Petroleum Royalties and Excise

Report

190

Joint Committee of Public Accounts

Parliament of the Commonwealth of Australia 1981

THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

JOINT COMMITTEE OF PUBLIC ACCOUNTS

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INQUIRY INTO PETROLEUM ROYALTIES AND EXCISE

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Section 8.(1) of the Public Accounts Committee Act 1951 reads as follows:

8.(1) Subject to sub-section (2), the duties of the Committee are:

(a) to examine the accounts of the receipts and expenditure of the Commonwealth including the financial statements transmitted to the Auditor-General under sub-section (4) of section 50 of the Audit Act 1901;

(aa) to examine the financial affairs of authorities of the Commonwealth to which this Act applies and of intergovernmental bodies to which this Act applies;

(ab) to examine all reports of the Auditor-General (including reports of the results of efficiency audits) copies of which have been laid before the Houses of the Parliament;

(b) to report to both Houses of the Parliament, with such comment as it thinks fit, any items or matters in those accounts, statements and reports, or any circumstances connected with them, to which the Committee is of the opinion that the attention of the Parliament should be directed;

(c) to report to both Houses of the Parliament any alteration which the Committee thinks desirable in the form of the public accounts or in the method of keeping them, or in the mode of receipt, control, issue or payment of public moneys; and

(d) to inquire into any question in connexion with the public accounts which is referred to it by either House of the Parliament, and to report to that House upon that question,

and include such other duties as are assigned to the Committee by Joint Standing Orders approved by both Houses of the Parliament.

PREFACE

1. The Committee's inquiry into this matter commenced as part of its general inquiry into the Report of the Auditor-General for 1977-78 which was the subject of the Committee's 176th Report to Parliament. In that Report, the Committee stated that it had decided to examine separately the matters concerning offshore petroleum royalties and excise on which the Auditor-General had made further comments in his 1978-79 Report. Those comments and other references in the Auditor-General's Reports for 1979-80 and 1980-81 appear in Chapter 4 of this Report.

2. The Committee invited the producers, ESSO Australia Limited and Hematite Petroleum Proprietary Limited, to make a presentation concerning offshore petroleum operations in Bass Strait. The Committee also visited the Bass Strait facilities including the Halibut Offshore Platform and the Long Island Point distribution installation. The Committee records its appreciation of the assistance given by the producers.

For and on behalf of the Committee.

David M. Connolly, MP
Chairman

M. J. Talberg,
Secretary,
Joint Committee of Public Accounts,
Parliament House,
CANBERRA.

25 August, 1981

INQUIRY INTO PETROLEUM ROYALTIES AND EXCISE

TABLE OF CONTENTS

CHAPTER		PAGE
	Preface	(v)
1	Summary of Conclusions and Recommendations	1
2	Royalties and Excise Duties	
	Development of Petroleum Resources in the Bass Strait	5
	Legislative Provisions Governing Royalties	7
	The Effect of the Seas and Submerged Lands Act 1973	8
	Legislative Provisions Governing Excise Duties and Pricing	9
3	1980 Legislation	12
	Background	14
	Petroleum (Submerged Lands) (Royalty) Amendment Act	16
	Value at the Wellhead	
4	Matters Raised by the Auditor-General	18
5	The Inquiry into Royalties	
	Legislative support for procedures in royalty collection	24
	Delay in determining the wellhead value	26
	Accounting for Commonwealth Revenue by the Designated Authority	28
	Reasons for the increased royalty payments in 1977-78	30
	Other Royalty matters raised by the Auditor-General	31
6	The Inquiry into Excise Duties	32
	Monitoring of Production- Back Allocation/Mass Balance Program	33
	The documentation of the procedures	35
	Attempts at alternative solutions	
APPENDIX		
A	'Crude Oil Pricing and Levy Arrangement' - Appendix to Statement No. 4, 1979-80 Budget Speech.	39
B	'Crude Oil & Liquified Petroleum Gas - Pricing and Levy Arrangements' - Appendix 1 to Statement No. 4, 1981-82 Budget Paper No. 1.	47

C Total Crude Oil Production 1979/80 51

D Dates of Hearings and Inspections - List of Witnesses and Observers 53

CHAPTER 1

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

Royalties

1.1 While the legislation passed by the Commonwealth Parliament in 1980 purports to vest in the States and the Northern Territory certain powers over and title to the territorial sea around Australia, the Committee doubts that these Bills were suitably framed to achieve their stated purpose. The Committee considers that ultimate authority and responsibility over the territorial sea still remains with the Commonwealth.

1.2 Having regard to the extent of the responsibility retained by the Commonwealth under the Coastal Waters (State Powers) Act 1980 and the Coastal Waters (State Title) Act 1980 combined with the overall Constitutional situation, the Committee considers that it would have been more appropriate for the legislation to provide for the Joint Authority established under the Petroleum (Submerged Lands) Amendment Act 1980 to function in relation to the territorial sea within the 3 mile limit as well as the adjacent areas outside the 3 mile limit. To maintain the spirit of the agreement between the Commonwealth and the States and for administrative convenience the Joint Authority could be empowered to delegate appropriate functions to the Designated Authority. The Committee recommends that:

- the terms of the 1980 legislation be discussed with the States with a view to having the legislation amended prior to being proclaimed, to empower the Joint Authority established under the Petroleum (Submerged Lands) Amendment Act 1980 to function in relation to the territorial sea as well as the adjacent areas.*

1.3 During its inquiry the Committee found that those with the day to day responsibility for the collection of the Commonwealth's share of royalties were State Government officials and therefore under no obligation to furnish full explanations to the Commonwealth. While the Committee believes that the State Government officials have cooperated fully with Commonwealth officials in exercising their responsibilities, the Committee finds this situation most unsatisfactory and is strongly of the view that new methods must be implemented to make relevant officials accountable to both the Commonwealth and State Parliaments. The Committee believes a means of achieving this accountability is for the relevant Commonwealth and State Parliamentary Committees to conduct future inquiries into offshore matters jointly. *

1.4 The Committee is concerned that the Designated Authority is not responsible to the appropriate Commonwealth authorities for the procedures adopted for royalty collection and recommends that:

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* See Chapter 3

- discussions take place between the respective Commonwealth and State Authorities and between Auditors-General to ensure that royalty collection procedures compatible with the requirements of both Governments are implemented under the existing legislation and under the 1980 Commonwealth legislation when proclaimed. *

1.5 While neither Esso/BHP nor the Victorian Designated Authority are able to be held to account by the Commonwealth Parliament, the Committee is gravely concerned that it took some seven years before the negotiations between these parties reached the stage where the Designated Authority decided that it was necessary to determine, in the absence of agreement with the producers, the well-head value of the petroleum produced and another five years to finally make a determination. The Committee regards the delay of twelve years in settlement of this issue as completely unsatisfactory.

1.6 The Committee is aware that the Designated Authority may have delayed its determination pending the clarification of legal issues but by so doing the Designated Authority left unresolved the value of payments to be made by the producers. The Committee is convinced that this episode reflects unfavourably on the administration of offshore petroleum development in Australia and on the attitude of the Commonwealth Departments concerned which should have acted more promptly to establish the role of the Designated Authority and protect the interests of the Commonwealth. *

1.7 The Committee is concerned that while the Department of National Development and Energy is able to establish that the Commonwealth receives the correct proportion of the total royalties collected by the Victorian Government, under current procedures it is unable to verify the calculation by the Victorian authorities of the total figure. In addition the Committee is concerned that the maximising of the royalty collections may conflict with collections of the excise levy. For example, crude oil may be allocated to a field which attracts a high over-riding royalty, but a low rate of excise levy under the four tier rate system.

1.8 The Committee is concerned that the Commonwealth cannot explicitly satisfy itself on this matter and recommends that:

- the Department of National Development and Energy and the Auditor-General's Office should be involved, in co-operation with the Victorian Auditor-General, in ensuring the correctness of the procedures to arrive at the royalty payments. *

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* See Chapter 5

1.9 The Committee was informed that, while the legislation requires the State to pay the Commonwealth its share of royalties within one month, it would seem the Commonwealth's share could well be paid immediately it is received by the State. It was suggested to the Committee that if there were to be any adjustment to the Commonwealth share or to the amount paid by the licensee, this could be made in the following month's payment to the Commonwealth. The Committee recommends that:

- arrangements be made for the Commonwealth share of royalties to be paid immediately it is received by the State, with any adjustments being made in the following month's payment. *

1.10 The Committee understands that following the Direction issued by the Designated Authority on 9 June 1980, a reassessment has been made of the value of petroleum at the well-head for all royalty periods from the commencement of production. The Committee recommends that:

- officers of the Department of National Development and Energy, and the Auditor-General's Office actively participate in the final verification of royalty calculations which should be completed as soon as possible.**

Excise ***

1.11 The Committee considers that the Government's crude oil excise levy policy was introduced without the Government being given sufficient advice of the practical difficulties involved and, in the light of experience elsewhere, with unnecessary complication. Furthermore, departments gave advice to Ministers in a budgetary context in the mistaken belief that the information required to enable ministerial decisions to be carried out was available. The Committee is of the view that there was inadequate liaison between the policy Departments developing the oil excise program and the Department which was to administer the program.

1.12 The Committee considers that the former Department of National Development must take a large share of the responsibility for the delay in developing a back allocation and mass balance program which is required to accurately calculate the amount of oil excise due to be paid and that the Department took an inordinately long time - about twelve months - to realise that documented procedures developed by the Victorian Department of Minerals and Energy were not available to it. The Committee recommends that:

- the Departments of National Development and Energy and Business and Consumer Affairs treat finalisation of the documentation of procedures as a matter of urgency and will expect to see substantial progress in this area in the near future.

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* See Chapter 5
** See Chapter 3
*** See Chapter 6

1.13 The Committee expects that, after the relevant Government departments have satisfied themselves that the documented procedures are adequate, the Auditor-General will be able to indicate his satisfaction that the excise levy program is being administered in a correct and accountable manner. The Committee intends to examine progress made in this area when it further considers the reports of the Auditor-General.

General *

1.14 Finally, the Committee has noted that only in United Kingdom and Canadian legislation has a 'well-head value' concept been used. The Canadian experience is of little practical relevance, however, as there has been as yet no commercial production of petroleum from Canadian offshore areas. In the United Kingdom royalties based on well-head value were applied to earlier offshore petroleum licensees but continuing difficulties of interpretation led to a revision of the procedures in 1976 and royalties are now calculated on an entirely different basis, without reference to well-head value, in respect of licences issued after that date. The Committee recommends that:

- the Department examine those procedures further with a view to adopting a much simpler and administratively satisfactory solution which will satisfy the requirements for maximisation and accountability of revenue.

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* See Chapter 6

CHAPTER 2

ROYALTIES AND EXCISE DUTIES

2.1 There are four main aspects to this inquiry:

- the exploration for and exploitation of petroleum products in the Bass Strait region;
- the legislative provisions governing royalties;
- the effect of the Seas and Submerged Lands legislation; and
- the legislative provisions governing excise duties.

