Mining RSPT Letter and AIG response **11/06/2010**

Dear All,

Krucible director Ray Koenig, who has 40 years experience in mining project development/management formulated this letter in response to a briefing by a senior Treasury official.
We believe we need to agitate in a professional manner and would like AIG to circulate Andrew Waltho' s response shown on the AIG website to all AIG members by email.
The more well considered anti RSPT messages circulating the better.
I also suggest we get someone from KPMG or a key Superfund to talk at MEGWA, SMEDG and BEDG on the effects of the RSPT. Any thoughts on this?

Cheers, Marcus Harris.

Ray's letter follows:

Dear Scott,

Thank you for the presentation on the RSPT in Burnie last Friday (4 June) and although it did make clearer the RSPT mechanisms I soon came to the conclusion that Treasury and the current Government do not understand how mining projects are financed. Just suggesting that Treasury would like to negotiate a new tax with the Mining Industry over 2 years is enough to cause finance sources for small Australian companies like Krucible Metals to dry up let alone saying that the taxes are being increased by 40% of profit before Income Tax.

I know you believe that paying off the mining company losses in bad times is supposed to compensate for the 40% increase as RSPT but when financing a project, this is not considered beneficial by banks and other risk venture financiers. Mining project financial models use conservative product pricing together with many sensitivity variables, including currency exchange rate. When a project is robust it will pass rigorous scoping studies and ultimately a bankable feasibility study {BFS} that heavily discounts the risk. Currently and historically, banks and other venture financiers know that mining projects are risky and demand exceptional profit margins to ensure they will confidently return their capital plus interest. Also using Pilbara Iron Ore operations owned by large cap high net worth mining companies, as the base case extraordinarily distorts an economic rent analysis.

Unfortunately the mining industry could have given advice before the RSPT announcement was released. Although it is too late, perhaps it would have been better to consider other options before announcing the tax changes. Your presentation caused me to consider what other options may have been available to you. States use a Royalty system because they cannot use another revenue tax. Therefore, if Treasury suggests transfer from the Royalty based system to a Federal 40% Profit Before Income Tax then both the States and the Miners would need to accept this – a difficult task for both the Federal and State governments.

Unfortunately the mining industry should have had the opportunity to consult with Treasury and the Federal Government before the internationally uncompetitive tax changes that is the RSPT announcement. Nevertheless, your presentation caused me to consider what other options may have been available to Treasury and the Rudd Government and I would have suggested the following:

1. The Rudd Government initially negotiates with the States who constitutionally own the mineral rights to take over those rights in return for a superior benefit. Now I know this would not have been easy but having the States royalties in place and a Federal tax on top will produce another layer of bureaucracy for the miners. This will certainly increase compliance costs for industry (as

you admitted) and reduces our mining industry's efficiency compared to overseas jurisdictions.

2. Treasury would have to clearly demonstrate to our mining companies that the 40% Profit Before Income Tax would be sustainable, without any fall back to the Australian Taxpayer covering future project failures as this is likely to not be supported by future or even the existing Governments.

3. Treasury would have to clearly demonstrate to our mining companies that the 40% Profit Before Income Tax would be competitive with other low sovereign risk mineral producing countries, such as Canada and Brazil and Ghana.

4.The Rudd Government has to explain why any new Tax which exceeds revenue derived from Royalties should be retrospective.

Australia's international standing as a low sovereign risk country is in disarray thanks to the poor consultation process and the current Government's demonstrated intransigence. Now the horse has bolted and the chance of negotiating with the states has disappeared. The only chance of re-establishing Australian low sovereign risk looks like a change of government and reversion to our current system. An opportunity to negotiate a better system is likely to be decades away.

As it is now, the potential for increasing the tax without damaging the mining industry is gone so that Canada, South Africa, Brazil and Indonesia are likely to be the recipients of finance planned for Australia. The BHPs and Rios have little trouble in adjusting their financing but for hundreds of small cap Australian mining companies exploring and developing mines in Australia, this is a disaster.

Our industry consists of dozens of small cap explorers with One in a Million chance of making a major discovery to a handful of well funded international conglomerates with global operations. Never-the-less these global players started life as small cap ventures like Krucible Metals. Small cap explorers /miners need venture capital for up to ten years to have a chance of being successful. The venture capital is obtained on the basis that these small cap miners will strike it rich. The fact that some have and that they rewarded their shareholders handsomely sustains our industry. It will not be sustained by the prospect of a 40% Profit Before Income Tax being imposed on that discovery. Treasury may think these small cap miners are inconsequential, BUT the future discoveries that will sustain our resources are demonstrably in their hands. They MUST be considered carefully and seriously in crafting any new RSPT. It is all very well for Treasury and the Government to offer a 30% rebate on exploration, but small cap explorers need venture capital to fund exploration in the first place. They can't survive on heavily audited government controlled rebate funds.

This brings up another point I would like to make is that cash flow is critical for all small explorers and miners. Selwyn Copper and Copperco no longer exist despite having very good operations, with delays in the payment chain they just did not have enough money at the end of the month and they went into receivership and disappeared. Waiting for the government either to refund royalties or to provide tax deductions is likely to do similar severe damage. I am sure this is not taken into account in your modelling.

Although it is all too late, I am willing to assist in framing any future approaches to the taxation system if the RSPT does or does not survive. I will send a hard copy of this on company letterhead.

Ray Koenig
Director
Krucible Metals
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