MINING SECTOR UPDATE

AUSTRALIA AND PAPUA NEW GUINEA

APRIL 2018

INTRODUCTION

Welcome to the April 2018 edition of the Mining Sector Update from Corrs Chambers Westgarth. Published each month, this briefing keeps you up-to-date with recent mining deals, market rumours, potential opportunities and relevant regulatory updates.

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IN THIS EDITION

- Success for the liquidators of Linc Energy in their appeal to the Queensland Court of Appeal.
- A look at Rio Tinto's US$4.15 billion coal asset divestments.
- Highlights of the changes proposed to the Commonwealth mineral exploration incentive scheme.
- Corrs partner Christine Covington discusses the updated policy for valuing land used for coal mining in New South Wales.
- We draw your attention to the hottest product in the battery metal market – lithium.

RECENT ANNOUNCEMENTS

Qld government supports Bowen Basin exploration

In a recent media release,[1] the Queensland government has awarded exploration rights over 131 square kilometres of the Bowen Basin to **Metroof Minerals** and **Sojitz Coal Mining**, to undertake coal exploration activities.

Oz Minerals announces takeover of Avanco Resources

In its latest ASX announcement,[2] **OZ Minerals** announced its A$418 million off-market takeover of ASX listed **Avanco Resources**, a copper and gold mining company with projects in Brazil. The takeover is subject to a 50.1% acceptance condition.

Jupiter Mines Limited to raise $240 million

Jupiter Mines has announced its plans to issue an IPO and relist on the ASX later this month.[3] The target for the IPO issue is 600 million shares, which, if achieved, will raise A$240 million for the manganese and iron ore focused mining company.

1. Dr Anthony Lynham, 'Explorers seek next-gen Bowen Basin Coal', *Media Release*, 22 March 2018.
2. Oz Minerals, 'OZ Minerals announces takeover offer for Avanco Resources', *ASX Announcement*, 27 March 2018.
3. Jupiter Mines Limited, 'Jupiter targets A$240m IPO and ASX listing', *Announcement*, 19 March 2018.

FEATURE CASE

LINC ENERGY'S DISCLAIMED PROPERTY NOT SUBJECT TO GENERAL ENVIRONMENTAL DUTY

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Linc Energy Limited (**Linc**) operated a pilot underground coal gasification project near Chinchilla. The project was operated on land owned by Linc, under the authority of a mineral development licence (**MDL**), petroleum facility licence (**PFL**) and environmental authorities issued under the *Environmental Protection Act 1994* (Qld) (**the EP Act**).

In mid-May 2016, the Chief Executive of the Department of Environment and Heritage Protection (**DEHP**) gave an Environmental Protection Order (**EPO**) to Linc, directing the company to comply with its "general environmental duty" under the EP Act.

Shortly afterwards Linc went into liquidation and on 30 June 2016, the liquidators, in reliance upon their powers under section 568(1) of the *Corporations Act 2001* (Cth) (**CA**), disclaimed the land, the MDL, the PFL and the environmental authorities. The liquidators then sought a direction from the court that they would not have to cause Linc to comply with the EPO on the basis that it imposed liabilities in respect of disclaimed property, and section 568D of the CA provides that a disclaimer terminates not only the company's rights in the disclaimed property, but also "*liabilities … in respect of the disclaimed property*".

At Trial[4]

The Chief Executive of the DEHP argued against the court making such a direction on the basis that the EPO did not attach to the property that had been disclaimed, and that an environmental authority was not property capable of being disclaimed under the CA.

One of the key issues at the original trial was whether the CA disclaimer discharged Linc from complying with its obligations under the EPO. The trial judge held that there was direct inconsistency between the operation of sections 568 and 568D of the CA and sections 319 and 358 of the EP Act. Ordinarily, State law is invalid to the extent of any inconsistency with Federal law, but the judge held that in this case, section 5G(11) of the CA rolled back the operation of its inconsistent disclaimer provisions, thereby allowing the provisions of the EP Act to have effect. This meant that Linc was obligated to meet the requirements of the EPO.