Development of Petroleum Resources in the Bass Strait

2.2 Although offshore permits were first awarded in the early 1950s, it was not until 1960 that Hematite Exploration Pty Ltd, a subsidiary of the Broken Hill Proprietary Company Limited, took up permits in the Bass Strait area. Towards the end of 1960 Hematite conducted aeromagnetic and seismic surveys which revealed potential oil-bearing structures. In 1964, BHP announced that Esso Exploration Australia Inc. would join its operations. *

2.3 As a result of an intensive exploration programme the following fields were discovered: **

1965	-	Barracouta
1966-1968	-	Marlin, Kingfish, Halibut, Tuna, Snapper and Flounder
1969	-	Bream and Mackerel
1972	-	Cobia
1978	-	Fortescue

2.4 After allowing for production lead times and for rational development of the fields, the following fields were brought into production: **

1969	-	Barracouta
1970-1971	-	Marlin, Halibut and Kingfish
1977	-	Mackerel
1979	-	Tuna

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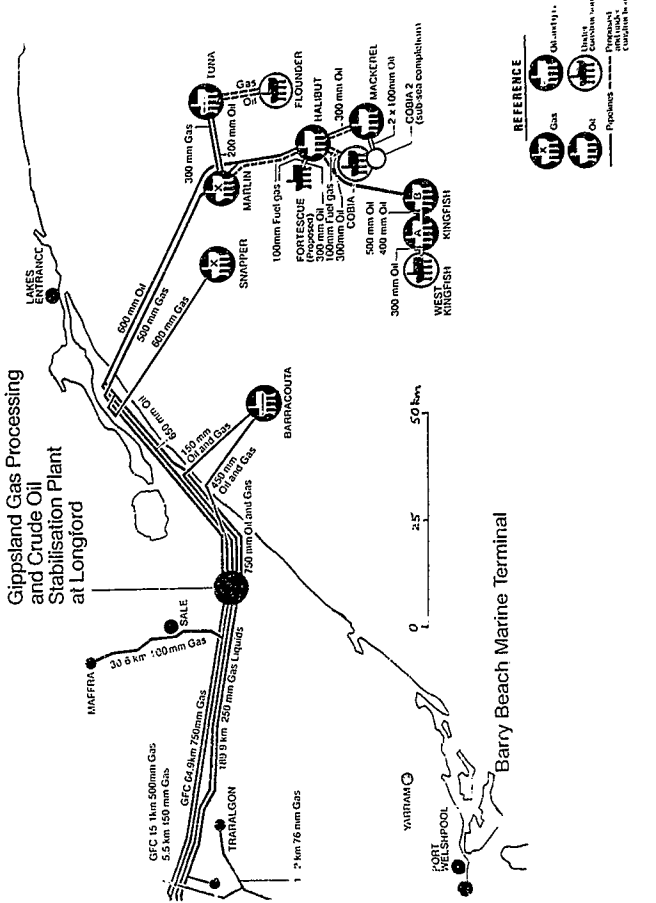
* Report of Senate Select Committee on Off-Shore Petroleum Resources 1971, Parliamentary Paper No. 201/1971

** Producers 24/5/79 briefing



Legislative Provisions Governing Royalties

2.5 In 1967, the then Government introduced the Commonwealth Petroleum (Submerged Lands) Act, 1967. Concurrently, each State introduced its own mirror legislation. While this was a novel departure from previous Commonwealth-State arrangements, it was intended to overcome any possible constitutional difficulty relating to sovereignty in offshore areas.

2.6 The preamble to the Commonwealth and the State legislation and to the agreement between the Commonwealth and the States records the reasons for this mirror legislation. It was stated that the exploration for and the exploitation of the petroleum resources of submerged lands adjacent to the Australian coast would be encouraged by the adoption of legislative measures applying uniformly to the continental shelf and to the sea-bed and subsoil beneath territorial waters. Accordingly the Commonwealth and the State Governments decided, in the national interest, that, without raising questions concerning, and without derogating from, their respective constitutional powers, they should co-operate for the purpose of ensuring the legal effectiveness of authorities to explore for or to exploit the petroleum resources of the submerged lands. As a result, the Governments agreed to submit to their respective Parliaments legislation relating both to the continental shelf and to the sea-bed and subsoil beneath territorial waters and also agreed to co-operate in the administration of the legislation.

2.7 A key appointment under the legislation is that of Designated Authority who is the relevant State Mines Minister. * The Designated Authority has wide powers for the day to day administration and supervision of the legislation including the collection of royalties. Reliance on a State Official to carry out functions under Commonwealth legislation raised doubt as to the extent to which that official may be held responsible to the Commonwealth for his actions.

2.8 The Petroleum (Submerged Lands) legislation, inter alia, provides for the payment to the Commonwealth and the States of offshore petroleum royalties of 10% on a notional well-head value. This value is calculated by subtracting from the sale price deductions to cover such matters as depreciation of capital items, cost of capital, and operating expenses. The legislation provides that the location of the well-head is at a valve station agreed between the Designated Authority, who in Victoria is the Minister for Minerals and

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* Department of National Development Submission 7/3/79

Energy, and the producers. Failing agreement it is the valve station that the Designated Authority determines. While under the 1967 Commonwealth-State Offshore Petroleum Agreement, the Designated Authority is required to consult the Commonwealth before making a determination, only he can determine. *

2.9 Currently, as the only offshore petroleum producing area is Bass Strait, Victoria is the only State which has been directly concerned with royalty payments. During the period 1969 to June 1980 royalties were paid under interim arrangements tentatively agreed between Victoria and the producers. In accordance with the Petroleum (Submerged Lands) Legislation, 60% of the basic levy paid is retained by the State and 40% is forwarded to the Commonwealth.

2.10 It was not until August 1976, that the Designated Authority formally initiated consultation with the then Minister for National Resources, pursuant to the 1967 Offshore Petroleum Agreement and prior to making a determination of well-head value. The Commonwealth's views were forwarded to the Designated Authority in August 1977. ** However, he did not make a determination until 9 June 1980.

The Effect of the Seas and Submerged Lands Act 1973

2.11 In 1973, the Commonwealth Government introduced the Seas and Submerged Lands Act which relates to the sovereignty in, above and below the territorial seas of the continental shelf and also to the recovery of minerals, other than petroleum, from these areas. The Act declares that the sovereignty of the areas is vested in and exercisable by the Crown in right of the Commonwealth.

2.12 Such was the significance of this legislation that its validity was challenged in the High Court. The Court upheld the legislation and decided, in December 1975, that ultimate constitutional responsibility in matters of offshore jurisdiction is vested in the Commonwealth up to the low water mark. ***

2.13 Following the Court's decision, the Department of National Resources became aware of the possible need to revise the offshore petroleum arrangements of 1967. The issues then became the subject of extensive consultations between the Commonwealth and the States, which included the Prime Minister and the State Premiers.

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* Minutes of Evidence, p. 46
** Minutes of Evidence, p. 47
*** Minutes of Evidence, p. 60

2.14 At the June 1978 Premiers' Conference, agreement in principle was reached on new Commonwealth-State arrangements for offshore mining. It was agreed that Commonwealth-State Joint Authorities would be established to administer the area beyond the three mile territorial sea, and Commonwealth legislation only would apply to that area. Decisions of each Joint Authority would be taken by the Commonwealth Minister (the Minister for National Development and Energy) and the relevant State Mines Minister acting jointly, but in the event of disagreement the Commonwealth's view would prevail. It was agreed that the Commonwealth would vest proprietary rights in the seabed of the territorial sea in the States, and the administration of that area would be carried out under State legislation. *

2.15 At the June 1979 Premiers' Conference, agreement was reached on the implementation of the offshore constitutional settlement between the Commonwealth and the States. The Conference decided to extend State powers in the three-mile territorial sea. This was to be effected by all States enacting legislation requesting the Commonwealth Parliament to pass the necessary legislation. It also decided to give the States title to the seabed in the three-mile territorial sea. It was agreed to make consequential amendments to the Seas and Submerged Lands Act 1973 to bring it into line with this decision. **

2.16 The Conference also agreed to establish a Joint Commonwealth-State Authority for each State (including the Northern Territory) to regulate offshore petroleum mining beyond the territorial sea. This was to be carried out under Commonwealth legislation and would utilize the existing offshore petroleum mining code. **

2.17 As discussed in Chapter 3, Bills giving legislative effect to these Agreements were enacted by the Commonwealth in May 1980. The Acts however will not come into operation until a date to be fixed by Proclamation.

Legislative Provisions Governing Excise Duties and Pricing

2.18 Pricing arrangements for locally produced oil have undergone considerable change since the commencement of commercial crude oil production in Australia in 1964, as have the levy arrangements since their introduction in 1975.

2.19 The price of crude oil produced in Australia has been subject to Government control since production commenced from the Moonie field in 1964. Oil from both the Moonie and Barrow Island fields (the latter came on stream in 1967) was,

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* Minutes of Evidence p. 47
** Minutes of Evidence p. 60

until 18 September 1970, priced at above import parity levels because of the inclusion of a substantial incentive component to encourage exploration.

2.20 The discovery of large oil reserves in Bass Strait in 1967, production from which commenced in 1969, resulted in major changes to the earlier pricing policy.

2.21 On 10 October 1968 the then Prime Minister announced that, for the 10 years beginning on 18 September 1970, all Australian-produced oil was to be used by Australian refineries - the so-called 'absorption' policy. (Australian refineries had since 1965, been required to purchase the output of the relatively small Moonie and Barrow Island fields). In addition, he announced that Australian crude oil producers would, for the first half of that period (i.e., from 18 September 1970 to 17 September 1975), receive the import parity price prevailing on 10 October 1968.

2.22 The quadrupling of OPEC prices in 1973 and 1974 was not reflected in the prices paid to producers; they remained unchanged until September 1975.

2.23 An excise levy on Australian-produced crude oil was first introduced, under the Excise Act 1901, in August 1975 when the then Treasurer announced the immediate imposition of a levy of $2.00 per barrel on the production of stabilized crude oil, and naturally occurring liquid petroleum gas (LPG). *

2.24 In September 1975, the then Prime Minister in announcing the oil pricing policy to apply for the five years ending in September 1980 introduced a distinction between 'new' and 'old' oil. For 'new' oil, defined as oil produced from fields discovered after September 1975, producers were to receive import parity prices, as set from time to time, less the $2.00 per barrel levy. Prices paid to producers of 'old' oil defined as oil produced from fields discovered prior to September 1975 were set for three years, to September 1978.

2.25 In the 1977-78 Budget, the Government announced an increase in the crude oil levy from $2.00 to $3.00 per barrel. As a further incentive to oil exploration, the Government also announced that 'new' oil discovered after August 1976 would, in addition to attracting import parity prices, not be subject to the levy. **

2.26 The Government also introduced a two tier duty rate system. The new policy provided for producers of 'old' oil to receive import parity prices (less the levy) for an annually increasing proportion of production or six million barrels, whichever was the greater, from each field or new development within a field. The proportions announced were 10% during the remainder of 1977-78, 20% in 1978-79, 35% in 1979-80 and 50% in 1980-81. Beyond 1980-81 the phasing arrangements were not defined. Oil for which producers received prices based on these arrangements was described as parity-related oil. For the remaining oil produced from each field, which was described as controlled-price oil, the producers received the price which was current when the new arrangements were introduced. *

2.27 In the 1978-79 Budget, the Government raised the price paid by refineries for all domestic crude to the import parity level. The phasing-in arrangements in respect of 'parity-related' oil announced in the previous budget were left unaltered. Under the arrangements, the levy on 'controlled-price' oil was increased so that it was equal to the difference between the import parity price and the price paid to producers. The levy of $3.00 per barrel on 'parity-related' oil was left unchanged. **

2.28 The mini budget of May 1979 introduced a four tier duty rate system under which the rates of levy on parity-related oil varied with the level of production from each field. Consequently, in order to calculate the total amount of levy payable, it became necessary to determine the production from individual fields as precisely as possible.

