McARTHUR RIVER MINE: ECONOMIC ISSUES – A Briefing, April 2006

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MRM is a wholly-owned subsidiary of Swiss mining giant Xstrata. Xstrata acquired the remaining 25% stake in MRM from a group of Japanese trading companies (Nippon, Mitsui and Marubeni) known as ANT Minerals in the second half of 2005 (*Xstrata 2005 Annual Report*). The proposed McArthur River Open Cut Project is promoted by the company as a A$66 million development that will extend the mine's life by 25 years (though it may be extended even more in the future as the current proposal is targeting only one-quarter of the available resource).

Many claims have been made in the media recently about the possible economic benefits of the McArthur River Mine Open Cut Project and the economic costs should it not proceed. A CLP flyer makes the following claims about the costs if the open cut does not proceed:

- "270 direct jobs lost;
- 1430 indirect jobs lost;
- 570 indirect jobs (construction phase) lost;
- $329 million dollars per annum income to the Territory lost;
- $523 million dollars per annum income to the Nation lost."

Some of these figures have been derived from the following tables presented in the Draft EIS (Ch. 17), though the figure of 1430 indirect jobs lost is hard to discern. The figures for the economic output ($m) and indirect jobs take into account multiplier effects and are derived from national input-output tables (produced by ABS) and an unpublished input-output table for the NT (produced by Prime Research and ACIL Tasman).

Annual Economic Impact of Current (Underground) Operations.

Region	Output ($m)	Income ($m)	Employment -direct & (indirect) jobs	Value-added ($m)
NT	357	49	330 (800)	184
Australia	561	96	(1940)	285

1. *How many of the current jobs are held by people from the Borroloola area?* The Draft EIS (3.7) maintains that approx 10% of workers live locally, mainly in Borroloola.
2. *Where do most of the workers and contractors live – Darwin or Mt Isa/Townsville?* The Draft EIS (3.7) says that approx 90% of the workforce works on a fly-in/fly-out basis out of Darwin, but does not specify where these people actually live.
3. *What assumptions are made in order to estimate the multiplier effects for both the existing mine and the open cut operations? How can the public access a copy of the Prime Research/ACIL Tasman analysis?*

Annual Economic Impact of Open Cut Operations

Region	Output ($m)	Income ($m)	Employment -direct & (indirect) jobs	Value-added ($m)
NT	329	39	270 (610)	175
Australia	523	84	(1700)	271

In the NT, annual spending by MRM will decrease from $41 million to $33 million if the mine shifts to open cut (Draft EIS, Ch 17).

Annual Economic Impact of the Construction Phase

Region	Output ($m)	Income ($m)	Employment -direct & (indirect) jobs	Value-added ($m)
NT	46	11	290	21
Australia	97	24	570	47

During construction of the open cut, companies in the NT are expected to capture $47 million of the construction spending (Draft EIS, Ch. 17).

4. *Is this an annual figure? How does it relate to the table above?*

Additionally, it has been claimed by the company that the project will make a $175 million contribution to the NT's Gross State Product (Source: Xstrata: McArthur River Mine, northern Australia - the future for a world leading resource.
http://www.mcarthurriver.com.au/pdf/Xstrata_Corp_Factsheet.pdf : accessed 29/3/06).

5. *How is this figure derived?*

However, it was reported in the NT News (28 February 2006) that McArthur River Mine had not paid mineral royalties to the NT Government in over a decade of operations. It is obliged to pay 18 per cent of its profits under the NT *Mineral Royalty Act*, but claims not to have made any profit since it opened. Other Australian jurisdictions, meanwhile (e.g. WA, Queensland), tend to charge royalties according to the sales value of the mineral rather than on a profit basis. It was reported that the cost of transporting the ore was being passed on to the mine by Xstrata's head office in Zug, Switzerland. Concerns have therefore been raised about *transfer pricing*.

6. *How can a mine keep operating for ten years whilst not making a profit?*

Currently, MRM has an agreement with Glencore International (a Swiss-based metal trading conglomerate which has owns 16% of Xstrata ordinary shares) to supply 204,800 wmt (wet metric tonnes) per annum in 2005 and 2006 of zinc concentrate (Xstrata plc Interim Report 2005: p90). This would constitute the bulk of the mine's export volume.

7. *Is transfer pricing the correct term to use in this situation and how usual is this practice in the mining industry?*

MRM responded by saying that the mine paid millions of dollars each year in other taxes, such as payroll tax.

8. *How true is this, and how much is paid in these other taxes?*

Under previous owners MIM Holdings (prior to mid-2003), it appears as though there was a similar global shifting of costs, which made the mine unprofitable. The *MIM 2002 Annual Report* announced an operating loss of $0.9m in 2002 for McArthur River Mine, although in 2001 an operating profit of $15.9m had been recorded. Operating profit means profit before interest, tax and foreign exchange are taken into account. The Annual report cites 'off-site realisation costs' as the reason for the low profitability:

> 'Both the McArthur River and Mt Isa lead-zinc mines are world competitive in terms of on-site operating costs but off-site realisation costs, mainly transport and smelting, represent up to 60% of total production costs (in the case of McArthur River) and are eliminating margins in a low price market' (p17).

