Government of South Australia

Department of Treasury and Finance

2025 METHODOLOGY REVIEW

DRAFT REPORT – MINING REVENUE ADDENDUM

Submission from the South Australian Department of Treasury and Finance

September 2024

1. The South Australian Department of Treasury and Finance (DTF) welcomes the opportunity to make this submission regarding the addendum to the Mining Revenue chapter of the Commonwealth Grants Commission's 2025 Methodology Review Draft Report.

2. The addendum provides further information on the Commission's proposals in the Draft Report to:

   - assess black coal in two price bands – above and below $200 per tonne;
   - assess brown coal separately and on the basis of actual revenue received; and
   - assess onshore oil and gas based on volume produced rather than the value of production.

3. South Australia does not support the Commission proposal to assess onshore oil and gas based on volume produced rather than the value of production, on the basis that it is inconsistent with what states do and raises policy neutrality concerns.

4. South Australia's positions on all the Commission's proposals are discussed further below.

Assessment of coal

Black coal assessment

5. South Australia notes the Commission's proposal to split the coal assessment into two price bands; namely above and below $200 per tonne. This is a departure from the Commission's initial proposal for a three-band assessment (i.e. below $200; above $200 up to $300; and above $300).

6. South Australia has previously raised policy neutrality concerns about the three-band approach, as the proposed top and bottom bands were based on the lowest and highest bands in Queensland's coal royalty system. We consider that the proposal to instead use two price bands derived from average prices across all jurisdictions would mitigate concerns about policy neutrality.

7. We also note the Commission's view that two bands would be less data intensive and less likely to be susceptible to data confidentiality issues.

8. The Commission has used data from 2020-21 to 2022-23 to test whether policy neutrality issues would have arisen in the 2024 Update under alternative price band methods. The Commission observed that the three-band approach produced a dominant state in one of the three assessment years, while the two-band approach did not produce a dominant state in any assessment year.[1]

9. Based on these findings, South Australia considers that if the Commission decides to split the coal assessment, the proposed two-band approach based on a $200 price threshold appears to be more appropriate than the three-band approach.

[1] For the purposes of its analysis, the Commission defined a state to be dominant if the difference between its share of the revenue base and its population share is more than 50 percentage points. While the concept of a dominant state has been used in a specific context in this instance, we note the Commission has previously proposed the introduction of a dominant state adjustment more broadly in the mining revenue category. South Australia does not support this proposal. Our position is detailed in our Tranche 1 submission.

10. We agree with the Commission’s view that the price threshold used to determine the two bands should be fixed across the assessment period rather than recalculated for each assessment year. This would minimise the data provision burden on the states and territories (states) and support the stability of the assessment. The price threshold could be recalculated as part of a methodology review to reflect any changes in commodity price trends over time.

Brown coal assessment

11. South Australia notes the Commission’s proposal to separately assess brown coal on the basis that the current combined assessment may be overstating Victoria’s assessed revenue raising capacity. The Commission proposes an actual per capita (APC) assessment, reflecting that it is not able to derive a reliable value of production for Victoria’s brown coal, as it is largely an internal transfer within mining/generation entities and therefore has no identifiable market price.

12. In this regard, South Australia notes that:

    - as Victoria is the only jurisdiction that raises brown coal royalties, an APC assessment would directly reflect Victoria’s policy settings, which is inconsistent with the policy neutrality supporting principle; and
    - moving brown coal out of the combined coal assessment is unlikely to be material. The Commission’s analysis of 2024 Update data showed that the largest impact of a separate APC assessment for brown coal would be an increase of around $11 per capita in Victoria’s GST share, well below the $40 per capita materiality threshold for the 2025 Review.

13. On balance, it appears more appropriate for the Commission to continue assessing brown coal in a combined coal assessment.

Assessment of onshore oil and gas

14. South Australia does not support the Commission’s proposal to assess onshore oil and gas capacity using the volume of production.

15. The Commission’s proposal is in response to Queensland’s view that the current assessment approach, which is based on value of production, does not reflect how Queensland levies petroleum royalties and therefore does not reflect what states do. This is despite every other producing state basing its royalties on the value of production, as shown below.