2.29 A copy of the paper 'Crude Oil Pricing and Levy Arrangements' which was issued as an Appendix to Statement No. 4 in the 1979-80 Budget Papers is reproduced in this Report as Appendix A. Developments in this area in 1980-81 are summarised in Appendix 1 to Statement No. 4, 1981-82 Budget Paper No. 1, which is included in this Report as Appendix B. Total crude oil production from each field in 1980 is indicated in the table at Appendix C.

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* 1975/76 Budget Speech
** 1977/78 Budget Speech

* 1977-78 Budget Speech
** 1978-79 Budget Speech

CHAPTER 3

1980 LEGISLATION

Background

3.1 The High Court decision of 1975 which upheld the constitutional validity of the 1973 Seas and Submerged Lands Act necessitated a substantial revision of the 1967 Agreement with the States and the legislative framework which had flowed from that Agreement, i.e., the Petroleum (Submerged Lands) Act 1967. Detailed discussions between the Commonwealth and the States at the Premiers' Conferences of 1977, 1978 and 1979, together with meetings of the Standing Committee of Commonwealth and State Attorneys-General, resulted in a new offshore constitutional settlement which was adopted at the Premiers' Conference on 29 June 1979.

3.2 On 23 April 1980 the Coastal Waters (State Powers) Bill 1980 was presented to Parliament. In his second reading speech the Prime Minister said the Bill would give effect to the Commonwealth's intention to:

> "share with the States and the Northern Territory powers and resources in the seas surrounding Australia which, as a matter of constitutional law, are presently the Commonwealth's alone." *

The Prime Minister also said that the legislative package was introduced

> "on the basis that the territorial sea is an area best left for local State jurisdiction - except on matters of over-riding national or international importance." *

3.3 The Coastal Waters (State Powers) Bill was introduced in response to legislation which had been enacted by each of the States requesting the passage by the Commonwealth Parliament of such a Bill. The Bill was also the cornerstone of the legislative package agreed to by the Premiers in 1979. That Bill, together with the Coastal Waters (State Title) Bill, coupled with a number of complementary Bills, including an amending Bill to the Seas and Submerged Land Act, purported to vest in the States and the Northern Territory certain powers over and title to the territorial sea around Australia. Doubts, however, have been expressed as to whether these Bills were suitably framed to achieve their stated purpose.

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* House of Representatives Hansard: 23 April 1980 p. 2165

3.4 In order to give effect to the Agreement with the States on off-shore petroleum mining, the Minister for Trade and Resources introduced a Bill to amend the Petroleum (Submerged Lands) Act of 1967. The Minister informed Parliament that the Bill would give legislative effect to the Agreement reached at the Premiers Conferences in October 1977 and 1978 namely:

> ". all off-shore mining would be conducted in accordance with a common mining code or codes;
>
> . Commonwealth legislation would apply beyond the three-mile territorial sea and State legislation within the three-mile territorial sea;
>
> . the present arrangements for the sharing of royalties for petroleum to be preserved;
>
> . there would be joint authorities in respect of all mining operations beyond the three-mile territorial sea consisting of the relevant Commonwealth and State Ministers. The view of the Commonwealth Minister would prevail in the case of disagreement;
>
> . the joint authorities would be responsible for:
>
> - major matters relating to titles (granting or *refusal, renewal, transfer, farm-ins etc*),
>
> - determining conditions of titles including work and expenditure,
>
> - *directions of a permanent or standing nature;*" *

The Minister also said:

3.5 "State Ministers would continue their active role. All *contacts would continue to be through the State Ministers*, and State departments would continue to handle day to day administration and supervision of operations." *

3.6 The Minister then presented the following Bills:

> . the Petroleum (Submerged Lands) (Royalty) Amendment Bill 1980;
>
> . Petroleum (Submerged Lands) (Registration Fees) *Amendment* Bill 1980;
>
> . Petroleum (Submerged Lands) (Exploration Permit Fees) Amendment Bill 1980;

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* House of Representatives Hansard: 23 April 1980, p. 2173

- Petroleum (Submerged Lands) (Pipeline Licence Fees) Amendment Bill 1980;

- Petroleum (Submerged Lands) (Production Licence Fees) Amendment Bill 1980.

3.7 While the assent of the Governor-General was given to the above legislative package on 29 May 1980, the Acts will not come into operation until a date to be fixed by Proclamation. At the time this Report was prepared the Acts had not been proclaimed.

3.8 The Committee understands that the States will pass their own legislation covering off-shore petroleum activities within the territorial sea. It is expected that this stage will be completed in 1981 and that the legislation will be as close as possible to the existing Commonwealth Petroleum Submerged Lands Act as amended. When this stage is completed the Commonwealth will, presumably, proclaim its new offshore legislation.

Petroleum (Submerged Lands) (Royalty) Amendment Act 1980

3.9 The Committee has examined this Act in relation to the matters raised by the Auditor-General. *

Royalty Payments

3.10 In order to clearly establish that royalties received by the Designated Authority, i.e., a State Government Minister, are received on behalf of the Commonwealth, Section 3 (a) of the Act provides as follows:-

> "(1B) Moneys paid to the Designated Authority, after the commencement of this sub-section, by way of royalty in respect of a permit or licence granted after the commencement of this sub-section, or granted before the commencement of this sub-section and continued in force under the law of the Commonwealth, shall be received by the Designated Authority on behalf of the Commonwealth";

3.11 In his second reading speech the Minister for Trade and Resources advised Parliament that:

> "this amendment is required to ensure that the constitutional position of the Commonwealth in

* See Chapter 4

> respect of the collection of moneys under Commonwealth legislation is properly safeguarded." *

CONCLUSIONS

3.12 Having regard to the interaction of the wording of sections 5, 6 and 7 of the Coastal Waters (State Powers) Act 1980 and sections 4, 5, 6 and 8 of the Coastal Waters (State Title) Act 1980 combined with the overall Constitutional situation the Committee doubts the extent to which, if at all, the stated objectives of those Acts if proclaimed will be achieved. The Committee considers that ultimate authority and responsibility over the territorial sea still remains with the Commonwealth.

3.13 As the Commonwealth will in any event retain so much responsibility over the territorial sea the Committee considers it would have been more appropriate for the legislation to provide that the joint authority should function in relation to the territorial seas as well as adjacent areas. Had the legislation so provided and the Joint Authority been given responsibility for making all necessary determinations and the collection and distribution of revenue in respect of both the territorial sea and the adjacent area the problems referred to in other parts of this report could more readily have been overcome.

3.14 Both to maintain the spirit of the agreement between the Commonwealth and the States and for administrative convenience it would be desirable for the Joint Authority to have the right to delegate such of its functions as it sees fit to the Designated Authority coupled with the right to specify terms of such delegation.

3.15 The Committee recommends that the terms of the 1980 legislation be discussed with the States with a view to having the legislation amended prior to being proclaimed, to empower the Joint Authority established under the Petroleum (Submerged Lands) Amendment Act 1980 to function in relation to the territorial sea within the 3 mile limit as well as the adjacent areas outside the 3 mile limit.

3.16 Quite independent of these matters the Committee doubts that the provisions of section 3(a) of the Petroleum (Submerged Lands) (Royalty) Amendment Act 1980 adequately protects the Commonwealth's position in respect of the collection of royalties. Because of the manner in which certain administrative functions in relation to the territorial sea and the adjacent area are passed over to the designated authority the Committee considers that in a practical sense the position of the Commonwealth in relation to the collection of money is not fully safeguarded. Should the Commonwealth Parliament wish to inquire into whether royalties are being properly collected there could be difficulties as it is likely that those with the day to day responsibility for the collection of the Commonwealth's share

* House of Representatives Hansard: 23 April, 1980, p. 2175

of royalties will be State Government officials and therefore under no obligation to furnish full explanations to the Commonwealth Parliament.

3.17 While the Committee believes that the State Government officials have cooperated fully with Commonwealth officials in exercising their responsibilities, the Committee finds this situation most unsatisfactory and is strongly of the view that new methods must be implemented to make the relevant authorities accountable to both the Commonwealth and State Parliaments. The Committee believes a means of achieving this is for the relevant Commonwealth and State Parliamentary Committees to conduct future inquiries into offshore matters jointly. The Committee has reached this conclusion in the certain knowledge that problems similar to those encountered by the Committee will continue unless a novel approach is adopted by both the Commonwealth and the State Parliaments.

Value at the Wellhead

3.18 The Minister for Trade and Resources advised Parliament that Section 6 of the Petroleum (Submerged Lands) (Royalty) Amendment Act 1980

> "enables the joint authority to direct the designated authority regarding ascertainment of the wellhead, of the value of petroleum at the wellhead, and of the quantity of petroleum recovered. Since royalty will be imposed and collected under Commonwealth legislation it is clearly essential for the Commonwealth to have the final say in respect of the determination of the royalty collections. This provision will apply, retrospectively to royalty periods which commenced or terminated before enactment of this Act. It has been included because a satisfactory settlement to the long standing dispute in respect of Bass Strait royalties has not yet been resolved." *

3.19 Since the passage of the above legislation there has been an agreement between the Victorian Designated Authority and Esso/BHP.** The terms of this Agreement which was reached under the provisions of section 9 of the Petroleum (Submerged Lands) (Royalty) Act 1967 are contained in a Direction issued by the Victorian Designated Authority dated 9 June 1980.

3.20 The Committee has noted that the Agreement contains a provision whereby officers (presumably officers of the Victorian Public Service) will reassess the value of petroleum at the wellhead for all royalty periods from the commencement of production.

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* House of Representatives Hansard: 23 April, 1980, p. 2175

** Report of the Auditor-General for Victoria, 1979-80

3.21 In May 1981 the Commonwealth received a payment of $2.19 million from the State as its share of additional royalty payments made by the producers on the basis of their recalculation of all interim royalty payments. The State Department of Minerals & Energy is conducting an examination to verify the producers' calculations.*

3.22 The Committee recommends that officers from the Departments of National Development and Energy and the Auditor-Generals' Office actively participate in the final verification of royalty calculations which should be completed as soon as possible.

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* Auditor-General's Report 1980-81, page 111

CHAPTER 4

THE MATTERS RAISED BY THE AUDITOR-GENERAL

4.1 The Auditor-General in his 1977-78, 1978-79 and 1979-80 Reports raised several matters relating to petroleum royalties and excise duties.

4.2 At paragraph 3.16.1, of his Report for 1977-78, the Auditor-General stated:

> "As a result of Audit enquiries in 1977-78, including consideration of the possible implications of the High Court judgment concerning the validity of the Seas and Submerged Lands Act 1973, it was suggested to the Department of National Development by memorandum dated 11 July 1978 that legal advice be sought to clarify whether the procedures, followed in the accounting for and the sharing of royalties and fees between the Commonwealth and the State of Victoria, complied with the provisions of the Petroleum (Submerged Lands) Act 1967 and the Audit Act 1901. Additionally, advice was sought on:
>
> - aspects relating to the apparent delay in determining the well-head value of the petroleum and the royalties payable; and
>
> - action being taken or proposed by the Department, following earlier representations by my Office, to confirm that all revenue due to the Commonwealth is being collected and accounted for by the Designated Authority."

