



Friday, 22 October 2010

By email: newtaxes@aph.gov.au

Senator Mathias Cormann
Chair
Senate Scrutiny of New Taxes Committee

Dear Senator Cormann,

Please find attached a submission (Part B) with respect to the MRRT which you kindly suggested we present.

Part A, which was sent to you firstly, primarily aimed to demonstrate that the proposed MRRT on the thermal coal industry and any other additional taxes e.g. ETS or a Carbon Tax, would not only impact the thermal coal industry but importantly power costs for businesses and homes throughout Australia, and:

Part B refers to iron ore

Part B

- Iron ore is not exclusive to Australia, but exists in many countries. Australia needs to maintain its competitiveness to supply iron ore markets. Australia is already competing against high grade ores from Brazil and will be competing additionally against low cost countries such as in West Africa.
- Australia is not the only supplier of iron ore, yet we are primarily direct shipping ore suppliers and hence one of the most environmentally responsible, least polluting suppliers.

Increasing investment in iron ore supply in low cost countries will replace Australian iron ores if we don't act to reduce our costs and remain competitive.

- There is considerable concern, not only among ANDEV members, that the current Government has already made an agreement with multinational companies that offers advantages to those existing multi-national producers, but disadvantages new Australian producers in relation to infrastructure and finance costs. It appears obvious the proposed MRRT fails to address key elements of importance to Australia's future.
- Additional costs that diminish our ability to compete in world markets will diminish revenue for Australia. Already, Australia's iron ore industry is facing greater competition than ever before given:

- (a) The introduction of (up to) 400,000 DWT ships and port handling facilities being built in Asia,
- (b) Panama Canal capacity being increased by 2015;
- (c) The resulting loss of Australia's freight advantage and freight cost protection;
- (d) Escalation of significant development of iron ore projects in West Africa, with low costs and high grade ores, and iron ore development in other countries, that will substantially impact on Australia's export tonnage.

Australia needs policies that encourage economic growth and the protection of living standards, particularly given the increasing revenue needed to accommodate our growing aging population (and other needs).

- Given the foregoing we need in Australia, pro-active policies to encourage investment in our iron ore industry, policies that enable Australia to maintain competitiveness in overseas markets and policies that maintain ongoing revenue from Australia's iron ore and related industries. The recent independent Fraser Institute report in 2010 is just one report that shows Australia's position is declining as a country in comparison to other countries which are more attractive to investment.

It is critical to remember the Australia is not the only country that has iron ore producers endeavouring to reach markets, and hence Australia must remain competitive, or we will see less revenue from iron ore exports.

1. Iron ore is abundant in the world.
2. There are large deposits in Australia of iron ore not yet developed, hence not producing jobs or revenue.

Australia should be seeking to benefit from export of its iron ore whilst demand continues. Development of these deposits should be encouraged not hindered by the introduction of a MRRT.

We are however concerned that potential future cost imposts of a MRRT will make investment in such mining developments uncompetitive in our already high cost country, when compared with African and other competitors with much lower wage rates and hence much lower cost.

3. Potential changes in royalty and taxation quantities and regimes, with the further risk of an ETS, environmental and other policies, have already diminished Australia's place as an investment option. As noted from the recent independent Fraser Institute Report, (commissioned just prior to the dropping of the RSPT) recently published:

Thursday, 12 August 2010

THE move to increase mining taxes is having an unsettling effect on mining company confidence across the globe, according to Canadian think tank the Fraser Institute, which said overnight Australian states are losing their attractiveness as mining destinations due to the federal government's recent tax grabs.

Chief among these are Australian states, most of which dropped significantly on the Fraser Institutes' Policy Potential Index which assesses how mineral endowments and public policy factors such as taxation and regulation affect exploration investment.

In a statement accompanying the release of the report, the Fraser Institute said international mining executives were looking less favorably on these formerly mining-friendly jurisdictions that are moving to increase taxes on the industry.

Australia is chief among these, according to the report, with the federal government's proposed resources super-profits tax having a significant impact on Australia's standing among global mining executives.

The 2009/10 index saw South Australia drop to 15th place overall from 10th, and Western Australia fell to 28th from 19th, the Northern Territory dropped to 30th from 14th, Queensland declined to 33rd from 24th, and New South Wales plummeted to 38th overall from 20th, according to the Fraser Institute.

Fifty-one jurisdictions were included in the mid-year report. The average rank of the Australian states fell to 31st place, from 18th in the 2009-2010 index.

The attempted tax grab impacted on Australia's reputation globally, and risked defining the country's attitude to the industry for overseas executives, according to the report, with more survey respondents saying they were worried about Australia's future taxes than agreeing they were familiar with local mining issues.

