GLENCORE

23 July 2020

Committee Secretary
Economics and Governance Committee
Parliament House
George Street
Brisbane QLD 4000
Email: egc@parliament.qld.gov.au

Dear Committee Secretary,

Royalties Legislation Amendment Bill 2020

Glencore is one of the world's largest globally diversified natural resource companies. The group was founded in the 1970s as a trading company and since then we have grown to become a major producer and marketer of commodities employing 160,000 people around the world. Our operations comprise around 150 mining and metallurgical sites and oil production assets. Our purpose is to responsibly source the commodities that enhance everyday life. We fulfil our purpose by delivering on our strategy to be active at every stage of the commodity supply chain. Our diversity by geography, product and activity, maximises the value we create for our business and its diverse stakeholders.

In Queensland Glencore owns and operates extensive coal, copper and zinc mining operations and is heavily involved in potential bauxite and carbon capture opportunities. In socio-economic terms, in 2019 our Queensland businesses engaged 8,960 employees and contractors with wages and salaries of $956 million, we spent a total of $4.6 billion on goods and services and paid $733 million in taxes and royalties. Our total economic contribution to the Queensland economy was $6.3 billion.

Glencore supports informed and constructive debate around tax reform because it is directly linked to the future of investment and trade competitiveness.

Glencore welcomes the Queensland *Royalty Administration Modernisation Program*, particularly because royalty payers will be able to appeal against the decisions of the Revenue Commissioner based on the merits of their case rather than the limited scope currently available under a 'judicial review' of the administrator's decision making. Merits based reviews have been available for other Queensland State taxes since 2001.

One of the key issues affecting Queensland royalty administration is setting the value of minerals sold to related parties. Intra-group sales often occur in many vertically integrated mining and petroleum groups such as Glencore and while mineral producers are required to apply for decisions on the pricing base used for royalty purposes, there has been a backlog of decisions that has caused uncertainty for miners and conflict with the administration. All of which is probably unnecessary if the system and points of reference were more transparent and leveraged off equivalent transfer pricing regimes applied for federal income tax purposes. These issues weigh heavily on the resources industries operating in Queensland.

A number of the submissions made below attempt to preserve the balance, integrity and function of *gross value royalty decisions* which will continue to be an important part of setting mineral prices for royalty purposes when sales are made to related parties of the producer.

PO Box R1543 · Royal Exchange · NSW 1225 · Australia
Level 44, Gateway, 1 Macquarie Place · Sydney · NSW 2000 · Australia
Tel +61 2 8427 6300 · Fax +61 2 9251 4740 · Web www.glencore.com.au

Glencore Investment Pty Limited ABN 67 076 513 034

Proposed changes to Petroleum Royalties

The State has proposed changes to petroleum royalties that will move the royalty base away from the *wellhead value* of gas to the *volume model* and this will affect royalties paid on gas extracted from coal seams prior to underground coal mining. Gas extraction carried out by coal miners is undertaken for employee safety and emission reduction purposes, rather than commercial gain. Glencore endeavours to abate greenhouse gas emissions by collection, sale and flaring the gases where it is possible to do so. These activities operate at an overall loss when viewed in their entirety and royalties simply add an additional cost that will rise with the pending changes. We are concerned at the scope for the Commissioner to apply benchmark prices for royalty purposes, even when gas is sold to independent buyers. We recommend reasonable limits be applied that require the Commissioner to consider the actual circumstances affecting the miner's operation including existing committed arm's length sales contracts, the proximity on coal mine to major gas markets and the practical relevance of available benchmark prices. We also require confirmation that flared gas from coal operations will remain exempt from royalty.

