



# SUBMISSION TO THE FEDERAL GOVERNMENT: 2015-16 Federal Budget

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## KEY POINTS

- A key challenge in achieving future growth in the industry is maintaining Australia's international competitiveness in the face of a changing global energy sector. A high-cost local environment, a complex domestic regulatory framework and the potential for other countries to capture market opportunities will continue to make it challenging for Australia to capture the next wave of global investment in the industry. The potential rewards however are significant for the Australian economy.
- An immediate challenge facing the industry in the medium-term is the downward pressure on prices that impact on project economics. The industry is experienced in managing this scenario, however there are important actions that governments initiate to improve the broader investment framework. Many of these are a little or no cost to government revenues.
- In a fiscal context, it is important that:
  - the immediate deductibility of exploration related costs be maintained in full.
  - the existing statutory effective life caps for oil and gas assets be retained and that the Government moves to introduce a phased reduction to match the terms that apply in competitor nations.
  - the crude oil and condensate excise regime be abolished from areas under state and territory jurisdiction to address the disincentive to future investment and the unnecessary red tape being placed in many producers.
  - the Government commits to work directly with industry to identify and implement measures to simplify the administration and operation of the PRRT regime.
- The Government revisits the imposition of cash bidding for the awarding of selected offshore acreage in the context of both the success of the work program bidding system and the pressures being placed on exploration budgets through low commodity prices.
- APPEA recommends legislative amendments be made to the *Fair Work Act 2009* in the areas of greenfields agreements, union rights of entry, protected industrial action and allowable matters under EBA agreements.
- The Government abolishes the duplicative and unnecessary regulatory obligations placed on project developers imposed through the provisions of the *Australian Jobs Act 2013*.
- The Government's energy policy framework focuses on the need to: remove regulatory and other barriers to allow more gas to flow into the gas market and draw a final line under the possibility of a domestic gas reservation policy and/or introduction of a so-called 'national interest' test, by definitively ruling out such policy approaches.



## BACKGROUND

Reliable, secure and competitively priced energy is crucial to our everyday lives in Australia. Oil and gas play a key role in meeting many of our energy needs. This should make the continued growth of this industry a priority for the Australian Government.

A key challenge in achieving future growth in the industry is maintaining Australia's international competitiveness in the face of a changing global energy sector. A high-cost local environment, a complex domestic regulatory framework and the potential for other countries to capture market opportunities will continue to make it challenging for Australia to capture the next wave of global investment in the industry. The potential rewards however are significant for the Australian economy.

An immediate challenge facing the industry in the medium-term is the downward pressure on prices that impact on project economics. The industry is experienced in managing this scenario, however there are important actions that governments initiate to improve the broader investment framework. Many of these are a little or no cost to government revenues.

The global market is now correcting for additional new supplies on line over the past year (much from US shale gas regions) coupled with less robust global demand growth. Global supply has increased at a greater pace than global demand, causing commodity price correction – a fall in the price oil.

**Figure 1: The real price of oil**



For Australian LNG projects, the price for LNG is generally linked to crude prices under long-term contracts. A major price correction of the kind now being experienced is a sharp reminder to big, long-established businesses as well as aspiring new entrants that the need to keep a tight hold on costs, and other fundamental operating issues, is ever-present.



Companies in the oil and gas industry operate in timeframes of a decade or more, taking into account a wide range of possible crude price, economic and policy developments. Short-term fluctuations generally do not have a significant effect on major planning decisions.

In the LNG business, where Australia is an emerging world leader, petroleum project prospects are coming under renewed scrutiny all round the world. Things may be tight in the short-term for Australian projects as costs for services and labour now also face downward pressure.

For industry, the price change means a return to business fundamentals: watching cash flow; scrutinising investment proposals anew, keeping an eye open for opportunities. It means being disciplined in all areas.

Commodity prices may be an uncertainty beyond the control of government but there are areas where governments can manage risk and even take advantage of the present situation. Now is a good time to redouble efforts to remove red tape, streamline project approval times, improve our tax efficiency and competitiveness and to make regulation an advantage in Australia's global competitiveness rather than a burden.

Australia has made some progress here recently but there is a lot more that can be done to enhance the investment environment for the upstream petroleum industry, which is now moving towards its seventh decade of being a national economic advantage.

Regulations that restrict the industry's capacity for innovation and flexibility, that impose unnecessary, duplicative or inconsistent bureaucratic processes unrelated to the risk of activity and that deliver no net benefit to the community can and must be addressed. The present price situation also provides an additional incentive to policymakers to ensure that petroleum investors continue to view this country favourably.

The industry and governments must work collaboratively to ensure projects under construction commence production in a timely manner and new projects continue to be developed. There are some factors that are largely outside the influence of key stakeholders, such as currency movements and fluctuations in commodity prices, however others are within the control of industry and/or governments.

For a range of reasons, Australia's perception as an attractive destination for investment is under pressure. In an environment of continued global competition for scarce capital, investment in Australian exploration and development projects continue to face strong challenges.

A significant level of investment is currently underway within the Australian oil and gas industry. Increased gas demand in Asia over recent years has seen six, following the recent commencement of production from the Queensland Curtis LNG project, of the twelve LNG projects currently under construction globally located in Australia. As these new projects commence production, there will be a significant lift in Australia's exports of resources and energy commodities.



