TR 2009/1 - Petroleum resource rent tax: transfer of expenditure incurred in relation to a project that did not have a production licence to other taxable projects of the person or other group companies under sections 45A and 45B of the Petroleum Resource Rent Tax Assessment Act 1987 where the expenditure is taken to be incurred by the person under sections 48 and 48A of that Act

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Taxation Ruling

Petroleum resource rent tax: transfer of expenditure incurred in relation to a project that did not have a production licence to other taxable projects of the person or other group companies under sections 45A and 45B of the *Petroleum Resource Rent Tax Assessment Act 1987* where the expenditure is taken to be incurred by the person under sections 48 and 48A of that Act

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This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

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What this Ruling is about

1. Under the provisions of the *Petroleum Resource Rent Tax Assessment Act 1987* (the PRRTAA)[1] a person is liable to pay Petroleum Resource Rent Tax (PRRT) on the taxable profit from a petroleum project worked out under that Act.[2]

[1] All legislative references are to the PRRTAA unless otherwise indicated.
[2] Section 21. The tax is separately imposed, by the *Petroleum Resource Rent Tax Act 1987*.

2. Taxable profit of a person for a year of tax in relation to a petroleum project is the excess of the assessable receipts derived by that person over the sum of:

(a) the deductible expenditure incurred by the person in relation to the project;

(b) the total of any amounts transferred by the person to the project in relation to the year of tax under section 45A (that is, transfers of transferable exploration expenditure between the person's PRRT projects); and

(c) the total of any amounts transferred by another person to the person in relation to the project and the year of tax under section 45B (that is, transfers of transferable exploration expenditure of PRRT projects between group companies).[3]

3. Section 48 applies where a transaction has the effect of transferring to the purchaser the whole of the entitlement of the vendor to derive assessable receipts of a petroleum project. Section 48A applies where the transaction has the effect of transferring part only of the vendor's entitlement to assessable receipts.

4. Under subsections 48(1) and 48A(5), a purchaser takes over expenditure incurred by a vendor in a petroleum project up to immediately before the transaction in proportion to the share of the vendor's assessable receipts in relation to a petroleum project transferred in effect to the purchaser. The purchaser in effect inherits the PRRT history of the particular interest in the project. This expenditure is commonly referred to as 'inherited expenditure'.

5. Division 3A of Part V provides for the possible transfer of exploration expenditure incurred on or after 1 July 1990 to another project. Section 45A provides for transfers generally, by which exploration expenditure of a petroleum project of a taxpayer must be taken to be incurred in relation to other PRRT projects of that taxpayer to the extent that it can be utilised in a financial year and so far as the rules in the Schedule to the PRRTAA (the Schedule) allow its transfer. Section 45B provides for the transfer of expenditure in relation to group companies, by which exploration expenditure of a petroleum project must be taken to be incurred in relation to other PRRT projects of other companies in a group of which the taxpayer is a member to the extent that it can be utilised in a financial year and so far as the rules in the Schedule allow its transfer. Section 45C provides for transfer of expenditure by the Commissioner where transfers required by sections 45A or 45B have not been made. Section 45D provides for the effect of transfers of expenditure, and section 45E provides for the interaction between transfers in relation to the calculation of instalments of PRRT and transfers in relation to a financial year.

[3] Section 22.

6. The Schedule provides the rules according to which expenditure is transferred. It also contains the rules according to which exploration expenditure is taken to be incurred, in relation to deductible expenditure actually incurred on or after 1 July 1990.

7. This Ruling considers whether and when a person may and must transfer expenditure to other projects of the person or to another group company under sections 45A or 45B where that expenditure was inherited under sections 48 or 48A in relation to a project that did not have a production licence before the expenditure is sought to be transferred.

Class of entities

8. This Ruling applies to a person[4] who has an interest in the assessable receipts of a petroleum project as defined in section 19.

9. However, this Ruling does not deal with the transferability of expenditure from petroleum projects covered by Part 2 (Class 2 Augmented Bond rate exploration expenditure) and Part 3 (Class 2 GDP factor expenditure) of the Schedule.

