

Cases:

Mount Isa Mines Ltd v Seltrust Mining Corp. Pty Ltd Unreported, Supreme Court of Western Australia, No 1614 of 1985, 5 July 1985

United Dominions Corp Ltd v Brian Pty Ltd (1985) 157 CLR 1

Millhouse A. “Financing Joint Ventures” in W.D. Duncan (ed), *Joint Venture Law in Australia*, The Federation Press, Sydney, 1994, Chapter 5

The second part of Millhouse’ paper considers the important financial implications flowing from a venture being deemed a partnership at law. He discusses the distinctions between the powers and rights of partners as compared to venturers in an unincorporated (non-partnership) joint venture, namely the power to pledge the credit of fellow partners; the right to have partnership property applied in payment of the debts and liabilities of the firm; the status of a partner’s rights to assets of the venture and the implications of this upon dissolution; and the priority of creditors over lenders pursuant to the *Bankruptcy Act* 1966 (Cth) if the venture is a partnership. Having established the importance of the distinction between an unincorporated joint venture and partnership from a lender’s perspective, Millhouse then covers the legal principles as they have been applied to different unincorporated joint venture situations, arguing that when considering the definition of “partnership” under the various State Partnership Acts, a mining joint venture is less likely to be construed as a partnership than a property joint venture, due to the specific circumstances under which resource projects usually operate.

Legislation:

Partnership Act 1892 (NSW) section. 39

Partnership Act 1958 (VIC) section 43

Partnership Act 1891 (TAS) section 39

Partnership Act 1891 (QLD) section 42

Partnership Act 1895 (WA) section 50

Partnership Act 1891 (TAS) section 44

Partnership Ordinance 1963 (ACT) section 45

1.4 Taxation Aspects

Note:

Authors’ reference to either “Ralph Review” or “Ralph Report” refers to the *Report of the Review of Business Taxation: A Taxation System Redesigned* (Canberra: AGPS, 1999) commissioned by the Commonwealth Government under the chairmanship of J.T. Ralph.

Articles

Mykyta T. “Farm-in Arrangements in the Mining Industry: The GST Implications” (2000) 19 *Australian Mining and Petroleum Law Journal* 247

Mykyta gives a clear and concise explanation of the problems arising in the application of the “*GST Act*” to farm-in/farm-out arrangements. Through a hypothetical case study, the author

demonstrates how both the exploration activities of the farming-in entity, and the giving of an interest in return by the farming-out entity, may constitute “supply” for “consideration” subject to Goods and Services Tax (“GST”). However in the circumstances of a farm-in agreement, the supply of exploration services (consideration for tenement interest) is periodic and progressive, while the rights to the tenement (consideration for services) are conditional, creating potential cash flow problems because the GST liability and claiming of imputation tax credits are unlikely to arise in the same tax period. Mykyta offers several solutions, including (i) treating the transaction as a supply of a going concern, so that the transfer of the interest in the tenement would be GST-free; (ii) utilising the GST joint venture provisions, such that supplies and acquisition are treated as akin to transactions made within an entity (although the author raises concern that on the facts of *Pursell v Newberry*, a farm-in may not fit the description of ‘joint venture’ for tax purposes, and even if it did, may not alleviate the compliance burdens imposed in a farm-in arrangement); or (iii) invoking the discretion of the Commissioner of Taxation to override the general attribution rule and determine a different tax period to that in which the GST liability or the entitlement to an imputation tax credit is ordinarily attributable.

Cases:

Pursell v Newberry (1968) 118 CLR 381

Legislation:

A New Tax System (Goods and Services Tax) Act 1999 (“GST Act”)

Magney T.W. and Green P.C. “Taxation of General Mining and Petroleum - Selected Aspects”

Papers presented at the *Taxation Convention* arranged by the Western Australian Division of the Taxation Institute of Australia, 13-14 August 1982

In selecting particular tax aspects of mining and petroleum joint ventures for discussion, Magney and Green undertake an authoritative and thoroughly comprehensive analysis of the application of the relevant provisions of the *Income Tax Assessment Act 1936* (Cth) (ITAA) to:

- “allowable capital expenditure” under Division 10 (section 122A) and 10 AA (section 124AA) of the ITAA, including section 124AB and section 122B notices
- disposal, loss, destruction, or termination of use of property - sections 122K and 124AM
- “transferring the benefit of expenditure” - section 122B and 124AB
- petroleum farm-in arrangement
- change of interests - sections 124AO and 122R.

Legislation:

Income Tax Assessment Act 1936 (Cth)

Birch C. “Tolling Companies and their Income Taxation Features” (2002) 5(2) *Journal of Australian Taxation* 213

This in-depth and extensive analysis compares the income characteristics (including compliance costs features) of tolling companies with unincorporated joint ventures and equity joint ventures. Birch discusses the fiscal benefits of using tolling companies and provides a tax accounting model for determining tolling charges. Practical and detailed consideration is given to the procedures by which tolling charges can be determined, including the costs of assessing whether the “carrying on business” test is satisfied under the *Income Tax Assessment Act 1997* (Cth) (ITAA97), and the application of Part IVA of the ITAA97 to tolling companies.