**Box 1: Australian LNG Projects: Producing, Under Construction, Prospective**

Current

North West Shelf Project, Darwin LNG, Pluto, Queensland Curtis LNG

Under Construction

Wheatstone, Gorgon, Prelude, Ichthys, Australia Pacific LNG, Gladstone LNG

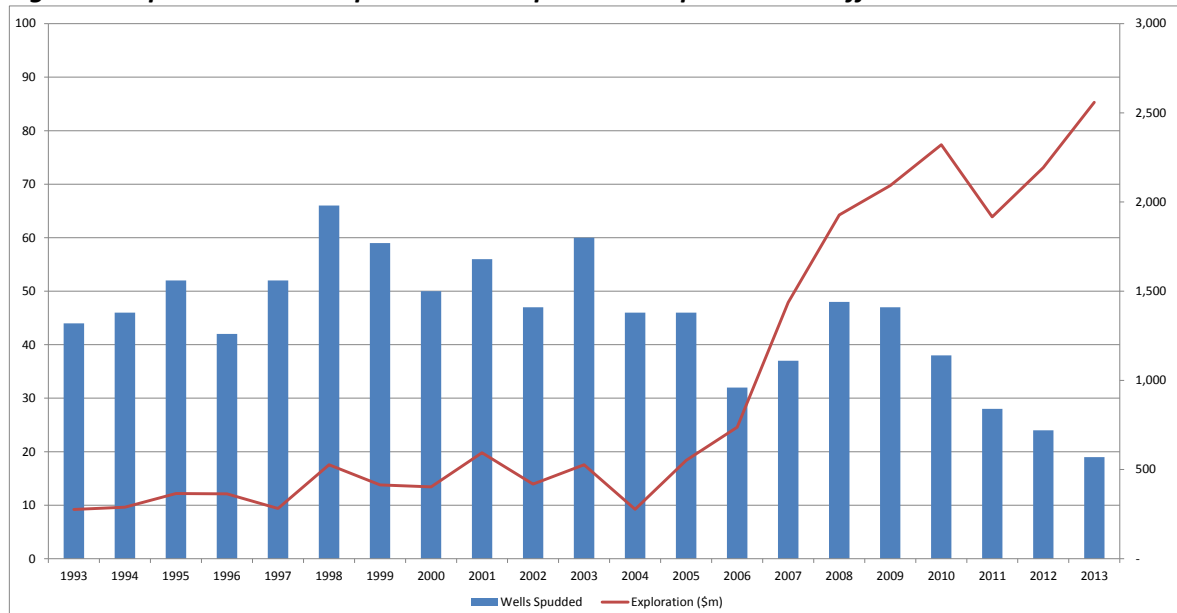
Prospective

Arrow LNG, Browse LNG, Greater Sunrise, Scarborough, Bonaparte LNG

While the Australian economy has benefited (and will continue to benefit significantly) from LNG investments committed to in the past, there are potentially more projects that could see a second wave of investment in the industry. Specifically, there is scope for Australia's LNG exports to expand further through expansion of existing fields and future discoveries.

The long term growth in the Australian oil and gas industry is dependent on the level of exploration. Oil and gas cannot be produced without first locating new resources and these cannot be discovered without drilling wells. The rising cost of oil and gas exploration has coincided with a reduction in the number of offshore exploration wells drilled, which have fallen by more than two thirds since the peak in 1998. See Figure 2.

**Figure 2: Exploration Wells Spudded and Exploration Expenditure – Offshore Areas**



Source: APPEA and ABS

The upstream oil and gas industry is integrated into the global trading system and is one of Australia's most globalised and trade-exposed industries. Investment in the development of Australia's oil and gas resources will depend on the commercial attractiveness of the operating environment. The last decade has been characterised by an increase in the cost of projects. This



has now been further complicated by a fall in key commodity prices together with a project decline in global economic growth.

The bottom line for commercial attractiveness is project economics – operating costs relative to output prices. There are many determinants of profitability – infrastructure suitability and cost, taxation policy, labour costs, location issues through freight costs, fuel and energy costs, communication costs, costs associated with meeting government regulations. Countries compete for a share of global investment largely on the basis of how potential investors consider domestic policies and the social environment contribute to prospective profitability.

Australia's abundant natural gas resources place it in a relatively good position to maintain long-term, cleaner energy security domestically and internationally. Natural gas also makes it possible for Australia to help meet the world's growing energy needs over the coming decades.

Just as importantly, the industry creates significant wealth for the country, including through the employment of many Australians, underpinning the revenue collections of governments and generating valuable export revenue for the Australian economy. Ensuring that we have a competitive fiscal framework is critical in maintaining and improving on Australia's overall global competitive position.

Commitments to new resource developments in Australia have slowed markedly over the last year. As the International Energy Agency (IEA) recently noted, the prospects for another round of major Australian projects will depend heavily on how costs evolve, on the deployment of new technologies, such as floating LNG (FLNG) and hydraulic fracturing, and on competition from other regions, notably North America and East Africa<sup>1</sup>. If not addressed, these cost and productivity challenges threaten to hold back plans for additional export projects.

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<sup>1</sup> International Energy Agency (2013), *World Energy Outlook 2013*, page 99 (available at [www.worldenergyoutlook.org](http://www.worldenergyoutlook.org)).



## ISSUES AND RECOMMENDATIONS

The future economic contribution of the industry will largely be determined through a combination of factors, ranging from successful exploration, further technological developments that will unlock the full potential of new and existing discoveries and the capturing of new market opportunities.

