

**ECONOMICS AND INDUSTRY
STANDING COMMITTEE**

INQUIRY INTO VANADIUM RESOURCES AT WINDIMURRA

**TRANSCRIPT OF EVIDENCE TAKEN
AT PERTH ON
WEDNESDAY, 22 SEPTEMBER 2004**

Members

**Mr A.D. McRae (Chairman)
Mr J.H.D. Day (Deputy Chairman)
Mr J.J.M. Bowler
Mr B.K. Masters
Mr M.P. Murray**

Committee met at 10.57 am**SMITH, MR RODERICK JAMES**

**Company Director,
Precious Metals Australia Ltd,
50 Bay View Terrace,
Claremont, examined:**

The CHAIRMAN: This committee is a proceeding of the Parliament and warrants the same respect as proceedings of the House demand. Even though witnesses are not required to give evidence on oath, any deliberate misleading of the committee may be regarded as a contempt of Parliament. I am led to believe that Mr Smith is the only person giving evidence this morning.

Did you complete the "Details of Witness" form and did you understand the notes attached to it?

Mr Smith: Yes.

The CHAIRMAN: Did you receive and read an "Information for Witnesses" briefing sheet regarding the giving of evidence before parliamentary committees?

Mr Smith: Yes.

The CHAIRMAN: I need to make a statement about parliamentary privilege and sub judice. The Western Australian Parliamentary Privileges Act 1891 provides absolute protection for witnesses appearing before a parliamentary committee, in so far as any information divulged to a committee is absolutely privileged and cannot be used outside the Parliament for any other purpose. However, this privilege does not currently extend beyond Western Australia. Therefore, while evidence provided to a Western Australian parliamentary committee cannot be used as evidence before any court in Western Australia, this protection does not automatically extend to other jurisdictions in Australia.

This matter is currently before the Australian Attorneys General and it is anticipated that future legislative changes will be effected to address this issue. Indeed, some Australian States have enacted legislative changes to extend their parliamentary privilege beyond the jurisdiction though the validity of these changes has not been thoroughly tested. However, to date this has not occurred in either Western Australia or New South Wales. I refer to those two States in particular because I am aware of actions that have commenced in New South Wales in relation to the Windimurra project. Given this, the committee is of the view that while a witness before a Western Australian parliamentary committee does enjoy absolute privilege in relation to the evidence within Western Australia, that privilege is not certain beyond this jurisdiction. That causes this committee to come to two views about the taking of evidence. The first is that we wish to provide privilege as far as our jurisdictional authority allows. We are cautious about moving into areas beyond that, where it would put either witnesses or this committee in some conflict with other courts in other jurisdictions. That is the first point we have discussed in the committee and we are mindful of it. The second point is that if it comes to the point that that may be of concern because of particular material or evidence you are presenting, I will probably put a circle around that and say that we should put it to one side for a moment. At some point during this morning's hearing, and if the circumstance unfolds, I may clear this room and the committee will decide whether it wants to move into a closed hearing. If we were to do that, we would then take evidence in a closed hearing and control the release of the information into the public domain. That is one of the mechanisms that we would use to protect you and the proceedings of the parliamentary committee.

Having said all that, the committee has received your submission. You provided further submissions to the committee during September. Is it that in particular that you wish to speak to today?

Mr Smith: Yes. I think the written submissions speak for themselves and I do not wish to introduce any new material. However, I want to make a brief address as a closing statement, bringing together a number of submissions that we have made in writing.

The CHAIRMAN: I think that is an appropriate thing to do.

Mr Smith: I will comment on the aspect of parliamentary privilege. I appreciate very much the chairman cautioning me and bringing that to my attention. Much has been made by Xstrata of the need for confidentiality. The fact is that in a detailed legal procedure there is no exemption for confidentiality. Everything has to be produced. If something is damaging to one's own case, it has to be produced to the other side. I think I am a lot less cautious about confidentiality than they may say they are. Ultimately, if it comes down to issues such as defamation, then truth is the ultimate defence. I intend to not hold back but I certainly intend to not embarrass the committee.

People from Xstrata have told the committee some amazing things. They have said its motive in closing Windimurra was nothing to do with a desire to manipulate the vanadium price. This is a key issue that is before the committee. While they tell the committee that, they tell investors, shareholders and lenders exactly the opposite. For example, they said last year that they reduced production of vanadium at Windimurra from 2001 because this was "not enough to facilitate market improvement so they closed it altogether". What could be clearer?

Did they tell the truth in this room or did they tell the truth in the 10 audited annual reports, interim reports, investor reports and letters quoted in our submissions? They said Windimurra could not reopen without spending \$50 million. We say that Xstrata has tried to baffle the committee with complex pseudo-scientific information, but the committee has only to look at what actually happened in 2002. In 2002, with all the detriments and warts they said existed, they produced 12 million pounds of vanadium at a cost of \$US1.48 per pound. If they merely did that again in 2004, they would have made \$US50 million profit.

