



*INPEX Operations Australia Pty Ltd
ABN 48 150 217 262*

*22/100 St Georges Terrace Perth
Western Australia 6000*

*Tel +61 8 6213 6000
Fax +61 8 6213 6455*

INPEX.com.au

Ref: PER-21534830356

1 November 2019

Committee Secretary
Standing Committee on Economics
PO Box 6021
Parliament House
CANBERRA ACT 2601

RE: Australia's oil and gas reserves

Thank you for the opportunity to participate in the inquiry into Australia's oil and gas reserves, and the arrangements that can maximise the benefits of the industry to Australians.

INPEX has been part of the business community for more than 30 years, and we are proud of our growing economic and social contribution to Australia. Our company's mission is to provide a stable and efficient supply of energy to our customers in a sustainable way.

As Japan's flagship oil and gas exploration and production company, INPEX is currently involved in approximately 70 projects across more than 20 countries.

INPEX is active in several projects in Australia and the Timor Sea, including Prelude, Bayu-Undan/Darwin LNG, Van Gogh, Coniston and Ravensworth. Ichthys LNG, however, is the crown jewel in our global portfolio. In our submission, we focus on the benefits of Ichthys LNG to the Australian people.

INPEX has had the opportunity to review the Australian Petroleum Production & Exploration Association (APPEA) submission and endorses the comments in that submission. The following comments are supplementary to the APPEA submission.

We hope the Senate Standing Committee on Economics (References) finds our contribution beneficial to its inquiry.

Yours sincerely

Tetsuhiro Murayama
Vice President Corporation Coordination

INPEX Submission: Australia's oil and gas reserves

Introduction

As a supplement to the APPEA submission, INPEX would like to illustrate some of the ways we contribute to the economic well-being of Australians and how Australia can continue to maintain competitiveness as an investment destination for the oil and gas industry to secure these benefits for generations to come.

We wish to note that the historical and structural factors that have influenced arrangements used by countries to maximise the benefits to the public from the oil and gas sector are broad ranging. Levers used to maximise benefits to countries and their citizens range from strong anti-corruption and bribery measures to effective environmental standards, from sound taxation policy to implementing international standards related to human rights.

By global measure, we are pleased that Australia has in place high standards for transparency, labour hire, accountability and sustainability that industry must meet in order to do business here. It reflects the fact that Australia is a stable democracy with strong government institutions and rule of law—qualities that has been successful in attracting the kind of investment that contributes significantly to national prosperity.

For specific comments regarding existing property rights, and specific arrangements used by other countries to maximise the benefit to the public of national oil and gas reserves, we refer the Committee to the APPEA submission.

Economic and social contribution

Ichthys LNG is a Joint Venture between INPEX group companies (the Operator), major participant Total, CPC Corporation and the Australian subsidiaries of Tokyo Gas, Osaka Gas, Kansai Electric Power, JERA and Toho Gas.

We are very proud of Ichthys LNG. It represents the single largest overseas investment by a Japanese company. By definition, Ichthys LNG is also the largest ever Japanese investment in Australia. This investment was underpinned by the world's largest project financing from 8 export credit agencies (including EFIC) and 24 commercial banks.

Ichthys LNG also represents:

- the largest discovery of liquid hydrocarbons in Australia in more than 50 years
- the first Japanese-operated LNG project in the world
- the largest semi-submersible platform in the world, Ichthys Explorer
- the largest ever French investment in Australia, and
- the longest subsea pipeline in the southern hemisphere.

Ichthys is a nation building project for Australia, with lasting positive social and economic impacts. A third-party Economic Impact Assessment concludes that, even under very conservative assumptions, the Ichthys Project will contribute to Australia \$190 billion in additional GDP and \$195 billion in exports.

Local content

For INPEX, it is not only what we produce, but how we produce it that is important to our engagement in Australia: we strive to conduct our business activities in a sustainable and responsible way.

INPEX is committed to local industry through our Australian Industry Participation Policy and Industry Participation Plan by which we provide opportunities for local industry to contribute to INPEX activities, and maximise Australian industry participation where competitively possible, based on health, safety and environment, schedule, quality and cost.

We actively seek suppliers and contractors whose objectives are compatible with ours—those with a commitment to delivering the highest-quality products, services and worldwide cost competitiveness in the marketplace and an unwavering commitment to safety.

During the construction phase of the Ichthys LNG Project (2012 to 2018), more than 49 per cent Australian content was achieved, which comprised of contracts, procurement and project owner costs.