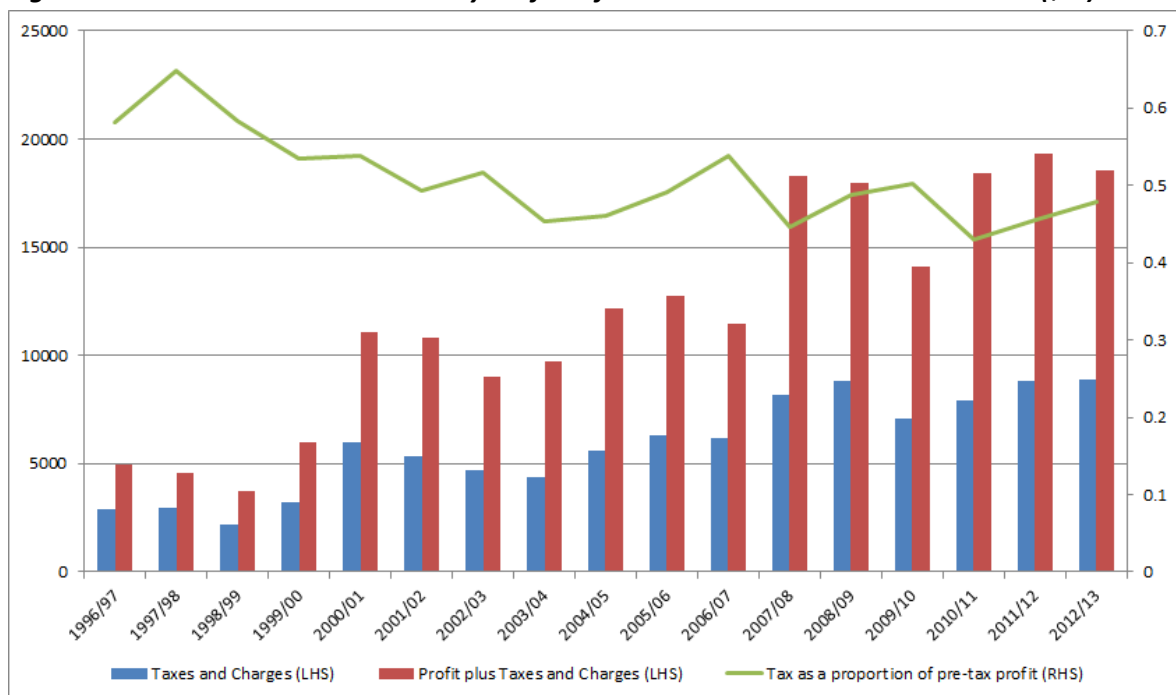
In order to realise the sector's potential, challenges and opportunities must be grasped by governments (on behalf of the community) and industry. Factors that will influence the future growth of the industry in Australia include:

- Maintaining a competitive fiscal framework
- Facilitating access to capital through a regulatory framework that supports investment and industry productivity.
- Achieving timely and secure access to resources for exploration and development.
- Enabling access to domestic and international markets on globally competitive terms without distortionary and interventionist policies.

### MAINTAINING A COMPETITIVE FISCAL FRAMEWORK

The fiscal framework is a key factor that shapes investment decisions in the oil and gas industry. Producers are confronted with an array of taxes, charges and fees in relation to petroleum activities. Fiscal imposts include resource taxes (including the petroleum resource rent tax, petroleum royalties and production excise), company income tax and a wide variety of other taxes, fees and charges. Data compiled by APPEA indicates that on average, taxes account for just under half of the industry's overall level of pre-tax profit (Figure 3).

**Figure 3: Estimated Petroleum Industry Profit Before Tax and Taxation Contributions (\$m)**



Source: APPEA Financial Survey



Total payments have averaged around \$8 billion per year over the last five years. Company tax is estimated to have accounted for slightly more than half of the total amount. Total payments are expected to increase in the coming years as a number of projects currently under construction commence production.

In the context of the 2015-16 Federal Budget, there are a number of areas that need to be addressed to ensure that Australia maintains fiscal competitiveness and that taxation does not impede future exploration and development decisions in the industry.

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## DEDUCTIBILITY OF EXPLORATION COSTS FOR INCOME TAX PURPOSES

The future growth of the industry is dependent on the level of exploration, however petroleum exploration is both high risk and costly. Figure 2 demonstrates the significant fall in exploration that has been recorded in offshore areas within Australia over the last two decades.

Oil and gas cannot be produced without first locating commercially viable resources and these cannot be discovered without undertaking exploration. Based on Geoscience Australia data for the period 1955 to 2011, a total of 4,248 'conventional' exploration wells were drilled in onshore and offshore areas. Of the wells drilled, only 1,200 were considered as being 'discoveries' (a discovery well is defined as a well that recovers petroleum or encounters a producible log pay zone). Of the total number of wells drilled, less than 10 per cent lead to any commercial production.

The immediate deductibility of the majority of exploration related costs has been a central feature of the income tax provisions that have applied to the oil and gas industry for many decades. In the 1976 Asprey Taxation Review, it was recognised that the immediate deductibility of such costs was the appropriate treatment. Specifically, it was stated that:

*"19.19..... Expenditure on exploration, which is a necessary and continuing part of a mining company's operations, should be treated consistently, whether successful or not. The Committee favours the approach that would make all exploration and prospecting expenditure immediately deductible against assessable income derived from any source." Asprey Tax Review, 1975 (pp. 293-94)*

Subsequent reviews into both the industry and the broader taxation framework have supported the continuation of the immediate deductibility provisions.