PETROLEUM ROYALTY RATES

	WA	NSW	VIC	QLD	SA	TAS	ACT	NT
Royalty Rate	10.0% or 12.5% at the well-head[(a)(b)]	10.0% at the well-head	10.0% at the well-head	Sliding rate scale based on average sales price and volume of gas produced	10.0% at the well-head	12.0% at the well-head	N/A	10.0% at the well-head
Royalty System	Ad valorem	Ad valorem	Ad valorem	Ad valorem	Ad valorem	Ad valorem		Ad valorem

(a) Except under the *Barrow Island Royalty Variation Agreement Act 1985*, which applies a royalty rate of 40% to resource rents (calculated on a similar basis to the Commonwealth's Petroleum Resource Rent Tax).

(b) A minimum rate of 5% applies to tight gas.

Source: Government of Western Australia, *Overview of state taxes and royalties, 2023-24.*

Inconsistency with the supporting principles

16. In October 2020, the Queensland Government introduced a new petroleum royalty framework, which marked a departure from the previous wellhead value-based regime that was consistent with other jurisdictions.

17. Under the new arrangements, royalties are calculated based on the volume of taxable oil or gas produced. The applicable royalty rate varies based on the average sale price of the resource being taxed – that is, higher rates apply when average prices are high. This means that, in addition to volume, the value of production of a resource has a direct impact on Queensland's revenue raising capacity in respect of that resource.

18. In considering the most appropriate approach for this assessment, South Australia notes that a volume-based assessment would be inconsistent with the 'what states do' and policy neutrality supporting principles.

19. The 'what states do' principle aims to ensure that the Commission's assessments reflect what states collectively do. The table above shows that states collectively base their petroleum royalties on the value of production, not volume. Queensland's petroleum royalty system is not solely based on volume, as the applicable royalty rate depends on the average sale price (a measure of the value of production) in the relevant royalty period. We consider that an assessment based on value of production better reflects what states collectively do than a volume-based assessment.

20. The policy neutrality principle aims to ensure that a state's policy choices do not directly influence its GST share. The Commission estimates that if the proposed change to a volume-based assessment had been applied in the 2024 Update, Queensland's GST share in 2024-25 would be around $29 million higher. In other words, Queensland could have received a higher GST share as a direct result of its policy decision to impose petroleum royalties differently from every other oil and gas producing state, which is inconsistent with the policy neutrality principle.

21. On this basis, we recommend that the Commission continues to assess onshore oil and gas on a value of production basis.

Data reliability

22. A further issue referenced by the Commission in considering this issue is Queensland's suggestion that the value of production data used in this assessment is unreliable, due to a lack of rigour and transparency in the collection and reporting of this data.

23. The scale and prevalence of the issues mentioned by Queensland have not been established. It is therefore not possible to determine if, and to what extent, HFE is being impacted.

24. South Australia considers that, given the revenue implications and the need to ensure compliance across industry, it is highly likely that states are sufficiently incentivised to undertake the necessary audit and assurance activities relating to self-assessed royalty returns, and to ensure the timely identification of any material variances in royalties payable.

25. As previously noted, Queensland's royalty regime also has a value component with royalty rates determined based on average sales value. This implies that Queensland would have an incentive to consider value of production data as part of its collection processes. As no state other than Queensland applies its oil and gas royalties on a volume basis, it is more likely that there would be issues with the quality of volume data, which would have implications for the reliability of a volume-based assessment.

26. Notwithstanding this, any specific concerns about data quality can be addressed directly by the Commission in consultation with the states, or through the Commission's established approaches to recognising data quality issues in its assessments.

27. A further consideration is that a volume-based assessment would not capture differences in the quality of resources across jurisdictions. For example, barrels of oil are not uniform in their quality, due to differences in elements such as sulphur content and other contaminants. A volume-based assessment would implicitly assume that all states produce the same quality of resources and have the same revenue raising capacity per unit produced. This is inconsistent with HFE.