

FEDERAL COURT OF AUSTRALIA

Glencore Investment Pty Ltd v Commissioner of Taxation of the Commonwealth of Australia [2019] FCA 1432

File numbers: NSD 1679 of 2017
NSD 1900 of 2017
NSD 1956 of 2017

Judge: **DAVIES J**

Date of judgment: 3 September 2019

Catchwords: **TAXATION** – transfer pricing – appeal from objection decisions of Commissioner of Taxation – amended assessments raised pursuant to Div 13 of *Income Tax Assessment Act 1936* (Cth) and Subdiv 815-A of *Income Tax Assessment Act 1997* (Cth) – related party international dealing – non-arm’s length dealing for the purposes of Div 13 – for the purposes of Subdiv 815-A conditions operating between two enterprises in their commercial and financial relations differing from those which might be expected to operate between independent enterprises dealing wholly independently – whether consideration paid to applicant by parent company for supply of copper concentrate within arm’s length range (Div 13) – whether profits did not accrue which might have been expected to accrue but for non-arm’s length conditions (Subdiv 815-A) – contract structured as “price sharing” agreement – adjustments made by Commissioner based on hypothesis of market-related contract – whether permissible to restructure contract as a market-related contract for the purposes of applying transfer pricing provisions – identification of hypothetical transaction for comparative analysis – *Chevron Australia Holdings Pty Ltd v Federal Commissioner of Taxation* (2017) 251 FCR 40 – 1995 OECD Guidelines “Recognition of the actual transactions undertaken” – no warrant to restructure agreement – price sharing and quotational period terms in comparable transactions between independent parties – price sharing percentage within an arm’s length range – no discount required for quotational period optionality back pricing term – onus of proof discharged – appeal allowed

EVIDENCE – role of expert witnesses

Legislation: *Evidence Act 1995* (Cth) s 79
Income Tax Assessment Act 1936 (Cth) ss 136AA, 136AC, 136AD
Income Tax Assessment Act 1997 (Cth) ss 701-1, 815-5, 815-10, 815-15, 815-20, 815-30, 815-40, 995-1
Income Tax (Transitional Provisions) Act 1997 (Cth) ss 815-1, 815-5, 815-15
Taxation Administration Act 1953 (Cth) s 14ZZ
Tax Laws Amendment (Cross-Border Transfer Pricing Act) (No 1) 2012 (Cth)

Cases cited: *Cameco Corporation v The Queen* (2018 TCC 195)
Channel Pastoral Holdings Pty Ltd v Federal Commissioner of Taxation (2015) 232 FCR 162; [2015] FCAFC 57
Chevron Australia Holdings Pty Ltd v Federal Commissioner of Taxation (No 4) (2015) 102 ATR 13; [2015] FCA 1092
Chevron Australia Holdings Pty Ltd v Federal Commissioner of Taxation (2017) 251 FCR 40; [2017] FCAFC 62
Commissioner of Taxation v SNF (Australia) Pty Ltd (2011) 193 FCR 149; [2011] FCAFC 74
SNF (Australia) Pty Ltd v Commissioner of Taxation (2010) 79 ATR 193; [2010] FCA 635
W R Carpenter Holdings Pty Ltd v Federal Commissioner of Taxation (2008) 237 CLR 198; [2008] HCA 33

Date of hearing: 5-7, 10-14, 17-19 December 2018

Registry: New South Wales

Division: General Division

National Practice Area: Taxation

Category: Catchwords

Number of paragraphs: 405

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ORDERS

**NSD 1679 of 2017
NSD 1900 of 2017
NSD 1956 of 2017**

BETWEEN: **GLENCORE INVESTMENT PTY LTD ABN 67 076 513 034**
Applicant

AND: **THE COMMISSIONER OF TAXATION OF THE
COMMONWEALTH OF AUSTRALIA**
Respondent

JUDGE: **DAVIES J**

DATE OF ORDER: **3 SEPTEMBER 2019**

THE COURT ORDERS THAT:

Subject to the parties advising the Court otherwise within seven days, the following orders will be made:

1. The objection decisions be set aside.
2. The objections be allowed.
3. The amended assessments for the income years ended 30 June 2007, 30 June 2008 and 30 June 2009 be set aside.
4. The respondent pay the costs of the applicant, such costs to be taxed in default of agreement.

Note: Entry of orders is dealt with in Rule 39.32 of the *Federal Court Rules 2011*.

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DAVIES J:

INTRODUCTION

1 The applicant (“**the taxpayer**”) has appealed pursuant to s 14ZZ(1)(b) of the *Taxation Administration Act 1953* (Cth) against objection decisions made by the respondent (“**the Commissioner**”) disallowing the taxpayer’s objections to amended assessments issued to it for the 2007, 2008 and 2009 income years (“**the relevant years**”). The taxpayer was assessed as the head of a multiple entry consolidated (“**MEC**”) group for Australian tax purposes, of which Cobar Management Pty Ltd (“**CMPL**”) is a member. In the relevant years, CMPL, which managed and operated the CSA mine in Cobar, New South Wales, sold 100% of the copper concentrate produced at the CSA mine to its Swiss parent, Glencore International AG (“**GIAG**” or “**Glencore**”). The amended assessments were raised by the Commissioner in the exercise of his powers under Div 13 of the *Income Tax Assessment Act 1936* (Cth) (“**ITAA 1936**”) and Subdiv 815-A of the *Income Tax Assessment Act 1997* (Cth) (“**ITAA 1997**”) on the basis that the consideration paid by GIAG to CMPL for the copper concentrate in the relevant years was less than the consideration that might reasonably be expected to have been paid in an arm’s length dealing between independent parties. The amended assessments included in the taxpayer’s assessable income additional amounts of \$49,156,382 (2007), \$83,228,784 (2008) and \$108,675,756 (2009) referable to the consideration which the Commissioner considered would constitute an arm’s length consideration for the copper concentrate that CMPL sold to GIAG in each of the relevant years, increasing the tax payable for the 2007 year by \$14,746,914.60, for the 2008 year by \$13,748,585.40 and for the 2009 year by \$43,822,776.60, plus shortfall interest charges were imposed for each of the relevant years in the amounts of \$6,043,704.90 (2007), \$4,355,479.48 (2008) and \$9,959,152.29 (2009).

HOW THE COPPER CONCENTRATE WAS PRICED IN THE RELEVANT YEARS

2 The CSA mine was acquired by the Glencore Group in 1998 and CMPL has been operating and managing the mine since 1999, following recommencement of mining operations. GIAG purchases all the copper concentrate produced at the mine which it then trades, mostly to

smelters. The purchases have been under a series of life of mine offtake agreements, the first of which was entered into between GIAG and CMPL in mid-1999 and which has since been amended and replaced from time to time.

3 Up until February 2007, the offtake agreements were structured as “market-related” agreements. In February 2007, CMPL and GIAG entered into a fundamentally different form of offtake agreement (“**the February 2007 Agreement**”), known in the copper concentrate industry as a “price sharing agreement”. The contractual terms are considered in greater detail later in these reasons but, for present purposes, it is sufficient to note that the copper concentrate which CMPL sold to GIAG in the relevant years was priced by using, as a reference point, the official London Metal Exchange cash settlement price for copper grade “A” averaged over “the quotational period”. The “quotational period” was, at GIAG’s option, either linked to the month of shipment of the copper concentrate from the loading port of embarkation or the month of arrival of the copper concentrate at the port of disembarkation. Within either alternative, GIAG had the option to elect one of three quotational periods to be declared prior to each shipment from the loading port, at which time GIAG would be aware of the average copper prices in (at least) one of the periods from which it was to make its selection (known in the copper concentrate industry as “quotational period optionality with back pricing”). A deduction was then made from the copper reference price for treatment and copper refining charges (“**TCRCs**”) which, for the calendar years 2007, 2008 and 2009, were fixed at 23% of the copper reference price (as calculated) for the payable copper content of the copper concentrate. In the copper concentrate industry, the fixing of the TCRC deduction as a percentage of the copper reference price is known as “price sharing”.

4 The amended assessments that were issued to the taxpayer incorporated two sets of adjustments:

- adjustments to remove the effect of the 23% price sharing mechanism and to replace it with 50% benchmark/50% spot TCRCs which the Commissioner identified as the “rate previously used by CMPL”; and
- adjustments to reflect the impact of a “consistently applied quotational period”.

5 The adjustments made by the Commissioner reflect the Commissioner’s primary case that the February 2007 Agreement was a non-arm’s length dealing which favoured GIAG to the detriment of CMPL, and that an independent mine producer with CMPL’s characteristics would not have agreed to price sharing at all or to quotational periods with back pricing

optionality and, instead, might reasonably have been expected to have sold its production in the relevant years under a life of mine agreement on market-related terms and limited quotational period optionality with no back pricing. The Commissioner contended that as the evidence did not establish that the consideration that CMPL was paid for its copper concentrate in the relevant years was equal to or more than the consideration that might reasonably be expected to have been paid, had the copper concentrate been sold on such terms, the taxpayer had failed to discharge its onus of proof.

6 For the reasons that follow, I have rejected the Commissioner's primary case as a misapplication of the provisions of Div 13 and Subdiv 815-A and found on the evidence that the consideration that CMPL was paid for its copper concentrate under the February 2007 Agreement in the relevant years was within an arm's length range. As the taxpayer discharged its onus of proving that the amended assessments are excessive, the appeal from the Commissioner's objection decisions should be allowed.

RELEVANT STATUTORY/TREATY PROVISIONS

7 The Commissioner relied on the provisions of both Div 13 of the ITAA 1936 and Subdiv 815-A of the ITAA 1997 in making the amended assessments for the relevant years.

Division 13 of the ITAA 1936

8 Although Div 13 of the ITAA 1936 is now repealed, it was operative in the years in question. Section 136AD of the ITAA 1936 relevantly provided as follows:

136AD Arm's length consideration deemed to be received or given

- (1) Where:
 - (a) a taxpayer has supplied property under an international agreement;
 - (b) the Commissioner, having regard to any connection between any 2 or more of the parties to the agreement or to any other relevant circumstances, is satisfied that the parties to the agreement, or any 2 or more of those parties, were not dealing at arm's length with each other in relation to the supply;
 - (c) consideration was received or receivable by the taxpayer in respect of the supply but the amount of that consideration was less than the arm's length consideration in respect of the supply; and
 - (d) the Commissioner determines that this subsection should apply in relation to the taxpayer in relation to the supply;

then, for all purposes of the application of this Act in relation to the taxpayer, consideration equal to the arm's length consideration in respect of the supply shall be deemed to be the consideration received or receivable by the taxpayer

in respect of the supply.

...

- (4) For the purposes of this section, where, for any reason (including an insufficiency of information available to the Commissioner), it is not possible or not practicable for the Commissioner to ascertain the arm's length consideration in respect of the supply or acquisition of property, the arm's length consideration in respect of the supply or acquisition shall be deemed to be such amount as the Commissioner determines.

9 Relevant definitions were set out in s 136AA of the ITAA 1936, as follows:

- (1) In this Division, unless the contrary intention appears:

...

agreement means any agreement, arrangement, transaction, understanding or scheme, whether formal or informal, whether express or implied and whether or not enforceable, or intended to be enforceable, by legal proceedings.

...

property includes:

- (a) a chose in action;
- (b) any estate, interest, right or power, whether at law or in equity, in or over property;
- (c) any right to receive income; and
- (d) services.

...

supply includes:

- (a) supply by way of sale, exchange, lease, hire or hire-purchase; and
- (b) provide, grant or confer.

...

- (3) In this Division, unless the contrary intention appears:

- (a) a reference to the supply or acquisition of property includes a reference to agreeing to supply or acquire property;
- (b) a reference to consideration includes a reference to property supplied or acquired as consideration and a reference to the amount of any such consideration is a reference to the value of the property;
- (c) a reference to the arm's length consideration in respect of the supply of property is a reference to the consideration that might reasonably be expected to have been received or receivable as consideration in respect of the supply if the property had been supplied under an agreement between independent parties dealing at arm's length with each other in relation to the supply;

...

- (e) a reference to the supply or acquisition of property under an agreement includes a reference to the supply or acquisition of property in connection with an agreement.

10 Section 136AC of the ITAA 1936 was in the following terms:

136AC International agreements

For the purposes of this Division, an agreement is an international agreement if:

- (a) a non-resident supplied or acquired property under the agreement otherwise than in connection with a business carried on in Australia by the non-resident at or through a permanent establishment of the non-resident in Australia; or
- (b) a resident carrying on a business outside Australia supplied or acquired property under the agreement, being property supplied or acquired in connection with that business; or
- (c) a taxpayer:
 - (i) supplied or acquired property under the agreement in connection with a business; and
 - (ii) carries on that business in an area covered by an international tax sharing treaty.

11 For each of the relevant years, the Commissioner made determinations both under s 136AD(1) and s 136AD(4).

12 The application of these provisions requires a comparison between the consideration for the property supplied (or acquired) with the arm's length consideration (as defined) of a comparable hypothetical agreement: *Chevron Australia Holdings Pty Ltd v Federal Commissioner of Taxation* (2017) 251 FCR 40; [2017] FCAFC 62 ("**Chevron**") at [17] per Allsop CJ and [119] per Pagone J. The need to posit a hypothetical agreement is for the purpose of ascertaining the arm's length consideration, which, fundamentally, is a factual inquiry into what might reasonably be expected to have been paid or received by way of consideration, if the actual agreement had been unaffected by the lack of independence and the lack of arm's length dealing. That factual inquiry must be based upon, and supported by, probative evidence including, where appropriate, expert opinion in order to identify a reliable substitute consideration for the actual consideration which was given or received: *Chevron* at [42], [50], [62] (Allsop CJ), [121], [126], [127] (Pagone J).

Subdivision 815-A

13 Subdivision 815-A of the ITAA 1997 was enacted in 2012 by the *Tax Laws Amendment (Cross-Border Transfer Pricing Act) (No 1) 2012* (Cth) but was made to apply retrospectively

to income years starting on or after 1 July 2004: s 815-1 of the *Income Tax (Transitional Provisions) Act 1997* (Cth) (“**Transitional Act**”). Subdivision 815-A was subsequently replaced by Subdivs 815-B to 815-D for income years commencing on or after 29 June 2013: s 815-1(2), s 815-15 of the *Transitional Act*.

14 The relevant object of Subdiv 815-A is set out in s 815-5(a) as follows:

815-5 Object

The object of this Subdivision is to ensure the following amounts are appropriately brought to tax in Australia, consistent with the arm’s length principle:

- (a) profits which would have accrued to an Australian entity if it had been dealing at *arm’s length, but, by reason of non-arm’s length conditions operating between the entity and its foreign associated entities, have not so accrued;...

15 Section 815-10(1) empowers the Commissioner to make a determination under s 815-30(1) for the purpose of negating a “transfer pricing benefit”. The determinations which the Commissioner can make under s 815-30(1) include, relevantly, the determination of an amount by which the taxable income of a taxpayer is increased: s 815-30(1)(a). The Commissioner made such a determination for each of the relevant years in question.

16 Section 815-15 sets out what constitutes a “transfer pricing benefit”. It provides:

815-15 When an entity gets a transfer pricing benefit

Transfer pricing benefit—associated enterprises

- (1) An entity gets a **transfer pricing benefit** if:
 - (a) the entity is an Australian resident; and
 - (b) the requirements in the *associated enterprises article for the application of that article to the entity are met; and
 - (c) an amount of profits which, but for the conditions mentioned in the article, might have been expected to accrue to the entity, has, by reason of those conditions, not so accrued; and
 - (d) had that amount of profits so accrued to the entity:
 - (i) the amount of the taxable income of the entity for an income year would be *greater* than its actual amount; or
 - (ii) the amount of a tax loss of the entity for an income year would be *less* than its actual amount; or
 - (iii) the amount of a *net capital loss of the entity for an income year would be *less* than its actual amount.

The amount of the **transfer pricing benefit** is the difference between the amounts mentioned in subparagraph (d)(i), (ii) or (iii) (as the case requires).

17 By s 815-10(2), s 815-10(1) only applies to an entity if the entity gets the “transfer pricing benefit” at a time when an international agreement containing an associated enterprises article or business profits article applies to the entity. Section 815-10(2) provides:

Transfer pricing benefit may be negated

...

- (2) However, this section only applies to an entity if:
- (a) the entity gets the *transfer pricing benefit under subsection 815-15(1) at a time when an *international tax agreement containing an *associated enterprises article applies to the entity; or
 - (b) the entity gets the transfer pricing benefit under subsection 815-15(2) at a time when an international tax agreement containing a *business profits article applies to the entity.

18 An “associated enterprises article” is defined by s 995-1 and s 815-15(5) of the ITAA 1997 as:

- (a) Article 9 of the United Kingdom convention (within the meaning of the *International Tax Agreements Act 1953*); or
- (b) a corresponding provision of another *international tax agreement.

19 In the present case there is an applicable international agreement, namely the *Agreement between Australia and Switzerland for the Avoidance of Double Taxation with Respect to Taxes on Income, and Protocol* [1981] ATS 5 (“**the Swiss Agreement**”).

20 Article 9 of the Swiss Agreement is in substantially the same terms as Art 9 of the United Kingdom Convention and, at the relevant time, provided as follows:

Where -

- (a) an enterprise of one of the Contracting States participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State; or
- (b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of one of the Contracting States and an enterprise of the other Contracting State,

and in either case conditions operate between the two enterprises in their commercial or financial relations which differ from those which might be expected to operate between independent enterprises dealing wholly independently with one another, then any profits which, but for those conditions, might have been expected to accrue to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly.

21 Section 815-20 of the ITAA 1997 provides that:

815-20 Cross-border transfer pricing guidance

- (1) For the purpose of determining the effect this Subdivision has in relation to an entity:
 - (a) work out whether an entity gets a *transfer pricing benefit consistently with the documents covered by this section, to the extent the documents are relevant; and
 - (b) interpret a provision of an *international tax agreement consistently with those documents, to the extent they are relevant.
- (2) The documents covered by this section are as follows:
 - (a) the Model Tax Convention on Income and on Capital, and its Commentaries, as adopted by the Council of the Organisation for Economic Cooperation and Development and last amended on 22 July 2010;
 - (b) the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, as approved by that Council and last amended on 22 July 2010;
 - (c) a document, or part of a document, prescribed by the regulations for the purposes of this paragraph.
- (3) However, a document, or a part of a document, mentioned in paragraph (2)(a) or (b) is not covered by this section if the regulations so prescribe.
- (4) Regulations made for the purposes of paragraph (2)(c) or subsection (3) may prescribe different documents or parts of documents for different circumstances.

22 The effect of s 815-20(1) of the ITAA 1997 was modified by s 815-5 of the Transitional Act which states that, despite s 815-20, for an income year that starts before 1 July 2012, the documents to which s 815-20 is taken to be referring are:

- the Model Tax Convention on Income and Capital and its Commentaries, as adopted by the Council of the Organisation for Economic Cooperation and Development (“**OECD**”); and
- the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, in each case as last amended before the start of the income year.

In the present case, thus, the relevant OECD Transfer Pricing Guidelines are the 1995 Guidelines (as updated in 1999) (“**the 1995 Guidelines**”) and the relevant OECD Model Convention is the Model Convention that was in place before each of the relevant years.

23 These provisions were also the subject of consideration by the Full Court in *Chevron*. The “conditions” referred to in Art 9 are those conditions existing between the two enterprises affecting their financial or commercial operations which differ from those which might be

expected to operate between independent enterprises dealing wholly independently with one another: *Chevron* at [82] (Allsop CJ), [153] (Pagone J). Allsop CJ described the word “conditions” in Art 9 as “broad and flexible” and, as Pagone J noted at [153], the relations existing between the enterprises are apt to be conditions that potentially operate upon the dealings between, and which bear upon, the inquiry whether there are such conditions operating between the two enterprises which differ from those that might be expected to operate between independent parties dealing wholly independently with one another.

24 Article 9 is the gateway to the application of Subdiv 815-A. That is, s 815-15 only applies if relevant conditions have been identified which operate between the two enterprises in their commercial or financial relations which differ from those which might be expected to operate between independent enterprises dealing wholly independently with one another: s 815-15(1)(b). If so, the issue then is whether there are profits which, but for those conditions, might have been expected to accrue to one of the enterprises but, by reason of those conditions, have not so accrued: s 815-15(1)(c). For that purpose it is necessary to hypothesise what profits “might have been expected to accrue” if the conditions in Art 9 were not present, assessed by reference to a comparable transaction to the actual transaction but one which is between independent enterprises dealing wholly independently with one another. Like Div 13, the hypothesis for the purposes of the application of Subdiv 815-A is an agreement which is not affected by the lack of independence and the lack of arm’s length dealing. The hypothetical thus requires hypothesising circumstances in a dealing where the conditions engaging the application of Art 9 to the enterprise are excluded and the conditions operating between them were as between independent parties dealing wholly independently with each other: *Chevron* per Pagone J at [156].

25 Section 815-15(1)(c) requires a comparison of two amounts – the amount of actual profits which accrued to the entity and the amount of profits which might have been expected to have accrued to the entity but for the “conditions”. For s 815-15(1)(c) to operate to permit Australia to impose tax on related party international agreements on a hypothesised arm’s length profit, there must be a causal relationship between the “conditions” referred to in Art 9 and “an amount of profits which...might have been expected to accrue to the entity” but which has not so accrued “by reason of those conditions”: *Chevron* at [81] (Allsop CJ), [155] (Pagone J). That causal relationship is posited by the “but for” test – namely, that an amount of profits had not accrued which might have been expected to accrue to the taxpayer but for the non-arm’s length conditions mentioned in Art 9. The function of the test prescribed by s 815-15(1)(c)

thus is to determine whether the non-arm's length dealing had the causative effect of reducing the amount of profits that would otherwise have been expected to accrue. If and to the extent that it does, the section operates to bring to account to tax those profits which did not accrue by reason of the non-arm's length conditions by removing the causative effect of those conditions on the profits which the entity might reasonably be expected to have accrued but for those conditions.

- 26 The requirement in s 815-15(1)(c) that the amount be calculated by reference to what "might have been expected" involves a predictive exercise, similar to that required by the provisions of Div 13. Although the word "reasonably" is missing from s 815-15(1)(c), there nonetheless must be a sufficiently reliable evidentiary basis to support the hypothesis of an amount of profits that "might have been expected" to accrue to the taxpayer and for that hypothesis to be supported, the predictive evaluation of an amount of profits that "might have been expected" to accrue to the taxpayer must be one that is more than a mere possibility. In other words, although Subdiv 815-A does not use the word "reasonably", the standard of reasonableness is founded in the evidentiary basis required to support the hypothesis.

The anti-overlap rule

- 27 Section 815-40 of the ITAA 1997 precludes double taxation arising from the simultaneous operation of Div 13 and Subdiv 815-A. Section 815-40 provides:

815-40 No double taxation

- (1) The amount of a *transfer pricing benefit that is negated under this Subdivision for an entity is not to be taken into account again under another provision of this Act to increase the entity's assessable income, reduce the entity's deductions or reduce a *net capital loss of the entity.
- (2) Subsection (1) has effect despite former section 136AB of the *Income Tax Assessment Act 1936*.

THE COMPETING CASES

- 28 It was not in issue for the purposes of Div 13 that CMPL and GIAG did not deal at arm's length with each other in relation to the supply of copper concentrate on the terms of the February 2007 Agreement. Nor was it in issue for the purposes of Art 9(a) of the Swiss Agreement and consequently Subdiv 815-A that GIAG, an enterprise of Switzerland, participated, directly or indirectly, in the management, control or capital of CMPL, an enterprise of Australia.
- 29 The taxpayer's primary case was that, unlike in *Chevron* where the terms of the loan diverged from terms which might be expected between independent parties dealing at arm's length with

each other, the terms governing pricing under the contractual arrangements which applied to the 2007, 2008 and 2009 years were terms that existed in contracts for the sale of copper concentrate between independent market participants and were thus terms that might be expected to be found in an agreement between the relevant hypothetical parties. The taxpayer submitted that the task of the Court was to determine:

- (a) whether the agreed price sharing percentage of 23% was one that might be expected to be agreed between independent parties in an arm's length transaction or within the range of price sharing percentages that might be expected to be agreed between independent parties in an arm's length transaction; and
- (b) if so, to what extent it might be expected that there be a discount allowed for quotational period optionality by independent parties in an arm's length transaction.

30 On the Commissioner's case, the hypothetical transaction should not be constrained by the actual terms under which CMPL supplied copper concentrate to GIAG in the relevant years. Those terms, on the Commissioner's case, were explicable by reference to GIAG's relational and financial control of CMPL. It was submitted that to constrain the hypothetical transaction to one which adopted price sharing for three years as the mechanism for determining the deductions from price to reflect TCRCs was unrealistic, artificial and contrary to the purpose of the transfer pricing provisions and would result in "a commercially unrealistic outcome...controlled by the taxpayer".

31 The Commissioner argued that the evidence did not establish that an independent mine producer with the characteristics of CMPL might be expected to have agreed to price sharing in early 2007 or at any time in the relevant years and the Court should reject the taxpayer's contention that price sharing was to be taken as the pricing mechanism for three years in order to postulate the statutory hypothesis. It was submitted that, accordingly, this case may not and should not be resolved by determining whether the 23% price sharing was a split which might be expected to have applied in a hypothetical transaction between independent parties for the sale and purchase of copper concentrate. A corollary argument advanced was that the evidence was that long-term contracts for the sale of copper concentrate were often renegotiated at least annually to reflect changing market conditions and the failure to renegotiate terms as to price

over a three year period was itself “a consequence of the distortion of commercial reality brought about by the lack of independence between CMPL and GIAG”.

32 The Commissioner additionally submitted that the evidence did not establish that a hypothetical mine producer with CMPL’s characteristics would have agreed to the quotational period optionality term which appears in the February 2007 Agreement. It was submitted that the only possible impact of that term would be to the detriment of the mine producer and to the benefit of the trader and there would be no reason for the hypothetical mine producer, bearing in mind the market in February 2007 and the reliable production that CMPL had experienced over the years, to agree to such terms.

33 The Commissioner identified the hypothetical transaction for the purposes of both Div 13 and Subdiv 815-A to be a long-term contract, originally dated July 1999 and amended and continued from time to time, between independent parties with the characteristics of CMPL and GIAG, for the sale of 100% of the copper concentrate for the life of the mine with terms as to price to be negotiated and amended as between the parties on an annual basis to reflect market conditions, including changing benchmark terms and the commercial needs of the parties.

34 In response to the Commissioner’s case, the taxpayer argued that there was no basis in fact or in law to assume a wholly different agreement for the sale of copper concentrate to that which the parties in fact agreed. In the alternative it was argued that if it was open to the Court in the circumstances of this case to disregard the actual terms upon which the copper concentrate was supplied in 2007, 2008 and 2009 for the purposes of the hypothesis (which was disputed), the evidence nonetheless demonstrated that an arm’s length seller with CMPL’s characteristics might reasonably have been expected to have entered into a price sharing agreement in similar terms to the February 2007 Agreement.

35 The competing cases of the parties require determination as to whether the hypothetical agreement for the purposes of the comparative analysis is to be a price sharing contract (as the taxpayer contended) or a market-related contract (as the Commissioner contended). The type of contract is important as the calculation of the TCRCs is an integer in the pricing of the copper concentrate under either type of agreement but the deduction from the copper reference price for TCRCs is calculated very differently under a price sharing contract to the way in which the deduction for TCRCs is calculated under a market-related contract, and so there will be differences in the pricing of copper concentrate depending on which methodology is employed.

Thus, the application of the statutory provisions will depend (at least in the first instance) on whether the consideration is to be determined on the hypothesis of an agreement in which the deduction for TCRCs is calculated as a percentage of the referenced copper price or by reference to market-based benchmark/spot terms.

CHEVRON

36 As both parties submitted that their competing positions were supported by the Full Court decision in *Chevron*, it is necessary to examine that case in more detail before considering the evidence and the application of Div 13 and Subdiv 815-A.

37 The facts in *Chevron* can be stated succinctly. The appellant (“CAHPL”), an Australian company, obtained a loan from its US subsidiary, without giving security or financial or operational covenants, at an interest rate of 9% pursuant to a credit facility agreement. The Commissioner assessed CAHPL pursuant to Div 13 and Subdiv 815-A on the basis that the interest exceeded the arm’s length consideration that might reasonably have been expected in an agreement between independent parties. At first instance (*Chevron Australia Holdings Pty Ltd v Federal Commissioner of Taxation (No 4)* (2015) 102 ATR 13; [2015] FCA 1092 (“**Chevron at first instance**”)) CAHPL’s case was that the statutory direction that the arm’s length consideration be compared with its actual consideration required its loan to be priced. In other words, what had to be priced was a loan without security or covenants to be given by a commercial lender to a borrower such as CAHPL with its credit rating and as a standalone entity. The primary judge rejected that contention, holding at [76] that what was required was “to depersonalise the agreement... so as to make it, hypothetically, between independent parties dealing at arm’s length”. In addressing the comparison directed by Div 13, his Honour also rejected the Commissioner’s contention that terms different from those of the actual agreement could be taken into account, holding that Div 13 did not require or authorise the creation of an agreement with terms different from those of the actual agreement. The primary judge found at [87] that the absence of security and operational and financial covenants given by CAHPL for the loan would have affected the interest rate, which was higher in the absence of such security and covenants and, had the loan been made under an agreement between independent parties dealing at arm’s length with each other, the borrower would have given such security and covenants and the interest rate, as a consequence, would have been lower. It was accordingly held that CAHPL had not shown that the arm’s length consideration assessed

by the Commissioner was excessive. On appeal, the Full Court affirmed the approach of the primary judge.

38 Allsop CJ stated at [46] that the statutory hypothesis is one directed to a reasonable expectation as to what consideration would be given by the party in the position of the taxpayer. In that case, the task was to identify from the evidence the consideration that might reasonably be expected to have been given or agreed to be given by a party in the position of CAHPL in respect of obtaining a five year loan if the parties to the agreement were independent from each other and dealing at arm's length, compared to the consideration actually given by the CAHPL. In that case the evidence was that CAHPL was part of a group that had a policy to borrow externally at the lowest cost and a policy that the parent will generally provide a third party guarantee for a subsidiary that is borrowing externally. His Honour said that in those circumstances, the consideration that might reasonably be expected to be given by a company in the position of CAHPL would be an interest rate hypothesised on the giving of a guarantee of CAHPL's obligations to the lender by a parent such as Chevron.

39 With respect to Subdiv 815-A, Allsop CJ stated at [82] that the notion of conditions in Art 9 refers to the circumstances or environment that can be seen to operate between the two enterprises in their commercial or financial relations which are different to the circumstances or environment which would operate between independent enterprises. The inquiry then for the purposes of s 815-15(1)(c) is what "amount of profits" might have been expected to accrue, but did not accrue by reason of those conditions. His Honour observed that s 815-15(1)(c) posits "a causal relationship between the 'conditions' referred to in Art 9 and 'an amount of profits which ... might have been expected to accrue to the entity' but which has not so accrued 'by reason of those conditions'". His Honour had regard to the discussion in the 1995 Guidelines as assisting in understanding the nature of that causal inquiry. At [90], Allsop CJ stated that these passages illuminated that the causal test in s 815-15(1)(c) is a "flexible comparative analysis that gives weight, but not irredeemable inflexibility, to the form of the transaction actually entered between the associated enterprises". His Honour stated that:

A degree of flexibility is required especially if the structure and detail of the transaction has been formulated by reference to the group relationship and a "tax-effective" outcome (even if, as here, one that is not said to be illegitimate). The form of that transaction may, to a degree, be altered if it is necessary to do so to permit the transaction to be analysed through the lens of mutually independent parties.