Birch then provides a lengthy discussion of the costs of complying with s 51AD of the *Income Tax Assessment Act 1936* (Cth) (ITAA 36), and of entering into long-term supply contracts. He argues that it is essential that a tolling company enter into take-or-pay long term purchase agreement that contains guaranteed purchase prices and income levels, regardless of output, to ensure a sufficient income stream to service and repay the debt, and to protect against cash-flow fluctuations. The impact of the Ralph Review on section 51AD (ITAA 36) is also considered. Birch concludes that while tolling companies facilitate fiscal benefits for participants by transferring the incidence of income tax in respect of a business activity to them, those fiscal benefits come at the cost of compliance costs., which can erode the fiscal benefits derived.

In the last part of Birch’s paper, he discusses the advantages and disadvantages of the use of tolling trusts, and compares this structure with the royalty trusts used in Canada and the United States.

Legislation:

Income Tax Assessment Act 1936 (Cth)

Income Tax Assessment Act 1997 (Cth)

Purcell L.E. “Ralph Business Tax Reforms Relevant to the Resources Industry” Paper presented at *Australian Mining and Petroleum Law Association Twenty-fourth Annual Conference, Fremantle, Western Australia, 26-29 July 2000, Session 3*

This paper considers the impact of the Ralph Report * review of business tax reforms on many areas of corporate transactions in the resource industry, including treatment of physical assets (accelerated depreciation no longer applies however companies may still choose their own effective life rate, which must be disclosed in income tax returns); capital expenditure provisions; corporate reconstruction; and new developments affecting realised tax losses. Purcell also looks at proposed changes in the tax treatment of farm-outs (Tax Value Method), information, blackhole expenditure, consolidations, mergers and acquisitions, and special due diligence issues. Specifically, the new proposals for taxation for joint ventures is considered in detail.

Reports:

* *Report of the Review of Business Taxation: A Taxation System Redesigned* (Canberra: AGPS, 1999)

Snowsill K. “Commentary on Practical Issues for Resource Companies under the *Income Tax Assessment Act*” [1985] *Australian Mining and Petroleum Law Association Yearbook* 161

The first part of Snowsill’s paper canvasses in detail, the legal and accounting aspects of the mining and petroleum deduction provisions under the *Income Tax Assessment Act* 1936 (Cth) (“ITAA”), specifically:

- exploration and prospecting expenditure (section 122J Division 10; section 124H Division 10AA)
- deductions for exploration expenditures and associated problems (section 124AH Division 10AA)
- allowable capital expenditures (section 122A Division 10; section 124AA Division 10AA)
- deductions for allowable capital expenditure (124AC to 124AE Division 10AA)
- Division 10 and 10AA deductions and carry forward losses.

Snowsill then comprehensively deals with the legal and practical difficulties associated with specific items of expenditures, namely: feasibility studies; costs of exploration licences; farm-ins; environmental and closure costs; and foreign exchange losses.

Phillips I. “Commentary on Practical Issues for Resource Companies under the *Income Tax Assessment Act*”[1985] *Australian Mining and Petroleum Law Association Yearbook* 154

Phillips provides a short but detailed commentary on the mineral transportation provisions under Division 10AAA of the *Income Tax Assessment Act* 1936 (Cth). The latter part of the paper addresses the consequences of disposing of a whole or part of an interest in mining or petroleum property, in its various forms, in particular, the problems in ascertaining what is deductible “expenditure” under sections 122K, 123K and 124AM, and capital gains tax implications.

Legislation:

Income Tax Assessment Act 1936 (Cth)

Henderson R. “Taxation of Joint Ventures” *Joint Ventures*, Seminar held on 25-26 September 1996, Melbourne and Sydney, Business Law Education Centre, 1996

presented again in updated form as:

Henderson R. and Tan T. “Taxation of Joint Ventures” Paper presented at BLEC Seminar in May 1998, *Annual Joint Ventures Seminar*, Business Law Education Centre, Sydney, 2000

This paper focuses on practical tax issues beginning with a comparison of the different tax implications of alternative structures used for joint ventures (company; partnership; unincorporated joint venture; and hybrid structures). The second part of the paper uses a case study example of an unincorporated (but hybrid) joint venture to explore some of the tax issues arising, including: structuring issues; direct holding of mining assets; use of an incorporated operator (including fringe benefit tax aspects); sales and marketing, and funding and finance issues. The paper concludes with an examination of a number of complex issues arising out of changes in joint venture interest, and the application of *Income Tax Ruling* 2378 on farm-ins.