The judge's findings caused disquiet in the insolvency industry, as its far-reaching consequences meant that liquidators may have to bear the cost of complying with environmental obligations of an insolvent company, ahead of the liquidators' own remuneration. Depending on the magnitude of costs and time required to meet those environmental obligations, compliance could significantly reduce or even extinguish returns which would otherwise be available to creditors, as well as delaying the finalisation of the winding up process significantly. The decision may also have had the effect of causing insolvency practitioners to refuse to accept appointment as administrators, receivers or liquidators of insolvent resource companies, thereby undermining the insolvency regime in Australia.

4. *Linc Energy Ltd (in Liq): Longley & Ors v Chief Executive Dept of Environment & Heritage Protection* [2017] QSC 53

In *this* case, the EPO *did* impose liabilities in respect of the property

Successful Appeal

On 9 March 2018, the original decision was successfully appealed. Justice McMurdo delivered the lead judgment in which he found that the liabilities imposed by the EPO were liabilities *"in respect of the property disclaimed"* and therefore had been terminated by the effect of the disclaimer provisions in the CA.

Justice McMurdo also held, in respect of the argument that section 5G(11) of the CA rolled back provisions inconsistent with the EP Act, that selected effects of a valid disclaimer could not be divorced from the operation of others, and that in any case, *"upon its proper construction, section 5G did not affect the operation and constitutional paramountcy of the disclaimer provisions."*

The EPO that was issued to Linc required it to perform its general environmental duty. However, the Court of Appeal held that once the land, plant, equipment and MDL had been disclaimed, there was no occasion for Linc to do so.

The State argued that the liabilities imposed by the EPO existed independently from any property held (or disclaimed) by Linc, and that an EPO is not required to specify relevant property, but rather a specific person (an EPO can be issued to a person in respect of land which that person does not own).

The Court of Appeal held that, according to the EP Act, the requirements of an EPO will not have the requisite connection with the property (such that its requirements would amount to "liabilities in respect of the property") in every case. But in *this* case, the EPO *did* impose liabilities in respect of the property, and therefore in this case, the disclaimer of the property extinguished those obligations:

> *"the connection between the disclaimed property and the liabilities under the EPO is … **clear and immediate:** the liabilities under the EPO were premised upon Linc's carrying out **activity which it could not and would not carry out, once the land and MDL had been disclaimed."** (emphasis added)*

Any EPO that requires a liquidator to incur particularly burdensome costs might be imposing obligations inconsistent with their winding-up obligations

Conclusion

This decision in the Queensland Court of Appeal may elicit a collective sigh of relief amongst liquidators but, interestingly, the Court left open the possibility that it might be possible for an EPO to be constructed such that it would *not* be avoidable with a disclaimer (i.e. if it is not sufficiently connected with the land or property disclaimed).

Furthermore, the Court of Appeal suggested that any EPO that requires a liquidator to incur particularly burdensome costs might be imposing obligations inconsistent with their winding-up obligations under the CA,[5] and given the outcome of this case, it is likely that the latter will take priority where there has been a valid disclaimer.

5. *Longley & Ors v Chief Executive, Department of Environment and Heritage Protection & Anor; Longley & Ors v Chief Executive, Department of Environment and Heritage Protection* [2018] QCA 32 at [126].

RECENTLY COMPLETED DEALS

Rio Tinto earns US$4.15 billion in recent coal asset sales

The press has been saturated with news of the three separate deals entered into by **Rio Tinto** over the past few weeks in relation to the sale of its last remaining coal assets.

The *Australian Financial Review* reported Rio Tinto's agreement to sell its Kestrel mine to private equity manager, **EMR Capital**, and IDX listed coal company, **Adaro Energy** for US$2.25 billion. This transaction is scheduled to complete later this year and is subject to FIRB approval.

Also amongst the transactions is Rio Tinto's sale of its 82% ownership of the Hail Creek coal mine and its 71% ownership in the separate Valeria thermal coal project to LSE listed **Glencore** for US$1.7 billion.

The Hail Creek divestment is anticipated to complete later this year, subject to regulatory approvals. The remaining stake in Hail Creek is owned by **Nippon Steel Australia**, **Marubeni Coal** and **Sumisho Coal Development**.

Rio also recently announced the sale of its 75% interest in the Winchester South coal project to ASX listed **Whitehaven Coal** for US$200 million.[6]

The total sale value of Rio's Queensland coal assets has been well in excess of the US$1.5 to US$2 billion portfolio value reported by *Bloomberg* and the *Australian Financial Review* in the second half of last year.