In the 2013-14 Budget, the Government indicated that it would restrict the immediate deduction for the cost of assets first used for exploration, by excluding certain petroleum (mining) rights and information. It was announced that the following would continue to be immediately deductible:

- costs of mining rights obtained from a relevant government issuing authority;
- costs of mining information from a relevant government authority;
- costs incurred by a taxpayer itself in generating new information or improving existing information; and
- mining rights acquired by a farmee under a recognised 'farm-in, farm-out' arrangement.

While the measure applied from the night of the Budget in 2013, the first tranche of legislation to enact the measure was not passed until mid-2014. Consideration is still being given to important aspects of the measure. A number of practical concerns have been identified by the industry that





are still to be addressed, including needing to ensure taxation does not inhibit parties within a joint venture or with interests in different permits realigning or reconfiguring their interests in order to more efficiently develop resources. In addition, the commitment to include the treatments contained in the current taxation rulings that deal with the treatment of farm-ins/farm-outs needs to be implemented as a matter of priority.

**Recommendation:** The immediate deductibility of exploration related costs that has shaped the historical taxation treatment of such expenditures be maintained in full.

## FACILITATING THE DEVELOPMENT OF DISCOVERED RESOURCES

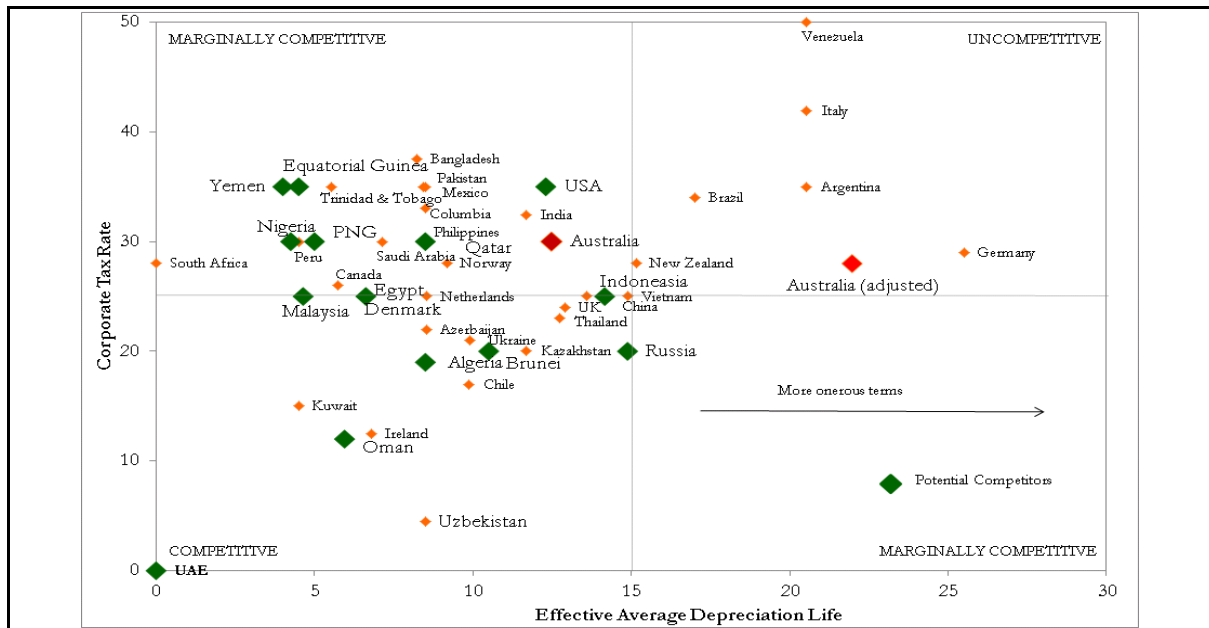
The petroleum industry is at the forefront of globalisation. Capital is mobile and the vast majority is obtained from foreign sources. It is a reality that the future development of the nation's petroleum resources will be heavily reliant on foreign capital and expertise. The loss of a dollar of investment in the Australian oil and gas industry is not replaced by a dollar of investment in other sectors of the Australian economy.

In terms of pursuing capital, investments in oil and gas projects are significantly challenged from a cost perspective. The fiscal terms that apply to these projects are one of the few mechanisms available to the Federal Government to improve the competitive position of these investments.

Under Australia's current company tax rules, the average period over which much of the capital invested in oil and gas projects can be written off for depreciation purposes is between 15 and 20 years. This is much longer than the three-to-ten year write-off periods available to gas projects on other jurisdictions that compete with Australian projects for investment capital. In addition, companies are restricted as to when costs can be deducted to a time when a project is first used. With the long lead times for many developments in the oil and gas industry, this can see deductions being deferred for periods of up to five years (or more).

A study was prepared by KPMG for APPEA that compares two key company tax provisions (the tax rates and the average effective depreciation life) for gas projects across a number of competing jurisdictions. The results are highlighted in Figure 4. The depreciation write-off scale attempts to factor in the special incentives that have been introduced by some countries, including investment allowances or accelerated depreciation (or both) to encourage investment in gas plant and equipment. Australian projects face a challenging framework compared to our competitors.