Legislation:

Income Tax Assessment Act 1997 (Cth)

Income Tax Ruling 2378

**Birch C. “Choosing the right Joint Venture Structure for a Farm-in or Farm-out” (2002)
5(1) *Journal of Taxation* 60**

Birch examines in detail, the compliance costs associated with income taxation of farm-outs, which will vary depending on (i) the structure of the farm-outs agreement, (ii) whether the taxpayer is a farmer or farmee, and (iii) whether the farmer and farmee is an equity participant.

He begins by describing a farm-out, but notes the type of interest will vary according to the different structures associated with joint ventures (in an unincorporated joint venture, participants have a direct interest in the assets of the ventures, as tenants in common, whereas in an incorporated joint venture, the equity participants hold only a shareholding in a special Purpose Vehicle (SPV) incorporated specifically for the venture purpose).

Birch discusses the practical and commercial reasons for utilising a farm-out, and the manner in which farm-outs can be legally structured, namely as a “deferred transfer farm-out” (where the farmee agrees to undertake certain obligations following which it is entitled to take an interest in the exploration title - these arrangements are usually drafted as an *option*, or an *executory contract to assign*) or as “immediate transfer farm-outs” (which involve an immediate transfer of an interest subject to an obligation to re-convey in the event of default in performance of farm-in obligations). Other farmout arrangements exist, for example, stepped or incremental earning programmes and the definition of farmout adopted by the Commissioner of Taxation in *Income Tax Ruling 2378* (IT 2378, para 1) encompasses a wide variety of arrangements. The major types of farm-outs are described, namely, carried interest agreements; unitised agreements; earned obligation agreements; production payment agreements and overriding royalties; and equalisation agreements.

In the second part of his paper, Birch analyses in detail, the compliance costs of farm-outs of assets. Issues examined include the costs associated with characterising the profit from a farm-out, under the provisions of the *Income Tax Assessment Act 1997 (Cth)* (“ITAA97”) according to the concepts of ordinary income and statutory income (including capital gains and expenses) and losses of either a revenue or capital nature. It follows that the proceeds from a farm-out of assets may be taxed in a variety of ways depending on the purpose for which the assets are held, before they are disposed of. Birch also discusses the situation where prospecting entitlements fall within the meaning of “trading stock” and problems in determining the cost price of trading stock. The implications for changes under the Ralph Review * to both these areas of tax law are also considered.

Birch draws attention to the complications that can arise when making depreciation balancing adjustments, if the parties’ intentions are not sufficiently documented during the drafting phase of

the farm-out agreement. He suggests that if parties enter into an agreement to transfer allowable capital expenditures, then a taxation clause could be included in the farm-out agreement. He provides a draft tax clause that may be used in the farm-out agreement (depending on the nominal value on the interests the subject of the farm-out) to cover the situation where a farmer disposes of its undivided fractional interest in exploration plant, or arguably to exploration or prospecting expenditures when a prospecting entitlement is disposed of.

Birch then examines in detail, the complex taxation problems arising under the ITAA97 in relation to (i) mining information; (ii) allowable deductions to the farmee for exploration and prospecting expenditures; (iii) capital gains provisions (eg. determining if a farmee has an equitable interest if it is under no obligation or limited obligation to earn an interest and determining what will amount to capital gains tax events) and (iv) calculating consideration on disposal.

The final part of the paper looks at compliance costs of farm-outs of shares. Birch concludes that a farm-out structured as a disposal of assets, bears more compliance costs than farm-outs structured as options over shares.

Legislation:

Income Tax Assessment Act 1997 (Cth)

Income Tax Ruling 2378

Reports:

* *Report of the Review of Business Taxation: A Taxation System Redesigned* (Canberra: AGPS, 1999)

Green P. "Practical Issues for Resource Companies Under the Income Tax Assessment Act" [1985] *Australian Mining and Petroleum Law Association Yearbook* 115

Green provides an extensive analysis of the tax provisions relevant to resources joint ventures under the *Income Tax Assessment Act 1936* (Cth) ("ITAA36"). Under the heading of exploration of and prospecting, Green considers the operation of sections 124AH, 122J, 122B and 124AB, including expenditure on exploration and prospecting, and petroleum farm-in agreements. He then examines expenditure in the course of "mining operations" and what is permitted as "allowable capital expenditure" as defined in Division 10 and 10AA of the ITAA36. A highly detailed discussion of the function and effect of notices under sections 122B and 124AB follows. Green then deals with transfers, changes of interest, and termination, and specifically with the issues of accessibility of proceeds arising from transfers of property under sections 26AAA or 25A, and with balancing charges.