However, it's not just sales on Rio Tinto's radar. Rio has recently signed an earn-in and joint venture agreement with **Raiden Resources**, just weeks after Raiden listed on the ASX. The *Australian Financial Review* reported that the mining major will invest US$31.5 million in Raiden Resources' Serbian exploration activities, for a 75% stake in the tenements.

It's not just sales on Rio Tinto's radar

6. 'Rio Tinto agrees sale of Winchester South to Whitehaven for $200 million', *Media Release*, 22 March 2018.

MARKET OPPORTUNITIES

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Worldwide rumours were sparked about Tesla's plans to secure raw battery materials directly from miners when Elon Musk appeared in Chile late last year. Since then, companies such as Toyota, Volkswagon and Samsung have been reported to have engaged in similar agreements,[7] as the demand for battery metals heats up.

This month we focus in on the rumours and opportunities in the lithium market.

Activity set to heat up at Pilgangoora

In late February, KRX listed Korean giant **POSCO** joined the ranks of China's SZSE listed **Ganfeng Lithium** and SSE listed **Great Wall Motor Company**, by investing A$79.6 million in ASX listed **Pilbara Minerals Limited**. The deal includes an off-take agreement securing Pilbara Minerals' position in the South Korean lithium market and an equity injection to accelerate stage 2 of their Pilgangoora project.

Altura announces control transaction discussions with key shareholder

Pilbara Minerals' neighbour in the Pilgangoora area, ASX listed **Altura Mining Limited**, has responded to speculation and confirmed that they are discussing a potential takeover transaction. In their recent ASX announcement, Altura emphasised that these discussions with substantial shareholder SZSE listed **Shaanxi J&R Optimum Energy Co. Ltd**, are incomplete and there is no certainty that the transaction will proceed.

Lithium prices surge, mergers expected

The Business Times reports that we may see a rush of merger deals globally within the lithium industry thanks to the surge in lithium prices. As the lithium-ion battery demand is driven by the electric vehicle market, car manufacturers and battery suppliers are also getting involved and taking stakes in the lithium industry.

While some expect a sharp decline in the lithium price, *Bloomberg New Energy Finance* states that a price collapse is unlikely.

Tom Hodgson, CEO of TSX listed **Lithium Americas Corp**, said the growth of **Ganfeng Lithium Co** and **Tianqi Lithium Corp** will mean "[t]here will be one or two new players in the oligopoly."[8]

The Business Times reports the following potential transactions:

- A number of companies are vying for TSE listed **Nurien Ltd**'s US$4 billion stake in NYSE listed **SQM** (Soc Quimica & Minera de Chile).
- **Tianqi** has been considering a Hong Kong share sale that could raise up to US$500 million.
- As mentioned above, SZSE listed **Shaanxi J&R Optimum Energy Co.** is in takeover discussions with ASX listed **Altura Mining Ltd**.
- NYSE listed **FMC Corp** is planning to spin off its lithium business later in the year, valuing the unit at US$3 billion.
- ASX listed **Galaxy Resources** is seeking partners to advance its Sal de Vida project.
- ASX listed **Tawana Resources** predicts it will become a target.

7. Kristie Batten, 'Scramble for battery materials accelerating', *Mining News*, 16 March 2018.
8. 'Lithium price surge expected to fuel rush in merger deals' *The Business Times (online)*, 22 March 2018.

The ATO remains focused on maintaining arm's length sales

The *Australian Financial Review* has reported that the Australian Taxation Office (**ATO**) is currently investigating the foreign owners of **Windfield Holdings**, NYSE listed **Albemarle Corp** (USA) and SZSE listed **Tianqi Lithium Corp** (China), to determine whether the prices Abermarle and Tianqi paid for Windfield's spodumene concentrate in 2015 and 2016 were reasonable. This follows a similar investigation by the ATO into prices paid by Singaporean subsidiaries of BHP and Rio Tinto for Australian commodities last year.

In an effort to avoid any future concerns, Windfield is seeking approval to implement an "advanced pricing arrangement" for 2017 to 2019 sales to Albemarle and Tianqi.