40 The Commissioner relied on that passage to contend that the causal inquiry directed by s 815-15(1)(c) concerning the conditions and profits which might have but did not accrue to

the taxpayer should be undertaken flexibly. However, that contention is based on a misreading of his Honour's reasons at [90]. Paragraph [90] must be read in the context of the discussion starting at [81], and it is worth setting out [81]-[91] in full:

81. Paragraph (c) of s 815-15(1) is central. It posits a causal relationship between the "conditions" referred to in Art 9 and "an amount of profits which ... might have been expected to accrue to the entity" but which has not so accrued "by reason of those conditions".
82. The notion of conditions in Art 9 refers to the circumstances or environment that can be seen to operate between the two enterprises in their commercial or financial relations which are different to the circumstances or environment which would operate between independent enterprises. The word "conditions" is broad and flexible...
83. That condition or these conditions operated between CAHPL and CFC in their financial relations and was or were manifested in the Credit Facility. The inquiry then for the purposes of s 815-15(1)(c) is what "amount of profits" might have been expected to accrue, but did not by reason of the conditions.
84. The understanding of the nature of that causal inquiry is assisted by the discussion in the OECD 1995 Guidelines (the Guidelines). Paragraph 6 of the Preface to the Guidelines sets out the general approach:

In order to apply the separate entity approach to intra-group transactions, individual group members must be taxed on the basis that they act at arm's length in their dealings with each other. However, the relationship among members of an MNE group may permit the group members to establish special conditions in their intra-group relations that differ from those that would have been established had the group members been acting as independent enterprises operating in open markets. To ensure the correct application of the separate entity approach, OECD Member countries have adopted the arm's length principle, under which the effect of special conditions on the levels of profit should be eliminated.

85. The arm's length principle is set out in Art 9 of the OECD Model Tax Convention on Income and Capital.
86. The Guidelines discuss the arm's length principle in Ch 1. In the discussion of Art 9, the Guidelines state at [B.1.6]:

By seeking to adjust profits by reference to the conditions which would have obtained between independent enterprises in comparable transactions and comparable circumstances, the arm's length principle follows the approach of treating the members of an MNE group as operating as separate entities rather than as inseparable parts of a single unified business. Because the separate entity approach treats the members of an MNE group as if they were independent entities, attention is focused on the nature of the dealings between those members.

87. The Guidelines in Section B, in dealing with the statement of the arm's length principle, discuss at [B.1.10] the practical difficulty in applying the arm's length principle that may arise from the fact that associated enterprises may engage in transactions that independent enterprises would not engage in. For instance, an independent entity may not be willing to sell or licence some

valuable intellectual property or know-how. Some of the discussion is illuminating:

[T]he owner of an intangible may be hesitant to enter into licensing arrangements with independent enterprises for fear of the value of the intangible being degraded. In contrast, the intangible owner may be prepared to offer terms to associated enterprises that are less restrictive because the use of the intangible can be more closely monitored. There is no risk to the overall group's profit from a transaction of this kind between members of an MNE group. An independent enterprise in such circumstances might exploit the intangible itself or license it to another independent enterprise for a limited period of time (or possibly under an arrangement to adjust the royalty).

88. Section C of the Guidelines concerns guidance for applying the arm's length principle. The section begins (at [C.1.15]) with a discussion of comparability as follows:

Application of the arm's length principle is generally based on a comparison of the conditions in a controlled transaction with the conditions in transactions between independent enterprises. In order for such comparisons to be useful, the economically relevant characteristics of the situations being compared must be sufficiently comparable. To be comparable means that none of the differences (if any) between the situations being compared could materially affect the condition being examined in the methodology (eg price or margin), or that reasonably accurate adjustments can be made to eliminate the effect of any such differences. In determining the degree of comparability, including what adjustments are necessary to establish it, an understanding of how unrelated companies evaluate potential transactions is required. Independent enterprises, when evaluating the terms of a potential transaction, will compare the transaction to the other options realistically available to them, and they will only enter into the transaction if they see no alternative that is clearly more attractive.

89. The Guidelines in a section beginning at [C.1.36] discuss the recognition of the actual transaction undertaken. The whole of [C.1.36]-[C.1.38], though long, should be set out:

A tax administration's examination of a controlled transaction **ordinarily should be based on the transaction actually undertaken by the associated enterprises as it has been structured by them**, using the methods applied by the taxpayer insofar as these are consistent with the methods described in Chapters II and III. In other exceptional cases, the tax administration should not disregard the actual transactions or substitute other transactions for them. Restructuring of legitimate business transactions would be a wholly arbitrary exercise the inequity of which could be compounded by double taxation created where the other tax administration does not share the same views as to how the transaction should be structured.

However, there are two particular circumstances in which it may, exceptionally, be both appropriate and legitimate for a tax administration to consider disregarding the structure adopted by a taxpayer in entering into a controlled transaction. The first circumstance arises where the economic substance of the transaction differs from its form. In such a case the tax administration may disregard the parties' characterisation of the transaction and re-characterise it in accordance with its substance. An example of this circumstance would be an investment in which an associated enterprise in the

form of an interest-bearing debt when, at arm's length, having regard to the economic circumstances of the borrowing company, the investment would not be expected to be structured in this way. In this case it might be appropriate for a tax administration to characterise the investment in accordance with its economic substance with the result that the loan may be treated as a subscription of capital. **The second circumstance arises where, while the form and substance of the transaction are the same, the arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner and the actual structure practically impedes the tax administration from determining an appropriate transfer price.** An example of this circumstance would be a sale under a long-term contract, for a lump sum payment, of unlimited entitlement to the intellectual property rights arising as a result of future research for the term of the contract (as previously indicated in paragraph 1.10). While in this case it may be proper to respect the transaction as a transfer of commercial property, it would nevertheless be appropriate for a tax administration to conform the terms of that transfer in its entirety (and not simply by reference to pricing) to those that might reasonably have been expected had the transfer of property been the subject of a transaction involving independent enterprises. Thus, in the case described above it might be appropriate for the tax administration, for example, to adjust the conditions of the agreement in a commercially rational manner as a continuing research agreement.

In both sets of circumstances described above, **the character of the transaction may derive from the relationship between the parties rather than be determined by normal commercial conditions and may have been structured by the taxpayer to avoid or minimise tax. In such cases, the totality of its terms would be the result of a condition that would not have been made if the parties had been engaged in arm's length dealings. Article 9 would thus allow an adjustment of conditions to reflect those which the parties would have attained had the transaction been structured in accordance with the economic and commercial reality of parties dealing at arm's length.**

(Emphasis added.)

90. The above discussion illuminates that the causal test in s 815-15(1)(c) based on Art 9 is a flexible comparative analysis that gives weight, but not irredeemable inflexibility, to the form of the transaction actually entered between the associated enterprises. A degree of flexibility is required especially if the structure and detail of the transaction has been formulated by reference to the group relationship and a "tax-effective" outcome (even if, as here, one that is not said to be illegitimate). The form of that transaction may, to a degree, be altered if it is necessary to do so to permit the transaction to be analysed through the lens of mutually independent parties.
91. There is nothing in the Guidelines that requires other than the independent status of the enterprises **from each other** in the transaction. Thus, to paraphrase the last sentence of [C.1.38], Art 9 (and so s 815-15(1)(c)) would allow an adjustment of conditions to reflect the conditions which the parties would have attained had the transaction been structured in accordance with commercial reality with the parties to the transaction dealing at arm's length.

(Emphasis in original.)

Read in context, it is evident that his Honour at [90] was simply encapsulating shorthand what is set out in the 1995 Guidelines at [C.1.36]-[C.1.38], namely the comparative analysis for the purposes of the causal test should ordinarily be based on the actual transaction as structured by the parties, save in the case of the two exceptional circumstances identified in the 1995 Guidelines where some adjustment to the form of the actual transaction may be necessary in order to undertake a comparative analysis with an agreement unaffected by the lack of independence between the parties and lack of non-arm's length dealing. His Honour starts at [81] with the observation that s 815-15(1)(c) applies a causative test by positing a causal relationship between the non-arm's length conditions and profits which might have, but did not, accrue to the taxpayer by reason of the non-arm's length conditions operating between the parties with respect to the actual transaction. His Honour observes at [84] that the understanding of the nature of that causal inquiry is assisted by the discussion in the 1995 Guidelines. His Honour sets out the relevant paragraphs from the 1995 Guidelines at [88] and [89], and then concludes at [90] that the 1995 Guidelines "illuminate" that the causal test in s 815-15(1)(c) based on Art 9 "is a flexible comparative analysis that gives weight, but not irredeemable inflexibility, to the form of the transaction actually entered between the associated enterprises". As his Honour noted, some "flexibility" may be required in the case of the two exceptional circumstances set out in the 1995 Guidelines "if it is necessary to do so" so as to permit that transaction to be analysed through the lens of mutually independent parties. It is important to emphasise that his Honour was not saying that the actual transaction may be recast as a different transaction for the purposes of the comparative analysis, other than in the case of the two exceptional circumstances referred to in the 1995 Guidelines.

41 Pagone J (with whom Allsop CJ and Perram J agreed) held that the focus of the inquiry called for by s 136AD(3) (the cognate provision to s 136AD(4) with respect to acquisitions) and s 136AA(3)(d) is an alternative agreement from the one actually entered into where the alternative agreement was made by the parties upon the assumptions that they were independent and dealing at arm's length. His Honour stated at [126] that the provisions do not require the construction of an abstract hypothetical agreement between abstract independent parties. Rather the hypothesis is of an agreement which was not affected by the lack of independence and the lack of arm's length dealing. His Honour stated that the task of ascertaining the arm's length consideration "is, therefore, fundamentally a factual inquiry into what might reasonably be expected if the actual agreement had been unaffected by the lack of independence and the lack of arm's length dealing".

42 In a passage relied upon by the taxpayer, his Honour stated at [128]:

The need to posit a hypothetical acquisition under an agreement for the purpose of evaluating it by reference to the standard of reasonable expectation requires a consideration of the evidence to determine a reliably comparable agreement to that which was actually entered into. That, as his Honour said at [499] required the hypothetical to remain close to the actual loan. The function of the hypothesis is to identify a reliable substitute consideration for the actual consideration which was given or agreed to be given, and the reliability of the substitute consideration depends upon the hypothetical agreement being sufficiently like the actual agreement.

Later in that paragraph in a passage relied on by the Commissioner, his Honour stated that:

The characteristics of the purchaser must be such as meaningfully to inform an inquiry into whether the consideration actually given under the agreement exceeded the arm's length consideration under the hypothetical agreement; or, to use the words of the learned trial judge at [80], in the hypothesis the independent parties are to have the characteristics relevant to the pricing of the loan "to enable the hypothesis to work".

His Honour stated that the actual characteristics of the taxpayer must, therefore, ordinarily serve as the basis in the comparable agreement.

43 At [129], in another passage relied on by the Commissioner, his Honour stated that the provisions of Div 13 are intended to operate in the context of real world alternative reasonable expectations of agreements between parties and not in artificial constructs. His Honour stated:

The comparable agreement may, therefore, usually assume an acquisition by the taxpayer of the property actually acquired under an agreement having the characteristics of the agreement as entered into but otherwise hypothesised to be between them as independent parties dealing with each other at arm's length in relation to that acquisition.

His Honour held the borrower may be a company like CAHPL which was a member of a group but where the consideration in respect of the acquisition identified in the hypothetical agreement was not distorted by the lack of independence between the parties or by a lack of arm's length dealings in relation to that acquisition. At [130] his Honour stated that the ultimate object of the task required by Div 13 is to ensure that what is deemed as the consideration by s 136AD(3) is the reliably predicted amount which the taxpayer might reasonably be expected to give or to have given by way of consideration, rather than a hypothetical consideration without reliable foundation in the facts or reality of the circumstances of the taxpayer in question. At [132] his Honour concluded that the evidence before, and found by, the primary judge "amply supported" the primary judge's prediction of the reasonable expectation of a borrowing by CAHPL being supported by security.

44 With respect to Subdiv 815-A, his Honour stated at [156] that the comparison which Art 9 requires to be undertaken is akin to that contemplated by Div 13 and the object is to determine whether conditions actually prevailing between the relevant enterprises differ from those which might be expected to operate if they had been independent and had been dealing wholly independently with each other. His Honour stated that the hypothetical in that exercise is undertaken for the purpose of determining whether the dealing which actually occurred might have been expected to have occurred on different terms, which will generally require that the parties in the hypothetical will have the characteristics and attributes of the actual enterprises in question. In that case, his Honour considered that ultimately the question was that of determining whether profits might have been expected to accrue to CAHPL if the transaction it entered into with the US subsidiary had been entered into where the conditions which operated between CAHPL and the US subsidiary did not operate, that is if they had been dealing with each other at arm's length in relation to the dealing as independent parties.

45 *Chevron* thus makes it clear that the positing of a hypothetical agreement is not for the purposes of pricing a hypothetical supply to a hypothetical buyer (or a hypothetical acquisition from a hypothetical seller) and the provisions do not permit or require the construction of an abstract hypothetical agreement between abstract independent parties. The function of the hypothesis is to identify a reliable substitute consideration for the actual consideration which was given so that the reliability of the substitute consideration depends upon the hypothetical agreement being sufficiently like the actual agreement to be a sufficiently comparable transaction against which to evaluate whether an arm's length consideration was given under the actual transaction (Div 13) or an amount of profits which might have been expected to accrue did not accrue (Subdiv 815-A).

46 As Allsop CJ and Pagone J both emphasised, for the hypothetical agreement to be sufficiently comparable to the actual agreement to enable a reliable substitute consideration for that paid or given to be determined, the characteristics and attributes of those parties which inform an inquiry into the pricing of the property supplied or acquired should also be taken into account. In *Chevron*, both at first instance and on appeal, the Court rejected the taxpayer's argument that the task was to ascertain whether it might reasonably be expected that CAHPL, as a standalone company, could obtain an unsecured borrowing, with no operational or financial covenants at less than 9% interest. As Pagone J stated at [130], it would distort the application of Div 13 and Subdiv 815-A to posit a hypothetical agreement on the basis that the taxpayer

was not a member of a corporate group or as if it were “an orphan” severed from the financial strength of its ultimate parent and corporate group.

47 Significantly, *Chevron* is not authority that the provisions of Div 13 and Subdiv 815-A ask what form of agreement might have been negotiated by entities dealing with each other at arm’s length. That approach was rejected by the primary judge in *Chevron* at first instance at [88] and nothing contrary is said in the Full Court decision. Nor does *Chevron* provide authority for the proposition put by the Commissioner, namely that the hypothetical transaction, for the purposes of addressing the statutory questions directed by Div 13 and Subdiv 815-A in the present case, is to be identified as a wholly differently structured agreement for the sale of concentrate to the actual agreement which the parties entered into. Not only was there no suggestion by the Commissioner that either of the two exceptional circumstances identified in the 1995 Guidelines have application in the present case, these reasons elucidate later why the approach of the Commissioner to the application of Div 13 and Subdiv 815-A must be rejected.

THE ARM’S LENGTH PRINCIPLE

48 It is necessary to say something more about Div 13 and Subdiv 815-A. In construing and applying the provisions of Div 13 and Subdiv 815-A it is important to bear in mind the international context in which the internationally accepted arm’s length principle has been adopted as the measure by which countries, and the extent to which countries, may bring to tax within their jurisdiction an appropriate share of tax revenue from the international dealings of multinational enterprises. The transfer pricing provisions give effect to the bilateral international agreements between sovereign countries about how each is permitted to bring to tax international related party transactions. The OECD has adopted the arm’s length principle as the means by which each country, and the extent to which each country, may bring to tax related party international transactions to ensure fairness and equity as between different taxing countries. Australia has adopted that international standard in Div 13 and Subdiv 815-A, the fiscal policy of which is to tax related parties in cross-border transactions on the basis of the arm’s length principle. The objective of the legislation is to ensure that such parties’ fiscal obligations for domestic tax purposes are based on the arm’s length equivalent dealing of the actual transaction entered into. A construction and application of those provisions that distorts the application of the arm’s length principle in related party international dealings by applying some different measure for determining an arm’s length price than one based on the arm’s

length equivalent of the transaction actually entered into, would not give effect to the policy objective.

49 That is not to say that Div 13 and Subdiv 815-A will apply to all non-arm's length cross-border dealings. A non-arm's length dealing may nonetheless have an arm's length consideration. As Middleton J noted in *SNF (Australia) Pty Ltd v Commissioner of Taxation* (2010) 79 ATR 193; [2010] FCA 635 at [39]:

A finding reached for the purposes of s 136AD(3)(b) that any two or more of the parties to an agreement were not dealing at arm's length with each other will not necessarily be determinative in considering whether the consideration given or agreed to be given for the purposes of s 136AD(3)(c) was not arm's length consideration. Where it can be concluded that, even though there was an absence of real bargaining, an arm's length consideration was given or agreed to be given, then s 136AD(3)(c) will not be satisfied and s 136AD will have no application.

Whilst the application of both Divisions is upon the predicate that there was an absence of real bargaining, it does not necessarily follow from an absence of real bargaining, nor must it necessarily follow, that the consideration agreed to be paid was not an arm's length consideration.

THE TAXPAYER'S EVIDENCE

50 The taxpayer relied on lay and expert evidence.

(1) David Kelly

51 The lay evidence was given by David Kelly. Mr Kelly is a chartered accountant by training who has been involved with the CSA mine in four capacities:

- prior to 2006, Mr Kelly worked as an auditor at Deloitte and audited the accounts of the CSA mine;
- from 2006 to 2009, he was employed by GIAG as the CSA mine's asset manager;
- from 5 November 2007 and until 9 October 2017, he was a director of CMPL (and the two GIAG subsidiaries which owned the CSA mine);
- since 2009, Mr Kelly has traded commodities for GIAG, including the copper concentrate produced at the CSA mine and sold by CMPL to GIAG.

52 Mr Kelly swore four affidavits in these proceedings in which he gave evidence about a range of matters, including: the copper market and pricing and terms of sale of copper concentrate; the Glencore Group and Glencore's business; GIAG's acquisition and ownership structure of

the CSA mine; his involvement with the CSA mine as the CSA mine's asset manager between 2006 and 2009, as a trader from 2009 onwards and as a director of CMPL from 5 November 2007 until 9 October 2017; the operations of the CSA mine during the relevant period; the mine's financial performance in 2006; the challenges the mine faced from 2006 to 2009; the logistics and risks for CMPL in selling its copper concentrate in the period 2006 to 2009, if it had been independent of GIAG and sought to sell its copper concentrate directly to smelters; and the offtake agreements under which CMPL supplied copper concentrate to GIAG over the period 1999 to 2009. He also exhibited to his affidavit examples of other offtake agreements for the sale of copper concentrate containing price sharing and quotational period back pricing optionality terms.

53 The Commissioner urged the Court to treat Mr Kelly's evidence with considerable caution, submitting he was not an independent witness, he had overstated parts of his evidence, his evidence included matters about which he did not have personal knowledge or relevant experience to give evidence on, and his recollection of events in 2006 to 2007 was shown to be sketchy and unreliable. Some of those criticisms were shown to have foundation but, ultimately, the matters that must be decided do not turn on the contentious parts of Mr Kelly's affidavit evidence, as these reasons will elucidate.

(2) Richard Wilson

54 Mr Wilson is an expert in market analysis of the global copper concentrate industry. Until 2011, he was the author, and since 2011 has been the editor, of the Brook Hunt Report, an annual publication examining the global markets for copper concentrate. Mr Wilson was also the co-developer of the C1, C2 and C3 mine costing analysis (to which reference will be made later in these reasons). Mr Wilson prepared three reports for these proceedings.

55 Mr Wilson's first report addressed the following questions:

- (a) whether the conditions (individually or together) that operate under the 1999 Offtake agreement as amended from time to time and including as amended by the Third Replacement Concentrate Agreement (together with its Addendums and Amendment) as they applied in the 2007 to 2009 calendar years differ from those that might be expected to operate between a producer/seller of copper concentrate in the position of [CMPL] and a purchaser independent of CMPL having regard to the circumstances of CMPL in the period 1999 to February 2007; and
- (b) if they do,
 - (i) how such conditions differ; and

- (ii) what profits (if any) may have been expected to accrue to CMPL by reason of such differences?

56 Mr Wilson's second report contained his response to, and comments on, the expert reports of the Commissioner's mining industry experts, Mr Leonard Kowal and Mr Marc Ingelbinck.

57 Mr Wilson's third report contained his response to supplementary reports of Mr Kowal and Mr Ingelbinck.

(3) Tony Samuel

58 Mr Samuel is a forensic accounting expert. He prepared one report which responded to the expert report of the Commissioner's financial analysis expert, Mr David van Homrigh.

THE COMMISSIONER'S WITNESSES

59 The Commissioner called the following expert witnesses:

(1) Marc Ingelbinck

60 Mr Ingelbinck is a mining industry expert. He formerly traded commodities for Cargill, Inc, before commencing a management position at Magma Copper in which capacity he traded the company's copper cathode, copper rod and sulphuric acid output, sourced third party copper concentrate feed and managed the company's price risk management programs. Later he was vice president, marketing and trading for BHP's base metals customer sector group with overall responsibility for all concentrate marketing within the group. Mr Ingelbinck prepared two reports for these proceedings.

61 In his first report, Mr Ingelbinck addressed the following questions:

- (1) For the [relevant years], do the conditions that were operating between CMPL and GIAG in their commercial and financial relations, differ from the conditions which might have been expected to operate between an Independent Producer/Seller and Independent Buyer dealing wholly independently with one another? If so:
 - (a) how and to what do such conditions differ; and
 - (b) what profits (if any) by reason of these conditions might reasonably have been expected to have accrued to CMPL but for those conditions?
- (2) For [the relevant years], is the consideration received or receivable by CMPL for the sale of Cobar copper concentrate to GIAG different from the consideration that might reasonably have been expected to have been received or receivable for the sale of Cobar copper concentrate by an Independent Producer/Seller to an Independent Buyer dealing wholly independently with one another? If so:

- (a) how and to what extent; and
 - (b) what consideration might reasonably have been expected to have been received or receivable by an Independent Producer/Seller but for that difference?
- (3) Please answer the above questions in the alternative and assuming that the Independent Producer/Seller was the operator of the Cobar Mine in the period 1 January 1999 to 31 December 2009 and:
- (a) operated in a commercial context as a wholly owned subsidiary of a multinational global resources company in the same or similar circumstances to that of CMPL and GIAG; or
 - (b) for the period between 1 January 2007 and 31 December 2009 operated as a stand-alone producer/seller of Cobar copper concentrate.

62 Mr Ingelbinck was subsequently asked to prepare a supplementary report addressing the following questions:

1. Whether my opinions as set out in my report would change or be affected in any way having read two affidavits of David Hinder Kelly and, if so, how and explain why.

In particular, having regard solely to the circumstances of CMPL in the period 1999 to February 2007, identify whether my opinions as set out in my report would change or be affected in any way, and, if so, explain why.

2. Having considered Mr Wilson's reports:
- (a) whether my opinions as set out in my report, would:
 - (i) change or be affected in any way and if so, how and explain why;
 - (ii) in particular, having regard solely to the circumstances of CMPL in the period 1999 to February 2007, identify whether my opinion as set out in my report would change or be affected in any way, and if so, how and explain why; and
 - (b) identify those statements in the second Wilson report that I agree with and those I disagree with. For any statement that I disagree with, provide reason(s) for that disagreement.

(2) Leonard Kowal

63 Mr Kowal is another mining industry expert with 35 years of experience with Inco Ltd, then the largest producer of nickel in the world, and, at the time of trial, an additional 12 years of experience providing consultant services to a wide array of metal producers. During his time with Inco Ltd, he was involved in negotiating various contracts and also marketing. Mr Kowal prepared two reports which addressed the same Questions 1 and 2 as Mr Ingelbinck was asked to address.

(3) David van Homrigh

64 Mr van Homrigh is a financial analysis expert. He was asked to analyse and provide advice on the financial affairs of CMPL for the period 18 December 1998 to 31 December 2009 and, in particular, the period from 1 January 2007 to 31 December 2009. In relation to the period from 1 January 2007 to 31 December 2009, Mr van Homrigh was asked to respond to the following questions:

1. Whether or not CMPL and/or the Cobar mine was profitable.
2. To what extent there was an uncertainty as to the profitability of future copper concentrate mining operations at the Cobar mine.
3. Whether or not CMPL required bank or other financing in order to operate the Cobar Mine and the nature of any such financing sought or provided.
4. The nature, and benefits to CMPL, of financial arrangements which were in fact in place as between CMPL and/or the Cobar Mine and the Joint Venture Participants and/or GIAG or any third party.

JOINT EXPERT REPORTS

65 Joint expert reports were prepared by:

- (a) the mining industry experts – Mr Wilson, Mr Ingelbinck and Mr Kowal; and
- (b) the financial experts – Mr van Homrigh and Mr Samuel.

66 Only the mining industry experts were cross examined on their reports.

THE COPPER CONCENTRATE MARKET

67 It is helpful to start with the evidence about the copper concentrate industry for context. Evidence explaining the copper concentrate market was given by the three mining industry experts as well as by Mr Kelly and, in the broad detail, they all gave largely consistent evidence. A summary of that evidence follows.

Copper concentrate

68 Copper concentrate is produced at copper mines from the processing of sulphide and oxide ore. To produce pure copper from the ores, the copper concentrate must then go through further processing and refining, which is done at smelters. Copper concentrates are highly variable in composition in respect of the grades of their key elements (copper, iron, sulphur and various precious metals such as gold and silver) and the presence and levels of impurities. The variations arise due to differences in copper mineralogy present in an orebody. The copper content of copper concentrate varies from around 10% to around 50% depending upon the

orebody and the processing techniques used to derive it. Each smelter has different requirements as to the copper concentrate that it purchases, which relate to its ability to treat the concentrate in light of the payable metals and impurities the concentrate contains.

The custom concentrate market

69 The production and smelting of copper concentrates within a corporate group is described as integrated production. Where copper concentrates are sold to independent third parties, this is known as the custom concentrate market. The participants in this market are miners, smelters and traders. Miners are sellers of copper concentrates and smelters are buyers. Traders (also known as merchants) act as intermediaries and both buy and sell copper concentrates. Copper concentrate can be sold under long-term arrangements with a smelter or a trader (which accounts for around 80% of custom concentrate trading) or on the spot market (approximately 20% of all custom concentrate trading). The contractual arrangements which govern these sales are known in the industry as offtake agreements.

70 Mr Ingelbinck in his first report commented at para 12:

The relationship between non-integrated mines and custom smelters is largely a symbiotic one. A copper concentrate producer who does not have a home to monetise its production has a serious problem. So does a custom smelter who does not have sufficient primary raw material supply to run its operation. This is reflected in the fact that in my experience the vast majority of copper concentrate purchase/sales agreements are structured on a long-term basis which provides the seller with a guaranteed home for its output, the buyer with security of raw material feed and allows both parties to avoid a greater degree of volatility in commercial terms which tends to prevail in the spot market.

71 Long-term offtake agreements can provide for ongoing sales over a fixed number of years or for the “life of the mine”, and may be for specified quantities of concentrate or for the whole of a particular mine’s production. The experts were agreed that the advantage to a miner of an entire production offtake agreement is that the miner is guaranteed that all of its production will be sold as and when it is ready to be shipped, which effectively transfers risk to the buyer.

Pricing of copper concentrate

72 Due to the highly variable nature of copper concentrate, there is no terminal market for copper concentrate where it can be traded at a precise known price. In contrast, the price of refined copper is typically set by reference to the price quoted on a metal exchange such as the London Metal Exchange. In Mr Ingelbinck’s words, “recognising this” the industry has adopted a pricing structure for its contracts which follows a reasonably well-established framework.

However, each contract is individually negotiated and have varying terms that affect the price of the copper concentrate. As Mr Wilson stated, the detail and pricing of the individual contracts will vary greatly depending on the needs and risk appetites of the seller and buyer and whether the contracts are for spot sales or medium/long-term contracts.

73 The evidence was to the effect that copper concentrate sold under offtake agreements will generally be priced by reference to:

- (a) the price of copper metal on a metal exchange, such as the London Metal Exchange, averaged over a given period of time (known in the industry as the “quotational period”);
- (b) the deductions to be made from the reference price for the TCRCs; and
- (c) other adjustments for the payable copper content in the copper concentrate (noting that smelting processes will usually not recover 100% of the copper content in concentrate) and penalties for deleterious elements.

Copper metal price

74 Copper metal can be traded on one of three metal exchanges, the largest of which in terms of volume of copper and other metals transacted is the London Metal Exchange. It was common ground between the experts that the copper metal price is extremely volatile and unpredictable with “ups and downs”. Mr Wilson explained that copper metal prices are influenced by many factors which include global industrial activity; overall copper metal inventory levels in London Metal Exchange approved warehouses; the value of the US dollar against other currencies; the general copper supply/demand outlook; and changes to metal supply and demand, such as disruptive elements like industrial action, flooding, and earthquakes. Mr Wilson stated that prices also respond to the results of regularly published macroeconomic data from key countries/regions, such as China, the Eurozone and the USA.

Quotational periods

75 Quotational periods vary from contract to contract but are typically linked either to the month of shipment of the copper concentrate from the port of embarkation or the month of arrival of the concentrate at the point of disembarkation. The quotational period can be specified as a single day, a week or a month. Where the quotational period is longer than a day, the average of the published daily settlement prices for the chosen quotational period is used. For example, for a contract with a quotational period of M+1, the average daily London Metal Exchange

prices in the calendar month after the month of shipment are used to calculate the price of the copper concentrate.

76 Offtake agreements can contain one quotational period or multiple quotational periods for a given payable metal and, where multiple quotational periods are identified, the contract will stipulate the process for selecting which quotational period will apply (known in the industry as “quotational period optionality”). Additionally, some contracts allow the buyer to choose from several quotational periods where the price in at least one quotational period is known at the time of selection. This type of optionality is commonly referred to in the industry as “quotational period optionality with back pricing”.

77 Relevant quotational period abbreviations and their meanings include:

2MPMOSS Two months prior to month of scheduled shipment

1MPMOSS Month prior to month of scheduled shipment

M-1 Calendar month prior to month of shipment

M or MOS Calendar month of shipment

M+1 Calendar month following month of shipment

M+2 Second calendar month following month of shipment

M+3 Third calendar month following month of shipment

M+4 Fourth calendar month following month of shipment

M+5 Fifth calendar month following month of shipment

1MAMA Calendar month after month of arrival

2MAMA Second calendar month after month of arrival

3MAMA Third calendar month after month of arrival

4MAMA Fourth calendar month after month of arrival

5MAMA Fifth calendar month after month of arrival

TCRCs

78 The notional purpose of TCRCs is to cover smelting and refining costs and to provide the buyer (whether a trader or smelter) with an element of profit but, as Mr Wilson explained, the actual TCRCs negotiated are, in practice, a result of market forces and often bear little relationship to the actual cost of treatment and refining of the copper concentrate. As with copper metal prices, TCRCs are highly volatile and from time to time TCRCs and copper metal prices move in opposite directions.

