Chapter 1

Excise Legislation Amendment (Condensate) Bill 2008 and Excise Tariff Amendment (Condensate) Bill 2008

Reference

1.1 The Excise Legislation Amendment (Condensate) Bill 2008 and the Excise Tariff Amendment (Condensate) Bill 2008 were introduced into the House of Representatives on 15 May 2008. On 18 June 2008 the bills were referred to the Senate Economics Committee for report not before 26 August 2008, with particular reference to:

(a) the impact of the changes on retail prices of domestic gas and electricity in Western Australia, and any consequent effect on consumer prices;

(b) the impact of the decision on the industry generally and on the exploration for petroleum products in Australia; and

(c) the impact of the decision, and the decision-making process, on domestic and international investment confidence in Australia.

1.2 The terms of reference also stated that the committee must conduct hearings in Western Australia and hear evidence from, inter alia, industry bodies and joint venture partners on the North West Shelf.

Conduct of the inquiry and submissions

1.3 The committee advertised the inquiry on its website and in *The Australian* on 25 June 2008, calling for submissions by 7 July 2008. The committee also directly contacted a number of relevant organisations and individuals to notify them of the inquiry and to invite submissions and appearances before the committee. Three submissions were received as listed in Appendix 1. These appear on the committee's website.

1.4 The committee visited the North West Shelf Venture Karratha Gas Plant and Pluto LNG Project on 14 July 2008. Public hearings were held in Perth on 15 July 2008 and in Canberra on 11 August 2008. The witnesses are listed at Appendix 2.

Acknowledgement

1.5 The committee thanks all those who contributed to its inquiry by preparing written submissions and giving evidence at the hearings.

Purpose of the bills

1.6 The Excise Legislation Amendment (Condensate) Bill 2008, in conjunction with the Excise Tariff Amendment (Condensate) Bill 2008, remove the current exemption from excise of condensate produced in the North West Shelf project area and onshore areas. This measure was announced by the Treasurer on 13 May 2008[1] and applies to condensate produced from midnight on 13 May 2008.[2]

Excise Tariff Amendment (Condensate) Bill 2008

Provisions of the bill

1.7 The bill amends the *Excise Tariff Act 1921* to apply the crude oil excise regime to condensate produced in the North West Shelf project area and onshore Australia. This removes the current exemption of condensate from the crude oil regime.[3] It also introduces a new crude oil excise regime for production of condensate, equivalent to the regime applied to stabilised crude petroleum oil produced from petroleum fields discovered on or after 18 September 1975.[4]

1.8 The bill also makes amendments to ensure that production of condensate prior to the application of the bill (which is after midnight (by legal time in the Australian Capital Territory) on 13 May 2008) contributes to meeting the 4,767.3 megalitres (30 million barrels) threshold before the crude oil excise becomes payable.[5]

Excise Legislation Amendment (Condensate) Bill 2008

Provisions of the bill

1.9 The bill amends the *Excise Act 1901*, the *Petroleum Excise (Prices) Act 1987* and the *Petroleum Revenue Act 1985* to facilitate setting the condensate price for excise purposes.[6] These Acts are required to be read with the *Excise Tariff Act 1921*. The amendments made to the *Petroleum Excise (Prices) Act 1987* ensure the method for determining the price of condensate for calculating the crude oil excise payable in relation to the production of condensate is the same as the method for determining the price of stabilised crude petroleum oil. The amendments to the *Excise Act 1901* and the *Petroleum Revenue Act 1985* ensure consistency of the treatment of condensate with stabilised crude petroleum oil for the purposes of the crude oil excise.[7]

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1 *Budget Paper No.1*, 2008–09, pp 1–36.

2 Excise Tariff Amendment (Condensate) Bill 2008, *Second Reading Speech*.

3 *Revised Explanatory Memorandum*, p. 7.

4 *Revised Explanatory Memorandum*, p. 10.

5 *Revised Explanatory Memorandum*, pp 10–11.

6 *Revised Explanatory Memorandum*, p. 9.

7 *Revised Explanatory Memorandum*, p. 11.

Background

North West Shelf Venture project

1.10 The North West Shelf Venture (NWSV) is Australia's largest resource and infrastructure project with capital expenditure over almost three decades totalling $25 billion and with currently more than $10 billion in further capital investment either committed or under consideration. In 2007, the project accounted for 48 per cent of Australia's petroleum production (54 per cent of natural gas production and 39 per cent of oil, condensate and liquefied petroleum gas (LPG) production) and total indicative sales of approximately $11 billion.[8]

1.11 Based on huge gas and condensate fields on the North West Shelf of Western Australia, the Venture supplies natural gas to the domestic market in Western Australia, liquefied natural gas (LNG) to Japan and condensate, crude oil and LPG to other foreign markets. The NWSV comprises six multi-national companies, with each participant holding an equal share in future gas sales, subject to various joint venture arrangements. The participants are BP Developments Australia Ltd, Chevron Australia Pty Ltd, Japan Australia LNG (MIMI) Pty Ltd, Shell Development (Australia) Ltd, BHP Petroleum (North West Shelf) Pty Ltd, and Woodside Energy Ltd. Woodside is the operator of the project. Japan Australia LNG (MIMI) Pty Ltd is an investment vehicle of Mitsui and Mitsubishi.[9]

What is condensate?

1.12 Natural gas comes from three types of wells: oil wells, gas wells, and condensate wells. Natural gas that comes from oil wells is typically termed 'associated gas'. This gas can exist separate from oil in the formation (free gas), or dissolved in the crude oil (dissolved gas). Natural gas from gas and condensate wells, in which there is little or no crude oil, is termed 'nonassociated gas'. Gas wells typically produce raw natural gas by itself, while condensate wells produce free natural gas along with a semi-liquid hydrocarbon condensate.[10]

1.13 Condensate is a light crude oil extracted from so-called ‘wet’ gas, and is processed mainly to produce petrol. While some crude oil, technically called ‘stabilised crude petroleum oil’, is subject to excise, condensate has since the 1977–78 Commonwealth budget been excise-free.[11]

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8 North West Shelf Venture, *Submission 3*, p. 3.

