

26 February 2020

The Honourable Jackie Trad
Deputy Premier, Treasurer and
Minister for Aboriginal and Torres
Strait Islander Partnerships

Dear Deputy Premier

Queensland Petroleum Royalty Review

I refer to my letter to you dated 24 December 2019, enclosing my first report on the Queensland Petroleum Royalty Review (the Review).

I am pleased to provide you with the **enclosed** second report on the Review, with a focus on evaluation of the Volume Model and the revised Legislated Netback Model. You decided that no further consideration should be given to the Industry Model.

In the second report, I recommend that the Queensland Government:

1. approve the Volume Model for CSG to replace the existing petroleum royalty regime, to commence on 1 July 2020;
2. approve OSR conducting industry consultation on implementation of the Volume Model to commence on 1 March 2020 and conclude by 27 March 2020;
3. approve OSR undertaking further work to develop the Volume Model for non-CSG petroleum (oil, condensate, LPG and natural gas) and report to Government on implementation timeframes by 27 March 2020; and
4. consider providing industry with an undertaking that the Volume Model settings will not change for 5 years from the date of commencement (1 July 2020).

I am available to discuss any aspect of the Review.

Yours sincerely



Jay Weatherill
Chair
Petroleum Royalty Review Working Group

Queensland Petroleum Royalty Review

Second Report by the Hon Jay Weatherill to the Queensland Government

February 2020

Contents

1. Executive Summary	3
2. Background	5
3. Further Submissions	6
4. Alternative petroleum royalty models	7
Revised Legislated Netback Model	7
Advantages of revised Legislated Netback Model	7
Disadvantages of revised Legislated Netback Model	7
Volume Model	8
5. Royalty revenue modelling.....	9
Current arrangements, Volume Model, and revised Legislated Netback Model.....	9
Volume Model and current arrangements	10
Revised Legislated Netback Model (various scenarios) and current arrangements	11
6. Findings.....	12
7. Conclusion	14
8. Recommendations	15
9. Acknowledgements	16
10. Attachments	17

1. Executive Summary

This is my second petroleum royalty review (**Review**) report (**second report**), which should be read in conjunction with my first report dated 24 December 2019, to the Queensland Government (**first report**).

The first report made findings concerning the relative merits of the *Volume Model*¹ and the *Industry Model*². A third model emerged late in the consultation process – the *Legislated Netback Model*³. As the Review Working Group (**Working Group**) had not had the opportunity to consider the Legislated Netback Model I recommended to the Honourable Jackie Trad, Deputy Premier, Treasurer and Minister for Aboriginal and Torres Strait Islander Partnerships (**the Deputy Premier**) that she extend the period of consultation to allow consideration of this model and to allow time for further submissions. The Deputy Premier accepted this recommendation and also decided that no further consideration should be given to the Industry Model.

The Working Group reconvened on 7 February 2020 to consider the Legislated Netback Model.

I advised the Working Group that the Deputy Premier did not propose further considering the Industry Model in its current form for reasons stated under 'Background' below. At the request of the Australian Petroleum Production and Exploration Association (**APPEA**), the Office of State Revenue (**OSR**) undertook further revenue modelling for the Volume Model using actual Liquefied Natural Gas (**LNG**) and domestic gas sales data in addition to previous modelling done using industry benchmark indicators.

The Deputy Premier agreed to a request from APPEA dated 14 February 2020 to extend the Review consultation period until close of business 21 February 2020.

On 23 February 2020, Australia Pacific LNG Pty Limited (**APLNG**) submitted a revised version of the Legislated Netback Model (**revised Legislated Netback Model**). APLNG state that the revised Legislated Netback Model followed ongoing discussions with industry and assert that the majority of industry prefer a legislated netback type model, although support at that time was not unanimous. Further, that industry want the regime to be locked in without amendment for 7 years. At least Santos Limited (**Santos**)/GLNG and Senex Energy Limited (**Senex**) support the Volume Model (with a preference for actual gas sales as an input, rather than industry benchmark indicators).

The Review focus continues to be on the complexities associated with the large LNG projects and options for addressing those complexities, while addressing the other objectives of the Review as set out in the Terms of Reference.

Revised Legislated Netback Model

The revised Legislated Netback Model submitted by APLNG and industry uses a netback methodology, which is a variation to the Legislated Netback Model originally proposed by an industry participant. I note that support for a netback methodology more broadly can be found in a recent Queensland Court of Appeal decision, which found that the netback method adopted by the former Treasurer in making the petroleum royalty decision (**PRD**) for the APLNG project is capable of determining royalty payable on gas used in that project.⁴

While the revised Legislated Netback Model reduces some of the uncertainties of the current regime regarding allowable deductions and related party transactions for the LNG projects (through subtracting fixed dollar per gigajoule (**GJ**) deductions from actual LNG sales revenue), it still suffers from being inequitable because the fixed deductions would have different impacts on petroleum producers and LNG projects depending on their capital investment decisions and the efficiency of their operations. Given the market strength and influence of the LNG projects, relative to the domestic petroleum producers, the fixed deductions would need to be set at levels that do not disadvantage domestic petroleum producers

¹ First report, 12-16

² Ibid, 16-20

³ Ibid, 21

⁴ *Australia Pacific LNG Pty Limited & Ors v The Treasurer, Minister for Aboriginal and Torres Strait Islander Partnerships and Minister for Sport* [2020] QCA 15

through a relatively lower fixed deduction between the wellhead and first point of disposal and relatively higher fixed deduction between the first point of disposal and the LNG sales point. Also, it is uncertain how domestic related party sales are to be treated under the revised Legislated Netback Model in circumstances where they may not have the equivalent of an arm's length LNG sales price from which to subtract the downstream fixed deduction.

