



Federal Pre-Budget Submission

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About CME

The Chamber of Minerals and Energy of Western Australia (CME) is the peak resources sector representative body in Western Australia. CME is funded by its member companies, which generate 95 per cent of the value of all mineral and energy production and employ 80 per cent of the resources sector workforce in the state.

The Western Australian resources sector is diverse and complex, covering exploration, processing, downstream value adding and refining of over 50 different types of mineral and energy resources.

In 2014-15, the value of Western Australia's mineral and petroleum production was \$99.5 billion. Iron ore accounted for approximately \$54 billion of production value to be the state's most valuable commodity. Petroleum products (including LNG, crude oil and condensate) followed at \$24 billion, with gold third at \$9 billion.¹

Notwithstanding the decline in the price of several export commodities, the estimated value of royalty receipts the state will receive from the resources sector is still to comprise over 16 per cent of estimated total state revenue in 2015-16, or around \$4.4 billion.²

As at September 2015, there was approximately \$171 billion in resources sector projects committed or under construction in Western Australia and a further \$110 billion in proposed or possible projects.³

Recommendations

Economic Competitiveness

- Internal government savings measures should again be prioritised in the 2016-17 budget.
- The growth in tax revenue due to bracket creep is not economically viable in the long term, will hinder broader growth and needs to be addressed as a priority in the tax white paper process.
- The government should maintain its focus on a predictable, transparent and stable fiscal regime to assist in attracting more projects to the resources sector development pipeline.
- The government must prioritise reducing the corporate tax rate to closer to average Organisation for Economic Cooperation and Development (OECD) levels as a key outcome of the tax white paper process.
- The 2016-17 budget should include provision for the review and expansion over time of the \$100 million credit cap for the Exploration Development Incentive (EDI).
- The government must maintain the current fuel tax credits and excise systems in the 2016-17 budget, and beyond, to ensure fairness and competitiveness for the resources sector.
- While there are no changes to the goods and services tax (GST) distribution method being progressed, ongoing interim grants for Western Australia should be budgeted in the 2016-17 budget and forward estimates.

¹ Department of Mines and Petroleum (DMP), *Western Australian Mineral and Petroleum Production Statistics Digest 2014-15*, 2015, p. 11.

² Government of Western Australia, *2015-16 Budget, Budget Paper No. 2 Volume 2*, www.ourstatebudget.wa.gov.au/Budget-Papers, pp. 541 & 593

³ DMP, 2015, *loc. cit.*

- The Treasurer should direct the Commonwealth Grants Commission to reconsider the distribution of GST revenue and the current horizontal fiscal equalisation (HFE) policy, moving instead to an equal per capita (EPC) distribution mechanism as a priority.
- Provision for the asset recycling initiative should be retained in the 2016-17 budget.
- The budget should retain provisions for co-funding arrangements with the State Government toward future development of new essential infrastructure for exports.
- The budget should retain provisions for co-funding arrangements for Western Australian projects identified in the *National Partnership Agreement on Land Transport Infrastructure Projects*.
- The government should release the final report of the Commonwealth Grants Commission's 2013 local government review and allow for transparent consideration of budget saving opportunities in local government grant funding.

Natural Resources

- The 2016-17 budget should include funding provisions for the Office of Environmental Protection Authority in Western Australia to execute its regulatory role under the agreements, rather than be reliant on introducing partial cost recovery mechanisms for matters of national environmental significance.
- The 2016-17 budget should therefore not include any provision for cost recovery for environmental regulation.
- Proposed reforms must not result in unintended consequences, such as longer timeframes for securing approvals, locking up land from exploration, and greater uncertainty, cost and regulatory burden for resources sector companies.

People and Communities

- The 2016-17 budget should include specific funding support for science, technology, engineering and mathematics (STEM) related programs in schools, including the industry-led STEM-WA initiative.
- Funding should be allocated and prioritised to further support the resources sector in its education, training and employment programs aimed at fostering sustainable participation of Aboriginal Australians in the workforce.
- The budget should include funding measures to ensure appropriate childcare support is in place to facilitate greater participation of women in the workforce.
- There should be no change to current fringe benefits tax arrangements given the adverse impact any changes will have on company costs and labour mobility.
- Workplace relations policy changes, as suggested by the Australian Mines and Metals Association (AMMA), should be implemented to deliver increased revenue to the budget.

Context

CME and the Western Australian resources sector

Throughout 2015 the Western Australian resources sector continued to undertake its significant shift from construction-led growth through to operational growth. As more projects commence operations, this will lead to a smaller overall workforce and greater overall exports.

With greater exports in the global market, not just from Western Australia but also from global competitors, the prices of several commodities has again fallen throughout 2015. Whether prices will continue to fall is uncertain; however, it appears likely the sector is now moving toward normalised, cyclical pricing patterns.

