

**DIAMOND (ARGYLE DIAMOND MINES JOINT VENTURE) AGREEMENT AMENDMENT BILL
2008**

Introduction and First Reading

Bill introduced, on motion by **Mr E.S. Ripper (Minister for State Development)**, and read a first time.

Explanatory memorandum presented by the minister.

Second Reading

MR E.S. RIPPER (Belmont — Minister for State Development) [12.15 pm]: I move —

That the bill be now read a second time.

Mr Speaker, the purpose of the Diamond (Argyle Diamond Mines Joint Venture) Agreement Amendment Bill 2008 is to ratify an agreement made on 21 May 2008 between the state, Argyle Diamond Mines Ltd and Rio Tinto Diamonds Ltd. Referred to as the variation agreement, it will provide for the variation of an agreement made on 17 November 1981, titled the Diamond (Argyle Diamond Mines Joint Venture) Agreement Act 1981 as varied; that is, the state agreement. This legislation is necessary in order to give effect to the variation of the state agreement set out in the variation agreement.

To put this legislation in context, I will provide some background on the diamond mining operations of Argyle Diamonds Ltd, known as Argyle, and the reasons for a variation of the state agreement. As most members of this house will know, the Argyle diamond mine is located approximately 110 kilometres south of Kununurra in the east Kimberley region of Western Australia. The mine is now owned and operated by Argyle, a wholly owned subsidiary of Rio Tinto Ltd, and is one of the world's leading sources of diamonds, producing around 30 million carats, or six tonnes, of diamonds per year. The majority of the diamonds produced are either near-gem quality or industrial quality. The mine is famous however for its unique pink and champagne-coloured gems, even though these comprise only a small minority of the total diamonds produced.

The Argyle Diamond Mines Joint Venture commenced mining the alluvial diamond deposits in 1982 and mining in the main ore body commenced in 1985. Since then, more than 650 million carats of diamonds have been produced. However, open-pit mining is nearing the end of its commercial life, with such mining scheduled to cease in 2008 and the processing of recovered ore to be completed by the end of 2009.

Argyle proposed a transition from open pit to an underground mining operation, with a view to extending mining of the ore body to at least 2017 and possibly through to 2024. The risk profile of the underground mine is greater than the pit operation however, and initial feasibility studies undertaken by Argyle indicated that the project economics would be marginal at best. As a consequence, Argyle sought financial assistance from the state to continue its mining operations under the state agreement by transitioning to an underground mining operation.

In late 2005 the government approved in principle an offer of financial assistance, being in summary to reduce the rate of royalty payable by Argyle under the state agreement on sorted rough diamonds and to amend Argyle's processing obligations under the state agreement. The detail of the proposed financial assistance, as subsequently negotiated and agreed between the state and Argyle, is contained in the variation agreement for which ratification is now being sought. Argyle's proposals to undertake underground mining operations were submitted in November 2005 and approved in January 2006 under the state agreement.

Stage 1 of underground mining is expected to commence in the last quarter of 2008 and ramp up to full production of about 17 million carats per year by around 2011, with mining continuing until around 2017. The development of stage 2 of the underground mine is expected to commence around 2013 and continue until around 2024.

Argyle's operations provide employment and local industry participation opportunities generally in the Kimberley region of Western Australia and provide real employment options for the region's Indigenous residents, who comprise the majority of the local population. Argyle is the largest single contributor to the Kimberley economy, with 25 per cent of its present full-time workforce being Indigenous people, of whom about half have been recruited locally. The company committed to achieve at least a 25 per cent Indigenous workforce by 2010, and it achieved this in 2007. It now has a target of 40 per cent Indigenous employment by 2010.