Legislation:

Income Tax Assessment Act 1936 (Cth)

Poulos P. “Taxation of Joint Ventures” Paper presented at Legal and Accounting Management Seminar, *Joint Ventures: 1998 Seminar Papers, Part III Paper 4, LAAMS Publications, Sydney, 1998*

Poulos considers the range of different joint venture structures and examines the tax advantages and disadvantages of each. Beginning with an incorporated structure, Poulos notes that for the purposes of a joint venture there are no special tax considerations outside those of the normal taxation of companies, but in considering the disadvantages, he advises that for a capital intensive joint venture with start up losses, where the participants require access to losses, the corporate structure is probably not preferred. He then examines the tax implications of an unincorporated joint venture, highlighting the differences between a partnership and an unincorporated joint venture, the latter being preferred over a partnership, as it achieves total tax independence with regard to application election, tax administration and tax compliance. The tax implications of unit trusts, hybrid and new structures (pooled development fund; limited partnership, and production sharing contract) are also considered, along with the potential for the tax avoidance provisions (section 51AD and Division 16D of the *Income Tax Assessment Act 1936*) which can deny deductions when transacting with tax exempt bodies, for example, where “tolling” joint venturers take advantage of depreciation deduction and pass on these benefits to a tax-exempt user.

The second part of Poulos’ paper discusses the issues and tax implications arising with changes in joint venture interests. Capital gains tax (“CGT”) and stamp duty issues are considered for an incorporated joint venture and in relation to an unincorporated joint venture, there is particular emphasis on the potential deemed assessable realisation of trading stock and balancing changes in relation to certain tax deductible assets, when there is a partial change of joint venture interest. Poulos also considers the CGT and stamp duty issues in a farm-in situation, in particular whether the expenditure commitment of the participant farming-in may form part of the sales consideration in respect of the interests being farmed-out, ie. whether it gives rise to a balancing charge recapture. He argues that while *Income Tax Ruling ITR 2378* will allow a farming-in participant to claim a deduction for exploration expenditures (ie. it does not constitute consideration for balancing change and CGT purposes) this may only be the case at an early “wildcat” stage. He also warns that farming-in participants may incur disproportionate expenditure where the participant farming-out is “free carried” and depreciation deductions are based on relevant ownership percentage in the property.

Legislation:

Income Tax Assessment Act 1936 (Cth)

Income Tax Assessment Act 1997 (Cth)

Leslie W.D. “Some Practical Problems of Joint Venture Agreements - Expansions (Including Tax Aspects)” (1981) 3 *Australian Mining and Petroleum Law Journal* 58

Leslie enumerates the principle kinds of expansion involved when one or more parties wish to increase the exploration activities of the joint venture (in area, intensity, or type of mineral) and highlights the practical problems associated with them. When drafting expansion clauses, it is

important to balance the existing rights of the dissenting joint venturers with the desire of the party keen to expand. The kinds of conflict that can arise and methods of reconciling them are considered.

Leslie sets out the mechanisms by which adjustments to parties positions can be effected and the practical issues to consider when drafting such clauses. He warns that careful consideration should be given to tax provisions when drafting expansion clauses, otherwise they may inadvertently cause serious tax consequences, especially to a diluting party. The “change of interest” provisions under the *Income Tax Assessment Act 1936* (Cth) are comprehensively examined, in particular section 59AA covering depreciation on disposed property. Leslie argues that sections 59AA, 122R, 124AO and 123F do not properly apply to changes of interest in joint venture property in the normal kind of non-participatory expansion, and that sections 59, 122K, 124AM and 123C apply to dispositions of a joint venturer’s individual share of joint venture property, but only where the share is disposed of in its entirety.

Legislation:

Income Tax Assessment Act 1936 (Cth) sections 59, 59AA, 122K, 122R, 123C, 123F, 124AM, 124AO

Bratby W.H. “The Taxation Consequences of the Introduction and Retirement of Participants of Mining and Oil and Gas Ventures” (1983-1984) XVIII *Taxation in Australia* 950

Bratby provides a thorough and comprehensive examination of the taxation consequences of variations to the participants across a range of venture entities in the course of a joint venture. Provisions of the *Income Tax Assessment Act 1936* (Cth) (“ITAA36”) which have a bearing on the re-organisation or restructuring of the various types of ventures are considered, particularly the capital and revenue aspects as between the in-coming and out-going venturers. Part I and II covers changes in shareholders and transfer of activities in companies (including sections 122A, 123A and 124AA on expenditures, sections 59, 122K, 123C and 124AM on disposals, sections 122J and 124AH on exploration expenditures and sections 122B and 124AH on deductions, of the ITAA36). Part III considers the tax consequences of changes in partnerships. Bratby’s commentary in Part IV dealing with changes in variations in joint ventures, provides a very practical and useful commentary on the types and reasons for variations arising and the application of both the general and mining provision (including sections 36, 36A, 59, 59AA, 122B, 122K and 122R of the ITAA36) to those variations.

The second part of Bratby’s paper examines in detail the taxation consequences of farm-in and farm-out arrangements, and problems encountered in practice. This extensive paper also contains four schedules discussing:

1. specific mining provisions which govern or affect the introduction or retirement of participants;
2. sections which are concerned with the quantum of consideration;
3. differences in the disposal sections; and
4. section 124AJ plus Treasurer’s comments.

