MINERALS COUNCIL OF AUSTRALIA

SUBMISSION TO THE SENATE ECONOMICS LEGISLATION COMMITTEE

Inquiry into Minerals Resource Rent Tax Repeal and Other Measures Bill 2013

21 NOVEMBER 2013

EXECUTIVE SUMMARY

The Minerals Council of Australia (MCA) offers comments on schedule 1 of the *Minerals Resource Rent Tax Repeal and Other Measures Bill 2013* to repeal the Minerals Resource Rent Tax (MRRT). The MCA considers that repeal of the MRRT will improve the competitiveness of Australia's tax system, reduce compliance costs and send a powerful signal that Australia is determined to remain a premier destination for investment in minerals resources.

Importantly, repeal of the MRRT will bring to an end the drawn out, acrimonious debate dating back to the Resource Super Profits Tax (RSPT) in 2010, helping to restore some sense of stability and certainty in Australia's resource taxation regime. This is even more important now as the industry faces challenges very different to those of 2010 with the industry confronting the challenge of maintaining competiveness and profitability in the face of lower prices, high costs and increased global supply competition.

The MRRT is an unnecessary, extra layer of taxation on top of company tax and royalties which was never required to ensure Australians received a fair share of the Millennium mining boom. The coal and iron ore industries were among the highest taxed industries in Australia before the introduction of the MRRT with an average tax ratio in excess of 40 per cent over the five years from 2006-07. Even with repeal of the MRRT, Australia will remain a comparatively high tax jurisdiction for coal and iron ore mining.

The mining industry has contributed an estimated $117 billion in company tax and royalty revenues since 2006-07. In addition to $21 billion in company tax and royalties paid in 2011-12, the minerals industry spent more than $34 billion on community projects and spending with local businesses. The industry is a vital part of Australia's economy with benefits flowing throughout the economy accounting for 18 per cent of GDP including direct flow on benefits to mining-related activities, almost half the value of Australia's exports of goods and services and employing almost 250,000 Australians directly.

This unnecessary tax has imposed unnecessary implementation and ongoing compliance costs on the industry. Affected taxpayers incurred significant set up costs on valuations and to implement systems and processes, additional resources to comply with the tax on an ongoing basis and substantial time spent by the industry and Government on guidance, compliance and legislation. Taken together, these costs are well in excess of the Explanatory Memorandum's estimated $10.5 million in ongoing costs. The enactment of any new tax has a relatively higher impact on smaller companies in particular. A more stable, certain and simpler tax system will reduce compliance costs and help restore industry confidence and bring to an end the uncertainty, compliance costs and damage to Australia's reputation as an investment destination.

Removing this additional layer of tax will help shift focus to the most pressing challenges to future growth in the industry - improving industry competitiveness and encouraging investment in a future pipeline of projects. A competitive, growing minerals industry will help to secure jobs, sustain and grow regional communities and increase future taxation revenues for the benefit of all Australians.

THE MINERALS RESOURCE RENT TAX

State of the Industry

Australia's minerals resources industry competes in a globally competitive industry characterised by volatile commodity prices and high capital investment. Coal and iron ore projects are capital intensive requiring large upfront capital commitments and in most cases, long lead times to profitability. A stable, competitive tax system is vital to attracting investment in the industry, particularly in this period of heightened market volatility.