The decline in commodity prices has affected company returns, and State and Australian Government finances. It has also impacted employment across the sector, with the recent reduction in workforce numbers attributable to a combination of both companies' profitability and the transition of projects from the construction phase to the operations phase. However, as a result of investment over the past decade, the base level of employment in the sector remains more than double the level of a decade ago.

The contribution of Western Australia to the national economy remains strong. Western Australia's real gross state product (GSP) rose 5.5 per cent in 2013-14, following 4.6 per cent growth in 2012-13, and was above annual average growth of 4.9 per cent over the past ten years.⁴ GSP is forecast to continue to rise, albeit at smaller levels than previously in Western Australia, yet it is still forecast to be equal to, and in several years greater than, increases predicted nationally.

The total value of Western Australia's merchandise exports was \$110 billion in 2014-15, down 15 per cent on the previous year. However, exports grew in volume by nine per cent, well above annual average growth of five per cent over the past 10 years, with the state contributing 43 per cent of Australia's national merchandise exports in 2014-15.⁵

Western Australia also dominates Australia's exports to major trading partners, accounting for 68 per cent of exports to China, 47 per cent of exports to Japan and 46 per cent of exports to Korea. These trade arrangements reflect the state's significance for both Australia and in the Asian region.⁶

While the 2014-15 value of Western Australia's resources sector of \$99.5 billion represents a fall of 19 per cent from 2013-14's record of \$122 billion, a weakening Australian dollar has helped offset falling commodity prices.⁷

While the total value of the sector has declined in line with commodity prices, the volume of exports has continued to increase across a number of commodities due to the considerable investment in resources sector projects over a long period of time. This includes increases in iron ore, petroleum, zinc, manganese and alumina.

Further, Western Australia's iron ore sales are forecast to rise by an annual average of 2.7 per cent to 799 million tonnes between 2014-15 and 2018-19. LNG sales are expected to grow from 20.4 million tonnes in 2014-15 to almost 50 million tonnes by 2017-18, assuming the Gorgon, Wheatstone and Prelude projects are operating at full capacity at this time and the North West Shelf maintains current levels of production.⁸

⁴ Department of State Development (DSD), *Economic Profile*, October 2015, p. 1

⁵ *Ibid*, p. 7

⁶ *Ibid*.

⁷ DMP, 2015, *loc. cit*.

⁸ DSD, 2015, *op. cit.*, pp. 5-6

As resources sector projects nearing the completion of construction in Western Australia begin producing, exports will continue delivering corporate taxes while maintaining a sustainable employment base in Western Australia. However, ongoing volatility with commodity prices will be a key determinant in the future growth and expansion of the sector.

Unfortunately, when considering the comparatively short list of proposed projects and the declining exploration figures, it predicts a potentially worrisome outlook for continued growth and development of the resources sector in the short to medium term.

As such, CME has prepared this budget submission focussing on policies and funding measures which aim to generate growth, enhance productivity, reduce regulation and make Western Australia a more competitive place to do business.

The government's focus on deregulation, removal of environmental approval duplications and cutting red tape is welcome. However, this is only the start of the process, with ongoing reform needed to enable businesses to grow and reverse the trend of declining exploration and project proposals.

CME has supported the government's approach of budgeting reductions in 2015-16, with savings achieved from departmental reviews and consolidations. **Internal government savings measures should again be prioritised in the 2016-17 budget.** These and other savings measures are critical in 2016-17 if we are to see improvements to the overall conditions of the Australian economy in the short term.

It is only with ongoing investment in the Western Australian resources sector will Australia be able to capitalise on its natural advantages and continue to spread long term economic benefits to the nation.

Economic Competitiveness

Tax reform

Tax reform must be guided by the two core objectives of improving the competitiveness of Australia's tax system and the nation's growth potential, and establishing a more sustainable and stable revenue base. These objectives can and should be achieved in a way that supports fiscal repair over time and maintains a high level of equity in the tax system.

To that end, CME endorses the submission from the Minerals Council of Australia to the Australian Government's Re:think Tax discussion paper.

The absence of personal income tax cuts in recent years has resulted in a substantial expansion of tax receipts due to continuing bracket creep. Income tax receipts are projected to grow by 33 per cent between 2014-15 and 2018-19. **The growth in revenue due to bracket creep is not economically viable in the long term, will hinder broader growth and needs to be addressed as a priority in the tax white paper process.**

While the removal of the mining and carbon taxes has assisted in policy perceptions of Australia as a place to do business, Western Australia remains a high cost place for the resources sector to do business, and this perception has a significant impact on investment and growth of the sector.

In an industry which is increasingly globally integrated, there are many opportunities for projects. However current global market conditions mean capital remains scarce.