The Audit Office also enquired into the reasons for the increase of some $9.2 million in royalty receipts in 1977-78 compared with 1976-77.

4.3 At paragraph 2.14.1, of his Report for 1978-79, the Auditor-General stated:

> "Among other things my Office suggested to the Department of National Development in July 1978 that legal advice be sought to clarify whether the procedures, followed in the accounting for and sharing of royalties between the Commonwealth and the State of Victoria, complied with the provisions of the Petroleum (Submerged Lands) Act 1967 and the Audit Act 1901.

> Reference is made in paragraph 2.3.2 of this Report to Audit representations to the Departments of National Development and Business and Consumer Affairs in February and June 1979 on their failure to finalise satisfactory arrangements for the verification of production from the various fields in Bass Strait; and, consequently, of the amount payable as excise on naturally occurring petroleum liquids. The verification procedures for excise also have relevance to the verification of Commonwealth revenue from Bass Strait Offshore Petroleum Royalties ($28 030 869 in 1978-79).
>
> Further Audit representations to the Department of National Development on 29 June 1979 referred to the continuing delay in the determination by the Designated Authority of the value at the well-head of the petroleum recovered and of royalties payable by the producer. My Office indicated that, while it appreciated the difficulties, and the role of the Designated Authority, it seemed that continuation of arrangements, under which royalties being paid continued to be assessed on an interim basis, were neither satisfactory nor in accordance with the apparent intention of the relevant legislation. The Department of National Development was requested to advise whether it was aware of and agreed with the details of the interim arrangements under which royalty was being paid; and with the nature, extent and adequacy of checks being carried out by the Victorian Department of Minerals and Energy of the costs deducted in assessing the interim well-head value."

4.4 At paragraph 2.3.2, of his Report for 1978-79, the Auditor-General stated:

> "In November 1978, my Office was represented at an interdepartmental meeting called by the Department of National Development to discuss, among other things, the role, functions and proposed scope of work of the Department in excise administration and to consider the adequacy of the arrangements including detailed method of examination.
>
> Subsequent Audit review indicated the Department of National Development still had not been able to implement all necessary checks; also it appeared further improvement was necessary in procedures for monitoring production from Bass Strait fields.
>
> Audit observations were addressed to the Department of National Development in February 1979 on the apparent lack of progress by the Department in

agreeing and implementing satisfactory arrangements with the Victorian Department of Minerals and Energy and carrying out necessary verifications. Advice was also sought from the Department of Business and Consumer Affairs on the implementation of the arrangements discussed between the Departments in November 1978.

Further Audit representations addressed to the Departments on 29 June 1979 expressed reservations concerning progress achieved to that time in connection with the verification of production from the various fields in Bass Strait. Reference was made to delay by the Department of National Development in providing certificates of production to the Department of Business and Consumer Affairs. Comments were also made concerning certain procedures proposed."

4.5 The Auditor-General's Office has further expressed its concern about the above matters, both at hearings of the Committee and in correspondence, with the then Department of National Development.

4.6 At its hearing on 8 May 1979, * the Committee was informed of the Audit Office's views that:

- the Department of National Development should consider whether it would not be prudent, in association with the State (of Victoria), to ensure that all action concerning the determination and collection of royalties at present is clearly being taken under Commonwealth legislation,
- the Audit Office has difficulty in accepting the approach taken by the Department in its submission to the Committee, namely, that the Commonwealth is unable to verify the Victorian calculation of royalties,
- the Department of National Development has a responsibility to ensure that there are agreed procedures which the Victorian Department (of Minerals and Energy) should follow in protecting both its interests and the Commonwealth's,
- the Audit Office expects the Department of National Development to arrange for the provision of regular reports and certificates from the State Department confirming that the agreed procedures are in fact continuing to be carried out,

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* Minutes of Evidence pp. 18-19

- the Audit Office expects the State Department to provide some indication of the results of the checks which it carries out,
- the Department (of National Development) has a responsibility to satisfy itself from time to time, by inquiries and visits to the State and to the installations, that the agreed procedures continue to be adequate and that the Victorian Department is in fact adequately protecting Commonwealth revenue,
- the procedures, checks, etc., ... cover factors relating to the continuing determination of well-head values and the matter of the volume of production and its back-allocation to the various fields, and
- it is a matter for the Department of National Development to ensure that the Commonwealth's interests are protected. (The present) audit is of the action being taken by the Department of National Development to protect the Commonwealth's interests.

4.7 Further Audit queries were contained in a memorandum of 29 June 1979 to the Department of Business and Consumer Affairs and the then Department of National Development as follows:

- it was necessary to monitor the volume and content of production of the various well-heads and to maintain controls and perform checks, etc., to ensure the accuracy of the recorded production as input to the back-allocation process as it did not seem that the current departmental procedures, checks and controls could be accepted as being adequate for that purpose;
- it was not clear how the 'best fit' analysis was selected; and whether once selected it continued to be utilised until further new samples were taken and analysed; or, alternatively, another result from the samples previously taken was substituted if the back allocation process commenced to show increasing discrepancies.
- whether the Victorian Department of Minerals and Energy examined in depth the automatic data processes used by the producer in the back-allocation of production.
- it was necessary to obtain a fully documented set of the procedures followed by the producers in those facets of the operations relating to measurement and

analysis of production from the well-head to the point of delivery, and an assurance that the Victorian Department was satisfied that those procedures were being followed.

- there was a need for a written agreement between the Department of National Development and Energy, and the Victorian Department on the nature, extent and frequency of checks of meter provings, readings and related aspects and of the back-allocation, which should be carried out as a minimum by the Victorian Department with copies of reports thereon being provided to the Commonwealth.

- the extent to which it is practicable for the Victorian Department to monitor the taking and analysis of samples of the well-stream composition and the sealing of meters.

- there should be a written report indicating the extent to which the Department of National Development and Energy is satisfied with all aspects of the back-allocation processes, including the equations, assumptions, etc., on which that allocation was based.

- whether the Department of National Development and Energy had provided any certificates of production to the Department of Business and Consumer Affairs.

- whether the understanding was correct that there are no adjustments of excise payments made on the basis of interim allocations between parity and non-parity production, but that the ratio between parity and non-parity production for the interim allocation for the subsequent period is varied to take account of any adjustments necessary to the previous period. If this is so whether this procedure results in the appropriate adjustment;

- it was necessary to take all measures practicable for the Department of National Development and Energy and, as appropriate, the Department of Business and Consumer Affairs, in association with the Victorian Department of Minerals and Energy, to ensure the amounts received as royalties and/or excise duty are those properly due to the Commonwealth.

- should there be any areas of moment where it is not practicable for the Commonwealth departments to be satisfied the Commonwealth's interests are protected, the position should be submitted for consideration at Ministerial level.

- the possibility that the interests of Victoria and the Commonwealth do not necessarily coincide where revenue due to the Commonwealth as excise is concerned. For example, it seems a procedure followed or interpretation, etc., made by the producer and accepted as valid by the Victorian Department of Minerals and Energy may result in increased royalties but less excise. In this context, it is noted that revenue to the Commonwealth from excise is considerably in excess of that from royalties.

- the action proposed to ensure the Commonwealth's overall interests are protected in these circumstances.

4.8 *The Auditor-General's Report for 1979-80 indicated* that several sections of the Petroleum Measurement and Accounting Manual had been received from the producers and were being examined by the appropriate Commonwealth Authorities. In addition the Department of National Development and Energy had advised the Auditor-General that:

- The State Department of Minerals and Energy had been advised of the situation reached and meetings had been held with officers of that Department and the producers.

- The possibility of obtaining the services of private consultants to assess whether the procedures used for sampling on the platforms can be regarded as satisfactory was being considered.

- As emphasised on earlier occasions there is no reason to believe that the procedures followed by the producers and the Victorian authorities were adversely affecting the level of Commonwealth royalty and excise receipts.

- Further development of the computer-based simulation model had been postponed in the expectation that the new procedures would provide a better understanding of the full well-stream composition data.

4.9 The Auditor-General's Report for 1980-81 indicated further developments in relation to the procedures for the measurement and allocation of production to the separate fields in the Bass Strait area and the calculation of royalties and excise due to the Commonwealth. The Auditor-General has expressed the view that although the action now taken or in progress is long overdue, the results when finalised should ensure that there is a satisfactory system of control over the substantial amounts of revenue involved.

CHAPTER 5

THE INQUIRY INTO ROYALTIES

5.1 Currently royalties are levied under the Victorian Petroleum (Submerged Lands) Act 1967 at the rate of 10% of the wellhead value. Of this 60% is retained by Victoria and 40% forwarded to the Commonwealth. In addition the State imposes, and wholly retains, an over-riding royalty of 1% on the Barracouta and Marlin fields and 2.5% on the Halibut, Kingfish, Mackeral, and Tuna fields.

5.2 The *questions on royalties raised in the* Auditor-General's Reports are recorded in Chapter 4 and include:

- whether the procedures for accounting for Commonwealth revenue by way of royalties satisfy the Commonwealth Petroleum (Submerged Lands) Act 1967 and the Audit Act 1901;
- the delay in determining the well-head value;
- whether all the Commonwealth revenue has been accounted for by the Designated Authority;
- the reasons for increased royalty payments in 1977-78;
- the procedures to be adopted in verifying production and revenue to be collected; and
- a possible conflict of interest between the State and Commonwealth Governments.

Legislative support for procedures in royalty collection

5.3 In his 1977-78 Report, the Auditor-General questioned whether the procedures for royalty collection complied with the Petroleum (Submerged Lands) Act 1967 and the Audit Act 1901.

5.4 In response to an Audit Office suggestion of 11 July 1978, the then Department of National Development requested advice on these procedures from the Attorney-General's Department. This advice was received on 6 March 1979.

5.5 A matter of fundamental importance was whether the royalties were being collected under the Commonwealth Petroleum (Submerged lands) (Royalty) Act 1967 or the

Victorian Petroleum (Submerged Lands) Act 1967. The representatives of both the Attorney General's Department and the then Department of National Development * asserted that the Designated Authority was operating under the Victorian Petroleum (Submerged Lands) Act 1967 in the collection of royalties. Under Section 157 of this Act, he is required to collect royalty revenue as a debt due to the State and subsequently, in accordance with this legislation, to transmit a proportion determined by formula to the Commonwealth.

5.6 In its advice of 6 March 1979, the Attorney-General's Department canvassed the question of the validity of the Victorian legislation. While several decisions including the December 1975 High Court decision in the Seas and Submerged Lands case suggested the probable invalidity of the State legislation, there was no actual decision of the High Court invalidating the State legislation and no constitutional challenge seemed likely.

5.7 Although constitutional questions arose from the High Court's December 1975 decision, the Victorian Government continued with the current arrangements for the collection of royalties pending the conclusion of negotiations between the Commonwealth and the States.

5.8 On the basis of the settlement adopted at the Premier's Conference of 1979, Commonwealth Legislation was introduced in May 1980 ** which purports to establish clearly that royalty payments are received by the Designated Authority on behalf of the Commonwealth. This legislation has not yet been proclaimed.

