



02 November, 2018

Dear Chair and Members of the Senate Economics Legislation Committee,

**RE: Submission to the Senate Economics Legislation Committee Inquiry on the Treasury Laws Amendment (Making Sure Multinationals Pay Their Fair Share of Tax in Australia and Other Measures) Bill 2018.**

This submission supports our member companies concern at changes to the Research and Development Tax Incentive Scheme given effect under this Bill, and specifically with the \$4million cap on research and development (R&D) cash refunds for expenditure on eligible R&D for companies with an aggregated annual turnover below \$20 million. In particular, we seek to highlight the negative financial impact of the changes on our member company, Northern Minerals.

Our submission seeks to detail:

1. The negative financial impact of the Bill on Northern Minerals and its heavy rare earths Project.
2. The potential of this ground-breaking Australian Project.
3. The Project's geopolitical significance.
4. Economic and social benefits to Australia and the Government from the Project.
5. Why uncapped cash refunds for eligible R&D were essential to developing the Project.
6. Three approaches to amending the Bill to ameliorate the negative impact on Northern Minerals, including two which would also support the development of the critical minerals industry over the long term.

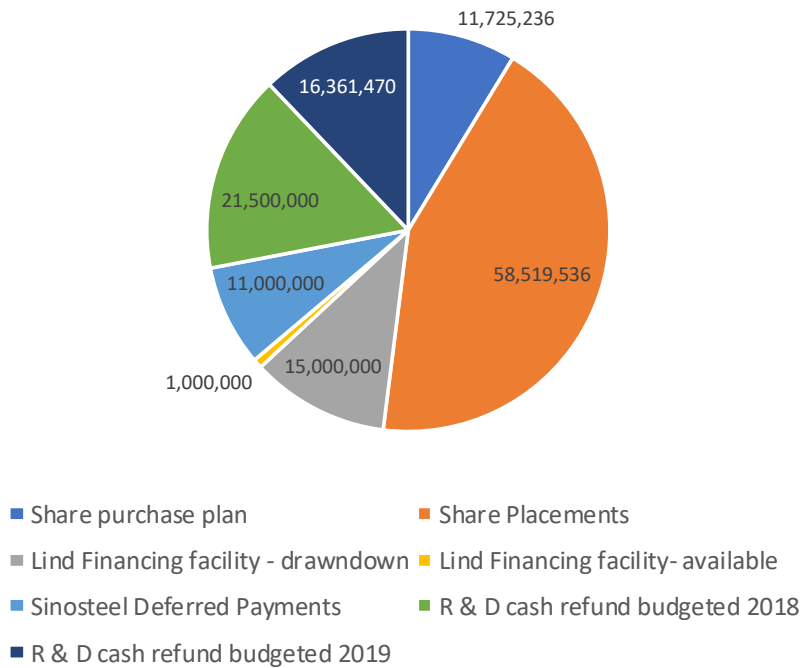
**1. Immediate financial impact on Northern Minerals and the Browns Range Heavy Rare Earths Project**

The Browns Range Heavy Rare Earths Project has been planned, financed and constructed relying on access to uncapped R&D cash refunds under the Government's long-established Tax Incentive Scheme over an eight-year period (2012/13 to 2018/19). In an opaque global heavy rare earths market, Northern Minerals has leveraged the cash refunds for money spent on eligible R&D to gain finance for a project that faced reluctance from traditional banks to provide finance.

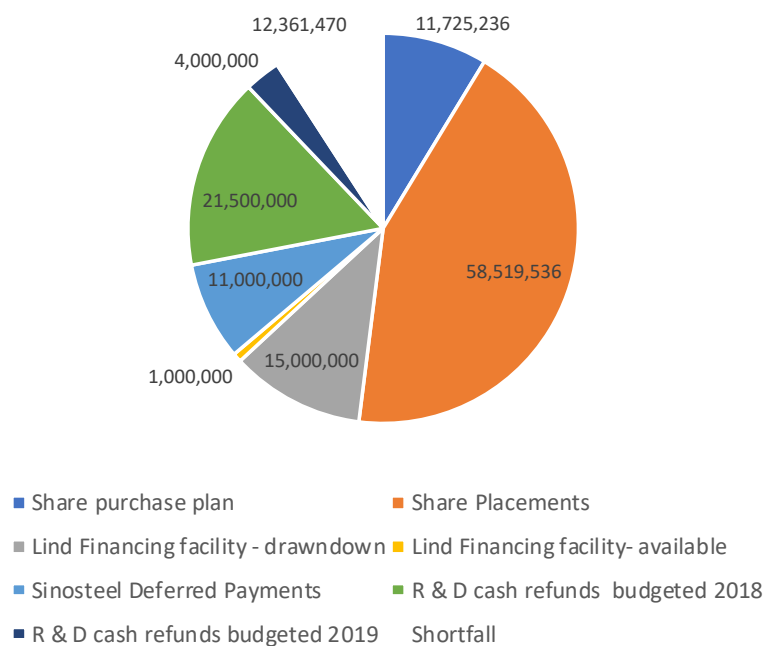
The retrospective nature of this Bill will create a \$12,361,470 million shortfall in the financing of the Project in 2018/19, the final year of the planned R&D program. This retrospective change by the Australian Government brings new and unexpected financial risk to the Project.