Ruling

10. Where a person acquires an interest or increases its interest in a project and the project has not yet obtained a production licence, the person cannot transfer any of the exploration expenditure they inherit under sections 48 or 48A to other projects of theirs or to projects of another group company pursuant to sections 45A or 45B.

11. Clause 15 of Part 4 of the Schedule is a current year rule to work out how much of a person's exploration expenditure on a project that has not obtained a production licence is available to be considered for, or excluded from, possible transfer. Subclause 15(2) of the Schedule identifies the part of the exploration expenditure that will be available for transfer as limited to the excess of total deductible expenditure actually incurred by the person over assessable receipts – excluding any inherited expenditure, as this was not actually incurred by the person.

[4] Person is not defined in the PRRTAA and therefore has at least the common law meaning. However, the PRRTAA expressly applies to partnerships (section 12) and to unincorporated associations (section 13) as if they were persons, with special rules in relation to the operation of the law in relation to partners and in relation to members of such associations. Neither partnership nor unincorporated association are specially defined for the purposes of the PRRTAA, but unincorporated association is defined to exclude a joint venture (definition, section 2) and so persons who are members of joint ventures that are not partnerships and not incorporated are separate taxpayers under the PRRTAA.

Example

12. In February 2005 XYZ Ltd acquires a 10% interest in the assessable receipts of a project for which an exploration permit has been granted. No petroleum project is yet in existence as a production licence has not been granted.

13. In the year ended 30 June 2008 XYZ Ltd enters into a transaction to acquire an additional 50% in the assessable receipts of the project by buying out a co-venturer's interest in project receipts.

14. XYZ Ltd is taken to have incurred the 'incurred exploration expenditure amount' that would have been the incurred exploration expenditure amount of the vendor had the financial year ended at the time when XYZ Ltd acquired the additional 50%.[5]

15. XYZ Ltd will calculate its transferable expenditure in relation to the exploration permit in accordance with Part 4 of the Schedule.

16. Under Part 4 of the Schedule only exploration expenditure actually incurred by a person is taken into account in calculating the amount of reduced notional exploration expenditure that is transferable by a person in relation to an income year.

17. Therefore, XYZ Ltd cannot transfer any of the exploration expenditure inherited on the acquisition of the 50% interest to another petroleum project in which it is interested pursuant to section 45A. Nor can XYZ Ltd transfer any of the exploration expenditure so inherited to a petroleum project of another member of the same company group pursuant to section 45B.

Date of effect

18. This Ruling applies to years of income commencing both before and after its date of issue. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation
4 February 2009

[5] Section 48 and definition of 'incurred exploration expenditure amount' in Clause 1 of the Schedule.

Appendix 1 – Explanation

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

Legislation

19. Under the provisions of the PRRTAA a person is liable to pay PRRT on their taxable profit from a petroleum project.

20. Section 22 calculates taxable profit of a petroleum project as the excess of assessable receipts derived by a person over:

- deductible expenditure incurred by the person in relation to the PRRT project;
- the total of the amounts (if any) transferred by the person to the project in relation to the year of tax under section 45A; and
- the total of the amounts (if any) transferred by another person to the person in relation to the project and the year of tax under section 45B.

21. Division 3A of Part V provides for the possible transfer of exploration expenditure incurred on or after 1 July 1990.

22. Section 45A provides for transfers generally, by which exploration expenditure may be taken to be incurred in relation to other PRRT projects of a person.

23. Section 45B provides for transfers of exploration expenditure to projects of other companies in the same group.

24. Section 2 defines transferable exploration expenditure (for the purposes of sections 45A and 45B) as expenditure that is, according to the Schedule, transferable by the person in relation to the financial year. This does not mean that any transfer is either required or possible in relation to that or any other financial year. The terms of the Schedule mean that such 'transferable expenditure' is only taken to be incurred when and to the extent that the expenditure can be deducted against assessable receipts in a financial year, even in relation to the project on which the expenditure from which it derives was actually incurred.

25. The Schedule contains provisions relating to incurring and transfer of exploration expenditure derived from expenditure actually incurred on or after 1 July 1990.

26. Part 4 of the Schedule provides the basis on which to calculate the amount of exploration expenditure that is transferable, being actually incurred in relation to an exploration permit or retention lease prior to the issue of a production licence.

