A dog's breakfast of a tax

A few weeks ago we looked at the negative implications of the proposed Resource Super Tax on the junior miners and exploration companies, a section of the market often overlooked by the media. Quite naturally, most of the talk about the potential impact of the Government's mining tax changes had focused on the bigger miners, BHP Billiton and Rio Tinto, after all that's where the bulk of the taxation windfall would come from.

At the time I ventured that the Government wouldn't lower the proposed resource tax rate because it would drastically reduce the forecast taxation revenue, meaning Canberra wouldn't be able to sustain all of its pre-election spending promises.

Amazingly from my perspective, we did see a major back-down from the Government. Under the government's compromise Mineral Resources Rent Tax announced a fortnight ago, the headline tax rate has been slashed from 40% to an effective 22.5%, whilst it has increased the profit level that the tax cuts in at to the long-term bond rate plus 7% – effectively about 12% at current values.

At the time the government said those changes, with others, would only drop the total tax take from the revised minerals resource rent tax by $1.5 billion over the forward estimates period. However those figures have quickly come under fire. Goldman Sachs was just the latest in a growing queue to query the Government's numbers, arguing tax receipts will fall by more than double the government's estimate to $3.1-$3.2 billion.

But over the past week the Government has actually come clean and admitted that the taxation shortfall is likely to be in the vicinity of $7.5 billion, an amazing miscalculation in anybody's language. The threads of this tax are beginning to unravel and it's only been a matter of weeks.

But breathlessly the Government was able to argue that this had all been cancelled out by a convenient revision by Treasury of forecasts with respect to commodity prices and production volumes over the next few years.

How can we have any faith in Treasury's numbers, when they've made major miscalculations measured in the billions of dollars with respect to the original RSPT, the revised MRRT and now budget estimates? That's three major revisions in less than three months! And this week we've seen China cut iron ore imports for the first time since 1998 and we've seen the Baltic Dry Index with its biggest decline in nine years.

The absurdity of the revised MRRT is underlined by its narrowness, which will hit just two commodities, iron ore and coal. This reinforces my view that this has never been about tax reform, or about Australians receiving a greater share of the wealth that is ours, as the Government's spin keeps telling us ad nauseam.

If this was the case we wouldn't have the ludicrous examples of the world's biggest silver mine at Cannington in Queensland, and the one of the world's biggest copper-gold-uranium deposits, Olympic Dam in South Australia, being exempt from the proposed new tax. Surely these are also irreplaceable resource assets fundamentally owned by the Australian people?

Instead, it's all about raking in as much cash as quickly as possible to fill the government's fiscal money pit that it has dug for itself. But even then has fallen through. And the electoral bonus is that it also shores up Labor's position in South Australia (because the Olympic Dam expansion may now not be cancelled) and Queensland (because the coal-seam gas players are getting a better deal).

The Government just weeks ago in its taxation propaganda were painting the big miners as essentially foreign-owned robber barons, nicking Australia's resource wealth from under the noses of its own citizens. But the easiest way for a cynical Government to achieve its aims is with a tax on the two most lucrative revenue-raisers at present, iron ore and coal. But what happens when the gravy train begins to ease up, as it inevitably will?

Future iron ore and coal price declines will have a detrimental impact on the taxation revenues from these two commodities alone. What will the government do then? The cynic in me says that the threshold and rates for the tax will inevitably be amended, or the tax simply broadened to include other commodities.

So whilst I am pleased that most junior and mid-cap miners have escaped the new tax, I wouldn't be too comfortable about things down the track. They could well be the next ones in the firing line. And who knows? The Government could change the rules after the next election if re-elected.

Let's remember that there are more than 850 resource companies listed on the ASX. The broader media initially seemed to ignore this important fact. Indeed, the smaller companies were just as fervent in their opposition to the initial tax proposal as their bigger brothers, and rather than embracing the new proposal like BHP, Rio and Xstrata, most have felt isolated by the shambolic negotiation process.

The development risks are particularly high with junior companies contemplating their first foray into production, with higher-risk projects and greater costs in terms of raising capital. This has not been taken into account with the proposed taxation threshold, which may suit the big miners but not the broader industry.

These sorts of junior companies are the ones with the most to lose and their job has just become even harder. And whilst the proposed 30% allowance for exploration expenses was not relevant to BHP, Rio or Xstrata in their negotiations with the Federal Government, it would have been a leg-up for many junior explorers. That has now gone.

If the Government ignores the smaller end of the mining industry, it does so at its own peril. It's often the bigger companies that come in and help fund projects, but it's the smaller ones that make them. If they're not getting funding, if they're not accessing the risk capital, whether within Australia or from overseas, then the amount of exploration that takes place decreases.

And of course so does the likelihood of finding these new deposits that the Government keeps talking about as being rightfully ours. Well, they're only ours and they can only be exploited when they're actually discovered.

Kind Regards,

Gavin Wendt
Founding Director & Senior Resource Analyst
MineLife Pty Ltd

Telephone: 02 9713 1113, Facsimile 02 9712 3953
Mobile: 0413 048 602

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www.minelife.com.au