### **Figure 4 Company Tax Rate/Depreciation Comparison – Gas Projects**



Source: APPEA (based on data supplied by KPMG)

Any decision to adversely change the write-off periods to period longer than currently apply will further disadvantage Australian producers compared with other jurisdictions. In reality, a reduction in the write-off period to say five years would provide a major boost to the economics of large scale gas projects.

**Recommendation:** As a minimum, the existing statutory effective life caps for oil and gas assets be retained. In addition, the Government moves to introduce a phased reduction to match the terms that apply in competitor nations.



The resource taxation framework that applies to oil and gas production in Australia is multi-layered and in many cases involves both Federal and State/Territory governments taxing the same activities.

- Offshore production (excluding the North West Shelf project) is subject to PRRT.
- Production sourced from the North West Shelf project is subject to Commonwealth crude oil and condensate excise and Commonwealth petroleum royalty.
- Onshore production and that sourced from projects located in submerged lands under state jurisdiction and in onshore areas is subject to Commonwealth crude oil and condensate production excise and royalty under the relevant state/territory jurisdiction, plus PRRT.

The crude oil excise regime has been in place since the mid-1970s. It applies to areas in tandem with Commonwealth or state/territory royalties, and since 1 July 2012, PRRT also now applies to projects such to excise and royalties. With the exception of the NWS Project, no other offshore projects are subject to excise.

Production excise was introduced as a levy on each barrel of oil production sold from eligible areas, and was subsequently modified to reflect the timing and production date of discoveries. Condensate was effectively excluded from the scope of the regime in the late 1970's, while in 1987, a 30 million barrel excise exemption was introduced for each field to further stimulate the development of oil discoveries. On 13 May 2008, the Federal Government removed the exemption of condensate from the crude oil excise regime.

Current information in relation to onshore production suggests that very few petroleum fields have or will ever exceed the 30 million barrel excise free allowance threshold. Even in the very limited cases where this threshold may be passed, the annual levels of production will be insufficient to incur an actual excise liability. In effect, there is not expected to be any excise incurred for onshore crude oil and/or condensate production in Australia. Despite this, all onshore producers are required to meet the on-going verification, administrative and compliance obligations imposed by the excise regime.

The imposition of a potential excise liability on onshore crude oil and condensate production (in the event of a future discovery) also has the real potential to discourage future exploration decisions. In particular, this may have implications for exploration in frontier onshore areas where the risk/reward balance can be different to more traditionally explored regions. High risk frontier exploration requires a fiscal framework that provides an incentive for risk capital to be directed towards these areas – the imposition of a potential excise liability on future discoveries clearly sends a strongly negative fiscal signal. Furthermore, the imposition of this form of taxation will be even more complex in the event that liquids production is generated from unconventional sources, where the existing provisions will largely be inoperable due a range of definitional and geological factors.



Most significantly, the Federal Government has also effectively recognised that PRRT is now the primary mechanism for the taxation of crude oil and condensate production and therefore the continued application of excise for areas that are unlikely to incur a liability is inconsistent with established benchmarks.

**Recommendation:** In recognition that:

- PRRT now applies to all onshore petroleum production and is the Federal Government's resource taxation benchmark;
- production excise duty is unlikely to be payable on current onshore discoveries;
- there are ongoing reporting and compliance burdens being placed on many onshore producers; and
- the potentially negative impact that production excise can have on onshore exploration decisions,

APPEA recommends that the existing crude oil and condensate excise regimes be abolished from all areas under state and territory jurisdiction.

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#### PRRT ADMINISTRATION AND COMPLIANCE

The PRRT regime is based on the relatively simple principle of revenues less costs. However, it can be complex and time consuming from a compliance perspective. Prior to 1 July 2012, the scope of the tax was limited to offshore projects, and therefore a relatively small pool of companies were directly impacted. The extension of the regime has seen many more companies (a large proportion are small or mid-sized entities) needing to comply with the provisions. Complex compliance obligations exist irrespective of whether a tax liability is incurred (which will generally not be the case).

For onshore operations, companies are effectively operating under a dual resource taxation framework (Federal and state) and therefore need to place a greater proportion of their limited resources on tax compliance. A reduction in the compliance burden on small and mid-sized companies should be a priority for government.

The decision to extend the tax onshore was a complex and costly process. The industry has worked with government to attempt to address the numerous technical issues that have arisen from the introduction and application of the tax. Work still needs to be done on a range of matters to ensure that the regime operates effectively and anomalous outcomes are addressed. The Australian Taxation Office has now commenced a process of auditing companies with onshore interests which is placing a further strain on the limited resources of impacted entities.



APPEA notes that in a joint media release from the Treasurer, Minister for Industry and the Minister for Finance on 24 October 2013, it was indicated that *“In relation to the Petroleum Resource Rent Tax, the Government is considering the issue of the onshore administration of this tax, in the context of its deregulation agenda and the removal of red tape.”*

**Recommendation:** The Government commits to work directly with industry to identify and implement measures to simplify the administration of the PRRT regime to reduce the burden on small and mid-sized entities.

