Exploration Development Incentive (EDI): policy design input provided by,

Dr. Michael C. Clarke, M.E.T.T.S. Pty Ltd
Consulting Engineers, Infrastructure Development and Resource Management

With Petroleum, Gas and Helium Addendum

The reply to the invitation to offer design input to the EDI is presented in three parts:

1. QUESTIONS & ANSWERS as per the original Request for Information. 1st April 2014

Chapter 2,

Q2.1. Will a 'no taxable income test' and a 'no mining activities test' effectively target the measure to junior minerals explorers who are not able to utilise their tax losses?

A2.1. Most junior minerals explorers (JMEs) NEVER grow into mining companies. Some have the intention and ability of developing mining projects if they find mineral, others are simply explorers who will 'flick' resources that they discover onto mining project developers. Both types of JMEs are useful.

The JMEs with the intention of looking seriously at mining if their exploration is successful will often seek Joint Venture Partners (JVPs) to provide CAPEX and operational expertise (including mining geology, mining engineering and logistics expertise). If a specific resource is to be offered to a potential JVP then that resource could be excised from JMSs exploration portfolio and be part of a defined mining project and not be eligible for further incentives.

JMEs that are looking for a 'flick' often have highly experienced geo-science (not mining) people as their directors and management that are capable of defining a JORC (Joint Ore Reserve Committee) defined RESOURCE. They often will not have the CAPEX to turn that Resource into a JORC Reserve however.

Q2.2. How should the 'no mining activities' test operate to ensure the incentive targets small mineral exploration companies?

A2.2. Perhaps the NO in 'no mining activities' could be replaced with NO SUBSTANTIAL in the test, with the SUBSTANTIAL being defined as say twice the gross return from mining being greater than the 'pure' exploration expenditure, that being expenditure spent of looking for new resources and not on extending mining reserves.

Q2.3. Could the approach to restrict eligibility to Australian resident companies that are widely held prevent some junior minerals explorers from accessing the incentive?

A2.3. How is 'widely held' to be interpreted; only publically listed companies? By having a restriction on the incentive only being offered to publically listed companies a greater degree of scrutiny is possible, but some private companies that undertake useful exploration work will miss out. An extra degree of reporting for private companies seeking the incentive would be useful and still provide better equity in the scheme.

Chapter 3

Q3.1. What are the pros and cons of companies distributing exploration credits to all shareholders compared to the alternative approach of requiring new share issues? Which is the preferred option?

A3.1. New share issues aimed at specific exploration activities would be a good option, a 'pro'. Here additional scrutiny and reporting requirements would be required to avoid scams, this being a major 'con'.

Chapter 4

Q4.1. Should the Exploration Development Incentive be available to companies exploring for quarry materials? Why/why not?

A4.1 YES, they should be available. Open cut mining and quarrying are often only differentiated by size of the project, e.g. some magnetite deposits have/are being 'mined' others are being 'quarried'. Also GOOD quarried rock for construction is getting harder to find near major urban centres in Australia and incentives could assist quarrying companies find new resources using gravimetric /magnetic surveys.

Q4.2. Would the proposed approach of aligning the definition with sub-paragraph 40-730(4)(a)(i) of the ITAA potentially exclude activities that are, by nature, the search for new discoveries? If so, please provide examples.

A4.2. Here it is useful to return to JORC for guidance (see annexure); by using the definitions of Inventory Mineral, Mineral Resource and Mineral Reserve. If the concepts contained in, 'Expenditure on activities normally associated with feasibility, including activities aimed at determining whether it is economically (including technically) feasible or commercially viable to proceed to development, or how best to develop a known mineralisation, would be excluded from the Exploration Development Incentive' are taken as fair, then the EDI could certainly apply to establishing Inventory Mineral and possibly Mineral Resources to some extent, but not Mineral Reserves where the modifying factors of mining, metallurgical, economic, marketing, legal, environmental, social and governmental aspects come into play. So perhaps go back to the ATO and have them review their definitions.