Legislation:

Income Tax Assessment Act 1936 (Cth) sections 36, 36A, 59, 59AA, 122A, 122B, 122K, 122J, 1122R, 123A, 124A, 124AA, 124AH, 124AJ, 124AM

Goddard J.R. “Joint Venture Accounting Procedures” [1985] *Australian Mining and Petroleum Law Association Yearbook* 35

Goddard discusses the practical implications for unincorporated joint ventures and considers the accounting and reporting problems that arise due to the unique nature of this type of joint venture. He first considers the formal reporting and disclosure requirements. As accounting procedures and reporting formats for exploration projects, are different from those needed for active operations projects, he suggests that these differences should be negotiated and agreed in the Joint Venture Accounting Procedures separately. He proposes that the operator should enter transactions on behalf of venturers to minimise disputes, and that the maintenance of a proper fixed assets register should enable the operator to provide sufficient information so each participant can readily account for these assets in their own accounting records. Goddard also suggests the accounting procedures adopted by the joint venture should be clearly set out and designed to disclose financial information in a way that facilitates the alternative tax treatments and accounting practice for each venturer.

Specific problems for management with respect to accounting procedures include: contributions by participants; creditors, accruals and provisions; fixed assets; production and costs; and budgetary controls over expenditure. Considerable discussion follows on the more contentious issues of administration costs and overheads and the methods by which they can be measured; differential contributions; changes in equity interests; and auditing requirements. Included in the appendix is a chart showing the accounting differences between a partnership and an unincorporated joint venture, and a proforma set of accounts for both an exploration joint venture and a joint venture engaged in active operations.

Lowe J.S. “Analyzing Oil and Gas Farmout Agreements” (1987) 41 *Southwestern Law Journal* 759

Written in a United States legal context, Lowe analyses the structure of typical farm-out agreements and considers problems and alternatives that practitioners must confront in drafting or reviewing farmout agreements. His article discusses US tax law related to farm-outs (in particular Review Ruling 77-176 which deals with farmouts) and farmor’s and farmee’s purposes for entering a farmout agreement, both of which will determine how the farmout is structured. The distinction between farmouts and operating agreements is drawn and definitions of support agreements, seismic option agreements, and other variations are given. The paper looks at preliminary matters to be considered, key characteristics of the agreement, and issues that must be addressed in preparing the farmout agreement.

The greater part of this article then proceeds to analyse in detail the essential elements of a typical US farm-out agreement. Many sample clauses are suggested in the course of the discussion. All

aspects of the drilling process are considered (eg. subject matter, geological information, commencement procedures, measuring of the drilling process, and performance standards) followed by an equally detailed discussion on the drafting of provisions for other issues (eg. tax, liability, reassignment, and environment). Lowe observes in summarising, that farm-out agreements are very much a function of tax rules, and that otherwise, the agreements will vary widely according to the goals of the parties. For this reason, farm-out agreements need to be flexible, and to this end, Lowe provides many alternative provisions.

Regulations:

Revenue Ruling 77-176

Moroney D.F. “Sole Risk in Mining and Petroleum Ventures: An International Perspective” [1986] *Australian Mining and Petroleum Law Association Yearbook* 164

The three different forms of penalty (production, cash and acreage) are discussed, and Moroney advises that penalties need to be considered from the point of view of the particular tax regimes jurisdiction (eg. will penalty payment be liable to income tax, or capital gains tax for the sole risk participant) and legal regimes (eg how will the local regulatory authority treat change of ownership inherent in varying rights to oil among the licensees.) Moroney describes the two types of oil fiscal regimes which exist in the world, namely royalty and tax regimes (where royalty is charged on a joint and several basis, but taxes are levied on an individual basis) and production sharing regimes (in which a ‘contractor’ (licensee) is responsible for the conduct and cost of all operations net of all taxes, and the host Government (or its national oil company) contracts to share oil produced. As sole risk operations were conceived of under royalty and tax regimes, there can be considerable commercial and accounting problems arising when sole risk operations are carried out under a production sharing regime. Moroney outlines the economic issues, and suggests that by providing in the agreement for ‘cost oil’ (allowed by percentage to the ‘contractor’ to cover production costs) and ‘profit oil’ (balance of oil produced which is shared between the ‘contractor’ and host Government) to be split in participating shares, some of these problems can be overcome.

Nicholls R.C. “Some Practical Problems of Joint Venture Agreements - Independent Operations (Including Some Tax Aspects)” (1981) 3 *Australian Mining and Petroleum Law Journal* 41

Nicholls provides a detailed discussion of the practical and drafting issues involved in accommodating independent operations in both mineral and petroleum exploration. Nicholls sets out the problems associated with cash, production and acreage penalty clauses, with examples given of various types of production penalties, highlighting the different treatment of the ‘recoupment element’ and ‘multiple element’ of the penalty. Nicholls observes that in mineral operations, it is not unusual for a non-consenting party’s working interest in the concession to be converted into either (i) an overriding royalty or gross revenue interest; (ii) a carried interest; or (iii) a net profits interest.

