

Revenue Legislation Amendment Regulation (No. 1) 2016

Explanatory notes for SL 2016 No. 25

made under the

Mineral Resources Act 1989

Petroleum and Gas (Production and Safety) Act 2004

General Outline

Short title

Revenue Legislation Amendment Regulation (No. 1) 2016

Authorising law

Sections 321, 417(1) and (2)(l) of the *Mineral Resources Act 1989*

Sections 590(3) and 859(1) of the *Petroleum and Gas (Production and Safety) Act 2004*

Policy objectives and the reasons for them

The main policy objective of the Regulation is to amend the *Petroleum and Gas (Production and Safety) Regulation 2004* to make improvements to strengthen the integrity of the royalty administration framework, providing certainty for royalty payers and ensuring that royalty liabilities are correctly accounted for. A further policy objective is to make consequential amendments to the *Mineral Resources Regulation 2013* ensuring, to the extent possible, consistency between the petroleum and mineral royalty administration frameworks.

Petroleum royalty is payable on any petroleum produced by a petroleum producer. The petroleum royalty rate is 10% of the wellhead value of the petroleum disposed of or, if s. 147(1)(b) of the *Petroleum and Gas (Production and Safety) Regulation 2004* applies, produced, by the petroleum producer.

The *Petroleum and Gas (Production and Safety) Regulation 2004* prescribes the method for working out the wellhead value of petroleum. The wellhead value is generally the amount the petroleum could reasonably be expected to realise if it were sold commercially, less the sum of certain expenses and any negative wellhead value.

The *Petroleum and Gas (Production and Safety) Regulation 2004* also prescribes when and how the Minister may make a petroleum royalty decision. A petroleum royalty decision is a decision about how one or more of the components of the wellhead value must be worked out for a particular transaction or particular period.

Under the *Petroleum and Gas (Production and Safety) Regulation 2004*, a petroleum royalty decision may be made if the Minister or a petroleum producer reasonably believes that the amount the producer determines the petroleum could reasonably be expected to realise is less than the market value of the petroleum or that certain expenses are more than the expenses that would reasonably be incurred in the circumstances. Given the complexity and variables involved in determining a component of the wellhead value, a petroleum producer may also seek a decision from the Minister about how one or more components of the wellhead value must be worked out.

The petroleum royalty decision provisions therefore provide an administrative framework to ensure the components of the wellhead value are determined on the basis of an arms-length transaction at market value. This is necessary as petroleum producers may dispose of the petroleum other than by selling it, such as using or flaring petroleum, or enter into petroleum transactions with related parties on terms which may not always reflect normal commercial terms.

For these reasons, it is imperative the petroleum royalty decision framework is sufficiently clear and operates to ensure the components of the wellhead value are correctly worked out and consequently, the correct petroleum royalty paid.

Similar to a petroleum royalty decision, a gross value royalty decision made under the *Mineral Resources Regulation 2013* is used to establish the value of certain minerals for the purpose of determining the correct mineral royalty liability payable. The *Mineral Resources Regulation 2013* provides an administrative framework to support the making of gross value royalty decisions. The gross value royalty decision provisions were reviewed and their operation clarified when the *Mineral Resources Regulation 2013* was remade in 2013.

From an administrative perspective, it is beneficial for the petroleum royalty decision framework to align with the gross value royalty decision framework. This ensures consistency and certainty for royalty payers, especially for those with joint petroleum and mineral royalty liabilities.

Achievement of policy objectives

The objectives will be achieved by:

- amending the *Petroleum and Gas (Production and Safety) Regulation 2004* to implement a new petroleum royalty decision framework; and
- making consequential amendments to the *Mineral Resources Regulation 2013* to align the gross value royalty decision framework with the new petroleum royalty decision framework to the extent possible.

Implementation of a new petroleum royalty decision framework will provide certainty for industry and the State regarding the scope and application of petroleum royalty decisions. The new framework specifies:

- how a petroleum producer may apply for a petroleum royalty decision;
- when the Minister may make a petroleum royalty decision;
- a petroleum producer's obligation to notify the Minister of particular circumstances affecting a petroleum royalty decision;
- the Minister's powers for making and amending a petroleum royalty decision;

- how royalty is to be accounted for prior to the making of a petroleum royalty decision; and
- a petroleum producer's rights of review.

Generally, the new framework operates for any petroleum disposed of, or produced, on or after commencement. Transitional arrangements apply in relation to existing petroleum royalty applications and decisions.

To the extent possible, the new petroleum royalty decision framework has been modelled on the established gross value royalty decision framework in the *Mineral Resources Regulation 2013*, subject to any modifications required to reflect the particular nature of petroleum royalty. Consequential amendments to the *Mineral Resources Regulation 2013* will refine the existing gross value royalty decision framework to align the two decision frameworks to the extent possible.

