

**In this edition we review the following:**

**The key components of the EDI approved by Federal Parliament.**

## EXPLORATION DEVELOPMENT INCENTIVE PASSED

On 3 March 2015, Federal Parliament passed legislation to implement the Federal Government's election commitment to provide an Exploration Development Incentive (**EDI**).

The EDI aims to encourage investment in small mineral exploration companies undertaking 'greenfields' mineral exploration. The EDI enables investors in these companies to receive a tax incentive where the companies choose to give up a portion of their losses relating to their exploration expenditure in an income year.

In our previous Resources Updates in March and July 2014, we outlined the key components to the proposed EDI as set out in the Federal Government's Discussion Paper released in March 2014.

### Key Components

#### Cap

The total financial impact of the EDI is capped at \$100 million for each of the three income years in which it operates (\$25 million in 2014-2015, \$35 million in 2015-2016, and \$40 million in 2016-2017). The incentive is not available for expenditure incurred in income years after 2016-2017.

#### The EDI system

Overall, the EDI allows eligible exploration companies to convert a portion of their tax loss to exploration credits which can be provided to eligible Australian shareholders to entitle the shareholders to a tax benefit. The form of the tax benefit depends on whether the shareholder is an individual or corporate entity. The EDI is generally not available to trusts, partnerships and exempt entities.

#### Which explorers are eligible to participate in the EDI?

Explorers wishing to participate in the EDI and issue exploration credits to investors will need to satisfy certain criteria:

- (a) The explorer must be a "greenfields mineral explorer" and incur greenfields minerals expenditure for the applicable income year. A greenfields mineral explorer for an income year is an entity (including any entities connected with or which are an affiliate of the first entity) that has not carried on any mining operations in the *current and immediately preceding income years*. The concept of affiliate is wide and will need to be considered carefully where an explorer is part of a group or has common control with other companies in the mining industry.
- (b) The explorer must be a disclosing entity during the applicable income year. A disclosing entity is one whose securities are listed or widely held (more than 100 persons).
- (c) The explorer must have no taxable income for the applicable income year.
- (d) The explorer cannot create exploration credits unless they have reported their estimated exploration expenditure and estimated tax loss for the prior income year to the Commissioner by 30 September of the relevant financial year and the Commissioner has declared the modulation factor for the credits to be created in that income year.

These criteria reflect the intention that the EDI address the tax disadvantage junior companies face relative to larger mining and exploration companies who have an assessable income against which exploration expenditures can be claimed as an immediate tax deduction.

## Eligible Expenditure

The EDI only applies to eligible greenfields exploration expenditure incurred in Australia from 1 July 2014.

Greenfields expenditure includes:

- (a) expenditure on mineral exploration, including geological mapping, geophysical surveys, systematic searches for areas containing minerals and searches for minerals by drilling or other means; and
- (b) expenditure incurred on activities for the purpose of determining the existence, location or quality of a new mineral resource.

The EDI will not apply to expenditure:

- (a) solely for the purpose of identifying the viability, rather than the existence, quantity, quality or location of a resource, such as feasibility studies;
- (b) in relation to exploration and prospecting for petroleum (or oil shale used for the production of petroleum); or
- (c) related to an "Inferred Mineral Resource" or higher classification under the Joint Ore Reserves Committee Code 2012 edition.

## Issuing exploration credits to investors

Participation in the EDI is voluntary. Eligible explorers wishing to participate in the EDI must make an irrevocable choice whether to provide credits to all shareholders or only to holders of newly issued shares (shares issued on or after 1 July 2014). If credits are only provided to holders of newly issued shares, all subsequent shares issued would need to be in a separate class of shares. If the entity does choose to issue credits, the amount issued to each shareholder must be in proportion to the number of shares held.

## Key take-away points:

The EDI is a step in the right direction to encourage investment in junior explorers, at a time where there are difficulties in raising capital for greenfields exploration.

There are, however, limitations and restrictions. Those companies wishing to take advantage of the EDI will need to consider their eligibility carefully.

The effectiveness of the EDI in increasing greenfields mineral exploration will be closely watched.

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