Northern Mineral made its Final Investment Decision on the Project in April 2017 based on a business case which anticipated 2018/19 would be the final year of the planned R&D program at Browns Range. All indicators are that this timeframe will be met.

### Planned Project financing - under existing Tax Incentive Scheme - 2017/18 to 2020/21



### Impact of Bill as currently drafted on Project financing - 2017/18 to 2020/21



Year	Cash Refund on Eligible R&D Received
2011/12	\$1,809,074
2012/13	\$6,025,492
2013/14	\$8,992,296
2014/15	\$4,985,413
2015/16	\$1,763,771
2016/17	\$2,672,972
<b>Total Received to date</b>	<b>\$26,249,018</b>

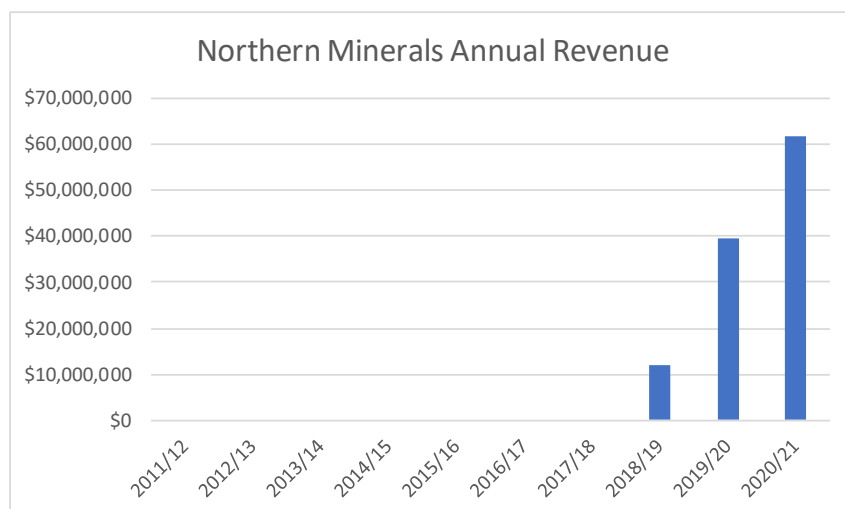
Year	Budgeted Cash Refund on Eligible R&D Claimed (not yet Received)
2017/18	\$21,562,688

Year	Budgeted Cash Refund on Eligible R&D
2018/19	\$16,361,470 – current Tax Incentive Scheme

Year	Capped Cash Refund on Eligible R&D under new Bill as drafted
2018/19	\$4,000,000

If R&D cash refunds are to be capped at \$4million in this current financial year, Northern Minerals will be forced to raise replacement funding from an alternative source. While the majority of shares in Northern Minerals are currently held by Australian investors, the most significant debt and equity investments in the Project have been made by Chinese companies with experience in rare earths processing and understanding of the market potential. Ideally, we would like to maximise Australian equity and debt in the project, however if this is not possible, the most likely source of funding to replace the R&D cash refund shortfall is from China – which would result in diluted Australian ownership.

In 2018/19, Northern Minerals will generate its first revenue and in 2019/20 is not expected to be eligible for the R&D cash refund program when its aggregated annual turnover is expected to exceed \$20 million. See graph below. The uncapped R&D cash refunds have been vital to financing and developing this innovative Project, which has created a new export opportunity for Australia.



Note: graph shows actual and projected revenue over the 2011/12 to 2020/21 period

## 2. A ground-breaking world-first project

The pilot stage of the Project produced its first rare earths carbonate in October 2018 and will commence export this year.