The second part of Nicholls paper identifies the tax aspects and treatment of (a) a cash penalty; (b) a production penalty; (c) an acreage penalty; and conversion of the non-participating party's working interest to (d) a carried interest; (e) a net profits interest; and (f) a net profits interest.

Morgan J. and Anzarut C. "Choice of Structure" *Joint Ventures*, Seminar held on 25-26 September 1996, Melbourne and Sydney, Business Law Education Centre, 1996

This paper provides an introductory overview of the factors to consider when choosing a joint venture structure. The major advantages and disadvantages with respect to tax and legal liability of the most common joint venture structures in Australia (joint venture companies, unit trusts, partnerships, limited partnerships, and unincorporated joint ventures) are covered.

Fahey J. "Tax Effective Joint Venture Structuring" in *The Rights and Duties of Joint Venturers in Tough Times*, Papers delivered at a 2-day Master Class, Business Law Education Centre, Melbourne, November 1990, Part 2 and Part 3

Fahey's paper (constituting Part 2) in this series of seminars, systematically details for each of four joint venture structures (incorporated, trust, partnership, and unincorporated) the tax advantages and disadvantages of each form, and the capital gains tax and tax treatment of joint venture income of each. Consideration is also given to the tax implications of hybrid structures, and to the use of tax exempt entities under the *Income Tax Assessment Act 1936* (Cth). Diagrams with notes explaining each joint venture structures, including tolling arrangements, are attached in the appendices.

Fahey's analysis is supplemented by Part 3, which offers three demonstration case study situations, with solutions as to the most effective structure for tax purposes.

Legislation:

Income Tax Assessment Act 1936 (Cth)

Novell D. "Aspects of Joint Ventures—Accounting procedures" Paper presented at *Second Annual Australian Mining and Petroleum Law Association (WA Branch) State Conference*, Scarborough, Perth, 22 October 1988.

Novell provides a very simple description of the structure of a typical 'joint venture' and 'participant' financial statement, followed by a brief explanation of some of the items commonly found in the statements.

Doran R.J.P. "Commentary on Joint Venture Accounting Procedures" [1985] *Australian Mining and Petroleum Law Association Yearbook* 68

The second part of Doran's paper considers key practical issues in relation to the role of the operator, in particular, monetary profit and conflict of interest. The situation faced by a non-operator, in balancing its approach to the joint venture is discussed, and suggestions given as to the role a non-operating venturer should fulfil. Doran then devotes considerable attention to

practical accounting issues encountered by the operator, in particular, budgetary controls, AFE procedures, and audits, and discusses in detail, the four main mechanisms whereby an operator may recoup its overheads and indirect costs, by way of (i) fixed monthly/annual charges; (ii) percentage of previous/anticipated budgets; (iii) percentage of operator's personnel costs; and (iv) percentage of operator's total administrative expenditures.

Wilson P.J. "Taxation Aspects of Sole Risk or How to Make the Tax System Work for You" (1986) *Australian Petroleum Exploration Association Journal* 123

Wilson describes the taxation implications of a sole-risk program and the taxation results that may be expected to flow to a sole-risk party and a non-sole-risk party. The taxation implications are considered under the headings of (i) income tax; (ii) resources rent tax; and (iii) resource rent royalty. The paper also considers how the tax system can be used to diminish the incentive for a company to allow a party to undertake a sole-risk operation.

Legislation:

Income Tax Assessment Act 1936 (Cth) sections 6, 25, 26, 82 and 124

Books

Milburn J.A. and Chant P.D. *Reporting Interests in Joint ventures and Similar Arrangements, Financial Accounting Series: Special Report, Financial Accounting Standards Board, Connecticut, September 1999*

This paper was developed due to concern over the lack of consistency between joint venture accounting standards and practices of G4+1 members and other jurisdictions. The differences are fundamental and significant, and relate to what should be considered a "joint venture" and the appropriate methods of recognition, measurement, and presentation of interests in a joint venture, however it is defined. Where some jurisdictions permit or require proportionate consolidation of some or all jointly controlled arrangements, others require the equity method of accounting in the same situations. The practical effects of these differences can be significant. This paper examines the conceptual frameworks and issues of the G4+1 jurisdictions and practical considerations involved in addressing these issues.