In the Northern Territory (NT), more than 1,150 local businesses have secured work through 6,000 contracts and purchase orders to date. Further, more than \$175 million in contracts and purchase orders have been awarded to 62 Aboriginal and Torres Strait Islander business.

The Ichthys Project created thousands of employment opportunities for locals in the NT, and approximately \$12.5 billion has flowed through the NT economy as a result of Project activity to date.

The total Western Australian (WA) cumulative commitment value for Ichthys Project construction from 2012 to 2018 was nearly \$9 billion.

Community contribution

Since 2012, INPEX and the INPEX-operated Ichthys LNG Project have funded more than \$4.5 million in community programs in Australia and invested more than \$9 million to support the development of training and education institutions in the NT.

Approximately 70 per cent of community sponsorship and investment funding has supported initiatives taking place in Darwin and across the NT. Community programs have also been sponsored in Perth and the Kimberley region in WA.

In 2019 to date, INPEX and Ichthys LNG have committed more than \$500,000 to support almost 50 community programs.

In November 2018 INPEX signed an agreement with the Larrakia people valued at \$24 million to establish the Larrakia Ichthys LNG Foundation Trust (Trust). The Trust is the first time a benefits agreement between an Aboriginal traditional owner group and a business entity was formed outside of native title obligations. It will provide further benefits to the Darwin Aboriginal community over the next 40 years.

International best practice

As a global company, INPEX works within international frameworks to strengthen the social and economic impact of our operations. INPEX is listed on global ESG indices, FTSE4Good and MSCI Global Sustainability, and strives to continuously improve its ESG performance. This is in addition to our compliance with Australian standards and regulations to maximise the benefits to local people.

INPEX has been a part of the Extractive Industries Transparency Initiative (EITI) since October 2012, working closely with governments, companies and civil society to promote transparency. EITI monitors and reconciles the payments made by companies to government and government to communities., INPEX is helping improve governance, reduce corruption and promote economic growth through stronger accountability and transparency required by EITI.

INPEX supports global standards relating to human rights, such as the International Bill of Human Rights, the International Labor Standards of the International Labor Organisation and the UN Guiding Principles on Business and Human Rights. In 2011, INPEX adopted the Ten Principles of the UN Global Compact, including areas relating to labour, environment and anti-corruption. INPEX is an active member of IPIECA, the global oil and gas industry association for environmental and social issues.

Contribution through taxation

One of the key areas of consideration when assessing the benefit to the public of national oil and gas reserves is the contributions made to overall taxation levels for a country.

We consider our tax payments a key part of INPEX's contribution to Australia. All INPEX companies and branch entities operating in Australia administer their tax compliance obligations in accordance with Australian tax law. From 2012 to 2017, INPEX companies and branch entities contributed a total of \$706 million in tax payments in Australia despite Ichthys LNG being in the construction phase.

Ichthys LNG is one year into its operating life of 40 years and where revenue is derived. It follows that over time, as production ramps up to full capacity and carry forward tax losses generated during the construction phase are utilised, the taxation payments and direct economic contribution to the Australian Government will increase. For projects within the oil and gas operating environment, the ultimate levels of taxation paid depend on the international oil price at the time of the sale of the products produced. The higher the oil price, the higher the ultimate returns to the Government in taxation.

To maximise the benefit to the public of the nation's oil and gas reserves requires companies to be able to economically locate and develop available reserves. Stable policy settings support this, including the economic settings required for an investment to be competitive. Globally, the trend is to lower the headline rate of company taxation thereby improving the net present value (NPV) of a project. A lower headline rate would help Australia compete against projects elsewhere in the world vying for the same capital allocation. Australia may wish to consider lowering the corporate tax rate as part of its efforts to attract investment in oil and gas projects.

The Petroleum Resource Rent Tax (PRRT) structure, before recent modifications, encouraged investment in Australian offshore oil and gas projects that might not otherwise have proceeded. The investing parties and the Australian community were aligned to the profitability of the project to receive a positive dividend. The significant amounts of foreign investment during the recent LNG boom highlighted that companies are prepared to back Australian oil and gas projects. Significant effort has been invested by the current and previous governments, to ensure that Australia operates within a resources tax regime which maximises the return to the Australian community while encouraging ongoing investment and growth in the sector. The outcomes of the 2017 Callaghan Review support the view that Australia's PRRT regime delivers on these objectives while providing a stable fiscal environment for investors. INPEX strongly encourages stability in the PRRT rules. Stable policy settings, including PRRT, are particularly important given the long timeframes and massive investment required to develop oil and gas projects.