9. *Why does McArthur River Mine have to pay for the transportation and smelting costs*?

MIM Holdings was sending most of its lead-zinc concentrate to Europe (MIM Annual Report 2002, p17). MIM owned two zinc smelters in Europe at the time – Duisburg (Germany) and Avonmouth (UK) – both of which recorded substantial operating losses in 2002. 70,000 tonnes per annum of McArthur zinc concentrate – over half of the mine's production - was being exported to the Duisburg smelter. The company sold its interest in this smelter in late 2002, partly in order to avoid environmental clean up costs (http://www.aktienboard.com/vb/archive/index.php/t-47531.html). Avonmouth smelter closed in March 2003.

10. *Why was it helping to prop up unprofitable overseas zinc smelters for years and therefore not paying mineral royalties to the NT Government?*

MRM has also been receiving an electricity subsidy from the NT Government since it opened. It is difficult to find out how much. NT Treasury documents available on the internet only indicate that the NT Government's estimated quantifiable contingent liability at 30 June 2003 for Pine Creek/McArthur River Electricity Purchase Agreements was $112 million (2004-05 Budget Paper No. 2: Fiscal and Economic Outlook), which is not particularly helpful.

Nevertheless, it was reported in the NT News (6 March 2005) that Xstrata had been seeking an electricity subsidy of up to $100 million from the NT Government to help it build a new processing facility on-site. Power and Water, however, is already selling natural gas to the mine at a price typically below what it was selling to everyone else. The NT Government rejected the additional subsidy proposal.

11. *How much in energy subsidies has MRM received since it started operating?*

The McArthur River Project Agreement Ratification Act 1992 gave effect to a franchise agreement between the NT Government and MIM. The Commonwealth and the NT Government would spend $11.25 million to upgrade roads from the mine site to the port (Toyne 1994). An amendment to the Act in 1993 validated the mining leases and thereby diminished the rights of native title claimants. The Commonwealth then purchased Bauhina Downs station for the Gundanji people for $1.7 million, who in turn agreed to forgo any claims for compensation from the Commonwealth arising from their native title interests (Toyne 1994). Section 22(4) of Schedule 1 to the Act also laid out the very lenient conditions upon which royalties would be paid, or not paid as turned out to be the case.

Also for the record, Xstrata's *Annual Report 2005* shows that the Executive Director of Xstrata Zinc, Santiago Zaldumbide, received US$3 million in emoluments and compensation during the 2004-05 financial year (p102). Xstrata attributable profits for 2005 were up 60% on the previous year to US$1.7 billion.

Claimed local benefits of the mine include:

- Revenue generated by the barge operation run by Carpentaria Shipping Services, a joint venture between Mawurli and Wirriwangkuma Aboriginal Association (MAWA) and P&O. The EIS Supplement claims that gross revenues for the shareholders range between $6M - $7M per year in which MAWA has a $31.7% interest (p4-4).

- Jobs and training for local Aboriginal people. The STEP program 2000-02 trained 19 Aboriginal participants. 6 have ended up working at the mine permanently (Draft EIS 15.3.4). Over the life of the mine, an average of 10% of mine staff have been local Indigenous people. This includes a total of 106 local Aboriginal youth employed in the mine's Maintenance Service Team (MST) program – the entry level traineeship for mine employment. In addition, 80 local Aboriginal people have been employed by the barge operation (EIS Supplement: 4-10; 17-5).

12. *Is this real employment or simply a training program?*

- Sponsorships and donations valued at approximately $50,000 per annum (Source: Xstrata: McArthur River Mine, northern Australia - the future for a world leading resource. http://www.mcarthurriver.com.au/pdf/Xstrata_Corp_Factsheet.pdf : accessed 29/3/06). A further $600,000 is committed to the local Borroloola swimming pool and its maintenance (EIS Supplement 17-5).

13. *How do these levels of local benefit compare with other NT / Australian mines?*

Another claim that has been made in full-page advertisements in the *NT News* is that there are over 400 NT companies that rely on MRM business.

14. *Is this correct?*

The current rehabilitation bond for the existing mine is $12 million reassessed annually (Draft EIS: App E). No bond has been negotiated as yet for the open cut proposal.

15. *What are the estimated long-term rehabilitation costs and what may the Territory Government and community be eventually liable for? cf. Mt Todd gold mine.*

<u>Additional Reference</u>

Toyne, P. 1994. The story of the McArthur River Mine. In *The Reluctant Nation: environment, law and politics in Australia*, ABC Books, Sydney.

Attachment 1: EPA Assessment

The NT Environment Protection Agency's assessment report (Feb 2006) also looked at economic issues (p36-38).

