Minerals and Petroleum Taxation:

A Review of Australia’s Resource Industry Fiscal Regimes and their International Competitiveness

Report of the Ministerial Council on Mineral and Petroleum Resources

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EXECUTIVE SUMMARY

Australia's Resources Sector
The value of resources to Australia lies primarily in its contribution to its exports. In 2003-04, resources contributed 38 percent of Australia's total merchandise exports of $109 billion. Of this, coal comprised 10 percentage points, non-monetary gold 5 percentage points, iron ore 5 percentage points and crude petroleum products 4 percentage points, with the remaining 14 percentage points made up of alumina, diamonds, copper, nickel, uranium, zinc and other minerals.

The current strength of the resources sector is evident by the level of investment in minerals and energy projects. In the six months to October 2005, twelve major minerals and energy projects were completed with total capital expenditure of $2 billion. The project completion rate in the six months prior to that was significantly lower than the completion rate of the previous six months (23 projects were completed in the six months to April 2005) but is around the average completion rate over the past seven years. The number of currently committed projects in Australia is at record levels.

However Australia's share of international exploration has declined by 30 percent since 1999. This has led to concerns that without successful greenfields exploration leading to new discoveries of petroleum and minerals, the current resources boom will not last and the export benefits that resources bring will dissipate.

Australia has been pursuing a comprehensive reform program over the past two decades to increase its economic efficiency and international competitiveness. These reform measures have opened Australia's economy to the world, provided a continually increasing economic prosperity and have resulted in Australia becoming one of the world's leading economies. Australia's minerals and petroleum sector has played a key role in this success.

The nature and economics of resource developments have changed over recent years. As a result of globalisation and its associated elements such as information technology, transportation convenience (reduced travel costs and time), growth in international trade and the consolidation of corporations into global entities, countries are now competing on a global scale for investments. This is particularly true for the resource sector, where mergers and takeovers have led to fewer but larger operators.

In this global environment, investment capital is highly mobile and competition for investment is fierce. Decisions on investments are made on a strategic global level in headquarters, often remote from project locations. Margins are being made ever tighter through a long-term decline in the real value of commodities which, despite the current boom, the Ministerial Council on Mineral and Petroleum Resources (MCMPR) does not anticipate changing. At the same time, more countries are seeking to tap into the same global investment base as regions previously perceived to be high risk become more attractive to investors.

It is common, therefore, for companies with prospective investment projects to seek from governments the best package of investment attraction. Consequently, Australia is competing against a greater number of potential investment destinations, on a global scale market for fewer (but larger) potential investors.

To compete in global markets, resource production and processing has to be very efficient. Australia remains internationally competitive due to its natural resource endowment and associated economies of scale, a highly productive labour force and the availability of efficient infrastructure. But to continue to attract major project investment, Australia must have a competitive fiscal regime, including tax and resource charges, investment attraction arrangements and supporting infrastructure. However, it should also be recognised that the volatility of international markets, such as changes in commodity prices and exchange rates, can often have a greater impact on investment decisions than the competitiveness of Australia's fiscal parameters.

In the Australian federal system, the Australian and State/Territory Governments have differing roles and responsibilities with regard to resource exploration and development.

Generally, under Australian law, mineral and petroleum resources are owned either by the Australian or State/Territory Governments rather than private individuals. However, governments in Australia do not engage in commercial exploration and development. Only the wealth-generating private sector initiates exploration and undertakes mining and petroleum development activities.

Working within the arena of all the Australian governments is the MCMPR, a joint consultative forum on resources issues. The MCMPR has a vision (see Appendix A) that by 2025 Australia will be recognised as a world-class location for minerals and petroleum exploration and development, with a competitive resources industry valued for its contribution to the sustainable development of the nation and the world.

This recognition should come from:

- Australia's attractiveness as an investment location, including its competitive fiscal regime;
- its demonstrated resource potential, resulting from the high quality and availability of resource information;
- its commitment to protecting the natural environment and implementation of best practice occupational health and safety;
- its excellent science, technology and research and development capabilities;
- its skilled, productive and educated people;
- the stability, certainty and efficiency of its regulatory environment, and
- the high level of community engagement and community appreciation of the industry's contribution to a sustainable future.