9 Information available at: http://www.nwsg.com.au/sp-frameset.html?about/index.html, accessed on 25 June 2008.

10 Natural Gas.Org website, *Processing Natural Gas*, http://www.naturalgas.org/naturalgas/processing_ng.asp, accessed 30 June 2008.

11 Richard Webb, 'Excise Legislation Amendment (Condensate) Bill 2008', *Bills Digest No. 115*, 2007–08, Parliamentary Library, Canberra, Australia, 27 May 2008, p. 2.

Crude oil excise

1.14 Condensate is currently exempt from the crude oil excise. This exemption was introduced in 1977 to encourage the development of the LNG industry in the North West Shelf.[12]

1.15 The Excise Legislation Amendment (Condensate) Bill 2008, in conjunction with the Excise Tariff Amendment (Condensate) Bill 2008 ends the current exemption from excise of condensate produced in the North West Shelf project area and onshore areas, and applies the crude oil excise regime to condensate at the rates currently applied to crude oil produced from fields discovered after 18 September 1975.

1.16 Under these arrangements the top crude oil excise rate, which applies once annual production reaches just over five million barrels in a year, is 30 per cent.[13] Currently, the first 30 million barrels of crude oil produced from a field is exempt from crude oil excise.[14]

1.17 The bills introduce provisions to exempt from excise the first 30 million barrels of condensate produced from a field. Production of condensate from a petroleum field prior to midnight on 13 May 2008 will contribute towards meeting this threshold before the crude oil excise becomes payable.[15]

1.18 The Whitlam government introduced the crude oil excise in August 1975 to redistribute to the community, via the government, some of the gains oil producers received after world prices increased in 1973. In determining the level of excise, the then government sought to balance the return to the community against the need to ensure adequate incentives for exploration and production of oil. This was evident in the major changes to the excise rates which occurred on 23 October 1984.

1.19 Before this change, the rates depended on whether oil was classified as ‘old’ or ‘new’. Oil discovered before 18 September 1975 was classified as ‘old oil’ and ‘new oil’ was oil produced from naturally occurring discrete accumulations discovered on or after 18 September 1975. The purpose of the excise revisions of 23 October 1984 was to encourage the development of a number of old oilfields that had not been developed due to inadequate returns under the previous oil excise scale. Under a new 'intermediate' excise category, such oilfields became eligible for concessional treatment. The exemption of condensate from excise was introduced in 1977 in the context of international oil prices exceeding domestic prices.[16]

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12 Richard Webb, Excise Legislation Amendment (Condensate) Bill 2008, *Bills Digest No. 115*, 2007–08, Parliamentary Library, Canberra, Australia, 27 May 2008, p. 2.

13 Excise Tariff Amendment (Condensate) Bill 2008, *Second Reading Speech.*

14 Excise Tariff Amendment (Condensate) Bill 2008, *Revised Explanatory Memorandum*, p. 9.

15 Excise Tariff Amendment (Condensate) Bill 2008, *Second Reading Speech.*

16 Richard Webb, 'Excise Tariff Amendment (Condensate) Bill 2008', *Bills Digest No. 114* , 2007–08, Parliamentary Library, Canberra, Australia, 27 May 2008, p. 2.

Value of sales

1.20 The value of sales is known as VOLWARE (the volume-weighted average realised price). The rates of excise are:

- set as a percentage of VOLWARE;
- rise as the annual sales volume increases; and
- vary depending in whether the oil is old, new or intermediate.[17]

1.21 The current rates on new oil are set out in the following table[18] and these are the rates the bill proposes to apply to condensate.

Annual sales (megalitres)	**Percent of VOLWARE**
0 to 500	0
Over 500 to 600	10
Over 600 to 700	15
Over 700 to 800	20
Over 800	30

Compensation for reduction in royalties

1.22 Establishing an excise on condensate will result in reduced royalties payable to the Western Australia (WA) government because crude oil excise payments are a deductible expense for calculating the offshore petroleum royalty. The Commonwealth government has committed to providing compensation to the WA government of $80 million for reduced revenue in 2007–08, with payments in future years adjusted to equal the loss resulting from removing the condensate exemption on royalty payments to WA.[19] After accounting for these compensation payments, the Commonwealth government is expecting to receive a continuing net revenue gain of $2.5 billion over the five year period from 2007–08 to 2011–12.[20]

Submissions and other evidence

1.23 The committee received only a small number of submissions. The issues raised with the committee dealt mainly with the reasons for the measure with little

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17 Richard Webb, Excise Tariff Amendment (Condensate) Bill 2008, *Bills Digest No. 114*, 2007–08, Parliamentary Library, Canberra, Australia, 27 May 2008, p. 3.

18 Richard Webb, Excise Tariff Amendment (Condensate) Bill 2008, *Bills Digest No. 114*, 2007–08, Parliamentary Library, Canberra, Australia, 27 May 2008, p. 3.

19 Excise Tariff Amendment (Condensate) Bill 2008, *Second Reading Speech*.

20 Excise Tariff Amendment (Condensate) Bill 2008, *Revised Explanatory Memorandum*, p. 7.

reference to other provisions of the bills. This report therefore provides only a short description of the provisions, with terms of reference covered in chapters two and three. Chapter two outlines the reasons given for the introduction of the bill and support. Chapter three investigates the issues raised by industry and draws conclusions.