27. To the extent that an amount of exploration expenditure is determined to be transferable under Part 4 of the Schedule, the transfer of any of that expenditure would still need to meet rules relating to the transfer of expenditure in Parts 5 and 6 of the Schedule. In particular, what is commonly referred to as the 'common interest rule'[6] would need to be met. The amount to be transferred is the amount, after augmentation under Part 7 of the Schedule, that can be absorbed against assessable receipts of a petroleum project in the transfer year. That amount must, and no greater amount may, be transferred.

28. Part 5 of the Schedule outlines the 'General rules relating to transfer of exploration expenditure'. Part 6 of the Schedule outlines 'Rules relating to transfer of exploration expenditure between group companies'.

29. Under sections 48 and 48A, a purchaser takes over expenditure incurred by a vendor in a petroleum project[7] in proportion to the share of the vendor's entitlement to assessable receipts in relation to a petroleum project transferred in effect to the purchaser.[8] Expenditure taken over in this way is commonly referred to as 'inherited expenditure'.

30. Section 48 applies where the transaction has the effect of transferring the whole of the entitlement of the vendor to derive assessable receipts in relation to a petroleum project.

31. Section 48A applies where the transaction has the effect of transferring part only of the entitlement of the vendor to derive assessable receipts in relation to a petroleum project.

32. Sections 48 and 48A apply to a transaction that has the effect of transferring an entitlement of a vendor to derive assessable receipts in relation to a petroleum project, whether or not an eligible production licence is then in force and whether or not an eligible production licence ever comes into force in relation to the project. Therefore, the sections apply even when there is only the transfer of an interest in assessable receipts while there is an exploration permit or retention lease or any other entitlement and even when an eligible production licence is not in force.[9]

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[6] Clauses 22 (Part 5) and 31 (Part 6) of the Schedule.

[7] Note that sections 48 and 48A apply not only to the transfer of an interest in assessable receipts of projects that have an eligible production licence but also to the transfer of an interest in assessable receipts where an exploration permit, retention lease or any other entitlement is in force even at any time when a production licence is not in force. See Miscellaneous Taxation Ruling MT 2004/1 Petroleum resource rent tax: effects of transferring an interest in an exploration permit or retention lease.

[8] Paragraph 48(1)(a) and subsection 48A(5).

[9] Paragraph 5 of MT 2004/1; such transfers may occur 'before the vendor's first year of tax in relation to the petroleum project', subsections 48(1A) and 48A(3), and eligible real expenditure (including exploration expenditure) may generally be incurred in relation to a project at any time even before or after the project (section 45), which exists while there is an applicable production licence in effect (sections 19 and 20).

33. Sections 48 and 48A expressly apply in relation to expenditure that would have been included in the 'incurred exploration expenditure amount' of the vendor of any year up to the transfer by the vendor, had the financial year ended immediately before the transfer by the vendor (subparagraph 48(1)(a)(ia) and paragraph 48A(5)(c)). This includes exploration expenditure actually incurred by the vendor in relation to the project, uplifted frontier expenditure of the vendor in relation to the project, and any amounts the vendor itself is taken to have incurred by operation of subparagraph 48(1)(a)(ia) or paragraph 48A(5)(c) (under the definitions of incurred exploration expenditure amount of clause 1 of the Schedule). Expenditure that the purchaser is taken to have incurred by application of these rules is taken to have been incurred at the time when the vendor incurred it, or is taken to have incurred it.[10] This kind of expenditure taken over in this way is commonly referred to as 'inherited exploration expenditure'.

Project did not have a production licence before the inherited expenditure is sought to be transferred

34. Where an exploration right or retention lease exists (but not a petroleum project as defined in section 19, because there is no applicable production licence) in relation to the transferring entity then the amount of transferable exploration expenditure that may and must be transferred to any other project, if all the relevant provisions in Part 5 of the Schedule are met, is calculated in accordance with the terms of Part 4 of the Schedule.