The MCMPR, at its meeting in July 2004, charged its Standing Committee of Officials (SCO) to examine and report to it on the fiscal environment in which Australia's mineral and petroleum industries operate. The examination was to be aimed at identifying possible reforms and advocate improvements to Australia's fiscal attractiveness while recognising the impact on State and Territory budgets. In particular, the review was to address:

a) direct and indirect taxes;
b) royalties;
c) utility prices;

d) implications of the net revenues received by jurisdictions from the resources sector on the financial incentive for jurisdictions to provide, or contribute to the provision of multi-user infrastructure that will facilitate the further growth of the sector.

The report was sought to assist in identifying the structural factors influencing decisions on resource investment in Australia and the potential impact these decisions may have on achieving the MCMPR's vision for Australia's minerals and petroleum industry in 2025.

International Competitiveness

Australia's fiscal regime is one of several factors that influence its competitiveness as a location for investment in resources exploration and development. Other factors include:

- prospectivity (the likelihood of finding a commercial discovery);
- sovereign risk levels (political, policy and regulatory);
- access to supporting infrastructure; and
- access to commercial markets.

Any assessment of the appropriateness of the fiscal regime must, to some extent, take those other factors into account as the commercial viability of an investment will depend on the range of the factors taken together.

Over a long period of time, Australia has proved highly prospective for many mineral resources and natural gas, although less so for crude oil. To improve perceptions of prospectivity all Australian governments undertake activities such as the provision of pre-competitive geological data.

In terms of low political, policy and regulatory risks, Australia compares very favourably with most nations competing for investment in resource exploration and development. Australian governments seek to project a very low sovereign risk as a key advantage in attracting investment in resource exploration and development. In the 2005 World Investment Risk Survey, Australia was ranked as 5th in the world, after topping the list as the least risky country for the three years previously. Up until this point, Australia's score for sovereign risk had been a perfect rating not achieved by any other country surveyed but issues of red and green tape, and land claims, had affected its score in 2005.

However, Australia's resources are often in remote locations and their development usually requires significant new infrastructure such as road, rail or ports. While such infrastructure can be very costly to provide, it is usually high quality and reliable.

Investors in resource developments in Australia have the freedom to sell their outputs both domestically and in export markets, subject to nuclear safeguards for uranium exports. Reforms in Australian energy markets and open access in infrastructure are facilitating greater freedoms in domestic markets for resources. Australia also provides relative proximity to rapidly growing export markets in Asia and the Pacific.

There are numerous surveys and studies available that provide some insights into the international competitiveness of Australia's economy, its fiscal regimes (covering income tax, company tax and general resource tax regime) and the attractiveness of investing in resources in Australia. The results of several of these studies are set out in Chapter 2 and key aspects are summarised below.

Generally, and for an economic overview, the IMD World Competitiveness Yearbook 2005 ranked Australia 9th out of 60 countries for their ability to provide an environment that sustains the competitiveness of companies. Similarly, the World Economic Forum: Global Competitiveness Report 2004-05 ranked Australia as 14th out of 104 countries in gauging the ability of the world's economies to achieve sustained economic growth over the medium to long-term. The Organisation for Economic Co-operation and Development (OECD) Revenue Statistics indicated that the total Australian taxation revenue of national, state and local governments, expressed as a proportion of gross domestic product (GDP), is the eighth lowest of the 30 OECD countries, and below the average for these 30.

For petroleum, the 2004 Wood Mackenzie study on Australia's competitiveness indicated an improved commercial success rate in Australia over the period of 1994 - 2003 of 10 percent (ranked 41 out of 57) and Australia ranked as the 6th most active exploration area in the world.