#### CASH BIDDING FOR NOMINATED ‘OFFSHORE’ ACREAGE

APPEA has been a long and strong supporter of the work program bidding system for the allocation of exploration acreage. The work program bidding system has served Australia well and has positioned the nation to be a supplier of gas to both domestic and global markets. The industry is estimated to have paid nearly \$200 billion in resource taxation since the early 1970’s. Legislation was passed in late 2013 that introduced cash bidding for nominated offshore acreage. The first round of acreage to be released that will be subject to the new cash bidding provisions will be released during 2015.

The Minister for Industry and Science, the Hon Ian Macfarlane MP, has recently been reported as saying that the fall in world oil prices to below \$US60 a barrel would precipitate significant cuts in oil and gas exploration in Australia, which would reduce (gas) supplies in the medium term. Specifically, the Minister is quoted as saying the *“Every oil and gas company in Australia will be cutting back on its exploration and development with oil prices sitting at \$60”*<sup>2</sup>.

While potentially providing the Federal Government with revenues through the acreage allocation process, the reality is that the measure will act to reduce funds available for exploration and in the longer term, negatively impact on taxation revenues from the production of oil and gas resources. In an environment of potentially low commodity prices, such a measure needs to be reconsidered as a matter of priority.

**Recommendation:** That the Government revisits the imposition of cash bidding for the awarding of selected offshore acreage in the context of both the success of the work program bidding system and the pressures being placed on exploration budgets through low commodity prices.

<sup>2</sup> Maher, Sid. 'Oil Plunge To Worsen Gas Crisis, Warns Ian Macfarlane'. The Australian 3<sup>rd</sup> January 2015. Available: <http://www.theaustralian.com.au/business/mining-energy/oil-plunge-to-worsen-gas-crisis-warns-ian-macfarlane/story-e6frg9df-1227173155468>



## FACILITATING ACCESS TO CAPITAL THROUGH A REGULATORY FRAMEWORK THAT SUPPORTS INVESTMENT AND INDUSTRY PRODUCTIVITY

### INDUSTRIAL RELATIONS REFORM

The Productivity Commission's review of Australia's workplace relations framework provides an opportunity for much-needed reform of a system that is failing the national interest. Improving workplace productivity is a crucial part of the global competitive challenge facing Australia's oil and gas industry.

Australia is regarded as a relatively high cost location for LNG projects due to their complexity, remote locations and most significantly the exposure to some of the highest construction costs in the world.

Australia's oil and gas industry believes strongly that labour relations reform must be placed at the centre of the national productivity agenda. To that end, APPEA has developed a blueprint for workplace relations reform in major project construction which aims to drive much-needed productivity growth and improve the industry's global competitiveness.

APPEA's blueprint for change – *Improving Labour Productivity: A Regulatory Reform Agenda*<sup>3</sup> – highlights a range of sector-specific problems with the *Fair Work Act 2009* (FWA) and makes a number of important recommendations. These changes are not only sensible, responsible, and achievable within the Federal Government's current term of office, but also critical if the sector is to increase investment and deliver more jobs.

In its current form, the FWA encourages high labour costs and low productivity on major resource project construction. It facilitates the continued ratcheting up of wages and allowances and project owners cannot be confident about the cost of labour over the full life-span of construction. This is undermining Australia's ability to capitalise on growing global demand for LNG.

Problems on major projects relate to both how terms and conditions are set at the outset of the agreement (greenfields agreement provisions) and risks to project performance and competitiveness despite one or more agreements being in place. These problems include the:

- Risk of protected industrial action during renegotiation.
- Broad scope of 'permitted matters' over which bargaining can take place.
- Misuse of right of entry provisions.
- Impact of unprotected action.

While APPEA welcomes the proposed amendments to the FWA, the oil and gas industry believes further amendments are needed. Specifically, adopting a new form of enterprise agreement –

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<sup>3</sup> See [www.appea.com.au/media\\_release/labour-reform-crucial-to-boost-australias-competitiveness](http://www.appea.com.au/media_release/labour-reform-crucial-to-boost-australias-competitiveness) and [www.appea.com.au/wp-content/uploads/2014/04/APPEA\\_ILP-report\\_web.pdf](http://www.appea.com.au/wp-content/uploads/2014/04/APPEA_ILP-report_web.pdf) for further information.



Major Project Agreements (MPAs) – that would specifically apply to major capital projects, such as multi-billion dollar LNG plants.

These MPAs would reflect both the scale of these projects and the timeframe required to develop them by:

- Limiting the time available to negotiate.
- Having the Agreement apply for the entire period of project construction as opposed to a renegotiation every four years.
- Requiring negotiations to be specific to individual major projects' circumstances, thus preventing the most recent deal struck automatically becoming the minimum benchmark for the next.

Once an MPA has been put in place, further reforms to protect major capital investments are required, including:

- Changing Right of Entry provisions, applying them only to those unions with which agreements have been made and subjecting permit applications to greater scrutiny.
- Bigger fines for unlawful industrial action.
- Raising the threshold for protected industrial action.
- Anti-picketing laws that deliver faster determinations regarding lawfulness.
- Re-introducing a well-resourced Australian Building and Construction Commission.

Urgent reform of the FWA is required in the following areas:

- Remove maritime unions as the sole and default bargaining representative body for employees in the maritime sector.
- Reduce access to legally protected industrial action; this should be an option of last resort used only when all other options are exhausted and only after genuine attempts to reach a satisfactory resolution.
- Reduce the scope of matters that can be included in enterprise agreements and over which industrial action can be taken. Ensure allowable matters relate to the direct relationship between employers and employees, not to third parties. This includes clauses that restrict hiring practices, entrench a union closed shop and undermine managerial decision-making.

