Submission to the WA Legislative Council Standing Committee on Legislation re:

Pilbara Ports Assets (Disposal) Bill 2015

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Summary

Atlas Iron Limited ("Atlas") was founded in 2004 and commenced iron ore exports from the Pilbara in the second half of CY 2008. Since that time we have exported in excess of 50 million tonnes of iron ore to our Asian customers, earning export sales revenues for Australia of $4.2B up to 31 December 2015.

These sales have enabled the company to maintain significant employment (currently ~600 people working directly on Atlas projects), pay $270M in royalties (including $251M to the State Government and $19M to Traditional Owners), $307M to Pilbara Port Authority (including pre-payments) in port charges and spend $3.8B in Western Australia on operating, exploration and capital expenditure.

It's our considered view that the current Utah Point port sale process is flawed in that it delivers an infrastructure access regime that provides a high degree of uncertainty around its access and pricing, undermining the ability of the current users to maintain and grow their businesses and in doing so provides further competitive advantage to the global mining houses that already dominate the Pilbara.

It's also our view that the historical management of Utah has levied unreasonable charges and levies on users which have generated supersized returns for the Government. This should be remedied for the long term and done so in a way which is fair to all port users.

The junior bulk commodity exporters operating in the Pilbara make a significant direct and indirect contribution to Western Australia. The unintended consequence of achieving a cash windfall of a few hundred million dollars in a once off payment through the Utah sale process could jeopardise the significant long term benefits for the State derived from ongoing production from smaller miners.

Our concerns fall into the broad baskets of access and cost, to address these concerns we request the following three key terms be included in the sale terms and conditions;

a) Utah Point must remain exclusively reserved for junior miners with no ability for the Operator to grant access to non-juniors,

b) The existing Utah users must have input on the Sale terms and conditions as well as the regulations that will apply to the operator post privatisation to protect against unaffordable increases in (or introduction of new) port charges. Amongst other things we would expect this to include an appropriate oversight body and a defined appeal process. We would expect this to ensure the base rate is not varied to prejudice port users.

c) The current $2.50 per tonne Cost Relief Package on Stock Yard 1 tonnage and $1.73 per tonne on Yard 2 (which applied from December 2015) is due to expire 30 June 2016 and must become a permanent component of the Utah Point pricing structure for all users and form part of the Sale terms and conditions to be adhered to by the operator post privatisation of Utah Point.

This paper should be read in conjunction with the paper supplied by Association of Mining and Exploration Companies (AMEC) of which Atlas is a member.