For minerals, the Metals Economics Group of Canada (MEG) survey of world mineral exploration budgets showed that global non-ferrous mineral exploration budgets rose strongly in 2004 but Australia's share of global budgets fell to 14.7 percent. This was down from 15.5 percent in 2003 and represented the lowest point in Australia's share of global mineral exploration in 20 years. The Fraser Institute (exploration) of Canada in its 2005 annual survey ranked the US state of Nevada for the 5th time in a row as having the best mineral policies, followed by Ireland and Manitoba, with Tasmania the only Australian state to make the top ten. Nevertheless, since its inception in 1996 Australia has generally scored well and is perceived as relatively mining friendly. The Behre Dolbear & Co Inc Consultancy Report of 2005 ranked Australia first on its 2005 ranking of countries for mining investment. Australia received the highest or equal highest score on four of those criteria – political and social issues, permitting delays and level of corruption.

The Colorado School of Mines: Global Mining Taxation Comparative Study of 2000 showed that Australia was middle-ranked in terms of internal rate of return for both gold and copper and middle-ranked in terms of effective tax rate (ETR) for gold. Only in terms of ETR for copper did Australia do well. This indicated that, in 2000 at least, a number of countries, many of which are in direct competition for minerals investment, had mineral taxation regimes more competitive than the regime in Australia. However, it is noted that a number of reforms have been implemented since 2000 to improve the competitiveness of Australia's taxation system.

The range of independent, international studies indicate that Australia generally ranks highly as a destination for investment in resource industries across a wide range of factors and that the same independent studies also indicate that Australia's State and Territory fiscal regimes are generally competitive.

Consequently, while our fiscal regimes are not beyond improvement, they are considered to be broadly appropriate when viewed together with our prospectivity, sovereign risk, infrastructure and access to markets to support the achievement of the MCMPR's vision of Australia being recognised as a world-class location for resources development by 2025.

The Minerals Council of Australia (MCA), the Australian Petroleum Production and Exploration Association (APPEA) and the New South Wales Minerals Council called for further analysis of mineral and petroleum tax regimes.

General Taxes

The Australian tax system involves taxes and other charges at Federal, State/Territory and local government levels in order to fund a range of government programs and community services. The principal aim of taxation is to provide the revenue necessary to fund government functions. However, taxation also allows governments to provide social and merit goods, support those for whom a free market would not otherwise provide and modify free market imperfections.

The main components of Australia's taxation system comprise personal income tax, company income tax and indirect taxes (including, principally, the Goods and Services Tax (GST)).

The Australian Government has implemented major reforms to the tax system to improve Australia's international competitiveness, including the reduction in the company tax rate from 36 percent to 30 percent in 2001. The tax system applying since 2000 has been designed to be internationally competitive and to reduce the tax burden of doing business in Australia. Australia's tax to GDP ratio is the eighth lowest of the 30 OECD countries; however, it should be noted that Australia's resources sector often competes against non–OECD nations.

Nine submissions received from industry raised numerous issues concerning the taxation regime. These issues included the impact of the loss of accelerated depreciation on capital intensive industries; 'blackhole' expenditures; tax deductibility of overseas exploration expenditures, taxes on business inputs; the operation of the GST; tax treatment of research and development expenditures; the tax consolidation regime; taxation of infrastructure financing arrangements; international taxation arrangements and the loss recoupment rules for companies. The issue of zonal tax offset schemes, while not raised by industry associations, was identified by one State jurisdiction. These issues are discussed in Chapter 3 of the Report.

Most of the issues raised by industry concerning the tax regimes in Australia (income tax, company tax, indirect taxes, GST and tax expenditures) fall outside the policy responsibilities of the resource Ministers. However, these issues can affect the competitiveness of the fiscal environment for Australian mineral and petroleum resources. In particular, the minerals and petroleum industries argue that Australia's depreciation arrangements are generally seen by industry and its representatives as less favourable than those applying in nations competing for resource investments, and this is often claimed by industry to be the single issue most impacting on the competitiveness of resource investment in Australia.

Furthermore, following the 2002-03 Budget, the Australian Government introduced statutory caps on effective lives for taxation purposes for certain assets (e.g. a statutory cap of 15 years was deemed for oil and gas assets even though the actual effective life of those assets could be significantly longer) on the grounds of industry strategic development and international competitiveness.

In response to industry's approaches to it in the context of preparing this report, the MCMPR will refer industry's concerns about the following issues to the attention of the Federal Treasurer:

- effective lives of assets for depreciation purposes;
- promoting Research and Development and access to technology;
- tax consolidation regime;
- loss recoupment rules; and
- zonal tax offset schemes.

