To: Office of State Revenue, Western Australia

Re: Duties Amendment (Farm-in Agreements) Bill 2020 – Consultation Draft

25 June 2020

Introduction

AMEC appreciates the opportunity to be consulted on the Office of State Revenue's (OSR) Duties Amendment (Farm-in Agreements) Bill 2020. The opportunity to consult on the draft amendments is important as our Industry is directly impacted by changes to the complex legislation governing farm-in agreements.

About AMEC

The Association of Mining and Exploration Companies (AMEC) is a national industry body representing over 275 mining and mineral exploration companies across Australia, the majority of which have project interests in Western Australia.

The mining and exploration industry make a critical contribution to the Western Australian economy, employing around 125,000 people in 2018/19. These companies collectively paid over $6B in royalties and generated more than $107B in mineral exports.

Comments regarding the Consultation Draft

General

Farm-in agreements are a standard part of mining operations. Overall, Industry finds the proposed farm-in agreement amendments prescriptive and complicated, challenging to be adequately followed by users without legal knowledge. Farm-in agreements are generally informal agreements which are negotiated in-house. The current farm-in requirements and amendments make the process formal and litigious. We acknowledge the OSR's aim to enact provisions for secure tax processes, however are concerned that overly prescriptive legislation will detract from the purpose of the agreement, and could have unintentional consequences on the agreement process in the event users are unfamiliar with the process, or unable to adhere to the complicated proposed requirements, without first engaging legal advice. AMEC supports government policy that does not significantly disadvantage new entrants in comparison with established companies.

Section 91K. Terms used

(1) The definition "exploration" could be interpreted as circular; as such AMEC recommends tightening this definition in line with the *Mining Act 1978*.

(2) S.91K(2)(b)(ii) under the definition of primary farmor, "until after the transfer is registered" the word "registered" should be replaced with "executed" or "signed" or some other language to capture the completion of a transaction and not registration of transfer. This will enable the provision to

appropriately exclude post-completion consideration, which will not prevent the farmor from being treated as a beneficial owner. This is particularly important as post-completion consideration is a very common structure in the mining industry, for example, royalties and/or milestone payments.

Section 91L. Farm-in agreements

(2) The limitation provided in this subsection is not expressly included in Section 13. To maintain consistency, AMEC recommends clause (2) is deleted. The suggested limitation unnecessarily prohibits the farmee from accessing the concession because it has a pre-existing interest or derivative mining right in respect of the tenement. Additionally, the prohibition would apply where there is a mismatch, whereby the farmee holds an interest or derivative mining right and wants to farm-in to obtain a derivative mining right or interest.

More generally, from a policy perspective we cannot see why the fact a party already has an interest of some sort in a tenement should prevent the concession applying to a subsequent farm-in. If the farm-in otherwise meets the criteria of a farm-in agreement, the fact of an existing interest should be irrelevant from a policy perspective. There are a number of reasons why someone who holds an interest may choose the farm-in model to increase its interest. Take-overs, acquisitions, or general changes in circumstances may result in renewed interest in a particular tenement, that one interest holder in that tenement wishes to consider by further expenditure in-ground, and another doesn't. The farm-in model is intended for this circumstance and to limit the concession seems arbitrary. The farm-in concession is intended to encourage exploration, not hinder it, and AMEC supports Government policy that does not hinder exploration.

Industry considers derivative mining rights to be very common. They can include scenarios where a farmee may hold such a right before a farm-in agreement, such as licence to access another's tenement to use a road, a right to access bore or search for water, to store fuel etc. A farm-in is also a derivative mining right as defined in the *Duties Act 2008*, as it will always include an authorisation of the kind referred to in section 118A of the Mining Act. This draft amendment does not appear to take that information into consideration.

In the event there is cause for potential conflict relating to existing farmee interests, we support the use of non-prescriptive legislation to allow for situation-specific tailoring.

(3) AMEC is supportive of retaining this clause (3) in the draft legislation. We have previously expressed concern that additional features may render the agreement ineligible, such as where the farmee has an alternative option to take shares in the farmor. However, we do query if a reimbursement feature (should the farmee withdraw) should be expressly recognised as being permissible.