The Project is producing a commodity vital to current technological development while creating jobs in one of the most remote parts of Australia. It is located 160 kilometers south-east of Halls Creek and 50 kilometers south east of the Yaruman Community at Ringer Soak in the East Kimberley. See map below.



Northern Minerals has invested \$180 million in the Project to date. It produces a mixed rare earth carbonate which includes a high grade of Dysprosium and Terbium which are key components of the highly energy efficient permanent magnet motors used in electric vehicles, wind turbines, air conditioning, and industrial robots.

Beyond producing a mixed rare earth carbonate, Northern Minerals is actively pursuing plans for downstream processing to increase the value of exports. In 2018 and 2019 the company is focused on establishing ore sorting and moving towards producing separated oxides which will allow products to be sold to a greater range of markets globally.

### Size of resource

Northern Minerals has spent \$35million on exploration to date at Browns Range. The Browns Range dome is a massive geological feature covering 1,500km<sup>2</sup> and stretching 60km x 30km, most of which hasn't been effectively explored. Northern Minerals believes there is huge, long term potential for production from Browns Range and the surrounding region. Northern Minerals also holds tenements for nearby Boulder Ridge and John Galt.

To date, Northern Minerals has drilled 14 targets at Browns Range, six of which have been converted to resources compliant with the Australasian Code for Reporting of Exploration Results, Mineral Resources and Ore Reserves (JORC Code). These are open at depth and along strike (length) which indicates upside potential. This compares to industry average conversion rates of 10,000 prospects drilled producing one mine. A current drilling program is showing extremely promising results with two new high-grade discoveries.

### 3. Geopolitical importance of product

Browns Range is the only producer of heavy rare earths outside of China.

There is growing global demand for the critical minerals used in the technologies that save energy and produce low cost or renewable energy – including Dysprosium and Terbium. Governments and companies in the US and Europe are increasingly focused on ensuring reliable supplies of such minerals. Geoscience Australia maintains a list of those minerals it has identified as of critical significance.

China has long dominated the supply of rare earths to world markets. This has been achieved by utilising its significant deposits of rare earths and also with focused investment in developing the facilities to process (beneficiate) ore into the high-grade oxides required by manufacturers throughout the world. The lack of beneficiation facilities outside of China currently means almost all ore mined outside China must be exported to the country for processing before it can be used by manufacturers throughout the world. This investment in processing has given China monopolistic control over the global rare earth market.

In 1992, Chinese Premier, Deng Xiaoping stated: “Saudi Arabia has oil, but China has rare earths.”

In 2011, China reacted to nations critical of its South China Sea activities by cutting rare earths exports. This resulted in global prices skyrocketing to historic highs. The price of Dysprosium peaked at US\$1,508 per kg in 2011. Prices subsequently fell when China resumed controlled export.

In 2017, China commenced a program of closing illegal heavy rare earths mines which use highly polluting leach mining techniques. This policy remains in place with mines continuing to close. Prices for heavy rare earths have risen as production in China has fallen.

In December 2017, the United States Geological Survey published its first critical minerals assessment since 1973. The report flagged the lack of US domestic and secure sources of a range of minerals that are expected to be used increasingly in critical technology. Later that month US President Donald Trump signed the ‘Presidential Executive Order on a Federal Strategy to Ensure Secure and Reliable Supplies of Critical Minerals’. The order states: *“It shall be the policy of the Federal Government to reduce the Nation’s vulnerability to disruptions in the supply of critical minerals, which constitutes a strategic vulnerability for the security and prosperity of the United States.”*

In February 2018, the US Department of the Interior released a draft list of 35 minerals deemed ‘critical’ to US national security. A following report by the Centre on Sustainable Investment at Columbia University noted that of the six minerals “most critical for the transition to the green economy”, the US only has domestic supplies of two – Tellurium and Indium. According to the Centre of Sustainable Investment – the remaining minerals are: Lithium, Cobalt, Neodymium and Dysprosium. Australia has deposits of all four of these minerals. Also in February, President Trump met with then Australian Prime Minister Malcolm Turnbull where the countries agreed to form a partnership on critical minerals. This work is being led by Senator the Hon. Matthew Canavan, Minister for Resources and Northern Australia and the Department of Industry, Innovation and Science.

In May 2018, the Western Australian State Government announced the appointment of a Task force to develop a Lithium and Energy Materials Strategy for WA. The strategy aims to maximize opportunities for the State from the global interest in its critical minerals and downstream processing and manufacturing potential. I am a member of the Industry Reference Group advising the Taskforce.

