

- (a) it is a payment in respect of land or buildings;
- (b) that land or building is for use in connection with administration or accounting in respect of relevant operations, facilities or other things carried on or provided for the petroleum project (things referred to in sections 37, 38 or 39); and
- (c) that land or building is not located at or adjacent to the site where those project operations, facilities or other things are carried on or provided.

182. The Explanatory Memorandum provides an example of the application of paragraph 44(k) as follows:

...this paragraph will, for example, bring within the scope of excluded expenditure payments in respect of office buildings in, say, a capital city but not payments in respect of project-related employee amenity buildings adjacent to the project site.<sup>9</sup>

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<sup>9</sup> Explanatory Memorandum, Petroleum Resource Rent Tax Assessment Bill 1987, Notes on Clauses, Clause 44: Excluded Expenditure at p 77.

183. Payments are in respect of land or buildings whether they are of a capital or a revenue nature, consistently with the general design of the PRRTAA and with the express terms of sections 37, 38 and 39 (which each apply to expenditure 'whether of a capital or revenue nature'). So such payments include (for instance) earthworks, purchase costs, lease payments, fitting out and refurbishment costs, and maintenance costs. Some of these costs may be incurred preparatory to the expected use of the land or building. As the land or building is one 'for use' in connection with certain administrative or accounting activities, paragraph 44(k) applies not only on the basis of the actual use of the land or building at the time the cost arises but according to the expected use, including use that will occur only after an extended program of expenditure is completed or use that will occur only after an introductory period.

184. The word 'adjacent' has not been defined in the PRRTAA. The Macquarie Dictionary<sup>10</sup> defines the meaning of the word 'adjacent' as 'lying near, close or contiguous; adjoining; neighbouring'. In the context of paragraph 44(k), 'adjacent' should be taken to mean the nearest practicable location for an administrative office for administrative or accounting activities in relation to the operations, facilities or other things administered or accounted for (land or buildings further away cannot be adjacent, if other land or buildings could practicably be closer to the operations, facilities or other things administered or accounted for). That nearest practical location may be on a floating platform, an island or mainland Australia depending on the characteristics of the operations, facilities or other things subject to the administrative or accounting activities. So what is the location, or the nearest practical location, must be worked out having regard to the characteristics of the particular petroleum project.

185. Expenditure to which any paragraph of section 44 applies will not be eligible real expenditure to that extent. However, the fact that expenditure is not excluded by paragraph 44(k) does not automatically mean that the expenditure is eligible real expenditure. Being excepted from that paragraph does not limit application of any other paragraph of section 44; for instance, paragraph 44(j) must be considered independently. Paragraph 44(k) applies to payments in respect of administrative or accounting use buildings or land, regardless of whether the payments are incurred indirectly, so far as the buildings are not adjacent to the place where the operations, facilities or other things administered or accounted for are themselves carried on or provided. Paragraph 44(j) applies to payments of administrative or accounting costs incurred indirectly. All payments, so far as they are in respect of land or buildings for use in connection with administrative or accounting activities, are themselves administrative or accounting costs. Incurred indirectly, they are excluded expenditure under paragraph 44(j). Administering or accounting for operations, facilities or other things not carried on or provided adjacently to the building, they are excluded expenditure under paragraph 44(k). Some expenditure may be excluded expenditure under both paragraphs accordingly (refer to Examples 12 and 19 of this draft Ruling).

<sup>10</sup> [Multimedia], Version 5.0.0, 1/10/01.



186. Expenditure that is not excluded expenditure will be eligible real expenditure from which deductible expenditure or transferred expenditure derive in any event only to the extent that it meets all the other requirements of the PRRTAA such as the pre-conditions to deductibility considered in TR 2010/D4.

187. If land and buildings that are for use in connection with administration or accounting activities are located at or adjacent to the site where the relevant operations and activities for the petroleum project that are administered or accounted for are themselves carried on or provided, and the land and buildings are also partly used for activities not in respect of the particular petroleum project, not in respect of relevant operations, facilities or other things for the project, or in respect of administering or accounting for relevant operations, facilities or other things for the project that are not carried on or provided adjacently, the payments in respect of the land and buildings will require an apportionment to determine the part (if any) that is not indirectly incurred. The Commissioner will accept as reasonable an apportionment of such expenditure on the basis of floor space, if different floor areas are used directly and solely for administration or accounting activities in carrying on or providing relevant project operations, facilities or other things and partly for mixed or other administration or accounting. However, if administration or accounting activities are undertaken only indifferently in relation to adjacent operations, facilities or other things referred to in sections 37, 38 or 39, and also in administration or accounting for other things not referred to in sections 37, 38 or 39, there may be no reasonable basis for apportionment and no part of the payments that is able to be identified as incurred directly (that is, not incurred indirectly) and as not excluded expenditure under paragraph 44(k) but as eligible real expenditure.