**Recommendation:** APPEA recommends legislative amendments be made to the *Fair Work Act 2009* in the areas of greenfields agreements, union rights of entry, protected industrial action and allowable matters under EBA agreements.

## PROMOTING LOCAL INDUSTRY PARTICIPATION – THE AUSTRALIAN JOBS ACT 2013

The *Australian Jobs Act 2013* (the Act) was introduced in 2013 as part of a broader local industry participation policy and seeks to influence procurement decisions connected with large investment projects in Australia. Rather than achieving its stated objective of increased local content in major projects, the Act imposes duplicative and unnecessary burdens on companies while distorting the efforts and outcomes of existing company procurement systems and processes. Existing systems already provide for full, fair and reasonable opportunity for local suppliers to participate in the delivery and operation of major projects.



The oil and gas industry recognises that local suppliers can provide significant advantages to projects through faster turnaround of services, localised employment, improved timings and improved communication. The industry continues to invest heavily both in financial terms and in the development of collaborative relationships to address capability, capacity, skills and training gaps.

When coupled with the potential for injunctions and other penalties, the Act introduces a system of onerous and complex administrative requirements to deliver the same results that companies have been achieving for some time. For example, the introduction of a 'trigger date' for the provision of an Australian Industry Participation (AIP) Plan without any clear need or definition has created significant ambiguity. As a result, the Act increases uncertainty and escalates compliance costs (particularly for smaller projects and/or those with limited exposure to the existing Enhanced Project By-Law Scheme (EPBS) structure) without a demonstrated commensurate additional benefit to Australian suppliers.

Government's should be more focused on providing a framework on allowing Australia to capture the next wave of potential capital projects rather than burdening entities with unnecessary red and green tape.

The Government should be encouraging local supplies to strengthen capabilities in the following areas.

- Having appropriate management systems to address legislative requirements for health, safety and environment
- Developing systems and processes required to prequalify.
- Knowing how to tender and submit compliant tenders.
- Complying with globally accepted technical standards for asset integrity and safety.

**Recommendation:** The Government should abolish the duplicative and unnecessary regulatory obligations placed on project developers imposed through the provisions of the *Australian Jobs Act 2013*.





## REGULATORY STREAMLINING

### ENSURING EFFECTIVE REGULATORY FRAMEWORKS

Regulation that is burdensome or imposes bureaucratic processes unrelated to the risk of the activity poses a real threat to ongoing investment, growth and prosperity in Australia. It also inhibits the industry's capacity to quickly react to changing global conditions and remain internationally competitive.

In particular, the need for an efficient regulatory environment and an ongoing Government led deregulation agenda must also be viewed in the context of the current downturn in the global oil price (as mentioned earlier). Exploration in particular, is very sensitive to projected prices of crude oil. With prices dropping, new exploration activity will be in decline. Around the world, explorers are winding back drilling programs and rigs are being stacked.

Processes that restrict innovation and flexibility, and impose unnecessary, duplicative or inconsistent bureaucratic processes unrelated to the risk of the activity and for no net benefit, pose a real threat to ongoing investment and growth in a constrained financial market. While many impacts on current and future investment, such as the high Australian dollar and low price of oil, are largely beyond the ability of industry or governments to influence, other key challenges such as deregulation must be addressed. The regulatory burden and fiscal arrangements facing Australian business is a challenge to our ability to quickly react to changing global conditions and remain internationally competitive. Importantly, addressing the regulatory complexity presents governments with the opportunity to generate real benefits at relatively little (if any) cost.

Australia's regulatory framework, particularly environmental regulation, contains overlapping, excessive duplicative and inconsistent requirements that are causing unnecessary project delays and ratcheting up costs. Green and Red tape is consistently raised by oil and gas companies as one of the top issues impacting the global competitiveness of Australia's resource sector.

A recent report from the World Economic Forum<sup>4</sup> has ranked Australia's trade competitiveness down by nine spots to 23<sup>rd</sup> in the world in 2014, with government regulation identified as one of the main contributors to the slump (along with restrictive labor regulations and tax rates). Australia sits at 124 (out of 144 countries in the survey) for burdensome Government regulation. At a time when new and lower cost oil and gas competitors in East Africa, North American and other locations are emerging, it is critical that Australia reduces unnecessary regulatory costs and improves productivity.

APPEA commends the Federal Government on the work undertaken so far in addressing unnecessary regulation and in reducing the compliance burden on businesses. A continuation of these initiatives should occur and be considered in the context of the 2015 budget.

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<sup>4</sup> World Economic Forum (2014), *The Global Competitiveness Report 2014 – 2015* (available at [www.weforum.org/issues/global-competitiveness](http://www.weforum.org/issues/global-competitiveness)).



ENABLE ACCESS TO DOMESTIC AND INTERNATIONAL MARKETS ON GLOBALLY COMPETITIVE TERMS WITHOUT DISTORTIONARY AND INTERVENTIONIST POLICIES.

ENERGY POLICY

In all sectors of the economy – not just oil and gas — maintaining access to open and competitive markets is in Australia's best interest.

APPEA in November 2014 provided a detailed submission to the Government's Energy Green Paper (EGP) supporting the development of the Energy White Paper (EWP).