The challenges facing the mining industry are different to those of 2010

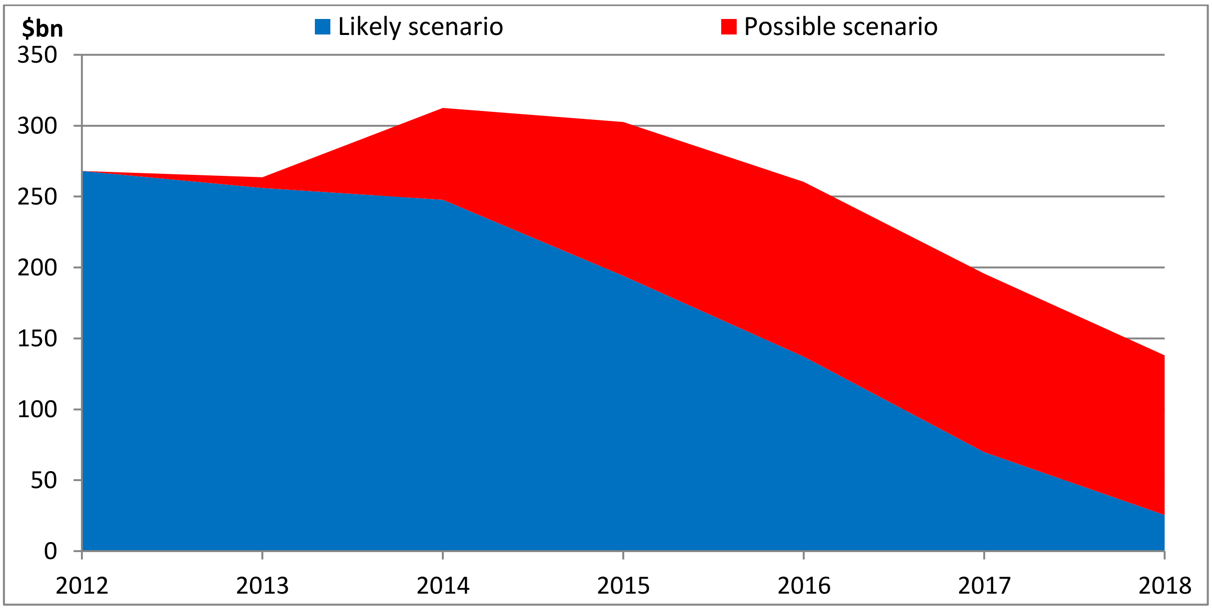
The challenges facing coal and iron ore mining are of a different nature to those of mid-2010 when the RSPT was first proposed. The focus then was on overcoming capacity constraints and maximising returns from high commodity prices. Today, the coal and iron ore industries confront the challenge of maintaining competiveness and profitability in the face of lower prices, high costs and increased global supply competition. Both industries have entered a phase of reduced profit margins contributing to cancelled or delayed projects.

Based on quarterly averages, prices for key commodities in September 2013 are between 35 and 50 per cent down on peak 2011 levels. Iron ore spot prices in 2012 averaged 23 per cent below 2011 prices. Despite a recovery in late 2012 and early 2013, prices in the third quarter of this year are down 30 per cent on the 2011 peak price. Average prices for high-quality metallurgical coal dropped 35 per cent in 2012 and have continued to ease through 2013 and are prices are currently at half of the peak in 2011. The average spot price for thermal coal is now almost 40 per cent its peak 2011 price.

A more competitive tax regime and improved sovereign risk profile will help secure investment

In the 12 months to April 2013, iron ore and coal mining projects worth $29 billion were cancelled or delayed (excluding associated infrastructure such as rail and port and Olympic dam). There is, however, potential for investment to secure a future pipeline of projects, and with that pipeline, jobs and future tax revenues. In April 2013, the Bureau of Resource and Energy Economics (BREE) reported that there are uncommitted projects in the coal and iron ore industries worth up to $188 billion - a significant proportion of the $300 billion worth of uncommitted minerals projects. BREE estimates that there is $113 billion worth of possible additional investment in 2018 (including oil and gas) if Australia realises the opportunity of potential projects.

Major mining projects – potential and committed as at April 2013



Source: Bureau of Resource and Energy Economics (BREE)

The recent expansion of iron ore and coal during the "investment boom" will ensure that as supply ramps up jobs will be secured in future decades. However, the challenge for Australia's mining industry lies in attracting the next phase of investment and projects by addressing operating and capital costs, and improving Australia's sovereign risk profile. Australia's overall tax burden, including the MRRT, is an important component of costs and the assessment of Australia's sovereign risk for future investment.