CONCLUSIONS

5.9 *The Committee is of the view that,* in relation to actions taken under current State legislation and in the absence of a High Court decision invalidating that legislation, procedures for validating royalty collections adopted by the Victorian Designated Authority do not have to comply with the Commonwealth Petroleum (Submerged Lands) Act 1967 and the Audit Act 1901. In these circumstances the Committee is concerned that the Designated Authority is not responsible to the appropriate Commonwealth authorities for the procedures adopted for royalty collection. The Committee recommends that *discussions take place between the respective* Commonwealth and State Authorities and between the Auditors-General to ensure that royalty collection procedures compatible with the requirements of both Governments are implemented under the existing legislation and under the 1980 legislation when proclaimed.

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* Minutes of Evidence p. 381 and In Camera Evidence
** See Chapter 3 of this Report

5.10 The Committee wishes to be satisfied that the Designated Authority will be clearly responsible to the appropriate Commonwealth Authorities for the procedures adopted for the collection of royalties.

Delay in determining the well-head value

5.11 The Auditor-General in his Reports for 1975-76 to 1978-79 inclusive reported* on the apparent delay in determining the well-head value of the petroleum produced. This uncertainty was due to the undetermined location of the well-head and the costs to be deducted in arriving at a net figure for well-head value.

5.12 The Committee was informed** that protracted discussions, between the producers and the Designated Authority were conducted from late 1968. In October 1975, when agreement between the producers and the Designated Authority had not been reached as to the well-head value of petroleum (particularly in respect of the royalty period ending on 31 August 1975), the Designated Authority notified the producers that, should agreement not be reached within one month, he would proceed to determine the value, as provided for in the Victorian Petroleum (Submerged Lands) Act 1967, Section 153.

5.13 It is understood that, at that time, the matters at issue between the Designated Authority and the producers included

- the location of the well-head;
- the deductibility in respect of the cost of platforms; and
- the deductibility of the cost of capital.

5.14 Following discussions which had continued with the producers and the decision of the High Court in the Seas and Submerged Lands case, the Designated Authority formally initiated, on 26 August 1976, consultation with the Commonwealth Minister (then for National Resources) pursuant to the 1967 Offshore Petroleum Agreement, prior to making a determination of well-head value. *** The Commonwealth Government's views were then forwarded in August 1977 to Victoria. The Designated Authority responded to the Commonwealth's views on the matter, but deferred making a determination because the Commonwealth requested such deferment until certain implications of the High Court

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* 1975-76 para 2.22.5, 1976-77 para 2.23.5, 1977-78 para 3.16.1, 1978-79 para 2.14.1

** Department of National Development Submission of 30 April, 1979,

*** Minutes of Evidence, p. 47

decision in the Seas and Submerged Lands case had been clarified. *

5.15 As indicated in Chapters 2 the Commonwealth and the States reached agreement on new offshore mining arrangements at the 1979 Premiers' Conference. In brief it was agreed the States territorial rights would be extended up to the three mile limit, while Joint Authorities would regulate offshore petroleum mining beyond this limit.

5.16 On 9 June 1980 the Designated Authority finally made a Determination on the value of petroleum at the wellhead, for all royalty periods from the commencement of production. The significant items included in the agreement are: **

(a) The location of the well-head with respect to wells drilled from fixed platforms is the choke valve or the first control valve located immediately downstream of the point known as the Christmas Tree.

(b) Duties of customs and excise levied by the Commonwealth on sales of petroleum products are excluded from the assessment of a well-head value.

(c) A proportion of the cost of platform structures is deemed to be post well-head fixed assets for purpose of depreciation allowance calculations.

(d) No allowance is made for the cost of working capital.

(e) Allowance is made for interest, at a fixed rate per annum, on the written down value (at the royalty depreciation rate) of all allowable post well-head fixed assets.

CONCLUSIONS

5.17 While neither the producers nor the Designated Authority are able to be held to account by the Commonwealth Parliament, the Committee is gravely concerned that it took some seven years before the negotiations between these parties reached the stage where the Designated Authority decided that it was necessary to determine, in the absence of agreement with the producers, the well-head value of the petroleum produced and another five years to finally make the Determination. The Committee, regards the delay of twelve years in settlement of this issue as completely unsatisfactory.

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* Report of the Auditor-General for Victoria, 1978-79

** Report of the Auditor-General for Victoria, 1979-80

5.18 The Committee is aware that the Designated Authority may have delayed its Determination pending the clarification of legal issues but by doing so, the Designated Authority left unresolved the value of payments to be made by the producers. The Committee is convinced that this episode reflects unfavourably on the administration of offshore petroleum development in Australia and on the attitude of the Commonwealth Departments concerned which should have acted more promptly to establish the role of the Designated Authority and protect the interests of the Commonwealth.

5.19 The Committee recognises the changed constitutional climate in the area of offshore powers since the mirror legislation of 1967. Thus, although there were earlier attempts to introduce such legislation, the Seas and Submerged Lands Act 1973 marked a significant milestone in this area, especially when its validity was upheld by the High Court in 1975. Prior to this, both the Commonwealth and Victoria had administered royalty collections without doubting the validity of the State legislation, the result being that the Commonwealth played a minimal role, receiving its royalties from the Victorian Government in accordance with the formula in the 1967 legislation. * However, when the validity of the Seas and Submerged Lands Act 1973 was upheld, the validity of the State legislation came into question and it was recognised by both the Commonwealth and the States that new arrangements would be necessary. As outlined above, events since 1975 have been directed to agreeing and implementing these new arrangements. The Committee again observes that an unacceptable delay of about five years has been involved in this process and does not consider that annual Premier's Conferences provided a sufficiently expeditious avenue of reaching agreement. Special arrangements should have been implemented aimed at resolving the issues with the State Governments more promptly.

Accounting for Commonwealth Revenue by the Designated Authority

5.20 In his 1977-78 Report the Auditor-General questioned whether action was being taken by the then Department of National Development to confirm that all revenue due to the Commonwealth had been collected and accounted for by the Designated Authority.

5.21 While the Committee recognises that interim royalty payments were being made by the producers under the Victorian Petroleum (Submerged Lands) Act 1967, it is concerned that these payments were properly made.

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* Victorian Petroleum (Submerged Lands) Act 1967, Section 129

5.22 The Committee was informed that, when the Commonwealth's share of royalties is forwarded by the Victorian Treasurer to the Department of Finance in Melbourne, each payment is accompanied by a statement, produced by computer, giving the following details:

- nett production meterings at platforms;
- dispositions and stock changes;
- gross value of production allocated to each field;
- allowable deductions for each field;
- deductions as a percentage of gross value for each field;
- nett well-head value for each field;
- royalty rate for each field;
- royalty payable for production from each field;
- royalty as a percentage of gross value.

5.23 In addition the Victorian Department of Minerals and Energy each month provides the Department of National Development and Energy with production statistics, used by the Department as a check against the production figures contained in the statement. Other information, such as the value of petroleum produced and deductions allowed for the period in question, is made available to the Department only in that statement.

5.24 From the information referred to above and other sources, such as publications of the Victorian Department of Minerals and Energy, the Commonwealth Department of National Development and Energy is able to identify the amount of royalty collected by the Designated Authority, and to verify that the Commonwealth's share i.e. 40% of that amount, is correctly calculated.

CONCLUSIONS

5.25 The Committee is concerned that while the Department is able to establish that the Commonwealth receives the correct proportion of the total royalties collected by the Victorian Government, under current procedures it is unable to verify the calculation by the Victorian authorities of the total figure. In addition the Committee is concerned that the maximising of the royalty collections may conflict with collections of the excise levy. For example crude oil may be allocated to a field which attracts a high over-riding royalty, but a low rate of excise levy under the four tier rate system. The Committee's concern was aroused by the Department's statement that:

> "Because the administration of the royalty system is in the hands of the Designated Authority, the Commonwealth is unable to verify the Victorian calculation of royalties. However, it seems reasonable to assume that Victoria would wish to

maximise royalty collections, and that the Victorian royalty collection and auditing procedures are effective for this purpose. In this respect Victorian interests should coincide with those of the Commonwealth." *

5.26 While the Committee does not doubt the veracity of this statement so far as it goes, it is concerned that the Commonwealth cannot explicitly satisfy itself on this matter and recommends that the Department of National Development and Energy and the Auditor-General's Office should be involved, in cooperation with the Victorian Auditor-General, in ensuring the correctness of the procedures to arrive at the royalty payments.

Reasons for the increased royalty payments in 1977-78

5.27 In his 1977-78 Report the Auditor-General drew attention to the fact that petroleum royalty receipts in that year exceeded the receipts for the previous year by $9,197,634 and that part of the increased payment in 1977-78 resulted from a late payment of $1 058 710 which had been due in 1976-77.

5.28 The Committee was informed ** that, in accordance with the legislation, the producers pay royalty on a monthly basis to the Designated Authority, within the calendar month following production. The Commonwealth's share of this is then transmitted, from the Victorian Treasury, by the end of the following month.

5.29 In this particular case, the Commonwealth's share of the royalty due on the production for April 1977, and received by the Designated Authority in May 1977, was not transmitted to the Commonwealth until 5 July 1977, when the due date was 30 June.

CONCLUSIONS

5.30 The Committee notes the Department of National Development and Energy's assurance that a late payment will not recur. The Committee was informed that, while the legislation requires the State to pay the Commonwealth its share of royalties within one month, it would seem the Commonwealth's share could well be paid immediately it is received by the State. It was suggested to the Committee that if there were to be any adjustment to the Commonwealth share or to the amount paid by the licensee, this could be

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* Department of National Development submission of 10/4/79 p. 2

** Minutes of Evidence 1/5/79 pp. 5 - 10

made in the following month's payment to the Commonwealth. *

5.31 The Committee recommends that arrangements be made for the Commonwealth share of any royalties to be paid immediately it is received by the State, with any adjustments being made in the following month's payment.

Other Royalty matters raised by the Auditor-General**

5.32 These matters broadly cover what the Audit Office regards as responsibilities of the Commonwealth Department of National Development and Energy in oversighting the work of the Victorian Department of Minerals and Energy to ensure that adequate procedures are in place to enable the correct amount of royalty payable to be determined.

5.33 The Committee notes that it is the responsibility of the Victorian Auditor-General to ensure that the Victorian Department of Minerals and Energy in turn fulfils its responsibilities in regard to royalty collection. The Committee is aware that for several years the Victorian Auditor-General has reported on royalty matters and that these reports have been the subject of inquiry by the Victorian Public Accounts and Expenditure Review Committee.

CONCLUSIONS

5.34 In the Committee's opinion the Department of National Development and Energy has been too willing to vacate the field in favour of the State authorities and has not made sufficient effort to establish check procedures by which to ensure that royalty payments are correctly determined. As recommended at paragraph 5.26, the Committee is strongly of the view that the Department of National Development and Energy and the Auditor-General, should be involved, in co-operation with the Victorian Auditor-General, in ensuring the correctnes of royalty payments.

5.35 The Committee wishes to draw to the attention of the Victorian Public Accounts and Expenditure Review Committee the apparent tardiness of the Victorian Department of Minerals and Energy in documenting procedures for the collection of royalty payments.

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* Minutes of Evidence 1/5/79 pp. 6 and 7

** See page 24

CHAPTER 6

THE INQUIRY INTO EXCISE DUTIES

6.1 The questions raised by the Auditor-General in relation to Excise Duties are recorded in Chapter 4. In brief, the Auditor-General was concerned with:

- the need for adequate procedures for monitoring production from the Bass Strait fields; and
- delays in the provision of Certificates of Production which are necessary to determine the excise due.