Windfield Holdings' Greenbushes mine in Western Australia is the world's biggest and highest-grade producer of lithium-rich spodumene rock. In recent years, Windfield has capitalised on surging lithium prices with revenues rising from A$201.7 million in 2014 to A$423.8 million in 2017, and profits similarly increasing from A$80.3 million to A$196.8 million.

Both Albermarle and Tianqi are making progress towards building their own WA-based lithium processing plants to benefit from the anticipated growth in demand for lithium products.

Windfield Holdings' Greenbushes mine in Western Australia is the world's biggest and highest-grade producer of lithium-rich spodumene rock

REGULATORY UPDATES

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COMMONWEALTH

Commonwealth introduces new and improved incentive regime to boost resources sector

The *Treasury Laws Amendment (Junior Minerals Exploration Incentive) Act 2017* (Cth) (**Act**) received royal assent on 28 March 2018. Under the legislation, the Commonwealth government will provide A$100 million over the next four years to "greenfields" exploration projects.

The Act amends the *Income Tax Assessment Act 1997* (Cth) (**ITAA**) to include a new Junior Mineral Exploration Incentive (**incentive**) scheme, which allows eligible exploration companies to issue exploration credits to their investors, as a means of distributing the company's tax losses as a refundable tax offset (or as franking credits, if the investor is a corporation).

Between 2011 and 2016, expenditure in greenfields exploration is reported to have fallen by approximately 70%. The incentive replaces the former Exploration Development Incentive (**EDI**), which was given effect in March 2015 and ceased after the 2016-17 income year.

Junior exploration companies have found it difficult to gain investment in the current market, as the nature of their activities is mostly high risk. The objective of the incentive is to assist smaller mineral exploration companies to raise capital by making investments in their projects more attractive. The Minister for Finance, Mathias Cormann, said in a recent statement that the incentive "will encourage junior explorers to take risks and have a go at discovering the next large-scale mineral deposit".[9]

Exploration credits will be allocated to eligible exploration companies on a first-come first-served basis, until the annual allocation is exhausted. Further, the Act limits the amount of credits a single entity can obtain to 5% of the total annual allocation, to manage the spread of credit distribution in the market. The Commissioner's allocation for the 2017-18 financial year will be capped at $15 million, making the maximum possible credit allocation for this period A$750,000, to 20 separate entities. Unlike the EDI, recipients of exploration credits will be limited to Australian resident investors who purchase newly issued shares.

Any unallocated exploration credits held by the Commissioner at the end of the financial year will accrue and be carried over to the following year. This means that, even if the uptake is less than the allowable cap in the initial years of the incentive regime, the full amount of the Government's budget allocation will remain available for distribution to eligible companies until the end of the four year incentive period.

The Department of Industry, Innovation and Science will conduct a review of the effectiveness of the incentive scheme in attracting investment by 30 June 2020.

9. "Unearthing Junior Mining Exploration opportunities", Media Release, 19 March 2018, 2.

NEW SOUTH WALES

Valuer General's Policy for the Valuation of Land used for Coal Mining

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The NSW Valuer General (**VG**) recently updated its policy for the Valuation of Land used for Coal Mining (**Policy**). The new Policy significantly changes the way in which land used for coal mining is valued. This will have implications for the way both land tax and council rates are calculated in relation to land used for coal mining, although the full extent of those implications remains to be seen.

The Policy was revised following a decision of the NSW Court of Appeal in *Perilya Broken Hill Ltd v Valuer-General* [2015] NSWCA 400 (***Perilya***). In that case, the Court of Appeal upheld earlier decisions of the NSW Land and Environment Court which held that minerals should be assumed to be owned by the owner of the coal mine for the purposes of land valuations, with future royalty streams payable to the landowner, despite the existence of any Crown reservations. This signalled a new interpretation of section 6A of the *Valuation of Land Act 1916* (NSW) which prompted updates to the valuation methodology under the Policy.

Summary of Perilya

The Court of Appeal decision upheld two Land and Environment Court decisions (*Perilya Broken Hill Ltd v Valuer-General (No 6)* [2015] NSWLEC 43 and *Perilya Broken Hill Ltd v Valuer-General (No 8)* [2015] NSWLEC 72). Special leave to appeal to the High Court was refused on 28 July 2016.