As mentioned previously, the variation agreement was entered into on 21 May 2008 between the state, Argyle and Rio Tinto Diamonds Ltd, known as RTDL. Argyle is the company currently comprising the joint venturers as defined in the state agreement. RTDL is also currently a wholly owned subsidiary of Rio Tinto Ltd, and it sorts and processes diamonds from Rio Tinto Ltd's diamond mines worldwide at its operations base in Antwerp. The variations proposed by the variation agreement include RTDL becoming a party to the state agreement. The financial assistance to be granted by the state to Argyle as proposed in the variation agreement, together with the

addition of RTDL as a party to the state agreement, are regarded as significant variations to the state agreement and, accordingly, require ratification by state Parliament in order to become effective. The variation agreement obliges the state to introduce a bill in state Parliament to ratify the variation agreement by 31 December 2008, or such later date as the parties may agree.

I will briefly outline the main provisions of the amendment bill now before the house.

Clause 4 of the amendment bill takes the opportunity to amend the definition of “the Agreement” in section 2, “Interpretation”, of the Diamond (Argyle Diamond Mines Joint Venture) Agreement Act 1981 as amended to make it clear that it includes all amendments made by the three variation agreements that have been negotiated since the original state agreement, as set out in schedule 2 of the act, was ratified.

Clause 5 of the amendment bill inserts in the act proposed section 3C, which will provide for the ratification of the current variation agreement. The variation agreement has been called the third supplementary agreement in this clause to maintain consistency with the terminology used in the two previous variation agreements; that is, the first supplementary agreement and the second supplementary agreement.

Clause 6 inserts in the act proposed schedule 5, which is the current variation agreement or third supplementary agreement.

I will now summarise the main variations contained in the variation agreement.

Clause 4(11) provides for a reduction in the annual royalty payable under the state agreement by Argyle on sorted rough diamonds produced under the state agreement to five per cent of free on board revenue, retrospectively effective from 1 January 2006 if underground mining operations commence by an agreed date, and will involve a cessation of the current 22.5 per cent of above-zero profit or 7.5 per cent of f.o.b. revenue royalty regime contained in clause 29(2) of the state agreement. Underground mining operations referred to as the “milestone event” are required to commence by 30 June 2009, or such later date as the state agreement minister may before then approve, in order for the reduction to take effect. This date, or approved later date, is called the milestone deadline. In the meantime, Argyle will remain liable to pay royalties at the rate currently applicable under the state agreement. The variation agreement recognises that in the 2006 calendar year, Argyle paid royalty at a rate of five per cent of the f.o.b. revenue, and provided a bank guarantee for possible additional royalty liability under the state agreement’s current provisions. Argyle’s five per cent f.o.b. revenue payment pre-empted the formal introduction of the new royalty regime but has been accepted by government on the basis of the provision of the bank guarantee. Argyle has paid full royalties since then in accordance with the state agreement. Upon the proposed variations becoming effective, and pending the reduction in royalty becoming effective—that is, the milestone event occurring by the milestone deadline—Argyle will revert to paying a five per cent of f.o.b. revenue royalty and providing a bank guarantee for possible additional royalty liability since 1 January 2006 under the state agreement’s current provisions. The bank guarantee already provided by Argyle will be replaced by the new bank guarantee covering possible additional royalty liability from 1 January 2006, and royalties paid by Argyle from the beginning of 2007 over and above the five per cent f.o.b. revenue rate will be refunded to it. In the event that the milestone event is achieved by the milestone deadline, the new royalty rate of five per cent of f.o.b. revenue will take effect from the commencement of the following calendar year, retrospectively from 1 January 2006, and the state will release all bank guarantees held by it. If the milestone event is not achieved by the milestone deadline, the current royalty provisions will continue to apply and Argyle must revert to paying full royalties. In addition, it will be required to pay all outstanding royalties owed since 1 January 2006. The state may enforce the bank guarantees held by it if the outstanding royalties are not paid.

Clause 4(2) and (3) provide for RTDL to become a party to the state agreement from the date the variation comes into effect. The subclauses also set out the basis on which Argyle may sell, transfer or dispose of to RTDL unsorted diamonds from the Argyle diamond mine for sorting and marketing by RTDL, as well as sorted diamonds for marketing by RTDL. RTDL’s marketing arrangements must first be approved by the state agreement minister, as is currently the case with Argyle under clause 6 of the state agreement. Argyle is proposing that it will sell to RTDL most of its diamond production, apart from pink diamonds to be cut and polished in Western Australia, for sorting and marketing by RTDL in Antwerp.