While APLNG assert that the revised Legislated Netback Model would achieve the Government's expectations of royalty revenue over the four years modelled, royalty revenue outcomes beyond 2023 would be significantly less than under the current arrangements and the Volume Model primarily because of the impacts from the LNG projects upstream infrastructure being substantially depreciated beyond the four years modelled, noting industry want the regime to be locked in without amendment for 7 years. This would require downward adjustments to the fixed deductions proposed under the revised Legislated Netback Model.

Volume Model

As stated in my first report, the principal benefit of the Volume Model is its simplicity. The asserted deficit is that it does not reflect actual sales and costs, and therefore arguably may discourage investment in marginal gas fields. However, the industry proposed revised Legislated Netback Model would have a similar deficit by using fixed deductions rather actual costs as deductions, particularly for efficient lower cost petroleum producers and projects. I note that further work is being done by OSR to determine whether the Volume Model could accommodate the industry preferred use of actual sales revenue rather than the industry benchmark indicators.

The Volume Model does not have the complexities and uncertainties of the revised Legislated Netback Model in relation to the inequity associated with fixed deductions and the uncertainty regarding domestic related party transactions. The Volume Model simply applies industry benchmark indicators (and as stated above, potentially actual sales revenue) to determine a rate which is applied to the volume of CSG at the first reliable point of measurement, reconciled back to the wellhead. OSR also propose a tiered rate regime, which supports petroleum producers in times of relatively low gas prices and provides the State with higher royalties in times of relatively high gas prices.⁵

Conclusions

APLNG assert that the majority of industry prefer the revised Legislated Netback Model. At least Santos/GLNG and Senex prefer the Volume Model. Despite the efforts of industry, they were unable to reach consensus on a preferred model. It is unlikely that providing more time to consider the models would achieve industry consensus.

While the revised Legislated Netback Model would be an improvement on the existing petroleum royalty regime, the Volume Model is more likely to achieve the objectives of the Review as stated in the Terms of Reference and is therefore the model I recommend to Government.

It would be reasonable for the Government to consider providing industry with an undertaking that the Volume Model settings will not change for 5 years from the date of implementation to provide the certainty they are seeking (noting industry initially sought an undertaking for 10 years and subsequently for 7 years).

While there are likely to be implementation and transitional issues with the Volume Model, these should be able to be resolved during implementation consultation.

⁵ First report, 14

2. Background

On 24 December 2019, I provided the first report to the Queensland Government recommending that:

1. approval be given for the Working Group continuing to evaluate the three following models and conclude such evaluation by 12 February 2020.
 - Volume Model
 - Industry Model
 - Legislated Netback Model;
2. a new petroleum royalty model be recommended for approval by 12 February 2020;
3. the Queensland Government approve a new petroleum royalty model on or before 28 February 2020; and
4. final industry consultation on the implementation of the approved new petroleum royalty model commence on 1 March 2020 and conclude no later than 27 March 2020.⁶

The Deputy Premier accepted the recommendations in my report.

On 7 February 2020 the Working Group reconvened to consider the Legislated Netback Model given it emerged late in the Review consultation process (20 December 2019) and the Working Group not having the opportunity to consider it before my first report was submitted on 24 December 2019.

I advised the Working Group that the Deputy Premier did not propose further considering the Industry Model in its then current form for the following reasons.

- Principally because the Industry Model does not achieve the objectives of the Review as set out in the Terms of Reference (being greater certainty, equity and simplicity for all parties and an appropriate return to Queenslanders for their non-renewable resources).
- Whilst the Industry Model reduces some of the uncertainties of the current regime regarding allowable deductions, even with reasonable adjustments, it still leaves unresolved some of the significant matters concerning related party transactions – for example, all three LNG projects would need to agree on an appropriate rate of return on the different amounts of capital expenditure they have incurred for their projects, and then agree such with Government.

At the request of APPEA, OSR undertook further modelling of the Volume Model using actual LNG and domestic sales data in addition to previous modelling done using industry based benchmark indicators (see under 'Royalty revenue modelling').

The Deputy Premier agreed to a request from APPEA dated 14 February 2020 to extend the Review consultation period until close of business 21 February 2020.

Attachment 1 is a summary of the meetings conducted for the Review since the first report.

Attachment 2 is a timeline of the Review key events since the first report.

⁶ First report, 33

3. Further Submissions

Following is a list of the submissions received during the extended Review consultation period. A summary of each submission and copies of the submissions are included at **Attachment 3**.