In July 2018 US Secretary of State Michael Pompeo, US Defense Secretary James Mattis, then Australian Foreign Minister the Hon Julie Bishop, and then Australian Defence Minister (now Foreign Affairs Minister) Senator the Hon Marise Payne met for the 2018 Australia-U.S. Ministerial Consultations (AUSMIN). They agreed to hold a critical minerals dialogue, with planning now underway for the meeting to be tentatively held in the first quarter of 2019.

In August 2018, the President of the United States signed into law legislation which prohibits the US Department of Defense from acquiring rare earth magnets from China, Russia, North Korea and Iran. While there are some provisos related to reliability and cost, the legislation is significant given over 90 per cent of rare earth magnets consumed by the US Military are currently produced by China alone.

In October 2018, the Australian Government's Resources 2030 Taskforce released its report on Australia's mineral commodity future. This report includes many references to the importance of well-funded and targeted Australian Government R&D programs and the importance of this to future economic activity.

#### **4. Economic and social benefits to Australia and the Government from cash refunds on eligible R&D**

Under the current R&D Tax Incentive Scheme, the Australian Government effectively makes seed funding investments in innovative and promising projects which have the prospect of delivering returns – both to the Government Treasury and the Nation.

It is important to note that cash refunds to companies on eligible R&D expenditure can result in a benefit to the Australian Government later in the form of tax collections on dividend payments. Projects that receive cash refunds for eligible R&D, lose a franking credit advantage on future dividends to shareholders. Any cash refunds received as a result of the R&D Tax Incentive Scheme are effectively treated as a debit to the company's franking account. This means that a company that has received a cash refund on eligible R&D expenditure will not be able to pay a fully franked dividend to shareholders until such a time that the refunds received from R&D are offset by tax paid.

The current pilot processing plant at Browns Range is designed to process 60,000 tonnes of ore per annum. The pilot is a preliminary stage towards full-scale production which will process 585,000 tonnes of ore per annum. Analysis by Deloitte Access Economics<sup>1</sup> indicates the pilot stage will boost the Gross Regional Product of the Kimberley region over its three-year operation by \$33 million, and provide mining, construction and service contracts to Western Australian businesses worth \$74 million.

During construction in 2017 the pilot stage of the Project provided an additional 90 FTE jobs (at peak there were 120 people employed) and now in operation employs 50 FTEs.

Other benefits of the pilot stage of the Project include:

- \$8.1million training to work program and on-site infrastructure providing trainee positions for local Aboriginal people. These traineeships will be run continuously to build capacity in nearby communities. The training program received \$4.8million in funding from the Australian Government's Building Better Regions Fund.
- Rare earth exports worth approx. \$19 million per annum (based on current rare earth prices).
- Mineral royalties of approximately \$500,000 to the WA State Government per year.
- Payroll tax of approximately \$500,000 to the WA State Government per year.
- GST and company tax paid to the Commonwealth Government.
- The purchase of goods and services – with preference given to local suppliers where possible.

Once at full scale production, Deloitte Access Economics<sup>2</sup> predict the Project will boost the Gross Regional Product of the Kimberley region over a 13-year period by \$393 million, create 406 FTE jobs during construction and an average of 135 FTEs during operation, and provide mining, construction and services contracts to Western Australian businesses worth \$773 million. At full-scale production, the Project will generate between \$270 million and \$310 million per year of economic activity across