35. Transferable expenditure that is incurred in respect of an exploration permit or retention lease prior to an issue of a production licence is calculated in accordance with the terms of Part 4 of the Schedule. The undeducted exploration expenditure is transferable in the same way as transferable expenditure incurred in respect of a project.

36. Non-transferable expenditure is calculated in accordance with the terms of Part 4 of the Schedule for each financial year and is then added up to give a total amount (Clause 15 of the Schedule). This assessment is performed afresh for each financial year.

37. Under subclause 15(1) of the Schedule, if assessable receipts derived in relation to the notional project exceed deductible expenditure then all (if any) exploration expenditure is excluded from transfer.

[10] Subsections 48(2) and 48A(7).

38. Paragraph 15(1)(a) of the Schedule is about all exploration expenditure of the year, whether actually incurred or acquired, including any uplifted frontier expenditure (that is, exploration expenditure uplifted because it is in relation to a designated frontier area). However the exclusion in paragraph 15(1)(b) of the Schedule is based on an equality or excess of total assessable receipts for the year, including acquired receipts, over total deductible expenditure actually incurred, excluding acquired expenditure. Once there is no net deductible expenditure actually incurred remaining, all exploration expenditure of the year must be excluded from being transferable.

39. Subclause 15(2) of the Schedule then identifies the part of the exploration expenditure that will be available for transfer as limited to the excess of the year's total deductible expenditure actually incurred by the person – necessarily excluding any acquired expenditure – over the year's assessable receipts – including any acquired receipts. (This amount includes any uplifted frontier expenditure for designated frontier expenditure actually incurred by the person, under paragraph 15(2)(b) of the Schedule.)

40. Subclauses 15(3) and 15(4) of the Schedule simply create an 'oldest first' rule for excluding the exploration expenditure actually incurred, where the year's exploration expenditure exceeds the year's cap.

41. Clause 15 of the Schedule is a current year rule to work out how much of the year's exploration expenditure actually incurred by the person (including uplifted frontier expenditure for designated frontier expenditure actually incurred) is available for or excluded from possible transfer. It works before the whole-of-project rules in clauses 16, 17 and 18 of the Schedule which further test on the basis of expenditures and receipts over the whole notional project.

42. Clause 16 of the Schedule then works out the amounts needed in calculating what expenditures over the life of the notional project (since the beginning of transferability, 1 July 1990) and to the end of the year, may be considered for transfer under Part 5 of the Schedule. The transferable amounts are worked out by reference to the total amounts of receipts derived and the total expenditures incurred from 1 July 1990 up to the end of the financial year in relation to which the transfer is to take place. These total amounts are the 'notional' amounts.

43. Only exploration expenditure of a permit or lease that exceeds assessable receipts (after deducting other expenditure), and was not excluded by clause 15 of the Schedule, can be transferable expenditure.

44. Consequently, if notional assessable receipts exceed notional deductible exploration expenditure no exploration expenditure is transferable. (Clause 17 of the Schedule).

45. Conversely, if notional deductible expenditure exceeds notional assessable receipts and the excess equals or exceeds notional exploration expenditure then an amount called the reduced notional expenditure (that is, so much of the exploration expenditure as was not excluded by clause 15 of the Schedule) is transferable. (subclause 18(1) of the Schedule).

46. Both notional deductible expenditure and notional exploration expenditure are limited to deductible expenditure or exploration expenditure 'actually incurred' by the person. Part 4 of the Schedule does not make reference to the term *'incurred exploration expenditure amount'* as defined in Clause 1 of the Schedule.

47. 'Incurred exploration expenditure amount' specifically refers to any amount that a person is taken to have incurred by subparagraph 48(1)(a)(ia) or paragraph 48A(5)(c). It is not relevant to the operation of Part 4 of the Schedule.

48. There is no specific reference to sections 48 or 48A in Part 4 of the Schedule nor can it be inferred that the Part includes sections 48 or 48A 'inherited expenditure'.

49. Therefore, any potential amounts inherited under sections 48 or 48A are not 'transferable exploration expenditure' under Part 4 of the Schedule for the purposes of Part 5 and 6 of the Schedule.

50. Any 'transferable exploration expenditure' would also need to satisfy the 'common interest rule' in subclauses 22(1) and 31(1) of the Schedule if the transfer is to projects of another group company.