The actions taken to reduce taxes on business inputs, particularly the changes to fuel excise arrangements and import duties will be of benefit to the resources sector. Any delays to the proposed phase in of changes to fuel excise arrangements (outlined in the Energy White Paper) would delay the potential benefits to the resources sector.

Resource Taxes and Royalties

The Australian and State/Territory governments generally own on behalf of the community minerals and petroleum resources in Australia, and impose access charges on minerals extraction and petroleum production to ensure that the community receives a benefit from their development. Access charges on the production of resources in Australia include specific Australian/State/Territory government taxes (e.g. petroleum resource rent tax, crude oil excise) and/or royalties imposed on both petroleum production and minerals extraction. Resource taxes and royalties represent the value of the resource to the government.

Economic rent of a resource in a competitive market is the value of the production when all necessary costs have been deducted. Depending on the economic rent, the resource tax can represent a significant component of the company's total tax burden. Ideally, a resource tax regime should ensure that the government receives no more than the value of the economic rent while minimising distortions to private decisions.

Government taxation of economic rent can take the following forms:

- royalties, duties or user pay taxes imposed on production, revenue or profit;
- the government's equity participation in the profits or dividends of the project;
- production sharing contracts (PSC) between the government and the company; or
- up-front payments paid pursuant to an auction of mineral or petroleum rights.

The resource tax methods generally employed in Australia are output-based (either specific or *ad valorem)*, profits-based taxes or royalties, or hybrids of both these methods. Resource tax regimes across Australia have evolved over time and significant differences apply across resources and across jurisdictions.

The current range of resource taxes and royalties applying in Australia comprise the following:

- minerals produced onshore are collected by the States and the Northern Territory but there is no common royalty regime in these jurisdictions, leaving a wide mix of specific, *ad valorem* and profit-based royalties;
    - the royalties raised under these multiple regimes average out at 3.5 percent of the gross value of mineral production;
- minerals produced offshore (outside the first three nautical miles from the territorial sea baseline) will attract an *ad valorem* royalty of 2.5 percent and a net income royalty of 15 percent (revenue from offshore minerals royalty is, in principle, shared 60:40 in favour of the States); but
    - currently there is no offshore minerals production;
- petroleum produced onshore and within coastal waters attracts royalties at 10 percent of net wellhead value of production which is collected by the States and the Northern Territory;
- crude oil produced onshore and in the North West Shelf production area is subject to a Commonwealth excise (the first 30 million barrels is excise exempt, varying excise rates apply to annual production at different levels);
- petroleum produced on Barrow Island off Western Australia attracts a resource rent royalty based on 40 percent of net cash flow, with revenue shared between the State and the Commonwealth;
- petroleum produced in Australia's offshore areas, except for the North West Shelf (NWS) production area, attracts a petroleum resource rent tax levied at 40 percent of net revenues from a project;
- petroleum produced in the North West Shelf production area attracts a royalty at 10-12.5 percent of net wellhead value, which is collected by the Australian Government, two thirds of which is shared with the Western Australian Government; and
    - crude oil produced from this area is also subject to crude oil excise;
- petroleum produced in the Joint Petroleum Development Area (JPDA) between Australia and East Timor is subject to fiscal terms set out in a PSC.

Submissions received from industry raised numerous issues concerning the resource taxes and royalties. These issues included the need for long term stability in tax arrangements; the removal of resource tax distortions on competing resources; the need for empirical evidence; the tax treatment of project closure and rehabilitation costs; excess deductions; other specific issues such as royalty arrangements applying to coal seam methane and the need for tax incentives for frontier petroleum exploration and gas developments; the treatment of cross boundary resource tax issues; and finally, a call for a comprehensive review of State and Northern Territory royalty arrangements and a move towards more uniform royalty arrangements.

The MCA and APPEA also raised a number of concerns about resource tax and royalty regimes across Australia and the MCA sought a comprehensive, independent review of those regimes to deliver uniformity, greater transparency and remove distortions.