79 TCRCs in long-term agreements can include both benchmark TCRCs and spot TCRCs and can be with or without price participation (with price participation, “**TCRCPP**”). Benchmark TCRCs, along with the level of any price participation, are established annually between major concentrate buyers and sellers during the so-called copper concentrate “mating season” that starts in around September of each year. Negotiations continue until TCRCs and the level of price participation are agreed between a major copper concentrate buyer and seller and these become the “benchmark” that may be adopted, with relevant adjustments, by other buyers and sellers that use this style of contract. In long-term contracts adopting the benchmark TCRCs, the TCRCs are usually negotiated annually and are subject to significant variations from year to year.

80 Prevailing spot TCRCs reflect the market dynamics at a particular point in time and can be very volatile and vary greatly throughout a year. The spot TCRC will usually bear little, if any, relationship with the benchmark TCRC and may exceed or be well below the benchmark TCRC.

Price participation

81 Price participation is a mechanism that may be applied to long-term copper concentrate contracts adopting benchmark TCRCs which enables both seller and buyer to participate in movements in copper prices. Mr Wilson described price participation as “essentially a ‘pain-gain’ mechanism”. He explained in his first report that price participation usually referenced a trigger London Metal Exchange copper price of 90c/lb, above which the refining charge would be increased by 10% of the amount by which the London Metal Exchange price exceeded this trigger. Below 90c/lb, the refining charge would be reduced by 10% of the amount by which the copper metal price fell below this trigger price. In this manner both buyer and seller benefitted from a proportion of the high copper price and vice versa. In 2006, London Metal Exchange prices were substantially above the price participation trigger level

and as a result buyers were provided with a substantial benefit (or profit) which had what Mr Ingelbinck described as a “significant impact” on the combined TCRCPP deduction. As a result, miners argued strongly for the removal of price participation from long-term contracts and price participation was set to zero in the 2006 mating season for 2007 annual benchmark contracts. However the 2006 Brook Hunt Report noted that it was not clear whether price participation would be reintroduced into long-term contracts.

Price sharing agreements

82 Price sharing agreements are another type of long-term contract for the sale of copper concentrate. Price sharing agreements are materially different to market-based contracts in the manner in which TCRCs are determined in that, under a price sharing agreement, the TCRC deduction is fixed for the duration of the contract as a negotiated percentage of the metal exchange copper price, so that the TCRC deduction and the metal exchange copper price are directly correlated to one another to remove the volatility of benchmark and spot TCRCs. Price sharing contracts do not provide for price participation and are not renegotiated annually but are typically set for the term of the contract.

83 Mr Wilson gave the following description of a price sharing agreement in his first report:

Price sharing, as the name suggests, is a mechanism that enables the concentrate seller (miner or trader) and buyer (trader or smelter) to participate in a percentage share of the copper price. Under a price sharing arrangement the TCRC is set as a percentage of the [London Metal Exchange] copper price. This percentage split is established through negotiation and the mechanism produces a TCRC fully correlated to the [London Metal Exchange] copper price. Under a price sharing arrangement, with concentrate processing charges effectively moving up and down in tandem with the income flow, this results in a lower TCRC when the copper price is low and a higher TCRC when the prices are high.

84 The 2006 Brook Hunt Report (of which Mr Wilson was the editor at the time) said of price sharing agreements that they are an agreement:

... in which the buyer’s fee is directly related to a percentage of the copper price. Typically, a minimum floor price exists below which the buyer’s fee does not change while above certain pre-determined prices the buyer’s participation becomes less within that price increment. The normal range of price sharing is 21-26%. Other terms and conditions are very similar to those in a standard market-related contract. Price sharing contracts provide another means of reducing the risk of large shifts in long terms TCRCs from one year to another. They are also reasonably equitable to both buyer and seller because when the copper prices are low, so too are the fees received by the buyer and vice versa.

85 Mr Ingelbinck agreed largely with this description.

86 Mr Wilson's evidence was that price sharing has several attractions to a miner, a purchaser and financiers in that, amongst other things, it allows for greater certainty of the projected cash flows for the mine/project as TCRCs are correlated with the income stream (that is, the London Metal Exchange copper price), thereby removing the volatility arising from the movement of the copper price and TCRCs in opposite directions, and makes the annual negotiating process easier because conditions applied to price sharing agreements are set for periods and not negotiated annually.

87 Mr Wilson also gave evidence that there is no standard price sharing contract. Amongst the contracts with a price sharing mechanism, some contracts have:

- a price sharing range between defined London Metal Exchange price caps and/or floors;
- percentages of price sharing that vary according to the London Metal Exchange copper price;
- a fixed percentage of price sharing regardless of the London Metal Exchange copper price; and
- annual price sharing escalators linked to a US GNP adjustment.

The spot market

88 The spot market for copper concentrate differs from the long-term market in that any tonnage can be sold at any time of the year. A spot sale can be initiated by sellers contacting buyers or *vice versa* or could be handled by a tender process or by private negotiation between the two parties. The prices and terms obtained in spot sales are highly dependent on market conditions prevailing at the time of the sale and the marketing and negotiating skills of the parties. Spot prices can be incredibly volatile and can vary greatly throughout a year. The TCRCs negotiated in spot contracts are more volatile than benchmark TCRCs in that they are especially driven by short-term market factors. In the period leading up to early 2007, spot TCRCs in some instances had exceeded, and in some instances had fallen well below, annual benchmark TCRCs, and had been as low as zero. There is also no correlation between the volatility of spot prices and the volatility of copper prices. The experts agreed that spot TCRCs are virtually impossible to predict and, as such, Brook Hunt does not try to forecast them.

Other components of a copper concentrate contract

89 Other reasonably standardised terms found in copper concentrate contracts relate to:

- the payable metal, or copper payable, in the copper concentrate;
- freight and insurance costs; and
- payment terms, including any prepayment terms.

The payable metal or copper payable in the copper concentrate

90 This is the negotiated percentage of the metal content of the concentrate to which the copper reference price, averaged over the quotational period, will be applied (as the smelting processes will generally not recover 100% of the copper in the concentrate).

Freight and insurance costs

91 These costs, as a matter of industry practice, are borne by the seller. The costs may be on a carriage insurance and freight (“**CIF**”) basis under which the miner/seller is responsible for arranging and paying for freight and insurance and managing the logistics involved in shipping and delivering the concentrate to the seller. Alternatively, the costs may be on a free on-board (“**FOB**”) contract where the responsibility for the goods moves from the seller to the purchaser when they pass the rail of the ship at the load point, but with a freight and insurance credit or allowance being charged to the seller based on prevailing or anticipated market rates to a given destination or destinations or discharge port. FOB contracts with such an allowance are often used where the miner does not have freight management or logistic capabilities and are generally economically equivalent for that miner to a CIF contract.

Payment terms

92 Copper concentrate contracts invariably provide that the seller will receive a provisional payment for the payable metals in concentrates which is reflective of the provisional estimates of the copper content and composition of the concentrate. If the customer is a smelter, the purchaser typically makes a provisional payment of 90% of the estimated value of the shipment, typically three business days after the arrival of the shipment at the destination port and following the exchange of various documents such as the bill of lading. If the customer is a trader, the provisional payment is typically made after an agreed number of days following receipt of the bill of lading and other documents. The seller gets a cash flow advantage of having the consideration paid earlier that might otherwise be the case.

MARKET KNOWLEDGE

93 It was common ground between the experts and, similarly, it was the evidence of Mr Kelly, that market participants, including miners, traders and smelters, access information in relation to the copper market and particularly the copper concentrate market from industry publications such as the Brook Hunt Reports (which Mr Wilson authored/edited for around 30 years). The Brook Hunt Report presents a global analysis of the market each year. Mr Kowal and Mr Ingelbinck both acknowledged that Brook Hunt is an authoritative resource and, whether accurate or not, influences negotiations in the copper concentrate market. Mr Kowal and Mr Ingelbinck each gave evidence that they relied upon Brook Hunt publications to support their opinions in these proceedings.

94 It was also common ground between Mr Wilson and Mr Ingelbinck that a mine producer and buyer would have regard to available information as to the state of the market as at 2007 and over the period 2007 to 2009 in deciding what terms to agree to at the start of 2007. In oral evidence Mr Ingelbinck said:

So the Brook Hunt Report is well recognised and well respected. It is one of a number – actually a fairly limited number of reports that are issued on this particular industry. There's only really two or three that are worth reading and I think Brook Hunt is probably the most respected. Mining companies are always faced with decisions as to what to do, what makes sense, what doesn't make sense. They will most certainly pay close attention to reports like the Brook Hunt Report. They will check and verify that there is – there appears to be a degree of consensus between the different reports issued by different independent parties.

They will – depending on how large the mining operation is and what their resource are – they will have done extensive work of their own to try and analyse where the market conditions are so they will look at various inputs to eventually make a decision as to whether a particular approach is more sensible than another approach.

95 Mr Kelly's evidence was to like effect, saying in cross examination that "we certainly reviewed the Brook Hunt Reports" though qualifying that "Glencore certainly had its own position" and would, from his experience, "calculate, quantify supply and demand, assess qualities on a quality by quality basis, form a view on credit, and – and trade around that as well".

COPPER MARKET LEADING UP TO 2007

96 The state of the copper concentrate market in late 2006 was considered by Brook Hunt in its 2006 Report and was also addressed by the mining industry experts in their reports. The following facts were not controversial.

97 During 2006, the average copper price had risen by more than 80% year on year to US\$6,279/t, which was four times the average copper price over the period 1998 to 2003 and, at the beginning of 2007, London Metal Exchange copper prices were at an all-time high. Mr Wilson described the increase in the average copper price in 2006 as “unprecedented”. Similarly, Mr Ingelbinck noted, “in recent history, the highest number had been the numbers that prevailed in calendar year 2006”. In cross examination, Mr Ingelbinck said that the 80% rise in copper prices in 2006 was “a somewhat unheard of event and caused all kinds of re-evaluations amongst industry participants as to what made sense and how to structure these agreements ... people were confused”.

98 Mr Wilson’s evidence was that, at the start of 2007, the trading on the forward market indicated an expectation of a material decline in copper prices, commencing in the second half of 2007 from what had been considered by the market (at the time) to be abnormally high levels. Brook Hunt’s estimates as at December 2006 of the London Metal Exchange price moving forward were that, for 2007, in money of day terms, the copper price would be around US\$2.70/lb, in 2008 US\$2/lb, in 2009 US\$1.34/lb and in 2011 less than US\$1/lb.

99 At the end of 2006, the Japanese benchmark TCRCs for the 2007 year were set at US\$60/dry metric tonne (“**dm**t”) and US6.0c/lb or US15.4c/lb for 30% concentrate, with price participation for benchmark TCRCs having been set at zero. The Japanese benchmark TCRCs for the 2008 and 2009 years would not be set until later in the 2007 and 2008 years respectively but were forecast to be around the same mark as follows:

Year	TC (\$/dm t Conc)	RC (c/lb)	PP (c/lb)	Combined(c/lbCu)
2007	60	6.0	0.0	15.4
2008	65	6.5	0.0	16.7
2009	60	6.0	0.0	15.4

100 Whilst the 2006 Brook Hunt Report stated that it was not clear whether price participation would, for later years, be reintroduced into long-term contracts, Mr Wilson and Mr Ingelbinck both gave oral evidence that, as at the end of 2006, it was their analysis of the market that it was highly unlikely price participation would be reintroduced in the 2008 to 2009 years.

101 At the end of 2006, spot TCRCs for 2007 were unknown and, the experts agreed, were volatile and inherently difficult to predict.

102 The Brook Hunt Report's analysis of the market forecast a shortfall of copper concentrate stocks relative to smelter demand in 2007. The Commissioner characterised the copper market as "turning around" in early 2007 to become a "seller's market", in which smelters required more concentrates than mines were capable of producing for at least two years and there was predicted to be a dramatic erosion of concentrate stocks. The taxpayer cavilled with that description, arguing that the 2006 Brook Hunt Report made it clear that the stock level predictions it provided were inherently uncertain, given the difficulties in estimating an appropriate "disruption allowance", and predictions about copper concentrate stocks could not be relied upon as a reliable gauge of market activity. The Report stated:

The copper concentrate market is notoriously complex and is driven by many variables. An understanding of the key variables and their influence on this market is critical in assessing the outlook for concentrate supply and demand and hence treatment and refining charges (TCRCs). All too often concentrate market projections are based solely upon forecasts of mine supply/smelter demand in isolation to these other variables, with the result that these forecasts are effectively meaningless.

103 Whilst Mr Ingelbinck disagreed with Mr Wilson about the reliability of market projections based on forecasts of supply and demand, both experts did agree that it was their analysis of the market as at early 2007 that balances for copper concentrates in 2007, 2008 and 2009 were likely to be tight and there was therefore an expectation that a significant increase in TCRCs was a relatively low probability. Mr Wilson's view at the time was that it was highly unlikely that TCRCs would go above US\$70 a tonne in the following three years.

BACKGROUND FACTS ABOUT GLENCORE

104 The background facts given by Mr Kelly about the Glencore Group and its operations in the copper concentrate industry were not contentious.

The Group's activities

105 The Glencore Group carries on worldwide operations in the natural resource industry, marketing and trading over 90 products, including copper concentrate, and holding interests across the world in industrial assets which include mines, smelters, refineries and infrastructure (including ports and rail). The evidence of Mr Kelly was that Glencore seeks to derive value from its investments in industrial assets by operating those assets, conducting marketing/trading activities in respect of the commodities produced by those assets and from the integration of these operational and marketing activities. Mr Kelly explained that by integrating its marketing activities with the industrial assets it invests in and operates, Glencore

can optimise the logistics required to process raw materials and deliver the end product to its customers.

Glencore's marketing division

106 Glencore's marketing team in the period between 2006 and 2009 had approximately 2,500 employees in 40 offices worldwide with responsibility for marketing commodities, selling commodities to smelters, arranging the logistics needed to deliver those commodities to buyers in accordance with Glencore's contractual obligations, performing quality control for the commodities that were purchased and sold, managing trade finance and generally managing the risks that Glencore was exposed to by virtue of the purchase and sale of those commodities. The logistics functions were performed by a group within the marketing department known as "Traffic".

Glencore's copper concentrate business

107 In 2006, Glencore was the largest seller of copper concentrate in the world. The copper concentrate which it traded originated either from mines it owned, or in which it held an interest, as well as mines owned by third parties.

108 Glencore's interests in mines in the relevant period included the CSA mine, which the group acquired in 1998. At the time of acquisition, the mine was not operative and was under care and maintenance. With the recommencement of mining operations in 1999, CMPL entered into an offtake agreement with GIAG for GIAG to purchase the entire production of copper concentrate for the life of the mine, and CMPL has since continued to sell its entire production of copper concentrate to GIAG under a series of replacement and amending offtake agreements (which are considered later in these reasons).

109 The evidence was that GIAG mostly sold the copper concentrate produced at the CSA mine in the relevant years to smelters in Japan, Korea, India, the Philippines and China. Mr Kelly's evidence was that the Asian market in 2006 to 2009 was (and remains) the biggest smelting market for copper concentrate and, in terms of seaborne trade, China then had (and it still has) the largest smelting capacity in the world, followed by Japan. The copper concentrate produced at the mine was warehoused on site and also in facilities at the Port of Newcastle to which it was transported by rail for shipping to the destination port nominated by the ultimate buyer. CMPL relied on Glencore's Traffic team to handle all the transportation and other logistics. Those logistics included locating available vessels to transport the copper concentrate from the

Port of Newcastle to the destination port, dealing with port issues, shipping delays and schedule changes, arranging letters of credit for the shipping, invoices and bills of lading, and managing the processes around the assays, including if the assays showed that the copper concentrate had not met the contracted specifications.

110 In addition to providing logistics support, between 1999 and 2009, Glencore, including through the support of a dedicated asset manager, provided ongoing assistance and expertise to CMPL in relation to CSA's operations. This assistance consisted of human resources contributions, mining expertise, as well as treasury services.

THE CSA MINE

111 The CSA mine is a high grade underground copper mine and copper concentrate plant located near the town of Cobar in New South Wales. Although in the relevant years it was the largest of the copper mines in the Cobar region, in relative terms it is a small mine. Mr Kelly deposed that by way of comparison some copper mines in South America (like Escondida) mine in a day or two what CSA mines in a year and, in 2006, the CSA mine's annual production of concentrate represented about 0.2% of world copper concentrate production.

112 During the relevant years, the mine's primary ore body, which was mined from an area known as QTS North, produced an homogenous copper concentrate of a consistently high grade. That ore body was comprised in a series of vertical lenses and was mined using the long hole open stopping method. Mr Kelly gave the following description of the steps involved in the mining operations:

- (a) mining of the underground stopes occurred at depths of about 1,400 metres to 1,500 metres;
- (b) vehicle and heavy machinery accessed the underground stopes via the decline, which was a road which descended into the mine from the surface in a corkscrew manner to a depth of about 1,400 metres to 1500 metres; regular worker and materials access to the mining operations was via a shaft that extended from the surface to a depth of 980 metres, and then via the decline to a depth of 1,400 metres to 1,500 metres;
- (c) the stopes, once accessed, were drilled and blasted;
- (d) once blasted, the ore was collected and transported in trucks to an underground stockpile located at a depth of about 980 metres;
- (e) from the stockpile, the ore was transported via the ore pass to a primary crusher and then to the surface via the vertical shaft;
- (f) once the ore reached the surface, the ore was transferred to mills where it was ground to a slurry;

- (g) the slurry was then pumped to a flotation tank to separate the different minerals which were skimmed from the flotation cells and then dried. This skimmed and dried material is the copper concentrate which the mine sold; and
- (h) copper concentrate produced at CSA was stockpiled before being transported by rail to the port at Newcastle from where it was then shipped to various ports in Asia.

113 In late 2006, mining also commenced in an area known as QTS South where the ore body was close to the surface but of a lower grade.

114 Mr Kelly's evidence was that:

- (a) the depth of the mine and the need to continue mining deeper into the ore body gave rise to significant technical and financial challenges for the mine and led to high operating costs. This was because the depth of the mine increased the complexity, time, effort and cost involved in extracting the copper ore from the mine face, getting it to the underground stockpile and then transporting it from the stockpile to the surface; the mine's depth required expenditure on infrastructure, extensive ground support and stabilisation regimes, as well as systems to provide adequate ventilation, power and air conditioning; and there were difficulties in accessing the deep underground stopes both to bring workers and equipment to and from the underground stopes and in transporting extracted ore to the surface and gave rise to congestion in the movements, as well as long trucking distances, restricting operations. Mr Kelly deposed that from at least 2004, CSA worked on projects with a view to making mining at depth more economical, including a proposal to extend the shaft to a depth of 1,500 metres;
- (b) the remoteness of the mine made it difficult to attract and retain employees and there were significant vacancies in key roles for long periods of time. For an 18 month period leading up to October 2007, there was no mine manager and at other times the mine manager changed regularly; and
- (c) the mine faced the issue of having enough water to support the mine's production. He explained that mining operations cannot occur without a water supply and Cobar is a dry town. Its main source of water is the Burrendong dam which caters for the greater Cobar region. The dam level fell to below 3% capacity in 2007 and there was not enough water to support the town, agriculture and mining. Priority was given to the town and agriculture and CSA was

required to find alternative water sourced by drilling for water, retreating water and trucking water to the site.

115 Mr Kelly was cross examined at some length on this part of his evidence, both as to his ability to give that evidence and in relation to whether these challenges inhibited the mine's performance in the relevant years.

116 It was put to Mr Kelly that he lacked the knowledge and experience to give evidence about the operations of the mine. Mr Kelly agreed that he relied on the technical mine management staff for the technical information, but he explained that he had experience in analysing operational reports first as an auditor of the CSA mine and later as asset manager during the relevant time. As he stated:

What I – what I would see and did participate in was all the financial related issues that came with operating at depth. The increase in costs relating to all the equipment and raw materials that went into mining at depth. The capital costs of sort of accessing that ore as well.

117 He was also a director of CMPL for some 10 years. He demonstrated a knowledge of the mine and there is no reason to doubt the reliability of the evidence he gave, which was corroborated by contemporaneous documents. Problems with ventilation, trucking distances, staff retention and water scarcity were all well documented at the time:

- (a) the 2007 budget and five year plan ("**2007 Budget**") (which was prepared around September 2006) evidenced that adequate ventilation and staff retention were issues for the mine at that time. The 2007 Budget expressly stated that a "key area of focus" of the CSA mine for the 2007 year would be "undertaking several projects to ensure the mine will have adequate ventilation for the future". Although no major changes were expected for the 2007 year, it was reported that "considerable project works" would commence "with planed [sic] major changes in 2008". Another key area of focus was listed as "[r]ecruiting & retaining the skilled people we need to ensure CSA operates safely and efficiently". With respect to staffing problems, the 2007 Budget reported over 20% vacancies in staff positions due to the "extremely difficult employment market" and noted that, in 2006, 43% of the staff employees left to take up new opportunities outside of CMPL and Cobar;
- (b) it is apparent from the mine's Operations Plan 2008–2012 (prepared in late 2007) ("**2008-2012 Operations Plan**") that an objective of the shaft extension

was to improve ventilation. The plan noted that the shaft extension was scheduled during the period 2008 to 2012 and would “[s]ignificantly reduce trucking distances in the mine which will allow a reduction in the number of trucks required” and, by reducing diesel trucks, would reduce the mine’s total ventilation requirements and “allow fresh air to be delivered to the lower sections of the QTS North section of the mine more efficiently”;

- (c) the 2008-2012 Operations Plan also noted under the heading “water supply” that:

With the continuing drought conditions of the Cobar region, the NSW state government has introduced restricted allocation to high security water users in our catchment. In order to deal with the possibility of reduced allocations in the future, CMPL has several contingencies to ensure the mine can still operate despite minimum raw water supply.

The document then outlined the contingencies and steps already taken. Despite these measures, the 2008-2012 Operations Plan noted that if the case worsened in the future, and the raw water allocation to the CSA mine site was significantly reduced or taken away, “drastic measures [would] need to be taken”. It stated that “[t]he first option [would] be to shut down the ore processing mill”.

118 It is noted also that whilst the CSA mine did not commit to the shaft extension in the years in question, the project was ultimately approved in 2011 or 2012 at a projected cost of \$300 million, albeit then abandoned in 2013 after in excess of \$170 million was spent because of safety issues.

119 The Commissioner contended that the fact that the CSA mine achieved record levels of production in 2006, 2008 and 2009 indicated, in any event, that the failure to extend the shaft did not inhibit the performance of the CSA mine in the relevant years. However, the contention disregards the evidence that CMPL spent significant capital in 2005 and 2006 on works to elevate mine production levels and improve the long-term productivity of the mine, which included commencing mining operations in the area known as QTS South in late 2006 to access an ore body close to the surface but of a lower grade ore. The 2007 Budget identified the completion of the QTS South development as another “key focus” for the 2007 year, with the expectation that it would be in full production in 2007 and “supplement output from the main operations in the QTS North area”.

120 I accept Mr Kelly's evidence about the depth of the mine giving rise to significant technical and financial challenges and that the mine in 2006 and 2007 was experiencing difficulties with staffing and water supplies. In addition, there was documentary evidence showing that the mine had experienced difficulties in the past with ground instability, such as stope failures and ground collapses. However, as the contemporaneous documents also evidenced, as at late 2006 and early 2007 the mine had plans and steps in place dealing with these matters and there was nothing in the contemporaneous documents which identified any uncertainty for the mine in relation to its capacity to continue mining in 2007, 2008 or 2009 or to suggest that CMPL considered that there was any real risk that its level of production would not continue throughout those years. Indeed, the review of the 2006 year set out in the 2007 Budget noted that mine production of ore in 2006 had increased by over 30% to 810,000 tpa and concentrate production in 2006 would be "an all-time record for CSA". It also stated that "this [had] been achieved even with high turnover in both staff and AWA positions and finishing the year with over 20% vacancies in staff position [sic] due to the extremely difficult employment market".

MINING COSTS

121 Mining costs are broken down into C1, C2 and C3 costs. In the 2006 edition of Brook Hunt's Copper Costs, Mines and Project – Summary and Analysis Report, C1, C2 and C3 costs are defined as follows:

- (a) C1 costs: the direct cash costs which include mining, milling and concentrating, on-site administration, smelting, refining, concentrate freight and marketing costs, amongst others, net of by-product credits (such as silver);
- (b) C2 costs: the C1 costs plus depreciation; and
- (c) C3 costs: the C2 costs plus interest and indirect costs.

122 The cash cost (C1) and total cost (C3) provide the cash margin and the operating margin of the mine respectively.

123 In oral evidence Mr Wilson (who was the co-developer of the C1, C2 and C3 costing analysis) described the difference between cash cost (C1) and total cost (C3) of a mine in the following way:

So the cash cost should be the sum of mining costs, processing costs, which would be milling, the on-site administrative costs, the cost of delivering product to the smelter plus the treatment and refining charges less any by-product credit so, for example, from

the CMPL perspective, that would be a silver credit of several cents a pound, so that would be the cash cost. The total cost would be the sum of the cash cost plus depreciation and amortisation of the mine plus various corporate-type overheads, like an assigned overhead might also include royalty payments, expiration charges, basically anything else that can be allocated to that mine so that would then give you a fully allocated total cost.

124 Based on the budgeted C1 and C3 costs for the 2006 year, in March 2007 Brook Hunt listed the CSA mine as being at the 83rd percentile of C1 costs of the total copper concentrate being produced and going into the market. On the actuals for the 2006 year, which were higher than the budgeted costs, Brook Hunt placed CMPL at the 89th/90th percentile, meaning it was a “high cost” mine. Brook Hunt defined a high cost mine as one whose competitive position places it at about the 75th percentile of the cost curve.

125 Mr Wilson’s evidence was that the high costs of the mine made CMPL vulnerable to fluctuations in gross revenue for its concentrate. Neither Mr Ingelbinck nor Mr Kowal gave contrary evidence.

THE CONTROL EXERCISED BY GIAG OVER THE CSA MINE

126 It was not in dispute, and there was clear evidence, that GIAG exercised financial and managerial control over the CSA mine during the relevant years.

127 In his role as asset manager of the CSA mine (whilst employed by GIAG) Mr Kelly undertook the following activities:

- (a) reviewing the mine's operating numbers and analysing them and liaising with the mine's general manager based on this analysis;
- (b) financial modelling to support the value of the mine;
- (c) assisting with the preparation of statutory accounts;
- (d) benchmarking CSA's costs against other similar assets owned by Glencore;
- (e) assisting with recruitment;
- (f) reviewing any capital expenditure projects and analysing them;
- (g) liaising with Glencore to obtain approvals for the capital expenditure CSA needed to fund new projects;
- (h) liaising with individuals within Glencore to assist CSA to deal with specialist issues that arose, for example, health and safety issues at the mine;
- (i) liaising with Glencore about the mine's insurance needs;

- (j) assisting CSA with implementing exploration programs to locate new sources of ore at the mine that were economical to mine;
- (k) liaising with CSA and Glencore about Glencore's involvement in the Cobar community; and
- (l) assisting CSA with general legal compliance.

128 In cross examination he said he also:

- (a) approved capital projects at the mine;
- (b) assisted in the compilation and review of the mine's budgets (for approval by Glencore); and
- (c) authorised the payment of cash calls from CMPL's current account facility with GIAG.

129 Mr Kelly explained that the current account facility is an intercompany account controlled by GIAG. GIAG uses the account to credit the payments in USD due to CMPL under the offtake agreement and when CMPL needs to access cash to meet operating costs in Australia, it makes a cash call to GIAG so that a nominated sum can be transferred into CMPL's Australian account. Mr Kelly deposed that he was not aware of any occasion when a cash call was not met by GIAG. GIAG also uses the current account facility for group purposes. For example, in 2006 GIAG took US\$100 million from the account to loan those funds to another group entity, Glencore Nickel, and then forgave the loan. Although the forgiveness was later reversed for tax reasons no entry was made in the current account facility reflecting the reversal. Mr Kelly was not involved in these transactions but he agreed that the forgiveness of the loan would have been a decision made by GIAG as well as the decision to reverse the forgiveness of the loan.

130 The Commissioner submitted that the fact that CMPL was making an advance of US\$100 million to another company within the corporate group, at least prior to the reversal of it, suggested that CMPL had considerable cash reserves and was regarded as being in a healthy cash rich position. It was submitted that there was no suggestion of any identification of vulnerability or uncertainty in relation to the financial position of CMPL at that point in time. The relevance appears to relate to the Commissioner's case that the Court should reject the contention that independent parties in the position of CMPL and GIAG might be expected to switch from a contract on benchmark terms to a price sharing contract in late 2006/early 2007.

If such evidence be relevant to the issues for determination, the evidence, however, must be viewed as a whole, which relevantly also includes the unchallenged evidence that in 2006, the CSA mine was a high cost mine in a period of extreme market volatility.

131 Mr Kelly's evidence also was that in his role as asset manager he was primarily focused on its financial performance so that he could report on its performance to the wider Glencore Group. He agreed in cross examination that he exercised financial control over the mine and did so "with a view to maximising profit for the Glencore Group" as a whole. The Commissioner also placed considerable reliance on this evidence in support of its primary case, to which reference is made later in these reasons.

132 For present purposes, it should be noted that it was not disputed that there were conditions operating between GIAG and CMPL which differed from those that might be expected to operate between independent parties dealing wholly at arm's length with each other, thus satisfying the requirement of s 815-15(1)(b) and I find on the strength of Mr Kelly's evidence that such conditions included GIAG's control and management of the CSA mine.

BUDGETS

133 Mr Kelly deposed that once a year, the management at CMPL presented a budget and five year plan for the CSA mine to Glencore for approval. This budget and plan was prepared each year around August or September for the following calendar year.

FINANCIAL PERFORMANCE OF THE MINE IN 2006

134 In 2006, the CSA mine achieved a record production of 140,452 dmt, but its operating costs (in AUD) exceeded the budgeted costs by 31% and the C3 costs (the total metal costs including capital costs) (in AUD) exceeded actual costs by 37%. Mr Kelly stated that although in 2006 the net profit and net revenue far exceeded budget, this was attributable to what turned out to be an increase in copper prices in 2006 which had not been forecast or budgeted.

135 Mr Kelly further deposed that by the end of 2006, it was apparent that management forecasts and budgets in previous years had been inaccurate. Mr Kelly explained that many of the operating costs were affected by matters beyond CMPL's control, such as fuel costs, electricity costs, tyre costs, mobile fleet costs and labour which had all increased in 2006. He agreed also that many of the costs of the CSA mine were also affected by movements in foreign exchange rates, such as the appreciation in the Australian dollar against the US dollar in 2006. As the 2007 Budget recorded, commercially the mine had performed well in 2006, due to record high

metal prices, but operating costs had been high, some due to external factors outside the control of the mine, such as fuel, power and cement increases and increased royalties due to higher revenue.

136 As a result of the unforeseen high copper price there was also a discrepancy between the actual TCRCs for 2006 and the budgeted TCRCs for that year. The actual TCRCs as a percentage of revenues was about 14.9%, whereas the budgeted TCRCs for that year had been 31.8% of the budgeted revenue for that year.

2007 BUDGET

137 The 2007 Budget:

- (a) set a copper price assumption of US\$2.54/lb for 2007 (compared to Brook Hunt's assumption of US\$2.70/lb) which it noted was "a conservative position, given the current market prices for copper and the outlook for the metal over the next 12 months";
- (b) budgeted for TCRCs at US16.7c/lb for 2007 (compared to Brook Hunt's assumption of US15.4c/lb) on the assumption that benchmark TCRCs would be used by the mine in 2007 and in future years. The Commissioner submitted that, significantly, in the 2007 year that indicated an expectation that TCRCs would continue to be determined by reference to the benchmark price and not by price sharing; and
- (c) forecast the unit cost mining to rise slightly on a tonnage basis and to fall slightly on a recovered metal basis.

