RSM Bird Cameron

RSM Bird Cameron
Level 21
55 Collins Street Melbourne VIC 3000
PO Box 248 Collins Street West VIC 8007
T +61 3 9286 1800 **F** +61 3 9286 8199
www.rsmi.com.au

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Manager
Not for Profit and Industry Tax Concession Unit
Small Business Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: ExplorationIncentive@treasury.gov.au

Dear Sir or Madam

I provide the following comments on the design of the Exploration Development Incentive ("EDI") as outlined in the Discussion Paper from Treasury and the Department of Industry in March 2014 ("Discussion Paper")

RSM Bird Cameron is a national accounting services firm providing audit, assurance, corporate finance and tax services to a large number (more than 40) of ASX listed junior exploration companies.

The economic benefit to Australia of the exploration activities conducted by junior exploration companies (JECs) is well argued in the Mineral Council of Australia's (MCA) issues paper: Exploration Policy - Response to the Policy Transition Group of November 2010. Exploration underpins Australia's mining industry and Australia's mining industry underpins the country's economy. JECs have no or little capacity to raise debt. Their capital is predominately raised in the equity markets. The JECs we advise have struggled to raise adequate capital since the Global Financial Crisis. As the abovementioned MCA issues paper points out, Canada's Flow Through Share scheme has been successful in attracting capital to exploration projects. Whilst the proposed EDI is not as attractive as Canada's Flow Through Share scheme, it is a step in the right direction. Passing an exploration incentive back to investors will decrease the risk of their investments and by inference it should make it easier for JECs to raise capital. Our concern is that the Exploration Credit Cap will be too insignificant to influence the investment decision. Secondly, the Exploration Credit Cap will add significant complexity to the operation of the EDI. Thirdly, the policy design of the EDI to accommodate the Exploration Development Cap will cause a lag between the investor decision to commit capital to a JEC and the receipt of the Exploration Credit.

On 31 March 2014, the Melbourne office of RSM Bird Cameron invited clients and contacts from the junior exploration sector in Melbourne to discuss the policy frame-work of the EDI. Comments from this forum have been taken into account in writing this submission. Submission responses are numbered in accordance with the questions raised in Discussion Paper.

Question 2.1. The proposed exclusion from the EDI of JECs with mining activities is too broad. We have an existing ASX listed micro-cap client with a very small, low life, mining operation in Queensland. The client's mining operation helps fund an exploration program on other tenements. This client has significant carry forward tax losses. It would seem against the policy intent of the EDI to preclude a micro-cap ASX listed company from the EDI because it happens to operate a small mining operation. An annual threshold for revenue from mining operations should be established, say $100 million, beyond which the EDI could not be accessed. The proposed exclusion from the EDI for JEC’s with taxable income would be unnecessary if an annual revenue threshold for mining activity was implemented.

Question 2.3. If the predominate driver behind implementing an EDI is to encourage exploration expenditure by junior explorers, the EDI should not be restricted to only widely held entities. Subsidiaries of widely held entities and non-widely held private companies should be eligible for the EDI.

Minority shareholders would be prejudiced if they were not entitled to claim an exploration credit because the JEC was controlled by a large-cap shareholder. It would seem that the fairest way of implementing the EDI is to not restrict it to only widely held entities but to exclude “large” taxpayers from being able to claim the exploration credit where they have a shareholder stake in the JEC of more than 50%.

Question 3.1. In theory restricting the EDI to shareholders of new share issues makes economic sense in encouraging new spending on greenfield’s exploartion. In practice it would be costly to administer. The compliance costs of the EDI should be kept to a minimum. Accordingly, the EDI should be available to all shareholders.

Question 4.1. No comment

Question 4.2. Expenditure eligible for the EDI should extend to exploration activities conducted by third parties on behalf of the JEC. The EDI would need to extend to exploration activities near an existing ore body and feasibility studies otherwise few of the JECs we spoke would be eligible. The JECs we spoke to said that only a fraction of the exploration expenditure they incur would be on greenfields exploration as this was described in the Discussion Paper. Provided a mining activities revenue threshold of $100 million (consistent with the response at question 2.1) is established, the EDI could be directed towards exploration expenditure incurred by JECs.

Questions 5.1, 5.2, 5.3. and 6.1. The three modulation processes put forward in the Discussion Paper will all cause complexity and add to the compliance cost of administering the EDI. The Discussion Paper summarises key advantages and disadvantages of each method. On balance the feedback from my clients indicated that a combination of the ex-post and ex-ante modulation would be preferred to the other two methods explained in the Discussion Paper.

As an alternative, it would be simpler to administer and for investors to understand, an EDI based on a percentage of the eligible exploration expenditure incurred by the JEC. This would align the EDI more closely to Canada’s Flow Through Share scheme. Treasury could calculate a relevant percentage based on historic levels of eligible expenditure that would approximate or fall well within the expenditure cap of the proposed EDI over the forward estimates. This would give greater investor certainty, be arguably preferred by both investors and JECs and if appropriately set by Treasury, be less costly to the revenue than each of the three modulation methods proposed in the Discussion Paper.

Yours faithfully

Simon Aitken
Director