Q4.3. Conversely, would this definition capture exploration activities that are evaluating the economic viability of a known resource?

A4.3. Resources can be understood to various levels of confidence. The concept of 'truly greenfield' resources is however only rarely applicable these days, an example being a large zinc/lead resource found in NSW during aeromagnetic/ gravimetric surveying that covered ground that was previously thought not to be prospective for base metals. JMEs that have a new look at old brownfield sites are often looking for associated minerals, remnant minerals and mineral resources that are dependant on the mineral price for potential economic viability. Using the approach outlined in Clause 24 'Eligible exploration expenditures would be those incurred on activities that are deployed for the purpose of determining the existence, location, extent or quality of a new [or poorly defined] mineral resource in Australia. In broad terms, the intent of this definition is to encourage 'grassroots' exploration activities, or the generative and early stage exploration for new mineral deposits', seems a fair compromise.

[A major disincentive for searching for and finding truly greenfields deposits are the more strenuous environmental, native title and heritage clearances that these resources will require. Dealing with NGOs and Environmental Agencies can be a commercially hazardous exercise. Is the EDI partially meant to be a compensation for meeting and overcoming these hazards?]

Chapter 5

Q5.1. Under ex-post modulation, will exploration companies be able to provide investors with an indication of the likely value of the exploration credit based on existing information sources about both their own and the sector's exploration intentions?

A5.1 Ask the 'bean counters' otherwise No comment

Q5.2. Is the greater certainty under an ex-ante modulation approach desirable, noting the trade-offs (greater regulatory burden, not fully utilising the cap and potential delay in starting the scheme)?

A5.2 Ask the 'bean counters' otherwise No comment

Q5.3. Is the greater certainty under an ex-post and ex-ante modulation approach desirable, noting the trade-offs (greater regulatory burden and potential delay in starting the scheme)?

A5.3 Ask the 'bean counters' otherwise No comment

Chapter 6.

Q6.1. Subchapter 6.2 illustrates one way of ensuring companies that provide their shareholders with exploration credits give up the economic benefit of tax losses. Is there a simpler or better way to achieve this?

A6.1 Ask the 'bean counters' otherwise No comment

2. Petroleum, Gas and Helium Addendum, 7th November 2014

Mr Joshua Reakes,
EDIC

COMMENTS on the excision of hydrocarbons and gases from the Incentive and the definition of a mineral

Section 15. *'Only expenditure on exploration for minerals will be eligible for the Incentive. The Incentive will not apply to exploration for:*
- *shale oil; and*
- *petroleum, including coal seam gas, and any naturally occurring hydrocarbon or naturally occurring mixture of hydrocarbons, whether in a gaseous, liquid or solid state'*

This Section excludes some of the most necessary and potentially productive exploration. Points:

1. Petroleum, methane, and associated HELIUM are all MINERALS,
2. Shale-gas, shale-oil, tight-gas, tight oil and helium are mineral plays that have considerable exploration success risk, but also produce very valuable products where exploration is successful, and
3. The products have major energy security and export earning potential.

Such minerals should NOT be excluded from the Incentive.
The other categories for comment were addressed in the original M.E.T.T.S. submission.

Dr. Michael C. Clarke, CPEng FIEAust, FAusIMM, RPEQ
Infrastructure Development and Resource Management Engineer
M.E.T.T.S. P/L ACN 050 710 015
PO Box 843 Helensvale, Qld. 4212 Ph: 07 5502 8093 7th November 2014

Caveats and FOI

I have undertaken this review at the behest of Antony Pietsch, Analyst, Small Business Tax Division of the Australian Treasury (Antony.Pietsch@TREASURY.GOV.AU). The review was undertaken without remuneration from Treasury and represents my (METTS's) views only.

The opinions expressed are from my observations. Consequently they may be wrong because of information of which I was unaware (unknown & unknowns) and in light of subsequent information I may change my view. With this caveat, the opinions expressed are my best endeavours. I have no fundamental objection to FOI requests and submission publication with these caveats.

3. Annexure: An Interpretation of JORC Minerals Code.