



Response to 2010 Review Draft Report

Mining revenue

Department of Treasury and Finance

September 2009

Tasmanian position

- Tasmania broadly accepts the Commission's approach to assessing Mining revenue.
- However, we consider that there is a strong case, with supporting data, that Tasmania cannot apply Australian average royalty rates to its less profitable mines. This has been a long standing issue for Tasmania.
- We have collected some data that provides a conservative estimate for a possible adjustment to Tasmania's revenue base.
- For consistency with the treatment of uranium, bauxite should be assessed in the energy group due to its relatively high royalty rate.

1. Tasmania accepts for the 2010 Review most aspects of the Commission's proposed Mining revenue assessment, including the:
 - use of value of production to assess each state's revenue base;
 - use of ABS data, rather than ABARE data, to measure VoP;
 - treatment of revenue from grants in lieu of royalties actual per capita; and
 - disaggregation of mineral production into energy and non-energy minerals, noting, however, that this approach produces a crude grouping of minerals.
2. Our main outstanding concern with the Commission's approach is that it does not capture the higher costs and lower profitability of Tasmanian mines. As discussed in previous submissions, this restricts the State's capacity to apply average taxation rates to its mining operations.
3. This is clearly evident when comparing the ratio between gross operating surplus (a proxy measure of profit) with value of production for each state. As can be seen in Tables 1 and 2, Tasmania's ratio is around a quarter of the national average – far lower than any other state.

Table 1 – Ratio of gross operating surplus* to value of production, mining

	NSW	Vic	Qld	SA	WA	Tas	NT	Aust
2001-02	0.35	0.57	0.48	0.48	0.56	0.12	0.71	0.51
2002-03	0.37	0.48	0.54	0.57	0.54	0.13	0.63	0.52
2003-04	0.37	0.64	0.52	0.40	0.49	0.09	0.69	0.49
2004-05	0.39	0.45	0.58	0.42	0.58	0.15	0.55	0.53
2005-06	0.47	0.51	0.57	0.41	0.67	0.15	0.55	0.58
2006-07	0.62	0.63	0.60	0.52	0.72	0.25	0.58	0.65
Average	0.35	0.57	0.48	0.48	0.56	0.12	0.71	0.51

*Gross operating surplus also includes gross mixed income

Source: ABS: *State Accounts (5220.0); Mining Operations, Australia (8415.0)*.

Table 2 – Ratios in Table 1 relative to the Australian average

	NSW	Vic	Qld	SA	WA	Tas	NT	Aust
2001-02	0.68	1.12	0.93	0.95	1.10	0.23	1.39	1.00
2002-03	0.72	0.93	1.05	1.10	1.05	0.24	1.22	1.00
2003-04	0.76	1.30	1.05	0.81	1.00	0.17	1.40	1.00
2004-05	0.73	0.84	1.08	0.78	1.09	0.29	1.03	1.00
2005-06	0.81	0.87	0.97	0.70	1.14	0.26	0.95	1.00
2006-07	0.95	0.97	0.92	0.80	1.10	0.39	0.89	1.00
Average	0.77	1.00	1.00	0.86	1.08	0.27	1.15	1.00

4. Tasmania has previously suggested that the Commission could adjust each state's revenue base using ABS GOS data. However, we understand that the Commission was reluctant to apply a GOS adjustment to all states to address what it considered to be a problem specific to Tasmania.
5. In the absence of a general methodology adjustment (as developed and proposed by Tasmania), we consider that the Commission should make a jurisdiction-specific adjustment to Tasmania's revenue base to reflect its clearly reduced capacity to raise mining revenue. Our mining department, Mineral Resources Tasmania, has compiled some data that would be suitable for such an adjustment.
6. Because of the nature of Tasmania's royalties system – it is a hybrid system where royalties are paid on net sales and profit – MRT collects information on the profitability of each mine. Where a mining operation is running at zero profit or at a loss, that mining operation pays only the net sales component of the royalty (1.6 per cent of net sales).
7. We consider that the mining production assessed with little or no profit royalty should provide a *conservative* indication of the proportion of total mining production on which Tasmania would not be able to apply Australian average tax rates. We consider such an estimate would be conservative because it would be based on the production of the least profitable mines only.

8. For this exercise, MRT analysed royalty returns for 2008-09 from the nine major mines operating in Tasmania¹. MRT found that of the nine major mines analysed, three of these mines – all producing non-energy minerals – were paying net sales royalties only, or a very small amount of profit royalty. This production made up 13 per cent of total net sales value for Tasmania.²
9. It is, therefore, appropriate to make an adjustment to Tasmania's revenue, and this could be implemented through either one of two ways:
 - reducing Tasmania's non-energy mineral base by 13 per cent; or
 - by applying the difference between the average effective tax rate and Tasmania's net sales rate to 13 per cent of Tasmania's base – the result would reflect the amount that could then be deducted from Tasmania's assessed revenue.
10. It is likely that the 13 per cent figure would be higher in a typical year. Most metal prices were still at historically high levels in 2008-09 and we would expect that in most other years mines would report lower profitability and that the adjustment would be larger rather than smaller. We would recommend that the Commission round the 13 per cent figure up to 15 per cent when applying the adjustment.
11. If the Commission intends to apply this adjustment for Tasmania and would prefer the most contemporary data possible, Tasmania could provide annual data updates for such an adjustment.

Treatment of bauxite

12. We argued in our previous submission that some minerals should be moved between the energy and non-energy groups according to their royalty rates. This is the approach that the Commission took with uranium, an energy mineral, after noting that its royalty rate was closer to a non-energy mineral rate.
13. Tasmania suggested that bauxite should be assessed with energy minerals because the average policy was to apply higher royalty rates to bauxite. As Table 3 shows, Tasmania's analysis suggests that assessing bauxite as an energy mineral is material.

¹ There are eleven major mines in Tasmania, but two are not currently operating. One was closed due to low zinc prices, the other will open once the nickel price reaches a 'sustainable' level.

² We have kept this analysis at a fairly aggregated level for confidentiality reasons. Further details of this data should be available on request.

Table 3 – Estimated financial impact of assessing bauxite with energy group, 2005-06

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT
\$ million	-7.0	0.6	-21.4	26.7	1.9	1.5	0.0	-2.3
\$ per capita	-1.0	0.1	-5.3	13.1	1.2	3.0	0.0	-10.8

Source: Tasmanian response to CGC Position Paper 2008/10 *Mining Revenue*

14. The Draft Report did not provide any information as to whether this recommendation was considered, but we assume that it has not been implemented. We would argue that, consistent with the treatment of uranium, bauxite should be assessed in the energy minerals group. This approach should apply to any other mineral that clearly does not 'belong' in its default group.
15. In their meeting with Tasmania on 28 July 2009, Commission staff indicated to Tasmania that the Commission is reluctant to selectively move minerals between groups, simply to appease the self-interests of states that propose such movements.
16. Tasmania agrees with this in principle, but only to the extent that such movements are not material. Where they are material, the Commission's own guidelines require (for consistency) that the minerals should be moved.
17. To a great extent, the issue of which group minerals should be attributed to is a difficult one when only two groups are proposed. While we understand the simplification intent behind the proposal, in its previous submissions, Tasmania has pointed out the 'crudeness' of such an approach, compared with a more disaggregated approach to determining revenue raising capacity for particular minerals.