Revenue grab creates little revenue

Economics & Deregulation and Governance & Service Provision | Alan Moran Bookmark
The Drum Unleashed 5th July, 2010

The Resources Super Profits Tax (RSPT) comprised two aspects. One was its naked theft of decades of shareholder investment. The other was a tax increase on new mines that would derail the locomotive of the Australian economy.

The focus of the Minerals Resource Rent Tax (MRRT) as a replacement of RSPT is on substituting current output based royalties with profit based royalties. Many see advantages in this and profits based royalties are quite common throughout the world. But a mechanical change of this nature is not consistent with the Government's revenue estimates. The RSPT was estimated to raise an additional $9 billion a year. Based on Government statements, MRRT still raises $7.5 billion a year.

On the information that the Government has presented, it is however difficult to see how the replacement MRRT collects any additional revenue at all. The RSPT applied to the written down assets of mines but MRRT is levied on their current valuations. This removes the retrospective tax aspect which accounted for almost all the previously envisaged tax revenue. Furthermore, MRRT is restricted to iron ore and coal and its rate is reduced from 40 per cent to, in effect, 22.5 per cent.

Other elements of the MRRT would also reduce its revenue raising capacity. Thus, the tax free threshold becomes the bond rate plus 7 per cent - about 13 per cent compared with under 6 per cent for the RSPT and new investment is eligible for an immediate write-off.

Moreover, in the case of iron ore, state royalties are likely to generate more tax revenue than the MRRT. This is because MRRT is to be levied "as close as possible to the point of extraction", whereas the present royalty is levied at the port. As demonstrated by the prolonged litigation over the use of BHP and Rio's Pilbara rail lines, iron ore at the mine head is worth very little.

The Gillard Government recognises that confiscating part of existing investment streams leads the dispossessed to fight tooth and nail. And no special tax is actually justified. According to the Australian Tax Office, mining paid an effective tax rate of 28 per cent in 2007/8 (41 per cent including royalties) compared with the average tax rate across all sectors of 25 per cent.

Unlike measures that expropriate existing investments, an increased tax on new projects is a legitimate area for governments to consider. However, potential resource development cannot simply be milked.

The experience of increased levels of taxation in South Africa, Mongolia, and different Canadian provinces demonstrates the footloose nature of exploration expenditure. In all these cases higher taxes led to marked reductions in exploration activity. Australia enjoys no domination of mineral reserves, not even in coal or iron ore - and the enthusiasm that governments of Australia's rival mining provinces have expressed for our proposed new tax baggage is colourful evidence of this.

Julia Gillard says, "Australians are entitled to a fairer share of the mineral wealth ... that we all jointly own and ... can only be dug up and sold once". But for all practical purposes, mineral deposits, like iPads and AIDS drugs, only exist if someone discovers or invents them. A special tax on them will seriously dampen the search for hidden wealth. Hence, any government demanding significantly more sit-down money masquerading as "fairness" is likely to see a reduced income stream for the nation as a whole.

For Australia, this is especially the case if the target is mining where local firms have demonstrated

world leadership. Australia imposing an additional tax rate on mining is like the US placing punitive taxes on Apple, Google and Cisco. And the effect would be similar - the assembled skills would move or at least see their activities directed to overseas locations.

The fact is that there are not and cannot be any super profits, or "rents" in mining for governments to tax. Entry into the mining industry is open-ended and the existing players are ferociously rivalrous. Profits of miners can never be sustained at levels significantly above those of average businesses. Any super profits are whittled down by competition from new ventures.

This is evident in long term profit data. Australian miners' annual return on capital from 1973 to 2009 was 14.7 per cent, somewhat higher than the all industry average of 13.6 per cent. Two decades ago, the mining industry's long term return on capital was 11.7 per cent, considerably below the 14.7 per cent average for all industries. Mining could again experience lower than average profit levels - and very quickly if the Chinese economy is wobbling.

The Government has said the new MRRT will "provide certainty". This is a curious statement from a government that has created turmoil by announcing, out of the blue, a massive revenue grab. It is made all the more so by the lack of detail on the provisions of the tax and how it raises the revenue claimed of it.

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> November
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> June
> May
> April
> March
> February
> January
2012

> December
> November
> October
> September
> August
> July
> June
> May
> April
> March
> February
> January
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2010
2009
2008
2007
2006
2005
2004
2003
2002
2001
2000
1999
1998
1997
1996

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