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## **SUBMISSION TO THE AUSTRALIAN TREASURY**

### **CONSULTATION PAPER – OPTIONS TO ADDRESS THE DESIGN ISSUES IDENTIFIED IN THE PETROLEUM RESOURCE RENT TAX REVIEW (CONSULTATION PAPER)**

Woodside welcomes the opportunity to provide this submission in response to the Consultation Paper (including the Part A and Part B Recommendations) and looks forward to participating in further consultation.

#### **Executive Summary**

Woodside was encouraged by the Treasurer's recognition of Petroleum Resource Rent Tax (PRRT) as the preferred way to achieve a fair return to the community without discouraging investment.

Woodside supports the Part B Recommendations relevant to the offshore industry.

However, Woodside believes that elements of the Part A Recommendation have the potential to undermine stability, fairness and competitiveness of Australia's tax regime, as:

- the substantial investments already made via exploration permits and retention leases may not be respected – potentially increasing concerns over fiscal risk;
- Government may end up picking the “winners” and “losers” in the industry as a result of decisions to apply different fiscal terms to different projects;
- changes to the PRRT alone do not address issues with broader fiscal settings which are required to ensure a level playing field; and
- changes to PRRT and the broader fiscal terms should also be focussed on encouraging investment in growth projects, including incentivising the use of existing infrastructure to minimise project costs and maximise returns to both the Government and project proponents as well as encouraging investment in assets that offset climate change effects.

Woodside believes that a working group should be established representing policy-setters, administrators and industry, to consider further the concerns raised and recommend a package of fiscal changes to Government. There is precedent for this type of consultation developing sustainable solutions in relatively contained timeframes.

Woodside would fully support a process of this nature and would commit to a reasonable timeframe in which recommendations could be made. Woodside has also participated in similar consultation forums with industry, including:

- the Australian Taxation Office (ATO) Energy and Resources Working Group;
- the Resource Tax Implementation Group – established by Government to support the legislative drafting of resource taxation reforms; and
- the Business Tax Working Group established by the Treasurer.

## The Part A Recommendations

Woodside is the largest Australian head-quartered oil and gas company with interests in both producing Liquefied Natural Gas (LNG) projects and future LNG developments.

We understand that our social licence to operate relies on establishing and maintaining meaningful and long-lasting relationships with our stakeholders and the communities in which we operate.

These are just some of our contributions:

- since 2001, Woodside has paid A\$2 billion in PRRT across its Australian portfolio;
- Woodside paid approximately A\$525 million in taxes and royalties to the Commonwealth and State Governments of Australia in 2016;
- Woodside has paid more than A\$6 billion in taxes in Australia over the past five years;
- as an operator, in 2016, Woodside spent nearly A\$4 billion on local content and services to support Australian jobs and businesses – this represented 83% of the company's total global content spend; and
- Woodside supplied over 20% of the total gas for Western Australia in 2016.

Woodside is uniquely invested in ensuring the ongoing stability, fairness and competitiveness of Australia's tax regime.

Woodside believes that elements of the Part A Recommendations have the potential to undermine these principles as outlined below.

### Substantial investments have already been made in exploration permits and retention leases

It was recognised in the PRRT Review that any significant increase in the tax on existing petroleum projects may substantially increase concerns over fiscal risk. In recognition of this principle, existing projects (i.e. those with a production licence in force) are to be excluded from the Part A Recommendations.

However, this does not take into account the substantial investments already made via exploration permits and retention leases which were based on tax arrangements in place for nearly 30 years. If any of the elements of the Part A Recommendations are implemented for these investments, concerns over fiscal risk may be increased.

In addition, it would be perverse for future developments from these permits or leases to be taxed more heavily as this would be a disincentive to their progression.

Creating two classes of PRRT projects, new and existing, is also problematic.

The exclusion of existing exploration permits and retention leases, or other appropriate transition arrangements, should be subject to further consultation.

### Unintentionally picking the winners and losers

Even if the concerns on fiscal risk are put aside, Government may end up unintentionally picking the "winners" and "losers" in the industry.

Companies have different PRRT profiles, even within the same projects. This is due to many reasons such the type of projects invested in (gas and oil projects have different PRRT profiles), the extent of exploration portfolios (because these can be used to offset taxable profits in some circumstances) and the length of time these projects have been operating (because relatively new projects will have significant pools of unutilised credits which augment over time).

This means that the potential changes to the PRRT as set out in the Part A Recommendations will have different implications for different companies. For example, companies that have few future growth options will be less impacted by prospective changes to the legislation. Companies seeking to invest in growth projects may be more affected by prospective changes and these are the very companies which the legislation should support as they seek to sanction new growth.

Adopting any of the elements in the Part A Recommendations, as they currently stand, could mean that some companies are left relatively unaffected whilst others could face additional hurdles in seeking to sanction growth projects. Australia still has significant discovered resources which have yet to be commercialised. These resources should not be impeded for the sake of “grandfathering” perceived benefits to old projects.

Consideration of the impact of potential changes on particular projects should be subject to further consultation, particularly in relation to the manner in which such changes may be transitioned.

#### *The Australian tax regime should be considered holistically*

Project proponents can be expected to pay taxes that account for typically 70% of the total value that projects generate (calculated on Net Present Value basis). This is already a high percentage ‘government take’ before any changes to the PRRT are made.

We note that PRRT is only one of the taxes that support this government take; there is also corporate tax. Changes to the PRRT alone do not address issues with broader fiscal settings which are required to ensure a level playing field.

Consideration should be given to balancing the Part A Recommendations with changes to other fiscal settings in either the PRRT itself or corporate tax laws. This matter could be further explored by the proposed working group.