- a. ██████████, dated 12 February 2020
- b. Senex Energy Limited, dated 12 February 2020
- c. ██████████, dated 13 February 2020
- d. Tri-Star Group, dated 20 February 2020
- e. Australia Pacific LNG Pty Limited, dated 20 February 2020
- f. Australia Pacific LNG Pty Limited, dated 22 February 2020
- g. Santos Limited, dated 22 February 2020

4. Alternative petroleum royalty models

Revised Legislated Netback Model

On 22 February 2020, APLNG submitted the revised Legislated Netback Model. APLNG state that the revised Legislated Netback Model followed ongoing discussions with industry with the majority of industry preferring a legislated netback type model, although support at that time was not unanimous. At least Santos/GLNG and Senex do not support the revised Legislated Netback Model, preferring the Volume Model using actual LNG sales, rather than industry benchmark indicators as proposed by OSR.

Following are the design principles of the revised Legislated Netback Model.

- The same model should be applicable to domestic gas and integrated LNG projects.
- Royalty will remain payable at 12.5% of the wellhead value.
- LNG feed gas revenues will be determined using actual LNG sales revenues, adjusted by a fixed A\$/GJ **midstream** processing deduction for each GJ sold as LNG. [For the purposes of this report, industry refer to the 'midstream' as that part of the CSG-LNG value chain between the first point of disposal of gas (typically the exit to the upstream gas processing facilities) and the LNG sale.]
- Domestic gas revenues will be determined using actual domestic sales revenues.
- A fixed A\$/GJ upstream processing deduction will be applied against each GJ of gas sold (as domestic gas or LNG feed gas) to represent all upstream deductions. This will be indexed annually by the Consumer Price Index (**CPI**) (Note: For small producers Government should consider a higher fixed deduction to encourage additional development. For example, if their gas production falls under a threshold, then you can apply to have actual expenses deducted above the mandatory netback level).
- Flared and used gas volumes across the value chain are not subject to royalty.
- The regime will be locked in without amendment for 7 years.

Advantages of revised Legislated Netback Model

- It is asserted by industry to provide greater certainty than the current regime for petroleum producers and the State (e.g. fixed tariffs in place of statutory deductions, and pipeline and liquefaction costs).
- Levers within the model could be adjusted to provide an appropriate return for Queenslanders for their valuable non-renewable resources (e.g. tariffs and royalty rate).
- Administratively simpler than current petroleum royalty regime and removes some of its complexities (e.g. the need for some PRDs).
- The majority of industry prefer the calculation of petroleum royalty to be based on the actual sales revenue.
- Netback models are used in other jurisdictions.

Disadvantages of revised Legislated Netback Model

- While gas valuation issues are dealt with for CSG used as LNG feedstock, through subtracting from arm's length LNG sales the fixed deductions, valuation issues would remain in circumstances where a petroleum producer disposes of gas to a related party e.g. a petroleum producer sells gas to a related party power station. Therefore, a published valuation method and/or PRD may be required for these types of non-arm's length transactions.
- The revised Legislated Netback Model contemplates allowing actual expenses to be deducted where they exceed the fixed deductions/mandatory netback level, if gas production falls below a threshold

(unspecified). The submission proposing the revised Legislated Netback Model did not specify the scope of the actual expenses that would be allowed as deductions. If there is no change to the current legislated regime for deductions, concerns raised during the Review regarding deductions would remain.

- The process required to consider applications made by petroleum producers to allow any actual expenses would add to the complexities of the existing regime e.g. petroleum producers would have to provide OSR with all actual expenses and justify those expenses that are above the mandatory netback level. In addition, if they are related party transactions then a PRD may be required.
- While appropriate fixed deductions (tariffs and tolls), and any review mechanism, would need to be discussed as part of the implementation consultation process, the fixed deductions would still need to be considered and determined by Government which may create a potential area of dispute.
- The legislation would necessarily obligate entities that are not petroleum producers and do not have a royalty liability to disclose certain information to petroleum producers (e.g. an LNG marketer, who may be a separate but related entity, would have to provide details of their sales revenue to the petroleum producer, as sales revenue figures would be required for royalty calculation purposes). Such disclosure may not be acceptable to an entity who is required to keep its sales revenue confidential and is problematic in cases where multiple consents for the disclosure are required from joint venture partners.
- Fixed tariffs, as opposed to actual costs, would disadvantage petroleum producers and LNG projects with lower capital and operating costs.
- It is uncertain what would be defined as a 'related party' and an 'arm's length sale' for the purposes of the revised Legislated Netback Model.
- It is proposed that the CPI apply to the fixed upstream processing deduction, but not the fixed midstream deduction. Applying a consumer index to petroleum production costs is not considered appropriate, in particular, for costs related to depreciation of capital.

Volume Model

Since my first report, OSR has undertaken further work to refine the Volume Model, including consultation with technical gas field experts to confirm the practical application of the model.