Minerals Industry tax and community contribution

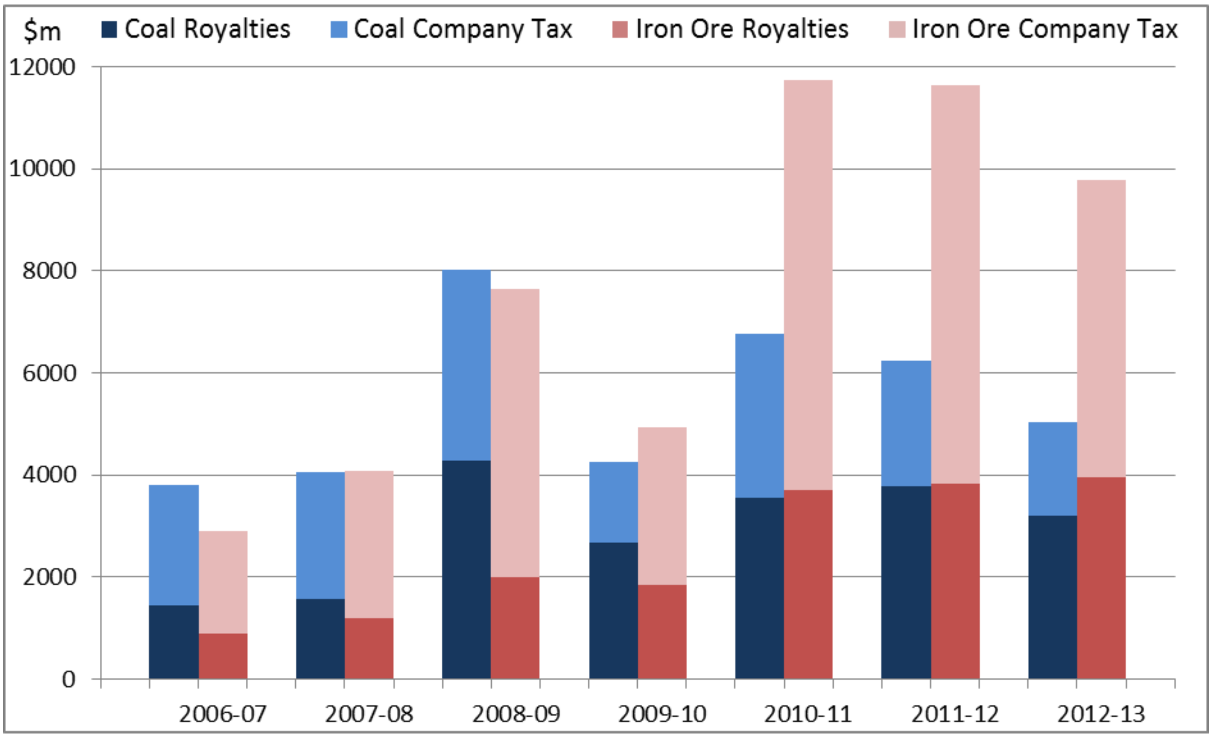
The MRRT was not necessary to ensure all Australians benefited from the Millennium mining boom. Minerals resource companies have been Australia's largest taxpayers in recent years and the mining of iron ore and coal were among the highest taxed industries in Australia, even before the introduction of the MRRT.

The minerals industry pays substantial company tax and royalties

Analysis by Deloitte Access Economics (DAE) shows that over the past five years the overall tax contribution of the minerals industry has been high and stable averaging in excess of 40 per cent. Australia's minerals industry has paid almost $117 billion in company tax and royalties since 2006-07, including $21 billion in 2011-12. Coal and iron ore have contributed the majority of minerals tax receipts.

The MRRT added a third mechanism to company tax and royalties to tax resource profits derived from the extraction of coal and iron ore. Company tax is linked directly to profitability bringing in substantial revenue in years when commodity prices were high over recent years. The majority of royalties are based on the value of mineral production with relatively high royalty rates applying to coal and lump iron ore. Royalties have been raised in recent years on coal in Queensland, on iron ore in WA and a supplementary coal royalty was proposed in New South Wales increasing the effective tax take in times of lower profits. In some cases, recent royalty increases were justified on the basis of the introduction of the MRRT and should, therefore, be reduced in line with the MRRT repeal.

Iron ore and coal tax contribution



Even with repeal of the MRRT, Australia will remain a relatively high tax jurisdiction for coal and iron ore mining with an effective rate of 41 per cent in 2011-12 according to the MCA's 2012 tax Survey.

Analysis by Goldman Sachs released in January 2013 has confirmed that, even without the MRRT, Australian iron ore and coal producers are at the upper end of global resource royalty and tax scales. Australia was found to be in the top quartile of countries based on a total tax take of 44 per cent compared with a global average of around 39 per cent.

The large contribution to revenue will continue without the MRRT. As the Treasurer noted in his second reading speech "While mining companies in Australia will no longer be required to pay the mining tax, they will continue to pay their fair share of tax through State royalties and company tax."

Broader sharing of the benefits of mining

In addition to the industry's tax contribution, new data on the minerals industry's community spending shows that the industry spent $34.7 billion on community projects and with local businesses in 2011-12. This includes community infrastructure such as libraries, health facilities, transport, education and training, support for local sport and spending on indigenous contractors and local businesses. Community spending is an important part of the industry maintaining a social licence and supporting sustainable development of the industry.

The industry's tax and community contribution is in addition to the prosperity generated by the mining industry as Australia's biggest exporter, creating jobs and investment across Australia. Recent research by the Reserve Bank of Australia (RBA) confirmed the significance of the mining industry to Australia's economy, particularly over the last decade. It found that the resources sector accounts for around 8 per cent of GDP (around 18 per cent of GDP including flow on benefits to mining-related activities) and indirectly almost 10 per cent of total employment.