4.8 Objectives and Benefits of the Mine Expansion

The draft EIS presents the objectives of the mine as securing the long-term viability of the McArthur River operation by changing from underground mining, which is becoming uneconomical due to reduced output rates and safety issues necessitating increased expenditure, to open cut mining methods. This will provide MRM with the opportunity to increase its participation in the zinc business and to capture an increased portion of the market for zinc concentrates, which is increasing significantly in demand.

The benefits of this proposal to the Northern Territory have been stated in the draft EIS as significant and include the contribution of $175 million to the Gross State Product of the Territory, the creation of an average 290 jobs during construction and 610 during operation (including flow-on effects). Additionally, the proponent estimates that it will contribute $329 million annually to the economic output of all industries in the NT (including flow-on effects).

A 2004 study undertaken by ACIL Tasman (prepared for the then Office of Territory Development) found that MRM directly impacts on the economy via its production, employment and investment and through its demand for a range of goods and services it indirectly generates additional output, value added (the building block of Gross State Product) and employment in the Territory. General equilibrium modelling of these direct and indirect impacts indicated that if MRM were to close at the end of 2005 the Northern Territory economy would experience a decline in GSP and employment. Estimates for the twelve month period after mine closure indicated that:-

- GSP would be 0.96% lower;
- Employment would be 0.57% lower; and
- Wages and salaries paid to Territorian's would be 1.18% lower.

These direct and indirect impacts highlight that MRM was (in 2004) contributing some $84.1m to the Territory's GSP (direct and indirect contributions). The majority of MRM's direct contribution is via wages and salaries as MRM was not profitable and was not paying royalties or state taxes.

A respondent to the EIS raised a concern regarding the uncertainty of the current mine life indicating that it the underground mine was originally proposed to have a mine life of 25 years and is being decommissioned after only 10. Further, the respondent is concerned that the proponent has not demonstrated that the operation will remain viable given that "the EIS states that during mining if strip rates are too high, ore quality is low or the zinc price falls, there is the possibility that the mine would close within the 25-year life" The EIS states "As the ore-body deepens, ever increasing amounts of waste must be uncovered for each tonne of ore. The ratio of waste tonnes mined to ore tonnes mined is termed the 'strip ratio'. Above a certain strip ratio, depending on ore grades, metal prices, and mining and processing costs, it is no longer economic to mine the ore by open cut methods" This has implications for the stated benefits of the proposal and calls into question the value of diverting the McArthur River and associated impacts in the face of this uncertainty. The proponent expresses confidence that the proposal will be viable and indicates that if the mine life is reduced, contingencies are in place to ensure there will be no long-term detrimental impacts postclosure.

The Northern Territory Government took part in a nation-wide survey of recreational and indigenous fishing (2000-01 National Recreational and Indigenous Fishing Survey). The latest estimates from the survey (URS 2005b) place spending on recreational fishing in the Northern Territory at $26.7 million in 2000-01, down from the 1995 estimate of $30 million. Total recreational fishing effort in the Territory was estimated at 1.9 million hours, with barramundi the most popular target species, accounting for 42% of all hours fished. The Amateur Fishermen's Association estimates that the McArthur River area accounts for considerably more of the Territory's recreational fishing effort than the 11% assessed in 2002.

It is recognised that recreational fishing is responsible for significant tourism in the Territory, including in the lower McArthur River. Access is through use of personal equipment or through charter companies. Inputs into amateur fishing trips are usually greater than the financial (market) value of the fish and seafood caught, but in compensation the fishermen receive additional recreational, social and cultural benefits that are difficult to quantify.

As discussed in the EIS, the environmental safeguards to be implemented as part of the Open Cut Project have been designed to ensure there will be no significant detrimental downstream effects. No impacts on the recreational fishing industry in the lower McArthur River are expected. Consequently the potential costs to the tourism and fishing industries in the region as a result of the project are considered to be negligible.

<u>Questions arising from the EPA assessment</u>

16. *Have there been any additional economic assessments by the NT Government of McArthur River Mine, apart from the ACIL Tasman report to the Office of Territory Development?If so, have they looked at all of the economic costs and benefits (including rehabilitation risks and the electricity subsidy)?*
    ECNT understands, following a discussion with Mines Minister Kon Vatskalis (17 March 2006) and following a statement made by the Minister in the NT Legislative Assembly during a debate on McArthur River Mine (see *Daily Hansard*, 30 March 2006), that an additional economic study has been completed by the Department of Business, Economic and Regional Development (DBERD). This has shown that the mine contributes 1% of the NT's Gross State Product ($141 million), not 4% as claimed by the CLP Opposition.

17. *Why is there no assessment by the EPA itself on the potential impacts on downstream fisheries and tourism values, rather than just repeating reassurances made by the company in the EIS?What would a full and thorough assessment find?*

18. *Another consideration is the potential impacts on the customary economy downstream of the mine, particularly should there be a major pollution incident.*