In OSR's consultation paper⁷ circulated to industry late 2019 they proposed a single rate apply to the volume of gas destined for both export and domestic markets. In my first report, OSR considered the alternative of applying two prescribed rates – one rate for CSG to be converted to LNG for export and another rate for CSG destined for the domestic market. OSR noted that further consideration of the basis of the rate or rates would be required following more detailed work on the model. Consequently, OSR propose the original single rate approach as set out in their industry consultation paper. I note APPEA's support for not having two rates applying to CSG. At the request of APPEA during the Working Group meeting on 7 February 2020, OSR undertook further revenue modelling for the Volume Model using actual LNG and domestic sales data, rather than the industry benchmark indicators. That modelling can be found in the following 'Royalty revenue modelling' section. As stated in the 'Executive Summary' further work is being done by OSR to determine whether the Volume Model could accommodate actual sales revenue.

Otherwise, the Volume Model and its inputs are as set out in my first report.

⁷ Queensland Treasury – Office of State Revenue, Petroleum Royalty Review Consultation on Volume Model, 21 November 2019, 10-11

5. Royalty revenue modelling

This section provides brief analysis and modelling of the indicative royalty revenue outcomes under the Volume Model and revised Legislated Netback Model compared with the arrangements under the current royalty regime (**the current arrangements**).

As with the royalty revenue modelling in the first report,⁸ the figures and charts in this section are for 'indicative' purposes only and should not be relied upon as representing estimated or actual royalty revenue outcomes for the Volume Model or revised Legislated Netback Model.

Current arrangements, Volume Model, and revised Legislated Netback Model

Chart 1: Comparison of petroleum royalty under the current arrangements, Volume Model and revised Legislated Netback Model