While CME supports Australia's existing anti-avoidance tax provisions, changes should only be enacted after consultation through the tax white paper process and in alignment with the OECD direction and action items. To act alone on transparency measures will undermine business confidence.

The government should maintain its focus on a predictable, transparent and stable fiscal regime to assist in attracting more projects to the resources sector development pipeline.

CME supports the government's election commitment of a 1.5 percentage point reduction in corporate tax rate in 2015. However, it is disappointed this will only impact businesses with turnover of less than \$2 million. A cut across the board in Australia's company tax rate would deliver economy wide benefits that are in the national interest. **The government must prioritise reducing the corporate tax rate to closer to average OECD levels as a key outcome of the tax white paper process.**

Exploration

Policies to advance exploration activities through incentives or credits benefit the nation by improving geological knowledge in remote and underexplored areas and by stimulating domestic investment in exploration companies that may otherwise have difficulty raising the required capital.

The commencement of the EDI this year is an important step towards stimulating critical investment in exploration activities. Without this ongoing investment in exploration, many resources would remain undiscovered, stifling the growth and prosperity of the sector and the economy into the future.

State Government modelling in Western Australia on its Exploration Incentive Scheme (EIS) found, in aggregate, for every \$1 million invested in the EIS the long run expected net benefit to the state in terms of higher GSP is \$23.7 million, showing the clear advantage received by the state for investment in resources exploration.⁹

CME considers the EDI should be broadened to include petroleum resources exploration expenditure, as well as mineral resources expenditure. This amendment would go a long way to ensure the reduction in petroleum exploration does not become as severe as the reduction witnessed in minerals exploration expenditure.

The 2016-17 budget should include provision for the review and expansion over time of the \$100 million credit cap for the EDI. With certainty and expansion of the cap, it is more likely industry will take up the EDI and the results witnessed with Western Australia's EIS will become more probable at a national level.

Fuel tax credits

CME acknowledges the government's regular confirmation there will be no departure from the wider regime whereby fuel tax credits partially or fully offset the excise on fuel used by businesses to produce goods and services. The credit scheme is based on the same tax principle underpinning the GST, which is to avoid taxes on business inputs which would distort investment and production decisions.

Mining is one of many business activities eligible for fuel tax credits. The credit scheme is important due to the heavy reliance of resources companies on diesel fuel as an input into operations, which are generally not undertaken on publicly funded roads.

Diesel accounts for up to one quarter of operating costs in some mines. Removing the offset would impose cost increases of four to seven per cent on typical minerals projects. While no tax is levied on fuel inputs in competitor nations such as the United States, Indonesia and Canada, to do so in Australia would have a detrimental effect.

When increasing the fuel tax excise in October 2014, the government's passing of legislation ensuring a corresponding increase in fuel tax credits to offset the excise increase (with indexing occurring again throughout 2015) was appreciated.

The government must maintain the current fuel tax credits and excise systems in the 2016-17 budget, and beyond, to ensure fairness and competitiveness for the resources sector.

⁹ ACIL Allen Consulting, *Economic Impact Assessment Exploration Incentive Scheme*, January 2015

Good and services tax distribution

In recent times, Western Australia has been a net donor of GST. This redistribution away from the state has come at the expense of timely and strategic State Government investment in infrastructure and services, such as roads, ports and town development to support Western Australia's economic growth now and into the future.

CME acknowledges the government's \$499 million GST infrastructure funding grant to Western Australia provided in the 2015-16 budget as GST replacement revenue. **While there are no changes to the GST distribution method being progressed, ongoing interim grants for Western Australia should be budgeted in the 2016-17 budget and forward estimates.**

Fiscal policy should reward productivity and economic growth. Under the current HFE policy, this is not the case. For example, if Western Australia reduces certain royalty rates, it could gain more in GST than it loses in royalty revenue, although to the detriment of other states.¹⁰

By delivering equitable government service delivery in every state, regardless of local economy and workforce participation, the HFE policy provides no incentive for people to move to areas of economic growth or for governments to enact policies to attract investment and encourage growth. This is a key concern for Western Australia's resource sector, which is still facing short term shortages of specialised, highly skilled labour that could potentially be eased through domestic migration.

The Treasurer should direct the Commonwealth Grants Commission to reconsider the distribution of GST revenue and the current HFE policy, moving instead to an EPC distribution mechanism as a priority.

CME also considers broader reform to the GST needs to be addressed as a priority in the taxation white paper.

Infrastructure

Due to current fiscal constraints, no individual level of government in Australia is able to fund all infrastructure necessary to support the nation's economic growth. Attracting private sector participants is therefore a critical enabler of financing future infrastructure needs.

Divestment of government owned assets provides another option for making capital available to fund new infrastructure. The Australian Government's asset recycling initiative provides an incentive to stimulate the benefits of divestment at state government level.