138 For the year 2007 the estimates were of:

- (a) earnings before tax of AU\$157.7 million;
- (b) cash flow from operations of AU\$93.9 million, representing an operating margin of 30%, above the target of 25%; and
- (c) net cash flow after capital expenditure of AU\$46.3 million.

139 It was reported that cost control would be an important focus of the business in 2007.

140 The 2007 Budget expected an increase to mine production in 2007 but noted that concentrate levels would be lower due to a lower feed grade. This meant that a lower amount of copper metal was predicted to be produced in 2007 as compared to 2006. Consistent with the predicted

falling grade, the offtake agreement between CMPL and GIAG was amended on 2 February 2007 to reduce the copper content from 30% to 28.5%. Mr Ingelbinck observed that this was a recognition that the mine was seeing that the grade had decreased.

141 The 2007 Budget forecast for the 2008 year:

- (a) a copper price budgeted at US\$2.27/lb (compared to the Brook Hunt forecast of US\$2/lb); and
- (b) forecast benchmark TCRCs of US\$21.8c/lb (compared to the Brook Hunt forecast of US\$16.7c/lb).

142 The 2007 Budget forecast for the 2009 year:

- (a) a copper price budgeted at US\$2.04/lb (compared to the Brook Hunt forecast of US\$1.27/lb); and
- (b) forecast benchmark TCRCs of US\$19.2c/lb (compared to the Brook Hunt forecast of 15.4c/lb).

143 The Court was asked to find, and I accept, that the Budget was based on what, at the end of 2006 and start of 2007, both the mine and GIAG considered to be reasonable figures for both the copper price and the TCRCs for the coming years.

144 The Commissioner submitted that CMPL was forecasting significant profits would be realised by the CSA mine based on its financial assumptions. That submission can be accepted. The Commissioner contended that, consistent with its strong financial position, the Budget for the 2007 year had a positive outlook, forecasting that the mine would generate profits and have positive net cash flows, sufficient to meet operating and capital requirements, notwithstanding that the Budget was produced on the basis of a deliberately conservative price assumption. That was not Mr Kelly's view. In cross examination, Mr Kelly rejected the proposition that the 2007 Budget, viewed as a whole, reflected a "very positive picture". He stated:

I read these reports and I see increasing operating costs, increasing capital costs, falling grade, the need to expose alternative mining phases closer to surface because the geological risks at mining at depth – I see all of them identified in these reports as risks to mine so, no, I don't agree with you.

145 When put to Mr Kelly that there was nothing there to suggest that there was any identified risk as to production for the following three years, he disagreed, stating that:

There is. There's reference to increasing costs ... I think the management report does detail the capital forecasts required to access that ore. It outlines the increasing operating costs and the risks to those blowing out even further. It reports on falling recoveries, falling head grade in mine, falling copper concentrate grade produced. These are all things that the report specifically details. The mine plan, the budget going forward, specifically talks about all of these things.

146 Ultimately, as these reasons will elucidate, the issues that must be determined do not depend on whether the 2007 Budget, properly analysed, projected a positive outlook or something less rosy, as Mr Kelly indicated.

JANUARY 2007 MANAGEMENT REPORT

147 It appears that the change from the market-related offtake agreement to a price sharing agreement had an immediate negative financial effect. The January 2007 monthly management report, under the heading "Financial", stated:

January production was above budget for the month, despite lower than budget throughput, compensated by higher ore grade. Copper price has fallen substantially since the end of the last financial year, and CMPL still has open positions on a number of 2006 provisional invoices. **Revenue for January is down, as a result of low December stocks, sold in January, lower copper prices, 2006 shipments finalised at lower copper prices and the first effects of the new 2007 sales contract's price sharing agreement.**

January costs were in line with budget, but the overall result was well under budget, because of the revenue issues above.

(Emphasis added.)

148 Mr Kelly was asked questions in cross examination about the January 2007 monthly management report. Mr Kelly said that the monthly management reports are typically prepared early in the following month. When asked whether he was able to explain why the impact on revenue to CMPL of the price sharing agreement was recorded in the January 2007 monthly management report when the price sharing agreement was not entered into until 2007, Mr Kelly answered that he did not know.

2007 REVIEW IN THE 2008 BUDGET AND FIVE YEAR PLAN

149 The 2008 budget and five year plan, under the heading "2007 overview", reported that during the past year, the mine did not perform as well as expected. It was reported that "[t]urnover, increasing costs, lowering skill levels and under performance by contractors all contributed to a shortfall in the budgeted production". It also reported that employee turnover was still high but had dropped from previous years to just under 23% for the year.

150 Under the heading "Finance" it was reported that revenue in USD was 13% over budget for the year, with stronger copper prices more than compensating for lower sales. It was also reported that:

- the biggest impact on cost was the change to price sharing, rather than TCRC as previously budgeted; and
- cash flow remained strong with US\$103 million cash reserves at year end. However this exposure to a stronger AUD had resulted in unrealised exchange losses in the year of AU\$10.7 million.

PROJECTIONS WITH 23% PRICE SHARING AGREEMENT

151 In cross examination, Mr Kelly's evidence was that if costs were a main focus for 2007, it was "very reasonable someone would look to try and focus on the costs line because [CMPL] can't control the revenue line". His evidence was that:

... if you can put in place a formula that can take out that volatility in the treatment charge as a margin on your revenue line, then I think that's 100% what you would do. Just like what CSA might have considered doing with its fuel costs or its electricity costs or locking in the price of tyres going forward.

152 It was then put to Mr Kelly that it would fly in the face of the aim of cost control to agree to a TCRC figure of 23% when, on CMPL's own conservative assumptions, that cost was estimated to be 6.5% of the assumed copper price (US16.7c TCRC over US\$2.54 copper price). The following exchange occurred:

MR KELLY: No, I don't agree with you. I think that CSA or CMPL will consider many factors and in an environment where the ore body is getting deeper, they're spending more money to access it, the risk of being able to access it and recover all that's there with the stresses of the geology, all those factors ultimately drive their cost of mining upwards. That's one thing that they can influence over. They cannot influence on copper price. At that point in time, they've got a very unreliable budgeting process, they've been unable to accurately forecast and budget any of their production numbers or cost numbers. And I think if you look at treatment charge and refining charge as being a cost of production, which in effect it is because it's a reduction to revenue, then I think they would certainly look at putting in a formula that meant that that cost ultimately moved with the price of copper they were able to sell for. What it did do was lock in a margin whereby, yes, if the price went up, their treatment charges went up, of course that's how it worked and they were able to enjoy the benefits of a higher price. But likewise when a treatment charge as a percentage of the price goes down because the price is falling, they're able to manage their costs so they aren't exposed to that volatility. And in the 2005/2006 period, you've got this market where TCRCs had gone up and then gone down, tracking spot against benchmark, they had been volatile, you had a change in the way benchmark was being established at the end of 2006. You had no price participation included in it for 2007. You had Japan's influence in the market falling and China stepping up in terms of total

concentrates brought under benchmark. All these factors going on, you have a look at your operating costs on the market that you're referring to reference to, it is very reasonable someone has a look at trying to manage its costs versus any other alternative.

COUNSEL: But, Mr Kelly, why would you agree to something that's nearly four times what, on your own estimation, is the reliable costs you've put in your budget moving forward?

MR KELLY: Your calculations are based on a forecasted price that at the end of 2006, not one person, not one investment company, not one analyst was forecasting to continue any trend other than a downwards trend. I think the history of budgeting was such that – I think it's very reasonable someone would look to try and focus on the costs line because it can't control the revenue line.

COUNSEL: But, Mr Kelly, another thing you referred to then is all the risk moving forward but we just went through the executive summary. It's a very positive picture, contained metal resources continuing to increase each year. This is not a mine that is identifying in its guiding planning document any uncertainty as to its production moving forward, is it?

MR KELLY: No. I read these reports and I see increasing operating costs, increasing capital costs, falling grade, the need to expose alternative mining phases closer to surface because the geological risks at mining at depth – I see all of them identified in these reports as risks to mine so, no, I don't agree with you.

153 Mr Kelly agreed that for the 2008 year, based on the forecast copper price figure and TCRCs for that year in the 2007 Budget, the TCRC was around 9.6% of the forecast copper price. For the 2009 year, based on the forecast copper price figure and TCRCs for that year in the 2007 Budget, the TCRC was around 9.4% of the forecast copper price.

154 A line of cross examination then followed directed to showing that the decision to switch to price sharing left a margin for CMPL based on its budget for 2008 of only three to four cents per pound between the forecast costs and forecast copper price at 23% price sharing and put the viability of the mine at risk moving forward if fuel or other costs increased. A similar proposition was put for the 2009 year. Factually, the line of cross examination was directed to having Mr Kelly agree that the decision to switch to price sharing was one that would have rendered the CSA mine financially unviable based on its own budget and forecasts. Mr Kelly disagreed, saying that "it did the opposite" and "actually guaranteed the viability of it".

155 This line of cross examination was shown to be based on an incorrect premise as the Commissioner deducted forecast costs in AUD from forecast revenues in USD. The analysis in fact showed that the mine, based on its own budgets, would have predicted a healthy profit margin as at the end of 2006 based upon a switch to 23% price sharing in the following year.

156 I accept Mr Kelly's evidence that the switch to price sharing was one that might be expected to have "guaranteed the viability" of the mine. The taxpayer's unchallenged calculations of the margins for the 2007, 2008 and 2009 years of the 23% price sharing based on CMPL's forecasts in the 2007 Budget, correctly accounting for the currency difference in the line items, showed margins over total cost as a percentage of copper price and C1 cost as follows:

Budgeted margin over total cost as a % of copper price:

2007: 34.63%

2008: 25.39%

2009: 27.39%

Budgeted margin over C1 cost as a % of copper price:

2007: 39.09%

2008: 30.22%

2009: 31.51%

157 Mr Wilson described these margins as "healthy". Mr Wilson's evidence was that:

... the move to a price sharing contract in 2007 would have virtually guaranteed that a high cost producer such as CMPL would remain profitable even under a very low copper price environment as was forecast by Brook Hunt in 2009.

158 However, in cross examination, Mr Wilson agreed that if CMPL's aim was to be as profitable as possible, the commercially rational thing to do in February 2007 would have been to stay with the current terms, which were part benchmark and part spot TCRCs.

159 Mr Ingelbinck described the decision to shift to 23% price sharing as "irresponsible" because the 2007 benchmark TCRC for 2007 was forecast to be US15.4c/lb for 30% concentrate, whereas the projection at 23% price sharing was US63.25c/lb, more than four times higher than the 2007 benchmark.

160 Mr Kowal was similarly of the view that the change from benchmark to price sharing terms was difficult to justify commercially because of the increase in the TCRC cost based on the Brook Hunt forecast price for copper in 2007.

161 The differences in the views expressed by the experts are considered in detail later in these reasons.

TERMS AND CONDITIONS UPON WHICH COPPER CONCENTRATE WAS SUPPLIED BY CMPL TO GIAG

162 The first offtake agreement between CMPL and GIAG was entered into on 5 July 1999 (“**First Offtake Agreement**”), pursuant to which GIAG agreed to buy all of the concentrate produced by CMPL for the life of the mine. The terms of the First Offtake Agreement included:

- (a) CMPL agreed to sell and deliver, and GIAG agreed to buy and take delivery of, the entire production of copper concentrate from the CSA mine for the life of the mine starting from 1 July 1999;
- (b) GIAG was to pay for 96% of the copper content of the copper concentrate (subject to a minimum deduction) at the official London Metal Exchange cash settlement quotation for Grade A copper as published in USD in the ‘Metal Bulletin’ in London, averaged over the relevant quotational period, less the TCRCs;
- (c) a typical analysis of the quality of the copper concentrate produced was required to have a copper content of approximately 30%;
- (d) there was one quotational period for material produced after 1 July 1999, which was the month following the month of production, with this single quotational period to remain valid for the life of the mine;
- (e) the amounts to be deducted as TCRCs in respect of copper concentrate for the period between 1 July 1999 and 30 June 2000 comprised a treatment charge, a refining charge that was subject to an adjustment for “price participation” under which the charge would increase if the copper price exceeded a certain amount and would decrease if the price fell beneath that amount, and a penalty to be deducted when the bismuth content of the concentrates exceeded a certain percentage;
- (f) the amounts to be deducted as the TCRCs in respect of copper concentrate and freight allowances for each delivery year after July 2000 were to be negotiated and agreed prior to the commencement of the corresponding shipment based on the existing Japanese benchmark; and
- (g) if GIAG opted to take FOB Newcastle, then GIAG would be entitled to a freight credit as if the copper concentrate had been sold Cost Insurance and Freight

Free Out (“**CIFFO**”) Main Japanese Port, with the credit fixed for each contractual year.

163 The First Offtake Agreement was subsequently continued by the first replacement concentrate agreement (“**First Replacement Agreement**”), entered into on 1 October 2004. Relevantly, the First Replacement Agreement introduced quotational period optionality with back pricing as follows:

- (a) for shipments during October 2004 until December 2004, the quotational period for copper was, at GIAG’s option, one of three quotational periods to be declared on a shipment by shipment basis by, at the latest, the end of the second month following the month of arrival of the carrying vessel at the discharge port; and
- (b) for shipments from January 2005 onwards the quotational period for copper was, at GIAG’s option:
 - (i) one of two classes, each of three quotational periods, to be declared on an annual basis at the time of negotiation of the terms for the new contractual year; and
 - (ii) then, within each of those two classes, one of three quotational period options to be declared on a shipment by shipment basis by GIAG at a later time.

164 The First Replacement Agreement was continued by the Second Replacement Agreement, entered into on 1 January 2005. Relevant differences included the term that the amounts to be deducted as the TCRCs in respect of copper concentrate were to be negotiated and agreed between CMPL and GIAG in the form of an Addendum prior to the commencement of the corresponding year, based on 50% of the tonnage reflecting the Japanese benchmark and 50% reflecting the spot market. Price participation was also to be negotiated between CMPL and GIAG prior to the commencement of the corresponding year on the basis of the Japanese benchmark.

165 The Second Replacement Agreement was subsequently amended by addenda and amendment agreements entered into by the parties on 20 April 2005, 21 June 2005, 7 July 2005, 21 July 2005 and 5 December 2005.

166 A Third Replacement Agreement was entered into on 12 December 2005 which was subsequently amended by addenda and amendment agreements entered into by the parties on 2 March 2006, 14 August 2006, 2 February 2007, 3 February 2007, 23 April 2008 and 6 May 2009. The Third Replacement Agreement (before the 2 February 2007 amendment) contained the following relevant differences from the Second Replacement Agreement:

- (a) the quotational period was, at GIAG's option, either linked to the month of shipment of the copper concentrate or the month of arrival of the shipment, with the choice to be declared by GIAG on an annual basis at the time of negotiation of the terms for the new contractual year (1 January to 31 December). With either choice, GIAG had the option to select from three quotational periods with the quotational period to be declared on a shipment by shipment basis;
- (b) the TCRCs were to be negotiated annually for the term of the contract on a 50% benchmarked and 50% spot market basis; and
- (c) delivery was, at GIAG's option, either CIPFO main port Japan, Korea, India or China, or on basis FOB S.T. Newcastle, Australia, in which case a freight and insurance allowance was to be mutually agreed on an annual basis and credited to GIAG, 100% of which was to be deducted from GIAG's provisional payment to CMPL or in-warehouse, with the right to store material at the Cobar mine facilities.

167 The 2 February 2007 amendment changed the pricing structure for the copper concentrate that CMPL sold to GIAG from a "market-related" basis to a "price sharing" basis. It also relevantly further amended the manner in which the TCRCs would be calculated and the time within which GIAG was required to declare which of the groups of quotational period would be used to establish the copper reference price. The February 2007 Agreement provided that:

- (a) the election to be made by GIAG as to whether to link the quotational period to the month of shipment of the copper concentrate from the loading port of embarkation or the month of arrival of the copper concentrate at the port of disembarkation was to be made prior to each shipment from the loading port;
- (b) the TCRC was fixed for the 2007, 2008 and 2009 contractual years at 23% of the copper reference price based on the quotational period declared by GIAG for each shipment multiplied by the final payable copper content of the copper concentrate; and

- (c) price participation was not to apply for the 2007, 2008 and 2009 contractual years.

168 The February 2007 Agreement also relevantly provided for a reduction in the level of approximate copper concentrate to 28.5% (from the 30% which had previously been specified).

169 The Commissioner's case was that the First Offtake Agreement under which CMPL sold copper concentrate to GIAG in 1999 was structured generally in accordance with the industry standard benchmark terms. It was argued, however, that as the financial performance of the CSA mine improved, the terms on which CMPL sold copper concentrate produced at the CSA mine were changed in favour of GIAG and at the expense of CMPL. It was argued that the following terms in the February 2007 Agreement affected the amount that CMPL was paid by GIAG for copper concentrate produced by the CSA mine and differed, in GIAG's favour, from benchmark terms:

- (a) the way in which quotational periods were to be determined for the purposes of calculating the applicable copper price;
- (b) the way in which the deduction for combined TCRCs was calculated; and
- (c) the way in which the freight and insurance allowance was determined if GIAG opted to take delivery of the concentrates FOB at the Port of Newcastle, Australia.

170 It was argued that the provisional payment terms may also have diverged from typical benchmark terms, but only in relation to the time at which the payment was to be made, not the quantum of the payment. The Commissioner also submitted that other terms in operation between the parties, such as those related to the percentage of payable metal and to the procedure for assaying the copper concentrate purchased, diverged from terms that might have been expected to have been agreed between independent enterprises dealing with one another at arm's length, but the Commissioner did not seek any determination from the Court as to whether or how those terms affected the price payable under the offtake agreement.

171 No evidence was adduced by the taxpayer about the negotiation of the February 2007 Agreement and the Commissioner urged the Court to draw a *Jones v Dunkel* inference from the failure of the taxpayer to adduce such evidence that the uncalled for evidence would not have assisted the taxpayer's case because it would have revealed the absence of any negotiation of the terms of the Agreement. Such an inference is unnecessary, however, as the taxpayer did

not put into issue whether, nor did it contend that, the February 2007 Agreement was a negotiated agreement and an arm's length dealing.

MR KELLY'S EVIDENCE ABOUT THE LOGISTICS AND RISKS FOR CMPL IN SELLING ITS COPPER CONCENTRATE IN THE PERIOD 2006 TO 2009, IF INDEPENDENT OF GIAG

172 Mr Kelly gave evidence about what was likely had CSA sought to sell its copper concentrate directly to smelters. I observe that much of this evidence was irrelevant because it ignored the corporate relationship completely and, thus, did not engage with the statutory questions for determination under Div 13 and Subdiv 815-A. As *Chevron* made clear, the object of the comparable analysis is to determine what consideration might reasonably be expected to have been received by CMPL for the copper concentrate that it sold to GIAG in the relevant years had those parties been independent of each other and dealing at arm's length. The hypothesis of an agreement is one that was not affected by the lack of independence and lack of non-arm's length dealing, not of an abstract agreement between abstract independent parties, ignoring the corporate relationship and approaching the task on the premise that CMPL was a standalone miner. In this case, as a subsidiary of a multinational commodity trading group selling all of its copper concentrate to GIAG for the life of the mine, CMPL did not have, and had no need for, any marketing department or agency agreement in place to market its copper production, nor did it have to arrange the logistics required for transporting its copper concentrate to any overseas destination as this was all done by Glencore's Traffic team. In those circumstances, the consideration that might reasonably be expected to be received by an independent seller of copper concentrate in the position of CMPL must therefore be determined on the hypothesis of an independent buyer of copper concentrate in the position of GIAG acquiring the whole of CMPL's copper concentrate for the life of the mine and providing logistical and marketing support to the seller of the copper concentrate, and on the hypothesis of an independent seller of copper concentrate in the position of CMPL selling the whole of its production of copper concentrate to an independent buyer for the life of the mine, and with no need for a marketing department or logistics expertise. However I should refer to Mr Kelly's evidence for the sake of completeness.

173 Mr Kelly gave the following evidence in his first affidavit about what was likely had CSA sought to sell its copper concentrate directly to smelters:

Identification of potential smelter customers

163 For a miner, particularly one with limited in-house marketing skills, one of the

significant advantages of a longer term offtake agreement with a purchaser of its commodity is that it monetises a specific volume of production (in some cases, all or a given proportion of the mine's production). That is, such an offtake agreement provides the miner with the security that the relevant agreed volume of its production will be lifted and sold. It also provides the miner with a regular and reliable cash flow (assuming the creditworthiness of the relevant buyer), and enables the miner to concentrate on production, without the risk of not being able to place its tonnages into the market. This is particularly advantageous where the miner produces a commodity for which supply and demand fluctuates and price is volatile.

164 Had the Offtake Agreement with GIAG not been in place between 2006 and 2009, it is unlikely that any one smelter would have agreed to enter into a long term agreement to purchase all or a significant proportion of CSA's tonnage. That is because smelters will, and between 2006 and 2009 would, typically purchase copper concentrate from a number of different producers in an effort to:

- (a) minimise the impact of the producer not being able to supply the required tonnages in a particular month (for example, because of issues with production or an employee dispute);
- (b) minimise the impact of there being a delay in the arrival of any given shipment at the disembarkation port; or
- (c) obtain copper concentrates of different qualities, which might be blended by the smelter to manage its feed requirements.

165 If CMPL had sought to sell its tonnages directly to smelters in the period 2006 to 2009, it would have likely been required to contract with number of smelters in order to move all of its available tonnage. Based on its forecast production tonnages in 2007 to 2009, I expect that CMPL would have had to sell to 3 or 4 different smelters and keep back approximately 10,000 tonnes to have "in reserve" in case there were any unplanned disruptions to its production schedule.

Terms of hypothetical smelter sales

166 Had CMPL managed, despite its limited marketing expertise, to sell the copper concentrate produced by CSA between 2006 and 2009 directly to smelters, then such sales would have been by way of long term offtake agreements and/or short term or spot sales. It is likely that each of the long term offtake agreements would have been different, and would have included different [quotational periods]. For example, the smelter could have specified:

- (a) M+1 or M+3;
- (b) 2MAMA or 3MAMA; or
- (c) M+1 or 2MAMA.

167 If the sales had been made on the spot market, then the smelters would have bid for the tonnages on specified terms that would have typically included the [quotational period] the smelter required for the sale. If CMPL was considering a number of bids, it is likely the different bids would have had different [quotational periods].

Risk of hypothetical smelter sales

- 168 Had CMPL sought to sell its copper concentrate directly to smelters in the period 2006 to 2009, its ability to place its product would have been impacted by any disruptions to processing at the purchasing smelters. For example:
- (a) the purchasing smelters may have reduced their consumption (possibly entirely) during periods of planned maintenance; and
 - (b) the smelters may have been impacted by unforeseen events such as fires, earthquakes, floods or unplanned downtime caused by technical issues experienced at the smelter and may have declared a force majeure event under the offtake agreement. (By way of example, in the last 6 years, the PASAR smelter in the Philippines has been closed for 6 months because of a fire in its acid plant, for 6 months because of a typhoon and for 1 month because of an earthquake.) In these circumstances, the smelter would not have been obliged to take unshipped copper concentrate and CMPL would have been forced to sell it on the spot market.
- 169 Further, CMPL would have been exposed to any changes in import regulations in the jurisdiction where the purchasing smelters were located. If such changes were drawn to CMPL's attention after the copper concentrate had been shipped, the vessel carrying the copper concentrate could have needed to be diverted to a Port that would accept the copper concentrate and there would be a delay in CMPL receiving payment from the smelter for that cargo (as payment is typically made after the vessel arrives at the receiving port). Further, if the vessel had other cargoes on it, CMPL would have been responsible for paying demurrage until another Port could be found that would accept delivery of the copper concentrate (if another Port could be found).

Payment on Production

- 170 Apart from the Offtake Agreement between CMPL and GIAG referred to above, I am not aware of any other offtake agreement for copper concentrate between 2006 to 2009, or since, with a prepayment provision that requires the buyer to pay the seller 100% of the provisional value of unshipped production tonnage within a number of days following production. Had CMPL not entered into the offtake agreement with GIAG, it would only have received payment for concentrate upon arrival at the receiving port and would have borne the risk of delays in shipping. The provisions of the GIAG Offtake Agreement that provided for payment 14 days after the end of the month of production provided CMPL with a steady cash flow, regardless of whether it was able to ship its concentrate.
- 171 The facility for payment on production also provided CMPL with certainty about its cash flows each month and the knowledge that its operational costs could be met.
- 172 Although there were no major delays in the shipment of CSA's copper concentrate during the period between 2006 and 2009, this was not something that was known at the end of 2006. At this time there was, as is always the case for a producer, a risk that CMPL's shipments of concentrate could be delayed. This has in fact been a problem for CMPL in recent years when the moisture content of up to 60,000wmt (which, in 2007, had a value of in excess of US\$100 million based on a copper price of \$3.17 per payable pound) of copper concentrate was too high, which meant that it was incapable of being

shipped. The copper concentrate has been outside the quality specifications contained in the Offtake Agreement and, contractually, CMPL has not been entitled to receive any payments from GIAG under the Offtake Agreement. Regardless, CMPL has been paid for its production 14 days after the end of each production month.

174 In his second affidavit Mr Kelly further deposed that between 2006 and 2009, the CSA mine was producing about 150,000 tonnes of copper concentrate each year and, in his experience, it was unlikely that any one smelter would have purchased 100% of this tonnage. He also gave evidence that there were risks associated with any disruptions to the planned shipping schedule and delays may have an impact on price, the timing of the payment to CMPL and, if CMPL was not able to deliver copper concentrate to its customer in accordance with its contractual obligations, the smelter may be able to terminate the contract. He also explained that there was a risk that a force majeure event may intervene and affect any unshipped material. He said that the risk of a trader under an offtake agreement being able to call force majeure was significantly less than the risk of a smelter being able to call force majeure. If the force majeure event went on for a specified period of time, it would allow the smelter to cancel any unshipped product and, if it went for a longer period of time, it would allow the smelter to cancel the contract. In both cases CMPL would need to sell the product that was destined for that smelter on the spot market in which case CMPL would bear the risk of the spot market terms not being as favourable to it as the terms under the contract the subject of the force majeure event. Further, he gave evidence that if CMPL was selling its copper concentrate directly to smelters, it would be impacted by any disruption to processing at the smelter and it would need to mitigate that risk by selling to a number of smelters in a number of different countries so that the impact of a disruption or change in import regulations affecting one of its smelters was minimised.

175 He also gave evidence that if CMPL did not sell all of its copper concentrate to GIAG or one of its trading competitors, it would have to have had to establish a function to perform the following tasks:

- marketing: it would need people with worldwide marketing expertise who understood the copper market and knew the global buyers and sellers to sell its copper concentrate into the global market;
- it would need people to arrange for the logistics necessary to ship its copper concentrate and need people to arrange booking vessel space, assays and insurance; and

- it would need people to arrange for invoicing and collection of payments and would also need a management accountant to manage credit risk and someone to head foreign exchange and trade risks.

176 He stated that in his experience it would not be economically feasible for a mine such as CSA to have established a team with the relevant expertise to bring its concentrate into the market. From a commercial view point its most realistic option was to sell to a trader and, by agreeing to sell off all of its production to a single trader, CMPL was assured of a market for all of its production. He stated that by having an offtake agreement with a trader like GIAG, CSA could focus on mining and overcoming the cost/efficiency issues because GIAG took full responsibility and risk for marketing the copper concentrate and delivering it into the global market, and also managing the variable production.

177 Mr Kelly was extensively cross examined on this evidence. Mr Kelly agreed in cross examination that he had not personally negotiated the terms of a copper concentrate agreement as at 2007 and, at that time, had no experience in negotiating an offtake agreement on behalf of a mine producer with a smelter. He agreed he could not say what a smelter might have offered CMPL for its copper concentrate in 2007, nor what terms would have been agreed. He also agreed that he could not say what terms CMPL might have been able to negotiate with a shipping agency in 2007. However his evidence was that CMPL could not have marketed, or organised the logistics for the transport of, its copper concentrate without experienced teams which it did not have at the time.

178 He was also challenged on his evidence that it would not be economically feasible for a mine such as CSA to have established a marketing/logistics team with the relevant expertise. Mr Kelly agreed that CMPL made very significant profits in 2006 but said that was simply on the back of the all-time high copper price and that operating costs had gone up, the copper grade of the mine was reducing and capital costs were increasing. His evidence was that:

MR KELLY: So whilst they were profitable, extremely profitable, sure. It was simply on the revenue line, and I think, at that point in time, the belief of everybody was that whilst they were historical prices, historically high prices, they were not – there was no longevity in them.

COUNSEL: I'm just interested - - -?

MR KELLY: They were going to retreat to a – sorry, they were going to retreat to more historical levels. And at those levels, CMPL was, you know, perhaps uneconomical, especially if grade continued to fall like it was.

...

MR KELLY: As at the end of 2006, the industry's view – my view included – was that copper prices were not going to remain at those levels. So whilst they sat on a significant amount of cash, they had a significant amount of capital required to – for the mine's longevity. They had increasing operating costs and sought the additional costs to go and employ a new commercial team in light of that market were deemed to be uneconomical. Not – uneconomical.

179 Mr Kelly then agreed that he had no experience of what it would have cost CMPL to employ someone with marketing expertise in the context of a commercial team in a mine nor knowledge of what, in January or February 2007, it would have cost CMPL to engage a logistics team, or what it would have cost CMPL to engage a management accountant and someone to hedge foreign exchange and trade risks. When put to him that there was no basis for his evidence that it would not be economically feasible for a mine such as CSA to have established a team with the relevant expertise to bring its concentrate into the market, he disagreed.

180 The Commissioner submitted that Mr Kelly's evidence that it would not have been economically feasible to employ staff to perform the marketing and logistics functions was shown to be without foundation. It was also submitted that the market for concentrate in late 2006 was a seller's market, in which smelters required more concentrate than mines were capable of producing for at least two years, and there was predicted to be a dramatic erosion of concentrate stocks. It was submitted that, having regard to market conditions prevailing in late 2006 and early 2007, the risk of CMPL not finding a buyer of its product at that time would have been slight.

181 The short point to make in response to the Commissioner's submissions is that as a standalone company, without the support of GIAG, CMPL could not have sold its copper concentrate, whether to a trader or to a smelter, without its own marketing and logistics teams or engaging third parties for that purpose and, it may reasonably be inferred, would not have had the same negotiating and bargaining power as GIAG, whether or not a seller's market. The Commissioner's submissions also highlight the misdirection both of the affidavit evidence given by Mr Kelly on this subject matter and of the cross examination. CMPL was not a standalone miner in the relevant years. As made clear in *Chevron*, the task of ascertaining the consideration that might reasonably be expected would have been paid to CMPL for the copper concentrate that it sold to GIAG is not to be undertaken upon the hypothesis that CMPL was not a member of the Glencore Group. As Pagone J cautioned at [130], to do so would distort the application of Div 13 and fundamentally undermine its purpose of substituting as a comparable a real world arm's length consideration which could predictably have been agreed

between them on the hypothesis that they had been independent and dealing at arm's length. In the present case, the relevant mine producer for the purposes of the hypothetical agreement is a mine producer with all the characteristics of CMPL, which include, as earlier stated, that it had no need for a logistics or marketing division because it sold the whole of its production for the life of the mine to a buyer with GIAG's characteristics, namely a trader with a substantial marketing team which purchased the whole of the mine's production for the life of the mine.