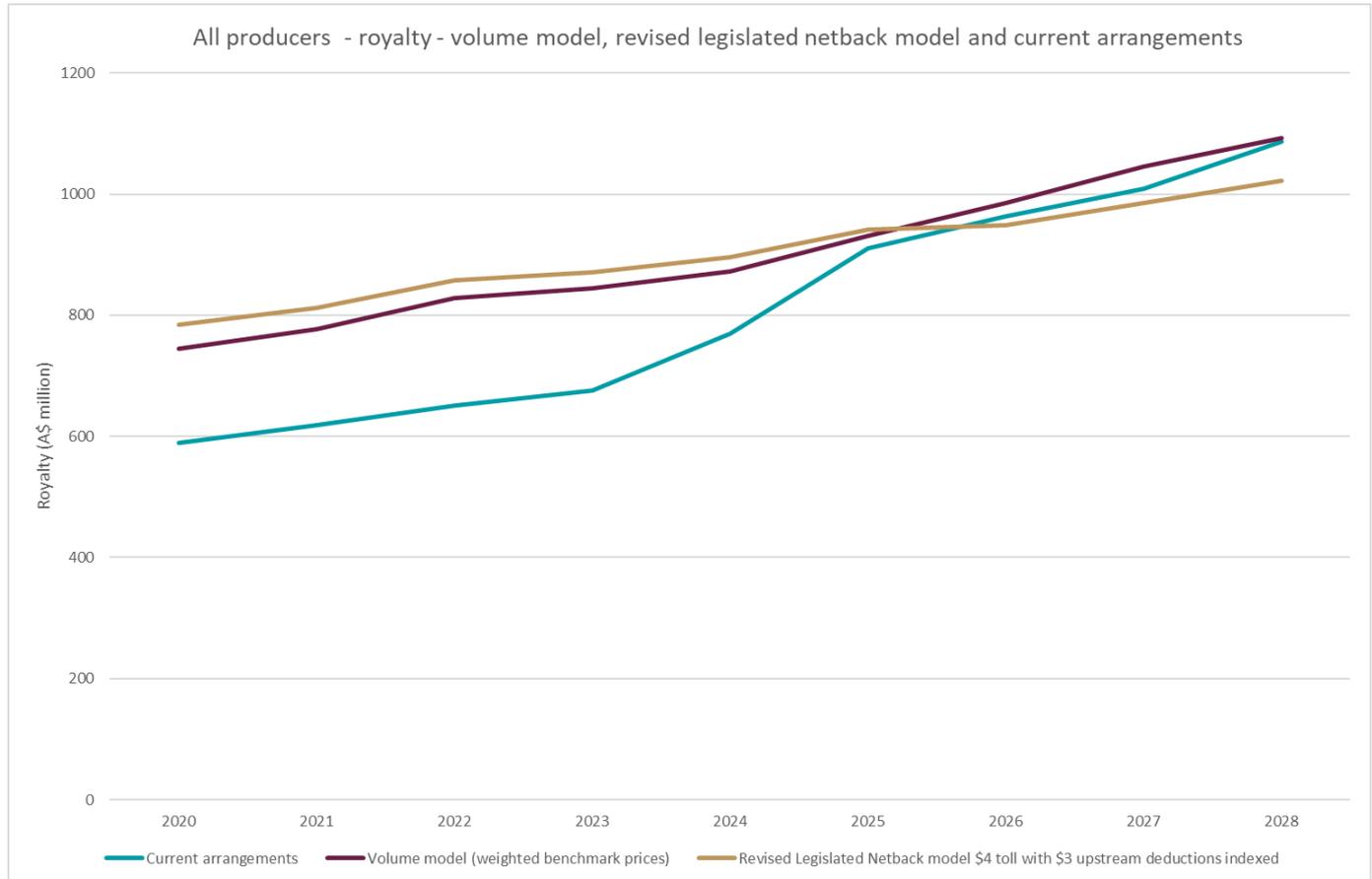


Chart 1 shows petroleum royalty over the nine-year period to 2028 under the current arrangements, Volume Model and the revised Legislated Netback Model.⁹ Assumptions for the revised Legislated Netback Model include a midstream toll of \$4/GJ and upstream fixed deduction of \$3/GJ indexed by 2% per annum. The chart shows that petroleum royalty under all three models follows an upward trend over the nine-year period to 2028. This is driven by an assumption that the Brent oil prices will increase over that period.¹⁰

Under the scenarios shown for the revised Legislated Netback Model and the Volume Model,¹¹ total petroleum royalty is similar for the nine-year period. Petroleum royalty under the revised Legislated

⁸ First report, 22-26

⁹ The modelling of the revised Legislated Netback Model is based on, where applicable, data provided by representatives from the three major LNG projects to assist modelling the Industry Model and Volume Model. For all smaller petroleum producers, OSR has input forecasted values based on data available through petroleum producer estimates to 2023. Where petroleum producer estimates do not capture elements of the revised Legislated Netback Model, such as for years post 2023, OSR has assumed values based on information available at the time of writing

¹⁰ As modelling was performed in collaboration with the three LNG projects, the results reflect their data and assumptions and may not align with Queensland Treasury's assumptions. In particular, [REDACTED]

¹¹ The results are specific to the scenarios modelled and data assumptions, and therefore are indicative only

Netback Model shows a flatter trend than royalty under the Volume Model, which mostly reflects the indexation of deductions in the revised Legislated Netback Model.¹²

Volume Model and current arrangements

Chart 2: Comparison of petroleum royalty under the current arrangements and under the Volume Model – benchmark vs actual sales

