GUNDJEIHMI

ABORIGINAL CORPORATION

Parliament of Australia

Senate Standing Committee on Economics

INQUIRY INTO THE URANIUM ROYALTY (NORTHERN TERRITORY) BILL 2008

Submission of the Gundjeihmi Aboriginal Corporation

3 March 2008

Introduction

1. Established in 1995, the Gundjeihmi Aboriginal Corporation (GAC) represents the rights and interests of the Mirarr traditional Aboriginal owners of, inter alia, the land now subject to the Ranger Project Area and the Jabiluka mineral lease. The Mirarr people have over 30 years experience of uranium development on their traditional lands. They are, therefore, uniquely experienced with the social, environmental, and financial impacts of uranium development. The GAC welcomes the opportunity to provide a submission in relation to the Uranium Royalty (Northern Territory) Bill 2008.

2. The GAC has been the royalty receiving entity for the Ranger uranium mine since 1995. The corporation has, therefore, some 14 years direct experience of the management of uranium royalty equivalents. The members of the corporation have been variously associated with the management of both the Gagudju Association Incorporated and the Djabulukgu Association Incorporated, both of which had previously acted as the royalty receiving entity for the Ranger uranium mine. It is in the interest of articulating this combined experience with uranium royalty management and advocating the rights of traditional Aboriginal owners of land subject to uranium mining that the corporation makes this submission.

3. This submission in no way represents any change in the position of the Mirarr traditional owners with respect to the proposed Jabiluka uranium mine. The Mirarr remain opposed to this proposed development, which is today subject to a long term care and maintenance agreement between the Mirarr, the Northern Land Council, and Energy Resources of Australia. Given this position, neither historic nor possible royalty regimes in relation to Jabiluka are discussed in the submission.

The Ranger royalty regime

4. On 3 November 1978 the Northern Land Council (NLC) and the Commonwealth government executed an agreement under the *Aboriginal Land Rights (Northern Territory) Act* 1976 (the ALRA) in relation to mining for uranium on the Ranger Project Area. The royalty that applies at Ranger was annexed to this agreement in the form of a determination by the then Trade and Resources Minister and the then Aboriginal Affairs Minister.

5. The agreement provides for a total *ad valorem* royalty of 5.5%. Other financial arrangements under the agreement included up-front payments and an annual rental. Up-front payments from the Commonwealth to the NLC totalled $1.3 million payable in stages up to the mine's first production. The Commonwealth also paid $150,000 per annum for four years to the NLC for it to meet administrative costs associated with the Ranger project. The Commonwealth also agreed to pay the NLC $200,000 in annual payments, termed rentals.

6. As stated in the explanatory memorandum to the Bill, the Ranger *ad valorem* royalty of 5.5% consists of three components: 2.5% being the applicable royalty on Aboriginal reserves under the then NT Mining Ordinance, 1.75% being the so-called negotiated payment for traditional owners, and 1.25% as payment to the Northern Territory Government as a grant in lieu of royalty in accordance with a 1978

Memorandum of Understanding between the Commonwealth and Northern Territory governments. The sum of the first two percentages, 4.25%, is paid into the Aboriginal Benefits Account (ABA).

7. Until 2006 these funds were subject to a statutory distribution ratio of 30% to local Aboriginal interests, 30% to the ABA and 40% to land councils in the Northern Territory. While local Aboriginal interests still receive 30% of these funds, land councils are today funded under separate arrangements.

8. There are a number of noteworthy matters regarding the November 1978 agreement. Firstly, as noted in Altman 1983, 'the [mining] company has taken over the total Commonwealth liability in respect of royalties'.[1] This significant point has been frequently overlooked in discussion of the financial arrangements which apply at Ranger. Also, the annual payment of a 'rental' was not linked to inflation and has therefore declined significantly in agreement year (1978) values. Perhaps most important to Aboriginal interests was the fact that the negotiated royalty of 1.75% was treated as a statutory royalty (i.e. it was combined with the statutory royalty) and therefore subject to the distribution provisions of the ALRA. This meant that only 30% of the negotiated royalty flowed to the affected region. In other mining agreements 100% of negotiated royalties flow to the affected regions. As a result of this arrangement, local Aboriginal interests have netted 1.275% of the total Ranger revenue per annum.