Xstrata told the committee that they were the junior partner, that PMA alone negotiated government infrastructure support and that they did not know anything about the commitments that may have been reached with government. The Government's own records will show this is simply not true. Xstrata was the majority owner and the lead decision maker from the outset. They were never at any time a minority partner in this project. They are a party and a signatory to all the arrangements reached with government. Xstrata said that the current strength in the vanadium price was a peak and that it had already fallen 25 per cent. That is not true. The price has not fallen. Xstrata said that it would use an average for 2004 of \$US2.80 per pound. The year's actual average is \$5.44, and today it is \$5.75 a pound with all the signs that it is going higher.

When the committee sought to understand Xstrata's motives, Xstrata talked in circles about "rational behaviour". We heard that term repeated almost like a religious mantra. But they could not explain why they would close a profitable mine and rush to destroy a plant that had cost various parties over \$200 million. They could not explain why they would prefer to spend \$12 million to bury the plant instead of selling it for real money. Nor could they explain why they apparently concealed their intent from the Government, the community and PMA. There is an explanation, after all, of what Xstrata meant by "rational behaviour". It lies in the statements made by Mr Reid, a member of the executive committee of Xstrata, the details of which have been put before you in written submission.

Xstrata is pursuing a systematic, cold and ruthless course of consolidation leading to the ability to restrain production of a range of minerals and so to increase prices. Mr Reid proposes an outcome under which there would be total producer consolidation, systematic under-investment in a number

of key commodities and a shortage of new projects, thus squeezing supply. He looks for dominance by diversified companies such as Xstrata, limits on production capacity and barriers to new greenfields project. He then gives vanadium as an example in that treatise, whilst Mr Gonsalves comes before you and denies any such intent. Xstrata talked of an industry moving from the current land grab and multiple acquisitions - their words again - to a few powerhouses establishing the rules. Even Xstrata warns that the next stage after its maximising cash and protecting its position is inevitable government scrutiny; it even foresees that. In the case of Windimurra, Xstrata is implementing its own philosophy of economic rationalisation. They are maximising their cash by driving up the price of vanadium and other minerals, so inflating the price received by the other mines. They are protecting themselves by destroying the Windimurra assets in Western Australia and now they face government scrutiny.

The CHAIRMAN: Thank you for that. When you say that Xstrata was a party and signatory to all negotiations and agreements signed off with government, what do you mean by that? Can you elaborate?

Mr Smith: Indeed. The two principal agreements that we talked about in the last session are the power purchase agreement and the gas purchase agreement. Xstrata the subsidiary and Xstrata AG the parent are actually parties to those agreements. Those agreements could not be negotiated or entered into on their behalf without their knowledge. They were a party to it. Xstrata had a full-time executive in PMA's office, Frank Rothera, who went to the meetings and was involved in all these things. The draft agreements were approved by Xstrata. They were involved; they did not come into this picture after those arrangements were put in place.

The CHAIRMAN: Were you party to any discussions in Europe with Xstrata principals in the pre start-up discussions?

Mr Smith: Yes. When we first invited Glencore - as it was then - into the project I went to Zug. I made many trips during the period as we negotiated their involvement. It eventually culminated in a heads of agreement when they came in with us. We then negotiated the detailed joint venture agreement. If you are referring specifically to the negotiations with government or the transactions that arose, I do not recall any of that being negotiated or taking place in Zug - I think it all happened in Perth. It was certainly the case with e-mails and other correspondence. The documents were drafted by Freehill Hollingdale and Page, who were appointed by Western Power and AGL. The negotiations with them were with Tony Simpson, Frank Rothera and myself.

[11.10 am]

The CHAIRMAN: Tony Simpson was involved at the very earliest.

Mr Smith: At the absolute outset he was virtually the first man on the ground. He and Tom Heaton came out in 1996 or 1997 and helped run the process of the feasibility study. When Xstrata bought in, it bought 51 per cent of the project from the outset - that was the joint venture. We also established a management company called Vanadium Australia Pty Ltd, of which Xstrata owned 51 per cent. Tony Simpson was the managing director and I was the chairman. Xstrata had a majority of people. Frank Rothera was on it. The Xstrata subsidiary was the operator.

The CHAIRMAN: Are you aware that Tony Simpson now says that the whole assessment and design was flawed?

Mr Smith: Are you referring to the comment he made to this committee?

The CHAIRMAN: Yes.

Mr Smith: I am.

The CHAIRMAN: What do you have to say about that?

Mr Smith: I would love to address that. That was an outstanding statement. It shocked me in several ways. Mr Simpson appeared to attempt to take some of the blame for a fundamental flaw,

which may explain that the ultimate outcome of the project was its closure. He did that very bravely and unnecessarily, because he did not make a mistake of the type that he mentioned. The mistake was not made; there was no fundamental flaw. From memory - I am sure this is correct - he said that the metallurgical design of the plant relied on an assumption that a vertical slot would be cut from the ore body, taking equal proportions from the top 10 metres, the second 10 metres and so on, which was design A, B, C and D. However, when they came to dig a pit, the pit had a slopey wall and they did not get that blend. At that point, Mr Bowler I think said, "Do you mean you planned a square pit?" He said, "No, but we never reconciled the metallurgical side with the mining side, and that resulted in a fundamental flaw."