188. Payments in respect of land or buildings, to which paragraph 44(k) may apply, are not limited to payments for the acquisition or occupation of such land or buildings. For instance, payments of outgoings in relation to a building or land, insurance payments in relation to a building or land, payment for fitout and adjustment to fitout of a building or land, and payment for irregular services such as window cleaning are all payments in respect of the land or buildings. And in this context payments in respect of only part of the land, or part of a building, are payments in respect of the land or the building. Similarly payments in respect of more than one piece of land or building are payments in respect of each of them.

### **Record keeping**

189. Section 112 is an offence provision which requires a person to keep records that record and explain all transactions and other acts engaged in by the person or any other person that are relevant for the purpose of ascertaining the person's PRRT liability. In any appeal or review under Part IVC of the *Taxation Administration Act 1953*, the onus is on the taxpayer to establish that an assessment is excessive.

190. The onus of proof that expenditure was incurred and was incurred in carrying on or providing the operations, facilities and other things for the petroleum project and was not excluded expenditure is on the person. Sufficient records to evidence and explain each claimed expenditure must be kept. If a taxpayer cannot ascertain or trace (in some reasonably appropriate direct way) an administrative, accounting, wages, salary or other work cost to show the extent to which it was incurred and was directly attributable to carrying on or providing the operations, facilities and other things of kinds referred to in sections 37, 38 or 39 for the petroleum project, the expenditure will be excluded expenditure under paragraph 44(j) because it will be incurred indirectly and will not constitute eligible real expenditure giving rise to deductible expenditure or transferred expenditure. Similarly, records must be kept to ascertain and explain the amount of a deduction for an expenditure that is in the nature of a payment in respect of land or building for use in connection with administrative or accounting activities at or adjacent to the sites where operations, facilities or other things comprising the petroleum project are carried on or provided, as if the land or building cannot be shown to be at or adjacent to the sites paragraph 44(k) may apply to exclude the payment.

191. There will be an offence under section 112 if records are not retained for seven years 'after the completion of the transactions or acts to which they relate', as has been discussed in TR 2010/D4. But the passing of the seven year retention period, which means no offence under section 112 is committed if the records are no longer retained, does not relieve the person from the onus of proof in relation to the expenditure if the records are not retained. Section 44(j) may thus apply because the taxpayer can no longer show in some direct way the extent to which an administrative, accounting or work cost was incurred in carrying on or providing the relevant operations, facilities or other things, although the person may once have had relevant records which were retained only for the seven year retention period. In the same way, paragraph 44(k) may thus apply because the taxpayer can no longer show the extent to which the land or buildings for use in connection with administrative or accounting activities and in respect of which a payment is incurred are located at or adjacent to the site where the operations, facilities or other things accounted for or administered were carried on or provided.

## Appendix 2 – Alternative views

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**①** *This Appendix sets out alternative views and explains why they are not supported by the Commissioner. It does not form part of the proposed binding public ruling.*

192. Alternative views relating to the issues discussed in the Explanation section of this draft Ruling have been considered in this section. The reasons the Commissioner considers the alternative views to be incorrect are explained in the 'Analysis' following each alternative view.

### Alternative view 1

#### ***What are administrative costs***

193. It is not correct to treat the expenditure incurred on insurance, office supplies, general selling expenses, motor vehicles and project management as administrative costs. If these costs relate to a petroleum project they are incurred in carrying on the project. Expenditure incurred on preparing PRRT instalment statements and PRRT return is incurred in complying with the PRRTAA. Therefore, it ought to be eligible real expenditure.

#### ***Analysis***

194. Administrative costs have not been defined in the PRRTAA. The ordinary meaning of the words applies. Dictionary definitions and ordinary usage may assist in identifying the meaning of the words in their context. The costs incurred on insurance, office supplies, general selling expenses, motor vehicles and project management are costs that are generally reflected in what is described as administration expenses in the general financial statements of a company prepared in accordance with general accounting principles.

195. Expenditure incurred in preparing a PRRT return is incurred (in some wider sense) in relation to a petroleum project, but it is not incurred in carrying on or providing any of the operations, facilities or other things that comprise a petroleum project or that are otherwise of kinds referred to in sections 37, 38 or 39 and so that can be eligible real expenditure from which deductible expenditure or transferred expenditure derive. As discussed at paragraph 168 of TR 2010/D4, the PRRTAA does not treat expenditure as eligible real expenditure merely on the basis that but for the petroleum project, the expenditure would not have been incurred.