9. Whilst the negotiated financial arrangements referred to above have provided a regular inflow of funds to the relevant organisations, the level of annual receipts has varied dramatically, despite the financial strength of the mine operator (see Figure 1). A financially weak operator, more volatile commodity prices, or a less benign economic environment may very well have resulted in a cessation of mining (temporary or otherwise), thereby increasing environmental risks and the viability of the organisations and social services reliant on that income.

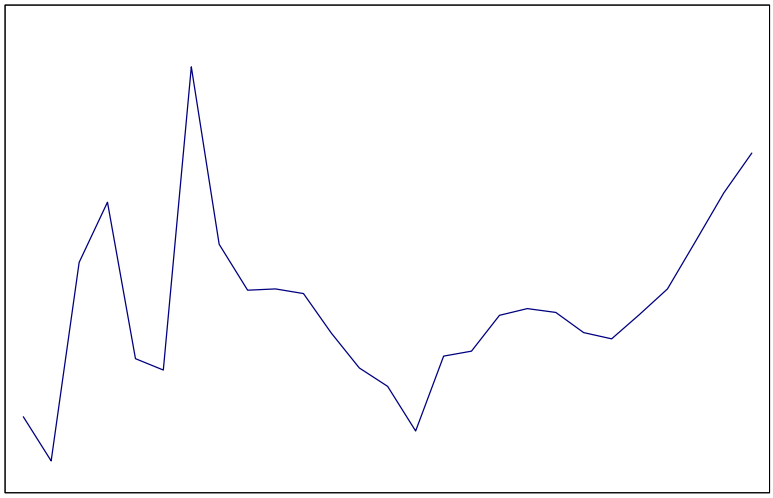

FIGURE 1: The volatility of Ranger uranium royalty receipts in Kakadu National Park, 1979 to 2007 (values removed). This shows receipts of the 30% of the 4.25%* ad valorem *royalty over time.

[1] Altman, J.C. 1983, *Aborigines and Mining Royalties in the Northern Territory*, Australian Institute of Aboriginal Studies, p.57.

'Impediments' and marginal mining

10. The bill arises from the deliberations of the Uranium Industry Framework, which identified 'uncertainty surrounding fiscal arrangements applying to uranium developments in the Northern Territory'[2] as an impediment to the development of the uranium industry. If this contention is agreed, then the task is to provide regulatory certainty for investors. The present bill, however, will not provide such certainty. Its shortcomings, particularly in relation to Aboriginal interests, would lead to unnecessary complication and indeed disputation over time. However, the contention itself (that existing fiscal arrangements impede uranium development) is far from certain.

11. No evidence has been provided to support the contention that more extensive uranium mining would have taken place had the historic royalty arrangements been profit-based. A commercial decision to risk exploration and development capital is based on more significant considerations than a 1.25% *ad valorem* royalty - not the least being traditional owners' consent. Such investment decisions are more likely to hinge on other considerations like commodity price/volatility, resource grade and cost of extraction. Further, marginally viable mining ventures which decide to mine under the royalty arrangements proposed in the Bill are more likely to fail given the marginal nature of the investment decision.

12. The Australian Government should only entrust the mining of uranium to companies that can clearly demonstrate the capacity to safely manage this responsibility. Indeed, given the mineral's strategic value and the substantial social and environmental impacts associated with its development, surely the government should only encourage companies with a strong balance sheet, good record in mining uranium and a clear ability to assess the viability of a mining venture. This will avoid marginally viable investments. We are not aware of any legislation that will ensure these needs are met. There is a significant risk that a profit-based royalty regime would encourage the development of marginally profitable mines, risking inadequate environmental and social protection from mining impacts.

13. In the case of mining in highly sensitive and internationally important regions such as Kakadu, it is unimaginable that the Australian Government would support a royalty regime that risks marginal ventures closing prematurely and posing serious ongoing social and environmental risks.

Volatility of profit-based royalty schemes

14. Royalty income in Kakadu has varied considerably over the years since Ranger commenced production. From relatively large payments in the early 1980s, to a drop in the mid-80s, to record highs in the late 80s and a steady and then dramatic decline to the mid-1990s, this income has been especially volatile. Such volatility poses a serious financial, managerial, infrastructural and service delivery risk to Aboriginal communities reliant on that income.

[2] Minister for Resources and Energy, Hon. Martin Ferguson, Second Reading Speech, 3 December 2008.