182 Mr Kelly's evidence was, however, relevant insofar as it identified further commercial relations that operated between CMPL and GIAG which differed from those that might reasonably be expected to operate between independent enterprises dealing wholly independently with one another, namely:

- (a) GIAG undertook all the marketing and logistics to sell the CSA copper concentrate production on the global market and assumed the whole of the risk of on selling; and
- (b) the requirement for GIAG to pay CMPL 100% of the provisional value of unshipped production tonnage within a number of days following production, whether or not the concentrate was shipped, which meant that GIAG bore the risk of delays in shipping.

183 It also identified the benefits to CMPL of the contract:

- (a) it monetised the whole of the production of copper concentrate for CMPL;
- (b) the facility for payment on production provided CMPL with certainty about its cash flows each month and the knowledge that its operational costs could be met; and
- (c) CMPL had no need of a marketing or logistics department because that was all done by GIAG.

MINING INDUSTRY EXPERT EVIDENCE

184 It is useful at this juncture to review the mining expert evidence.

Joint mining industry experts' report

185 The three experts met in conference for the purpose of identifying the matters in their respective expert reports where they were agreed, where they disagreed and their respective reasons for that agreement and disagreement.

186 The experts were in agreement that:

- TCRCs can be fixed or benchmark based;
- TCRCs can be part benchmark and part spot market-based;
- combined TCRCs can be determined on a price sharing basis;
- quotational periods can be fixed and be at a party's option;
- an offtake agreement can have multiple quotational periods with optionality;
- one of the parties can be granted quotational price optionality;
- an independent seller of copper concentrate in the position of CMPL might be expected to have agreed to multiple quotational periods; and
- the impacts of quotational period optionality on a seller can be both positive and negative depending on the market circumstances, and are not directly related to the gains, if any, realised by the buyer and it is almost impossible to determine the actual value received by the seller and the buyer as in some instances the seller wins and in other instances the buyer wins.

187 They also agreed that there was nothing in the pricing or quotational period clauses of the February 2007 Agreement that did not also exist in contracts between independent market participants, though Mr Ingelbinck qualified that context and timing are critically important to determine what might reasonably be agreed between independent parties in similar circumstances as existed between CMPL and GIAG.

188 The experts summarised their differences and reasons for their differences as follows.

189 With regard to whether independent sellers would have switched to a 23% price sharing agreement:

- (a) Mr Wilson's opinion was that it was both prudent and reasonable for CMPL to have switched from a mix of benchmark and spot TCRCs to price sharing, pointing to the fact that in 2006 the CSA mine was very high cost and price sharing removed the uncertainty of large movements in benchmark and spot TCRCs. Based on Brook Hunt's price forecasts made in December 2006 for 2007, 2008 and 2009, the CSA mine would have been profitable and viable, and in his opinion it was more important for the mine to remain viable, rather than

whether or not price sharing would have produced a better or worse profit for the mine.

- (b) Mr Kowal and Mr Ingelbinck were of the opinion that the switch to a 23% price sharing agreement would not improve the profitability or viability of the mine relative to what it had been under a continuation of benchmark TCRCs (with or without a modest spot component), even assuming increases in the 2008 and 2009 TCRCs to match what they were in 2006 (which had not been forecast by any market analysts), and the only beneficiary from the price sharing contract would have been GIAG in 2007 and 2008. As such they were of the opinion that independent sellers in similar circumstances would not have agreed to such a switch.

190 With regard to the 2004 contractual amendment to include quotational period optionality with back pricing:

- (a) Mr Wilson accepted that quotational period optionality with back pricing was far less common in offtake agreements but, of the three contracts with quotational period optionality with back pricing he had reviewed, it was not clear to him that any obvious value was placed on back pricing.
- (b) Mr Kowal and Mr Ingelbinck were of the opinion that the back pricing which was introduced in the First Replacement Agreement entered into in 2004 should never have been entered into by CMPL as it provided substantial (but not necessarily quantifiable) value for the trader for which there was no quid pro quo. The amendment in 2007 for quotational period back pricing on a shipment by shipment basis was said by them to be an additional advantage for GIAG for which there was no quid pro quo.

191 Mr Wilson and Mr Kowal both attempted to quantify the magnitude of the total negative impact of the quotational period optionality with back pricing for the years 2007 to 2009 on CMPL's net revenues in those years, assuming GIAG as buyer had been limited to selecting one early or one late quotational period in each year rather than on a shipment by shipment basis including back pricing. Both analyses were based on hindsight. On Mr Wilson's analysis, the outcome may not have been significantly different. Depending on the quotational period selected, the difference was approximately US\$10 million (on Mr Wilson's analysis) compared with US\$85-\$100 million (on Mr Kowal's analysis).

192 The joint report also included six worked examples prepared by Mr Ingelbinck to demonstrate the impact of the type of optionality that was incorporated into the contract between CMPL and GIAG in the form in which it was restated in the Third Replacement Agreement dated 12 December 2005. The examples showed a wide variety of possible outcomes which ranged from breakeven to significant profits for the buyer and both positive and negative possible outcomes for the seller depending on the quotational period selected. Mr Ingelbinck said of those worked examples that:

The impact of the broad type of back pricing optionality that was incorporated in the CMPL-GIAG contract starting in 2004 was at worst neutral and in most cases very beneficial for the party that has been granted the optionality.

The impact on the party that has granted the optionality is less easy to define and can vary significantly.

Mr Wilson's evidence

193 In response to the question:

Whether the conditions (individually or together) that operate under the 1999 offtake agreement as amended from time to time and including as amended by the [Third Replacement Agreement] (together with its Addendums and Amendment) as they applied in the 2007 to 2009 calendar years differ from those that might be expected to operate between a producer/seller of copper concentrate in the position of [CMPL] and a purchaser independent of CMPL having regard to the circumstances of CMPL in the period 1999 to February 2007 -

Mr Wilson's opinion was that the conditions both individually and taken together under the contractual arrangements between GIAG and CMPL as they applied in the 2007 to 2009 calendar years did not (with the exception of the payment terms) differ either in respect of their contractual terms or in respect of the expected financial impact of those terms from those conditions that might be expected to operate between a producer/seller of copper concentrate in the position of CMPL and a purchaser (including a purchaser having substantially the same characteristics as GIAG) which is independent of CMPL.

194 The payment terms concerned the obligation on GIAG to pay for 100% of the provisional value of any concentrate produced but not shipped 14 days after the end of each production month against the presentation of various standard documents. In Mr Wilson's opinion, this term not only provided CMPL with interest free working capital, but more significantly provided CMPL with a reliable monthly cash flow and relieved it from the risk of being unable to ship concentrate after production. In Mr Wilson's opinion, the payment terms were clearly advantageous to CMPL.

Price sharing

195 Mr Wilson's opinion was that it was reasonable and prudent for a company in the position of CMPL, as the operator of a high cost mine with C1 costs placing it on the 90th percentile of copper mine costs, to replace the TCRCPP formula with the 23% price sharing formula which it adopted in 2007. Mr Wilson reasoned that market sentiment was predicting a steep decline in London Metal Exchange prices from US\$2.70/lb in 2007 to US\$2/lb in 2008 and down to US\$1.27/lb in 2009. He pointed out that the TCRC market was highly volatile and that, in 2004, the TCRC was US13c/lb and, in 2006, it had trebled to US46c/lb. He explained that the switch to price sharing terms in 2007 removed one of the two unknowns by eliminating the volatility of TCRCs and, for a mine concerned with cost, if the mine could have guaranteed on the basis of Brook Hunt's price forecast it would still would have been profitable, that would have been a very strong commercial incentive to switch to price sharing. He stated that, on the basis of its own cost budgets, it would have still made money at Brook Hunt's US\$1.27/lb price forecast for 2009.

196 In his second report, Mr Wilson elaborated:

In considering the shift away from a long-term/spot market contractual arrangement to price sharing in 2007, I would reiterate what I stated in my previous report that as a high cost mine with C1 costs placing it on the 90th percentile of copper mine costs, it remains my opinion that it was commercially reasonable and prudent for CMPL to have adopted this mechanism. In the end, the adoption of a price sharing arrangement such as that which was adopted by CMPL is a matter of commercial judgment having regard to the particular risk appetite and cost pressures facing a particular mine.

The use of full price sharing terms as set out in the CMPL-GIAG Contract in 2007 removed one of the two unknowns by eliminating the volatility of TCRCs. The absence of a price sharing floor gave CMPL added protection as the buyer was not guaranteed a minimum share of the price. It also meant that CMPL would have known precisely at any time during this three year contract what CMPL's net price would have been for any given copper price. Put another way, by fixing the TCRC at 23% of the copper price CMPL would have known with a high level of certainty the breakeven copper price for the CSA mine in each of the three years through the fixing of the TCRC. In my opinion, this is particularly important for a high cost mine such as CMPL which can quickly move into a loss position as copper prices decline (as was anticipated by market commentators in late 2006 and as shown by the [London Metal Exchange] forward price curve for copper). Although it is apparent in hindsight that copper prices did not decline significantly over the three year period, benchmark TCRCs did not increase significantly, and price participation was not reintroduced, the use of the price sharing arrangement was, in my opinion, a conservative and reasonable approach to minimising risk. If copper prices had fallen significantly over the three year period and TCRCs had increased, CMPL could have endured serious financial difficulties

197 Mr Wilson also noted that typically in a price sharing agreement a minimum floor exists below which the buyer's fee does not change, but the February 2007 price sharing arrangement did

not have such a minimum floor. It was said by Mr Wilson that the absence of such a term provided further protection to the seller in that, as the copper price fell, CMPL's revenue would also decline proportionately but, if there was a floor, it would decline disproportionately and by a greater amount.

198 Mr Wilson's evidence was that between 2007 and 2009, the normal range of price sharing was 21-26%. In his experience the lowest price sharing contract was 20%.

199 Mr Wilson was tested on the opinion he expressed that it was reasonable and prudent for a company in the position of CMPL, in February 2007, to agree to a three year 23% price sharing agreement.

200 He was asked whether he agreed if, in 2007, there was an escalation of operating costs above projected costs as there had been in 2006 of around 30%, a decision at the start of 2007 to adopt a 23% price sharing agreement would put the financial viability of the CSA mine at risk. Mr Wilson disagreed that a hypothetical mine producer like CMPL would have had a concern about costs escalating in 2007 as he believed that cost escalation had peaked but, on the assumption he was asked to make, namely that CMPL had a concern that costs may escalate in 2007, Mr Wilson did agree that the decision to adopt a 23% price sharing agreement would put the financial viability of the mine at risk.

201 Mr Wilson was asked whether, if the hypothetical mine producer followed the Brook Hunt forecast at the end of 2006, it would be highly likely that the mine producer would be worse off financially by agreeing to a three year price sharing agreement instead of remaining on the terms they had at the start of 2007. He agreed with that proposition.

202 Mr Wilson was asked whether he agreed that according to CMPL's own forecasts it was highly likely that it would be worse off by going to a 23% price sharing agreement rather than remaining with the terms as at the start of 2007. He agreed with that proposition.

203 However, Mr Wilson maintained it was reasonable and prudent for CMPL, in February 2007, to switch to the 23% price sharing agreement because CMPL in 2009 could have guaranteed, under a 23% price sharing contract, it would have remained profitable and covered its cash production cost. He confirmed his opinion that even if CMPL went to 23% price sharing in February 2007, it was likely to remain profitable. But when asked whether he agreed if CMPL's aim was to be as profitable as possible, the commercially rational thing to do in

February 2007 would have been to stick with the current terms, which were part benchmark and part spot, Mr Wilson replied that he did agree.

204 Mr Wilson also agreed in cross examination that there was not one instance reported in Brook Hunt of a mine that had an existing long-term offtake agreement with a trader changing the terms from benchmark to price sharing; and agreed that he did not know of any instance of a price sharing agreement being entered into in 2007 by a mine; nor was he aware of any mine in current production entering into a price sharing agreement in respect of 100% of its production, nor one that was limited to a three year period.

205 In re-examination, the taxpayer's calculations of the budgeted margin (which the Commissioner did not contest) were put to Mr Wilson and, when asked what he said to the proposition that going to a 23% price sharing agreement put the viability of the mine at risk, Mr Wilson replied that he thought the margins "look pretty healthy" for a high cost mine and, as at 2007, the margins were "pretty well in line with what [he] would expect to see".

Quotational period optionality

206 Mr Wilson did not specifically address the quotational period optionality with back pricing clause in the February 2007 Agreement in his first report. Rather his evidence was about quotational period optionality generally.

207 In response to Mr Ingelbinck's evidence about quotational period optionality, Mr Wilson stated that traders typically include quotational period optionality in an offtake agreement. He explained that the trader will normally on-sell the product to smelters under both long-term contracts and spot sales which will inevitably have a variety of quotational periods and TCRCs, with the consequence that if the trader purchases concentrate under an agreement with a fixed quotational period and sells to smelters on the basis of various quotational periods, it will bear the price risk resulting from different quotational periods. Mr Wilson's evidence was that traders, in his experience, want to avoid this risk and will try to match the purchase and sale quotational periods or hedge the absolute price exposure between differing purchase and sales quotational periods and typically include quotational period optionality in an offtake agreement which gives them an opportunity, in addition to hedging, to minimise the price exposure risk arising from different purchase and sale quotational periods. He stated that if a producer were to sell to a series of smelters, instead of to a single trader, it would not only be exposed to the risk of dealing with smelters, it would inevitably be exposed to a range of different quotational periods that arise from contracting with smelters in different countries and it would expose the

producer to quotational periods over which it had little (if any) control. Thus, Mr Wilson stated, since an offtake agreement with a trader effectively replaces multiple contracts between the producer and several smelters that will collectively contain many differing quotational periods, it is to be expected, and is common in his experience, for an offtake agreement with a trader to provide for quotational period optionality. His evidence was that optionality is critical for a trader and, in a commercial sense, is the “price paid” by a producer such as CMPL to obtain the benefits of an offtake agreement with a trader and a “home to monetise its production”. Mr Wilson also said that the “so called price optionality is virtually impossible to determine in advance bearing in mind that mines such as CMPL are price takers, and that if a mine such as CMPL were to sell to a range of smelters and also sell a portion of their production on the spot market, they would be exposed to a similar and unpredictable range of quotational periods”.

208 In his third report, in response to Mr Ingelbinck’s supplementary report, Mr Wilson stated there was no industry standard practice which demonstrated a correlation or a relationship between TCRCs and quotational period optionality. He agreed, though, that the question of optionality and the extent to which optionality might include back pricing will be one of the many factors taken into account in an overall negotiation of a contract.

209 In cross examination, Mr Wilson said that he “wouldn’t disagree” with Mr Ingelbinck that back pricing quotational period optionality is far more likely to have a discernible negative impact on the seller’s revenue. However he disagreed that, over a three year period, it would be highly likely that back pricing quotational period optionality with the shipment by shipment declaration would have a discernible negative impact on the seller’s revenue. According to calculations he did “without hindsight” on those three years, he estimated a negative impact of \$8.6 million. Mr Wilson was then challenged on his expertise to be able to say at any point in time what quotational period would, or would not, have been selected by a trader because he had never been a trader himself and never selected a quotational period. Mr Wilson disagreed, stating that although he had not done any direct trading himself he knows what traders look at when they are selecting quotational periods.

210 Based on his analysis of three contracts (the Erdenet Contract, the Barmenco Contract and the Peak Gold Contract, all of which are addressed later in these reasons), Mr Wilson said in oral evidence that he would not necessarily expect the introduction of back pricing to be accompanied by a corresponding benefit in an agreement. He stated:

... because when I have examined each of the back pricing contracts that have been provided into evidence, it is unclear to me on any of those contracts except for the one contract with Barmenco that any consideration, any obvious consideration, had been made for the benefit of back pricing for the account of the buyer.

211 Mr Wilson then added that he believed that GIAG did in fact give consideration, being the provisional payment of 90% of the value of any unshipped production at the end of the production month plus 14 days. However, he accepted in cross examination that the benefit to CMPL of earlier payment was “really just a nominal benefit” given that CMPL had more than enough money in its current account to cover any cash flow needs.

212 When asked whether it was his opinion that one might reasonably have expected independent parties to agree the changes to the quotational period clause in the February 2007 Agreement without a corresponding benefit, Mr Wilson replied that he was not convinced by the contracts he had seen, apart from the Barmenco Contract “which stands differently from the others”, that there was necessarily a benefit conferred by the buyer to the seller for back pricing. He added:

The only contract where one can see any benefit, it is very, very small, so I am not convinced, although it certainly is something that could have occurred, I cannot find any evidence in those contracts bar the one where any benefit has been given, or consideration has been given for the back pricing.

213 However, later in cross examination Mr Wilson was taken to the 2006 Brook Hunt Report which stated:

Some contracts with trading companies include the option for the trading company to nominate in advance an early or late Quotational Period, paying elsewhere in the terms for this right.

214 He agreed that if a buyer can nominate a quotational period with the benefit of hindsight, he would expect them to pay elsewhere in the terms. When put to him that he would agree that he would expect a buyer to pay even more for that right, if a buyer can nominate a quotational period not just with hindsight but on a shipment by shipment basis, Mr Wilson responded “potentially, yes”. When questioned why “potentially” and not “yes”, Mr Wilson explained that he had not seen it in any contract other than the February 2007 Agreement and the Barmenco Contract (to which reference is made later in these reasons). He stated that such a term was “highly unusual”.

Mr Ingelbinck’s evidence

215 The Commissioner asked different questions of Mr Ingelbinck than the question asked of Mr Wilson by the taxpayer.

216 The first question asked Mr Ingelbinck to opine on the conditions that were operating between CMPL and GIAG in their commercial and financial relations on a year-by-year basis for 2007, 2008 and 2009 and whether such conditions differed from the conditions that might have been expected to operate between an independent producer/seller and an independent buyer dealing wholly independently with one another. If so, Mr Ingelbinck was asked to say how, and to indicate what profits (if any) by reason of these conditions might reasonably have been expected to have accrued to CMPL but for those conditions.

217 In response to that question, Mr Ingelbinck's opinion, in summary, was that during the relevant period, the conditions that were operating between CMPL and GIAG in their commercial relations deviated materially from what might have been expected to operate between an independent producer/seller and an independent buyer who had been, since 1999, parties to a long-term life of mine offtake agreement structured in line with benchmark TCRCs. Mr Ingelbinck identified four differences:

- the price clause called for a lower copper payable percentage than was the industry norm;
- the TCRC deduction as a percentage of copper price was inconsistent with industry benchmark terms and prevailing market conditions;
- the quotational period clause "bestow[ed] extremely liberal optionality upon GIAG" which was not a feature of long-term offtake agreements; and
- the delivery clause allowed for CIFFO India deliveries at no extra cost to GIAG and gave GIAG the right to take delivery FOB S.T. Newcastle at a freight and insurance allowance to be set annually.

218 Mr Ingelbinck opined that, had it not been for these differences, CMPL would reasonably be expected during the relevant period to have incurred benchmark TCRCs which were significantly lower than the 23% price sharing formula; to have achieved copper prices more in line with market averages (resulting from a steady production and fixed quotational periods) as opposed to the prices selected by GIAG "courtesy of their back pricing privileges"; to have been paid for a higher percentage of the copper contained in its concentrate; and to have incurred lower freight costs. He opined that all four of these factors would have improved CMPL's revenue and therefore profitability, with the first two factors being the most significant. In his opinion, both the 2007 switch to 23% price sharing and the 2004 introduction

and 2007 expansion of quotational period optionality were clearly beneficial to GIAG and detrimental to CMPL.

219 To the question:

For [the relevant years], is the consideration received or receivable by CMPL for the sale of Cobar copper concentrate to GIAG different from the consideration that might reasonably have been expected to have been received or receivable for the sale of Cobar copper concentrate by an Independent Producer/Seller to an Independent Buyer dealing wholly independently with one another? If so:

- (a) how and to what extent; and
- (b) what consideration might reasonably have been expected to have been received or receivable by an independent producer/seller but for that difference -

Mr Ingelbinck opined that as a direct result of the commercial conditions between CMPL and GIAG being materially different from what might reasonably be expected to exist between independent buyers and sellers in similar circumstances, the consideration CMPL received for the sale of the copper concentrate to GIAG was materially different and well below what an independent seller would likely have received from an independent buyer for the sale of the same material. He stated that the difference between the consideration CMPL received from GIAG and what an independent seller would likely have received from an independent buyer in similar circumstances equalled the profit foregone by CMPL as its operating costs remained the same in either case.

220 Specifically with respect to question 2(a), Mr Ingelbinck opined that CMPL incurred TCRCs which were substantially higher than those prevailing in the overall market in general and the benchmark market in particular. It also received copper prices lower than market averages as GIAG exercised its ability to pick pricing periods from a range of options and well after their prices had been established. It was paid less than the market norm for the copper contained in its concentrate and indirectly incurred higher freight costs than would normally have been the case.

221 With respect to question 2(b), Mr Ingelbinck opined that independent sellers would, under similar circumstances, have received a much higher consideration which would have reflected the significantly lower prevailing benchmark TCRCs; copper prices more in line with market averages unaffected by the broad degree of quotational price optionality including back pricing privileges; copper payable percentages of 96.5% to 96.7% (subject to a minimum deduction of one unit); and freight allowances consistent with rates to Japan, Korea, and China.

222 To the question:

Please answer the above questions in the alternative and assuming that the independent Producer/Seller was the operator of the Cobar Mine in the period 1 January 1999 to 31 December 2009 and:

- (a) operated in a commercial context as a wholly owned subsidiary of a multinational global resources company in the same or similar circumstances to that of CMPL and GIAG; or
- (b) for the period between 1 January 2007 and 31 December 2009 operated as a stand-alone producer/seller of Cobar copper concentrate -

Mr Ingelbinck opined that there is no barrier to entry for sellers who are able to offer a good quality copper concentrate at market terms, and the owner/operator of a mine can comfortably achieve prevailing market terms regardless of whether such owner/operator is a standalone independent entity or a wholly owned subsidiary of a multinational global resources company in the same or similar circumstances to that of CMPL and GIAG. In his opinion, an independent owner/operator of the CSA mine would have been able to secure a life of mine offtake agreement with similar conditions as those that existed in the First Offtake Agreement entered into in 1999.

223 Mr Ingelbinck was not provided with Mr Kelly's affidavits for the purposes of his first report. For his second report, Mr Ingelbinck was provided with Mr Kelly's first two affidavits and was asked to say whether his opinions changed or were affected in any way by having read those affidavits and, if so, to explain how and why. He was also provided with Mr Wilson's reports and asked to advise whether, having considered Mr Wilson's reports, his opinions had changed or been affected and, if so, how and why. His view was that nothing in Mr Kelly's affidavits or Mr Wilson's reports caused him to modify his opinions.

Price sharing

224 In his first report, Mr Ingelbinck opined that CMPL's decision to agree to a shift to a 23% price sharing agreement starting in 2007 was not reasonable and prudent but irresponsible because it would be more costly to CMPL than sticking with the benchmark approach, having regard to what was known to market participants towards the end of calendar year 2006, namely that:

- (a) the copper price had risen significantly over the course of 2006 and for 2007 was forecast at US\$2.75/lb;

- (b) the 2007 benchmark TCRC discussions were well advanced with the consensus view that the outcome would be US\$60/dmt and US6.0c/lb or US15.4c/lb for 30% concentrate; and
- (c) the concentrate market had tightened significantly and market observers such as Brook Hunt were forecasting such conditions would continue to exist for a number of years.

225 On Mr Ingelbinck's analysis, using the January 2007 London Metal Exchange forward curve values, the 23% price sharing approach would have cost CMPL a combined TCRC of US63.25c/lb, being more than four times higher than the 2007 benchmark.

226 He also gave evidence that he was not aware of any other parties bound by a traditional benchmark style contract who, at the end of 2006, agreed to drop the TCRCPP structure in favour of a 23% price sharing approach.

227 In his supplementary report, Mr Ingelbinck further observed that:

- (a) based on the Brook Hunt forecasts, the expected impact for 2007 would be that the expected revenue under the 23% price sharing agreement would be lower than if CMPL had stayed with benchmark TCRCs; and
- (b) Brook Hunt's projection for the benchmark TCRCs for the period 2007 to 2009 showed that benchmark TCRCs were expected to average 8.1%.

228 In cross examination Mr Ingelbinck agreed that his issue was not with the entry into a price sharing agreement but with the percentage. He agreed that one of the advantages of a price sharing agreement is that it removed the element of volatility and the lack of correlation between TCRCs and copper price. However, in his opinion, the analysis in entering into a three year price sharing agreement was very different to a long-term agreement. In his opinion, with a three year price sharing agreement, he expected that the forecast copper prices and TCRCs for those years would be looked at, which would show that the forecast TCRCs as a percentage of copper price was far less than the 23% agreed on and a seller would come to the conclusion that price sharing was not appropriate. Whilst he accepted that one of the factors that a mine might well take into account in setting a percentage for a price sharing agreement was the past performance between TCRCs and copper prices, his view was that a seller would have taken into account that the consensus forecast amongst the industry was that it was highly

likely that balances for copper concentrate for the next three years would be tight and the expectation was that a significant increase in TCRCs was a relatively low probability.

Quotational period optionality with back pricing

229 In Mr Ingelbinck's experience, fixed quotational periods "are the norm" in long-term contracts, although most use the month of shipment or the month of arrival at the destination port as the anchor point to define the quotational period. Mr Ingelbinck stated that maintaining a regular shipping schedule and consistent fixed quotational periods provides the miner with a degree of comfort that market average prices are being achieved for its output, though that was not to say that some mines would not consider granting some degree of quotational price optionality, particularly if the buyer was prepared to offer "compensation" for the flexibility. However, he stated that "most if not all mines would balk at allowing an optionality structure which incorporates back pricing privileges" in long-term contracts. He stated that this was exactly the type of structure that GIAG introduced in 2004, where the buyer can elect to apply the average price of any one of three consecutive months with the election to be made by the end of the middle month (by which time both the averages of the first and middle months are known), and this modification "dramatically improved the value of the contract for GIAG at the expense of CMPL". He stated that he did not recall having ever seen "anything quite as liberal in long-term benchmark contracts".

230 Mr Ingelbinck explained the reasons for the enhancement of such a profit-making opportunity as follows:

... the [quotational period] optionality awarded to GIAG in 2004 was further enhanced with the 2 February 2007 amendment in that the buyer could now, on a shipment by shipment basis, choose between an "early" or a "late" set of potential [quotational period] alternatives from which to make a final election. That choice had to be made by the time the vessel sails. The "early" option gave the buyer the choice between M-1, M or M+1 whereby M is the month of shipment. The "late" option gave them the choice between the first month after the month of arrival at discharge port (1MAMA), 2MAMA or 3MAMA. In both cases, the final election had to be made by the end of the middle month. The enhancement for the buyer lies in the fact that, if price activity does not enable buyer to realize a back pricing margin in the period between the start of the month prior to the month of shipment and the Bill of Lading date, they get another bite at the cherry by opting for the "late" [quotational period] which allows them to seek back pricing margin opportunities in the 1MAMA – 2MAMA period.

231 Mr Ingelbinck said further in cross examination:

... the introduction of such type of optionality takes away any control that the ... seller had ... and gives it to the buyer which results in a situation where the buyer can do no

wrong. The buyer can – you know, a qualified buyer will elect – sometimes they will make good margins on it; sometimes they won't. The back pricing situation, as it exists – and we all agreed on that – can actually result in the seller receiving a benefit. It can also result in the seller receiving a significant detriment. ... He has no control over it, so that the distinction I would like to make is that, by making this introduction, the buyer gets to take advantage of optionality with no downside risk whatsoever... [T]he seller basically lives with – sometimes lives with the consequences of that or, sometimes, because of the particular QP – quotational period that's elected, may end up with no impact, a positive impact or a negative impact.

232 Mr Ingelbinck's opinion was that an independent seller would not have agreed to the quotational period optionality with back pricing clause incorporated into the February 2007 Agreement. In essence, it was his view that it provided substantial advantages to GIAG without a quid pro quo granted to CMPL in that GIAG on a shipment by shipment basis could choose between an "early" or a "late" set of potential quotational period alternatives from which to make a final election, expanding GIAG's back pricing enabled quotational period optionality. In his first report he stated that he found it "impossible to justify that any mine that was party to an existing benchmark style contract where fixed [quotational periods] are the norm would allow the introduction of extensive [quotational period] optionality including substantial back pricing privileges without receiving a reasonable degree of compensation for same".

233 Mr Ingelbinck disagreed with Mr Wilson's opinion that the advantage of quotational period optionality and back pricing to a trader lies principally in the risk management opportunity it provides having regard to the variety of end purchasers to which the trader will sell. In his opinion traders "crave optionality" because it can enable them to create profitable quotational period mismatches even in cases where the optionality does not include back pricing privileges.

234 In oral evidence Mr Ingelbinck elaborated on his opinion that the quotational period optionality with back pricing clause in the February 2007 Agreement provided substantial value for GIAG without a quid pro quo for CMPL. He stated:

...the shift from an annual declaration to a shipment by shipment declaration means that, in effect, as starting in 2007, the buyer had the ability to look at two instances – an early instance and a late instance – to take advantage of optionality and back pricing, meaning that if they failed to be able to take advantage in the first instance, there was a second bite at the apple. There is still no guarantee they would have always been able to take advantage of it but it basically doubled their chances in a volatile market to be able to take advantage of it. So, again, my view is, in a situation like that, whatever compensation is agreed on ought to be greater than what would have been agreed on in the annual declaration of the early versus late quotational periods.

235 Mr Ingelbinck was also asked to respond to Mr Wilson's opinion that there was a corresponding benefit, namely the change in the provisional payment clause. Mr Ingelbinck agreed that the

introduction of payments against production, even if the shipment was not made, would help the cash flow situation and stability of cash flows for CMPL but, against this, the First Replacement Agreement had also introduced CIF India deliveries at no extra cost which, in his view, was “a very big detriment to the seller” because the freight allowance that would be associated with shipments to India was far greater than the freight allowance for Japan, China and Korea, which was the original structure for the contract.

236 In cross examination Mr Ingelbinck stated that by introducing back pricing optionality, the buyer gets to take advantage of optionality with no downside risk. Whilst Mr Ingelbinck agreed that the buyer can get it wrong and choose the wrong quotational period and is not guaranteed to make a profit, he maintained that the buyer is guaranteed not to lose anything on it. His evidence was that “categorically, there is no way a qualified trader can make a mistake on having that optionality. Zero”. However, the view expressed by him was shown to be incorrect. The evidence showed that as the result of the elections made by GIAG in respect of three shipments in the 2009 year, the price that it paid to CMPL was not the lowest price and GIAG in fact paid \$4.8 million more for the concentrate than it would have otherwise. Mr Ingelbinck conceded that CMPL was \$4.8 million better off as a result of the quotational periods elected by GIAG.

Mr Kowal’s evidence

237 Mr Kowal was asked to opine on the same Questions 1 and 2 that were put to Mr Ingelbinck.

238 Mr Kowal’s opinion was that the contractual relationships of CMPL and GIAG changed markedly over the period from 1999 to 2009 as the sustainability of the CSA mine increased. In his opinion, a series of revisions to the commercial arrangements between the parties resulted in a disproportionate amount of the value of the business being captured by GIAG and this would not have been expected to operate between an independent producer/seller and an independent buyer. He stated that the February 2007 amendment saw the “most profound revisions” to the contract with modifications to the conversion charges rising to 23% for the copper price and another major revision to the quotational period. He stated, in summary, that as CMPL became more dependable as a producer of copper, and a generator of cash, GIAG modified the contractual relationship to:

- increase the charges; and
- reduce the price realised for copper concentrate -

all to the detriment of CMPL's profitability. In his opinion, an independent buyer would never be able to alter the terms and the conditions of a concentrate contract in such a manner with an independent producer/seller.