Specific drafting recommendations

The following are our detailed suggested changes to the Bill that will improve royalty administration by achieving more balance between the position and rights of the Commissioner and royalty payers. The changes will also create more certainty and facilitate better compliance practices:

- **Clauses 46 of the Bill:** Proposed new section 63(6) of the *Mineral Resources Regulation 2013* (MRR) states that *the revenue commissioner cannot be compelled to make a gross value royalty decision for a mineral ... to the extent the decision would decrease the gross value taken to apply for the mineral, if royalty was payable for the return period.* Meanwhile, new section 63(7) states that a decision of the Commissioner not to make a gross value royalty decision under section (6) is a *non-reviewable decision.*

  These proposed provisions are at odds with the existing royalty regime (section 59) and could undermine the veracity of gross value royalty decisions (GVRD) as a mechanism for setting the value of minerals sold to related parties. The producer of minerals that are sold or disposed of to a related party must lodge a return and pay royalties within the limited times specified by the *Mineral Resources Act 1989* and associated regulations (MRR), yet it is unclear how the producer can calculate royalties payable if the Commissioner has not made a value decision. Queensland Treasury hold the same view, see the discussion on page 14 of the July 2020 *Response to Consultation Submissions.*

  The producer is also under a mandatory obligation to make an application for a GVRD (under section 60) *as soon as practicable* after the mineral is sold but the time taken by the Office of State Revenue to make these decisions is an ongoing problem with the administration of Queensland royalties, noting that it is not uncommon for years to pass before a GVRD decision is made.

  With no royalty value decision there is no certainty for a producer on the amount of royalty payable are no rights of appeal either to QCAT or the Supreme Court. These new provisions will further undermine the GVRD regime and will encourage producers to report low values for royalty purposes because, to do otherwise, could mean that they never receive a value decision and achieve certainty for sales made to related parties. Submitting royalty returns with low sales values will run risk of penalties and interest being imposed by the Commissioner if a decision is eventually made. There are existing contradictions and inequities in the regime for valuing minerals sold in these circumstances. Rather than addressing these, the proposed changes will make matters worse for mineral producers in Queensland.

Similar comments are made in regard to Clause 49 and new sections 65(7) and (8) that provide that the Commissioner cannot be compelled to amend an earlier decision to the extent it will decrease the value applying to the mineral if the royalty was payable for the return period. In practical terms, this could mean that a producer could be prohibited from correcting errors in an earlier application for decision and will need to resort to formal appeal rights where the Commissioner refuses to amend.

- **Clause 48 of the Bill:** The time allowed under section 64 of the MRR for a producer to advise the Commissioner of an incorrect GVRD should not be reduced from 60 days to 30 days. The complexity of these issues and required documentation requires more time, not less. We recommend that 90 days be available for a producer to advise the Commissioner of an incorrect GVRD.
- **Clause 49 of the Bill:** A time limit should apply to the Commissioner to amend an earlier gross value decision under revised clause 65(5)(b) of the MRR when the Commissioner has given notice of an investigation. When notice is given there is no obligation on the Commissioner to conduct the investigation in a reasonable time period and so giving a notice can hold review periods open indefinitely. Furthermore, as submitted during consultation, if the Commissioner provides a notice under new section 65(5)(b)(i) it is appropriate for the Commissioner to be allowed to consider both increases *and decreases* in the gross value of the mineral. A change in the method or formula for setting mineral values can often result in both positive and negative adjustments to prior return periods. It is inappropriate to confine adjustments to increases in these circumstances.
- **Clause 129 of the Bill:** Additional words need to be added at the end of new section 64(3) of the Taxation Administration Act 2001 (TAA): *"To remove any doubt, it is declared that this subsection applies only to matters relating to the decision and not to the how the gross value of the mineral is finally worked out in accordance with that decision."* These additional words are necessary because if a formula or method for deciding the value of minerals is stated as general principles, the producer should reasonably be able to object to the way the Commissioner has applied those principles.
- **Clauses 135 and 145 of the Bill**: Despite retention of the exemption for flared or vented gas arising from coal mining operations in section 49(1)(a)(i) of the MRR, there is no apparent way for flared and vented gas to be excluded from the calculation of royalties under the amendments to the *Petroleum and Gas (Royalty) Regulation 2004*. The definition of *domestic gas* in section 135(1)(b) includes *petroleum produced by the petroleum producer in a return period* that is *flared, used or vented*. Meanwhile, section 145 states that the producer *must pay petroleum royalty for the period on the volume of domestic gas produced in the period*.