The CHAIRMAN: In the pit design?

Mr Smith: In the pit design. This is one copy of the feasibility study. There are two volumes of the executive summary. It is a very detailed document. I know that you know what feasibility studies are, but I wanted to make the point that the feasibility study was done by the world's largest engineer, Fluor Daniel. It was audited very extensively by independent engineers appointed by Xstrata, IMC from London, which had also audited its operations in South Africa. It had a huge level of expertise thrown at it. It cost millions of dollars. Banks scrutinised it; everybody scrutinised it. There was no chance that it could have made such a fundamental flaw as doing the metallurgical test work based on one set of parameters and building a mine on the other. Without dragging you through the detail of the thing, I can point out that the project had a JORG compliant 21-year ore reserve. One of the exciting things about the project was that it had a long proven life. To have a JORG reserve of ore, a pit design is needed. We had a 21-year mine design, which is unprecedented. The metallurgical test work in these volumes, which Simpson says was overlooked, refers extensively to the mine plan and vice versa. The whole thing was predicated on a desire to mix and match the different zones of ores. I will read a couple of paragraphs from the executive summary. At page 4-15 of the mining section it states -

Material from zones B and C combined would generally provide a suitable mill feed. The clay content in zone A is too high to be the sole feed material for the plant whilst the hardness of zone D would limit mill throughput, and hence require blending with softer material.

It goes on to refer to the mining method -

The efficiency of the process plant is significantly improved by the blending of these zones . . . Feed to the crusher will be a combination of blend from the high clay and hard material with low clay or softer material from the middle horizons of the pit.

. . . Premining is limited to that necessary to expose sufficient ore from zones 2 and 3 . . . ready for crusher operations on Day 1 of operations.

. . .

. . . Table 4.6 is a detailed plan showing monthly, quarterly or half-yearly figures for the first 5 years, . . .

Although each parcel of ore from each zone was scheduled for the first five, we never got to the first five years, as you know. I just happened to have this extract in my file because it was under cover of a letter, dated 14 December 1999, from me to Xstrata in South Africa, in which I talked about the mine plan. We proposed to mine 90 000 bank cubic metres ahead of treatment starting in order that we could disclose all the ore. I wrote to inform Xstrata that we were able to deal with the contract and that the contractor, at its own cost, would mine 270 000 BCMs of ore down to 28 metres. They were prepared to make that investment ahead and open up the ore body. It is a difficult ask for the committee to totally come to grips with detailed technical issues when one group is saying one thing and another group is saying another. It is hard to become an expert on magnetite treatment, even should you want to do so. I do not think it is necessary. I am not trying

to show the detail; I am trying to say that Mr Simpson was not right when he said that these issues were not considered and were not planned for. There was no omission in this study; there could not have been, due to the level of exertion and expertise that went into it.

Mr B.K. MASTERS: If there had been that omission that Mr Simpson has claimed, I presume that someone could have taken legal action against the producers of the feasibility study for such a basic oversight.

Mr Smith: I think that is a very good point. In fact, the nature of the agreement with the engineers included a process guarantee on only the front part of the plant, which was mining, crushing, grinding, magnetic separation and production through to magnetite. They guaranteed that process and they would have sued if there had been a major problem. Mr Payne has pointed out to me that, notwithstanding the agreement, if they were negligent, they would be sued.

Mr B.K. MASTERS: Yes, potentially liable.

Mr Smith: Yes.

Mr J.H.D. DAY: Do you think Xstrata might just have been cutting its losses? Although it might have thought there was some negligence, it might have come to the conclusion that it was not worth pursuing.

Mr Smith: No, I do not think so. We were involved in the contractual negotiations with the engineer well past our sale of the interest, because we maintained an obligation, a liability, to any outstanding contractual claims. We were aware of what was going on. However, there was not thought to be any flaw in the feasibility study. The issue of whether magnetite was recovered, how much could be recovered and what remedial work needed to be done comes down to what I think a member of the committee said; that is, there was the process of de-bottlenecking remediation work ongoing through the early life of the mine. Murrin Murrin is still going through it and after a long and tenacious effort is paying dividends, literally. There were a number of teething problems in different areas. The one teething problem that was not sorted out was optimising the magnetic separation. Mr Gonsalves said something I know to be true; that is, Mr Simpson put up a proposal for capital to do that. It was in 2001, when they had held back production. They did not want to spend another \$3.3 million to fix the problem. Ordinarily, if you are trying to maximise production and revenue, you would just make those changes. Those are not fundamental flaws; they were just optimisations that were yet to be carried out.

The CHAIRMAN: Progressive developmental changes.

Mr Smith: Indeed, yes.

Mr B.K. MASTERS: I confirm that that is normal in the mining industry. My experience is that it took the very first synthetic rutile plant that Westralian Sands put in down at Capel two years to reach 100 per cent capacity because of the tweaking and the small refinements it had to make along the way.

The CHAIRMAN: My experience in iron ore beneficiation suggests the same learning process as well.

Mr Smith: Indeed. This was a major, complex plant that had never before been built in Australia. We all knew that when we went into it.