Price sharing agreement

239 Mr Kowal's conclusions included that the utilisation of price sharing contracts is directly related to the securing of finance for new projects or project expansions. He stated that Brook Hunt concurred with this finding when it stated that "these trading houses typically invest in mining projects together with particular Japanese smelting companies and the prime function of the former is to provide finance for the mine project in exchange for equity and to act (in some cases) as agent for buying or selling the project's concentrate production". Mr Kowal was demonstrated in cross examination to have taken that quote from Brook Hunt out of context altogether in that he confused a price sharing contract with what Brook Hunt had referred to as a reference contract. In cross examination it became apparent that Mr Kowal's evidence on this topic rested on a misunderstanding of what a price sharing agreement in fact is and he candidly acknowledged in cross examination that the only knowledge he had about price sharing agreements was based on the information provided in the Brook Hunt Reports and professionally he had no experience at all of price sharing agreements. The Commissioner submitted that these matters did not undermine his evidence as to whether a hypothetical mine might reasonably have been expected to have agreed to price sharing at 23% in February 2007. I disagree. He had no experience at all with respect to price sharing contracts and had no specialist knowledge qualifying him to express any opinion about price sharing contracts.

Quotational period optionality with back pricing

240 Mr Kowal's evidence was that the use of multiple quotational periods does occur and is one of the few variables available to the buyer in its negotiations with the seller. He stated that while optionality offers potential benefit to the buyer, the downside to the seller is limited if, in fact, the declaration of the option is not done frequently. He stated that a frequently utilised declaration period is annually, which means that, for 12 months, the relationship between the actual market price for copper and the seller's price for copper concentrate will be known. He opined that the need for six options was not consistent with the market at the time nor his experience. In his opinion, giving away control of the number of quotational periods and the control of declaration is not a required condition and "nor should one allow it", as "[d]oing so

means that the seller is no longer accountable for the realised price for his commodity". He stated that this was something that he had never encountered in his career.

241 Mr Kowal agreed with Mr Ingelbinck that it was very hard, if not impossible, to place a precise value on back pricing. He also agreed with Mr Ingelbinck that the provision of quotational period optionality with back pricing conferred a considerable advantage on GIAG as the buyer of copper concentrate for which there was no quid pro quo adjustment in favour of CMPL.

242 For the purposes of this proceeding, Mr Kowal valued the quotational period optionality in the February 2007 Agreement by comparing the revenues received by CMPL based on the quotational periods in fact selected by GIAG with the revenues that would have been received by CMPL had a single quotational period been chosen for the relevant period. Mr Kowal's analysis was around US\$86 million to US\$100 million predicated on the assumption that traders would select the same quotational period for the whole of the relevant period. In Mr Wilson's view, Mr Kowal's analysis was fundamentally flawed in that he kept the same quotational period for all three years. Mr Kowal accepted in cross examination that he had no experience of what a trader would do and had no basis upon which to assume that the trader would select one quotational period for the whole of the three years. Mr Kowal also accepted that the calculations he had done could only be done with the benefit of hindsight.

FINANCIAL EXPERTS REPORTS

243 The questions asked of Mr van Homrigh for his expert opinion were as follows:

... [i]n relation to the period from 1 January 2007 to 31 December 2009...

- (a) Whether or not CMPL and/or the Cobar Mine was profitable;
- (b) To what extent, there was any uncertainty as to the profitability of future copper concentrate mining operations at the Cobar Mine;
- (c) Whether or not CMPL required bank or other financing in order to operate the Cobar Mine and the nature of any such financing sought or provided; and
- (d) The nature, and benefits to CMPL, of financial arrangements which were in fact in place as between CMPL and/or the Cobar Mine and the Joint Venture Participants and/or GIAG or any third party.

(Errors in original.)

244 As to question (a), the financial experts agreed that the CSA mine was very profitable during each of the relevant years, with a return on equity of between 15% and 34% each year. However, it is irrelevant whether or not CMPL was profitable in the relevant years, since the

statutory questions must be answered by looking at the events at the time the price sharing agreement was entered into.

245 As to question (b), the financial experts agreed that mining operations are inherently risky but also agreed that the 2006, 2007 and 2008 five year plans showed that the CSA mine was forecast to generate profits and to have positive net cash flows sufficient to meet operating and capital requirements. Mr van Homrigh considered that it was evident from CMPL's annual budgets and projections, and through its monthly accounting and reporting, that CMPL was considering and managing the various risks to the CSA mine, including the extent and quality of the resource, mine planning, operations and ore processing, capital expenditure, and copper prices. He also considered that the CSA mine had substantial financial reserves during the relevant years available, if necessary, to absorb the effects of cycles in the business. Mr Samuel addressed the question differently, opining that there was very significant uncertainty as to the future profitability of the mining operations at the CSA mine because it was inherently difficult to project future copper prices and because of the risks specific to the mine itself. Both views can legitimately be accepted as they are not irreconcilable, but nothing turns on the experts' views in terms of the application of the statutory tests under Div 13 and Subdiv 815-A, as these reasons elucidate later.

246 As to question (c), the experts agreed that "[as] it transpired", the CSA mine generated more than enough cash to cover its operating and investing cash flows during the relevant years and did not enter into external financing. This question has no relevance at all to the issues for determination.

247 As to question (d), Mr van Homrigh did not identify any specific benefits or detriments bearing upon statutory questions in these proceedings and Mr Samuel was instructed not to address this question.

248 In short, the expert evidence of the financial experts was totally irrelevant to the issues for determination.

OFFTAKE AGREEMENTS

249 The taxpayer put forward a number of examples of agreements for the sale of copper concentrate between independent parties which contain quotational period optionality (including back pricing) and/or price sharing mechanisms. It was submitted that those agreements demonstrate that these features:

- (a) were actually agreed in the copper concentrate market in the period leading up to and during the relevant years; and
- (b) are therefore conditions which form part of a pricing structure that might be expected to have operated between a producer/seller of copper concentrate in the position of CMPL and a purchaser wholly independent of it during the relevant years.

250 Examples of contracts with price sharing mechanisms put before the Court were:

- (a) the contract between Red Earth Pty Ltd, GIAG and Cadan Resources Corporation dated 12 January 2012 (“**Red Earth Contract**”);
- (b) the contract between Redbank Mines Ltd and GIAG dated 29 November 2006 (“**Redbank Contract**”);
- (c) the contract between GIAG and Jiangxi Copper Company Ltd dated 20 December 2001 (including several amendments) (“**Jiangxi Contract**”);
- (d) the contract between BMAG and Tintaya SA dated 16 October 2003 (“**BMAG-Tintaya Contract**”);
- (e) contracts between Tritton Resources Ltd and Sempra Metals & Concentrate Corp dated 25 October 2002, 11 October 2002, 12 December 2005 and 24 January 2007 (“**Tritton Contract**”); and
- (f) the contract between PT Freeport Indonesia and PASAR dated 30 May 2005 (“**PTFI-PASAR Contract**”).

251 Examples of copper concentrate contracts with back pricing optionality before the Court were:

- (a) contracts between GIAG and Peak Gold Mines Pty Ltd dated 28 May 2004 and 7 March 2005 (including an amendment to the latter dated 21 February 2007) (“**Peak Gold Contract**”);
- (b) the contract between GIAG and Barmenco Investments Pty Ltd dated 1 July 2004 (including amendments to that agreement) (“**Barmenco Contract**”);
- (c) the contract between Oxiana Golden Grove Pty Ltd and GIAG dated 4 July 2008 (“**Oxiana Jaguar Contract**”);
- (d) the contract between Oxiana Golden Grove Pty Ltd and GIAG dated 22 February 2008 (“**Oxiana Golden Grove Contract**”);

- (e) the Red Earth Contract;
- (f) the contract between the Mongolian-Russian Joint Venture Erdenet and GIAG dated 30 April 2007 (“**Erdenet Contract**”); and
- (g) the contract between Montana Resources LLP and Glencore Ltd dated 11 January 2007 (“**Montana Contract**”).

252 It is noted that Mr Kelly was not involved in the negotiation of any of these contracts.

Contracts with price sharing mechanisms

253 Each of these contracts was the subject of detailed deconstruction. The taxpayer did not contend that any of these agreements were directly analogous but did submit that they provided illustrations of price sharing agreements between arm’s length parties under copper concentrate agreements between 2002 and 2011. The Commissioner’s submission was that the consideration of these contracts did not support the proposition that price sharing provisions were adopted in situations comparable to that faced by CMPL in late 2006 and throughout the relevant years. Aside from pointing to contractual differences, the Commissioner argued that the contracts were not relevantly comparable either because the contract was with a mine subject to finance or a mine which had not yet commenced production.

Jiangxi Contract

254 The Jiangxi Contract (under which GIAG was the seller and Jiangxi Copper Company Ltd was the buyer) was first executed in December 2001 and amended several times between November 2002 and February 2011. Throughout its life the Jiangxi Contract contained a price sharing mechanism for a combined TCRC of 22.5% of the copper price over the applicable quotational period. The Commissioner noted, however, that price sharing terms were applied to one 10,000 dmt shipment by GIAG to Jiangxi and then only up to August 2003. From August 2003 the parties reverted to TCRCs applicable to different qualities of copper, with only one quotational period, as opposed to optional quotational periods and with respect to low grade copper concentrate at 24.5%.

Redbank Contract

255 The Redbank Contract was a life of mine agreement for the sale of 100% of the Redbank mine production comprising copper cement and copper concentrate. The agreement was executed in November 2006. Clause 8.2 provided for a combined TCRC of 20% of the copper price for

the quotational period for the payable copper content. The quotational period was, at the buyer's option (to be declared prior to each shipment), either 1MAMA or 3MAMA.

256 Mr Ingelbinck was of the opinion that if not for the fact that the Contract quantity was less than 5,000 dmt per year the Contract might be regarded as comparable. Mr Wilson's view was that "whether or not the volume of concentrate contracted for is small or large, the benefits of a price sharing contract are equally applicable to a mine producing smaller or larger volumes of concentrate".

257 The Commissioner contended that there were critical differences, in that Redbank had not yet commenced production, under the Contract GIAG was granted only two quotational periods and did not enjoy any back pricing privileges, and GIAG took delivery under the agreement in Australia so had to bear the freight costs itself.

258 The taxpayer did not deny that there were differences between this contract and the February 2007 Agreement but submitted that this contract nonetheless was a relevant example of a price sharing agreement entered into between arm's length parties within a few months of the February 2007 Agreement between CMPL and GIAG and is therefore contemporaneous evidence of the conditions to which independent parties in the copper concentrate market were agreeing at that time. It was submitted that the differences asserted by the Commissioner did not provide a valid basis for ignoring the terms agreed under the Redbank Contract as a reference point.

Red Earth Contract

259 The Red Earth Contract was put forward by the taxpayer as an example of an agreement that was a price sharing agreement which included quotational period optionality with back pricing. This agreement was for the life of the Tapgura mine, beginning on 1 January 2010, and provided for the sale of 100% of the mine's annual production (estimated to be approximately 5,000 wet metric tonnes ("wmt")). The quotational period was, at the buyer's option, either 1MAMA or 3MAMA, to be declared by the end of 1MAMA (by which time the 1MAMA value would be known but the 3MAMA value unknown). The Contract also provided for a combined TCRC of 21% of the copper price established as set out in the quotational period clause for the payable copper content.

260 The Commissioner similarly submitted that the quantities expected to be sold under the Red Earth Contract were significantly smaller than CSA's annual production. The Commissioner

also distinguished this contract on the basis that it was an agreement that related to a project which was then only at the exploration stage and the mine never in fact came into production. The taxpayer submitted that these characteristics did not justify disregarding the Contract as relevant as an example of price sharing and quotational period optionality with back pricing agreed between independent parties to a sale of copper concentrate.

Tritton Contract

261 This Contract was executed in 2002 and amended in 2004, 2005 and 2007. It provided from time to time for the sale of 100% of concentrate produced by the seller at any mine commissioned through the Tritton copper project and Girilambone exploration project (initially expected to range between 70,000 and 100,000 dmt per annum, but estimates were higher in later years) for the life of the mine. The buyer could declare a quotational period of either 2MPMOSS or 4MAMA for each shipment, with the election to be made any time prior to the beginning of the second month prior to the month of shipment. There was also a tiered price sharing formula as follows:

- (a) if the copper price over the quotational period was less than US70c/Ib, 21%;
- (b) if the copper price over the quotational period was greater than or equal to US70c/Ib but less than US85c/Ib, 22%;
- (c) if the copper price over the quotational period was greater than or equal to US85c/Ib but less than US\$1.05/Ib, 26%; and
- (d) if the copper price over the quotational period was greater than or equal to US\$1.05/Ib, 27.5% (but 12.5% for the difference between the copper price over the quotational period and US\$1.05).

262 The Commissioner distinguished this contract on the basis that it was entered into “a number of years prior to production starting”. The taxpayer did not assert that this contract was directly analogous but again submitted that the Contract was relevant as an example of a price sharing contract between independent parties.

PTFI/PASAR Contract

263 This contract was executed in 2005 but its terms applied to tonnages beginning in 2008. The Contract provided for the sale of between 100,000 dmt and 140,000 dmt of copper concentrate in each year from 2008 to 2012 (ie a five year period). This contract had a 21% price sharing

component which applied to one third of the contemplated production and was subject to a floor and ceiling between a copper price of US80c/lb and US95c/lb.

264 Mr Wilson agreed in cross examination that:

- (a) he could not say when this agreement was negotiated;
- (b) market conditions were different in 2005 when compared with 2007;
- (c) the terms would “potentially” be impacted by the fact that the agreement was in advance of the relevant production; and
- (d) the agreement was entered into in the context of external arrangements with financiers. Mr Wilson did not deny that the involvement of a financier may have influenced terms.

265 Mr Wilson also agreed it was inaccurate to characterise this agreement as a 21% price sharing agreement simpliciter. He agreed that once the floor and ceiling were taken into account, the 21% price sharing figure was close to the then prevailing percentage of TCRC and price participation over copper price.

266 The Commissioner also distinguished this contract on the basis that it was entered into well in advance of production.

BMAG-Tintaya Contract

267 This contract was executed in 2003 between two BHP companies and was a price sharing agreement in respect of one third of the “material” sold in each shipment at 25.5% of the London Metal Exchange price over the quotational period subject to a minimum deduction of US20c/lb of copper. Different TCRCs applied to the remaining material.

268 According to Mr Ingelbinck (who had involvement in this contract) the pricing terms were not negotiated by the parties but were set by the BHP Group’s commercial department as providing for a fair transfer pricing value which would withstand scrutiny by the taxation authorities. He also gave evidence that his view at the time was that the price sharing percentage fixed upon was within an arm’s length range.

269 Mr Ingelbinck’s evidence was that the percentage was determined by reference to historical data, not on the ratio of TCRC forecasts to predicted copper prices. The 25.5% price sharing in that contract was substantially higher than Brook Hunt’s then forecast TCRCs as a percentage of the predicted London Metal Exchange copper prices at the time (around 17%

based on forecasts for 2004 to 2006). On this basis, Mr Ingelbinck accepted that this contract had a margin over the top of the range of forecast TCRCs as a percentage of copper price, being 8.5%. Mr Ingelbinck also accepted that if a price sharing contract was set by reference to forecasts, the forecast percentage may be subject to an uplift factor for the additional benefits that price sharing provides.

270 The mine was transferred to another BHP company in 2006 but, to Mr Ingelbinck's knowledge, the price sharing percentage was not changed. Mr Ingelbinck agreed that "theoretically" it could have been changed if it was considered at the time not to be arm's length.

271 The Commissioner contended that this contract was not comparable as it was in the nature of a distribution agreement between related companies, only one third of the production covered by the agreement was on price sharing terms, and the Tintaya mine was only starting up at the time the agreement was entered into. In Mr Wilson's view, although styled as a distribution agreement, it was an offtake agreement but he did agree that the Tintaya mine would be in a very different bargaining position from that of CMPL because, whilst CMPL had been reliably producing year on year, Tintaya had been out of production for a period of a number of years. Mr Wilson also agreed that the fact that Tintaya entered into the agreement in late 2003 would tell the Court nothing about the likelihood of CMPL entering into the price sharing agreement it made with GIAG in February 2007, save that it would provide a reference point.

Other price sharing agreements referred to in the Brook Hunt Report

272 The 2006 Brook Hunt Report identified several other examples of price sharing agreements that were in place by December 2006, including agreements between Cerro Corona and LS Nikko, and Chapada and Birla Copper. In relation to the Chapada agreement, the Brook Hunt Report stated:

Yamana Resources committed to its Chapada copper/gold project in Brazil in November 2004 with construction commencing immediately and with commissioning anticipated in late 2006. The \$178M project, located in the State of Goias, 270km northwest of Brasilia, is fully financed and is based on a 19 year mine life. Output in the first five years will be considerably above average reflecting higher head grades in the shallow open pit during this period. Proven and probable reserves are 310.5Mt grading 0.34% Cu and 1.03g/t Au. Yamana has concluded concentrate offtake contracts for 150kt/a of its production, including 50kt/ a with Atlantic copper and 100kt/a with Birla Copper basis price sharing on a sliding scale (~21-23%). Concentrate grades are expected to be 28% for copper and around 20g/t for gold. The project was commissioned in November 2006.

273 Both contracts were entered into before the mines came into production and the price sharing only covered part of the production. The Cerro Corona contract also had a floor and ceiling below and above which the price sharing formula did not apply. As Mr Wilson had observed in his evidence, however, the fact that no floor price existed in the February 2007 Agreement was in fact a significant benefit to CMPL under a low or very low copper price scenario, which is what Brook Hunt was forecasting at the time, because he said it gave CMPL added protection as the buyer was not guaranteed a minimum share of the price.

274 Mr Kowal opined that in most cases, the price sharing contracts referred to in the 2006 Brook Hunt Report “coincide[d] with the start-up of the mine or a major expansion at an existing operation”, and “Japanese smelting companies and their associated financial conglomerates were involved in ownership and most likely financial support”. He stated that “it would surprise [him]” if financiers linked to the Cerro Corona and Chapada projects did not require long-term agreements. The Commissioner similarly observed that the Cerro Corona and Chapada contracts were “entered into at the time when the mine was financing its build and bringing the mine into production” as a basis for distinguishing these contracts from the February 2007 Agreement.

275 The taxpayer submitted that the involvement of financiers did not provide a compelling reason to distinguish the contracts, as the evidence was that price sharing was a style of contract adopted by parties to reduce volatility and risk – in particular, the volatility associated with TCRCs (as well as price participation) and the lack of correlation between TCRCs and prevailing copper prices. As Mr Wilson opined:

While it is true that some price sharing contracts are entered into in circumstances where there is significant bank financing, the reason for this is that banks may require or the producer may deem it appropriate, to minimise its exposure to TCRC volatility so that it can have more certainty over its cashflow to service its debt. The same commercial strategy of wishing to avoid TCRC volatility and to obtain a more predictable cashflow is one that... many producers, particularly high cost producers, might reasonably be expected to adopt.

276 The taxpayer did not submit that the Cerro Corona or Chapada agreements were directly analogous to the February 2007 Agreement but submitted that they were, nonetheless, relevant examples of price sharing data points.

Copper concentrate contracts with back pricing optionality

277 The taxpayer submitted that these contracts illustrated the broad variety of quotational period clauses, including quotational periods with back pricing optionality, that might be expected to be agreed between independent parties. A table of the different periods appears below.

Contract	Quotational period clause
Peak Gold Contract	At buyer's option, M-1, MOS or 3MAMA to be declared prior to shipment.
Barmenco Contract	<p>For July 2004 shipment: average of calendar month of January 2005.</p> <p>For October 2004 shipment: at buyer's option, either 1MAMA, 2MAMA or 3MAMA, to be declared by the end of 2MAMA.</p> <p>For all other shipments: at buyer's option, either as per item (A) or (B) below, to be declared on a shipment by shipment basis:</p> <ul style="list-style-type: none"> (A) M-1, MOS or M+1 (exact month to be declared by the end of MOS); or (B) 1MAMA, 2MAMA or 3MAMA (exact month to be declared by the end of the 2MAMA).
Oxiana Jaguar Contract	At buyer's option, either 2MAMA or 3MAMA to be declared by last day of 2MAMA.
Oxiana Golden Grove Contract	At buyer's option, either August 2008 or September 2008 to be declared by end of August 2008.
Red Earth Contract	At buyer's option, either 1MAMA or 3MAMA to be declared by end of 1MAMA.
Erdenet Contract	At buyer's option, either MOS, M+1 or M+2 to be declared by last day of M+1.
Montana Contract	<p>At buyer's option, either as per (A) or (B) below to be declared by the first day of MOS:</p> <ul style="list-style-type: none"> (A) 2MPMOSS, 1MPMOSS or MOS (exact month to be declared by first day of MOS); or (B) 3MAMA, 4MAMA or 5MAMA (exact month to be declared by first day of 5MAMA).

278 The Commissioner argued that these contracts demonstrated that it is a feature of agreements for the sale of copper concentrate that, where a buyer enjoys a degree of quotational period optionality, the quid pro quo for the benefit of that optionality ordinarily takes the form of a discounted or reduced TCRC, although it may be reflected elsewhere in the contract.

Barmenco Contract

279 The taxpayer submitted that the Barmenco Contract provided objective evidence of a contract between independent parties (GIAG as buyer and Barmenco Investments Pty Ltd as seller) containing a materially identical degree of optionality to that which appeared in the February 2007 Agreement.

280 Under the Barmenco Contract, which was first entered into in July 2004, GIAG agreed to purchase from Barmenco Investments Pty Ltd, as seller, the entire annual mine production of the Eloise mine for the life of the mine. As at 2004, the Eloise mine was a similar-sized operation to the CSA mine, with approximately 500,000 mt of ore extracted in 2004 (compared with 625,000 mt at the CSA mine). The treatment charge was benchmarked to the Japanese benchmark settlement less either US\$7 (2005, 2006) or US\$10 (2007) with full price participation, less an additional US\$3 if the quotational period in option (B) was declared, and the refining charge was equivalent to the Japanese benchmark settlement less US1c.

281 Clause 11 entitled GIAG to choose from two groups of three quotational periods, with back pricing. GIAG had the option to choose from a suite of “early” quotational periods (option (A)) or “late” quotational periods (option (B)) for each shipment. If GIAG chose option (A), it could select from amongst M-1, MOS and M+1 by the end of the month of shipment (at which point the average copper prices for M-1 and MOS were already known but the average copper price for M+1 remained unknown). If GIAG chose option (B), it could select between 1MAMA, 2MAMA or 3MAMA by the end of the second month following the month of arrival (at which point the average copper prices for 1MAMA and 2MAMA were already known but the average copper price for 3MAMA remained unknown).

282 Mr Wilson explained the interaction between the quotational period clause and the TCRC provision in the Barmenco Contract as follows:

The Barmenco agreement is an example of an agreement where the agreed TCRC reduces if a particular quotational option is exercised. For the 2005 and 2006 tonnages of approximately 70,000dmt and 60,000dmt respectively, there is a \$7 per tonne reduction in the annual Japanese Benchmark treatment charge and a 1 c/lb reduction in the refining charge. The contract then provides for a further reduction of the

treatment charge of \$3 per tonne in the event that the option provided for in clause 11(b) is exercised. This \$3 per tonne of concentrate reduction was equivalent to 0.5c/lb of copper, which represented 0.16% of the 2006 copper price, which averaged US\$6,722.14 per tonne. This was equivalent to US\$10.84 per tonne of copper which is negligible and immaterial in a copper concentrate agreement.

283 The Commissioner argued that the Barmenco Contract, properly analysed, cannot support a finding that the hypothetical mine producer with GIAG's characteristics might reasonably have been expected to agree to the quotational period terms in the February 2007 Agreement. It was argued that there was a lack of comparability in that it was agreed in different market conditions in 2004; the evidence showed declining production at the Eloise mine in the period up to 2004 when the Contract was first agreed (with the relevant back pricing quotational period optionality term in place) whereas the production at the CSA mine leading up to 2007 was predicted to increase; the mine was under a new owner and one who had not previously owned a mine; the terms included what by 2007 was an approximately 16.67% discount to the TCRC; and, without knowing all of the circumstances of the negotiation, the Court could not reach any conclusion as to whether or not this agreement supports a conclusion as to what might have been expected at a mine under continuous ownership, with an existing 100% life of mine offtake agreement and with increasing and not declining production of good quality copper concentrate in the market in 2007. Moreover, it was said, Mr Wilson's evidence that the Barmenco Contract was "unusual" and the only contract that he could identify with "anything comparable to the GIAG/CMPL clause" showed just how exceptional that agreement was.

284 If it be a relevant distinguishing characteristic that Barmenco had not had previous experience as a mine owner, the evidence was that up until 2004 it had provided mining services and Mr Kelly's evidence was that he thought "they certainly would have had experience in running contracts for all of mine production". There is no reason to doubt the reliability of that evidence, which was not challenged. Although in his second report, Mr Ingelbinck described Barmenco as an inexperienced seller, in cross examination he accepted that he had no specific basis for making that assertion. To the contrary, Mr Wilson's opinion was that the Barmenco Contract with GIAG was negotiated with a degree of sophistication (as opposed to inexperience) on the seller's part. As Mr Wilson explained:

From looking at the Barmenco website and the Barmenco Contract, as at 2004, Barmenco appear to be experienced mining operators with extensive underground mining experience. I do not know whether Barmenco had any marketing experience at that time but it was and is common for miners such as Barmenco and CMPL to not have any marketing experience. The benefits provided to the seller under the contract are quite significant including discounts to TCRCs and appear to show sophistication on behalf of both parties. The contracts display the outcome of sophisticated

bargaining between an experienced seller and buyer...

The complex nature of this contract and the various concessions granted to Barmenco by GIAG for certain [quotational period] optionality suggests to me that, far from having no internal expertise to market copper concentrate, whomever negotiated this contract on behalf of Barmenco had a degree of commercial knowledge of and experience in the copper industry.

285 I accept Mr Wilson's evidence.

286 More particularly, I do not accept the assertion of the Commissioner that "there is just no basis" for the Court to rely on this agreement to reach a conclusion as to what might have been expected of a mine producer with CMPL's characteristics in February 2007. Even if there are points of distinction to be made, the Contract, nonetheless, is an example of a contract between independent parties acting at arm's length containing a materially identical quotational period optionality clause where the value attributable to the back pricing is identifiable in the terms of the contract itself, namely in the provision for a TCRC discount in the event that the quotational period in option (B) was declared. Mr Wilson and Mr Ingelbinck were both of the opinion that the quid pro quo for the benefit of the back pricing was the TCRC discount. In Mr Wilson's opinion, the discount was an obvious corresponding benefit. Mr Ingelbinck similarly gave evidence that:

So there is only one contract, which is the Barmenco Contract, which is a benchmark based contract that incorporates a discount. And I think Mr Wilson agrees with me on that. We do not see anything in that contract other than the very distinct optionality clause that would give justification to that discount. So we are linking – we are both saying the discount is a function of the optionality.

287 Unlike the other agreements put forward as comparables (reference to which follows), it is possible to form a reliable view about what, if any, discount was agreed simply by a review of the Contract itself.

Peak Gold Contract

288 The Peak Gold Contract was a two year contract for the supply of the entire mine production of concentrate from the Peak Gold mine between July 2004 and June 2006. Clause 10 of the agreement provided that the quotational period was, at the buyer's option, M-1, MOS, or 3MAMA, to be declared prior to shipment (at which time the M-1 value would be known, but the MOS and 3MAMA values unknown). For shipments between July 2004 and December 2005, TCs ranged from US\$20-30/dmt and RCs ranged from \$US0.02-0.03/lb of payable copper. For shipments from January 2006 onwards, TCRCs were to be mutually agreed.

289 The Commissioner argued that the Peak Gold Contract was not relevantly comparable because of the lower copper grade of the material being sold and the “more limited” quotational period optionality provided for in clause 10 of the agreement. The taxpayer submitted that these matters do not provide a proper basis for disregarding the Peak Gold Contract as an example of quotational period optionality and back pricing which existed under an offtake agreement between independent parties in the relevant period.

Erdenet Contract

290 The Erdenet Contract was a contract for the sale of 30,000 wmt of copper concentrate from the Erdenet mine in Mongolia (+/- 10% at the seller's option) in four equal shipments between June and September 2007. The quotational period was, at the buyer's option, MOS, M+1 or M+2, to be declared by the buyer for each shipment on the last day of the month after shipment (at which time MOS and M+1 values would be known, but the M+2 value would be unknown). The TCRCs were fixed as set out in clause 9.

291 Mr Kowal suggested that because the concentrate under this contract was sold at the Russian/Mongolian or Chinese/Mongolian border “where GIAG picked up the material”, the “logistics of this transaction would have been difficult for most buyers and therefore Erdenet would be amenable to GIAG's terms”. That statement was factually incorrect. As Mr Wilson explained, traders (including GIAG) which purchased copper concentrate from Erdenet did not “pick up” the concentrate at the border – they on-sold it directly to Chinese smelting companies on a “delivered at frontier” basis, and it was then the responsibility of those smelting companies to arrange freight to their respective smelters.

292 The Commissioner argued that the Erdenet Contract was not analogous to the agreement that CMPL entered into with GIAG because it was for specific tonnage (30,000 wmt), not 100% offtake for the life of the mine.

Montana Contract

293 The Montana Contract was a contract for the sale of 10,000 dmt in the second half of 2007. Clause 7 provided for a TC of US\$20/dmt and an RC of \$0.04/lb of payable copper, with no price participation. The quotational period was, at the buyer's option, either as per item (A) or (B) below, to be declared by the buyer on the first day of the month of shipment:

- (A) 2MPMOSS, 1MPMOSS or MOS (with the exact month to be declared by the buyer by the first day of the month of shipment, ie by which time the 2MPMS and MPMS values would be known but not the MOS value); or
- (B) 3MAMA, 4MAMA or 5MAMA (with the exact month to be declared by the buyer by the first day of the fifth month after the month of shipment, by which time the 3MAMA and 4MAMA values would be known but not the 5MAMA value).

294 The Commissioner submitted that this contract illustrated Mr Ingelbinck's evidence that the quid pro quo for quotational period optionality is likely to be a substantial discount to TCRCs as in this case the parties had agreed upon TCRCs as low as US\$20/dmt without price participation whereas, at the end of 2006, TCRCs were predicted to be US\$60/dmt in 2007. I note at this juncture that it was not Mr Ingelbinck's evidence, however, that the quid pro quo for quotational period optionality is likely to be a substantial discount to TCRCs. Rather his evidence was that it would be expected that the seller would receive reasonable compensation for the buyer's flexibility.

Oxiana Golden Grove Contract

295 The Oxiana Golden Grove Contract provided for the sale of 10,000 dmt (+/-5%) of copper concentrate from the Golden Grove mine in Western Australia in mid-2008. The quotational period was, at the buyer's option, August 2008 or September 2008, to be declared by the end of August 2008. TCRCs of US\$24/dmt and US\$0.024/lb of payable copper were applicable.

296 In his supplementary report, Mr Kowal referred to the assay of the copper concentrate, stating that the deleterious levels of zinc, chlorine, fluorine, arsenic and cadmium made the concentrate a "dirty product metallurgically". In Mr Kowal's opinion, this meant that Oxiana was "probably happy to find a home" for the concentrate. The Commissioner relied upon this in his opening address, stating that there is a link between the pricing terms and the quality of the copper.