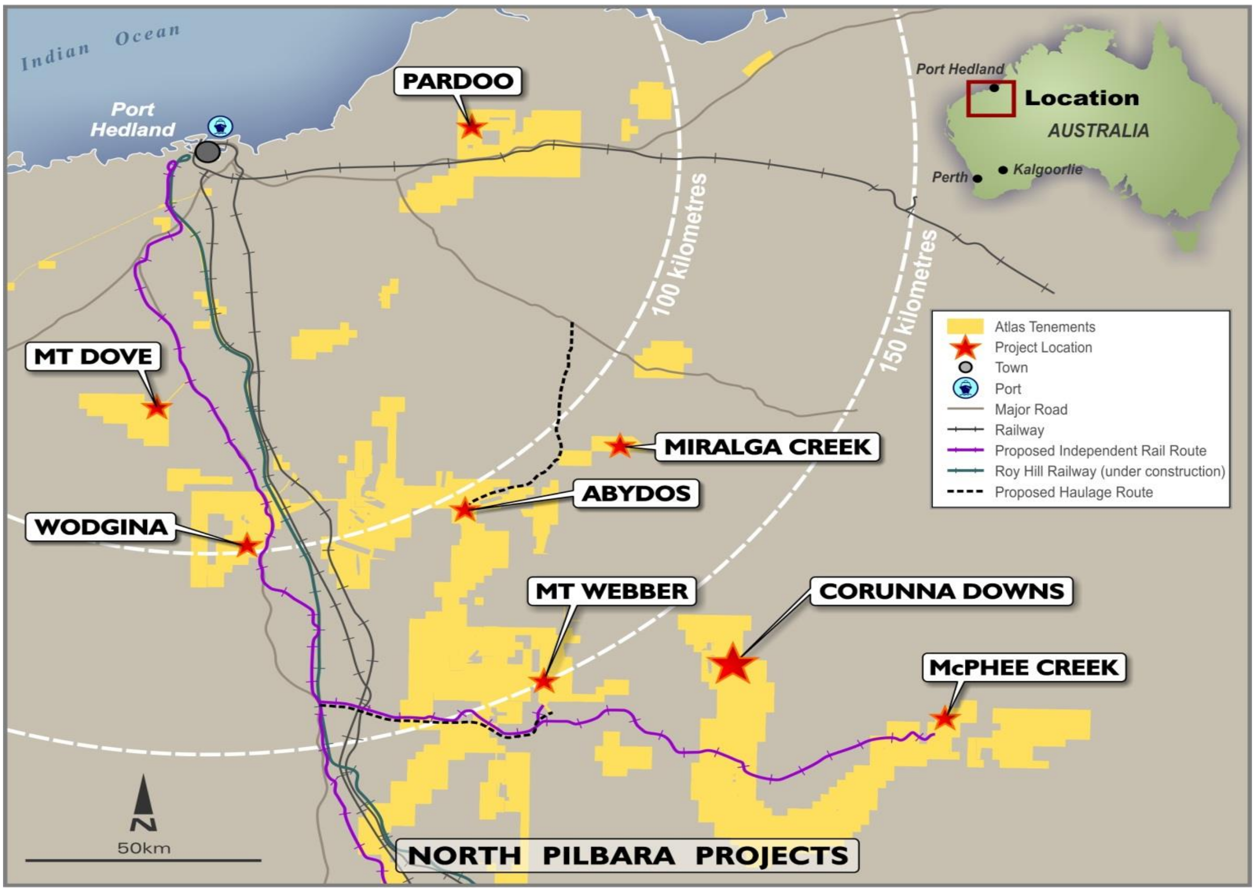
Background

Atlas was founded and listed on the ASX in December 2004. Atlas initially explored the Pilbara for a number of commodities including manganese, gold, nickel, copper, uranium, chromite, zinc, lead and iron ore. The company recognised early in its first year that a number of iron ore prospects in close proximity to Port Hedland had strong potential for development. Subsequently we changed our name to Atlas Iron from Atlas Gold and became exclusively focused on iron ore project development. The Majors had previously held most of this ground and considered it of insignificant iron ore potential because of the relatively small deposit size and relatively low iron ore quality. The first project we developed was Pardoo, located 75 kilometres east of Port Hedland. Initial mine life was less than 3 years and the first deposit we started mining was called Connie and was less than 400,000 tonnes of iron ore grading 56-57% Fe.

The majors are currently collectively exporting in the order of 2 million tonnes per day from large scale mine developments so it is clear should they own all our deposits, they would remain undeveloped. In the absence of a junior iron ore developer the assets we mine would remain stranded and undeveloped for the benefit of Western Australia and the local regional communities. They do not match the size or quality of those owned by the Majors. These deposits do not attract the same headline iron ore price on a per tonne basis. All our ores are sold at a significant discount.

The provision of Utah for the use of junior mining companies is essential for the development of all small (<200Mt) iron ore deposits located within trucking distance of the port of Port Hedland. We would not have been able to access funding to develop any of our deposits without the clear line of sight to port capacity at Utah.

In 9 years Atlas has commissioned 5 new mines; Pardoo, Mt Dove, Wodgina, Mt Webber and Abydos, all of which have exported iron ore through Utah Point. We continue to mine at 3 of these and currently export at a rate of 14–15 million tonnes per annum (Mtpa). On a revenue basis we are a top 10 Western Australian based company. Atlas is the single biggest user of Utah providing some two thirds of total throughput.



Through the development of our projects we have achieved significant innovation in many areas that have further demonstrated commercial opportunity to Atlas and other potential entrants to the sector. They include;

1. Modified infrastructure at the Wodgina mine to produce tantalum and process iron ore simultaneously, delivering a feasible project,

2. ABS and GPS Technology deployed on our road trains increases their safe application through driver management, reduced road footprint and in minimising impact on other traffic.

3. We have introduced new iron ore products to the market which are now accepted by steel mills in South Korea, China, India and Japan. Providing evidence and sales precedence for the benefit of other existing and new junior iron ore mining companies.

4. Achieved significant cost reductions through a unique contractor collaboration agreement. In exchange for significantly lower operating costs the contractors get access to a form of profit share and cost clawback when prices recover. This is now being explored by many other companies.

Atlas relies heavily on contractors to provide mining, processing and haulage services. We also rely on the use of a multi user port and third parties to provide stevedoring and freight. We do not typically use contractors that have a heavy presence working with the major mining companies. We use smaller, more nimble contractors with experience in the scale of operations where we operate. These are either privately owned family businesses or smaller public listed or public unlisted companies.

We have found these contractors to be largely very supportive of ongoing innovation around technology applied to productivity, safety and commercial relationships.

Atlas has recently completed pre-feasibility studies on the Corunna project which at current iron ore prices and current operating costs presents a significant opportunity for the company. Following behind the Corunna project (~4Mtpa targeted production rate), is the McPhee Creek Project (5-10Mtpa targeted production rate) which provides further development potential. Each of these projects is well defined and the company expects to be able to develop them in a way to sustain an export rate in the order of 15Mtpa for in excess of 10 years.

Key requirements for a successful Utah Point model moving forward

As noted above Atlas considers there are three key requirements to ensure that Utah Point remains a viable means of export for the smaller producers, those being:

1) Non-Juniors excluded from Utah

As part of the funding model for the development of Utah, Atlas made $23M of pre-payments, which the Port Hedland Port Authority used to part fund the Utah port construction. This funding was ultimately returned to Atlas in the form of crediting as pre-paid port charges. Atlas also funded a further $14M of pre-payments on behalf of one of the other junior proponents, Aurox Resources Ltd, and took over its port allocation when its project did not prove viable, hence saving Pilbara Ports from having an underutilised facility. We also point out this was done in an environment of the port increasing its charges at a rate well beyond inflationary levels.