At the same time, industry does not have a consensus view on a preferred royalty system. Views differ on the relative importance of the different criteria and, in the view of the MCMPR, trade-offs are necessary and even inevitable. For example, profit based taxes may be preferred for very large, long life projects such as gas projects. However, the administrative complexity of such regimes means that they are unlikely to be suitable for relatively small, low value projects such as quarrying. Profit related royalties have a number of efficiency benefits but also involve greater administrative costs and complexity and risk greater volatility to government revenues.

In contrast, an *ad valorem* royalty regime can be distorting because it does not respond to cost changes, while specific rate royalty, varying only with output, is the most distorting of all.

A complication is that royalty arrangements do not function in isolation and are but one element in government's overall taxation framework. Given the variety of objectives governments seek to achieve through royalty policy, and the limited extent to which any one regime will meet them, and the diverse nature of resource projects, it may be that a range of taxation regimes is necessary and appropriate.

In response to industry's submissions, the MCMPR does not believe that a comprehensive, independent review of fiscal regimes is necessary or justified. No single type of resource tax is likely to be ideal for all circumstances and a range of resource tax regimes is probably unavoidable.

In spite of this, and to assist jurisdictions provide greater uniformity across royalty regimes, the MCMPR endorses the following principles for resource tax regimes. These are, to the greatest extent practical, that resource tax regimes should compensate the community for allowing the private extraction of Australia's depletable resources while seeking to ensure:

- economic efficiency (not distorting commercial decisions regarding the levels of capital and other inputs devoted to economic activities which should be made in response to market signals);
- equity (relating to the resource developer's capacity to pay; fairly sharing the burden and benefits of revenue collection between the resource developer and the community; being uniform across all taxpayers in equal situations and being competitively neutral across competing resources);
- administrative simplicity (minimising compliance and administration costs for business and government);
- consistency with broader environmental, social and fiscal objectives (taking account of the need for reliability and predictability of revenues, being mindful of externalities such as environmental, social or infrastructure objectives); and
- international competitiveness (the tax regimes do not harm the competitiveness of Australian resource producers relative to overseas suppliers and do not act as an incentive to invest in overseas resource projects in preference to competing Australian resource projects).

The MCMPR does not support an independent review of State and Territory royalty arrangements but jurisdictions could consider the need to review their resource tax and royalty regimes against the above principles and recommendation.

In considering the above principles, there is also a need to avoid distortions arising from different royalty policies and rates when resource projects cross jurisdictional boundaries. It is noted that principles concerning cross jurisdictional situations applying to petroleum taxation have been agreed by officials from the Western

Australian and Australian Governments. On the basis of this agreement, the MCMPR supports the following principles being applied to petroleum taxation in cross-jurisdiction situations:

- a petroleum pool which extends beyond the production licence to an area where no production licence exists may be extracted through the production licence area even if the vacant area is in a different jurisdiction under the "Rule of Capture";
- resource taxation should be initiated on production from a licence area;
- apportionment of petroleum in a straddled pool should be based on location prior to issue of the first production licence to authorise extraction; and
- transparent, arms-length valuation of petroleum transfers to be used as the taxation base, where these occur. Where a non-arms-length transaction occurs the jurisdiction authorities should determine a reasonable price based on an internationally accepted transfer price methodology.

The MCMPR agrees:

- to the creation of a Royalty Consultation Group from all Australian, State and Northern Territory resource departments to develop agreed administrative standards involving royalty concepts and definitions, to benefit from shared experience and to develop a consistent set of administrative standards involving royalty concepts and definitions;
- to the general principle that the treatment of project closure costs depends on the nature of resource tax regime and that:
  - if the tax is profit based, then project closure costs should be deductions;
  - if the tax is production based on a proportion of sales value, then project closure costs should not be deductions;
  - if the tax is production based on well-head (or mine-head) value, then project closure costs would only be deductions if they relate to post-wellhead (or post-mine head) costs actually invoiced during a royalty period for payment in the short term; and
- that excess deductions for a project under *ad valorem* royalty regimes should not be transferable to other projects or be eligible for a refund from previous years' royalty payments.