297 Mr Kelly (whose evidence on this point was unchallenged) stated that Mr Kowal's observations were inaccurate. Mr Kowal conceded that he would "defer" to Mr Kelly's responses in relation to deleterious elements in copper concentrates.

298 Further, in relation to the Oxiana Golden Grove concentrates, Mr Wilson stated that:

- (a) he was not aware of there being any difficulties in placing Golden Grove copper concentrates into the custom concentrate market;

- (b) a zinc content of 1-2% is below levels that would typically be penalised;
- (c) a chlorine content of up to 300ppm would not normally attract a penalty; and
- (d) neither the arsenic nor the cadmium contents of the concentrate could be deemed as being “elevated”.

299 The taxpayer submitted in light of the above, the Commissioner had not shown any compelling reason for disregarding the Oxiana Golden Grove Contract as a relevant example of an agreement between arm's length parties involving quotational period optionality, including back pricing.

300 The Commissioner made no submissions on this contract.

Oxiana Jaguar Contract

301 The Oxiana Jaguar Contract was a contract for the sale of 5,000 dmt (+/-5%) of copper concentrate from Golden Grove's Jaguar Mine in 2008. It provided for a quotational period at the buyer's option of 2MAMA or 3MAMA, to be declared by the last day of the second month following the month of arrival (at which point the 2MAMA value would be known, but the 3MAMA value would be unknown). The TC was fixed at US\$27/dmt and the RC at US\$0.027/lb of payable copper.

302 In his supplementary report, Mr Kowal described the copper concentrate sold under this agreement as “even ‘dirtier’” than Golden Grove concentrate given its 3-5% zinc content, 1-3% lead content, and up to 1000 ppm of arsenic. Mr Kowal subsequently resiled from this position and “deferred” to Mr Kelly on these matters.

303 Mr Kelly's evidence was that “none of the impurity levels contained in the copper concentrate produced at the ... Jaguar mine restricted the markets into which that copper concentrate could have been sold”, including the zinc, chlorine and fluorine, cadmium and lead levels.

304 Mr Wilson also disagreed with Mr Kowal's observations. He noted that he “cannot understand why Mr Kowal believes that the arsenic content of the Oxiana Jaguar mine, at 1000ppm would be an issue for this product, this being only 50% of the limit at which arsenic content is usually penalised”.

BMAG-Tintaya Contract

305 This contract is mentioned above in relation to its price sharing terms. The terms also incorporated quotational period optionality, including an ability for BMAG to change the

quotational period once during the Contract year, provided that the change did not affect the metal in any shipment for which the quotational period had already commenced. The quotational period was, at BMAG's option, any month from 2MPMS through to M+5, to be declared by BMAG prior to the first shipment (or the start of the Contract year, if earlier). Mr Wilson described the BMAG-Tintaya Contract in the following terms:

As I would have expected, given this contract was an offtake arrangement (although it was called a distribution agreement) that involved an intermediary/trader selling to multiple purchasers and destinations, there were provisions for [quotational period] optionality... The [BMAG-Tintaya] contract contained many [quotational period] options as I would expect in a contract with an intermediary/trader. In summary, the optionality in this contract provided that prior to the earlier of the start of the contractual year or the quotational period for the first shipment, BMAG at its option, was able to declare the quotational period with respect not only to copper, but also gold and silver, being any month from the second month prior to the month of scheduled shipment, through to the fifth month after the month of scheduled shipment. This gave BMAG the option to select one of eight [quotational periods] for each metal, for a total of 24 potential [quotational period] choices. Also, having selected its [quotational periods] for a given year, BMAG had the option to change any of the [quotational periods] for any metal at any time, once again during the contractual year, with that change applying to all subsequent shipments, thus giving BMAG a further choice of three out of 24 [quotational period] options.

306 The taxpayer submitted that this contract is a further relevant example of an agreement incorporating both extensive quotational period optionality (including an ability for the buyer to change its quotational period preference mid-year, ie in response to changing market conditions) and a price sharing component. Further, it was submitted, although it was a related party agreement, Mr Ingelbinck's view was that the terms agreed were arm's length, "within the range". It was submitted that the terms are illustrative of the broad variety of conditions that were agreed amongst participants in the copper concentrate market in 2004 and retained in the relevant years, despite rising copper prices. As Mr Wilson noted:

Tintaya was not a new mine when it was owned by BHP. The price sharing component that was applied to one third of the tonnage was 25.5% of the copper price, which was at the higher end of what other buyers and sellers in this market were paying (CMPL agreed to 23% price sharing that was close to the average for these contracts). Also, unlike the CMPL-GIAG price sharing agreement that had no floor price condition, in the Tintaya-BMAG contract BMAG was guaranteed a minimum of 20c/lb from the price sharing arrangement. As regards the price sharing component, I should add that the Tintaya-BMAG distribution contract was agreed in March 2004. Prior to this, copper prices had been in [sic] languishing below \$1/lb in each year between 1998 and 2003. In the final quarter of 2003 copper prices were rising strongly but despite this, Tintaya accepted a 25.5% price sharing component in this new distribution agreement.

“COMPARABLE” CONTRACTS

307 As Pagone J in *Chevron* commented at [128], in some cases the consideration that might reasonably be expected to be given in an agreement in which the parties were independent and dealing at arm’s length may be found in comparable dealings in an open market. In the present case, contrary to the Commissioner’s contention, the examples of offtake agreements put forward by the taxpayer have probative value as illustrations of contracts between independent mine producers and traders for the sale of copper concentrate containing price sharing mechanisms and/or quotational period optionality clauses, including with back pricing, consistent with the joint position of the experts that such terms were standard in copper concentrate contracts in the relevant years and there was nothing in the price sharing or quotational period clauses of the February 2007 Agreement that did not exist in contracts between independent market participants.

308 The Commissioner’s position, however, was that the taxpayer did not establish that any of those contracts were truly comparable transactions and the Court could not, on the basis of those contracts, reach any conclusion as to what might have been expected of a mine producer with the characteristics of CMPL in February 2007: cf *Commissioner of Taxation v SNF (Australia) Pty Ltd* (2011) 193 FCR 149; [2011] FCAFC 74 (“*SNF (FFC)*”). It will be necessary to return to this contention but, for present purposes, I accept the submission for the taxpayer that these agreements demonstrate that price sharing and quotational period optionality provisions:

- (a) were actually agreed in the copper concentrate market in the period leading up to and during the relevant years; and
- (b) are therefore conditions which form part of a pricing structure that might be expected to have operated between a producer/seller of copper concentrate and a purchaser independent of it during the relevant years.

THE TASK

309 Before addressing the statutory questions by reference to the evidence elicited by the parties, it is useful to set out the task to be undertaken.

310 As earlier stated, in general terms Div 13 applies to substitute an arm’s length price for the consideration received for the supply of property or services (or given for the acquisition of such property or services as the case may be) in respect of a taxpayer in a non-arm’s length dealing under an international agreement. Similarly, in general terms, the purpose and effect

of Subdiv 815-A is to substitute an arm's length profit for the non-arm's length profits which resulted from a non-arm's length dealing under an international agreement. For that purpose, it is necessary to hypothesise a reliably comparable agreement not affected by the lack of independence and the lack of arm's length dealing for the purpose of determining whether the consideration actually given for the copper concentrate that CMPL sold to GIAG in the relevant years was less than the consideration which might reasonably be expected to have been paid if the parties had been independent and acting at arm's length in relation to the supply (Div 13) and, in the case of Subdiv 815-A, whether an amount of profits might have been expected to accrue to CMPL if the transaction it entered into with GIAG had been entered into, had CMPL and GIAG not been related and been dealing with each other at arm's length.

311 The taxpayer contended that the agreement that must be hypothesised is one for the sale of 100% of the copper concentrate from the CSA mine over a period which covers the 2007, 2008 and 2009 years, under an agreement which is structured on a price sharing basis and which provides the purchaser with quotational period optionality including with an element of back pricing. It was submitted that unlike the position in *Chevron* – where the controlled loan agreement, which was structured without security and covenants, would not have been seen in the market between independent enterprises – the provisions in the February 2007 Agreement were observable in contracts between GIAG itself and enterprises independent of it, and there was nothing to suggest that those counterparties were acting other than in a commercially rational manner.

312 The Commissioner, on the other hand, argued that the 23% price sharing term and the quotational period optionality provisions introduced by the February 2007 Agreement were “simply integers in how the consideration receivable by CMPL from GIAG ... was to be calculated”. It was submitted that the statutory questions to be addressed are: what might reasonably have been expected to have been agreed between independent parties having relevant attributes of CMPL and GIAG as the price of (the consideration for) the copper concentrate (Div 13); and what financial conditions might have been expected to operate between those parties as to the price of the concentrate (Subdiv 815-A). The Commissioner argued that to resolve the statutory questions under Div 13 and Subdiv 815-A, the Court must therefore determine what terms as to the price of the concentrate – which included freight, TCRCs, price participation and quotational periods – might have been expected to have been agreed between independent parties. It was submitted that the evidence did not support a finding that it might reasonably have been expected that CMPL would have sold its copper

concentrate to GIAG in the 2007, 2008 and 2009 years on the same or similar terms to the actual agreement, had CMPL and GIAG been independent and dealt with each other at arm's length in relation to the supply.

313 The taxpayer argued that the Commissioner's approach, rather than pricing the copper concentrate as sold under the actual agreement that was in place between the related parties, required the Court to engage in a speculative task of re-imagining all of the terms of the contract to which independent parties might be expected to have agreed, including by:

- (a) converting a contract that applied for the whole of the 2007 to 2009 period, with no facility for annual renegotiation, into one that was renegotiated annually;
- (b) replacing the price sharing basis of the actual agreement with a TCRC provision set by reference to the Japanese benchmark; and
- (c) replacing the quotational period optionality with back pricing under the actual agreement with a different quotational period provision.

314 I accept the taxpayer's submission. In my opinion, the Commissioner's approach impermissibly restructures the actual contract entered into by the parties into a contract of a different character. The decisions in *Chevron*, both at first instance and on appeal, make it clear that the hypothetical should be based on the form of the actual transaction entered into between the associated enterprises but on the assumption that the parties are independent and dealing at arm's length, in order to identify a reliable substitute arm's length consideration for the actual consideration given or received. This is consistent with, and confirmed by, the 1995 Guidelines, referred to by Allsop CJ in *Chevron* at [89], which state at [C.1.36], in a section headed "Recognition of the actual transactions undertaken", that restructuring the controlled transaction under review is generally inappropriate when making the comparison of the conditions in a controlled transaction with conditions in transactions between independent enterprises dealing at arm's length and that the analysis "ordinarily should be based on the transaction actually undertaken by the associated enterprises as it has been structured by them". The 1995 Guidelines also state at [C.1.36] that in the examination of whether a "controlled transaction" satisfies the arm's length principle "in other than exceptional circumstances", the actual transaction should not be disregarded or other transactions substituted, and that:

Restructuring of legitimate business transactions would be a wholly arbitrary exercise the inequity of which could be compounded by double taxation created where the other tax administration does not share the same views as to how the transaction should be structured.

315 The 1995 Guidelines go on to identify two circumstances in which it may, “exceptionally”, be appropriate and legitimate to disregard the structure adopted by the taxpayer in the controlled transaction. The 1995 Guidelines, in [C.1.37], identify these exceptional circumstances as:

- (a) where the economic substance of the transaction differs from its form. In such a case the tax administration may disregard the parties’ characterisation of the transaction and re-characterise it in accordance with its substance; and
- (b) where, while the form and substance of the transaction are the same, the arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner and the actual structure practically impedes the tax administration from determining an appropriate transfer price. The 1995 Guidelines give as an example of this circumstance a sale under a long-term contract, for a lump sum payment, of unlimited entitlement to the intellectual property rights arising as a result of future research for the term of the contract, stating that while it may be proper to respect the transaction as a transfer of commercial property, it would nevertheless be appropriate for a tax administration to conform the terms of that transfer in its entirety (and not simply by reference to pricing) to those that might reasonably have been expected had the transfer of property been the subject of a transaction involving independent enterprises, by adjusting the conditions of the agreement in a commercially rational manner as a continuing research agreement.

316 Paragraph [C.1.38] is important. It states:

In both sets of circumstances described above, the character of the transaction may derive from the relationship between the parties rather than be determined by normal commercial conditions **and may have been structured by the taxpayer to avoid or minimise tax. In such cases, the totality of its terms would be the result of a condition that would not have been made if the parties had been engaged in arm’s length dealings.**

(Emphasis added.)

317 This paragraph makes it clear that any restructuring of the actual agreement for the purposes of the comparative analysis is limited to the two exceptional cases outlined in the 1995 Guidelines, each being instances where the form of the transaction adopted by the parties “rather than be determined by normal commercial conditions ... may have been structured by the taxpayer to avoid or minimise tax”. The 1995 Guidelines explain that, in such cases, the

totality of the terms of the agreement would be the result of a condition that would not have been made if the parties had been engaged in arm's length dealings, thereby in those limited circumstances making it both appropriate and legitimate to recast the transaction for the purposes of the hypothesis so as to reflect the economic and commercial reality of the transaction as one between independent parties dealing at arm's length. It should be observed that, in restructuring, the substituted transaction should, nonetheless, still align with what can reliably be hypothesized to be a comparable dealing to the actual dealing in order reliably to determine an arm's length consideration for that dealing. That is made clear by [C.1.37].

318 Paragraph [C.1.41] also illuminates that the two exceptions are not intended to be alternatives to the general rule. It states:

The difference between restructuring the controlled transaction under review which, as stated above, generally is inappropriate, and using alternatively structured transactions as comparable uncontrolled transactions is demonstrated in the following example. Suppose a manufacturer sells goods to a controlled distributor located in another country and the distributor accepts all currency risk associated with these transactions. Suppose further that similar transactions between independent manufacturers and distributors are structured differently in that the manufacturer, and not the distributor, bears all currency risk. In such a case, the tax administration should not disregard the controlled taxpayer's purported assignment of risk unless there is good reason to doubt the economic substance of the controlled distributor's assumption of currency risk. The fact that independent enterprises do not structure their transactions in a particular fashion might be a reason to examine the economic logic of the structure more closely, but it would not be determinative. However, the uncontrolled transactions involving a differently structured allocation of currency risk could be useful in pricing the controlled transaction, perhaps employing the comparable uncontrolled price method if sufficiently accurate adjustments to their prices could be made to reflect the difference in the structure of the transactions.

319 The present case is not a case falling within either of the exceptions referred to in the 1995 Guidelines. The economic substance of what the parties transacted does not differ from the legal rights and obligations created by the February 2007 Agreement and there was no suggestion at all that tax considerations, rather than normal commercial conditions, shaped the terms of the Agreement such that it can be said that the totality of the terms derived from the relationship of the parties and "the actual structure practically impedes the tax administration from determining an appropriate transfer price".

320 To the contrary, the February 2007 Agreement was a form of agreement seen in the market between independent enterprises in the relevant years and, as the experts agreed and as illustrated by the "comparable" contracts, the price sharing methodology adopted by the parties under that Agreement was a recognised, legitimate and accepted way for copper concentrate to

be priced and one which other market participants, independent of each other and dealing at arm's length, also adopted at the time in respect of the supply of concentrate by a mine producer to a trader. No adjustment is required to the form of the Agreement to reflect that transaction as one entered into between independent parties dealing at arm's length in order to conduct the comparative analysis and, contrary to the Commissioner's submission, there is nothing in the structuring of the actual February 2007 Agreement that would "skew" the statutory inquiry or "be inconsistent with commercial reality". Significantly, Mr Ingelbinck had no issue with the pricing methodology adopted under the February 2007 Agreement. His issue related to the percentage that was chosen. Similarly, Mr Ingelbinck's disagreement with the quotational period clause was not so much with the quotational period options provided to GIAG but related to "the value of those [quotational periods]" and whether sufficient value was provided to CMPL for the back pricing component of it. Nor was there evidence to suggest that a price sharing agreement would never be adopted by an independent mine producer like CMPL and an independent trader like GIAG dealing wholly independently with each other.

321 The price sharing term was not simply an "integer" in the pricing of the copper concentrate, as the Commissioner contended, but a different market mechanism altogether by which to price copper concentrate. As the experts agreed, a price sharing contract and a market-related contract are fundamentally different types of contracts as the copper concentrate is priced materially differently under a price sharing agreement to how it is priced under a market-related contract. Whereas under a market-related contract the TCRCs are set by reference to a benchmark set annually and/or spot terms, with no correlation to the prevailing copper prices, under a price sharing agreement the TCRCs are fixed as a percentage of the metal exchange copper price for the duration of the contract so that the TCRC deduction and the metal exchange copper price are directly correlated to one another. Thus, there will be differences in the pricing of copper concentrate and the price payable, depending on the pricing structure used.

322 There is thus no warrant to restructure the February 2007 Agreement from a price sharing contract to a market-related contract for the purposes of determining the causative effect of the non-arm's length dealing on the profits that CMPL accrued, and I reject the Commissioner's contention that the appropriate hypothetical for the purposes of this exercise is a market-related contract. Substituting market-related TCRCs for TCRCs calculated as a fixed percentage of copper prices would produce a hypothetical transaction based upon different commercial considerations and a different commercial structure to that which was actually entered into. It involves and requires fundamentally rewriting the actual arrangement and engaging in an

extensive exercise in commercial judgment which does not accord with, or give effect to, the objective of the arm's length principle.

323 There are further reasons to reject the Commissioner's primary case.

324 In predicating an agreement on benchmark terms, the Commissioner argued that the onus of proof on the taxpayer required the taxpayer to establish that a mine producer with CMPL's characteristics might be expected to have agreed to price sharing in early 2007 and that the evidence did not establish that, if CMPL had sold all of its production of copper concentrate under an agreement on terms unconditioned by its relationship with GIAG, it would have sold its copper concentrate on the same or similar terms to the terms on which it did sell the copper concentrate in the relevant years. In putting that argument, the Commissioner has incorrectly elided the two statutory questions directed by the provisions. The first question is whether there has been a non-arm's length dealing between enterprises in an international dealing (Div 13) or, in the case of Subdiv 815-A, whether the conditions which operated between the enterprises in international dealings differed from those which might be expected to have operated between "independent enterprises". That question is directed at establishing the precondition to permit an adjustment, for fiscal purposes, of the actual consideration received or paid (as the case may be) by an entity to an amount which is an arm's length equivalent. The second question is whether the consideration received for that dealing was less than or greater than an arm's length amount (as the case may be) (Div 13) or, in the case of Subdiv 815-A, whether there was a causal relationship between the non-arm's length conditions and profits not accruing to the taxpayer. The second question is a different inquiry to the first question. The statutory task directed by the second question is to determine an arm's length consideration for the actual transaction entered into and the need to posit a hypothetical agreement is for the purpose of evaluating an arm's length amount for the actual transaction. For that purpose, the hypothesized independent dealing is a comparable agreement to the actual transaction but where the consideration is not distorted by the parties' lack of independence and lack of arm's length dealing: *Chevron* at [4] (Allsop CJ), [129] (Pagone J). The Commissioner's submission that to answer the second question in this case first requires resolving what terms independent parties might reasonably be expected to have agreed on conflates the preconditions for the second question to arise with the exercise of determining a non-arm's length consideration.

325 In *Cameco Corporation v The Queen* (2018 TCC 195) (“*Cameco*”), the Tax Court of Canada recently rejected an approach similar to that taken by the Commissioner in this case. Justice Owen noted at [751] that:

...the task under the traditional transfer pricing rules is to ascertain the price that would have been paid in the same circumstances if the parties had been dealing at arm’s length. The traditional transfer pricing rules must not be used to recast the arrangements actually made among the participants in the transaction or series, except to the limited extent necessary to properly price the transaction or series by reference to objective benchmarks.

At [714], his Honour said that in asking whether the transactions would have been entered into by persons dealing at arm’s length the Canadian transfer pricing provisions are “not asking the Court to speculate as to what arm’s length persons might or might not have done in the circumstances”.

326 The opinions of Mr Ingelbinck and Mr Kowal in response to Questions 1(b) and 2(b) asked of them similarly elided the two statutory questions by using benchmark terms as the starting point for their consideration, based on their view that had CMPL been dealing at arm’s length with GIAG it would have sold the copper concentrate on terms different to a price sharing agreement. As a consequence of this elision, their opinions in response to Questions 1(b) and 2(b) have little utility because Questions 1(b) and 2(b) did not direct the experts to address the correct statutory questions.

327 There is another issue with the opinions expressed by Mr Ingelbinck and Mr Kowal. Both Mr Ingelbinck and Mr Kowal opined that an independent seller of copper concentrate in the position of CMPL would have obtained more profits under a contract based upon benchmark TCRCs than CMPL in fact obtained, and that the 23% price sharing provision was thus “beneficial to GIAG” and led to a “revenue deficiency” for CMPL. It was on this basis that each reached the ultimate conclusion that it was unreasonable for CMPL to have agreed to sell its copper concentrate to GIAG pursuant to a 23% price sharing contract. However, this type of analysis involved precisely the same kind of hindsight reasoning which was rejected in *Cameco* at [757]-[758] because “[i]t is looking at what was the outcome of the transaction”.

328 In that case, the Canadian taxpayer, Cameco Corporation, had entered into long-term contracts to sell uranium to its Swiss trading subsidiary. After the supply contracts were executed, the price of uranium rose significantly. The result was that profits from the Canadian-sourced uranium were realised largely in Switzerland rather than in Canada. The Canadian Revenue

Agency (“**CRA**”) re-assessed Cameco, attributing additional profits to it in respect of the sale of its uranium, relying on the Canadian transfer pricing provisions, amongst other provisions.

329 The reasons in *Cameco* record that, unlike copper concentrate, uranium is not listed on a metals exchange but is bought and sold under spot or long-term contracts, which apply different kinds of pricing mechanisms. These consisted of: fixed pricing models (eg \$15/lb); base escalated pricing (“**BPC**”) models (which specify a base price that is escalated over time according to a specified formula which typically accounts for inflation); market-related pricing mechanisms (which specify a price that is determined by reference to one or more indicators of the market price of uranium, as published by leading companies in the industry); and hybrid pricing (which uses a combination of base escalated and market-related pricing mechanisms): at [25]-[32]. The supply contracts between Cameco and its Swiss subsidiary included ones which used the BPC pricing model.

330 Owen J found that the BPC transactions provided the taxpayer with an appropriate level of compensation. His Honour reasoned that they were long-term contracts, the duration of which was within the range of other long-term contracts reported for that period, and that they were for volumes of uranium that were not excessive when compared to arm’s-length wholesale contracts made during the same period. Owen J further observed at [731]-[737] that commodity producers would sell production under BPC contracts to secure a guaranteed revenue stream for that production even if the (market-related) price was expected to move higher, on the basis that there is a “well-established concept in finance, known as the ‘Certainty Equivalent’, which clearly suggests that rational actors will accept a lower guaranteed amount in lieu of a higher expected, but riskier, cash flow”.

331 His Honour found that the transfer pricing analysis of the CRA’s experts had been, to a significant degree, based on hindsight. The CRA’s experts had used the taxpayer’s actual results on the sales of uranium to third parties in the years in issue, under market-based pricing mechanisms, to determine the margin that would be achieved at arm’s length by a seller of uranium under BPC contracts. It was held that it was not possible to use contracts with market-based price mechanisms as reliable arm’s length comparables for determining the relevant margin on BPC contracts because the future price in fact obtained under the market-based contracts depended on the future price of uranium, which was uncertain at the time the BPC contracts were made. The Court’s reasoning was as follows:

[810] ... [I]f market-based contracts are used to determine the arm's length margin in a future year, the analysis is in essence using hindsight to determine the margin because the future price is the result of the choice made at the inception of the contract.

[811] To understand this point, it is helpful to first recite an opinion of Doctors Shapiro and Sarin [who were the taxpayer's experts]:

Without the benefit of hindsight, no contracting option is unequivocally better than another, and none is *prima facie* irrational. Whether a supplier or consumer ends up better off under a base-escalated contract, a pure market-price contract, or a market-price contract with a ceiling, depends on the future price of uranium. Only in hindsight can one know whether a particular type of contract was the right one for a buyer or seller to enter into, and on an *ex-ante* basis, any choice could be reasonable depending on counterparty preferences and other market circumstances.

[812] The actual price of uranium in a future year under a market-price-based contract reflects the result of the originally neutral choice made when the arm's length persons agreed to the price mechanism in the contract. In the case of a commodity with a potentially volatile price, the future result will almost invariably favour one pricing choice over another, different pricing choice even if the initial choices each reflected arm's length terms and conditions. Accordingly, to measure the price under a non-arm's length [BPC] contract against the result under a market-based contract is in effect to use hindsight—ie the result of the original choice—since the result could not be known at the time the contract was executed. This skews the calculation of the margin by the “result” component of the choice of price mechanism, contrary to the 1995 Guidelines.

332 Equally so, applying the reasoning in *Cameco* to the present case, it is irrelevant to compare the extent to which the results achieved under the price sharing contract entered differed from those that would have been achieved under an alternative agreement based upon benchmark TCRCs and to do so with the benefit of hindsight.

333 It follows that I also reject the other construct of the Commissioner's case, namely, that to discharge its onus of proof, the taxpayer had to prove that had CMPL sold its copper concentrate on terms unconditioned by its relationship with GIAG, it might reasonably be expected that it would have sold its copper concentrate on price sharing terms.

334 The Commissioner's case started with the proposition that the evidence showed that the pricing of copper concentrate is established through a process of negotiation between buyer and seller in the context of a “framework” contract between buyer and seller covering a whole range of terms and conditions including TCRCs, price participation, quotational periods and penalties, but that the main aspects of the contract subject to negotiation are the TCRCs and price participation. That proposition was uncontroversial and is accepted.

335 The Commissioner next submitted that the terms of the hypothetical transaction for the purposes of both Div 13 and Subdiv 815-A must, therefore, include a long-term, or framework, agreement between the hypothetical buyer and the hypothetical seller, as made in 1999, amended and continued over time, and where it might reasonably be expected that there would be annual negotiation of contract terms going to price (including TCRCs, quotational periods, and freight allowances) to reflect market conditions, which negotiations would take place by reference to annual benchmark terms and to market conditions as reported in publications such as Brook Hunt.

336 It was then contended that the February 2007 Agreement was “therefore to be understood as a means adopted by related parties, influenced by the lack of independence between those parties and the conditions operating between them, of setting the price payable for concentrate within the context of such a long-term framework agreement which permitted amendment in writing from time to time and contemplated annual negotiation of price”. It was submitted that “[i]t would skew the statutory inquiry and be inconsistent with commercial reality to approach the statutory tasks as if the contractual relationship between the parties was determined solely by [the February 2007 Agreement], and to constrain the transaction to require that it be one which fixed price for three years by a price sharing arrangement” and “[a]ccordingly, the starting point for that analysis is not what would have been agreed ‘under a price sharing contract of at least three years’ duration which applied for the 2007 to 2009 years”.

337 The extension of the argument was that price sharing was not commercially rational if the aim of the mine producer was to make as much profit as possible. It was submitted that neither Mr Ingelbinck nor Mr Kowal considered that an independent party in the position of CMPL would have agreed to switch to price sharing, that Mr Wilson agreed that it would not be commercially rational to do so if the aim was to make as much profit as possible and Mr Kelly’s evidence was that making as much profit as possible “was precisely” GIAG’s aim in managing its mining assets. It was submitted that:

The Court would readily conclude that any other multinational commodities group, and any other orphan independent mine, would similarly have had the aim of maximising profitability, and that price sharing would not have been commercially rational in the circumstances. Mr Wilson’s evidence was that on the available market information at the end of 2006, it was highly likely that CMPL (and it would follow any independent mine producer with its characteristics) would be worse off financially by agreeing to the price sharing agreement for three years rather than remaining on the terms as between CMPL and GIAG at the start of 2007.

338 I have already addressed why that argument wrongly elides the question of whether the preconditions exist for the exercise of power under Div 13 and Subdiv 815-A with the task of evaluating an arm's length consideration for the actual dealing. There are three other points to make about these submissions.

339 The first point is that neither Div 13 nor Subdiv 815-A directs an inquiry into the commercial prudence of the non-arm's length contract or transaction entered into. The inquiry directed is a comparative analysis of the consideration given under the actual agreement with a comparable "real world" arm's length consideration. Nothing different is said in the 1995 Guidelines. Where at [C.1.37] reference is made to adjustment of the conditions of the agreement "in a commercially rational manner", it is in the context of the second exceptional circumstance where the structure of the transaction is not explained "by normal commercial conditions" but may have been structured to avoid or minimise tax so that some adjustment to the transaction may be required to bring a "commercial reality" to the independent dealing hypothesis.

340 Secondly, in construing and applying the provisions of Div 13 and Subdiv 815-A, it is essential in giving effect to the policy objectives of those provisions not to intrude into the analysis concepts more appropriately found in other provisions, such as Part IVA of the ITAA 1936. The arm's length principle does not introduce, or involve, any investigation or consideration of purpose or motive: *W R Carpenter Holdings Pty Ltd v Federal Commissioner of Taxation* (2008) 237 CLR 198; [2008] HCA 33 at [38]. Nor does the assessment of an arm's length consideration involve an inquiry into what profits might reasonably be expected to have been obtained on a differently structured transaction, nor is the question whether, had the transaction been structured differently, it might reasonably be expected that greater profits would have accrued.

341 Thirdly, even if it be relevant to consider the commercial prudence of that which was transacted, hindsight could not be used to second-guess the commercial judgment made at the time as to the pricing methodology to adopt.

342 However, in case I am wrong in my analysis, later in these reasons I also address the Commissioner's argument that the evidence did not establish that independent parties in the position of CMPL and GIAG might have been expected to enter into such an agreement.

PRICE SHARING HYPOTHETICAL

343 The starting point for the analysis is that it is a feature of price sharing agreements that the TCRC deductions are fixed as a percentage of the metal exchange copper price for the duration of the contract. It is also a feature that a price sharing agreement does not contemplate annual variations to the agreed percentage. Comparable terms existed in the February 2007 Agreement. Additionally, the contracts put into evidence by the taxpayer relevantly included price sharing contracts containing quotational periods with optionality, demonstrating that the provision of quotational periods with optionality was a feature of price sharing agreements.

344 I do not accept the Commissioner's contention that those contracts cannot provide a probative basis for the Court to conclude that such kinds of terms might be expected to have been agreed between a mine producer with CMPL's characteristics and a trader with GIAG's characteristics. The Commissioner argued that none of those contracts were directly comparable, and there was no evidence of any price sharing agreement entered into in the copper concentrate market in any of the relevant years, or of any mine in production agreeing a 100% offtake agreement on price sharing terms, or that any other mine had ever entered into a three year price sharing agreement. Such an approach was rejected by the Full Court in *SNF (FFC)*. As the Full Court stated at [102], if correct, it would have the consequence that "a taxpayer who bears the onus in tax appeals, could never succeed in such a [transfer pricing] case for the bar will be set at an unattainable height". The Court thus described a submission by the Commissioner that sought "to discern the presence of a strict norm of operation inflexibly requiring one kind of comparable and forbidding all others" and which "refuse[d] to admit the possibility of making adjustments for differences" as being "deeply impractical". In my view, the contracts adduced by the taxpayer evidence the degree of variability in contracts adopting such terms and are probative evidence that such terms might be expected to operate between hypothetical mine producers and traders independent of each other and acting at arm's length.