The two other areas in the world that saw their standing drop – Quebec and Nevada – also looked at introducing new mining taxes in the survey period.

Report author Fred McMahon said uncertainty over future tax regimes was the driving factor in the drop in the standing of Australian states in the survey.

*Overall, the top 10 jurisdictions in the mid-year survey were Alberta, Finland, Quebec, Yukon, Saskatchewan, Chile, Newfoundland and Labrador, Botswana, Alaska and Nevada. **(Please note, Australia and our States are not even in the top 10 indeed all these countries rank above Australia, as indeed 30 countries now rank above the average of Australian States)***

Australia must ensure it prepares for increased competition from low cost countries that if unaddressed will significantly steal further investment away from investing in iron ore in Australia and diminish Australia's market share, therefore we need to urgently create and implement policies that enable Australian iron ore to be cost competitive in export markets.

4. The Australian iron ore (and thermal coal) industries will be made less profitable should any new additional tax be applied, and will have increased costs due to any new additional tax, leaving less funding available for investment. Political decision makers cannot continue to rely on Australia being able to compete on world markets against lower cost commodities from low cost countries in the near term, if taxes and costs go up, and hence should factor in less, not growing, ongoing revenue. We need to make the most of the revenue available to the nation from our iron ore (and thermal coal) projects.

Australia will increasingly compete against countries with much lower labour costs such as African countries and elsewhere. This submission is not however requesting that magnetite ores be given any individual exemption from MRRT. There are vast quantities of other non magnetite ores available in Australia before magnetite ores need to be processed to earn revenue, such processing causing far greater pollution than the abundantly available higher grade ores.

5. 2010 Federal Intergenerational report finds:

- Life expectancy will continue to rise; and,
- The aging population will increase; putting stress on Government services (hence increasing revenue will be required).

Those of us now working and heading to retirement age will be making up part of this aging population requiring increased services.

Do we really want to lessen a very valuable source of revenue for Australia from the iron ore industry given the increasing needs of this aging population, their pensions, their health requirements, expenses for senior citizens' homes etc?

It is too often forgotten that revenue needs to be earned before spending can occur, be it on defence, police, roads or health services. Debts due to over spending can be repaid, hence if we choose policies that curtail the iron ore industry, this potentially large revenue source will be reduced and less revenue will be available for Australia and its future.

6. There are considerable concerns and exposure that the MRRT is currently designed so that there is no tax deductibility in relation to the MRRT for new infrastructure, and concerns regarding lack of deductibility for new finance expense.

To quote Andrew Forrest in the Kalgoorlie Miner of 1 October (and similar in other publications):

““The tax suits only those players who already have their own infrastructure and who have always denied third party access” he said

“The three big mining companies deliberately designed this tax with no tax deductibility for infrastructure.”

According to Mr Forrest, without infrastructure access or investment there will be no new mines.

“These three big miners know this and they are trying to shut the door to new entrants,” he said.

In relation to iron ore projects (and thermal coal) it is critical that new iron ore (and thermal coal) projects are not prevented from being developed because they need to build infrastructure and undergo new finance costs.

The Policy Transition Group (“PTG”) has indicated that the MRRT taxing point is “the first saleable form (at mine gate)”. As a result, MRRT will be payable by integrated mining companies in relation to projects before they have had a chance to recoup the cost of infrastructure (mainly rail transportation and port facilities, but also power stations, etc).

Transportation and shipping infrastructure are vital components of mining projects, many of which are located in regional Australia. Without such infrastructure, the mining projects would essentially become stranded deposits, devoid of value.

The MRRT must therefore either allow full deduction for the capital and operating cost of infrastructure, or recognize that scarce infrastructure in regional Australia – particularly in the Pilbara region of West Australia where a small number of infrastructure owners can make substantial profits at the expense of captive mining projects – should attract a significantly higher allowance of return on capital and operating cost than would be considered normal. Infrastructure assets are strategic in nature, and the MRRT must recognize this.

In applying this to the “Resale Price” method of valuing resource revenue, a significantly higher allowance for return on capital and operating costs must be permitted, as it is this strategic asset that hold a substantial amount of value and not necessarily the resource itself, hence preventing an unfairly high calculation of the value of resource revenue. The PTG should review infrastructure charges in the Pilbara – as an example, one company gave up half of its iron ore resource plus additional price participation above a specified (low by today’s standards) iron ore price, in order to access rail and port infrastructure.

An approach contrary to the position advocated above would unfairly benefit existing infrastructure owners, at the expense of new entrants, and hence stifle the additional and constant infrastructure investment that is so necessary in the mining industry.

