Exploration Development Incentive: Policy Design

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In response to the Treasury and Department of Industry Discussion paper (March 2014) on the proposed Exploration Development Incentive (EDI), the Australian Institute of Geoscientists (AIG) hereby submits its response to the questions posed in that document, including some additional consideration.

The AIG is the leading professional institute representing geoscientists employed in all sectors of industry, education, research and government throughout Australia. AIG is a not for profit organisation, run by members for members, which aims to advance the skills, status and public perception of more than 3,000 members both within Australia and overseas. The broad base of the AIG encourages transfer of technical expertise, experience and awareness of issues affecting all aspects of professional geoscience practice.

Since the onset of the global financial crisis, the AIG has been regularly surveying its member base and makes its results available not only to its membership base, but to kindred associations, media and general public. The AIG is acutely aware of the high level of un- and under-employment within its member base (18.7% and 14.8% respectively, http://www.aig.org.au/australian-geoscientist-unemployment-soars/).

The AIG welcomes the implementation of the EDI as in its opinion, it has the potential to reduce the destructive volatility associated with exploration activity, which by its nature should be a long term, deductive process. Furthermore, while the AIG has made its own submission, it would like to draw The Treasury's attention to the submission by the Association for Mining and Exploration Companies (AMEC). The AIG and AMEC held informal discussions and in broad terms, are aligned in terms of their positions and as such, the AIG lends its support to the AMEC submission.

The AIG thanks The Treasury for this opportunity to participate in the design of the EDI and looks forward to future opportunities to refine the program as it evolves.

Regards,

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Identifier	Question	AIG Response
2.1	**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?**	Yes when considered as an entity in isolation. The question is less clear when mining corporations with taxable losses have significant equity stakes in junior minerals explorers.
2.2	**How should the 'no mining activities' test operate to ensure the incentive targets small mineral exploration companies?**	No analysis undertaken.
2.3	**Could the approach to restrict eligibility to Australian resident companies that are widely held prevent some junior minerals explorers from accessing the incentive?**	No, the AIG is unaware of any reason why a restriction to eligible Australian resident companies may exclude legitimate claimants.
3.1	**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?**	AIG is of the opinion that all existing securities should be eligible for EDI benefits. In forming its opinion, the AIG took into account: • The administrative ease associated with its position, compared to complexity and cost associated with establishing a second class of securities. • A view that a new class of shares would benefit new investors but disadvantage existing (and loyal) shareholders, many of whom have suffered losses in recent years. • A wariness that a two-tier security classification may result in current securities becoming 'orphans'.
4.1	**Should the Exploration Development Incentive be available to**	No. The fundamental difference that must be taken into account is that:

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	companies exploring for quarry materials? Why/why not?	• Bulk, base and precious metal exploration and mining is a high risk, low probability activity where the uncertainty is associated with locating an economically viable deposit. The marketability of the product is a consideration once a deposit is discovered. • Quarry products are low-risk exploration propositions, where the uncertainty lies with identifying a market for the product. The marketability of the product is often the primary consideration before the process of discovery is undertaken.
4.2	**Would the proposed approach of aligning the definition with subparagraph 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.**	Seems adequate.
4.3	**Conversely, would this definition capture exploration activities that are evaluating the economic viability of a known resource?**	Yes, there is potential to capture known resources through the permission to include 'Exploration Targets' as defined in the 2012 Edition of the JORC Code. Exploration Targets are projects that have sufficient information to make an order of magnitude tonnage-grade estimate (within ranges), but insufficient information to be defined as Inferred. Exploration Targets often exist in areas that are subject to a relatively high level of geological information, or involve deposits that are easy to discover from remote sensing exploration methods (such as iron). The deliberations that led up to the establishment of the current JORC Code included much discussion about reducing the ability to publish unreasonable Exploration Targets, thereby limiting their use to those projects where there is a reasonable informed basis on which to make the estimates. Exploration Targets are therefore relatively low risk propositions compared to true 'greenfields' exploration programs, as it only takes a handful of drill holes to establish their veracity. Companies that have

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		Exploration Targets can (relatively) easily raise venture capital and should not be subsidised.
5.1	**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?**	No opinion.
5.2	**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)?**	No opinion.
5.3	**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)?**	No opinion.
6.2	**Subchapter 6.2 illustrates one way of ensuring the scheme converts tax losses into exploration credits and does not provide a greater benefit. Is there a simpler or better way to achieve**	No opinion.

	this?	
Other matter 1	**Project scale**	Under the proposed definition, it is possible for a claimant to meet the EDI requirements by undertaking exploration activity in close proximity to mature mineral camps (e.g. Kalgoorlie). By their nature, projects in known mineral camps are often subject to extensive information due to: • Long ownership histories • Extensive Government surveys and data • Applying knowledge from proximal projects to assess the target potential (are all the right ingredients/geological features in place). As project sizes decrease with maturity/proximity to known mineral camps, the AIG opines that a minimum areal size test be applied to qualify for EDI benefits. This would help assure that: • Claimants are undertaking work in genuine greenfields locations, rather than those that qualify by 'box ticking' • The type of exploration activity is likely to add to the geological knowledge and benefit the owners and industry at large (the knowledge of a large area is of more use to the wider industry than work undertaken on small project areas) • The system does not inadvertently promote decreasing rates of return that can be expected in mature terranes (the best deposits are usually the first to be discovered) • Benefits flow to those that invest in activities that can unlock entire new mineral camps. For example, the discovery of the world-class Nova-Bollinger nickel sulphide deposit in 2012 is a case example.
Other matter 1	**Venture scale**	The AIG believes that EDI claims should reside within a minimum and maximum investment range. • A minimum claim must be introduced to ensure that expenditure is not used to 'land bank' by using EDI benefits to subsidise the State mandated holding costs of a project. The established and accepted *modus operandii* is '*use it or lose it*', and as

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	such any tax benefit should flow to those corporations undertaking legitimate activities. A minimum claim ensures that the capped benefit does not get excessively diluted by numerous small applications. Furthermore, a minimum claim requirement promotes bureaucratic efficiency. • A maximum should be introduced to ensure that anomalously large claims do not disadvantage other claimants by reducing the available pool of the residual EDI benefit.