The paper outlines the basic problem, that the idea of enterprises sharing control over "assets" and business activities with other enterprises seems inconsistent with an accounting framework that defines assets and accounting enterprises in terms of exclusive control relationships. The concept of control and the nature of joint control of venture rights and assets are discussed. Chapter three analyses the three methods for reporting a joint venture interest, namely:

- the equity method (which portrays the venturers' interest by presenting its investment in the net assets of the joint venture);
- the proportionate consolidation method (which present the venturer's interest as a pro-rata portion of each of the assets, liabilities, revenues, and expenses of the venture); and

- the expanded equity method of accounting (which combines elements of the equity method and proportionate consolidation method, by recognising summarised proportional amounts of the assets, liabilities, revenues, and expenses of the joint venture as separate line items within the venturer's financial statements).

The unique characteristics of a joint venture relating to the sharing of their activities, sharing of risks, common control, and collective determination of outcomes, have far reaching implications as to the nature and extent of disclosures necessary to provide users with an adequate understanding of these arrangements, their financial effects, and potential implications for future cash flows.

Each of the Canadian, New Zealand, United Kingdom, United States and Australian jurisdictions are compared. It is noted that in Australia, the Australian Accounting Standards Board (AASB) issued a revised standard, AASB 1006 in December 1998 that defines a joint venture in identical terms to the International Accounting Standards Committee (IASC) and Canadian Institute of Chartered Accountants (CICA) standards. However, the Australian standard goes further and distinguishes *joint venture entities* from *joint venture operations*, and requires use of the equity method for joint venture entities and reporting of the venturers' share of the assets, liabilities, revenues, and expenses of joint venture operations.

Regulations:

Australian Accounting Standards Board – AASB Standard 1006

Wei Y. “The Taxation Consequences of Different Business Structures” in Wei Y. *Investing in China—The Law and Practice of Joint Ventures*, The Federation Press, Sydney, 2000

Wei considers the taxation consequences of choosing different business vehicles. Even though taxation may not be the decisive factor in the process of making an international business choice, it is definitely one of the most important considerations. The first part examines the Chinese taxation consequences of using different foreign investment vehicles. The second part analyses the Australian taxation consequences of these vehicles, leading to the conclusion that a joint venture, especially an equity joint venture, is the most desirable investment structure from a taxation point of view.

Alexander H. “Tax Aspects of Joint Ventures” in W.D. Duncan (ed), *Joint Venture Law in Australia*, The Federation Press, Sydney, 1994, Chapter 7

Alexander provides a comprehensive analysis of several tax aspects of joint ventures. He first discusses in detail, the features which for tax purposes distinguish an unincorporated joint venture from a partnership as defined in the *Income Tax Assessment Act 1936 (Cth)* (ITAA) according to the criteria of (i) joint receipt of income; (ii) “association of persons”; (iii) co-ownership of property; and (iv) “carrying on a business” in participation with others. Alexander describes mutual insurance associations and cost book companies (in which product is shared in kind) as other examples of structures that do not constitute partnerships for tax purposes. While it is

thought that the distinction between these structures and partnerships is found in the application of the “mutuality principle”, this definition becomes problematic when the members of the association are engaged in trading type transactions. By contrast, an unincorporated joint venture more closely fits the mutuality principle, as participants do not trade with each other, but participate in a common enterprise—the product should not be considered as “profits from trading”. However, if the participants were to engage in tolling activities or charge for use of their facilities at a profit, the venture may be characterised as a partnership for income tax purposes.

Also considered in detail, are the circumstances in which an operator, either as agent or independent contractor, is entitled to claim outgoings as an allowable deduction under section 51(1) of the *Income Tax Assessment Act 1936* (Cth).

The second part of Alexander’s paper provides a thorough examination of the tax accounting, income tax, and capital gains tax consequences of classification as a joint venture. In regard to inventory and product, Alexander argues it is better that it be considered trading stock on hand of each participant from the time each is able to dispose of the inventory or product in specie, notwithstanding that they only own undivided interests in the trading stock until its division or appropriation in specie. The division in specie will not involve the disposal of trading stock for the purpose of section 36 ITAA, although it may involve a disposal and acquisition of review assets in the form of undivided interests in that trading stock, which in turn may attract the operation of section 36A of the ITAA. Alexander discusses the operation of depreciation provisions with respect to plant or articles owned by participants including where there is a change in participants, or interests of a participant. Treatment of investment allowances and development allowances (where the joint venture is pre-qualified under the *Development Allowance Authority Act 1992* (Cth)) are also considered. The circumstances in which a profit or gain may be considered income, and where the disposal of an asset will produce assessable capital gain, are examined in detail.

In the final part of the paper, Alexander highlights examples of the use of joint venture vehicles, including an analysis of mining and petroleum joint ventures, and the application of special tax provisions specific to that industry under Division 10, 10AA and 10AAA of the ITAA and under the *Petroleum Resource Rent Tax Assessment Act 1987* (Cth). Also examined in detail is the tax position of non-residents under the ITAA and double tax treaties to which Australia is a party.