Monitoring of Production - Back Allocation and the Mass Balance Program

6.2 Because the rate of excise varies according to whether a field is classified as small (less than 2 million barrels per annum), medium (2-15 million barrels per annum) or large (over 15 million barrels per annum) it is necessary to draw up a systematic method by which end products (gases, LPG and crude oil) are allocated back to the various gas and oil fields in the Bass Strait production area. The results of this back allocation are then used for the calculation of royalty and excise payments.

6.3 The back allocation procedure is based on the assumption that all end products and all well streams (oil and gas straight from the various fields) are composed of known proportions of the same fixed set of basic components (nitrogen, carbon dioxide, methane, ethane, propane, butane, pentane, crude oil). The well stream compositions and volumes are adjusted to take account of that part which is either consumed as fuel or flared (burnt as waste). These adjusted well streams are then used as the basis for the back allocation of end products.

6.4 The mass balance procedure is a measure of the difference, on a component by component basis, between the assumed total mass input to the processing plant and the measured output, in the form of end products. *

6.5 While the principles underlying the back allocation mass balance program are relatively straightforward, the Committee was informed ** that the collection of

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* Minutes of Evidence PP 87, 151

** Department of National Develoment and Energy submission of 19 November 1979.

representative samples of the full well stream is a technically difficult exercise for the following reasons.

- there is no assurance that any sample obtained from a well is representative of the fluid throughout the reservoir (the sample may not even be representative of the fluid in the immediate vicinity of the well being sampled);
- if a well draws fluid from two or more zones in the reservoir, the sample may be a mixture of two sets of fluids and may not be representative of either;
- where both oil and gas are produced from the same reservoir, as occurs in Bass Strait, the flow rates of each will almost always be different, (consequently it is fortuitous if a sample of fluid is representative);
- the composition of the sample will change with variations in reservoir pressure;
- because of technical limitations, the underlying measurements may only be accurate to within plus or minus one per cent;
- the full well stream composition can vary with production rates and reservoir depletion.

Despite all the above difficulties it is, nevertheless, critical to the back allocation and mass balance program to accurately measure the full well stream composition. The Committee appreciates that the measurement of the full well stream composition is by no means precise.

6.6 The Committee was also informed that, as no other country requires a producer to allocate end products back to the well stream, there is no established experience upon which to draw. Although a number of co-producers, eg the Brent oilfield of the North Sea, have such arrangments these are commercial agreements and unavailable to Australian authorities.

The documentation of the procedures

6.7 In addition to the Victorian Department of Minerals and Energy's need for information from the back allocation and mass balance program for royalty calculations, the Commonwealth Government requires information which relates the volume of production to particular fields to determine the excise due from these fields. The development and details of this policy were outlined in Chapter 2 and appear more fully in the submissions from the Department of Business and Consumer Affairs (whose responsibility it is to collect

excise) and the then Department of National Development which are included in the Minutes of Evidence. *

6.8 The need to develop a mass balance program was recognised as early as December 1969 when the Designated Authority indicated to the producers that the value of the products would be allocated to the producing wells according to a method which was to incorporate a material balance involving the volumes and chemical compositions of the petroleum which was recovered at the well-head and the petroleum products which were sold. The Commonwealth Government only became involved in the detail of this mass balance program when it introduced its current excise levy policy in the 1978/79 Budget. Prior to this a flat rate levy had applied to all "old" oil production.

6.9 With the introduction of the excise levy and in view of its involvement in the administration of the off-shore petroleum legislation, the then Department of National Development agreed to assist the Department of Business and Consumer Affairs in the verification of stabilized crude oil production from the Bass Strait fields.

6.10 An indication of the difficulties which were facing the then Department of National Development appears in a memorandum which it forwarded to the Department of Business and Consumer Affairs on 13 September 1979. ** The Department wrote it understood that the Department of Business and Consumer Affairs had had discussions with Esso concerning their back allocation program and that Esso had indicated they were giving priority to writing these up, a process which could take a few months. The Department expressed the view that "this really is quite unsatisfactory" given that the Victorian Department of Minerals and Energy had been first asked for copies of the procedures in February 1979 and subsequently in May and July. The Department stated that it was pressing the Victorian Department again to expedite the writing up of procedures. The Department was subsequently informed by the the Victorian Department that an estimated six man months of work remained and that it was hoped that the exercise could be completed by about December 1979.

6.11 The picture which emerges from this chronology of events is that the then Department of National Development had undue optimism that the procedures, which it needed to monitor production, were properly documented and available. This is understandable, given the Victorian Department of Minerals and Energy had been collecting a variable overriding royalty since 1969 and it would have been expected

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* Minutes of Evidence PP 42 - 107

** Department of Business and Consumer Affairs submission of 16 November 1979

such procedures would have been fully documented. However, it appears that it took until the middle of 1979 for the increasing realization that this was not so to be fully understood and even later for the Department to recognise that it would take much longer than the initially anticipated few weeks for acceptable documentation of the procedures to be available for examination by the Commonwealth.

6.12 The Committee understands that draft documentation is now under consideration by the appropriate Commonwealth authorities. The Committee has also been advised that the Department of National Development and Energy is seeking the services of a consultant to advise on procedures regarding well-stream composition. As yet an appointment has not been made because of difficulty in locating the necessary expertise, despite world wide enquiries.

Attempts at alternative solutions

6.13 Recognising the difficulties it was encountering in the verification of [illegible] duty the Department of Business and Consumer Affairs began exploring alternative arrangements during mid-1979.

6.14 The first difficulty related to the role of the Victorian Department of Minerals and Energy. While the Department of Business and Consumer Affairs is responsible for ensuring that the correct amount of excise is collected, it had not at that time proved possible for it to verify the accuracy and completeness of the production figures that were the basis of the parity and non-parity split. Thus the Department raised with the then Department of National Development the possibility of direct departmental involvement with the producers. In this regard the Department of Business and Consumer Affairs claimed that in all other areas of excise collection it worked directly with the producers of excisable goods rather than through intermediate agencies. The Department noted its dependence on the Victorian Department of Minerals and Energy which is a party the Commonwealth Department cannot in any way hold to account.

6.15 The Department of Business and Consumer Affairs therefore suggested to the then Department of National Development that additional information be obtained direct from the producers which would make it possible for a closer appreciation by both departments of the parity/non-parity allocation to be determined in relation to the excise calculation.

6.16 In addition, the Department of Business and Consumer Affairs drew attention to the security provisions available

to it under the Excise Act. This legislation provides for a payment to be required by way of a securiy from persons clearing goods when all of the information necessary to correctly assess the duty payable has not been forthcoming or is not available. The Department suggested * that security of 1% or 2% of the duty calculated by Esso/BHP as being due at the time of weekly payment might be required. This would be a considerable sum and it was thought that it might provide the incentive for earlier resolution by the Company of the correct parity/non-parity proportions of production. The Committee understands this proposal was not proceeded with.

6.17 In the absence of the back allocation and mass balance program the Department of Business and Consumer Affairs did not have sufficient information to establish that the correct parity and non-parity proportions had been calculated by Esso. To overcome this deficiency the Department proposed that it confine itself to the verification of the amount of crude oil subject to the excise levy, something it was readily able to do, while the Department of National Development took the role, with appropriate legal backing, for determining the parity/non-parity production allocation. Again, the Committee understands that this proposal was not taken up.

CONCLUSIONS

6.18 The Committee regards the lack of adequate procedures and the consequent delays as negligent. We believe that the crude oil excise levy policy was introduced without the Government being given sufficient advice of the practical difficulties involved and in the light of experience elsewhere, with unnecessary complication.

6.19 The Committee's view is reinforced by the fact that while the 1978/79 Budget speech was delivered on 15 August 1978, to the Committee's knowledge the first contact between the Department of Business and Consumer Affairs and the Department of National Development and Energy to discuss implementation of the policy was made only 6 days earlier, on 9 August. Because of the need to maintain Budget secrecy, it had not been possible for prior consultation with Esso/BHP. Instead, after discussing the matter with the Department of National Development and Energy, the Department of Business and Consumer Affairs had assumed it would be able to accurately calculate excise liabilities by drawing upon the procedures developed by the Victorian Department of Minerals and Energy for assessing its variable over-riding royalty. Both Departments confirmed that it was only with the passage of time that it was found that the procedures used by the

* Minutes of Evidence, p. 174

Victorian Department were not as well defined and documented as required. This led to the Commonwealth exerting increasing pressure on the Victorian Department to have the documented procedures made available as early as possible.

6.20 The Committee concluded from this evidence that Departments had given advice to Ministers in a budgetary context in the mistaken belief that the information required to enable ministerial decisions to be carried out was available. One witness told the Committee that "at the time no one really envisaged the mass of technical detail involved in satisfying the Commonwealth on the revenue side".

6.21 This and similar statements confirm the Committee's view that the changes to the oil excise levy were recommended to Ministers without the officials knowing whether that program could be adequately implemented. In addition it appears that there was little if any liaison between the policy Departments developing the program and the Department which was to administer it. We reached this conclusion on the basis of evidence that the Department of Business and Consumer Affairs was not formally involved in the policy consideration, and was being concerned only with the administrative process of implementation.

6.22 In view of the significance of the excise levy program the Committee believes that departments have been negligent in not ensuring that adequate procedures were in place. From the viewpoint of the Government, the public, and the producers not insignificant amounts of revenue are involved. While the Committee believes that well-stream flows are accurately metered, evidence was received that the probable error in collection of excise in 1978-79 due to inaccuracy in the back allocation procedures could exceed plus or minus $10 million.* Both the economic and political significance of this program - the levy on crude oil and LPG yielded $3,108 million in 1980/81 - lead the Committee to strongly condemn an administrative system which allows such a situation to occur and remain unresolved.

6.23 In particular the Committee, while not absolving the Department of Business and Consumer Affairs, considers the former Department of National Development must take a large share of the responsibility for the delay in developing a back allocation and mass balance program. The Committee does not accept that the Department should have assumed the procedures developed by the Victorian Department of Minerals and Energy for assessing royalty payments would be readily available. It considers that the Department took an inordinately long time to realise this was not so.

6.24 Although the current oil excise levy policy was introduced in the 1978-79 Budget the documentation of

* Minutes of Evidence, page 174

procedures has not yet been finalised. The Committee recommends that the Departments of National Development and Energy and Business and Consumer Affairs give this matter urgent attention and expects to be advised of substantial progress in the near future. Efforts to acquire the services of a consultant to advise on the procedures regarding well stream composition should be pursued.

6.25 The Committee expects that, after the relevant Government departments have examined the documented procedures and have satisfied themselves that the procedures are adequate, the Auditor-General will be able to indicate his satisfaction that the excise levy program is being administered in a correct and accountable manner. To this end, the committee intends to examine progress made in this area when it further considers the reports of the Auditor-General.

6.26 The Committee is also concerned that the administering Departments do not appear to have ensured at an early stage that the procedures necessary to implement a program meet the requirements of an external auditor. It seems to the Committee that it would be more efficient for Departments to ensure this at an early stage in the development of a program rather than subsequently encountering avoidable difficulties. The Committee therefore suggests that the co-ordination process of developing a new government program should include clearance by the Auditor-General to ensure that review and audit mechanisms are satisfactory.