345 I accept the taxpayer's submission that the Court's task in the present case is to determine:

- (a) an applicable price sharing percentage or range; and
- (b) what, if, any, quid pro quo might be expected for the quotational period optionality conferred on GIAG.

Price sharing percentage

346 I am satisfied on the evidence that the 23% price sharing rate was within an arm's length range: *SNF* (FFC) at [128].

347 First, as at the end of 2006, the price sharing percentage of 23% sat within the "normal range of price sharing" of between 21-26% that the 2006 Brook Hunt Report identified as existing in the market at that time. The Brook Hunt Report also referred to specific examples of price sharing agreements with percentages within that range. There was no challenge to the reliability of the "normal range of price sharing" of between 21-26% identified by Brook Hunt.

348 Secondly, the "comparable" contracts in evidence had price sharing percentages ranging from 20% to 27.5%. Whilst none of those contracts can be said to be truly comparable, collectively they are probative evidence of percentages agreed in arm's length contracts. Mr Wilson said in oral evidence that such agreements would have been "reference point[s]" for price sharing terms.

349 Thirdly, as at the end of 2006, the information available in the Brook Hunt Report revealed that the long-term historical average ratio of Japanese benchmark TCRCs (including any price participation component) to the London Metal Exchange copper price was 22%. Mr Ingelbinck agreed in cross examination that it may be relevant to have regard to the past relationship between TCRCs and copper prices in working out an appropriate percentage in a long-term price sharing agreement, though he qualified that it was his view that it would have been more relevant to look at the forecast TCRCs as a percentage of forecast copper prices in fixing the percentage for the February 2007 Agreement, given that the price sharing was for three years only.

350 Fourthly, the evidence showed that the BMAG-Tintaya Contract (entered into at the end of 2003), in which Mr Ingelbinck was involved in setting the rate based on historical data, had a margin of 8.5% over the top of the range of Brook Hunt's then forecast TCRCs as a percentage of the predicted London Metal Exchange copper prices at the time (17%, based on forecasts for 2004 to 2006). Nonetheless, Mr Ingelbinck gave evidence that he had considered the percentage of 25.5% to be a "fair transfer price".

351 Fifthly, although there was no direct evidence of the actual percentage of TCRCs and price participation paid by CMPL over the period from 2000 to 2006, figures extrapolated from a document appended to the Commissioner's Position Paper showed, according to the taxpayer's

analysis, that the historical average median ratio of CMPL's TCRCs to its copper sales was approximately 21%. Mr Ingelbinck agreed that apart from in 2005, when the ratio had been 25.59%, all the other numbers in that document seemed to be reasonably consistent with the Brook Hunt Report.

352 Sixthly, though on Mr Ingelbinck's evidence the prevailing forecasts at the time may be more relevant in the exercise of fixing the percentage for a price sharing agreement of three years, there was no evidence to suggest that independent parties dealing at arm's length would only have regard to the prevailing forecasts in determining the percentage of the price sharing for such a term.

353 Seventhly, Mr Ingelbinck accepted in cross examination that independent parties dealing at arm's length might reasonably agree to an uplift of the forecast percentage to reflect the additional benefits of a price sharing agreement – ie volatility reduction and certainty.

354 Notwithstanding the view expressed by Mr Ingelbinck in cross examination that the forecast ratios would have been more relevant for a price sharing contract of three years duration, he was not asked to give his opinion as to an arm's length price sharing percentage of a comparable contract between independent parties with the characteristics of GIAG and CMPL and he did not address that question in his reports. It would therefore be purely speculative to reason that the percentage might be expected to have been some lesser rate than the 23% agreed based on Mr Ingelbinck's evidence. In contrast, the 2006 Brook Hunt Report provided a reliable evidentiary basis of arm's length price sharing percentages at the relevant time and the percentage of 23% comes within the "normal range" identified by that Report. Moreover, the comparability of the price sharing percentage with the average median ratio of TCRCs as a percentage of copper price based on historical data lends further support to the conclusion that the 23% rate was within an arm's length range.

Quotational period optionality

355 The starting point for this analysis is the common ground between the industry experts that the impacts of quotational period optionality on a seller can be both positive and negative, depending on market conditions. It was also common ground that quotational period optionality with back pricing was desirable for a trader but "it was very hard, if not impossible to place a precise value on back pricing", and that the value that was provided to GIAG by the quotational period optionality could not be quantified.

356 Mr Kelly's evidence was that the value to a buyer of such a clause needs to be considered as part of the package of commercial terms that are provided for under a given contract. As Mr Kelly explained:

In my experience, contractual negotiations involve both sides weighing a range of different factors. In my copper trading activities, I generally do not seek to equate the benefit conferred on one party by one proposed item in a contract (in this case, a discount to benchmark TCRCs) with the benefit conferred on the other party by another item (in this case, the granting of [quotational price] optionality). Rather than approaching the negotiations on the basis of one benefit being given 'in return for' another, in my experience, it is common in the industry for the bargain to be struck more holistically.

He was not challenged on that evidence.

357 Mr Wilson and Mr Ingelbinck similarly gave evidence that normally the provision of back pricing optionality is just part of the overall bargain between the parties. In cross examination Mr Ingelbinck agreed that, at the end of the day, back pricing is "a matter of negotiation for the parties".

358 Mr Wilson and Mr Ingelbinck also agreed that the Barmenco Contract was the only agreement that either of them had seen which put a specific price on back pricing privileges. The difference between Mr Wilson and Mr Ingelbinck was that whereas Mr Wilson could not identify something obvious by way of price paid in the contracts he had seen (apart from the Barmenco Contract), Mr Ingelbinck's evidence was that he was "confident that a more thorough review of the timing and the terms of the agreements will show a degree of compensation paid by the buyer to secure the optionality (ie the contracts have lower TCRCs than contemporaneous contracts that do not allow back pricing have)". He explained that the lack of information about what was negotiated, market terms at that time, and information as to precisely when the terms were negotiated meant that it was not possible to form any reliable view about what if any discount was agreed from simply reviewing contracts after the event.

359 The Commissioner submitted that an analysis of the contracts before the Court "bears out Mr Ingelbinck's prediction that those agreements would provide for a degree of compensation for [quotational period] optionality". In his written submissions the Commissioner referred to a 2002 agreement between Placer Pacific (Osborne) Pty Ltd and GIAG ("**Placer Contract**") in which the quotational period option was granted to the seller (not the buyer) and provided for an increase of \$2.50/dmt in the treatment charge if the seller exercised a quotational period option; the Barmenco Contract, under which the buyer had the option to elect from a suite of

“early” quotational periods (option (a)) or “late” quotational periods (option (b)) and, if the buyer elected option (b), the TCRC was subject to a discount which ranged from US\$7 to US\$16.4/dmt of concentrate in return for GIAG being granted quotational period optionality and back pricing privileges; and the Montana Contract, in respect of which it was said that “the parties... agreed upon [TCRCs] as low as US\$20/dmt without price participation, whereas, at the end of 2006, [TCRCs] were predicted to be US\$60 in 2007. On the other hand, GIAG enjoyed the option of six [quotational periods]”. The Commissioner submitted that these agreements illustrated that the quid pro quo for quotational period optionality “is likely to be a substantial discount to TCRC” and thus that:

As such, the hypothetical seller having relevant characteristics of CMPL would not have agreed to grant [quotational period] optionality of the kind CMPL granted to GIAG under [the February 2007 Agreement], including back pricing privileges with shipment-by-shipment declarations of the kind CMPL granted to GIAG during the relevant years, without receiving substantial compensation for that in the form of a substantial discount to [TCRCs].

360 Mr Ingelbinck and Mr Kowal both considered that the quotational period optionality with back pricing clause in the February 2007 Agreement “provided substantial (but not necessarily quantifiable) value to [GIAG] for which there was no quid pro quo”. Mr Ingelbinck’s opinion, however, was shown to be based on the incorrect view that a trader cannot make a mistake on back pricing optionality and Mr Kowal’s opinion was shown to be based on a flawed analysis of the quotational periods in fact selected by GIAG and based on an assumption of quotational periods fixed annually which he agreed he had no proper basis to assume. Moreover, to the extent that each of them attempted to value the quotational period optionality for GIAG in the relevant years by comparing the revenues received by CMPL based on the quotational periods in fact selected by GIAG with the revenues that would have been received by CMPL had a single quotational period or combination of quotational periods been chosen in the relevant years, it is clear that such comparisons can only be done with the benefit of impermissible hindsight: cf *Cameco* at [810]-[812]. Mr Kowal acknowledged that the exercise he undertook could not have been done at the beginning of 2007. I accept the taxpayer’s submission that the difference between the prices that CMPL did receive and the prices it would have received had fixed quotational periods been used annually can only be known after the fact, and once the London Metal Exchange copper prices for the whole of the relevant years were known. As such, this difference in price is not one that would have been ascertainable by parties in the position of CMPL and GIAG as at early 2007, agreeing to an optionality clause of the kind in the controlled transaction. It follows that the difference between the revenues received by

CMPL under the kind of back pricing optionality provision that was in fact in place and the revenues that would have been received by it had some other quotational period provision been in place provides no reliable indicator as to how independent parties – without the benefit of a crystal ball advising them of future London Metal Exchange prices and market movements – would have valued the benefit conferred upon GIAG under the February 2007 Agreement. Accordingly, I place little weight on the opinions expressed by Mr Ingelbinck and Mr Kowal that the quotational period optionality in the February 2007 Agreement had “substantial value” to GIAG or upon their analyses.

361 I note also that it was not the evidence of either Mr Ingelbinck or Mr Kowal that the quid pro quo for quotational period optionality “is likely to be a substantial discount to TCRC”.

362 Mr Ingelbinck’s evidence was that he:

.. [found] it impossible to justify that any mine that was party to an existing benchmark style contract where fixed [quotational periods] are the norm would allow the introduction of extensive [quotational period] optionality including substantial back pricing privileges without receiving a reasonable degree of compensation for same.

363 However, he did not address what an appropriate quid pro quo might be expected for the provision of such optionality and nor did Mr Kowal.

364 I do not accept the Commissioner’s submission that the evidence supported the conclusion that it might be expected that an independent producer in the position of CMPL would have been able to secure substantial discounts to TCRC terms if it were to agree to the kind of quotational period optionality with back pricing found in the February 2007 Agreement.

365 First, I accept the taxpayer’s submission that it is inapposite to compare the TCRCs agreed under the Montana Contract to spot/benchmark TCRCs and to conclude based on that comparison some element of discount. As Mr Kelly explained:

[T]his contract is not and has never been negotiated based on an annual reference. It is a TCRC negotiated between a buyer and a seller at a point in time for a particular market. What's interesting about this is it doesn't follow any typical treatment charge and refining charge, because typically you would see a - a copper refining charge as an equivalent of the treatment charge - so 20 and two. In this case it's 20 and four, so it's not comparing the same treatment charge and refining charge ... I certainly wouldn't draw a comparison in the markets for negotiating this contract to negotiating an annual benchmark contract.

366 When put to Mr Kelly that it looked very much like there was a discount agreed to the treatment charge as part of the price paid for the quotational period optionality, Mr Kelly disagreed.

367 Neither Mr Ingelbinck nor Mr Kowal addressed whether this contract evidenced a substantial discount for the quotational period optionality.

368 Secondly, whilst both the Placer Contract and the Barmingo Contract demonstrate some obvious quid pro quo for the optionality, they appear to be unusual. Mr Wilson and Mr Ingelbinck agreed that the Barmingo Contract was the only agreement they had seen which appeared to put a specific price on back pricing privileges. Mr Kowal did not address whether he had seen any other contracts with a discount agreed to the TCRC as part of the price paid for the quotational period optionality.

369 Thirdly, whilst the Commissioner argued that other terms in the February 2007 Agreement conferred significant advantages to GIAG to the detriment of CMPL, such as the freight terms, it is not evident that because of such terms it might reasonably be expected that there would be a substantial discount to TCRCs in a comparable transaction between independent parties acting at arm's length.

370 Viewing the evidence as a whole, I find that I am not satisfied that a discount might be expected to have been allowed between independent parties for the benefit of the quotational period optionality provided for in the February 2007 Agreement.

Freight and provisional payments

371 I should nonetheless separately address the Commissioner's arguments on the freight and provisional payment provisions.

372 The February 2007 Agreement provided for a freight and insurance allowance to be mutually agreed annually by the parties on the basis of "prevailing spot market rates to main port Japan, Korea, India or China" and to be credited to GIAG, unless otherwise agreed. The Commissioner argued that the option to use freight rates from Australia to India conferred a significant advantage on GIAG to the detriment of CMPL in that shipping rates to India were "considerably more expensive" than rates applicable to Japan, Korea or China and Mr Kelly's evidence was that only a very small proportion of shipments were in fact to India. It was submitted that the fact that GIAG opted to use the freight rate for shipments to India for the 2009 year highlighted "exactly how detrimental that clause was to CMPL".

373 It was submitted further that the evidence of other contracts supported the proposition that the hypothetical seller in the position of CMPL would not have agreed to a rate such as that struck in 2009 in that:

- (a) the Barmenco Contract provided for freight to be at spot rate on the basis of 10,000 wmt to the main Japanese port, where freight rates to Japan are cheaper than those to India;
- (b) an agreement between Kagara Zinc Ltd and GIAG dated 23 June 2005 provided for market rates to be mutually agreed on a shipment by shipment basis; and
- (c) under Amendment No 4 to the Peak Gold Contract, freight was to be agreed between the parties based on actual shipment size.

374 It was submitted, in addition, that it might be expected that independent parties dealing wholly independently with one another would have been expected to agree the freight allowance by reference to prevailing spot rates to destinations that were actually shipped to and “[c]ertainly, it would not be expected that independent parties would agree such favourable freight rates for GIAG as part of the balance of terms struck for the sale of copper concentrate under a long-term offtake agreement in the relevant years”.

375 I do not accept these submissions.

376 First, the use of a FOB freight provision whereby the buyer arranges for freight, and is provided with a mutually agreed freight allowance which is deducted against the amount paid to the seller, was a standard term in contracts for the supply of copper concentrate in the relevant years.

377 Secondly, the Commissioner’s complaint impermissibly relies on hindsight analysis – that is, that few shipments were made to India for 2009 and the rates for shipping to China, Japan, and Korea in that year were less than the actual rate charged.

378 Thirdly, it does not follow from the simple fact that GIAG received a higher freight allowance in 2009 than if it had chosen the freight rates for China, Japan, or Korea that it might be expected that independent parties would not have agreed such terms. As Mr Kelly explained in cross examination, there are a number of different factors which might affect freight rates agreed between the parties.

379 The Commissioner did not contend that the provisional payment clause, which provided for a 100% provisional payment, was a condition which differed from what might be expected to have been agreed between independent parties. However, it was submitted that the timing of the payment was an “unusual feature” in that it provided for CMPL to be paid for material produced but not shipped in a given month. Although it was accepted that this clause had

potential benefits for CMPL, it was submitted that the benefit to CMPL of earlier payment was really “just a nominal benefit” bearing in mind the balances in the current account facility held by GIAG for CMPL. Further, it was Mr Ingelbinck’s evidence that the provision also had benefits for GIAG arising from its ability:

- (a) to withhold material from the market temporarily should GIAG wish to avoid being forced to sell in a sloppy concentrate market;
- (b) to operate profitably if the material has been priced and there is a contango market: that is, it is anticipated the price will increase in the future;
- (c) to build up larger lots to secure more beneficial freight rates; and
- (d) to do some or all of the above.

380 Accordingly, it was submitted, the provisional payment mechanism was not sufficiently favourable to CMPL to compensate for accepting the unfavourable price sharing and quotational period terms. Further, it was submitted, the taxpayer had not proved that CMPL did receive any benefit of a value that offset, or reduced in any way, the detrimental contractual terms.

381 I reject the submission that the taxpayer needed to prove that CMPL did receive a benefit from the provisional payment mechanism which was more than nominal, first because it was the common evidence of the experts that it was advantageous to CMPL to be paid on production, rather than having to wait until shipment of the concentrate to be paid, not just from a cash flow perspective, but also from a risk perspective and, second, because the benefits conferred by the timing advantage are simply to be weighed as part of the holistic bargain that might be expected to have been agreed by independent parties acting at arm’s length.

CONCLUSION

382 Accordingly I find that the taxpayer has established that the prices that CMPL was paid by GIAG for the copper concentrate it supplied to GIAG under the February 2007 Agreement were within an arm’s length range and accordingly the taxpayer has discharged the onus of proof on it.

383 The Div 13 determinations were premised on the claim that the consideration received by CMPL for the copper concentrate that it supplied to GIAG in the relevant years was less than the “arm’s length consideration” (in the defined sense) which might reasonably be expected to have been received by a producer/seller of copper concentrate in CMPL’s position selling to

an independent buyer in GIAG's position under an agreement between independent parties dealing at arm's length with each other. As I have concluded that the consideration paid by GIAG to CMPL for the concentrate fell within the range of consideration that might reasonably be expected to be paid, the amended assessments are therefore not supported by Div 13 and are excessive.

384 So too, for the purposes of Subdiv 815-A, CMPL did not get a transfer pricing benefit within the meaning of s 815-15(1) of the ITAA 1997 because, for the purposes of s 815-15(1)(c), there was no amount of profits which, but for the conditions mentioned in Art 9 of the Swiss Agreement might have been expected to accrue to CMPL but which, by reason of those conditions, did not so accrue. The amended assessments are therefore not supported by Subdiv 815-A and are excessive.

THE COMMISSIONER'S CASE

385 In case it is necessary, I should deal with the Commissioner's case that the evidence did not establish that independent parties in the position of CMPL and GIAG might have been expected to enter into an agreement on price sharing terms or with the range of quotational period options contained in the February 2007 Agreement. The analysis that follows assumes, contrary to how I have found, that the predicate of an agreement on price sharing terms must first be established on the evidence.

386 For the following reasons advanced in the taxpayer's written submissions, I am satisfied on the evidence that it might reasonably be expected that an independent mine producer in the position of CMPL might be expected to enter into a price sharing agreement in early 2007.

387 First, the unchallenged evidence was that the CSA mine was a high cost mine and a high cost mine, susceptible to a reduction in the margins between its revenues and operating costs, might be expected to have been interested in removing the uncertainty of large movements in benchmark TCRCs and spot TCRCs by fixing a margin of the copper price that ensured that it would remain in operation, especially so during a period of extreme market volatility. The Commissioner's case ignored the fundamental differences between contracts on benchmark terms and contracts on price sharing terms.

388 Secondly, an independent seller as at the beginning of 2007 would have known that benchmark TCRCs had been historically volatile, ranging from around 10% of the London Metal Exchange copper price to 30% of the London Metal Exchange copper price. While by the beginning of

2007 the benchmark TCRC for 2007 had been set, the benchmark TCRCs for 2008 and 2009 were unknown. Further, although the 2008 and 2009 benchmark TCRCs had been forecasted by Brook Hunt, such forecasts had proven historically to be highly unreliable. Thus, whilst CMPL's own budgeted profit forecast for 2007 (which was prepared on a conservative position on the basis of benchmark terms) forecast significant profits, there was no assurance that the forecast TCRC/copper price ratio reflected in its budget or in Brook Hunt's Reports for 2008 and 2009 would, in fact, eventuate.

389 Thirdly, while price participation had been set to zero in the benchmark TCRC for 2007, and it was the common view of the experts that price participation would not be reintroduced in 2008 or 2009, the 2006 Brook Hunt Report made clear that there was uncertainty as to whether it would be reintroduced in later years. Mr Ingelbinck agreed that, in early 2007, "no-one in the industry knew whether it would be reintroduced". Mr Ingelbinck also agreed that in 2006, price participation was a material aspect of the cost that a mine subject to a benchmark TCRC contract incurred, with 2006 price participation representing almost 50% of the total TCRCPP and that a price sharing agreement ruled out the risk of price participation being introduced into the equation.

390 Fourthly, spot TCRCs had been even more volatile in the years preceding 2007, ranging from zero c/lb up to around 45c/lb. Brook Hunt did not try to forecast spot TCRCs, which Mr Wilson said are "virtually impossible to predict" and Mr Ingelbinck agreed were "more difficult to predict than are benchmark TCRCs" and that "neither of them [spot or benchmark TCRCs] are entirely predictable in the first place". The spot TCRCs for the 2007 to 2009 period were thus unknown and were not forecast nor able to be forecast. Further, given that the relationship between spot TCRCs and benchmark TCRCs had been historically volatile, the benchmark 2007 TCRC gave no indication of what spot TCRCs over the ensuing years might be. Mr Ingelbinck agreed that, as at the beginning of 2007, "what was not known and could not be predicted [was] where spot TCRCs would be".

391 Fifthly, as at the beginning of 2007, the London Metal Exchange copper price was extremely volatile and difficult to predict. Having reached all-time highs at the end of 2006 after a rapid escalation, market sentiment was that the price would fall, but it was not possible to predict when, at what speed, or to what levels. Although pricing forecasts were available, in prior years such forecasts had proved to be materially inaccurate. Mr Ingelbinck's evidence was that the rise in copper prices in 2006 was "a somewhat unheard of event and caused all kinds of

re-evaluations amongst industry participants as to what made sense and how to structure these agreements ...people were confused”.

392 Sixthly, not only had benchmark TCRCs, spot TCRCs and London Metal Exchange copper prices been historically volatile and subject to “significant changes”, but their relationship to one another had also been subject to significant volatility, there being no correlation between them. In the period 2000 to 2006, the value of TCRCs and price participation as a percentage of CSA’s copper revenues ranged from 11.6% to 26.8%, with a median of 20.7%. Further, at the end of 2005, the budgeted 2006 TCRCs were approximately 31% of the budgeted copper sales revenues for 2006. At the end of 2006, the budgeted 2007 TCRCs were 12% of the budgeted copper sales revenues for 2007. However, this was simply a function of the all-time high copper prices, and to be achieved required the denominator of the equation to remain large. Under a price sharing agreement, the volatility associated with the lack of correlation between London Metal Exchange copper prices and benchmark/spot TCRCs was avoided. Further, Mr Ingelbinck agreed that different participants in the market could have taken different views about the importance of avoiding such volatility, and that this would ultimately be a commercial decision.

393 Seventhly, the evidence showed that based on its own costs budgets and Brook Hunt’s price forecasts as at 2006, CMPL would have been viable and would have expected to generate a profit margin of at least 25% and up to 40% (depending on the costs figures chosen) in each of the relevant years under a 23% price sharing contract. Mr Wilson thought that the margins “looked pretty healthy” for a high cost mine as at 2007 and that the margins were “pretty much in line with what [he would expect to see]”.

394 It cannot be said that the entry into a price sharing contract was irrational, having regard to the benefits of such contracts and the market circumstances.

395 The Commissioner, on the other hand, argued that the adoption of a price sharing agreement in replacement of benchmark terms would have compromised the financial viability of the mine, if the concern of the producer was one of increasing operating costs as at the end of 2006. It was submitted that “indeed Mr Wilson accepted that if there was a concern as to escalating operating costs ([which] Mr Kelly said there was) agreeing to the 23% price sharing and the escalation of figures that involved was a decision that would put the financial viability at risk”. There are two responses. First, the Commissioner’s contention that the adoption of a price sharing agreement in replacement of benchmark terms put the viability of the mine at risk

moving forward if fuel or other costs increased was shown to be incorrect. Secondly, Mr Wilson's answer must be considered in context. It is clear from the line of questions put to Mr Wilson that he disagreed with the premise upon which the question was put, namely that there was, in fact, a concern that there might be escalating costs in the 2007 period. In Mr Wilson's view, cost escalation should have peaked. It is also incorrect that Mr Kelly gave evidence that "there was a concern at the mine as to escalating operating costs". What Mr Kelly in fact said in the transcript references footnoted was that "operating costs had actually, in fact, been going up" in 2006 and he referred to CMPL as having "increasing operating costs" in 2006. The 2007 Budget did refer to CMPL having increasing operating costs in 2006 and recorded that cost control would be an important focus of the business in 2007 but there was nothing expressed in the Budget about a concern as to increasing operating costs in 2007.

396 The Commissioner urged the Court to draw a *Jones v Dunkel* inference from the "glaring" absence of evidence that anyone at CMPL considered that it would be in CMPL's interests for it to amend its pricing terms so as to provide for price sharing, rather than the pre-existing benchmark style terms. It was submitted that had anyone at CMPL considered that in February 2007 it was in CMPL's interests to enter into a price sharing agreement, the Court would readily expect the taxpayer to have led such evidence. That contention is rejected as subjective motive is completely irrelevant to the application of Div 13 and Subdiv 815-A, even on the Commissioner's case with respect to how the statutory provisions operate. Accordingly, I draw no such inference.

397 The Commissioner submitted that similarly the Court would reject the contention that a hypothetical mine producer with CMPL's characteristics would have agreed to six quotational period options with back pricing and shipment by shipment declarations in February 2007. It was submitted that the only possible impact of such an agreement would be to the detriment of the mine producer, and to the benefit of the trader. It was submitted that there would be no reason for the hypothetical mine producer, bearing in mind the market in February 2007 and the reliable production the mine had experienced over the years, to agree to such terms. It was also submitted that given Mr Wilson's evidence that the quotational period that will be agreed between a mine and a trader will come "down to the holistic negotiation of the contract between the buyer and the seller" and there is no fixed framework for what the quotational period should be and that there was no evidence of the negotiation of the February 2007 Agreement, there was no basis for the Court to conclude that it might reasonably be expected that a hypothetical mine producer in the position of CMPL might reasonably have been expected to agree the

unfavourable terms as to quotational periods agreed in the February 2007 Agreement. This last submission has no support in the legislation or any authority and is also rejected. As *Chevron* makes clear at [131] (Pagone J), what might reasonably be expected to be given or agreed to be given under a hypothetical agreement if the parties had been independent and were dealing at arm's length is an objective determination.

398 Accordingly, if it were necessary to decide, I would be satisfied that the taxpayer had established the predicate of a 23% price sharing agreement with the quotational period clause found in the February 2007 Agreement.

SINGLE ENTITY RULE

399 An additional argument advanced by the taxpayer was that Div 13 did not apply to it because the relevant international agreement was between GIAG and CMPL and, although in accordance with the single entity rule in s 701-1 of the ITAA 1997 CMPL is taken to be part of the taxpayer, being the head company of the taxpayer's MEC group, for the purposes of working out amounts of income tax liability and losses of the taxpayer, the single entity rule does not deem an international agreement under s 136AD(1) to have been entered into by a head company when it was in fact entered into by a subsidiary member of the relevant tax group. The taxpayer relied on the following passage in *Channel Pastoral Holdings Pty Ltd v Federal Commissioner of Taxation* (2015) 232 FCR 162; [2015] FCAFC 57 at [119]:

It is convenient to speak of Div 701 as the "single entity rule" applying to the members of a consolidated group, as the heading to s 701-1 indicates, but it is important not to confuse whatever might be understood by such a label or description with what the section actually provides. The effect of Div 701 has been described as creating a statutory fiction but it may be more helpful, and more accurate, to describe its effect as a statutory direction concerned with the calculation of a composite liability. The statutory direction in s 701-1(1) is not that a subsidiary of a consolidated group is to be treated as non-existent, or that it ceases to be a taxpayer or that it does not derive or make assessable income or gains, or does not incur losses or outgoings. The statutory direction, rather, contemplates the continued existence of a subsidiary of a consolidated group but directs that for the limited purposes of determining "liability" or "losses" of the members of the group, the subsidiary is to be treated as [part] of the head company... The single entity rule is a statutory direction which removes the need, which had previously existed under the former grouping provisions, for separate returns and assessments, **but the rule does not create a general statutory fiction that the individual parts of the consolidated group do not continue to have an existence or that their individual existence is not specifically relevant in the working out of the liability ultimately falling upon the head company.**

(Emphasis added in the taxpayer's submissions.)

400 That passage does not support the proposition advanced. To the contrary, as made clear in that passage, the single entity rule operates as a “statutory direction” that, for the limited purposes of determining “liability” or “losses” of the members of the group, the subsidiary is to be treated as part of the head company, rather than as a separate entity, and for that purpose, the actions and transactions of the subsidiary member are treated as having been undertaken by the head company. The single entity rule does not have the effect that a subsidiary of a consolidated group is to be treated as non-existent, or that it ceases to be a taxpayer or that it does not derive or make assessable income or gains, or does not incur losses or outgoings. For the purposes of the application of Div 13 the relevant “taxpayer” is still CMPL and so too for the purposes of Subdiv 815-A, the relevant “entity” is CMPL. There is no inconsistency between these provisions and the single entity rule.

PENALTIES

401 In view of my conclusion, the question as to whether the refusal of the Commissioner to remit all or part of the shortfall interest charge imposed on the taxpayer does not arise for consideration.

OBSERVATIONS ON THE EXPERTS’ EVIDENCE

402 Ultimately, the outcome in this case did not turn on preferring the evidence of one expert over another expert on matters where conflicting opinions were expressed by the experts. However, had the case required the Court to determine whose evidence to accept where the experts did express differences of opinion, the following oft-repeated observations about the role of the expert would have become material in assessing the evidence.

403 The reports of each of the mining industry experts included expressions of opinions on matters outside their specialist knowledge and, in some instances, without the witness having any foundation for the view expressed. Experts, however, perform a particular role. The role of the expert is to provide independent assistance to the Court by providing an objective and impartial opinion on matters within the specialist knowledge of the expert: s 79 of the *Evidence Act 1995* (Cth) (“**Evidence Act**”). It is not the role of the expert to be an advocate for the party calling them nor to express views or speculate on matters about which the expert does not have specialist knowledge. An expert should make it clear when a matter falls outside his or her expertise. Experts need to exercise particular caution to avoid making assertions of fact which have no foundation, otherwise they are seen to be advocating a case rather than providing objective and impartial assistance. Unfounded or speculative reasoning may also undermine

or diminish the persuasiveness and cogency of the opinions expressed by the expert on matters on which she or she is qualified to give an opinion, eroding confidence in the accuracy, reliability and objectivity of such opinions. In the present case, each of the experts, obviously keen to supply with the Court with reasoning supporting the position of the party on whose behalf they gave evidence, strayed from time to time into becoming advocates for the party by proffering opinions and making comments on matters which they were not qualified to give. Experts should be mindful of their role to assist the Court and take care to comply with the Code of Conduct in expressing their views.

404 There is another reason for doubt to be expressed about the reliability of Mr Kowal's evidence. There is significant uncertainty as to the extent to which Mr Kowal himself authored his reports. He was engaged by Charles River & Associates in 2016 to assist with advice it was providing to the Commissioner in connection with the audit of Glencore. Mr Kowal said that "Charles Rivers was the contractor to the AGS, and Charles Rivers asked me to help them in certain aspects of the preparation of the report". Mr Kowal's report was described by him as a "report made by Charles River & Associates that [he] had input into". Although Mr Kowal stated that "by far the majority [of his report] is mine" he frankly conceded that components of his report were prepared by Charles River & Associates and it remains wholly unclear which parts of his reports were prepared by him and which parts were not. In the circumstances I cannot conclude that the expressions of opinion in his report are based "wholly or substantially" on specialist knowledge possessed by Mr Kowal based on his training, study or experience as required by s 79 of the Evidence Act.

CONCLUSION

405 In view of my conclusions, the objection decisions should be set aside and the amended assessments for the 2007, 2008 and 2009 income years set aside. Subject to argument by the parties, there should be an order that the Commissioner pay the taxpayer's costs of the proceedings.

I certify that the preceding four hundred and five (405) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Davies.

Associate:

Dated: 3 September 2019