

Mineral Royalty Act: Royalty Guideline – RG-MRA-008 Eligible Exploration Expenditure

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Purpose

1. This Guideline explains the operation of eligible exploration expenditure (EEE) as defined in the Mineral Royalty Act 1982 (NT) (the MRA) and how the Territory Revenue Office (TRO) will administer the deduction in the calculation of net value for royalty purposes.
2. This Guideline is issued by the Secretary under section 4E of the MRA.

Introduction

3. Section 10 of the MRA sets out the formula for calculating the net value of a saleable mineral commodity sold or removed without sale from a production unit. The rate of royalty is applied to the net value to establish liability for the relevant royalty year.
4. Net value is calculated in accordance with the formula:

$$NV = GR - (OC + CRD + EEE + AD)$$

where:

NV is the net value from a production unit in a royalty year.

GR is the gross realisation from the production unit in the royalty year.

OC is the operating costs of the production unit for the royalty year.

CRD is the capital recognition deduction.

EEE is any eligible exploration expenditure.

AD is any additional deduction under section 4CA.

5. EEE is defined in section 4 of the MRA and is the focus of this Guideline.

What is EEE

6. To qualify as EEE, the expenditure incurred by the royalty payer (which must be reasonable in amount) must be in respect of work carried out:
 - (1) in the Northern Territory on or after 1 July 2003
 - (2) or outside the Territory
 - (3) in connection with a mineral occurrence on a mining tenement which forms part of the production unit
 - (4) and directly in respect of the exploration for determining the existence, location, extent or quality of a mineral occurrence on the land comprised in the mining tenement, parent exploration retention licence or parent mineral exploration licence in retention (ERL) or mineral authority corresponding to that licence from which the mineral is ultimately derived.

Mineral Royalty Act: Royalty Guideline – RG-MRA-008 Eligible Exploration Expenditure

7. As paragraph 6(4) makes clear, the underlying title is critical to determining whether the exploration expenditure is an allowable deduction. The definition of 'mining tenement' under the MRA specifically excludes, for example, a mineral or extractive mineral exploration licence within the meaning of the *Mineral Titles Act 2010* (NT) (or successor legislation). Therefore, any exploration expenditure incurred on an exploration licence is not recognised as EEE for royalty purposes.
8. In addition, exploration expenditure incurred on a mining tenement that does not form part of the production unit, or on land comprised in an area subject to an ERL that does not later become a mining tenement that forms part of the production unit, is not considered EEE for royalty purposes. Critical to the recognition of EEE is the concept of a production unit. Guideline [RG-MRA-002](#): Production Unit provides further information on the key concept of a production unit.
9. Expenditure (reasonable in amount) incurred by the royalty payer that is directly attributable to exploration work on land that comprises a mining tenement that forms part of the production unit or parent ERL may be claimed as EEE. This can include, but is not limited to, the costs of the following activities:
 - (5) digging pits, trenches and holes, and sinking bores and tunnels in, on or under the mining tenement to ascertain the quality, quantity or extent of ore or other material
 - (6) drilling or other methods undertaken to ascertain the quality, quantity or extent of the ore body (provided they do not relate to an ore body subject to an existing mine pit)
 - (7) extracting and removing ore, material or other substance for sampling and testing (provided they do not relate to an ore body subject to an existing mine pit)
 - (8) diverting water from any natural spring, lake, pool or stream situated on or flowing through the mining tenement
 - (9) sinking a well or bore on the mining tenement and extracting of water for any purpose in connection with exploring for minerals on the mining tenement
 - (10) pegging and surveying
 - (11) producing exploration data, including maps, photos and remote imagery
 - (12) depreciation in relation to capital items used in exploration activities.
10. If the expenditure is only partly attributable to mineral exploration work on either a mining tenement that forms part of the production unit or on land comprised in a parent ERL that subsequently forms part of the production unit, only an appropriate proportion of the expenditure may be claimed as EEE for the production unit.
11. Types of expenditure that are not generally considered to be EEE include, but are not limited to:
 - (1) tenement rentals
 - (2) costs not directly related to mineral exploration such as entertainment expenses, donations, gifts, interest and financing costs
 - (3) development and production of the existing mine
 - (4) acquisition costs of tenements
 - (5) purchase cost of capital items
 - (6) payments by way of compensation made to traditional Aboriginal owners or representatives of traditional Aboriginal owners under the *Aboriginal Land Rights (Northern Territory) Act 1976* (Cth).