15. The fortunes of the first royalty receiving entity for the Ranger mine (and the first such entity established to receive royalties derived from mining on Aboriginal land), the Gagudju Association Incorporated, closely paralleled those of Energy Resources of Australia. The problem of such an intimate association with the vagaries of mining was highlighted in the Kakadu Region Social Impact Study:

> *'By the early 1990s, for a variety of reasons, this strategy was in difficulty. First, on the income-side, revenue from mining activity began to decline (especially in real terms) as the world price of uranium dipped. The* [Gagudju] *Association's tourism-linked enterprises were also experiencing financial difficulties owing to the 1989 pilots' strike, the recession of the early 1990s and the subsequent decline in forecasted tourism growth. The capacity of Gagudju to fulfill its service delivery functions (while maintaining its business investments and making payments to individual members) gradually declined.'* [3]

16. The decline in royalty revenue from the Ranger mine could not have occurred at a worse time for the Gagudju Association. In short, when the association most needed finance from Ranger (the mid to late 1990s), it was receiving the smallest payments on record. While Gagudju's financial problems were the result of many factors, for present purposes it is enough to note that the volatility of the Ranger royalty income, while not responsible for those problems *per se*, did little or nothing to ameliorate them and appears even to have exacerbated them.

17. Importantly, this volatility was experienced under an *ad valorem* royalty regime, under which at least some of the volatility of markets and the business are counterbalanced by the royalty being determined by the volume of sales. Such volatility would be significantly amplified under a profit-based royalty regime because profit volatility is greater than sales volatility. Profit-based royalties would expose Aboriginal interests to even greater instability than that experienced by the Gagudju Association in the 1990s.

Delayed benefit to traditional owners

18. It is stated that the primary purpose of the Bill is to remove an 'impediment' to the development of the uranium industry in the Northern Territory, namely, uncertainty with respect to fiscal arrangements. While we question the premise upon which this purpose is based, the bill itself raises a number of important considerations.

19. Under a profit-based royalty scheme, royalties are not payable until a profit has been realised by the mining operation. Given the customarily high capital expenditure costs associated with exploration, development and extraction at uranium mines, profit is not realised until the later part of the venture's life. Such delay increases the risk associated with the venture, with a high prospect of traditional owners waiting years for any financial benefit. Such benefit may in fact never eventuate, whereas the impacts of exploration and development are inevitable. Given that it is invariably senior Aboriginal people who ultimately make the decision as to whether or not

[3] Kakadu Region Social Impact Study, 1997, *Report of the Study Advisory Group*, Supervising Scientist Division, p.12.

mining occurs, it may well be the case that these very people will not live to see any profit-based royalty from the mine. The profit-based royalty proposed in the bill would, therefore, itself act as an impediment to uranium development.

20. While there is nothing in the legislation to prevent any mining company negotiating up-front or any other payments over and above the statutory profit-based royalty, there is similarly no guarantee that traditional owners will receive any income from mining on their land prior it turning a profit. The traditional owners must simply hope that the mining company concerned appreciates the need for such an income during these times. However, given the fact that the legislation may well lead to more marginal mining ventures it is far from certain that new and unknown (and possibly disreputable) companies will not seek to take advantage and pay traditional owners as little as possible as infrequently as possible.

Administrative complexity

21. By its very nature a profit-based royalty scheme is administratively complex, particularly for Aboriginal communities that are often without specialist administrative resources. The effective monitoring of mining company operating and capital costs and a reliable assessment of issues such as depreciation are well beyond the means of most, if not all, Aboriginal communities.

22. The calculation of profit is itself often a particularly vexed question, as noted in O'Faircheallaigh 2003:

> *'… it is possible to define the 'profit' of a mining operation in a number of ways. This is largely because costs, especially costs of capital (interest depreciation) can be accounted for in different ways and at different times, and depending on how this is done profits may vary considerably. This is a major issue across the wider business community both in Australia and internationally.'* [4]

23. The calculation of production-based royalties is, by contrast, significantly simpler and in a very real sense more transparent than a profit-based royalty scheme. Such transparency is entirely in keeping with the spirit of partnership between Aboriginal communities and mining companies that is a requirement of sustainable development.

24. A new layer of complexity is added to the determination of profit in instances where mining companies may seek to purposefully conceal profit for taxation and other benefits. While the practice of 'transfer pricing' is sometimes considered something of the past in the mining industry (with an infamous example of it taking place arising from bauxite mining at Gove in the Northern Territory), it remains a regular focus of Australian Taxation Office campaigns.[5]

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[4] O'Faircheallaigh, C. 2003, *Financial Models for Agreements between Indigenous Peoples and Mining Companies*, Centre for Australian Public Sector Management, Griffith University, p.15.