6.27 Finally, the Committee has noted that only in the United Kingdom and Canadian legislation has a 'well-head value' concept been used. The Canadian experience is of little practical relevance, however, as there has been as yet no commercial production of petroleum from Canadian offshore areas. In the United Kingdom royalties based on well-head value were applied to earlier offshore petroleum licensees but continuing difficulties of interpretation led to a revision of the procedures in 1976 and royalties are now calculated on an entirely different basis, without reference to well-head value, in respect of licences issued after that date. * The Committee recommends that the Department examine those procedures further with a view to adopting a much simpler and administratively satisfactory solution which will satisfy the requirements for maximisation and accountability of revenue.

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* Minutes of Evidence, p. 55

BUDGET SPEECH 1979-80

APPENDIX TO STATEMENT No. 4

CRUDE OIL PRICING AND LEVY ARRANGEMENT

APPENDIX TO STATEMENT No. 4

CRUDE OIL PRICING AND LEVY ARRANGEMENTS

On 29 June 1979 the Minister for National Development announced new excise levy rates for domestically produced oil. Those rates are related to the price paid by refineries for Australian-produced crude oil (the 'import parity' price) and to the price received by Australian oil producers. Pricing arrangements for locally-produced oil have undergone considerable change since the commencement of commercial crude oil production in Australia in 1964, as have the levy arrangements since their introduction in 1975. The summary below traces developments in both areas.

The price of crude oil produced in Australia has been subject to Government control since production commenced from the Moonie field in 1964. Oil from both the Moonie and Barrow Island fields (the latter came on stream in 1967) was, until 18 September 1970, priced at above import parity levels because of the inclusion of a substantial incentive component to encourage exploration. Prices received by the Moonie and Barrow Island producers prior to September 1970 were $3.14 per barrel and $3.24 per barrel respectively.

The discovery of large oil reserves in Bass Strait in 1967, production from which commenced in 1969, resulted in major changes to the earlier pricing policy.

On 10 October 1968 the then Prime Minister announced that, for the 10 years beginning on 18 September 1970, all Australian-produced oil was to be used by Australian refineries—the so-called 'absorption' policy. (Australian refineries had, since 1965, been required to purchase the output of the relatively small Moonie and Barrow Island fields.) In addition, he announced that Australian crude oil producers would, for the first half of that period (i.e., from 18 September 1970 to 17 September 1975), receive the import parity price prevailing on 10 October 1968. On the basis of this policy producers were to receive the prices shown below:

	Per barrel
	$
Bass Strait	2.06 to 2.10(*a*)
Barrow Island	2.23
Moonie	2.15

(*a*) Varied according to quality differential.

The quadrupling of OPEC prices in 1973 and 1974 was not reflected in the prices received by producers; they remained unchanged until September 1975.

An excise levy on Australian-produced crude oil was first introduced on 19 August 1975 when, in the Budget Speech for 1975-76, the then Treasurer announced the immediate imposition of a levy of $2.00 per barrel on the production of stabilised crude oil, and naturally occurring LPG. The levy was initially announced as a rate set in dollars per barrel and, while the *Excise Act* 1901 sets the rate in dollars per kilolitre, the dollars per barrel equivalent is, for the sake of continuity, used in this appendix. The levy was added to the price paid by refiners to producers; the outcome was thus as follows:

	Bass Strait	Barrow Island	Moonie
	per barrel	per barrel	per barrel
	$	$	$
Price received by producers	2.10	2.23	2.15
plus levy	2.00	2.00	2.00
Price paid by refiners	4.10	4.23	4.15

On 14 September 1975, following a review of policy, the then Prime Minister announced the oil pricing policy to apply for the five years ending 17 September 1980. That policy introduced the distinction between 'new' and 'old' oil. For 'new' oil, defined as oil produced from fields discovered after 14 September 1975, the policy provided for producers to receive import parity prices, as set from time to time, less the $2.00 per barrel levy. The import parity price in September 1975 was about $8.90 per barrel for the equivalent of Bass Strait oil. (No Bass Strait oil attracted import parity price at that time.)

Prices paid to producers of 'old' oil, i.e., oil produced from fields discovered prior to 14 September 1975, were set for the three years ending 17 September 1978 as shown in the following table. These prices took into account the varying costs of the respective producers and their rates of return. It was also announced that the Industries Assistance Commission would be asked to review the pricing levels to apply between 18 September 1978 and 17 September 1980.

Price to producers	Sept. 1975 to Sept. 1976	Sept. 1976 to Sept. 1977	From Sept. 1977
	per barrel	per barrel	per barrel
	$	$	$
Bass Strait	2.33	2.33	2.33
Barrow Island	2.73	2.88	3.17
Moonie	3.00	4.35	5.25

The prices paid by refiners reflected these prices plus the crude oil excise levy which had been introduced in August 1975 at the rate of $2.00 per barrel.

In the Budget for 1977-78 the Government announced an increase in the crude oil levy from $2.00 to $3.00 per barrel. (The levy on naturally occurring LPG has been changed since 1975 but as it is outside the scope of the subject under discussion, it is not considered further in this appendix.) As a further incentive to oil exploration, the Government also announced that 'new' oil discovered after 18 August 1976 would, in addition to attracting import parity prices, not be subject to the levy. (That policy was reaffirmed by the Treasurer on 24 May 1979.)

The 1977-78 Budget also embodied a major change to the then existing oil pricing policy. The new policy, which was broadly in line with the thrust of the

Industries Assistance Commission's report on Crude Oil Pricing released in September 1976, left unaltered the existing $3.00 per barrel levy but introduced a significant change to the arrangements for determining prices paid to producers for 'old' oil. The new policy provided for producers of 'old' oil to receive import parity prices (less the levy) for an annually increasing proportion of production or 6 million barrels, whichever was the greater, from each field or new development within a field. The proportions announced were 10 per cent during the remainder of 1977-78, 20 per cent in 1978-79, 35 per cent in 1979-80 and 50 per cent in 1980-81. Beyond 1980-81 the phasing arrangements were still to be determined.

The import parity price was to be determined each six months (on 1 July and 1 January respectively) by the responsible Minister. (In a statement on 27 June 1979 the Prime Minister announced that the Government would adopt a more flexible approach to the timing of price adjustments to take account of OPEC pricing decisions.) In determining that price, account is taken of the posted price of Saudi Arabian light 'marker' crude, freight and insurance costs to the nearest refinery port, and quality differences between Saudi 'marker' crude and oil produced from each Australian oil region, i.e., Bass Strait, Barrow Island and Moonie. Variations in freight and quality differentials result in relatively small variations in import parity prices.

Oil for which producers receive prices based on these arrangements may be described as *parity-related* oil; for the remaining oil produced from each field—which may be described as *controlled-price* oil—the producers receive the price which was current when the new arrangements were introduced.

The prices received by producers and the prices paid by refiners for 'old' oil immediately following the 1977-78 Budget were:

	Bass Strait	Barrow Island	Moonie
	per barrel $	per barrel $	per barrel $
Parity-related oil—			
From 17.8.77 to 31.12.77—			
Paid by refiners(*a*)	13.00	13.00	13.00
Less levy	3.00	3.00	3.00
Price to producers	10.00	10.00	10.00
From 1.1.78 to 30.6.78—			
Paid by refiners(*a*)	12.62	12.62	12.99
Less levy	3.00	3.00	3.00
Price to producers	9.62	9.62	9.99
Controlled-price oil—			
From 17.8.77 to 30.6.78—			
Paid by refiners	5.33	5.88	(*c*)
Less levy	3.00	3.00	(*c*)
Price to producers(*b*)	2.33	2.88	(*c*)

(*a*) Import parity price
(*b*) Controlled price.
(*c*) The Moonie producer receives the parity-related price for all production.

In the 1978-79 Budget the Government raised the price paid by refineries for *all* domestic crude to the import parity level. The phasing-in arrangements in respect of 'parity-related' oil announced in the previous Budget were left unaltered and, in accordance with those arrangements, the proportion of oil for which producers received the 'parity-related' price was increased from 10 per cent to 20 per cent as from 1 July 1978. Under these arrangements the levy on 'controlled-price' oil was increased so that it was equal to the difference between the import parity price and the price paid to producers. The levy of $3.00 per barrel on 'parity-related' oil was left unchanged.

Under those arrangements the outcome in 1978-79 was:

	Bass Strait	Barrow Island	Moonie
	per barrel $	per barrel $	per barrel $
Parity-related oil—			
From 1.7.78 to 31.12.78—			
Import parity price	12.59	12.64	13.52
Less levy	3.00	3.00	3.00
Price to producers	9.59	9.64	10.52
From 1.1.79 to 30.6.79—			
Import parity price	13.66	13.75	14.80
Less levy	3.00	3.00	3.00
Price to producers	10.66	10.75	11.80
Controlled-price oil—			
From 1.7.78 to 15.8.78—			
Paid by refiners	5.33	5.88	
Less levy	3.00	3.00	(*b*)
Price to producers	2.33	2.88	
From 16.8.78 to 31.12.78—			
Import parity price	12.59	12.64	
Less levy	10.26	9.76	(*b*)
Price to producers	2.33	2.88	
From 1.1.79 to 30.6.79—			
Import parity price	13.66	13.75	
Less levy	11.28	10.85	(*b*)
Price to producers	2.38(*a*)	2.90(*a*)	

(*a*) Increase in price to producers on earlier periods to compensate for credit terms extended to refiners.
(*b*) The Moonie producer receives the parity-related price for all production.

On 29 June 1979 the Minister for National Development announced new import parity prices to apply from 1 July 1979 and new levy arrangements to apply to 'parity-related' oil. (Since 28 June 1979 prices charged by some OPEC members have included officially sanctioned market premia on the basic posted price charged by Saudia Arabia for its light 'marker' crude. Australian import parity price, however, continues to be based on the posted price of Saudi light

'marker' crude i.e., it excludes the market premia.) The levy arrangements in relation to 'controlled-price' oil from Bass Strait and Barrow Island remain unaltered as follows:

	Bass Strait	Barrow Island
	per barrel	per barrel
	$	$
Import parity	18.66	18.84
Less levy	16.25	15.91
Price to producers	2.41(*a*)	2.93(*a*)

(*a*) Increase in price to producers on earlier periods to compensate for credit terms extended to refiners.

The new levy arrangements for 'parity-related' oil distinguish between fields as follows:

- For fields with an annual production of less than 2 million barrels, the levy remains at $3 per barrel. The outcome from 1 July 1979 for these fields, including total production at Moonie is:—

	Bass Strait	Barrow Island	Moonie
	per barrel	per barrel	per barrel
	$	$	$
Import parity price	18.66	18.84	19.71
Less levy	3.00	3.00	3.00
Price to producers	15.66	15.84	16.71

- For fields with an annual production of at least 2 million but less than 15 million barrels, the levy is $3 per barrel *plus* 75 per cent of increases after 30 June 1979 in the import parity price. Consequently, the return to producers now is their return from 1 January 1979 *plus* 25 per cent of increases after 30 June 1979 in import parity prices. The outcome from 1 July 1979 is:—

	Bass Strait	Barrow Island
	per barrel	per barrel
	$	$
Import parity price	18.66	18.84
Less levy	6.75	6.82
Price to producers	11.91	12.02

- For fields with an annual production of 15 million barrels or more, which covers only certain Bass Strait fields, the levy from 1 July 1979 to 31 December 1979 is $3 per barrel *plus* the increases on 1 January and 1 July 1979 in the import-parity price. This leaves the returns per barrel to the producer at their levels from 1 July to 31 December 1978. The outcome between 1 July and 31 December 1979 is:—

	Bass Strait
	per barrel
	$
Parity-related price	18.66
Less levy	9.07
Price to producers	9.59

- From 1 January 1980, the present return to producers in respect of these Bass Strait fields of $9.59 per barrel will be indexed according to increases in the Consumer Price Index after the December quarter of 1978 or increases in import parity prices after 1 July 1979, whichever is the lesser. The levy will take up the balance of the import parity price.