Mr J.H.D. DAY: On that point, you said in your opening statement that Xstrata was trying to blind us with science in relation to a number of aspects, including the \$50 million cost of reopening the plant, which it estimated it would cost. If you do not think it would have cost \$50 million to get the mine going again, what would it have cost?

[11.20 am]

Mr Smith: I think when I gave evidence before I took the wrong tack in saying to you that I had been told that it would be \$16 million. I think you corrected me then and pointed out that it would be \$19.3 million because there were the magnetic beneficiation improvements on top of the \$16 million. That was the figure given to me by Tony Simpson. He also gave that figure to our chairman, the Earl of Warwick. I went around the plant. I am familiar with the plant. He showed me the individual items, the individual pieces, and the costs of remedying them. I am convinced it would have been \$16 million, but having said that I then realised that we do not even need to go there because, as I said in my opening statement, it did produce 12 million pounds. They can say that this or that was not optimal, but where were the failings? It did produce 12 million pounds in 2002. They cannot deny that; it is a fact. The other fact is that it cost \$1.48 per pound to produce it and the price is now \$5.50. If they just did nothing better, spent nothing on it, just opened it warts and all and said, "Gee, that is a shambles, isn't it? But, wow, it is making \$US50 million per annum."

Mr J.H.D. DAY: But what was the price then? You have just mentioned the price now, but what was the price when decisions were being made about whether it should be reopened or not?

The CHAIRMAN: In 2001.

Mr Smith: In 2001 it was very low, of course. They are not telling us when the decision was really made. They say the decision to close was made on 21 April 2004 at an executive committee meeting in Zug. I cannot remember the price on that day but I think it was over \$3 a pound. Certainly all the commentary was that it had been strong. It was profitable at that time. I do not believe a decision was made then because they had already sold the plant for a peppercorn and they had advised the power company back in March that it was closing. I do not know when the decision was made, but it has certainly been strengthening throughout 2004.

Mr J.H.D. DAY: That is with the benefit of hindsight, which is a wonderful thing.

Mr Smith: It is.

Mr J.H.D. DAY: Do you agree that maybe Xstrata might not have been sure about what the price was going to be. Therefore, judgments have to be made, and they might have made a judgment in good faith.

Mr Smith: I think that is a reasonable question. Thank you for giving me the chance to address it. These are the people who hold themselves out to be the world experts. Glencore is the largest trader in physical commodities in the world. If they do not have the best market intelligence available, they are really not doing their job and giving the project the best chance. They studied it very carefully. I think they have a good idea what the market is doing. I do not think the market has surprised anyone. All the commentary by Metal Bulletin throughout the year has talked of shortages, impending shortages, great growth from China. I read just yesterday that in the United States demand grew 15 per cent in 2003 over 2002. World demand was growing even without the China factor. If you have a mine that is profitable even at those prices, why not keep it on care and maintenance for another year? What does it cost to have half a dozen guys up there greasing the wheels? They did not do that. They actually concealed the fact and rapidly went about a proactive destruction.

The CHAIRMAN: What do you say to the proposition that comes from the submission made by Xstrata if you could put all the picture together? The motive falls into three areas. We talked about the ore body. They say that the characteristics and the mineral content of the ore body gave them problems. They also said that processing gave them problems. The third element was the market volatility. We put those three elements of this project together - the ore body, the processing and the marketing. We keep coming back to those three and trying to understand how they interact with each other and give you the sum.

Mr Smith: Yes. That is useful. The ore body has not changed since the feasibility study was written. It was based on very extensive test work by equipment suppliers and magnetic separators, and Xstrata had many years of experience in treating magnetite in South Africa. The ore body did not deliver any surprises. Sometimes you read about ore bodies not coming up to scratch, but this one was thoroughly delineated. Hardly an ore body in the world has been developed with a 21-year proven life. That reflects the enormous amount of drilling, geo-technical test work and magnetic separation test work that had been done. The ore body did not surprise anyone. If there were shortcomings in the plant, they could be remedied. It is only ever a matter of cost with plant.

The CHAIRMAN: Just before you go off the ore body, the two critical things we hear about in terms of the Windimurra ore body is the softness of the rock being pulled out of the ground.

Mr Smith: Yes.

The CHAIRMAN: Which has an implication for processing.

Mr Smith: Yes.

The CHAIRMAN: Then we have the variants in the different zones of the ore inside the total body of the ore being extracted. You are saying that those things were well known and there were no surprises.

Mr Smith: The softness of the ore body - there was no surprise, but I should explain one area. One of the outstanding advantages of this ore body is its width, the fact that it outcrops at the surface. There was a zero ore waste ratio. The pit advanced at only one metre per month. It was a very, very simple open cut. There was no high waste ratio, no pre-stripping or anything required. The softness of it allowed free digging. It was a joy to see it operate. I seriously wish you could have seen it. A bulldozer sat at the top of the slope and pushed material to the bottom, where the front end loader picked it up and took it to the plant. You could not have a simpler ore body. The softness gave those advantages. It also meant that it was very soft to grind. I remember at the time all the test work was done that there was evidence that it would not take much energy to grind it. However, the engineers were very conservative and they made us put in an extremely large mill - 5.6 megawatts - which I think was the equal biggest ore mill in Australia. It only ever drew about half of that, 2.8 megawatts, because the ore was on the softer end of the scale. There was no surprise; it was not different. It was certainly at the softer end of the scale. That has some implications in the treatment, which would have been addressed in that \$3.3 million project. All it meant was that they were overgrinding it. It was a surplus of riches. It was overgrinding the material and a lot of the magnetite was getting ground to a very fine particle size and it was being washed out into the tailings dam.