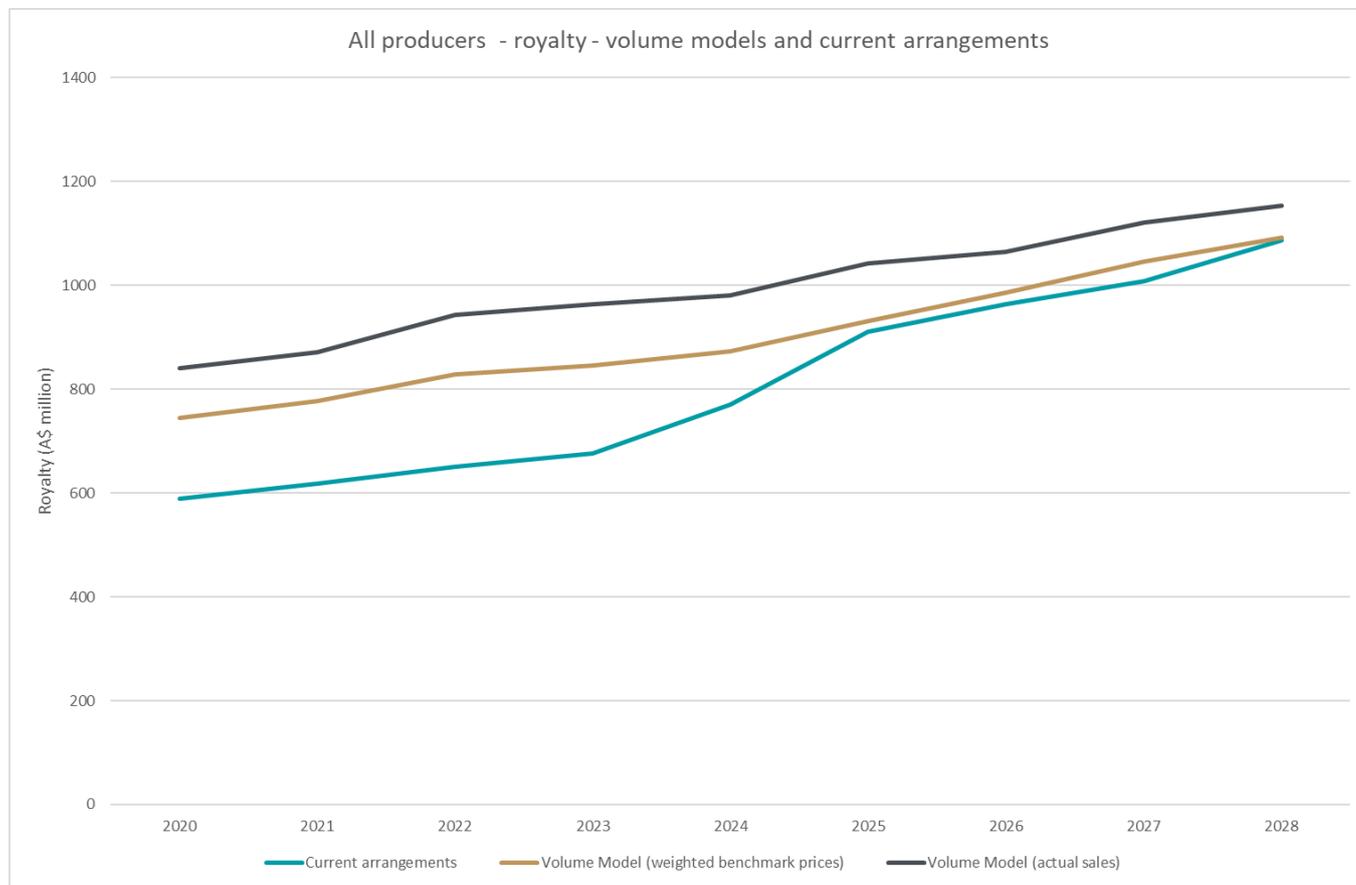


Chart 2 shows a Volume Model option which uses actual sales (LNG and domestic sales) as inputs for the benchmark, rather than a calculated benchmark based on specified industry indicators, such as the Brent oil prices. Petroleum royalty under the actual sales option is estimated to be on average \$95 million per annum higher than under the Volume Model using the calculated benchmark. This reflects that OSR assumed a relatively conservative LNG to oil price slope i.e. 13.5% as an indicative input for the Volume Model. A similar petroleum royalty revenue outcome under the calculated benchmark option could be achieved as under the actual sales price option through adjustments to the royalty rates and tiers.

¹² A similar type of result could be achieved under different versions of the Volume Model

Chart 3: Comparison of petroleum royalty under the revised Legislated Netback Model scenario analysis and current arrangements