If the MRRT continues to be proposed for iron ore (and thermal coal), amendments are required to ensure that future projects will not be disadvantaged.

An early announcement in that regard is important so that the MRRT does not make it any more difficult to build new infrastructure or raise money for new projects.

7. If the loss of additional revenue from the iron ore (or thermal coal) industry via the MRRT poses difficulties for the government, one possible option could be to consider the advice of the IMF. The Washington-based IMF, in a report on the Australian economy, said the mining tax should be broadened beyond coal and iron ore to other commodities to help reduce inflationary pressure, and many have pointed to the injustice of just targeting iron ore and coal, particularly when other commodities such as copper and gold have enjoyed, and are forecast to continue enjoying, meteoric price rises. Since the MRRT agreement gold and copper prices have continued to escalate. Perhaps a super tax could be considered for gold and copper for new projects in the instances where gold and copper prices exceed the prices as at the date of the MRRT?

It is relevant and significant to note that the recent September 2010 ABARE forecast shows significant improvement in Australian commodity revenues (please see attached) and this means that the forecast budget deficit will be reduced, hence the budget can return to surplus earlier than planned and the opportunity exists to lessen the MRRT (and exempt thermal coal) .

Further tax revenues could also be achieved through further large increases in taxation on cigarettes and alcohol, plus additional taxes on drug and alcohol related illegal activities. These products are well known to cause great drains on Australian revenue.

8. To date the debate on taxation or “super profits” taxation or “resource rent” taxation, has focused very much on market activity in the recent past and short term production future, and on the myth that these growing markets will still be available to Australia on an ongoing basis. They won’t be if Australia’s costs continue to go up and Australia becomes uncompetitive. It is acknowledged that since 2004 there has been a step change in the market for most commodities corresponding to the emergence of China as a voracious consumer of raw materials. In Australia’s case the neglect of infrastructure investment, the slowness of government approvals and the resultant slowed development of new sources of supply contributed to a short term period of boost in commodity prices.

We say “short term” as the market is not content with paying higher prices and is very actively pursuing the development of cheaper alternatives, especially in low cost countries such as Africa. Many unthinking pundits subscribe to the “super cycle” concept and foresee a long period of sustained growth for Australia, but they completely ignore the reality, a reality readily available to them through history, that to continue to be able to supply in any cycle, you must remain competitive. They should be able to remember what has happened to economies throughout the developed world, such as USA, Europe and Australia, who used to manufacture goods, however given that they are now no longer competitive in comparison to cheaper Asian and Indian countries especially, their own manufacturing industries have closed. We ask the Committee to be alert to this when considering our request to minimise the MRRT, amend it so that new projects are not disadvantaged (and drop the MRRT on the lower priced thermal coal).

The mining boom could be relatively short and in the case of iron ore (and thermal coal) the information herein should clearly show that much care needs to be taken to keep the iron ore (and thermal coal) industry competitive and able to continue contributing important revenue for Australia.

Prices are dictated by the world market:

The state of the iron ore industry until very recently was exacerbated by the rapid introduction and expansion of Brazilian and low cost countries export tonnage, which continues to this day. The future will however be more difficult given (a), (b), (c), and (d) above. As previously mentioned, many Australian companies, as well as multinationals, are investing in West Africa and elsewhere instead of Australia, to take advantage of the low cost labour and related costs offshore Australia.

This will have dire consequences for Australia’s future and Australia’s standard of living.

The abovementioned more recent “super cycle”, will be in an environment where there are abundant reserves in countries outside Australia ready to substitute for high cost Australian supply, and markets which are currently “ours”, turning to other less high cost sources.

So it is true to say that there will be increased market volumes but we will see more increased volumes supplied from countries that are cost competitive.

The highly regarded and independent International Fraser Institute in Toronto has noted that:

“While nations globally are striving to simplify their tax codes, Australia seems intent on adding complexity to its resource taxes: the RSPT is out; the MRRT is in, and the petroleum resources rent tax (PRRT) is expanded.”

And

“The problem with assessing Australia’s return to competitiveness is that the dust is suspended in mid-air, instead of settling. The mineral resources rent tax (MRRT) numbers don’t add up, details are uncertain, complexity has increased, and the whole episode creates new risks for Australian miners.”

And concludes that in regard to the MRRT:

“Complexity and uncertainty have produced a deadweight competitiveness loss.”

We have put forward this information in the hope that you and the Senate Scrutiny of New Taxes Committee you chair will give needed consideration to the iron ore industry in Australia and its key issues.

Best regards

Greg Anderson, Jan Ford, Chris Codrington and Hans Mende
ANDEV Executive, on behalf of the
Membership of ANDEV

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