The CHAIRMAN: Overgrinding and running a power station are very poor efficiencies.

Mr Smith: And it was not putting enough load on the power station. That is right. That made a good power station with over-capacity. One reaction to all of this was to increase production. We always planned to double the production. There was so much excess capacity. That would have been a better result than closing it. They may have said something about overgrinding. Because of the way the material is classified, it was classified using hydrocyclones, which are used in gold ore and in the iron ore business, where the weight of the particle determines when it is removed from the circuit and is no longer subjected to further grinding. That was not so efficient in this process, because the particles weigh a lot because they are a dense magnetite, not because they are larger than the host material. It was found that hydrocyclones were not the ideal system for classifying the material. The fix for that was to use screens, which was the alternative method used in many gold mines - DSM wedgewire screens. They trialled that and set one up. Tony showed it to me with great pride. It was very effective and it fixed that problem, but he was not given the capital to implement it. That is the only aspect you could point out from the ore body. There were no other surprises in the ore body at all.

[11.30 am]

The CHAIRMAN: Given those three areas of what Xstrata argued in its evidence were cause for concern - that is, ore body processing, marketing and the interaction and combination of all those things - fast forward to the point at which they make that decision some time between putting it into care and maintenance and the public announcement: how long would it have taken you to get someone interested in the open market place to take on that project?

Mr Smith: I do not think it would have taken very long at all. In 2004 we were having a minerals boom. I do not have the statistics for 2003, but in that year many companies were raising \$5 million and \$10 million just to go exploring. A couple of companies approached me informally, each of which have around \$100 million in the bank. They were desperately looking for new projects. It is quite hard to find a new project at any time. I believe it would have been snapped up very quickly.

I mention in the document here that Xstrata made the rather unusual -

The CHAIRMAN: Has Xstrata got that full capital value?

Mr Smith: Would it have sold for \$180 million? I think that would have been difficult. I cannot say that that would have been easy.

The CHAIRMAN: I suspect you are right. How can you reconcile our guess that you would not have got the full capital value of the project in the open market with Xstrata's not unreasonable desire not to give someone a subsidised entry into the market? There has been a lot of debate on that, but how do you reconcile it?

Mr Smith: It is a good point, thank you. Xstrata gave evidence very stridently and I think you asked people from Xstrata to repeat their comments on the fact that if Windimurra were to reopen, it would not depress the price of vanadium. Xstrata does not have any other vanadium operations in Australia. It has one in South Africa. If it could sell Windimurra for \$50 million or \$20 million and the new owner could produce vanadium without adversely affecting the market price, what would be wrong with that? It would have \$20 million or \$50 million in the bank and it would not have spent \$12 million destroying it and it would not have alienated the community and a Government.

The CHAIRMAN: Do you think Xstrata's assertion was right; namely, that it would not have affected the market price?

Mr Smith: No, I do not. I think it would have affected the market price. It would not have driven it back to where it was, but it would have pulled some of the shortage out of the market; there would have been a contraction in the price, but to a level that would remain very profitable. There has been an increase in demand equal or greater to the amount of supply from the mine.

Mr J.H.D. DAY: Xstrata made the point that it would have been prepared to sell the mine for - I cannot remember the terminology - but something like a "realistic" price. It was certainly not interested in giving a potential competitor a free ride or discount or cost of entry into the industry. Is that an unreasonable approach for a company to take? Probably most companies would take that approach, would they not?

Mr Smith: Xstrata did not even do that. It did not make it available for sale and find that that amount could not be raised. It did not test it. Remember, we raised \$120 million.

Mr J.H.D. DAY: On that point, as you will have heard, Xstrata argued that the fact that this mine was not operating and that it was effectively available would have been well known in the mining industry, which is a pretty small community given the sort of companies that might be able to buy an operation like this.

Mr Smith: Yes, it did say that, but it gave no signal that it was available. I have not put it in my written submission, but I know that in 2003 another company approached it - Thai-Gypsum. I know that specific company and I do not know what others there may have been. However, Pete

Nienaber sent an e-mail to Tony Simpson saying that Xstrata would not sell the mine for less than \$200 million, and there were no further discussions from that point. Xstrata claimed that the Australian market had already been tested. It said that that was because whenever PMA tried to raise money it could not do so. That is disingenuous for two reasons: firstly, it is simply not true; we did raise a great deal of money on the strength of the Windimurra project - \$45 million in equity and a total of \$120 million, including farm-out and mines. That was four years ago. When we sold out to Xstrata, the price was \$1.30 and today it is \$5.50. For Xstrata to say that there was no point in its advertising that project for sale because PMA had already proved that it could not raise money was ridiculous. There is a whole industry out there. Many people would like to have a go. Xstrata did not want to sell it even for what it cost. I do not think it is reasonable and fair, given there are other stakeholders. They can sit there in Zug and be clinical and selfish, but PMA has a \$30 million investment in that project; the Government has a \$30 million or greater investment; Mt Magnet Shire Council spent something like its entire annual budget on a road for them; and Australian Pipeline Trust put \$30 million in. A lot of stakeholders were not even consulted.