To our knowledge, quantitative comparisons between profit based systems and specific or *ad valorem* regimes on indicative resource projects have not been attempted in Australia. Modelling would benefit informed decision-making on comparison between these tax regimes. The Department of Industry, Tourism and Resources (DITR) has tasked the Australian Bureau of Agricultural and Resource Economics (ABARE) to undertake a study of the potential cost/benefits of the application of profit based taxes in areas of energy resources currently using output-based taxation regimes, and taking into account revenues, business compliance costs and administrative costs.

The MCMPR requests Resource Departments to assist ABARE by providing relevant information.

Industry's concerns raised about the need for incentives for frontier exploration are currently being addressed through the Minerals Exploration Action Agenda. Concerns raised by the petroleum industry about the need for development incentives are also under discussion between APPEA and relevant Australian Government Departments.

Utility Prices and Other Issues
The MCMPR addressed utility prices in its examination of Australia's fiscal competitiveness. A number of issues other than taxation were also raised by industry as impacting on the competitiveness of the Australian resource sector. These other issues were both fiscal and non-fiscal and are addressed in Chapter 5 of the report.

Industry submissions did not raise any issues concerning energy and water utility prices or energy and water utility markets.

An industry submission did raise, however, concerns about the impact of climate change on fiscal competitiveness. This issue is outside the terms of reference of this report and is being addressed through the Council of Australian Governments (COAG), work being carried out by State and Territory Governments and the initiatives under the Australian Government's Climate Change Forward Strategy.

Industry also raised concerns about junior explorers' access to finance and requested a flow-through shares (FTS) scheme to address these concerns. The primary argument in favour of introducing an FTS scheme is that it will materially enhance the capital raising capability of Australian exploration companies, particularly the junior sector. This, in turn, will boost resource exploration expenditure in frontier areas, place the resource sector on a more sustainable footing and potentially increase the rate of discovery of commercial mineral and petroleum deposits. Such a scheme would assist the resources sector to respond to the current global upswing in commodity prices and, over the longer term, enhance Australia as a centre for resource excellence.

Industry submissions raised concerns about access to pre-competitive geoscience data and requested increased expenditure on pre-competitive geoscience survey program to achieve national coverage of basic geoscience datasets to modern standards. In conjunction with the initiative of FTS, improving the management and delivery of geoscience data will help arrest the decline in Australia's competitive position in mineral exploration and underpin discovery of the next generation of major mineral deposits by lessening exploration risk. Such a program has received the support of all jurisdictions.

The MCMPR, at its 25 November 2005 meeting, also strongly urged the Commonwealth to consider implementation of an enhanced national pre-competitive geoscience programs, along with a FTS scheme, and as means of encouraging further mineral exploration in Australia.

The MCA submission proposed a review of the arrangements for the allocation of mining rights across Australia consistent with a set of principles that they are advocating. Allocation regimes across Australia are generally well understood, transparent and predictable. Accordingly, the MCMPR was not convinced that such a review is required.

Industry has continuing concerns about financial surety instruments despite the development of a strategic framework for mine closure by the then Australian and New Zealand Ministerial Council (ANZMEC) in 2000 to provide guidance on financial surety instruments. The Standing Committee of Officials is aware that a number of jurisdictions have reviewed their bond policies in recent years and industry concerns are being addressed.

The issue of project closure costs and deductibility should be treated in conjunction with financial surety instruments. In noting industry's position that a national approach is required for providing for bonds or the costs of rehabilitation, the MCMPR re-endorses the strategic framework for mine closure developed by ANZMEC in 2000 and notes jurisdictions are progressing their own financial surety instruments against that framework.

An industry association also raised concerns about the significant costs of complying with safety regulations and the impact this is having on small businesses in the resources extraction sector. The relevant actions are currently being taken under the MCMPR's National Mine Safety Framework to implement a detailed and practical implementation plan in consultation with stakeholders.

Infrastructure for Resource Developments

Australia's fiscal competitiveness is not limited to its taxation and royalty regimes; it also encompasses expenditure related matters, such as infrastructure provision. The importance of efficient, world class infrastructure in enhancing the international competitiveness for investment is widely documented in studies.