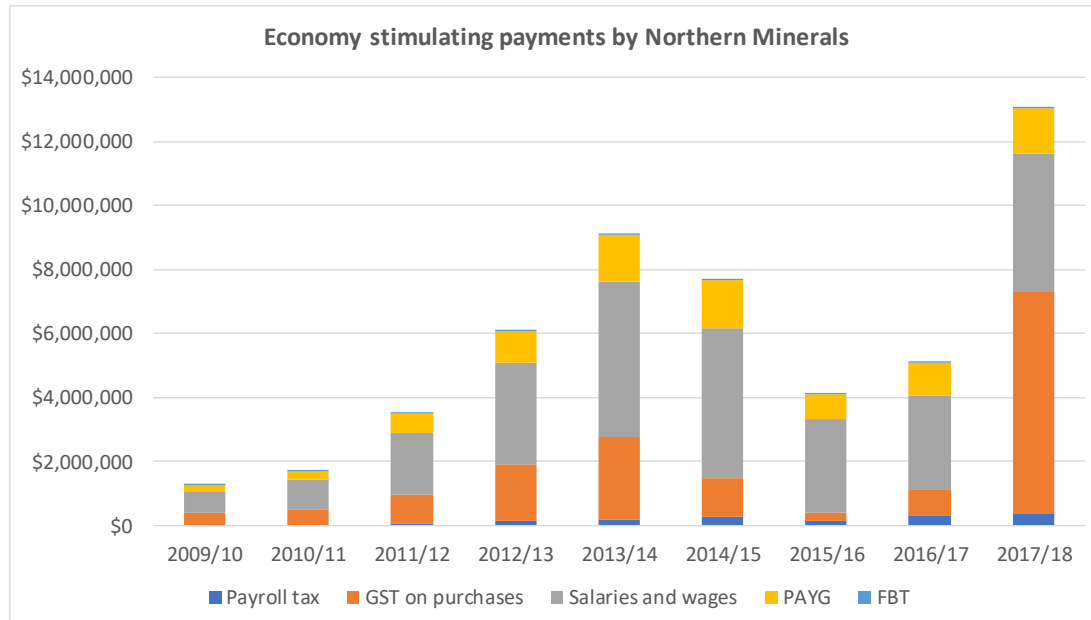
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<sup>1</sup> Deloitte Access Economics, economic impact study of the Browns Range Heavy Rare Earths Project, 2016.

<sup>2</sup> Deloitte Access Economics, economic impact study of the Browns Range Heavy Rare Earths Project, 2016.

Australia; approximately 80% of this economic activity is expected to benefit Western Australia, and up to \$10 million of this will directly benefit the local area.

At full-scale production, the Project will also contribute significantly increased royalties and payroll tax to the State Government and GST and company tax to the Australian Government.



Note: the above graph doesn't include the significant sums paid to businesses for goods and services.

## 5. Uncapped cash refunds for eligible R&D were essential to developing Browns Range

The Browns Range deposit is found in hard rock whereas Chinese deposits are mined from ionic clays. Hard rock mining processing of this type has not been done before.

Given the product specifications and market for Australian Dysprosium and Terbium are yet to be proved, financing for the pilot stage of this project presented many technical challenges and has been achieved through a number of sources. The R&D cash refunds have been a vital part of financing the establishment of the pilot stage of the Project.

The pilot processing plant provides the opportunity for Northern Minerals to assess the economic and technical feasibility of the full-scale production stage of the Project and to conduct further research and development on the process. The full-scale plant, if economically and technically feasible as we aim to demonstrate by the pilot plant, will be the first commercial scale source of heavy rare earths outside China. The cash refunds on eligible R&D expenditure have been a vital component in funding the development of what is now a new export industry for Australia.

The funds accessed by Northern Minerals through the R&D cash refund have added to the company's confidence in undertaking detailed studies into hard rock heavy rare earths mining and processing. This has resulted in innovative enhancement initiatives as the Project has progressed through its development phases.

## 6. Suggested amendments to the Bill to protect the Critical Minerals Industry

Option 1: Amend the Bill to remove the \$4million cap on cash refunds on eligible R&D expenditure for companies with an aggregated annual turnover below \$20 million.

Northern Minerals has been advised by the Department of Industry, Innovation and Science that twenty companies benefited from R&D cash refunds in 2015/16.

Option 2: Amend the Bill to exempt projects that support the development of critical minerals and those associated with energy production and efficiency from the \$4million cap on cash refunds for eligible R&D expenditure for companies with an aggregated annual turnover below \$20 million.

Under the Bill as drafted, clinical trials have been scoped out of the \$4million cap on cash refunds in this way. Innovation and Science Australia (ISA) is the body responsible for determining whether eligible R&D expenditure satisfies the definition of a clinical trial. The Bill could be amended to make ISA also responsible for determining whether eligible R&D expenditure satisfies the definition of a critical mineral project. Geoscience Australia maintains a list of minerals deemed as critical commodities to Australia and could provide the definitions.

This approach is supported by the WA State Government, the WA Liberal Opposition, the WA Nationals and the Chamber of Minerals and Energy WA.

Option 3: An alternative amendment would be to allow existing projects, where the current R&D arrangements have been used to finance the project, to be grandfathered in the 2018-19 financial year. This would allow projects such as Northern Minerals to be completed according to their planned financing structure. This option would support advanced existing projects but not future projects.

This amendment would acknowledge the risk posed to advanced projects which have made investments and proceeded in reliance on the established R&D Tax Incentive Scheme.

Should you have any queries please do not hesitate to contact me on [REDACTED]

Yours sincerely

Paul Everingham  
**Chief Executive**