The CHAIRMAN: One of your submissions included a range of options for statutory reform by Mr Michael Hunt. Some of that referred to making provision for the response of the state minister - a couple of options were provided - in some way intervening and causing in the future the value of a project like Windimurra to be tested on the open market place and making that a condition of the granting of a licence and so on. How long do you think you would have needed to see the market come to a view about the value of the bid for the Windimurra project?

Mr Smith: A proper process would have been to engage someone to put together an information memorandum on the project, to invite all comers to make submissions, to sort them and to conduct site inspections, to open the records to scrutiny and go through a tender process. That is the way a professional company would have done it. That could have been done in, say, 90 days.

The CHAIRMAN: In three months?

Mr Smith: Yes.

Mr B.K. MASTERS: I want to explore a couple of issues relating to Xstrata's ability to significantly profit from much higher prices for vanadium pentoxide. I understand that most vanadium goes into steel making, is that correct?

Mr Smith: Yes.

Mr B.K. MASTERS: In general terms, what percentage of vanadium is in those sorts of specialty steels?

Mr Smith: About 80 per cent of it is converted to ferro-vanadium and then used in high-strength low-alloy steel. About 10 per cent goes into tool steels, such as Sidchrome spanners and screwdrivers and things and the rest goes into the more exotic markets of aerospace with the titanium alloys.

Mr B.K. MASTERS: What is the vanadium content in those steels?

Mr Smith: It is very low, which is one reason demand is pricing elastic. High-strength low-alloy steel has about one per cent vanadium. The ultimate buyer of a ship that contains vanadium steel would not know what the vanadium price is to him.

Mr B.K. MASTERS: Do you have a rough idea of the cost of a tonne of that steel to buy now ex a steel mill before fabrication.

Mr Smith: I do not know, I am sorry.

Mr B.K. MASTERS: I guess I am trying to convince myself that, as you just said, the dollar value of vanadium in one of those specialty steels is so small that even if the price of vanadium pentoxide doubled or tripled, it would make no real difference to the buyer of that steel product at the end of the day.

Mr Smith: I worked out at one time that a \$20 adjustable spanner had about 2c worth of vanadium in it, so if it had 3c or 4c, it would not really impact. A jumbo jet costs, I believe, \$US150 million and contained at one time \$US50 000 worth of vanadium, so that gives you an order of magnitude anyway.

Mr B.K. MASTERS: Can I explore an issue that the Chairman touched on. I think you have already supplied the information. It relates to the ore reserve statement for the Windimurra deposit. Prior to the commencement of mining, what was the ore reserve statement on tonnes of ore and the average vanadium pentoxide volume?

[11.40 am]

Mr Smith: From memory, it was 106 million tonnes at 0.57 per cent.

Mr B.K. MASTERS: The plant was designed to accommodate and treat 0.57 per cent V₂O₅ or was there a little bit of high grading at the beginning of the project?

Mr Smith: Yes, there was a small measure of high grading in the first 10 years.

Mr B.K. MASTERS: That was to produce ore at what average grade?

Mr Smith: I really do not recall the grading.

Mr B.K. MASTERS: It would not have been a doubling.

Mr Smith: No, it was quite immaterial. Because of the process, whatever is put through the grinding and beneficiation produces magnetite of a consistent grade, so it does not matter what grade of ore is put through it.

The CHAIRMAN: We have had a number of discussions about what conclusion this inquiry might come to. I have expressed my personal view as the Chair that I am concerned that there was no opportunity for the market to be tested. Do you have a view of the way in which somebody else coming in and operating Windimurra should have occurred, given that you had already taken advice from the people there? Do you have a preferred sense of how the market might have been tested in the case of Windimurra or a similar project in which an operator was going to close and effectively disbar anybody else from entering into that project?

Mr Smith: Okay. If I may start answering that by finishing the previous question put to me, one of the members asked, "Is it not unreasonable for a company to say it does not want to assist a competitor or anyone else to go into business? 'Why should we not just take our marbles and run?'" I mentioned, partly in answer to that, that there are other stakeholders in this. The very fundamental one, the absolutely overriding, inescapable fundamental one, is that it is not their vanadium; it is yours, it is the community's, it is the Government's -

The CHAIRMAN: The people of Western Australia.

Mr Smith: Yes, and I know that you understand this. I will not labour it too much, but we do have this wonderful system in which our community owns our resources. Other communities do not have that advantage. South Africa and America do not. People are given a monopoly right to exploit resources, and the only form of payment for that under current legislation is the royalty. It is not a tax; it is payment on terms for that deposit. It is quite likely that needs and aspirations of a multinational company run from elsewhere will be at odds with what is best for the Western Australian community. Why should that not be so? We have a need to run hospitals and schools, but the companies have a need to make profits for shareholders. There must be a balance where each gets a reasonable return, otherwise the system will not work.

