Government of **Western Australia**
Department of **Treasury**

Western Australia's Submission to the Commonwealth Grants Commission's 2025 Methodology Review

Draft Report – Mining Revenue

September 2024

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Acknowledgement of Country

This report was prepared by the Department of Treasury (WA Treasury) on the traditional Country of the Wadjuk people of the Noongar Nation.

WA Treasury respectfully acknowledges the Traditional Custodians of Country throughout Western Australia and their continuing connection to Country, Culture and Community.

We pay our respects to all members of Western Australia’s Aboriginal communities and their cultures and to Elders past and present.

We acknowledge and pay tribute to the strength and stewardship of Aboriginal people in sustaining the world's oldest living culture and value the contribution Aboriginal people make to Western Australia's communities and economy.

We recognise our responsibility as an organisation to work with Aboriginal people, families, communities, and organisations to make a difference and to deliver improved economic, social and cultural outcomes for Aboriginal people.

Further information relating to this report may be obtained by emailing igr@treasury.wa.gov.au

Mining Revenue

KEY POINTS – MINING REVENUE

Coal

The coal mined across States varies significantly in quality. This quality translates to a variation in the royalty rate that can be imposed, and leads to different royalty-raising capacities across those States.

All low-quality coal, as mined in Victoria, Western Australia and Tasmania, should be assessed together to reflect a lower revenue-raising capacity from the higher-quality coal in New South Wales and Queensland. This would also mitigate the dominant State problem created by assessing Victoria's brown coal in its own assessment.

Materiality

Whilst there is a conceptual case for a differential assessment of low-quality coal, materiality should be applied consistently within the Mining Revenue assessment. Under the CGC's current methods, if a differential assessment of a mineral does not meet the $40 per capita threshold, then it should be included in the Other Minerals component.

Onshore oil and gas

We support the conceptual case for assessing onshore oil and gas using volume of production rather than value of production. Whether it is assessed separately, or part of Other Minerals, it should be subject to materiality.

This submission responds to the *Mining Revenue* chapter and *addendum*, as part of the Commonwealth Grants Commission's (CGC's) 2025 Review of the methods it uses to recommend GST grant distributions among the States and Territories (referred to as States hereafter).

Coal

The CGC proposes to change the capacity measure for brown coal.[1] This is essentially due to Victoria's brown coal being 'inferior' to black thermal coal.[2] Therefore, a separate, differential revenue-raising capacity for brown and black coal is proposed. However, the distinction between brown and black coal is largely a question of quality (energy content and moisture) rather than brown and black coal being entirely separate products. Similarly, there are significant variances in the quality of black coal between States that the assessment should recognise.

1 Commonwealth Grants Commission, *2025 Methodology Review Draft Report*, page 75, paragraph 116.

2 State of Victoria (Department of Treasury and Finance), *Victorian response to CGC 2025 Review consultation,* page 23. Victoria's low-quality coal hinders its local market and export potential. Hence, it is not traded on markets and has no market price.

The CGC's proposal to split coal by price band (as a proxy for quality) has highlighted that different quality coal commands different prices and affords different royalty rates. Premium, highly sought coal commands high prices and royalty rates (through capturing mining company rents). However, low-quality coal, such as that mined in Victoria, Western Australia, and Tasmania, can only attract relatively low royalty rates.

The CGC further proposes to separately assess Victoria's brown coal because it considers there is no reliable way to estimate Victoria's value of production, and it is the only State that produces brown coal.[3] But the CGC also notes that States that produce low-value coal would be unable to apply the average royalty rate to that coal.[4]

The CGC outlines, in both the 2020 Review and 2015 Review, that there is significant variation in royalty rates across States. However, it notes a common pattern:[5]

- Low-value minerals (such as salt, sand and gravel) are subject to volume-based royalties;
- Hard-rock minerals (such as nickel, copper and gold) attract relatively low royalty rates. Iron ore is an exception, being a higher quality hard rock mineral that attracts a relatively high royalty rate (because it requires far less processing than other hard-rock minerals);
- Soft rock or shallowly-mined minerals (such as bauxite and coal) attract a relatively high royalty rate; and
- Onshore oil and gas attract high royalty rates.