As a result of significant delays and budget over runs toward the end of the project construction, Atlas also contributed staff, accommodation and engineering support as well as $9M in further Utah funding for no recourse. This funding was not returned to Atlas as a port charge discount or a pre-payment credit.

In order to increase our throughput through the Port Atlas also invested a further $73M into infrastructure located in Utah Yard 2. This has not and will not be returned to Atlas by way of pre-paid port charges.

Utah is a unique facility currently designed to accept bulk commodities exclusively via road train haulage, a mode of transport not utilised by major producers who have extensive rail networks. The company has invested many hundreds of millions of dollars on a business model that relies on cost effective access to Utah.

Atlas does not have access to an alternative port facility.

It is unreasonable that by oversupplying global iron ore markets and forcing down prices, that the majors could then be rewarded with the direct benefit of our investment in port infrastructure by using it to further ship ore.

Purchasers of Utah are likely to find major producers as attractive customers due to their financial strength and in an unregulated market a Utah purchaser would likely gravitate to providing services to major miners at the junior's expense. Historical difficulties in enforcing the third party rail service obligations of the major producers are indicative of the challenges faced for juniors in achieving continued access to Utah Point if majors are in there; it is therefore the simplest solution to prohibit their utilisation of the facility as part of the current privatisation process.

2) Permanent Reduction in Costs

It is our view that the Pilbara is highly prospective for deposits suitable to junior mining companies. In the event that those deposits are not warehoused by the majors and there is a reasonable access regime at a reasonable price, new mines will be developed and Utah should be able to deliver a significant dividend for generations.

A key to ensuring this is possible is that port charges do not provide an overwhelming impediment to doing so. Port access and ship-loading charges for Atlas prior to the Government and stevedoring contractor providing temporary rate relief totalled in excess of $10 per tonne, which is some 300% above the port costs per tonne payable by major producers. While this differential in part results from the historical capital investment in port infrastructure made by the majors it also reflects the hyper-inflated rates of return generated by the State on Utah Point.

Commonwealth guidelines suggest a return of 8-12% on Government port infrastructure is acceptable and the States own guidelines have previously targeted returns in that range but a report prepared by Deloitte and commissioned by Atlas indicated returns in excess of 30% were generated on Utah in the 2015 financial year and that significant overcharging was occurring.

Temporary relief of Utah charges of up to $2.50 per tonne has been provided by Pilbara Ports in conjunction with the State for the 2016 financial year and these concessions are due to expire 30 June 2016. If the rates are allowed to revert to previous levels the rates of return on the asset will revert to being in excess of 30% and the viability of the users will again be under question. We expect to also maintain the pro rata relief provided in Yard 2 for $1.73 per tonne on the same terms.

While from a short term perspective achieving a high yield would present attractively to the Government as it means purchasers of the Utah facility would pay an inflated price, any such scenario then consolidates the purchasers need to charge high prices to users to get a return and will mean the underlying projects are no longer viable to the detriment of the miners and the State.

Atlas views it has been significantly overcharged for using Utah and that inflated returns the Government has received are in large part due to the improved throughput from the facility arising from Atlas' investment in Yard 2 infrastructure at its cost and risk, and that these efficiencies of scale should be recognised in the form of lower rates.

The Government should ensure that any sale process is based on a realistic yield on original capital invested and such yield should be engrained in the sale legislation for the future protection of the users.

3) Input into Terms and Conditions

The current users of Utah rely heavily on access to the facility over time for the sustainability of their businesses. Currently 3 parties comprise 100% of the throughput of the facility. Atlas has not been consulted as part of the sale process or been given an opportunity to comment or make submissions on an access regime.

We are concerned that any access regime concluded with the successful purchaser that is brought back to parliament will represent the conditions agreed at that time. It is our view that these conditions will fulfil the ambition of maximising the sale price while prejudicing existing and future users of the facility.

Prior to the sale proceeding the current proponents need to have protections in place against changes to rates charged or conditions of use imposed by the purchaser of Utah Point such that the users business' remain viable.

Conclusion

Atlas is very proud of our track record in working with regional communities, our people and contractors and all other important stakeholders to deliver a business that can make a real difference where we operate. Through access to Utah we have been able to bring many billions of dollars earnings here to WA and we believe this is sustainable for the long term.

Our ability to obtain investment in our mine development pipeline relies on a methodical, balanced well managed port facility. Current indications are that the current sale process is overly focussed on the short term benefit of maximising the upfront sale price. Atlas believes this is occurring at the expense of putting in place a framework for the longer term sustainability of the facility, which if developed with the current users through consultation will provide better outcomes for all parties.

We would be pleased to discuss our submission further with the Committee.

David Flanagan
Managing Director