A first provision, which must be there to ensure the right outcome, is information. As the legislation stands - this is an oversimplification perhaps - the only role the Government has, once Windimurra opens, is that it must put in a royalty statement once a year and calculate the royalty payment pursuant to the regulations. Then the mines inspectorate goes up there occasionally and

does an extremely good job looking after safety in the pit design and things like that, but there is no other need for feedback. Under the environmental provisions, I think that people have to lodge a closure plan if they close a mine, but all that talks about is what they will do with the wastes and things; it does not talk about the social impact, ownership or anything like that.

The Earl of Warwick has asked me to raise with you a point that is perfectly relevant here. He suggests the point should be made that if the State negotiates stricter covenants, they would not be worth a cracker unless, and only unless, they were attached to the title, as opposed to a corporate entity. In the global economy, where transnationals trade companies and major assets as a matter of course, who do you pin the covenants on? However, he said that having read Mr Hunt's submission he thinks that a broad area of application has been addressed in the European Union; that is, the European Economic Community Maastricht Treaty 1992, in particular the social chapter as regards the rights of stakeholders to be consulted in advance of any factory closure or redundancy. While the Maastricht treaty does not provide remedial measures, it does address a fundamental issue. In a global economy, should communities be kept in the dark about decisions that vitally affect them? Whatever powers a Government grants itself, whatever covenants it insists upon, they are worthless if the Government does not have a clue about what is going on. In this case Xstrata looked at the documentation and concluded it had no reason or need to tell anybody, and it did not do so, so no parties had a chance to react and to put alternative views. I think the outcome might have been different had that happened. It might even have benefited Xstrata. They said to you in the committee, "We were amazed at the reaction by the other stakeholders. We had no idea when we closed it that people would react so strongly." The great thing about being forced to tell people what you are doing is that you flush out those concerns and you give an opportunity to come up with alternatives. We did not put it in our submission, but I now put to you that a reporting mechanism is the very least. There must be consultation between all stakeholders before the closure of a mine, as there is now for the opening of a mine.

The mechanism that Michael spelt out, he has been at pains to make fit very simply within the existing Mining Act rather than try to create whole new legislation. There is a system whereby covenants are placed on mining leases. Those covenants include a wide range of things: complying with the Aboriginal Heritage Act, complying with the Environmental Protection Act, and things like that. It could so easily have other measures controlling the giving of information and obligations to either commence operating a mine or to not cease it without permission. In Queensland and New South Wales, people need to get the permission of a minister before they close a mine, so there is some opportunity for someone to investigate and make conclusions.

We propose a mechanism whereby if someone is not exploiting an economic deposit, he can be plaited through the forfeiture provision. People would need to make a case in front of a warden, so it would be an open court. The other side would have a chance to put its economic proof forward. The warden could make a recommendation to the minister. It would then still be open to the minister to forfeit the tenement, do nothing or impose a fine. Any mechanism needs those failsafes, and it needs ultimately a minister to be able to make a call as to public interest.

The CHAIRMAN: I think I agree with you.

Mr Smith: You will see raised the bogey of sovereign risk, which is absolutely not applicable.

The CHAIRMAN: The sovereign risk argument does not exist if that is known as a condition, surely.

Mr Smith: Indeed.

The CHAIRMAN: Risk is about things that people do not know about or things that they think might be beyond their control.

Mr Smith: Yes, that is true.

The CHAIRMAN: The requirement for information flow is not an unknown risk. It is just an obligation of responsibility.

Mr J.H.D. DAY: Unless a potential investor thinks it more likely that a Government might intervene in a way that produces difficulties for the company.

The CHAIRMAN: I accept that, but that is not suggested in the scheme that the witness has just described.

Mr Smith: Part of it is.

The CHAIRMAN: There is no unilateral intervention.

Mr Smith: In our proposal we do suggest that if a company wishes to close a mine, and it cannot convince the Warden's Court and later the minister that it is uneconomic, there will be provision for forfeiture.

The CHAIRMAN: That is not unilateral intervention power; that is a conditional power.

[11.50 am]

Mr Smith: I know; I am agreeing with you. Sovereign risk is about changing the rules after the event, is it not? I do not think this provision as proposed would be any concern at all because - I think I said this at the last meeting - if a company was in the position, as Xstrata was in 1997, of deciding whether to invest in a project, and if at that point, before it had turned a sod of earth or spent a dollar, it was concerned that in the event it was successful and profitable it might have to keep going, that would be a very unusual concern to raise at that time. If it was to be a concern, tell us - tell your joint venture partners now and tell the Government. The Government would not put a pipeline in and PMA would not do the joint venture with it. That provision would merely flush out a mal-intent, and I do not think it would ever happen actually, because I do not think companies would go into mines with the intention of closing them.

Mr J.H.D. DAY: You say it works quite okay in New South Wales.