The PRRT, by design, results in payments when 'above normal' profits on oil and gas projects arise. Adjustments to augmentation were made by the Government following the Callaghan Review. This recalibrated the speed to which above normal profits will be achieved in a project for which PRRT would become payable. This change applied to existing projects, including Ichthys LNG. A review on the Gas Transfer Price for integrated gas projects is currently underway. Additional retrospective changes to the rules would erode investor confidence and is potentially detrimental to future investment decisions.

With a 40 per cent rate of tax once payable, the PRRT regime allows investors to recover the costs of their investment. This concept is a founding principle of both the PRRT and other global fiscal systems for special tax regimes on oil and gas projects. It is important to recognise that the current cohort of LNG projects in Australia are nearly all in the early stage of operations. Given that it will likely take some time to recover the significant capital invested, it should come as a surprise to no one that PRRT does not get paid immediately upon the commencement of production. As with other fiscal regimes, once the investment is recovered, projects pay PRRT until the end of their operational lives.

One way to maximise the benefit to the public of national oil and gas reserves would be to attract more oil and gas investment to the country. This would expand tax revenue by increasing the revenue base rather than by increasing the tax burden on existing projects.

Over time, attracting additional investment to oil and gas projects in Australia will result in the income tax and PRRT systems delivering significant benefits for Australians for generations to come.

The APPEA submission covers in some detail why some other regimes capture higher taxation payments in earlier years, and we refer the Committee to that submission.

Maintaining international competitiveness

The contribution of the oil and gas sector to date is significant. Future investment in the sector will be important for the Australian public to continue to benefit.

Capital in the oil and gas sector is globally mobile and is invested where it can deliver the best outcomes for shareholders. A multinational corporation will likely have more projects under evaluation across the globe than it has the resources to invest.

The long-term fundamentals for global and regional gas/LNG demand are strong. This is illustrated by the recent significant increase in LNG demand from China, as part of its efforts to lower greenhouse gas emissions. Geographically, Australia is well placed to capitalise on this long-term demand. It is strengthened by the nation's relative economic and political stability, but Australia's competitiveness is not guaranteed.

The emergence of new natural gas sources, particularly in North America and East Africa, has created increased competition to meet growing global energy needs. The most significant challenge to the growth of Australia's natural gas industry is a high cost business environment that reduces the country's international competitiveness.

Imposing additional compliance costs on the Australian LNG sector will give Australia's competitors in LNG production, including Qatar, Malaysia, Russia, Indonesia, the United States and others, an advantage over Australia.

We note that no Australian LNG projects have been sanctioned since 2013. By contracts, projects in the United States, Canada, Russia, West Africa, Mozambique, Malaysia and Indonesia have all moved into development in that same period.

Further, we note that Australia's significant petroleum reserves are predominantly located in remote deepwater locations and require high capital expenditure on infrastructure to develop. This adds a higher degree of project cost and risk. In comparison, petroleum

reserves in countries against which Australia is competing for foreign investment can be produced at much lower cost due to resource location and cost of labour, among other factors.

Ensuring stable and consistent policy settings

The provision of certainty in policy direction and a stable regulatory framework is where the Government can have the most significant impact on stronger investment—and, in turn, secure ongoing benefits of oil and gas reserves for the Australian public.

As a general comment, INPEX's experience is that consistently clear decisions and trajectory in policy development provide a high level of confidence for potential investors and lowers the risk associated with investments. For a 40-plus year project like Ichthys LNG, it is difficult to adjust the commercial parameters in reaction to unforeseen policy decisions, and this can result in a downward revision in project economics. Such practices can dampen investment by creating a higher risk hurdle for future decisions.

We acknowledge policy settings need to change and develop over time. But to encourage new long-term business investment, we suggest such changes be prospective, not retrospective. Where there is the potential for decisions to have an impact on an existing project, the Government may wish to consider allowing for grandfathering provisions to instil a sense of confidence in prospective investors in Australia.

We note that adequate lead-in times granted by the Government to meet new requirements can also support large projects. This would enable companies to adjust their systems and processes to accommodate policy changes without undue operational disruption and high transaction costs. Coordination and clear points of contact across government agencies—state and federal—also assist companies to accommodate changes in policy in a timely way.

Conclusion

At this point in time, INPEX considers that the unique design of the operating regime for oil and gas companies operating in Australia is competitive by global standards, fair to the Australian community, and remains fit for purpose at a time when the industry is making decisions associated with the next phase of oil and gas investment in Australia.

We note that the present regime has underpinned Australia's emergence as a predominant player in natural gas production, significantly contributing to Australia's economy to the benefit of all Australians.