The mineral-by-mineral approach splits minerals to recognise in part the different royalty rates different minerals can attract. These variations generally reflect differences in processing requirements, which is similar within mineral types. Differences in quality also affect royalty rates. Table 1 highlights the vast range of coal royalty rates that are applied across States within the coal mineral category.

Victoria, Western Australia and Tasmania all apply rates much lower than the standard rate. This is not purely a policy difference. It is directly related to quality.

Table 1

Coal Royalty Rates

	NSW	Vic	Qld	WA	Tas	Standard Rate
2024 Update	~8%	5.2%	7-21%	<5%	~1%	7-15%

Source: Western Australian Treasury calculation based on CGC 2024 Update data. The Victorian rate is estimated by the CGC.

The rate gap widened in 2022-23 due to the implementation of a progressive royalty rate system in Queensland. This gap will increase further from the 2024-25 data year due to a flat-rate increase to New South Wales' royalty rates on coal. These increases further overstate the revenue-raising capacity in the States with lower rates.

3 Commonwealth Grants Commission, *2025 Methodology Review Draft Report Addendum – Mining Revenue*, page 5, paragraph 25.

4 Commonwealth Grants Commission, *2025 Methodology Review Draft Report*, page 68, paragraph 73.

5 Commonwealth Grants Commission, *Report on GST Revenue Sharing Relativities 2020 Review*, Volume 2 – Methodology for measuring State fiscal capacities (Part B), page 79, paragraph 16.

The royalty rate updates by Queensland and New South Wales reflect extraordinarily high profits received by coal producers in these States, due to global demand for higher-quality coal. Whilst the CGC has acknowledged coal quality is higher in Queensland, the quality of Western Australia's coal is significantly lower and has a much lower energy content than in both Queensland and New South Wales.[6] That is, it is an 'inferior' form of black coal. Hence, it is much less profitable and attracts a much lower royalty rate.

Like Victoria, Western Australia does not export coal. The majority of Western Australia's coal is used for power generation within State (in the same vicinity as the mine), and all of it remains in Western Australia. If the product were of higher quality and exported, Western Australia may be able to charge a higher royalty rate. Like Victoria's brown coal, it is not exposed to global market price fluctuations and associated economic rents, as is higher-quality black coal.

Therefore, the distinction should not be between brown and black coal. Victoria's brown coal, due to its low quality, cannot command a high royalty rate. This is also true for the coal mined in Western Australia and Tasmania, despite it being black coal. Furthermore, the royalty rates applied in Western Australia and Tasmania are lower than the rate currently estimated by the CGC for Victoria.

The mineral-by-mineral approach is intended to separate minerals into groups with similar revenue raising capacity. Therefore, grouping Western Australia's and Tasmania's coal with Victoria's brown coal in a separate 'Low-quality Coal' component would better achieve this goal.

The potential variation in the results of a separate low-quality coal assessment from uncertainties in estimating Victoria's value of production would not be large, compared to the impact of removing low-quality coal from the high-quality coal assessment. Hence, a low-quality coal assessment would improve the measurement of horizontal fiscal equalisation.

To justify an actual per capita (APC) assessment, the CGC stated that Victoria's value of production cannot be reliably derived.[7] It has been estimated in the past using Victoria's royalty revenue and estimated effective royalty rate based on the energy content of black coal. But the revenue raising capacity of brown coal is likely closer to that of low-quality coal in Western Australia and Tasmania, rather than the higher-quality coal in New South Wales and Queensland.

Our proposal would require the CGC to continue to estimate a value of production for Victorian coal. An APC assessment would not require this, but would apply a very different method to one mineral compared to all other minerals. This creates complexity, and a potentially worrying precedent.