Mr Smith: Yes. I think Mr Gonsalves told you that he was not aware that Xstrata has such a provision. It has just spent - what was it? - \$5 billion buying assets there. It was of such concern to Xstrata that the executive committee did not even know.

Mr J.H.D. DAY: It has bought assets in Queensland, has it not?

Mr Smith: I think it includes the coalmines in New South Wales as well, and they both have that provision. It was not even on the radar screen for it; yet if we had that when Mr Brown got the phone call, he would not have had to say, "Oh my God, I've got no levers at all. There's nothing I can do." He would have at least been able to negotiate an outcome that was more in line with the interests of the State.

The CHAIRMAN: Xstrata would not have had the capacity to just decommission without notice or without testing the market. That is the critical point that you are making.

Mr Smith: Yes, it is. I think you are right. You have mentioned that a couple of times. I think that is the crux of it, because if at the end of the day nobody else wanted to operate the mine either, some mines are not worth operating.

The CHAIRMAN: We are running a bit short on time now, because the Chamber commences in about eight minutes. However, I just wanted to ask whether you thought Xstrata maybe went into the project seeing it as an entry into Australia, without it really being its objective, and then after its other opportunities in Australia opened up, it thought that it did not really need Windimurra.

Mr Smith: I do not think so, because at the time it did this it was a much smaller company, and vanadium was one of its three key commodities. It was big in chrome and it was big in vanadium, and wanted to be predominant in vanadium. That was its strategy. We interested Xstrata in

Australia. It had not invested here before. We did a tremendous sales pitch on Australia, and I think that worked out. However, there were other ways of testing the market here. I do not think that was its motive.

The CHAIRMAN: Mr Smith, you have a couple of minutes to say whatever you like in summary, because I think we have tested all the things that we needed to do today.

Mr Smith: Mr Payne has reminded me that when we and Xstrata set about doing an economic assessment into the justification of spending \$121 million to build Windimurra, we generated this document and spent many millions of dollars. We did a lot of independent test work. A lot of work was brought to bear in making a decision of that magnitude. Xstrata says that it had no intention of constricting supply and driving up the vanadium price. In saying that, it had to have an alternative motive, and it says that its only motive - it repeats it and makes it very clear - was that it would do a detailed economic analysis of Windimurra. It studied in detail the prospect of spending \$50 million, and, as a result of that, it reached the clear conclusion that it had to write off a \$180 million investment, and everybody else's investment, and close the operation. For the purpose of *Hansard*, the study is about 10 volumes and weighs about 100 kilos. That is the economic study on the way in. Where is the economic study on the way out? I would expect to see a very detailed study before such a decision was made, if it was in economic terms. I am at a disadvantage. I do not know all the records it has or what it has given the committee. However, in evidence it referred to a couple of reports that had been written after the event in order to justify the decision: a report by Tom Heaton, and I mentioned that it had written a paper on magnetite recovery, which it has given to the committee. I would be very suspicious of anything written after the event to justify the decision. The only things that really count would be the minute of the meeting of the executive committee on 21 April 2004, which must set out the reasons, and a detailed economic assessment prepared prior to that date.

I think I am done. I thank you very much, gentlemen. I think that the process of a parliamentary inquiry is really the only way to get to the bottom of this sort of thing. It is well conceived. I have enjoyed imposing on you. I look forward to the outcome. Perhaps I will leave you with the thought that in going through what Mr Reid says are Xstrata's objectives in controlling world mineral prices etc, he gave very clear presentations to investors overseas about the way Xstrata wants to model the future. In the document - I have the full copy here - there was only one graph of any particular mineral, and that was vanadium. For Xstrata to follow through that plan in Western Australia with this vanadium mine and then deny it is quite incredible.

The CHAIRMAN: I will finish with a brief commentary on an article that appeared in, I think, the *Business Review Weekly* and was headed "Mine Games". The economics writer observed the different plays between all the parties involved in the Windimurra mine. However, one of the questions posed was: how does a provincial Government, with absolute control over and interest in mineral rights, protect itself from a globalised marketplace? You have just touched on that in drawing attention to that plan. Do you have any comments on that?

Mr Smith: I do. This is getting to a very wide issue. However, this will not be the only inquiry on this topic, and this will not be the only State of the only country considering it. We are seeing, undeniably, a trend whereby, for the first time in world history, five board rooms control the world's mining industry completely, and the consolidation is ongoing. I am not taking a moralistic point of view about that at all, but it does have implications for those communities that wish to exploit their resources in ways that suit them, not in ways that suit international mining companies.

The CHAIRMAN: Absolutely.

Mr Smith: If it keeps going in this way, as I think it will, it will lead to severe sanctions at the end of the day. The EU and the United States of America have taken very strong stands on oligopolistic or monopolistic situations before. That never applied to minerals; it applied to telecommunications

and other things. However, I think we will see increasing action here. It was just unlucky for us that we are sort of down here at the pointy end of things at the moment.

The CHAIRMAN: Mr Smith, thank you very much indeed for your time. We appreciate very much the quite extraordinary effort you and your company have made to present a significant body of material for us to use in this inquiry.

Mr Smith: Thank you very much.

Committee adjourned at 11.58 am