Clause 4(8) and (14) amend the royalty provisions of clause 29(1)(a) and (5) of the state agreement to accommodate the role of the RTDL in the sale of rough diamonds produced under the state agreement, while maintaining the liability of Argyle to pay royalties on all such diamonds. Royalty on the sale, transfer or disposal of sorted rough diamonds, whether by Argyle or RTDL, will continue to be paid by Argyle. The amendments provide for additional information to be provided on sales, transfers or disposals of sorted rough diamonds by RTDL.

Clause 4(17) amends Argyle's processing obligations under the state agreement. Argyle will remain responsible for the sorting, before sale, of all rough diamonds from the Argyle diamond mine, other than those to be sold to RTDL for sorting and marketing by that company. Argyle will also be required to undertake increased primary cleaning and sizing of its rough diamonds at the Argyle diamond mine and to continue to have cut and polished in Western Australia its high-colour, low-inclusion pink diamonds that have an expected polished weight greater than 0.25 carats. However, it will be released from any further processing obligations as currently set out in the state agreement. RTDL will be obliged to undertake the sorting, before sale, of all rough diamonds sold or transferred to it by Argyle for sorting and marketing by RTDL. Both Argyle and RTDL will be required to keep the state agreement minister and the Minister for Mines fully informed on their sorting arrangements and to ensure that such sorting is carried out in accordance with sorting and auditing procedures approved by the Minister for Mines. They must also ensure that the nature and extent of such sorting will be to a standard and level necessary to maximise the value of its diamonds before sale, transfer or disposal, as the case may be, as approved by the state agreement minister. Argyle and RTDL may, but will not be required to, undertake sorting in Western Australia. In anticipation of the proposed variations, Argyle has already located most of its sorting and valuing operations to Antwerp for RTDL to undertake the sorting and valuing of its rough diamonds formerly sorted in Western Australia. This is expected to be completed in the near future and continue.

Clause 4(12) amends the royalty offset provisions of clause 29(3) of the state agreement by suspending their operation while the five per cent of free on board revenue or bank guarantee arrangement applies, and by providing for them to cease to apply if underground mining operations commence by the agreed date, in which event the provisions for a permanent reduction in the royalty rate to five per cent of f.o.b. revenue will apply. Under the current provisions, in a year when Argyle pays only the minimum royalty of 7.5 per cent of f.o.b. revenue, a notional amount equal to the difference between that royalty and 22.5 per cent of the above-zero profit for that year is credited to an offset account. The provisions are intended to allow Argyle, in a year when it is liable to pay above-zero profit royalty, to use that offset amount to reduce its 7.5 per cent f.o.b. revenue royalty liability. The use of the offset amount to reduce royalties payable by Argyle is appropriate only when above-zero profit royalty is payable, and the variations address this point.

In summary, the variation agreement, if ratified by Parliament, will authorise the grant of financial assistance by the state to Argyle, as set out in the variation agreement, for the purpose of assisting it to undertake underground mining operations and, hence, to continue its operations under the state agreement. As stated earlier, the Argyle operations are a critical element of the continued economic wellbeing of the Kimberley region and are a source of real and meaningful employment opportunities for the region's Indigenous population. Argyle has achieved a 25 per cent Indigenous employment rate. It is now targeting an increase to 40 per cent Indigenous employment by 2010. If this can be achieved—indications to date point to its likely success—the Argyle diamond mine will become an outstanding example and beacon to encourage and inspire other employers in Western Australia to redouble their efforts in this most laudable endeavour to break the cycle of welfare dependency among the state's most disadvantaged citizens. Accordingly, I commend the bill to the house.

Debate adjourned, on motion by **Mr A.J. Simpson**.