Mineral Royalty Act: Royalty Guideline – RG-MRA-008 Eligible Exploration Expenditure

12. Any expenditure relating to the setting up and operation of the production unit should be claimed as a capital recognition deduction. For example, shaft sinking and cross cutting to provide access to an ore body is more appropriately to be treated as eligible capital assets expenditure. Guideline [RG-MRA-006](#): Capital Recognition Deduction provides further information.

Maximum EEE deduction cap

13. For royalty periods commencing on or after 1 July 2004, EEE can only be used as a deduction to reduce the royalty payable on the basis of net value by a maximum of 25 per cent of the amount of royalty that would otherwise be payable had EEE not been taken into account. This is best illustrated by example 1.

Example 1

In respect of the 2016-17 year, a royalty payer has incurred \$400 000 in EEE and has calculated the EEE claimable as follows:

	\$
Gross realisation	6 000 000
Less: Operating costs	(3 500 000)
Less: Capital recognition deduction	(1 050 000)
Less: Additional deduction	(0)
Equals: Net value	1 450 000
Less: Royalty threshold	(50 000)
Royalty value for EEE calculation	<u>1 400 000</u>
EEE claimable @ 25 per cent	<u>350 000</u>

As the production unit has calculated a positive net value, \$350 000 is the maximum EEE deductible in the 2016-17 year (25 per cent of the positive net value). This results in a net value for the royalty year of \$1 050 000.

The remaining unused portion of EEE of \$50 000 (\$400 000 - \$350 000) may be carried forward for use as a deduction in a future royalty period.

EEE is not applicable as a deduction when the royalty payer is in a negative net value position for a royalty year

14. EEE can only be used to reduce the net value to nil. Accordingly, if a royalty payer has arrived at a negative net value for royalty purposes after deducting operating costs, capital recognition deduction and any additional deduction from the gross realisation amount, EEE cannot be included to further increase the negative net value of the production unit.

Example 1

In respect of the 2016-17 year, a royalty payer has incurred \$500 000 in EEE and has calculated the net value as follows:

	\$
Gross realisation	4 500 000
Less: Operating costs	(2 900 000)
Less: Capital recognition deduction	(1 900 000)
Less: Additional deduction	(0)
Equals: Negative net value	<u>(300 000)</u>

As the production unit has calculated a negative net value, the EEE of \$500 000 cannot be applied as a royalty deduction in the 2016-17 year. However, the unused EEE may be carried forward for use as a deduction in a future royalty year for the purpose of calculating net value.

Carrying forward unused EEE

15. Royalty payers can carry forward any EEE they incur after 1 July 2003 that is not used, either because the production unit is in a negative net value position or the total EEE able to be claimed is in excess of the maximum deduction cap. The Secretary's approval to carry forward the unclaimed EEE is not required.
16. There is no time limit for the carrying forward of unused EEE. Accordingly, EEE can be carried forward until such time that it is fully utilised as a royalty deduction.

Transferability of EEE

17. EEE relates to exploration expenditure incurred by a royalty payer. Accordingly, it remains with the royalty payer who actually incurred the expenditure and cannot be transferred to another person.

GST

18. An amount of EEE is the amount exclusive of the GST (if any) payable in relation to that expenditure. Where an item of EEE is input taxed, the amount claimable is inclusive of GST.

Record keeping requirements

19. For general record keeping requirements, refer to [MRA Overview](#).
20. Every royalty return lodged with the Secretary must be assessed under section 18 or 19 of the MRA. In order for an assessment to be made, an audit may be conducted by an authorised officer to verify the information contained in the royalty return. This may be carried out at the mine site or the royalty payer may be requested to provide certain information.
21. For assessment or audit purposes, proper records must be kept and be made available to substantiate the costs claimed as EEE, including detailed cost schedules supported by source documentation relating to the relevant mining tenements and parent ERLs.

Mineral Royalty Act: Royalty Guideline – RG-MRA-008 Eligible Exploration Expenditure

22. The eligibility of EEE incurred may be reviewed by the Secretary in the year that the expenditure is incurred. This will allow any excess EEE to be carried forward into the next return period and alleviate the need to continually verify past excess EEE when it is ultimately claimed. However, as this may be subject to further review or audit, it is important that royalty payers retain their records relating to EEE.

MRA publications

23. Guideline [RG-MRA-001](#): Guidelines and Advance Opinions, which sets out information on the Guideline system, is incorporated into and read as one with this Guideline.



Michael Butler
Secretary
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For further information, please contact the Territory Revenue Office:

GPO Box 154
Darwin NT 0801
Email: ntrevenue@nt.gov.au
Phone: 1300 305 353
Website: www.revenue.nt.gov.au