Section 91M. Farm-in transactions

(2) We recommend tightening the definition of the provisions in this section, to make it clear that alternative arrangements to cash options are permitted. If the balance of the unspent farm-in amount is paid in cash to acquire the interest, it appears from Example 3 in the explanatory notes that the concession for exploration amounts previously spent will not apply, as the farm-in transaction is cancelled, even if the remaining amount paid in case was only minimal. Clarification is required to determine if this has been interpreted correctly, and if so, how duty will be calculated in that event.

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There are many legitimate reasons for a remaining amount to be paid in cash, for example, to either accelerate the earn-in, or address an event that prevents exploration that would otherwise mean the timeframe for expenditure cannot be met (for example COVID-19 border closures). It may only be a fraction of the overall expenditure that is paid in cash. The explanatory notes suggest the concession is lost entirely and this would be a wholly unreasonable outcome with wide-ranging implications. We would like to engage further on this once OSR clarifies its understanding of the duty liability and how it is calculated in those events.

Section 91N. Exploration requirement and exploration amount

(1) We recommend the requirement in (a) "by the farmee" be deleted, and replaced with a statement that the farmee can utilise a manager or contractor for S.91(N)(1)(a) and (b), and S.91N(4)(b) and (c). The draft wording is too restrictive and doesn't provision for the farmee commonly using a manager or contractor/s to carry out the work. Under the current legislation, the farmee is required to carry out the exploration itself. AMEC's recommendation supports reducing red tape such that so long as the farmee funds the exploration, and both the activity and the funding occur after the agreement is made, it should not matter who carries out the activity.

In relation to paragraph (a), there are examples of exploration that might extend beyond the boundaries of the tenement. One such example is airborne surveys. Broader regional exploration should be able to be counted as exploration and this paragraph does not adequately take account of those kinds of activities.

(2) Further clarification is required as paragraphs (b)(i) and (ii) appear to consider mining is included in exploration. We believe this definition requires tightening to clarify that the exploration activity permitted must relate to the type of mining allowed under the derivative mining right.

(5) While we agree that the Commissioner should have discretion and the Mining Act is one means of testing, the discretion should not be restricted to expenditure allowed to be used under the Mining Regulations in the calculation of expenditure for the purposes of expenditure conditions. For example, under the Mining Regulations certain administration costs are capped at 20% of other expenditure but these include things that should be fully claimable under a farm-in arrangement, if that is the commercial bargain of the parties. This includes things such as heritage survey costs, which should be properly counted for exploration purpose, and without which one could not undertake the exploration. If these kinds of administration costs are not intended to count as 'exploration', further consultation requested, as that is not our expectation.

As a general point, there are different references in section 91N to "after the agreement… is made" and "after the farm-in transaction is made". It is not clear if these references are referring to different things and, if not, why different language is used. Farm-in arrangements are often first documented in a binding term sheet, letter or heads of agreement and later replaced by a more formal agreement, which has the effect of terminating the initial agreement. As this is common there needs to be confirmation that the expenditure that is incurred after the initial document is signed but before the formal agreement is signed, is still the subject of the concession. We are not aware that this has been an issue in OSR practice to date, but given the substantial detail and complexity in the new legislation, it needs to be clearly addressed. This will also have implications for s91L as the formal agreement may be done around the time when the second stage of the earn-in is to commence (as

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the parties then know that the farm-in arrangement is continuing) but the reference to “when the agreement is made” in 91L(2)(a) appears to render the replacement formal farm-in agreement no longer a farm-in agreement, and yet the earlier farm-in agreement is now terminated.

Section 91P. General rules relating to charging of duty

(4) We take this to override section 27 so that unencumbered value is not relevant for calculating dutiable value in the farm-in transaction. It would be helpful for the explanatory notes to confirm this. If this is not the case, further consultation is needed. The additional considerations in S.91P(4) and S.91(R)(4) and (5) do not deal with unascertainable consideration such as uncapped royalties. We would be supportive of further consultation to consider the inclusion of additional considerations.

Section 91S. Treatment of certain options under farm-in agreements

(2) and the associated paragraph in the Explanatory Notes (page 22) suggest that a conditional option is otherwise not acquired until the condition is satisfied, which is incorrect.

Additionally, there are some cross-referencing errors on page 23 of the Explanatory Notes which refer to S.91T instead of S.91S.