51. Clauses 2 and 3 of the Schedule outline the requirements of what it means to have held an interest in relation to a petroleum project at a particular time, for the purposes of the Schedule.

52. A person will be taken to have held an interest in a petroleum project at any time they were entitled to receive receipts from the sale of petroleum from the project's production licence area, retention lease area or exploration permit area as applicable at the time or from the sale of marketable petroleum commodities produced from such petroleum.

53. Subject to a number of exceptions (contained in subclauses 22(2), 22(2AA), 22(2AB), 22(2A), 22(3) and 22(4) of the Schedule),[11] the 'common interest rule' states that the person must have held an interest in both the transferring project or exploration right[12] and the receiving project at all times from the beginning of the financial year in which the expenditure was incurred to the end of the transfer year (clause 22(1) of the Schedule).[13]

54. The question is whether the person has an interest at every relevant time.

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[11] Also refer to exceptions in relation to group companies in subclauses 31(2) and (3) of the Schedule.
[12] An exploration right includes both exploration permits and retention leases: ***exploration right***, clause 1 of the Schedule.
[13] See also subclause 31(1) of the Schedule in relation to Group companies.

55. Expenditure in relation to a project can be transferred if the earliest relevant exploration permit is granted, or the person's interest in the project is acquired, during the year and the expenditure is actually incurred by the person after that time (clauses 22(2) and 22(2AA) of the Schedule).

56. Under these circumstances the person doesn't need to hold the interest in the transferring entity for the whole year if the expenditure is actually incurred after the interest is acquired, or if the interest was held from the date of the earliest relevant exploration permit and that was granted only during the year. The expenditure can be transferred under these circumstances so long as it was incurred by the transferee and does not represent inherited expenditure under sections 48 or 48A (paragraph 22(2AA)(c) of the Schedule).

57. As the inherited exploration expenditure under sections 48 or 48A is taken to have been incurred by the purchaser at the time the vendor incurred it,[14] where the person had no prior interest in the transferring project they will be unable to satisfy the 'common interest rule' in subclause 22(1) of the Schedule.

58. Therefore, the person will not be able to transfer the 'inherited exploration expenditure' they are taken to have incurred because of the operation of sections 48 or 48A pursuant to sections 45A or 45B.

[14] Subsection 48(2) and 48A(7).

Appendix 2 – Detailed contents list

59. The following is a detailed contents list for this Ruling:

References

Previous draft:

Previously issued as TR 2008/D7

Related Rulings/Determinations:

MT 2004/1; TR 2006/10

Subject references:

- petroleum
- petroleum industry
- petroleum resource rent tax
- PRRT assessable petroleum receipts
- PRRT augmented bond rate exploration expenditure
- PRRT deductible expenditure
- PRRT exploration expenditure
- PRRT GDP factor expenditure
- PRRT petroleum projects
- PRRT transferable exploration expenditure

Legislative references:

- PRRTAA 1987
- PRRTAA 1987 2
- PRRTAA 1987 12
- PRRTAA 1987 13
- PRRTAA 1987 19
- PRRTAA 1987 20
- PRRTAA 1987 21
- PRRTAA 1987 22
- PRRTAA 1987 45
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- PRRTAA 1987 45A
- PRRTAA 1987 45B
- PRRTAA 1987 45C
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- PRRTAA 1987 48(1)(a)
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- PRRTAA 1987 48(1A)
- PRRTAA 1987 48(2)
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- PRRTAA 1987 48A(3)
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- PRRTAA 1987 Sch Cl 22(2AB)
- PRRTAA 1987 Sch Cl 22(2A)
- PRRTAA 1987 Sch Cl 22(3)
- PRRTAA 1987 Sch Cl 22(4)
- PRRTAA 1987 Sch Pt 6
- PRRTAA 1987 Sch Cl 31
- PRRTAA 1987 Sch Cl 31(1)
- PRRTAA 1987 Sch Cl 31(2)
- PRRTAA 1987 Sch Cl 31(3)
- PRRTAA 1987 Sch Pt 7
- Petroleum Resource Rent Tax Act 1987

ATO references

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