196. Costs that are incurred to support, or as part of, carrying out the management and administration of activities are administrative costs of those activities. Some administrative costs may also be wages, salary or other work costs of staff engaged in the management and administration of activities: those costs are both administrative costs and are wages, salary or other work costs, for the purpose of the application of paragraph 44(j). They will be excluded expenditure so far as they are incurred indirectly.

### **Alternative view 2**

#### ***Expenditure incurred indifferently for two objects***

197. In *Ronpibon Tin NL v. Federal Commissioner of Taxation* (1949) 78 CLR 47 the High Court only provided one example of expenditure that serves two objects indifferently. The circumstances in which expenditure serves two objects indifferently are therefore very limited and do not ordinarily go beyond directors' fees. The manner in which the concept of administrative cost and indifferent use has been applied in some of the examples in this draft Ruling (specifically Example 2) is unsupportable by the above case.

### **Analysis**

198. In *Ronpibon Tin NL v. Federal Commissioner of Taxation* (1949) 78 CLR 47, the High Court was considering the deductibility of:

- charges for management and directors' fees; and
- expenditure on cables, postages, stationery, audit fees and travelling and general expenses.

199. This is the reason that the High Court gave the example of directors' fees as a single outlay or charge which serves two objects indifferently. However, the use of the words 'an example' by the High Court clearly indicates that the Court's concept of expenditure that serves two objects indifferently is not limited to directors' fees only. Nor does the wording used by the High Court in any way suggest that the circumstances in which an expenditure or outlay serves two objects indifferently are very limited or are limited to directors' fees and to outlays very like them.

## Appendix 3 – Your comments

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200. You are invited to comment on this draft Ruling. Please forward your comments to the contact officer by the due date.

201. A compendium of comments is also prepared for the consideration of the relevant Rulings Panel or relevant tax officers. An edited version (names and identifying information removed) of the compendium of comments will also be prepared to:

- provide responses to persons providing comments; and
- publish on the Tax Office website at [www.ato.gov.au](http://www.ato.gov.au).

Please advise if you do not want your comments included in the edited version of the compendium.

<b>Due date:</b>	<b>13 August 2010</b>
<b>Contact officer:</b>	<b>Bhim Nagpal</b>
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## **Appendix 4 – Detailed contents list**

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## References

### *Previous draft:*

Not previously issued as a draft

### *Related Rulings/Determinations*

TR 2006/10; TR 2010/D4;  
TR 2010/D6

### *Subject references:*

- entertainment expenses
- joint ventures
- mining and petroleum
- PRRT
- PRRT assessable receipts
- PRRT closing-down expenditure
- PRRT deductible expenditure
- PRRT excluded expenditure
- PRRT exploration expenditure
- PRRT general project expenditure
- PRRT taxable profit

### *Legislative references:*

- PRRTAA
- PRRTAA 2
- PRRTAA 19(4)(b)(v)
- PRRTAA 37
- PRRTAA 38
- PRRTAA 39
- PRRTAA 40
- PRRTAA 41
- PRRTAA 44
- PRRTAA 44(a)
- PRRTAA 44(b)
- PRRTAA 44(j)
- PRRTAA 44(k)
- PRRTAA former 44(h)
- PRRTAA 112
- ITAA 1936 former 26(e)
- ITAA 1936 former 51(1)
- TAA 1953 Pt IVC

### *Case References:*

- Federal Commissioner of Taxation v. Dixon (1952) 86 CLR 540
- Ronpibon Tin NL v. Federal Commissioner of Taxation (1949) 78 CLR 47

### *Other references:*

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- Keating, P (Treasurer) and Walsh, P (Minister for Resources and Energy) 1984, RESOURCE RENT TAX ON 'GREENFIELDS' OFFSHORE PETROLEUM PROJECTS, media release, Canberra, 27 June 1984
- PRRT discussion paper (2009) Petroleum Resource Rent Tax: The deductibility of administrative, accounting and overhead expenditures incurred in carrying on or providing operations, facilities or other things of a kind referred to in sections 37, 38 and 39 of the *Petroleum Resource Rent Tax Assessment Act 1987*
- Report on the Operation of the *Petroleum Resources Rent Tax Assessment Act 1987*, November 1992, Department of Primary Industries and Energy (Commonwealth)
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