(3) We believe the grounds on which there will be no duty chargeable on relevant acquisitions because option will not be granted are too limited. We recommend expanding this inclusion to cover other ad-hoc situations where the option will not be granted, providing consistent concessions.

Response to specific OSR questions

Question 1

We consider the example scenario discussed in paragraph (b)(iii) where a farmee earns into an existing derivative mining right to be sufficiently common to require being included in the farm-in legislation. From a policy perspective, this scenario should be the subject of the concession. Consent of a third-party that may or may not be needed should not dictate whether the concession legitimately applies or not.

The assumption that consent is always needed, for the purpose of farm-in legislation, is incorrect. It is the terms of the original authorisation that will determine if consent is needed. For example, the original authorisation may expressly authorise the derivative rights holder to introduce a third-party without needing the tenement holder’s consent. Additionally, on occasions where the tenement holder’s consent is required, this is not unusual and is is a matter commonly dealt with, with consent often readily obtainable.

Question 2

It is not clear what “the parties’ agreement” in the question “Which of the following would the parties’ agreement usually provide for?” is referring to, but we have sought to answer the question in any event.

The terms of the agreement that creates the derivative mining right will dictate the process to be followed and the form of document to be used when the holder of those rights wishes to dispose of part of their interest to another party, in this case, the farmee.

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The form of document required by the derivative mining right agreement varies, and depending on how the derivative mining right agreement is drafted, the legal effect of the different types of deed vary.

- Bullet point one in the question appears to describe a deed of covenant or a deed of assignment and assumption, where the farmor transfers the benefit of the derivative mining right agreement to the farmee.
- Bullet point three in the question appears to describe a deed of novation where the existing derivative mining right agreement is replaced with a new one that is in favour of both the farmor and the farmee.

What the farm-in agreement itself requires, should in turn reflect what the underlying derivative mining right agreement specifies.

Therefore, in answer to the question, bullet point 1 is most common but 3 is also common. We do not usually see something that would fit the description of bullet point 2 but it could occur.

Question 3

Section 91M(4) is a very prescriptive requirement, appearing to be based on a number of incorrect assumptions about how farm-in agreements and 'split commodity' or 'mineral sharing' agreements (the relevant form of derivative mining rights for this purpose) are drafted.

For example, a mineral sharing agreement may relate to all of the minerals in a portion only of a tenement, rather than a portion of minerals in the whole of a tenement – or a combination of both. Any of these arrangements may then be the subject of a farm-in agreement.

We recommend re-wording paragraphs (b) and (c) to the effect of, if it can be ascertained that the farmee is not able to take 100% of the minerals, then the transaction will be considered a farm-in transaction.

If the farm-in relates to 'split commodity' transactions where rights to certain minerals only are granted, it is necessary to specify the mineral(s) the agreement will apply to, to provide clarity when co-mingled mineralisation occurs. As not all derivative mining rights are split commodity transactions, this will not apply in all cases of farm-ins into derivative mining rights. For example, a derivative mining right may apply to all minerals but only relate to a specified area of a tenement, and in this instance, the minerals may not be specified as such.

In regard to specifying the "quantity" of minerals, we assume this means quantity such as tonnes or ounces or similar, not percentage of minerals. If this is referring to the tonnes, this is very uncommon. When farm-ins are initially entered into, the project is at an exploration stage and there is generally limited evidence of mineralisation that may exist, so requiring a quantity limit would be an arbitrary practice and would render most farm-ins related to derivate mining rights outside the concession.

Similarly, requiring that the agreement specify whether or not the farmee is authorised to take any minerals is unnecessarily prescriptive. That is dictated by the rights of the relevant tenements and as such it is not always spelt out in the agreement. We cannot see any policy reason why it should be required for the concession to apply.

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We recommend that both (b) and (c) be deleted.

On a related point, 91M(4)(a) requires that the agreement "specifies the mining to be authorised". Again, this is often done in a very general way by reference to the rights allowed by the tenement in question. If this is intended to require any further specificity, further consultation on the proposed provision will be required.

91M(4)(d) then says that the farmee cannot have the same rights as the farmor. What does this mean? That is exactly what the farmee will have – it will have the same rights as the farmee but it will share them with the farmee. The purpose of this sub-clause and its drafting needs significant consideration.

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