  Section 15(2) of the *Petroleum and Gas (Royalty) Regulation 2004* says that if a coal mining lease holder mines coal seam gas under the Mineral Resources Act then for the purpose of the Petroleum legislation the lease holder is taken to *produce* the gas, however, it is not entirely clear whether the definition of *domestic gas* in section 135(1) will take priority over the provisions of the MRR. Sections 53 and Schedule 3, Part 2, section 7 of the MRR refer to the Petroleum regulations on questions of the value and rate applicable to coal seam gas but the quantity of gas sold or disposed of could be determined under the MRR (per sections 46 and 49(1)).
- **Clause 143 of the Bill:** New section 149L(3) of the TAA ensures that section 39 covering the tax windfall gains will apply to royalty refunds. This section requires that the Commissioner be satisfied that the taxpayer hasn't received the amount from another person before refunding to the taxpayer. It is our view that the refund to the taxpayer should be the overriding concern of the statute and not the commercial arrangements between the taxpayer and other parties. For practical purposes and given the range of possible commercial arrangements that may arise, it is difficult to

envisage how the Commissioner could be satisfied on the matters covered by the section.

- **Clause 147 of the Bill:** This submission is made is respect of *domestic gas* but the comments are equally relevant to *supply gas*, *project gas* and *liquid petroleum*. The Commissioner will have a broad discretion to apply benchmark prices even where gas is sold to an independent buyer. The Commissioner can apply this discretion when he or she *considers it is appropriate for the protection of the public revenue*. In making his or her decision the Commissioner may have regard to any of the following limited matters:

  (a) any arrangements existing between the petroleum producer and a person who purchases domestic gas;

  (b) the number of sales in the royalty return period;

  (c) the volume of domestic gas produced by the petroleum producer in the royalty return period that is sold to an independent buyer;

  (d) the volume of domestic gas produced that is sold to a person other than an independent buyer;

  (e) any other matter the revenue commissioner considers relevant.

  These provisions as drafted will ***not achieve*** improved royalty administration because they are imbalanced between the Commissioner and producers and provides inadequate guidance that is biased towards State revenue. The only real guidance on application of this discretion is in the words "*the protection of public revenue*". Gas producers who have pre-existing commitments under long term supply contracts could be unfairly exposed to increased royalties calculated at benchmark prices. This is particularly so because the Commissioner is able to apply this discretion even where sales are made to independent buyers.

  Mere consideration of *existing arrangements* and the other sales and volume information says nothing about relative weighting these matters are to be given when exercising the discretion. The Commissioner might consider, for example, that prior arm's length supply commitments made by a producer *do not protect the revenue* because gas prices have risen since those commitments were made. It would be inappropriate and unfair for the producer to be required to pay royalties based on current benchmark prices when receiving lesser amounts for gas sales.

  The statutory guidance for this discretion must be fairly balanced and better articulated so that it can be applied objectively to any given facts or circumstances. The arm's length standard should be a minimum point of reference but contemporary international income tax concepts would be preferred. Consideration should be given to the *commercial and financial conditions* that apply to the producer and under any existing arrangements decided under *arm's length conditions*. In practical terms this would mean, for example, that a producer of incidental gas at a remote coal mine would unlikely to be required to pay royalties based on the *Wallumbilla Benchmark Price* because, in real market terms, no one would be willing to pay that much for gas that is so far away from gas markets and major transmission pipelines.

Please contact me on telephone 02 [redacted] if you require more information of would like to discuss any aspects of this submission.

Yours sincerely,

Nick Talintyre
Director