The policy objectives can only be achieved through legislative amendment. The amendments are administrative in nature and do not affect the underlying basis of royalty liability.

Consistency with policy objectives of authorising law

The amendments to the *Petroleum and Gas (Production and Safety) Regulation 2004* are consistent with the policy objectives of the authorising law as the new petroleum royalty decision framework prescribes how to work out the value of petroleum for petroleum royalty purposes pursuant to section 590(3) of the *Petroleum and Gas (Production and Safety) Act 2004*.

The amendments to the gross value royalty decision framework in the *Mineral Resources Regulation 2013* are consistent with the policy objectives of the authorising law. Section 321 and s. 417(2)(l) of the *Mineral Resources Act 1989* contemplate that the amount or rates or method of calculation of royalty be prescribed by regulation.

Inconsistency with policy objectives of other legislation

There is no inconsistency with the policy objectives of other legislation.

Benefits and costs of implementation

The amendments will provide certainty for industry and the State as to the scope and application of petroleum royalty decisions. An effective petroleum royalty decision framework will ensure the wellhead value of petroleum disposed of or produced by a petroleum producer is correctly worked out and consequently, the correct petroleum royalty paid.

Alignment, to the extent possible, of the petroleum royalty decision framework and the gross value royalty decision framework achieves royalty administration efficiencies and ensures consistency and certainty for royalty payers, especially those with joint petroleum and mineral royalty liabilities.

The new petroleum royalty decision framework replaces an existing administrative framework. However, as it provides a clearer basis for making petroleum royalty decisions, there may be an increase in circumstances where decisions are made, with some resulting implementation costs. These should not be significant and would be offset by revenue benefits to the State from enhanced compliance with royalty obligations.

Consistency with fundamental legislative principles

The use of subordinate legislation is appropriate as the existing administrative frameworks for petroleum royalty decisions and gross value royalty decisions are contained in the *Petroleum and Gas (Production and Safety) Regulation 2004* and the *Mineral Resources Regulation 2013*. The amendments are administrative in nature and do not relate to substantive matters that affect the overall royalty payable.

Although it is arguable the Regulation departs from fundamental legislative principles as outlined in section 4 of the *Legislative Standards Act 1992*, any departure only occurs in the context of balancing fundamental legislative principles with the competing policy objective of maintaining the integrity of the royalty administration framework and ensuring State royalty liabilities are properly accounted for.

New section 148E *Petroleum and Gas (Production and Safety) Regulation 2004*

Under new section 148E, in making a petroleum royalty decision, the Minister may decide the value of, or a method or formula for, a component of the wellhead value of petroleum even if that component is not stated in a petroleum producer's application for a petroleum royalty decision. This provision may be regarded as breaching a fundamental legislative principle in that making a decision for a component not listed in the producer's application is inconsistent with the requirements of natural justice as it does not give the producer an opportunity to make submissions regarding that component.

The provision merely seeks to clarify the scope of the Minister's power to make an appropriate petroleum royalty decision and reflects the ultimate policy sought to be achieved of strengthening the integrity of the royalty administration framework to ensure royalty liabilities are correctly accounted for. The making of a petroleum royalty decision often involves complex commercial arrangements and often involves numerous components in determining the appropriate wellhead value. Clarifying that the Minister may consider all components in making a decision and not restricting the Minister's consideration to those components listed in a producer's application ensures the Minister can make an accurate determination of the components of the wellhead value, therefore ensuring the correct petroleum royalty is paid.

Any producer dissatisfied with a decision made has appropriate internal review rights to challenge the decision. Further, given the commercial complexity involved in such decisions, consultation with the producer is undertaken before any decision is made. The Minister currently consults with producers before making any decision, and will continue to do so once the regulation is made. This provides the producer with the opportunity to make any submissions in relation to any components being considered that are not specified in the producer's application for a decision. For these reasons, the provision is considered justified in the circumstances.

Consultation

The petroleum industry was consulted on the amendments to the petroleum royalty decision framework. While the petroleum industry was generally accepting of the new petroleum royalty decision framework, industry raised some concerns during consultation. In response, additional consultation on certain key issues was undertaken and refinements were made to the framework where considered appropriate.

The Office of Best Practice Regulation (OBPR), Queensland Productivity Commission was consulted regarding the Regulatory Impact Statement (RIS) system. OBPR advised that the amendments to the *Petroleum and Gas (Production and Safety) Regulation 2004* and consequential amendments to the *Mineral Resources Regulation 2013* are either excluded from the RIS system as they relate to the imposition of a royalty or are unlikely to have significant adverse impacts. As such, a RIS is not required.