#### *Incentivising the next wave of growth*

Australia has significant discovered but yet to be commercialised resources. It is important that fiscal settings, including the PRRT, are such that the commercialisation of these resources is encouraged and supported. This will ensure a fair return to both project proponents and the Australian revenue as the alternative may be that these resources do not get developed and the economic benefits to all associated with this growth will not materialise.

Some areas where incentives could be considered include:

- encouraging the use of existing infrastructure – this will reduce the overall cost of commercialising new resources and will maximise the return both to project proponents and the Australian revenue. Such incentives could include PRRT and corporate tax relief for asset swap arrangements which would reduce tax leakage for companies seeking to share infrastructure;
- corporate tax depreciation settings for long life capital intensive projects – changes to effective lives will enhance the profitability of projects for proponents. Such changes will impact the timing of tax receipts whilst still ensuring the Australian revenue receives the same nominal receipts; and
- encouraging the investment in lower emissions technology or in assets that offset climate change effects. This could be by way of additional deductions such as an investment allowance, tax credits or accelerated depreciation.

#### *Specific concerns on elements of the Part A Recommendations*

For completeness, the specific concerns of Woodside in relation to the Part A Recommendations are set out in Appendix A to this submission.

## **The Part B Recommendations**

The Part B Recommendations are considered to be largely administrative in nature and aimed at addressing integrity issues. To the extent relevant to offshore industry, Woodside supports the Part B Recommendations and has worked with Australian Petroleum Production & Exploration Association (APPEA) to develop industry-wide suggestions.

## **The Way Forward**

The design of the PRRT was deliberate to ensure a return to the community for above normal profits derived from natural resources (the 'resource rent') while aiming to minimise distortion of investment decisions. This regime has supported the development of marginal projects which, under a more onerous fiscal setting, would likely not have been developed.

Woodside remains of the strong view that the PRRT continues to work as originally intended. As a profits-based tax, it is not unusual to have declining PRRT at a time of declining oil and gas prices and prior to projects recouping their costs. The benefits from such projects must be measured over their full lifecycle and not adversely judged during periods of commodity price downturn.

However, it is acknowledged that there are perceptions that PRRT is not delivering a fair return to the community given the current economic environment.

Woodside believes that a working group representing policy-setters, administrators and industry be formed to consider further the concerns raised in this submission and recommend a package of fiscal changes to the Government. There is precedent for this type of consultation developing sustainable solutions in a relatively contained timeframe.

Woodside would fully support a process of this nature and would commit to a reasonable timeframe in which recommendations could be developed.

Woodside representatives remain available to discuss our feedback.

Yours sincerely



Anthea McKinnell  
**Acting Chief Financial Officer**

## **Appendix A – Specific concerns on the elements of the Part A Recommendations**

### *The Gas Transfer Price*

The *Petroleum Resource Rent Tax Assessment Regulations 2015* (the Regulations), were created to provide for the gas transfer pricing (GTP) arrangements.

The operation of these GTP arrangements is set out in detail in the Regulations and the accompanying explanatory statements. The design of these Regulations was the subject of detailed discussion and independent study. These took place during an extended period of review and consultation which ran over a number of years. Treasury, the Australian Taxation Office (ATO) and the Australian Petroleum Production & Exploration Association (APPEA) were involved. As a result of the extended consultation, the GTP arrangements include pricing methods and calculations that are largely congruous with commonly accepted transfer pricing methodologies.

The options presented for changes to the GTP arrangements represent a number of fundamental departures from the conclusions reached during that extended consultation. Accordingly, Woodside contends that the GTP arrangements should not be revisited.

### *The Uplift Rates*

Woodside contends that the uplift rates were never intended solely to preserve the real value of undeducted expenditure and compensate for the risk of losing deductions. Rather, the uplift rates are needed to ensure that the after-tax returns are sufficiently high to justify the risks and costs associated with petroleum exploration and development.<sup>1</sup> This distinction and the importance of the existing uplift arrangements, in light of the other settings within the PRRT – such as the high tax rate and the prohibition of refunds on general and exploration expenditure – has also been set out by APPEA in its submission to the PRRT Review.<sup>2</sup>

Woodside believes that the uplift rate for general project expenditure is entirely appropriate and remains a core feature within the PRRT that should not be disturbed.

Also of concern is the proposal to reduce the uplift rates for resource tax expenditures (i.e. state royalties, Commonwealth royalties and excise). Woodside is of the view that these expenditures are, in substance, not unlike other types of general project expenditure. In addition, the PRRT was never intended to be the primary tax on projects subject to these resource taxes. Reducing the uplift rates for resource tax expenditures is not appropriate – it may give rise to double taxation on these projects.

### *The Order of Deductions*

Woodside contends that changing the sequence of deductible expenditure creates a significant distortion between new and existing projects. Existing projects would continue to be allowed to compound exploration expenditure at significantly higher rates whilst new projects have to utilize such expenditure earlier. It is worth re-emphasising that allowing such a change to apply to new projects, without balancing other fiscal settings for these projects, would be an undermining of the principle of competitive neutrality.

### *Transferability*

Woodside comments made in relation to proposed changes to the order of deductions set out above apply equally to the proposed changes to the rules relating to the transferability of exploration expenditure.

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<sup>1</sup> Federal Government (1983) "Discussion Paper on RRT in the Petroleum Sector", p.5. See also Garnaut and Clunies-Ross (1983) "Taxation of Mineral Rents", p.4.

<sup>2</sup> APPEA (2017) "Submission to the Review of the Commonwealth Petroleum Resource Taxes", pp. 62 – 64.