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REVIEW OF THE PETROLEUM RESOURCE RENT TAX (PRRT) GAS TRANSFER PRICING ARRANGEMENTS

Introduction

We welcome the Australian Government's ongoing consultation with industry and the community on this issue and are pleased to provide a response to The Treasury's current consultation paper: "Review of the PRRT Gas Transfer Pricing arrangements."

This is BHP's third submission on the PRRT in recent years – we have previously submitted to the Callaghan Review and the Treasury's consultation paper in 2017: "Options to address the design issues identified in the Petroleum Resources Rent Tax Review."

BHP has paid more PRRT than any other company in Australia, funding more than A$12.2 billion in PRRT since 2000.

The design of the PRRT is that it taxes profits ('economic rents'), rather than value or volumes. Profits occur only after the licensed producer has made a return in excess of the capital costs of development. When such profits are made, the PRRT provides an equitable share of the returns from the development of petroleum resources between the beneficiaries: the Commonwealth (the Australian people) and the licensed producer.

In previous submissions, we have pointed to the significant benefit the PRRT has provided to the Australian community, not just in terms of the amount of PRRT paid, but also, company tax, resulting in an effective tax and royalty rate of over 55 per cent. Additionally, BHP also contributes excise and production based royalties.

BHP believes that the PRRT allows the community to equitably share in the benefit of investment in profitable projects over time (including during peak cycles).

In an environment of increasing costs and regulatory burden, the current PRRT regime has helped to attract capital investment in developing Australia's oil and gas industry. Critically, the next wave of investment in this industry in Australia requires a commitment to invest in developing offshore resources using and/or expanding existing processing infrastructure.

As reiterated in our previous submissions and engagement with the Australian Government on the PRRT over a number of years, BHP remains of the view that the current PRRT regime, including the gas transfer pricing rules, achieve their intended purpose.

Potential impact on BHP investment decisions

The design and stability of the PRRT has had a positive influence in stimulating large scale investment in the Australian oil and gas industry, whilst also providing significant benefits to the Australian community (including through job creation, company income tax payments and PRRT payments).

At BHP, there is fierce competition for capital globally and we employ a disciplined approach, via our Capital Allocation Framework, to transparently direct cash to its best use (Investments, the Balance Sheet or returns to shareholders). Any increase in projected tax outlays under the PRRT will detract from the attractiveness of investing in projects like the Scarborough natural gas field offshore Western Australia.

BHP has provided detail on the Scarborough Project in our submission to the Callaghan review and would welcome the opportunity to further discuss how changes in the gas transfer pricing rules could impact the viability of this development opportunity.

Review of the gas transfer pricing rules

As BHP submitted back in 2017, we welcome the opportunity to review the operation of the gas transfer pricing rules to ensure the rules are operating appropriately and achieve their intended purpose. It is in that spirit we provide our current submission.

However, our position has not changed since 2017. Each gas to liquid project has unique geographical, logistical and engineering challenges requiring bespoke process design. It follows that the extent of integration of upstream and downstream operations is a commercial decision. The existing gas transfer pricing arrangements, featuring a residual price methodology, remain an appropriate basis for determining the amount of assessable petroleum receipts for gas used to produce saleable liquids from an integrated gas to liquid operation.

BHP supports the Australian Petroleum Production and Exploration Association's (APPEA's) submission in response to the current consultation paper. Further comments on specific issues raised in the Treasury Consultation Paper are also included in the Appendix.

Our commitment to transparency

The Callaghan Review recommended that the current gas transfer pricing arrangements "be examined to identify changes that would achieve greater simplicity and transparency, ease of compliance and fair treatment of the economic rent from each stage of a petroleum operation."

BHP shares this commitment to tax transparency and reiterates its willingness to work with Treasury, and the Australian Taxation Office (ATO), to continue to improve transparency on the administration of the PRRT system.

Conclusion

BHP believes that the current gas transfer pricing arrangements remain ‘fit for purpose’.

BHP encourages Treasury to consider the critical importance of stable fiscal settings to any new investment decisions – particularly at a time when industry participants are making decisions that will shape the next wave of investment in Australian gas projects.

We look forward to discussing our submission with you in person.

Yours sincerely

Peter Beaven

Chief Financial Officer

Appendix

We provide further comment below on some specific issues raised in your consultation paper.

- **The potential use of comparable prices to determine the gas 'transfer price'**

  The Treasury Consultation paper seeks comment on how a comparable uncontrolled price (CUP) could be 'modified' to apply to feedstock gas.

  The significant challenges associated with finding and applying CUP's has been considered in more detail in the APPEA submission.

  The use of a CUP would require unique definitional modifications (bespoke to PRRT), departing from established OECD principles. It would also result in additional complexity and uncertainty which can deter investment and increase compliance costs.

- **Applying the current gas transfer pricing arrangements to infrastructure sharing arrangements**

  In our view, the fundamental design of the current gas transfer pricing arrangements will broadly accommodate new tolling and third party processing arrangements.

  Specifically, the residual pricing methodology (as it stands) can be applied to third party gas processing arrangements, but would benefit from clarification in some areas. These areas have been considered further in the APPEA submission.

- **The residual price methodology (RPM)**

  The gas transfer price regulations have been well designed following extensive consultation. The current provisions are generally well understood by industry and regulators alike.

  The RPM is a mechanism that removes uncertainty attaching to the question of how you determine the market value of gas in an integrated gas to liquid project.

  Under the RPM, the residual profit split method operates to equitably 'share' residual profits in an integrated LNG project – and reflects the risks inherent in both the upstream and downstream phase of a project.

  The RPM follows a prescriptive design – focussed on the project's capital and operating costs. This prescriptive design removes ambiguity and therefore, non-compliance risk. This is important in the context of certainty on tax cash flows.

  As a matter of principle, only project profits attributable to the upstream operations of a gas to liquid processing operation should be captured within the PRRT – given that the intention of the PRRT is to only capture resource rents in connection with the initial processing of sales gas. Other valuation approaches do not necessarily achieve this outcome alone. We believe the RPM achieves this.

Whilst other valuation approaches are available, the Callaghan Report made a very important observation in relation to the use of a simple 'netback method' for use in valuing gas:

"…changing the RPM to rely on the netback price only (thereby allocating all project profits to the upstream) would mean that project risks are no longer equitably reflected on all costs centres. The result would be that any rents attributable to the downstream would be captured in the upstream and subject to PRRT."[1]

- **Any changes should have genuine prospective application to wholly new projects**

  BHP remains of the view that any change should have genuine prospective application.

  That is, any change should apply to new production licences issued after the completion of this review.

[1] Refer p92 Callaghan Report