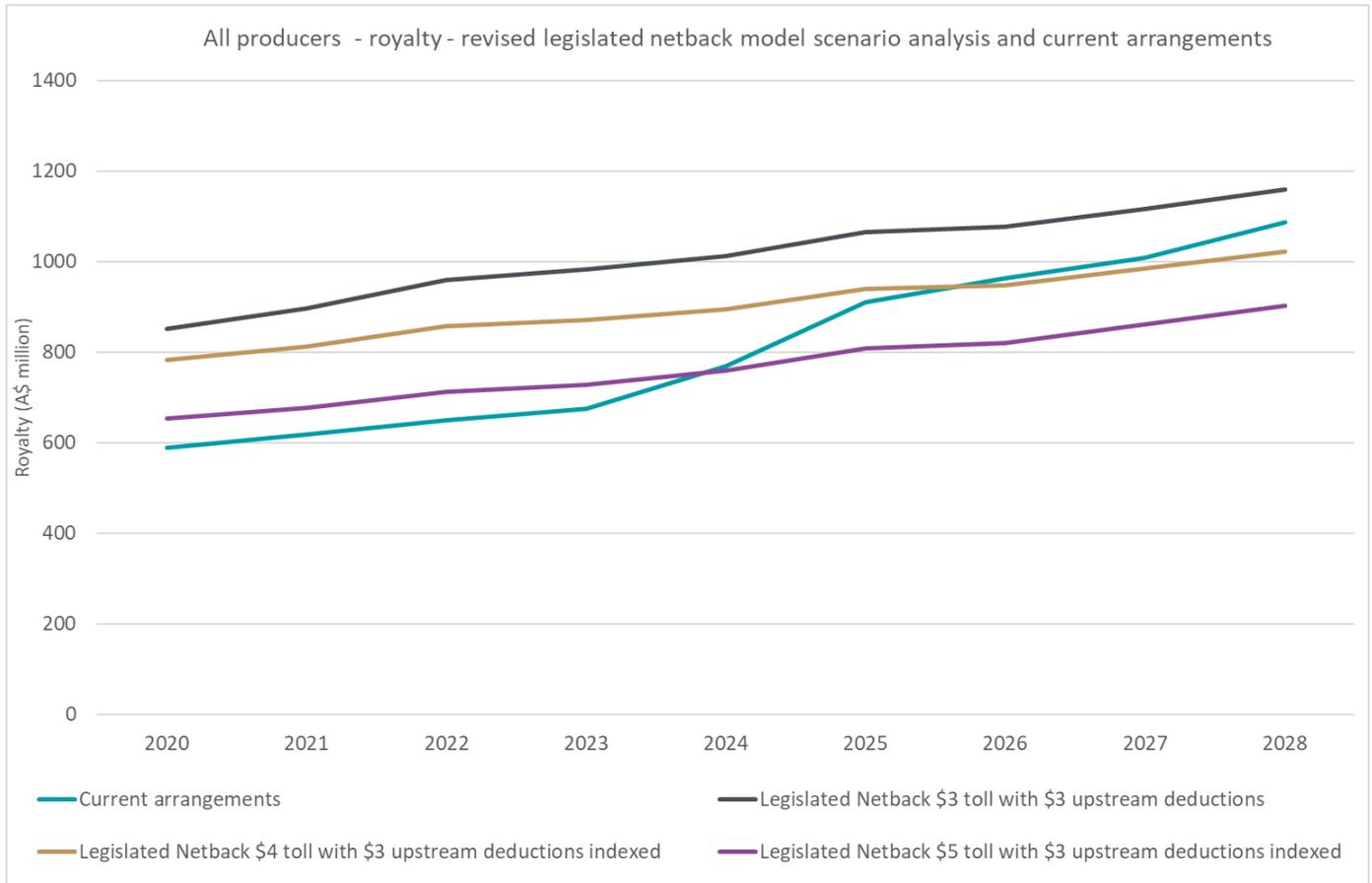


Chart 3 models three scenarios for the revised Legislated Netback Model using different tolls/fixed deductions, together with the current arrangements. The three scenarios have similar trends. Using the scenario which is closest to the current arrangements up to 2024 as an example, shows that royalty under the revised Legislated Netback Model with a midstream \$5 toll and \$3 fixed upstream deductions (indexed at 2%) is higher than royalty under current arrangements until 2023. However, from approximately 2024 onwards, royalty under the revised Legislated Netback Model is significantly lower than under the current arrangements. This is because under the revised Legislated Netback Model deductions are fixed (except for relatively small CPI increases) and capital depreciation being claimed as a statutory deduction over a 10-year period not being reflected in the revised Legislated Netback Model (but is included in the current arrangements). In 2028, petroleum royalty under the revised Legislated Netback Model is estimated to be \$184 million lower than under current arrangements.

6. Findings

As with the Volume Model, the principles of the revised Legislated Netback Model allow calibration in a way that could deliver an appropriate return to Queenslanders for their valuable non-renewable resources. The return to Queenslanders under the revised Legislated Netback Model would depend on the levels at which fixed deductions are set.

The revised Legislated Netback Model proposes that industry pays no royalty for the gas it loses or uses across its value chain, including flared and vented gas. I note that under the current petroleum royalty regime up to 3,000,000 cubic metres of flared or vented gas per wellhead is exempt from royalty. While a certain amount of flaring and venting of gas is necessary for safety reasons, the gas has a value which is owned by the State and arguably should be subject to royalty.¹³ I refer to my comments in the first report regarding the Volume Model being capable of being modified to appropriately deal with this issue.

As stated above under 'Executive Summary', while APLNG assert that the revised Legislated Netback Model would achieve the Government's expectations of royalty revenue over the four years modelled, royalty revenue outcomes beyond 2023 would be significantly less than under the current arrangements and the Volume Model because of the impacts from the LNG projects upstream infrastructure being substantially depreciated beyond the four years modelled, noting industry want the regime to be locked in without amendment for 7 years. This would require downward adjustments to the fixed deductions proposed under the revised Legislated Netback Model.

The first report concluded that the present royalty regime is not suitable for the existing configuration of the Queensland gas industry and that it should be replaced with a simpler model less capable of generating disputes.¹⁴ This remains the imperative.

The revised Legislated Netback Model would introduce fixed deductions for the midstream. Under the model, if gas production for small producers falls under a threshold, an application can be made by the producer to have actual expenses deducted above the mandatory netback level. The submission proposing the revised Legislated Netback Model did not specify the scope of the actual expenses that would be allowed as deductions. Therefore, the concerns raised during the Review regarding deductions would remain under the revised Legislated Netback Model.

The revised Legislated Netback Model reduces the scope of the dispute around valuation but does not eliminate the issue. PRDs would still be required for transactions between related parties where there is no arm's-length sale.

Royalty administration would be simpler under the revised Legislated Netback Model compared with the existing arrangements. Further, compliance costs would be reduced for both industry and the Government. Compliance activities would be required to ensure correct application of the model.

A legislated netback model appears to be used in some other jurisdictions.

The revised Legislated Netback Model does not address domestic supply. But the Review has already found a better approach would be to consider measures to address this concern directly, outside of the royalty settings.¹⁵

If the revised Legislated Netback Model was the Government's preferred model, implementation consultation would be required to establish whether a 1 July 2020 commencement was possible, as well as the ease of drafting and timing of amending legislation and assessment of the system updates required.

The revised Legislated Netback Model would be transparent but would disadvantage efficient low cost petroleum producers.

¹³ n 4, 15-16 [62]

¹⁴ First report, 32

¹⁵ bid, 31

I note in passing that OSR's royalty administration modernisation program will deliver positive changes in royalty administration (such as external merit review rights).

APLNG asserts that the Volume Model is 'disadvantageous to higher-cost resource extraction and acts as a disincentive to development and exploration for any producers and fields that face a higher marginal cost of production' and that 'this will likely defer development for many years permanently impacting investment, jobs, and reducing gas production'.¹⁶ Santos and GLNG do not support APLNG's submission and are of the view that the Volume Model 'is capable of delivering both acceptable financial and investment outcomes for industry'.¹⁷ In the first report I found that the Volume Model had more industry development risks than the Industry Model, but also that an industry development advantage of the Volume Model is that it is more likely to reward efficient low cost producers, who are best able to develop marginal fields including fields which may be presently locked up by less efficient producers.¹⁸ However, this point must be weighed against the difficulty of other producers gaining access to locked up wells especially those connected to proprietary infrastructure. Industry's continuous improvements in CSG exploration and development, through technology and experience, should further assist in the identification and development of what might otherwise be marginal gas fields. To the extent that there may be a need to incentivise the development of marginal gas fields, that should be considered by the Government separate to the petroleum royalty policy settings and administration.

