

CABINET - SUBJECTS FOR CONSIDERATION, 10th December, 1990.

CABINET	SUBJECT	DOCKET
<div data-bbox="1095 652 1274 689" data-label="Text"> <p>Not Relevant</p> </div>		
<p>No. V. LATE 10.2 Decision</p>	<p>Re. Cooper Basin royalties. APPROVED</p>	<p>M.M.E. 67/1988</p>
<div data-bbox="1072 1331 1252 1367" data-label="Text"> <p>Not Relevant</p> </div>		

10-2
MHE 67/88
SR 28/1/6
RAL:ZV

CONFIDENTIAL

TO THE PREMIER FOR CABINET:

Re: Cooper Basin Royalties

1. Proposal

Approval is sought to amend the Cooper Basin royalty negotiating position and, in the event that a negotiated settlement cannot be obtained by year end, approval in principle given to the use of legislative action to achieve the government's royalty objectives.

2. Background

2.1 Cabinet approval was given on 3 July 1989 for the formation of a task force to negotiate a new Cooper Basin royalty regime. The task force is chaired by Mr. R. Marrett, General Manager ETSA and members include representatives from Treasury, the Department of Mines and Energy, the Office of Energy and Planning and Crown Law.

The approved negotiating position is:

- Increase the royalty rate from 10% to 12.5%
- Change the basis for calculating wellhead value to reduce allowable deductions from sales revenue (the major change being to reduce the level of financing costs allowed as a deduction).

The impact of these changes would be to increase royalty from 4.6% of the present value of the future sales revenue, to 7.5% (approx.) based on pre-Iraq crisis oil price projections. These changes would be equivalent to additional State income averaging approximately \$25 million per year.

2.2 Cabinet approval was given on 25 June 1990 to draft amendments to the royalty provisions of the Petroleum Act to strengthen the State's negotiating position with the Cooper Basin Producers and to remove problems with

the existing provisions in their application elsewhere in the State (eg the Katnook development in the SE). A draft Bill has been prepared for which approval will be sought in the near future.

2.3

Clause 10(1) Legal Professional Privilege

The alternate view, which would no doubt be espoused by the Producers, is that the royalty rate changed at the relevant dates to that prescribed by the Petroleum Act, but the calculation of the well head value remains that specified in the Cooper Basin Indenture.

Clause 10(1) Legal Professional Privilege

3. Discussion

- 3.1 Negotiations with the Producers have centred on the comparison of the Indenture royalty regime with interstate equivalents, the task force's view of which is attached. The Producers have not presented any convincing evidence to refute this summary.
- 3.2 The task force has formed the opinion that the Producers would be willing to accept a negotiated settlement under which the royalty return to the State would be in the range of 6.5% to 7.0% of the present value of the future sales revenue (equivalent to an average of an extra \$15-20 million per annum above current levels on pre-Iraq crisis oil price projections). They have indicated resistance to an increase of the Royalty rate above the current 10%, but appear willing to accept some changes to the basis of calculation of wellhead value.
- 3.3 In the event a negotiated settlement cannot be achieved which results in a royalty return in the pre-Iraq crisis 6.5-7.0% range, it is considered that legislative action would be necessary to achieve a significant increase in Cooper Basin royalty in line with the Government's royalty objectives. Draft legislation to amend the royalty provisions of the Petroleum Act has been prepared. Draft amendments to the Indenture have also been prepared which clarify

that royalty on gas reverted to the Petroleum Act on 1.1.1988 and on liquids on 1.1.1993.

- 3.4 The flow-on impact of increased royalty on gas prices will need to be addressed by Government for either a negotiated or legislated resolution of the royalty issue. As previously advised, South Australian consumers can be protected from this impact by a rebate equivalent to approximately 25% of the net increase in royalty revenues.

4. **Recommendations**

It is recommended that:

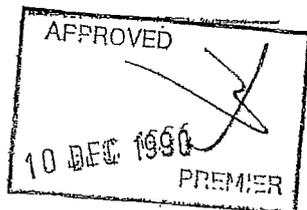
- 1) Cabinet support negotiation of a Cooper Basin royalty regime aimed at returning 6.5% to 7.0% of the present value of future sales revenues (on a pre-Iraq oil price scenario), to apply from 1.1.1991.
- 2) In the event that negotiations are not successful by year end, Cabinet endorses the principle of a legislative route to achieve the Government's royalty objective.

6.12.190



J H C KLUNDER
MINISTER OF MINES AND ENERGY

In Cabinet



AUSTRALIAN ROYALTY REGIMES APPLIED TO THE COOPER BASIN PROJECT

Royalty Expressed as a
Percent of Gross Revenue

Royalty Regime	TOTAL PROJECT	FUTURE PROJECT
South Australia	4.6%	4.6%
Queensland	6.2%	6.7%
Northern Territory	6.5%	6.8%
Victoria Offshore	7.0%	7.2%
Western Aust.	7.3%	8.2%
Victoria Onshore	10.0%	10.0%

Note: The percent of gross revenue is the royalty expressed as the NPV of the royalty received over the life of project in 1989 at the LTGRR, divided by the NPV of the gross revenue received over this period. Assumes future gas exploration successfully supplies 70 PJ/yr to 2020 and no future oil discoveries. Based on pre-Iraq crisis oil price projections.

"TOTAL PROJECT" denotes the period 1/1/64 to 31/12/23.

"FUTURE PROJECT" denotes the period 1/1/89 to 31/12/23.

Australian Royalty Regimes

The table below sets out the interstate royalty regimes that have been applied to the SA Cooper Basin project.

Our advice is that these regimes have been applied to a significant project in each State, or in the case of WA, a scheme that would be applied to a significant new onshore development.

It is requested that in any query of interstate authorities, DME not be identified as the source of this data.

	Royalty Rate (%)	Upstream Method	Capex Deprac Period (year)	Interest (%)	Downstream Method	Capex Deprac Period (year)	Interest (%)	Debt/Equity Ratio (%)
SA	10	CF	15	LTGBR \times 1.2	CF	15	18	N/A
Qld	10	SL	10	0	CF	10	LTGBR+4%	N/A
NT	10	SL	10	0	SL	10	0	N/A
Vic (off)	12	SL	20	8.5	SL	20	8.5	100
WA	12.5	SL	10	LTGBR	SL	10	LTGBR	60
Vic (on)	10	N/A	N/A	N/A	N/A	N/A	N/A	N/A

LTGBR = Long Term Government Bond Rate

CF = credit foncier

SL = straight line

Victorian offshore royalty rate averages 12.2%. In the DME calculation 12% was used.

The CF depreciation on downstream capex for SA continues for the life of the project.

Upstream capex denotes all capital expenditure from wellhead to Moomba plant outlet.

Downstream capex denotes all capital expenditure on PL2 and Port Bonython.

The Victorian onshore royalty is calculated as gross selling value rather than wellhead value.

23/3/90