TD 93/D145 - Income tax: how are business profits or losses calculated under Article 4 of Annex D (the Taxation Code) to the Treaty between Australia and the Republic of Indonesia on the Zone of Cooperation in an Area between the Indonesian Province of East Timor and Northern Australia (the 'Timor Gap Treaty')?

This document has been finalised by TD 97/4.

Draft Taxation Determinations (TDs) represent the preliminary, though considered, views of the ATO. Draft TDs may not be relied on; only final TDs are authoritative statements of the ATO.

Draft Taxation Determination

Income tax: how are business profits or losses calculated under Article 4 of Annex D (the Taxation Code) to the Treaty between Australia and the Republic of Indonesia on the Zone of Cooperation in an Area between the Indonesian Province of East Timor and Northern Australia (the "Timor Gap Treaty")?

1. The Timor Gap Treaty (which is reproduced as a Schedule to the *Petroleum (Australia-Indonesia Zone of Cooperation) Act 1990*) is unique among Australia's international agreements in that it provides for Australia and Indonesia to share equally in the benefits flowing from the exploration and exploitation of petroleum resources within Area A of the Zone of Cooperation.

2. Article 4(1) of the Taxation Code to the Timor Gap Treaty, in effect, allows both countries to tax simultaneously 50 percent of the business profits or losses of companies operating within Area A. However as there is no uniform definition contained within the Timor Gap Treaty of the term 'business profits' or 'business losses', questions have been raised as to the appropriate method of calculating business profits or losses for the purposes of Australian and Indonesian domestic tax laws.

3. Article 3 of Part II of that Schedule imposes a requirement on the Joint Authority (the body established by the Timor Gap Treaty to adminster Area A) that it deal only with enterprises wishing to explore for petroleum resources within Area A who are limited liability corporations established for the sole purpose of executing the production sharing contracts. Accordingly, the correct method of calculating the business profits or losses of a 'special purpose' company under Article 4(1) is to calculate the business profits or losses of the company and the tax liability arising therefrom under the tax systems of both Australia and Indonesia and then reduce those taxable amounts in each country by 50 percent. In the case of an Australian company operating within Area A, this will mean that all the usual provisions (including Division 10AA) of the *Income Tax Assessment Act* are available to be used in calculating the company's business profits or losses for Australian income tax purposes. Once this has been done then the resulting amount is to be reduced by 50 percent and the remainder subject to the normal company rate of tax applying for that year of income. Indonesian tax would be calculated along similar lines.

Commissioner of Taxation
3/6/93

FOI INDEX DETAIL: Reference No.

Related Determinations: TD 93/D144

Subject Ref: double taxation; Timor Gap Treaty; business profits; business losses; petroleum mining

Legislative Ref: Petroleum (Australia-Indonesia Zone of Cooperation) Act 1990; Div 10AA ITAA

ATO Ref: NO 90/3518-4

ISSN 1038 - 8982