The industry accounts for almost half the value of Australia's exports of goods and services, with the sectors covered by the MRRT – iron ore and coal – accounting for the majority of this, contributing $96 billion to exports in 2012-13. Together, the iron ore and coal sectors employ more than 90,000 Australians directly and hundreds of thousands more indirectly, many in rural and regional Australia. The industry is Australia's largest employer of indigenous Australians.

Given the minerals industry's tax contribution, community support and the generation of wealth across the economy, the industry disputes the argument that it does not pay its "fair share" of taxes in Australia or that Australians do not capture an appropriate return from the profits of industry at the peak of the resources cycle. Contributions through company tax, royalties, community spending and support for local businesses will continue and grow with a stronger minerals industry without the MRRT.

Tax compliance costs and uncertainty

The MRRT did not constitute tax reform. The MRRT added an unnecessary layer of taxation pushing Australia's tax rates to the upper boundary of international tax rates and added complexity to Australia's tax system. The acrimonious debate since the RSPT was first proposed in May 2010 not only harmed the competitiveness of Australia's tax system, it also damaged Australia's sovereign risk profile by injecting uncertainty and complexity into Australia's taxation framework.

The MRRT imposes high compliance costs on industry

Profits based taxes are complex taxes by their nature. The Explanatory Memorandum to the Bill estimates that repealing the MRRT will provide a substantial compliance cost saving of $10.5 million per annum. The minerals industry submits that this is a conservative figure and that ongoing compliance cost savings attributable to the repeal for industry would be even higher.

Importantly, the $10.5 million relates only to ongoing costs. Set up costs to implement system changes such as IT, staff training and undertaking asset valuations are substantially more. These costs are sunk costs and are therefore not captured as ongoing compliance costs but were significant.

The direct cost of ongoing and sunk expenditure associated with tax compliance on industry is only one dimension of the 'costs' associated with unnecessary and burdensome regulation. These costs are in addition to ATO administrative and set up costs, the time spent over the last three years on preparing guidance materials along with time spent on inquires, consultation and legislation. There are also costs associated with the distortions and uncertainty created by ineffective regulation which adds to the cost of making investments and ultimately impacts the Australian community. As noted earlier, compliance costs are regressive in that they impact disproportionately on small businesses.

Compliance costs associated with the MRRT and the tax system add to the growing volume of poorly targeted or ineffective regulation and legislation that has imposed unnecessary costs on Australian business.

Poor policy process and uncertainty damages Australia's reputation as an investment destination

The minerals industry adopted a constructive, principles-based approach to the reform of royalty and taxation arrangements as part of Henry Review. The principles guiding the MCA's approach to resource tax reform, prior to and throughout the development of the MRRT comprised:

- Resource taxation must not impede the industries' internationally competitiveness;
- Any change must be prospective;
- The tax must be differentiated by commodity;
- It must be resource-based; and
- It must be equitable and efficient to promote economic activity and improve the efficiency, simplicity and fairness of the tax system.

Although the MRRT was an improvement on the RSPT, and the Policy Transition Group (PTG) process was a demonstration of solid consultation on policy implementation, the mining tax debate spanning three and a half years of various legislation drafts, proposals and numerous parliamentary inquiries has created a high degree of uncertainty over the taxation of Australia's resources.

The perpetual uncertainty that has characterised Australia's resources and broader business tax regime over recent years threatens investment, jobs, growth and, ultimately, future taxation revenues.

Tax stability crucial to future investment and growth

A competitive, stable tax system is critical to attracting investment in the iron ore and coal industries to secure a future pipeline of investments vital to Australia's future economic prosperity. With the backdrop of lower prices, high cost structures, increasing royalties and a diminishing pipeline of investment projects, Australia's minerals industry faces challenges in securing the next phase of growth. Repeal of the MRRT will help Australia strengthen its reputation as an investment destination with stable and competitive taxation arrangements.

Technical changes since the exposure draft Bill

The MCA appreciated the opportunity to consult on the draft legislation and made a submission to Treasury on the draft *Minerals Resources Rent Tax Repeal and Other Measures Bill* on 31 October 2013.

The MCA welcomes the technical changes made to the legislation and explanatory memorandum based on comments provided to Treasury during the consultation process on the draft repeal Bill. The changes made to incidental coal seam gas from underground coal mining and to the integrity provisions removed potential compliance costs and more accurately meets the policy intent of repeal.