The level of industry support for one model or another is a relevant factor I have taken into account. While the majority of producers support the revised Legislated Netback Model significant producers support the Volume Model. Despite the best efforts of the industry bodies Queensland Resource Council (**QRC**) and APPEA and latterly the substantial efforts of Mr Warwick King from APLNG, industry alignment behind one model was not forthcoming.

As stated in my first report, the principal benefit of the Volume Model is its simplicity. The asserted deficit is that it does not reflect actual sales and costs, and therefore arguably may discourage investment in marginal gas fields, although I note this assertion has been challenged by some producers and has not been supported by any corroborating evidence. Also, OSR is undertaking further work to determine whether the Volume Model could accommodate the industry preferred use of actual sales revenue as an input to the model rather than industry benchmark indicators.

The Volume Model overcomes the remaining uncertainties associated with the revised Legislated Netback Model. The Volume Model simply applies industry benchmark indicators (or actual sales revenue) to determine a rate which is applied to the volume of CSG at the first reliable point of measurement, reconciled back to the wellhead. OSR also propose a tiered rate regime, which supports petroleum producers in times of relatively low gas prices and provides the State with higher royalties in times of relatively high gas prices.¹⁹

While there were no adverse legal or constitutional issues pressed during the Review with either the revised Legislated Netback Model or the Volume Model, I have left it to industry and the Government to seek their own advice on any such issues.

¹⁶ APLNG submission, 22 February 2020, 2

¹⁷ Santos submission, 22 February 2020, 1

¹⁸ First report, 30

¹⁹ bid, 14

7. Conclusion

I therefore conclude that the preferred new petroleum royalty regime should be the Volume Model.

I have not concluded that there is a basis for a differential rate for LNG and domestic producers given the difficulty of implementation. However, the design features of the Volume Model with its tiered benchmark price should benefit smaller domestic producers, particularly if actual sales are used as an input to the Volume Model.

There will be substantial implementation issues including the finalisation of benchmark rates and the levels at which tiers are set, the treatment of non-CSG petroleum products, the appropriate treatment of flared, vented gas and own use gas (e.g. gas used in the upstream gas processing facilities), and transitional issues including the special circumstances of producers who have constructed their contractual arrangements based on the current netback methodology. These issues will require intensive industry engagement, which should commence immediately if and when the Government decides to adopt the new royalty regime.

Given industry concerns that the Government could more easily alter the royalty rate by simply altering the less familiar Volume Model benchmark settings, and while the Government has expressed no intention to do so, I have nevertheless reached the conclusion that industry is entitled to an extended period of certainty. Industry asked for 10 years and then more recently 7 years. I believe 5 years of fixing the Volume Model benchmark settings is reasonable.

8. Recommendations

I therefore recommend that the Government:

1. approve the Volume Model for CSG to replace the existing petroleum royalty regime, to commence on 1 July 2020;
2. approve OSR conducting industry consultation on implementation of the Volume Model to commence on 1 March 2020 and conclude by 27 March 2020;
3. approve OSR undertaking further work to develop the Volume Model for non-CSG petroleum (oil, condensate, LPG and natural gas) and report to Government on implementation timeframes by 27 March 2020; and
4. consider providing industry with an undertaking that the Volume Model settings will not change for 5 years from the date of commencement (1 July 2020).

9. Acknowledgements

I would like to thank the Queensland Government for the opportunity to Chair the Review. I believe the Review has achieved the objectives set out in its Terms of Reference and can only serve to benefit all Queenslanders.

I would like to acknowledge and thank the members of the Working Group and the Technical Sub-Group for their advice and support during the Review process. In particular, Mr Andrew McConville, APPEA, Mr Ian Macfarlane, QRC and Mr Simon McKee, OSR.

A special thanks to the Review Secretariat – Mr Daniel Fielding, Ms Van Pham, Ms Martina McMahon, Ms Wing Poon and Ms Nicole Matrippolito. I always found these people to be professional and responsive.

I also acknowledge the many people and companies who contributed to the Review through making themselves available, often at short notice, to meet with me and share their expertise and views, and for their submissions.

While the Review outcomes may not satisfy the varied interests of all stakeholders, the process has benefited greatly from their contributions.

10. Attachments

Attachment No.	Document
1	Petroleum Royalty Review – Summary of Meetings
2	Petroleum Royalty Review – Timeline (continued from the first report timeline – i.e. from 24 December 2019)
3	Petroleum Royalty Review – Summary of Submissions
3a	██████████ submission dated 12 February 2020
3b	Senex Energy Limited submission dated 12 February 2020
3c	██████████ submission dated 13 February 2020
3d	Tri-Star Group submission dated 20 February 2020
3e	Australia Pacific LNG Pty Limited submission dated 20 February 2020
3f	Australia Pacific LNG Pty Limited submission dated 22 February 2020
3g	Santos Limited submission dated 22 February 2020