As in 1978-79, the prices charged to refineries are the import parity prices. The phasing towards 'parity-related' prices to producers up to and including 1980-81 remains as indicated above, with 6 million barrels per annum or 35 per cent of the production of each field, whichever is greater, attracting a 'parity-related' price in 1979-80. Beyond 1980-81 it has been announced that, for fields producing less than 15 million barrels per annum, the Government reaffirmed its in-principle decision to continue phasing towards a 'parity-related' price to producers beyond 50 per cent, but that, for fields producing more than 15 million barrels per annum, it does not intend that the proportion be increased above 50 per cent.

APPENDIX I TO STATEMENT No. 4

CRUDE OIL AND LIQUEFIED PETROLEUM GAS: PRICING AND LEVY ARRANGEMENTS

Appendix I to Statement No. 4 attached to the 1980-81 Budget Speech outlined the crude oil and LPG pricing and levy arrangements applicable in Australia at that time. This Appendix summarises the developments in this area since the last Budget.

CRUDE OIL

On 23 December 1980 and 26 June 1981 the Minister for National Development and Energy announced new determinations of import parity prices and associated crude oil levy rates to apply from 1 January 1981 and 1 July 1981, respectively. The determinations of the import parity prices were in accordance with the policy announced by the Minister for National Development on 4 July 1978. This policy is to base the import parity price for domestically produced crude oil on the official Saudi Arabian Light 'marker' price, adjusted to include quality differentials, freight, insurance and evaporation loss, and converted to Australian dollars; further adjustments are then made to allow for coastal freight, wharfage and credit terms. Australian refiners pay the resultant import parity prices for indigenous crude oil. Producers receive those prices less the levy payable to the Commonwealth. The determinations of the levy rates were in accordance with the arrangements announced by the Minister for National Development on 29 June 1979.

Official prices of Saudi Arabian Light 'marker' crude and the equivalent Australian import parity prices for Bass Strait crude over the past three years are shown below:

	Saudi Arabian Light 'marker' crude oil	Bass Strait crude oil
	($US per barrel, fob Ras Tanura)	($A per barrel, fob Westernport) (*a*)
1 July 1978	12.70(*b*)	12.59
1 January 1979	13.33(*c*)	13.66
1 July 1979	18.00(*d*)	18.66
1 January 1980	26.00(*e*)	24.77(*f*)
1 July 1980	28.00(*g*)	27.50
1 January 1981	32.00	30.23
1 July 1981	32.00	30.79(*h*)

(*a*) Prices (and levy rates) are set in dollars per kilolitre but, for purposes of comparison, are converted to dollars per barrel equivalents.
(*b*) Unchanged from 1 July 1977.
(*c*) Increased to $US14.55 per barrel with effect from 1 April 1979, and to $US18.00 per barrel with effect from 1 June 1979.
(*d*) Increased to $US24.00 per barrel with effect from 1 November 1979.
(*e*) The increase to $US26.00 per barrel was announced in February 1980, with retrospective effect to 1 January 1980.
(*f*) Based on $US24.00 per barrel, *see* footnote (*e*).
(*g*) Increased to $US30.00 per barrel on 17 September 1980 with effect from 1 August 1980, and to $US32.00 per barrel on 16 December 1980 with effect from 1 November 1980.
(*h*) This increase in the import parity price was due largely to changes in the $US/$A exchange rate.

The Commonwealth Government's excise 'take' in 1980-81 was equivalent to about 71 per cent of the average price to refineries, for domestically produced crude oil, of $28.89 per barrel. (In addition to the levy proceeds, the Commonwealth receives a share of the royalties paid by the producers. In 1980-81, that share amounted to $52 million and is recorded in 'Other Receipts'.)

The excise rate varies according to the date of discovery and the size of each field.

For oil discovered prior to 14 September 1975[1] the producers' return and hence the excise rate vary according to the size of each field (large, medium or small) and the category of production (parity related or controlled). Producers of 'new' oil from fields discovered on or after 18 August 1976 are not subject to any levy and receive the import parity price on the whole of their production.

In 1980-81 producers of 'old' oil received a higher return, related to the import parity price, on 50 per cent of production or on 6 million barrels per annum, whichever was the greater, for each field or substantial new development within a field. For the balance of their production from such fields, producers received a controlled return, i.e. the Government-determined price which applied at the time of the 1977-78 Budget, adjusted for changes in the costs incurred by producers in extending credit to refiners.

On 26 June 1979 the Minister for National Development announced an 'in-principle' decision to continue the phasing-in of the parity related returns to fields producing less than 15 million barrels per annum. The Government has decided that such phasing should continue for 3 years in steps of 5 per cent each year, commencing from 1 July 1981, i.e. to 65 per cent from 1 July 1983. For fields producing more than 15 million barrels per annum the proportion of production attracting parity related returns is to be held at 50 per cent.

The following revenue sharing arrangements apply in respect of *parity related oil.*

- for fields with an annual production of less than 2 million barrels (small fields) the levy remains at $3 per barrel and increases in price accrue entirely to producers;
- for fields with an annual production greater than 2 million barrels but less than 15 million barrels (medium fields), the levy is $3 per barrel plus 75 per cent of increases in the import parity price after 30 June 1979 (producers therefore receive the $10.66 per barrel they were receiving at that date plus 25 per cent of increases in the import parity price since then); and
- for fields with an annual production greater than 15 million barrels (large fields), producer returns from 1 January 1980 have been determined by indexing the 31 December 1979 return of $9.59 by the cumulative increases in the Consumer Price Index after the December quarter 1978 or cumulative increases in import parity prices after 1 July 1979, whichever is the lesser. (This arrangement was subsequently reviewed and the September quarter 1978 became the starting point for calculating increases in the Consumer Price Index from the 1 July 1980 adjustment.) Both 1981 adjustments have been based on movements in the Consumer Price Index, with the levy taking up the balance of the increase in the import parity price.

(1) Formally, the effect of the present excise by-laws is that this basis applies to oil discovered prior to 18 August 1976; this machinery provision reflects the fact that no discoveries between 14 September 1975 and 17 August 1976 have been identified.

The import parity prices for crude oil, levy rates and (gross) returns to producers applicable to the different categories of oil during 1981 are set out below:

PARITY RELATED OIL

(a) Small fields (less than 2 million barrels per annum)

	Bass Strait	Barrow Island	Moonie
	$ per barrel	$ per barrel	$ per barrel
From 1.1.81 to 30.6.81—			
Import parity price	30.23	30.61	31.81
Less levy	3.00	3.00	3.00
Return to producers	27.23	27.61	28.81
From 1.7.81 to 31.12.81—			
Import parity price	30.79	31.04	31.98
Less levy	3.00	3.00	3.00
Return to producers	27.79	28.04	28.98

(b) Medium fields (2-15 million barrels per annum)

	Bass Strait	Barrow Island
	$ per barrel	$ per barrel
From 1.1.81 to 30.6.81—		
Import parity price	30.23	30.61
Less levy	15.43	15.64
Return to producers	14.80	14.97
From 1.7.81 to 31.12.81—		
Import parity price	30.79	31.04
Less levy	15.85	15.97
Return to producers	14.94	15.07

(c) Large fields (over 15 million barrels per annum)

	Buss Strait
	$ per barrel
From 1.1.81 to 30.6.81—	
Import parity price	30.23
Less levy	18.69
Return to producers	11.54
From 1.7.81 to 31.12.81—	
Import parity price	30.79
Less levy	18.74
Return to producers	12.05

CONTROLLED OIL (i.e. the non parity related oil from medium and large fields)

	Bass Strait	Barrow Island
	$ per barrel	$ per barrel
From 1.1.81 to 30.6.81—		
Import parity price	30.23	30.61
Less levy	27.66	27.49
Return to producers	2.57	3.12
From 1.7.81 to 31.12.81—		
Import parity price	30.79	31.04
Less levy	28.21	27.92
Return to producers	2.58	3.12

TOTAL CRUDE PRODUCTION 1979-80

(MEGALITRES)

	Barracouta Gas	Barracouta Oil	Marlin Oil	Halibut Oil	Kingfish Oil	Mackerel Oil	Tuna Oil	Cobia Oil	South Mackerel Oil	Total
July	11.2	16.8	79.4	287.2	1319.1	451.6	.1	5.3	..	2170.7
August	9.9	16.5	73.1	351.2	1219.1	411.8	..	6.7	..	2088.3
September	4.9	15.3	66.2	332.2	1023.6	447.1	30.8	.2	..	1920.3
October	3.7	15.2	64.6	445.2	1131.6	457.4	34.8	..	..	2152.5
November	.4	5.5	67.8	306.8	1018.1	471.4	51.2	5.4	.2	1926.8
December	..	7.4	59.1	405.2	1082.5	431.8	37.4	7.6	26.4	2057.4
January	..	7.7	53.0	394.7	1040.3	450.4	53.1	10.4	28.9	2038.5
February	1.4	11.4	59.2	228.3	631.1	448.6	48.4	13.0	29.7	1471.1
March	2.4	14.3	60.4	364.2	586.4	523.2	37.3	5.3	34.6	1628.1
April	5.5	15.2	59.2	460.2	792.4	497.6	5.6	.2	33.0	1868.9
May	11.3	6.7	64.6	149.8	672.7	478.9	5.3	5.3	38.1	1432.7
June	16.9	1.9	80.0	302.6	545.0	329.5	.2	9.0	39.0	1324.1
TOTAL	67.6	133.9	786.6	4027.6	11061.9	5399.3	304.2	68.4	229.9	22079.4

APPENDIX D

DATES OF HEARINGS AND INSPECTIONS

LIST OF WITNESSES AND OBSERVERS

During the course of the Inquiry, hearings were held as follows:

In public	1 May, 1979	Canberra
	12 February, 1980	Canberra
In camera	8 May, 1979	Canberra

An inspection of Bass Strait facilities was carried out on 24 March, 1980.

The following witnesses were sworn or made an affirmation and were examined by the Committee during the Inquiry:

Mr. L. F. Backen	First Assistant Secretary, Oil and Gas Division, Department of National Development and Energy
Mr. F. J. Doyle	Director (Inland Services) Department of Business and Consumer Affairs
Mr. A. A. Garran	Principal Executive Officer Oil Industry Policy Branch, Department of National Development and Energy
Mr. F. I. Kelly	First Assistant Secretary, Bureau of Customs, Department of Business and Consumer Affairs

The Committee was assisted by the following observers:

Mr. P. Brazil	Attorney-General's Department
Mr. R. Crowle	Public Service Board
Mr. A. Finch	Department of Finance
Mr. F. Ford	Department of Finance
Mr. P. Ford	Department of Finance
Mr. B. W. Fraser	Department of the Treasury
Mr. G. Gibbons	Department of the Treasury
Mr. A. Harris	Department of Finance
Mr. P. Hinchy	Auditor-General's Office
Ms. P. Hicks	Department of Prime Minister and Cabinet
Mr. B. G. McCallum	Public Service Board
Mr. P. Treloar	Auditor-General's Office