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23 July 2020

Dear Committee Secretary

Queensland State Royalties - Royalty Legislation Amendment Bill 2020

Shell QGC welcomes the opportunity to provide input into the review of the *Royalty Legislation Amendment Bill 2020* by the Economics and Governance Committee.

QGC was first established in Queensland in 2000 to explore and develop Queensland's resources of natural gas in coal seams. Since this time, QGC has emerged as a leading Australian natural gas explorer and producer, developing and operating the world's first project to liquefy natural gas from coal seams, and establishing itself as a reliable energy supplier of gas to both domestic and international markets.

Consultation process

Shell QGC would like to acknowledge Treasury for their engagement with industry, and for addressing some of the key administrative concerns as part of the Bill, including the removal of mandatory information sharing requirements and the removal of a GST-inclusive reference price. Shell QGC will continue engagement with the Queensland Office of State Revenue in framing administrative guidance on the application of the announced provisions to provide certainty and clarity to Petroleum Producers on key outstanding issues, including: the application of benchmarks rates; defining 'LNG Projects'; valuing swapped volumes; and measuring production volumes.

Volumetric based royalty model

Shell QGC recognises the importance of providing a fair and reasonable return to Queensland for the resources extracted by the petroleum industry, and the importance of an efficient and equitable regime in which royalty is administered. In this regard, as expressed throughout the consultation process, Shell QGC retains concerns as to the appropriateness of the Volumetric Model, as the model is not believed to be a long-term sustainable royalty model that will meet the objectives as set out in the initial Royalty Regime Review Terms of Reference. The Volumetric Model does not recognise the costs of bringing gas to the market, and therefore will disincentivise the development of more complex or higher cost gas reserves. This will ultimately limit longer term gas supply from Queensland that will put upward pressure on gas prices in the future for LNG producers and domestic gas users, including manufacturers.

Furthermore, a Volumetric model is inconsistent with international best practice. This view is supported by Professor Andrew J Garnett of the UQ Centre for Natural Gas's submission to the Weatherill Working Group stating that "from the perspective of resource-owner benefits, such a "volume model" is suggested to be amongst the worst", and "… best practice in this area, according to the World Bank, many academic authors and similar resource-rich jurisdictions is to consider royalty settings in a long term and wider policy context and to base resource taxes and royalties on "economic-rent" (revenue minus costs)."[1]

Shell QGC maintains that an efficient and effective royalty regime should be based upon the true wellhead value of the petroleum. The value on which royalty is paid should be determined by reference to the reasonable costs incurred in extracting the gas and the actual revenues derived – to determine otherwise will distort commercial outcomes and result in inequality across the industry.

Retrospective impact on investment decisions

The introduction of the proposed volumetric model will retrospectively change the long-established royalty model under which significant investment commitments in Queensland have been made by the industry. Stable regulatory regimes are vital to investment decisions. Shell QGC sought and obtained an upfront agreement as to the appropriate calculation of gas royalties for LNG feedgas prior to committing to over $20 billion of investments in the QGC LNG Project in 2010. This change now comes around 6 years into a project that expects to operate for over 20 years.

LNG Benchmark rate

The legislation provides for a static reference point of 13.5% of the daily Europe Brent price as the LNG Benchmark price. Shell QGC submits that the Benchmark price should not be defined in the legislation, but rather be defined by an appropriate independent and transparent benchmark to ensure that the Benchmark price will reflect the dynamic LNG market conditions. In this regard we note that the ACCC uses the Japan Korea Marker (JKM) as assessed daily by S&P Global Platts (Platts) as an independent and transparent benchmark of Asian LNG prices for determining its netback series.

Lodgement period

The legislation seeks to remove the current requirement for lodging Annual reconciliation returns – these returns have historically allowed Petroleum Producers three months post year end to reconcile balances and ensure values are final and complete. Whilst we welcome the removal of an administrative compliance process, this change will increase the importance of the quarterly return, which will become a final return. This has not been reflected in the time allowed to prepare and lodge the returns, as these remain due within one month after the end of the period. Shell QGC requests that lodgement requirements are extended to 60 days after quarter end to allow producers sufficient time to collate accurate information and prepare the returns.

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[1] Professor Andrew J Garnett, "Comments on Petroleum Royalty Review, Consultation on Volume Model (Nov 2019)", 8 December 2019, p.2.

Thank you for consideration of the matters raised in Shell QGC's submission.

Yours sincerely

Luke Hutchinson
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