The *Perilya* decisions concerned the interpretation of the hypothetical "fee simple" to be assumed for the purpose of section 6A(1) of the *Valuation of Land Act 1916* (NSW), which provides:

> (1) *The land value is the capital sum which the fee-simple of the land might be expected to realise if offered for sale on such reasonable terms and conditions as a bona-fide seller would require, assuming that the improvements, if any, thereon or appertaining thereto, other than land improvements, and made or acquired by the owner or the owner's predecessor in title had not been made.*

Perilya had title to 11 mining leases applying to some 3,033ha of land near Broken Hill. It was common ground that the highest and best use of the land was as a mine for the production of lead, zinc and silver. The Valuer-General valued the land at $20,900,000 as at 1 July 2007. Perilya contended for a land value of $5,250,000. It became common ground, over the course of several proceedings, that all of the minerals were reserved to the Crown.

The Court of Appeal held that:

a) the hypothetical "fee simple" is an "absolute or pure title" which is not subject to the reservations of minerals to the Crown (applying the Privy Council's decision in *Gollan v Randwick Municipal Council* (1960) 6 LGRA 275, which the Court of Appeal held remains authoritative despite abolition of the Privy Council);

b) accordingly, any reservation to the Crown in the grant is to be disregarded for the purposes of s 6A(1) of the *Valuation of Land Act 1916*, and the value of land containing publicly owned minerals is to be determined on the assumption that the minerals are privately owned; and

There is a risk to coal mine owners that local councils will seek to increase their rates revenue from coal mines as a result of the Policy

c) the *Mining Act 1992* (NSW) imposes liabilities on the holder of a mining lease to pay compensation to affected landowners and to pay royalties to the Minister, which need to be brought to account in the valuation methodology. If the Minister receives royalties in respect of privately owned minerals, the Minister must pay seven eighths of the amount to the owner of the mineral (section 284). Where minerals are assumed to be privately owned, their value is to be determined as 7/8ths of the net present value of the royalty income.

Valuation methodology under the Policy

The Policy applies to coal mines, being land to which a mining lease for coal applies. Non-coal mines, exploration licenses, prospecting licenses and authorisation areas are not affected.

Under the Policy, the value of the coal resource in respect of a coal mine is attributed to the landowner, irrespective of any Crown reservations (following *Perilya*). The assumption is made that the owner of the land is not the operator of the mine. This means:

1. the value of the coal resource is valued by determining 7/8ths of the net present value of the royalty income (this follows from section 284(2) of the *Mining Act 1992* which deems 7/8ths of the Crown royalty payable under a mining lease to be returnable to the owner of the mineral); and
2. the value of the land is determined by reference to the present value of the residual surface land, deferred for the life of mine.

Implications of the Policy

The implications of the new valuation approach under the Policy are that, for the valuation of land used for coal mining:

a) the value of the coal resource will increase, potentially significantly, as it is attributed to the owner of the coal mine despite the existence of Crown reservations;

b) as **land tax** is not payable on the value of coal resource (see section 14F(4) of the *Valuation of Land Act 1916*), the land value, and therefore land tax, will likely decrease in most cases; and

c) as **local council rates** are payable in relation to the land including the coal resource, council rates will likely increase.

It is not known at this stage how local councils will factor in the increased land values in assessing council rates, and councils will not be required to update their valuations using the changed methodology under the Policy until 1 July 2019. There is a risk to coal mine owners that local councils will seek to increase their rates revenue from coal mines as a result of the Policy, subject to statutory limits and 'rate pegs' set by the Minister for Local Government and the Independent Pricing and Regulatory Tribunal.

Valuations have been issued under the new Policy for 2018, in respect of which the Valuer General is currently seeking feedback. It is intended that these valuations will be used for 2018 land tax assessments and 2019 council rates assessments.

OTHER NEWS

The 6th edition of our annual publication 'Investing in the Australian Mining Industry' is now live

Our Energy, Resources and Projects team has produced this sixth edition of *Investing in the Australian Mining Industry* as a useful source of information for those interested, or considering strategic investment, in this important Australian industry.

The publication provides background information in relation to the Australian mining industry generally – and the coal and iron ore sectors in particular. It explores some of the key legal considerations for investing in mining projects in Australia, covering topics such as investment structures, tax and royalties, employment relations, due diligence and financing.

A link to the publication is available here.

A useful source of information for those interested, or considering strategic investment, in this important Australian industry

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