Legislation:

Income Tax Assessment Act 1936 (Cth)

Development Allowance Authority Act 1992 (Cth)

Petroleum Resource Rent Tax Assessment Act 1987 (Cth)

Edey P.H. *Accounting for Interests in Joint Arrangements* Australian Accounting Research Foundation, Melbourne, 1985

In the first chapter in this book, Edey sets out the nature of a joint venture and the principal legal and accounting differences between incorporated and unincorporated joint arrangements. An

overview is given of the nature, legal characteristics, and advantages of a joint venture structure. Edey discusses the legal and accounting distinctions between partnerships and unincorporated joint ventures, and provides a table of the major legal and accounting distinctions between the two.

The second chapter examines the different accounting methods (cost method, equity method, proportional consolidation method, and expanded equity method) used for incorporated joint ventures, noting the trend to use jointly owned companies as vehicles for off-balance sheet financing and the use of non-recourse project finance by entities in the extractive industries. He describes the operation of these arrangements, and provides an illustration of the proportional consolidation method for a joint venture with four participants.

Chapter three of Edey's book gives a comprehensive and practical description of the different accounting methods used in (unincorporated) joint ventures and partnerships, under Australian Accounting Standards (AAS). The use of the "line-by-line method" (analogous to proportionate consolidation method) in the balance sheet is considered, and the arguments for, and against its use and application considered in detail. The "one-line" method (analogous to the equity accounting method) is similarly described in detail, with the advantages and disadvantages for its use set out. Edey argues that the two methods embody different views about the nature of a joint venture—the line-by-line methods views a joint venture as a collection of jointly owned assets and more correctly reflect the legal status of a joint venture, while the one-line method views a joint venture as a form of investment which may be more appropriate for many reporting entities from an economic perspective. Edey provides illustrations of both accounting methods for joint ventures, including a sample balance sheet, statement of costs of production, statement of cash receipts and payments, and profit and loss statement.

In Chapter four of his book, Edey deals with accounting issues that arise when entities engage in joint ventures and transact amongst themselves, and considers the methods for accounting for contributions and subsequent transfers of assets to a joint venture. Edey illustrates the points raised in Australian Accounting Standard AAS19 and discusses other common joint venture accounting issues within the context of historical cost accounting. Examples are given of the treatment of contributions of non-monetary assets, contribution of services, and supply of future services, together with examples of the problem in recognising fair value upon a change of proportionate interest and any associated goodwill or discount, or where one participant in effect subsidises the costs of another participant, giving rise to excess and reduced rates of contribution. Edey's final chapter considers disclosure of joint arrangements, in particular AAS 19 and 14 prescriptions on disclosure (name and activities, interest in output, share of assets, and commitments and contingencies) and the case for voluntary disclosure of other aspects of joint venture activity. The appendix contains an extract of AAS 19.

Regulations:

Australian Accounting Standards (AAS) 14 and 19

Wei Y. “Profits and Capital: Non-Taxation Aspects” in Wei Y. *Investing in China—The Law and Practice of Joint Ventures*, The Federation Press, Sydney, 2000

Wei examines remittance of profits and repatriation of capital. The Chinese authorities used taxation and foreign exchange control as a restriction to ensure that foreign investors kept profits inside China for as long as possible. Today, the taxation barrier has been lifted and foreign exchange control has also been eased through mechanisms provided in later legislation. Generally speaking, there are not many problems in remitting profits and investment capital in hard currency out of China on the winding up of foreign investment enterprises.

CONVERSION TABLE

<i>ITAA36</i>	<i>ITAA97</i>
6(1)	4-10; 4-15(2); 6-20; 70-10; 330-25; 330-240; 995-1(1)
25A	15-15
26AAAC	32-70
36(subsections)	385-(subsections)
36(1)	70-85; 70-90; 70-95
122A	330-85; 330-95
122B	330-235; 330-245; 330-250; 330-255; 330-260; 33-265
122J	40-80; 40-730; TP 330-10; TP 330-15; TP 330-20; TP 33-30; 330-305; 330-310; 330-315; 330-35; 330-325
122K	330-480; 330-485; 330-490
122R	330-520
123C	330-405; 330-480; 330-485; 330-490
123F	330-520
124	330-30; 330-125; 330-245; 330-270
124AA	330-85; 330-90; 330-95
124AB	330-235; 330-245; 330-250; 330-255; 330-260
124AC	TP 330-1
124AH	330-15; 330-35; 330-305; 330-310; 330-315; 330-325
124AM	330-480; 330-485; 330-490
124AO	330-520
124H	387-475

1.5 Finance

Articles

Fewster G.H. “Financing of Energy Resource Projects—Commentary” (1982) *Energy Law in Asia and the Pacific* 789, International Bar Association and Lawasia Research Institute, Matthew Bender & Company Inc 1982, Proceedings of Seminar on *Energy Law in Asia and the Pacific*, Singapore 1982

Fewster offers brief but practical comment on a few particular issues related to joint venture financing. In the case of non-recourse or limited recourse financing, Fewster questions the extent