Mining Sector Tax Measures in 2013 Federal Budget

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The 2013 budget (the Budget) released by Canada's federal government on March 21, 2013 (Budget Day) included several tax measures affecting the mining community.

Slower deduction of pre-production mine development expenditures

For tax purposes, many expenditures made by mining companies are treated as either "Canadian exploration expense" (CEE) or "Canadian development expense" (CDE). CEE amounts can be 100 per cent deducted in the year incurred, while CDE amounts are deducted at the rate of 30 per cent per year.

Currently, CEE includes "pre-production development expenditures," being those incurred to bring a new mine into production (and incurred before the mine is producing) in reasonable commercial quantities. Examples include amounts spent clearing or removing overburden, sinking a mine shaft or constructing an adit or other underground entry.

The Budget announced that pre-production development expenses will be treated as CDE, not CEE, starting in 2015. Such expenditures incurred during the period 2015 to 2017 will be treated as partly CDE and partly CEE; after 2017 all of such amounts will be CDE. The pre-Budget rules will apply for pre-production development expenditures made before 2017:

- Pursuant to a written agreement entered into before Budget Day; or
- As part of a mine development where either construction was started or engineering and design work for construction had commenced (as evidenced in writing) before Budget Day.

Slower tax recognition of these expenditures is not helpful for the mining industry, and affected taxpayers should review their expenditures to maximize CEE classification where possible.

Accelerated capital cost allowance eliminated for mining

Expenditures on certain property (depreciable property), such as buildings and equipment, are eligible for "capital cost allowance" (CCA), which is the tax version of depreciation. Each year in computing income, the taxpayer deducts part of the remaining expenditure balance in the relevant class of property (the UCC of that class), such that the property's cost is deducted from income over a period of years for tax purposes.

The CCA rate for most mining depreciable property is 25 per cent. However, in certain circumstances, the taxpayer can deduct up to 100 per cent of the UCC (up to the project's income for the year). This 100 per cent rate generally applies where the property was acquired before the mine came into production or as part of a significant mine expansion. Accelerated CCA offsets some of the risk of new mine investment, by deferring taxation of mine income until capital costs have been recovered.

The Budget phases out accelerated CCA for the mining sector over the period 2017 to 2021. Property acquired before Budget Day is not affected, nor is property acquired before 2018:

- Under a written agreement to acquire the property entered into before Budget Day; or
- As part of a mine development or expansion where either construction was started, or engineering and design work for construction had commenced (as evidenced in writing) before Budget Day.

The elimination of this important incentive is disappointing, and affected taxpayers should review their projects and maximize opportunities to use accelerated CCA for the remaining availability period.

Mineral exploration tax credit extended

Individuals investing in flow-through shares (FTS) issued by a mining company may be entitled to tax benefits beyond the renounced CEE/CDE available on all FTS. Where the FTS issuer incurs certain qualifying expenditures (essentially CEE incurred in mining exploration above or at ground level conducted in Canada) and renounces them to such a holder of FTS, that holder is entitled to an investment tax credit equal to 15 per cent of the renounced qualifying expenditures (the "mineral exploration tax credit").

Currently the mining company must incur qualifying expenditures by the end of 2013 and renounce them to the investor under an agreement made before April 2013. The Budget extends the 15 per cent mineral exploration tax credit for another year, by extending 1) the date for incurring qualifying expenditures to the end of 2014, and 2) the deadline for the company and the investor to enter into the FTS subscription agreement governing renunciation to March 31, 2014. M

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