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Schofield, Shelby

From: Davis, Graeme
Sent: Wednesday, 30 June 2010 9:10 AM
To: Barrett, Chris (Treasurer's Office)
Cc: McDonald, Hamish; Bartley, Scott; Mayo, Wayne; Bastian, Bruce; Parker, David
Subject: FW: Mine [~~SEC-PROTECTED~~]
Security Classification: PROTECTED

Chris

As discussed last night, these calculations do not take account of crediting royalties.

At its simplest, and assuming that we can stop the transferability of credited royalties, the effect of crediting royalties will be to raise the effective tax rates at the lower rates of return to the levels under current arrangements (presumably current rates are internationally competitive?). At higher rates of return the effective rates will be driven by the MRRT rates. That is, the average rate will either be the current ones or the MRRT ones, whichever is the higher.

Royalties vary considerably, particularly for coal. If a royalty was, say, 7% of revenue this will be more than 7% of profit (higher at lower rates of return). Calculations here normally lead to effective tax rates around the 40% mark (as per our own and KPMG calculations). That is, the MRRT will only make a difference to investment decisions if project expected rates of return are over 20%.

Now for the twist. It all depends on the shape of the cashflows and the cost of capital for the company relative to the uplift rate. If, for example, a company pays royalties early on in a project and has to carry the credit forward for MRRT purposes, then if the cost of funds for the company is less than the uplift rate (bond plus 7) then the effective tax rate will be lowered.

Of course, in any one year the rates could be different again depending on the profits in the year as per the tax calculation - if you take a single year of MRRT payments after they start paying, the effective tax rate will look high.

The indicative project calculations allowed transferability of all losses (including those generated from the starting base) and did not have royalties included. Given the discussion above, including royalties and crediting them while restricting transferability of losses from both the starting base and credited royalties would push up the average effective tax rates at the lower prices to be the same as those currently faced under royalties.

GCD

From: Bartley, Scott
Sent: Tuesday, 29 June 2010 7:23 PM
To: McDonald, Hamish; Barrett, Chris (Treasurer's Office)
Cc: Davis, Graeme; Mayo, Wayne; Bastian, Bruce; Parker, David
Subject: FW: Mine [~~SEC-PROTECTED~~]
Importance: High

Hamish

Your spreadsheet with Indonesian coal and Brazilian iron ore added and a chart summarising the results.

Note that the RSPT/MRRT calculations assume royalties are refundable.

We are also investigating this issue from another angle. If we look back over the period to the mid-1980s, our preliminary analysis suggests that the RSPT rate that produces resource revenue with an equivalent NPV value to then existing arrangements would appear to be around 30 per cent. In other words, based on that

comparison reducing the RSPT rate below 30 per cent would produce a worse outcome over that period. Note that this is a historical comparison and one for all resources. We need to think about a forward looking comparison and what it might mean for an iron ore/coal comparison (might be a lower rate).

It is important to note that there should be no inclusion of the resource value in the starting base when the RSPT/MRRT base is close to the equivalent rate. To do so will reduce revenue relative to the status quo.

Also included is some specific mine modelling under the alternative policy settings.

Regards

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From: Davis, Graeme
Sent: Tuesday, 29 June 2010 5:54 PM
To: Bartley, Scott
Subject: FW: Mine [~~SEC- IN- CONFIDENCE~~]

PROJECT AVERAGE TAX RATES (ATR) (1)

		Original RSPT	MRRT (2)	MRRT (2)
		3-year write-off 40% tax rate Uplift 6%	3-year write-off 30% tax rate Uplift 13% Mkt value 25 yrs	3-year write-off 20% tax rate Uplift 13% Mkt value 25 yrs
Coal (3) (new)				
	Multiple projects(7)			
	ATR (%)	53.6	46.2	39.2
	Prices down 40%			
	ATR (%)	46.5	38.6	32.0
Iron Ore(4) (new)				
	Multiple projects(7)			
	ATR (%)	56.4	48.9	41.8
	Prices down 40%			
	AER (%)	13.1	14.6	-13.4
Coal (5) - existing				
	Multiple projects(7)			
	ATR (%)	58.4	46.9	41.8
	Prices down 40%			
	ATR (%)	3.8	3.4	2.3
Iron Ore (6)-existing				
	Multiple projects(7)	56.5	36.4	33.6
	ATR (%)			
	Prices down 40%	55.8	27.3	27.5
	ATR (%)			

(1) Total RSPT/MRRT plus company tax as a percentage of total cash flow. Company tax rate set at 30%. Royalties not considered.

(2) Market value (NPV of pre-tax flows at 10% discount) spread over 25 years only relevant to existing projects.

(3) Hypothetical but representative (confidential) coal project.

(4) Based on public Macquarie Bank data for a typical Pilbara iron ore project.

(5) Confidential data.

(6) Extrapolated from public information on Fortescue Metals Group.

(7) Project within a multi project group at current prices