Concerns regarding Australia's level of infrastructure have been voiced by various industry, government and non-government organisations. A common complaint is that Australia fails to provide the level of infrastructure necessary to support project development in remote locations. Resource projects are frequently located in remote, inhospitable areas or in regional areas where transport, communications, town, water, electricity and port facilities need to be upgraded, enhanced or built from scratch.

Infrastructure for resource development falls within three general classes:
(a) project infrastructure (such as plant and equipment, water pipelines, energy generation, haul roads and landing strips, railways and ports);
(b) multi-user infrastructure (such as dams, power stations and transmission lines and public roads, railways, and ports); and
(c) social infrastructure (including housing, town water supply, health and education services, law enforcement, basic community transport and community welfare).

Resource companies finance and provide the project infrastructure necessary to enable resource revenues to be earned. Project infrastructure provided by resource companies is sometimes the only infrastructure built in very remote areas of Australia. Due largely to the remote location of resource projects, resource companies also frequently provide or significantly contribute to the provision of multi-user and social infrastructures that elsewhere in Australia would normally be provided by either private investors in infrastructure or governments.

While the provision of multi-user and social infrastructure in Australia has traditionally been a State or Territory Government responsibility, the Australian Government has played a positive role in infrastructure through:

- the provision of specific purpose payments (SPPs) to the States/Territories;
- investing in government business enterprises and agencies;
- the formulation of 'framework policies', such as infrastructure provisions in the *Income Tax Assessment Act* and the National Competition Policy; and
- the provision of incentives, delivered through the Strategic Investment Coordination process supporting multi-user infrastructure facilities.

The trend towards private provision of infrastructure has been reinforced by the emergence of significant capital availability in Australia for infrastructure investment, resulting from financial deregulation and Australia's superannuation policies during the 1980s and 1990s. Globally integrated capital markets are more capable of financing infrastructure projects. Also, with governments moving to introduce competition into regulated markets, continued government ownership creates scope for conflicts of interest and introduces added sovereign risk.

Government can have a legitimate role in facilitating the provision of infrastructure due to market failure, or on the basis of investment attraction and strategic development. In relation to the provision of infrastructure related to resource developments, this is usually based on investment attraction or strategic development grounds.

All governments across Australia are committing significant funding to infrastructure to support resource developments; however, the infrastructure challenge is not just about funding but getting the policy framework right and removing impediments to investment.

Some jurisdictions have concerns about the relative revenue flows to governments from resource projects and the relative imbalance between revenue benefits and fiscal costs, together with how the imbalance is addressed in the Commonwealth Grants Commission's revenues sharing methodology. The imbalance between States is a matter that those jurisdictions could raise directly with the Commission in its current review of its revenue sharing methodology.

The Prime Minister's Taskforce Report on Export Infrastructure has made a number of recommendations focusing on regulation which have been endorsed by COAG and are to be incorporated into a review of the National Competition Policy. The Australian Government has also pursued reforms to sections 51AD and 16D of the *Income Tax Assessment Act 1997* to encourage private investment in infrastructure.

Regulation has been the focus of the recent Prime Minister's Taskforce Report on Export Infrastructure. The Report concludes that there is no major infrastructure crisis, but there are some underlying weaknesses which need to be addressed if problems are not to become widespread, and to prevent future bottlenecks developing.

COAG considered the recommendations of the Taskforce on 3 June 2005 and agreed in principle to:

- hasten the long-term planning being undertaken under AusLink;

- extend AusLink planning and coordination to ports and associated shipping channels;
- each jurisdiction providing a report to COAG every five years on infrastructure;
- the Commonwealth facilitating the establishment of groups to coordinate logistics chains of national importance;
- reinvigorate the agenda for harmonising road and rail regulations; and
- establish “one-stop shops” in each jurisdiction for project facilitation and approvals.

At its meeting on 10 February 2006, COAG noted progress in the implementation of these six infrastructure measures. Implementation arrangements agreed by COAG include:

- a commitment to complete all 24 corridor strategies under AusLink by 30 June 2007 at the latest;
- extending the corridor strategies to include relevant capital city and associated regional ports on the AusLink National Network;
- undertaking a stocktake of logistics chains of national importance and encouraging industry to establish their own logistics chain coordination arrangements; and
- establishing a ‘one-stop shop' in each jurisdiction by 30 June 2006 for significant development projects.