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6 Adrian C Hutton, *'Geological Setting of Australasian Coal Deposits'* in R Kininmonth and E Baafi (eds), Australasian Coal Mining Practice (The Australian Institute of Mining and Metallurgy, 2009), Pages 70-72 [http://ro.uow.edu.au/cgi/viewcontent.cgi?article=1772&context=scipapers]

7 Commonwealth Grants Commission, *2025 Methodology Review Draft Report*, page 75, paragraph 115.

In addition, our proposal opens the opportunity for an alternative estimation (or simply a reasonableness check). This would use Western Australian and Tasmanian value of production per tonne to derive Victoria's value of production from its tonnes produced. Given the similarities in quality, this should assuage Victoria's concerns that the CGC overestimates its value of production.

A well-documented issue with a mineral-by-mineral approach is the deviation from policy neutrality if there is a dominant State within one mineral category. An APC assessment for Victoria's coal alone would render Victoria a dominant State in that component. By including Western Australia and Tasmanian coal in the assessment, it reduces the dominant State problem significantly, and hence improves policy neutrality.

Materiality

We consider there is a conceptual case to assess low-quality coal separately, as described above. We further consider that this does not require a materiality consideration because without this separation, assessing low-quality coal with higher-quality black coal will overstate the coal capacity of States with above-average production of low-quality coal. It is a more accurate reflection of States' revenue raising capacities.[8]

The CGC has acknowledged this in the context of brown coal.[9] It also implicitly agrees through its proposal to separate brown coal on the basis that it cannot reliably estimate values of production.

The conceptual basis is similar to those of all other minerals in the Mining Revenue assessment, some of which are not material. Materiality should only be considered as to whether such a mineral is assessed alone, or is included in the Other Minerals component.

Under the CGC's current methods (which are not proposed to change), if a differential assessment of a mineral does not meet the $40 per capita threshold, then it should be included in the Other Minerals component. We expect a differential assessment of each of brown coal or low-quality coal (as we propose, which includes brown coal) to redistribute well under $40 per capita compared to equal per capita, so it should be included in the Other Minerals component. This is consistent with the treatment incurred by any other mineral in the assessment.

We believe the CGC should apply this pragmatism to materiality more broadly.

[8] However, we consider the split of black coal by price bands should require a materiality test, as it is driven by policy differences, and price differences will tend to be transient and volatile. If the new methods are not material under recent high and volatile prices, then they should not be implemented.

[9] Commonwealth Grants Commission, *2025 Methodology Review Draft Report*, page 68, paragraph 73.

During the 2022 Update process, we noted that there was a tendency for the CGC to not adjust its assessments to address errors, purely based on materiality (and sometimes even when the error has a material impact).[10] For example, the CGC did not remove ACT mining revenue that was erroneously included in the Mining Revenue assessment, based on materiality.[11]

In addition, in the 2020 Review Draft Report, for the count of unoccupied dwellings in the Housing assessment, the CGC said it would not scale the Census data with Australian Institute of Health and Welfare (AIHW) data, which is more accurate, due to a lack of materiality from the change.[12]

Materiality should not be a factor when improving reliability of data or correcting errors.

Onshore oil and gas

We support the conceptual case to assess onshore oil and gas using volume of production rather than value of production. As with coal, materiality should not be a consideration to allow the change in measure. This approach would be pragmatic, more accurate, and based on a conceptual case. However, once that change is effected, its ability to remain a separate mineral must be tested.

We understand the CGC essentially proposes to assess two separate revenue bases – barrels for oil and cubic feet for gas. If a differential assessment of either distributes less than $40 per capita compared to equal per capita, it should be included in the Other Minerals component. This is consistent with the treatment of any other mineral in the assessment.

In addition, we note that royalties for other minerals (i.e., salt, sand and gravel) are also levied on volume measures rather than value of production. We acknowledge that the production of such minerals is much smaller than that of onshore petroleum and gas, but note, following our discussion above, and earlier on low-quality coal, that the conceptual case does not require a materiality test.

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[10] Western Australian Treasury, *Submission to Commonwealth Grants Commission, 2022 Update New Issues,* page 16.

[11] *Ibid.,* pages 15-16.

[12] Commonwealth Grants Commission, *Report on GST Revenue Sharing Relativities, 2020 Review, Draft Main Report,* Attachment 14 – Housing, page 14, paragraph 62.