Together with the Federal Budget, the EWP development process provides the opportunity to develop a policy framework to guide and facilitate the long-term development of Australia's energy industry. The EWP should therefore have a long-term focus with policy measures supporting the operation and enhancement of competitive markets.

Energy policy should in particular focus on efficient and competitive markets, increases in new energy sources to ease demand/supply constraints, regulatory reform and the need for removal of unnecessary barriers to continued investment in exploration and production.

As was noted above, Australia's upstream oil and gas industry is delivering substantial, economy-wide benefits in terms of investment, jobs, and regional development. For these benefits to be sustained, governments must resist calls for policy interventions that force non-commercial outcomes.

As one of Australia's highest value-adding industries, Australia's oil and gas industry should be a key part in any government policy measures aimed at developing high value-added products and services whether for domestic or export markets.

Analysis by PwC, released as part of APPEA's EGP submission, shows that for every dollar of domestic production, the oil and gas sector value-adds 70 cents to Australian output<sup>5</sup>. This compares to an average of 49 cents for every dollar of production for all other industries.

Too often in the current policy debate, however, many regard raising the value of a product through further processing as synonymous with increasing value added. The PwC analysis, like others before it, show that manufacturing is generally associated with quite low value-added contributions, particularly in comparison to the gas industry. The manufacturing industry adds less than 30 cents for every \$1 of supply used.

Australia's energy policy framework must therefore ensure that Australia's explorers and producers are not disadvantaged against producers of other energy sources – in Australia or

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<sup>5</sup> PwC (2014), *Value-adding: Australian Oil and Gas Industry, September 2014* (available at [www.appea.com.au/wp-content/uploads/2014/11/PwC-Report-Oil-and-Gas-Industry-Sept-2014-FINAL.pdf](http://www.appea.com.au/wp-content/uploads/2014/11/PwC-Report-Oil-and-Gas-Industry-Sept-2014-FINAL.pdf)).



overseas and attracts increased exploration in the many yet-to-be explored or under-explored areas of Australia.

Australia's gas supply industry is focussed on both its domestic and export markets and, as was outlined above, the Australian natural gas industry creates significant wealth for the country. The Government should continue to reject calls for inefficient, inappropriate and ineffective regulatory interventions, such as gas market reservation policies or so-called 'national interest' test and focus instead on market-based energy policies.

The Government should instead focus on the need to: remove regulatory and other barriers to allow more gas to flow into the gas market and draw a final line under the possibility of a domestic gas reservation policy and/or introduction of a so called 'national interest' test, by definitively ruling out such policy approaches.

Possible measures to promote greater price transparency in gas markets were considered in APPEA's submission to the Department's *Eastern Australian Domestic Gas Market Study* and to the *EWP Issues Paper*. The range of gas supply agreements that have been struck since the November 2012 EWP<sup>6</sup> and projects that have commenced production and supply to the domestic market suggests that there is sufficient information available to allow supply contracts to be concluded between willing buyers and sellers and for a range of other commercial arrangements to take place.

APPEA recognises the importance of ensuring a competitive and well informed Australian gas market continues to develop and also acknowledges the importance that bilateral contracts have played in underpinning market development across Australia.

Gas prices are increasing for a number of reasons, many of them not directly related to the transition of the eastern Australian market to include gas exports. New analysis by EnergyQuest<sup>7</sup> shows petroleum industry costs have been increasing globally and in Australia since 2000. Finding and development costs for new reserves increased six-fold between 2000 and 2013.

APPEA in particular rejects the need for an Australian Competition and Consumer Commission Price Inquiry into the eastern Australian wholesale gas market, or a Productivity Commission review (as was contemplated in the Energy Green Paper). There is no benefit in adding further to the profusion of reviews to which the gas market been subject in recent years. In particular, recommendations for a further review of the competitive nature of the gas market are unnecessary and will lead to further market uncertainty.

In relation to liquids, Australia will continue to produce a proportion of its liquids requirements from indigenous sources, however will rely on access to international markets for a growing proportion of its requirements. The key means by which Australia can secure its important liquids

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<sup>6</sup> See [www.appea.com.au/wp-content/uploads/2014/09/Gas-supply-deals-since-Nov-2012.pdf](http://www.appea.com.au/wp-content/uploads/2014/09/Gas-supply-deals-since-Nov-2012.pdf) for the most up-to-date list.

<sup>7</sup> A copy of the report, *Oil and Gas Industry Cost Trends*, is available at [www.appea.com.au/wp-content/uploads/2014/11/APPEA-Cost-Report\\_Final.pdf](http://www.appea.com.au/wp-content/uploads/2014/11/APPEA-Cost-Report_Final.pdf).



requirements, therefore, is through continued local exploration and ongoing and open access to international markets.

APPEA does not support the allocation of a fuel reserve volume to meet energy security arrangements. Energy security is best achieved through: allowing market forces to drive the selection of choices by ensuring that the various forms of primary energy compete on an equitable basis; a tax and regulatory framework that is stable and consistent; minimising complexity of regulatory processes; promoting global participation both with respect to sourcing or exporting energy and allowing trade in technology; and an attractive environment for exploration in Australia.

**Recommendation:** The Government's energy policy framework should focus on the need to: remove regulatory and other barriers to allow more gas to flow into the gas market and draw a final line under the possibility of a domestic gas reservation policy and/or introduction of a so-called 'national interest' test, by definitively ruling out such policy approaches.