COAG also agreed in principle to a simpler and consistent national system of regulation for ports and export related infrastructure and that this be considered in the COAG Review of National Competition Policy (NCP).

COAG considered the NCP’s review’s report at its 10 February 2006 meeting, and among other things, signed the Competition and Infrastructure Reform Agreement. The Agreement encompasses all governments’ commitment to achieve a simpler and consistent national approach to the economic regulation of significant infrastructure and to improve the functioning of markets. When economic regulation is required to determine the terms and conditions of access to significant infrastructure, states have committed to strengthening the consistency of such access regimes by working towards common principles to govern the operation of access regimes so as to minimise costs for infrastructure users operating across jurisdictions.

The Prime Minister’s Exports and Infrastructure Taskforce concluded that there is no major infrastructure crisis but highlighted some underlying weaknesses that must be addressed to prevent future bottlenecks developing.

Government involvement in the provision of infrastructure related to resource development would benefit from an agreed framework to guide that involvement and the MCMPR endorses the eight government guiding principles:

1. governments should ensure that infrastructure provision is the most efficient and effective mechanism to assist resource development;
2. government investment in infrastructure should result in net benefits to Australia. To this end there needs to be:
    - adequate co-ordination across governments; and

  - consistency in the principles applied by governments;
3. major infrastructure investment should provide value for money and governments' contributions should reflect the benefits to the general community. To this end, the infrastructure should be fit-for-purpose and a benefit-cost analysis undertaken;
4. governments should ensure that the risks associated with infrastructure construction and use are articulated and appropriately shared between government and the private sector. To this end, government should ensure the infrastructure is fit-for-purpose through a risk assessment;
5. where infrastructure pricing is utilised this needs to be efficient, and have a clear rationale;
   - if government intends to alter infrastructure use via pricing, then such pricing should be efficient and take account of the facts that:
     - once built, infrastructure costs are sunk; and
     - demand and supply conditions will alter the efficient pricing structure;
6. governments will ensure that they obtain the provision of services related to infrastructure (e.g. construction) in a manner that:
   - minimises the cost of service provision; and
   - is open, fair, and transparent;
7. decisions regarding the financing and pricing of infrastructure should be separated from decisions regarding the resource rent collection mechanism; and
8. any public contribution to infrastructure should be consistent with government policy, including economic, environmental and social objectives, and with Australia's international obligations, including World Trade Organisation requirements.

Finally, the MCMPR agrees that Australian and State/Territory Governments should adopt a more cooperative approach to facilitating the provision of infrastructure for resource projects of national significance, including considering a standard approach to the preferred form of assistance, involving greater harmonisation of processes.

While considering the above, the following two announcements as a consequence of the Federal Budget 2006-07, need to be noted:

Budget 2006-07 Announcement to improve the incentive for businesses to invest

As part of the Budget 2006-07, the Government announced an improvement in the incentive for businesses to invest in plant and equipment by more closely aligning depreciation which serves to reduce the cost of investing in new plant and equipment. The Budget would increase the incentives for Australian business to invest in new plant and equipment by increasing the diminishing value rate for depreciation from 150 per cent to 200 per cent for all eligible assets (new and second hand) acquired on or after 10 May 2006, including assets with statutory caps. It would also apply to project pool expenditure for new projects. This would allow businesses to write off the cost of new plant and equipment more rapidly for tax purposes, reducing the cost of investing in eligible assets over their effective lives. The changes would enhance the effectiveness of the uniform capital allowance regime, which was introduced by the Government in 2001. This measure would bring Australia more into line with other comparable countries and improve the international competitiveness of Australian business. Ensuring depreciation for tax purposes aligns with economic depreciation would also, the Government announced, assist business keep pace with new technology, enhance productivity and sustain economic growth.

and

Flow-through Shares Arrangements
As part of the 2006-07 Budget, the Government decided against the introduction of a flow-through shares arrangement into the Australian taxation system.