[5] See, for example, Mark Fenton-Jones, 'ATO blitz on transfer pricing', *Australian Financial Review*, 2 June 2007 and Kate Burgess, 'Tax watch on transfer pricing', *Business Review Weekly*, 13 September 2007.

Standing of traditional owners

25. A fundamental problem with the profit-based royalty regime is that it suggests that the stake traditional Aboriginal owners have in a mining operation on their land is that of an equity participant. While the risk of making no money (i.e. a royalty) is higher than with other royalty regimes, the prospect of making more money when profits are high is held out in the proposed regime. It is not accurate, however, to think of Aboriginal landowners as equity participants - for while they would be exposed to all and every risk associated with the market and with the business, they would not enjoy many of the other benefits associated with equity participation. For example, should a mine or the legal entity who owns the entitlements under its lease, be sold at a considerable profit, no royalty is payable. So profit-based royalties that bear equity risk do not generate equity returns and are therefore inequitable to the royalty recipient.

26. It is noteworthy that under a profit-based royalty scheme, changes in mining (such as the currently proposed expansion of the Ranger mine) would, as costs increase, lead to lower profits and therefore lower royalties. This reduction is given. Advocates of a profit-based royalty scheme suggest that this would be counterbalanced by larger royalty payments when the mine returns to profit. This, however, is a hope and not a given. The first scenario is certain - as costs increase profits reduce. The second scenario is uncertain - market conditions and other factors associated with the business will determine if, when and to what extent the company moves into profit. The forward projection of such factors is often highly speculative, making planning extremely difficult for Aboriginal communities.

27. The risks associated with profit-based royalties are well described in O'Faircheallaigh 2003:

> *'Thus while profit-based royalties may offer the prospect of high returns in some cases, they also carry the risk that Indigenous people will receive no income for periods during the life of the project, that income may be highly unstable and, where projects fail to become profitable at all (as can occur) that resource development will not generate any financial benefit Indigenous landowners.'* [6]

Flexibility over time

28. It is important for both Aboriginal and industry interests that royalty regimes incorporate a high degree of flexibility and adaptability over time. Community priorities change over time, with knowledge of the mining operation and its social and environmental impacts maturing in accord with the experience of mining. There should be provision, indeed flexibility, in financial arrangements to cater for such shifting priorities.

[6] O'Faircheallaigh, C. 2003, *Financial Models for Agreements between Indigenous Peoples and Mining Companies*, Centre for Australian Public Sector Management, Griffith University, p.16.

29. It should be noted that no one royalty scheme is appropriate to all mining operations. In particular, a profit-based royalty is not appropriate for a short-lived mine with high capital expenditure costs. The establishment of a single statutory royalty scheme for all operations in unnecessarily restrictive.

Conclusion and Recommendations

30. The Gundjeihmi Aboriginal Corporation considers that the proposed profit-based royalty scheme in the Bill would disadvantage traditional Aboriginal owners by virtue of the increased risk they would face regarding financial returns from mining on their lands, and thus would be a significant disincentive to consent for mining. The proposed scheme would expose traditional Aboriginal owners to increased social, economic and ecological risks as it will encourage marginal mining ventures currently discouraged by a nominal *ad valorem* royalty and be administratively complex.

31. Further, the proposed royalty scheme does not appropriately recognise the primary stake-holding that traditional Aboriginal owners have in mining operations on their country. There is an inherent mistake in considering traditional Aboriginal owners as quasi equity participants. The compensatory component for mining on Aboriginal land factored into the production/output based royalty schemes is missing in the profit-based royalty model.

32. The proposal is inflexible and inappropriate for an industry and environment that requires as much flexibility as possible, given the unique circumstances of each opportunity.

33. It is recommended that the Senate not support the Uranium Royalty (Northern Territory) Bill 2008 in its current form as no evidence has been provided that its intent will be achieved and its implementation will not detrimentally affect the interests of traditional owners.

34. It is further recommended that the Australian Government: -

    i. Undertake an economic impact study on the effect the proposed bill will have on the interests of Aboriginal Australians, and where such study identifies an adverse impact, amend the Bill to appropriately protect and support Aboriginal interests;

    ii. Provide evidence that the 18% profit-based royalty scheme proposed in the Bill will expand mining of uranium not currently being undertaken because of the *ad valorem* approach; and

    iii. Amend the Bill so that it provides appropriate flexibility and variability.