Provision for the asset recycling initiative should be retained in the 2016-17 budget.

Long term, transparent, coordinated planning and prioritisation of essential infrastructure needs is also important for prospective private sector investor confidence and preparedness for changes in economic conditions to ensure infrastructure is not barrier to future exports from new resources sector projects.

The budget should retain provisions for co-funding arrangements with the State Government toward future development of new essential infrastructure for exports.

Planning for transport to enable people to travel to workplaces, operations and maintenance components to travel to sites, and commodities to travel to market via the state's ports is also critical.

The budget should retain provisions for co-funding arrangements for Western Australian projects identified in the *National Partnership Agreement on Land Transport Infrastructure Projects*.

¹⁰ See commentary and analysis in State Government submission to the Commonwealth Grants Commission 2015 methodology review at: https://cgc.gov.au/index.php?option=com_attachments&task=download&id=1874

Local governments

Australian and State Government agencies have made substantial efforts toward cost reduction and improving efficiency. This objective does not appear to have flowed through to local governments in Western Australia. In many instances, local governments are seeking to significantly increase rates payable for resources sector companies by increasingly differentiating the rate for these companies.

The *Review into Improving the Impact of the Financial Assistance Grants on Local Government Financial Sustainability* terms of reference required the Commonwealth Grants Commission to investigate the benefits of tied grants and report to the Australian Government by the end of 2013.

Tied grants are a means of improving the effectiveness and efficiency of local government spending and could assist in delivering the focus on prudent financial decision making that is currently being prioritised at other levels of government. Updating the *Local Government (Financial Assistance) Act 1995* and greater oversight from the Treasurer in adopting or rejecting Commonwealth Grants Commission recommendations for financial assistance grants could also assist.

Unfortunately, the review report has not yet been publicly released. **The government should release the final report of the Commonwealth Grants Commission's 2013 local government review and allow for transparent consideration of budget saving opportunities in local government grant funding.**

Natural Resources

One stop shop agreement

The resources sector supports the Australian and State Government commitment to implementing a 'one stop shop' environmental assessment and approvals process.

The one stop shop will include the same high level of environmental protection, while minimising process duplication and delays between levels of government regulation. In establishing environmental assessment and approval bilateral agreements, the resources sector does not seek to remove or diminish environmental standards or safeguards. Instead the sector seeks to create a more streamlined process in meeting environmental outcomes and seeks to retain a high level of public confidence in the decision making process.

The implementation of the agreements will result in a significant increase in the workload of an already stretched Office of the Environmental Protection Authority in Western Australia. **The 2016-17 budget should include funding provisions made to the state agency to execute its regulatory roles under the agreements, rather than be reliant on introducing partial cost recovery mechanisms for matters of national environmental significance.**

The Australian Government's Department of the Environment introduced cost recovery for environmental impact assessments and some strategic assessments in October 2014. This was not supported by the resources sector. Cost recovery models should not be used to recover the costs incurred by the government in performing its mandated regulatory functions. Rather, its funding should be provided through the normal budgetary process. **The 2016-17 budget should therefore not include any provision for cost recovery for environmental regulation.**

Northern Australia

CME appreciates the government's announcement to establish a new \$5 billion Northern Australia Infrastructure Facility as part of the Developing Northern Australia White Paper.

Supporting infrastructure development in northern Australia is critical to develop new projects in remote areas through the provision of affordable energy and water, enabling efficient supply chains, and adequate port infrastructure.

Access to land is fundamental to the success of any resources sector project. The white paper includes an important government commitment to improve native title processes by resolving outstanding claims, reducing red tape and improving efficiency and certainty over access to land. These efforts to reduce the costs to do business in northern Australia will ensure the state's Pilbara and Kimberley regions remain attractive investment destinations for proponents of resources sector projects.

Proposed reforms must not result in unintended consequences, such as longer timeframes for securing approvals, locking up land from exploration, and greater uncertainty, cost and regulatory burden for resources sector companies.

People and Communities

Skilled workforce

As the Western Australian resources sector continues to transition from a construction phase to an operations phase, its workforce will need to be highly skilled, mobile and productive. These needs are compounded in an environment of ongoing maintenance requirements, higher technology operations, an ageing workforce and projected skills gaps.

The Australian Chief Scientist recently stated 75 per cent of the fastest growing occupations require STEM skills and knowledge.¹¹ Also, the Committee for Economic Development of Australia report into Australia's future workforce stated 40 per cent of Australian jobs existing today have a moderate to high likelihood of disappearing in the next 10 to 15 years due to technological advancements.¹² These statistics are stark evidence as to the importance of ensuring the Australian education sector has a clear focus on attracting students and educators to STEM disciplines.

The resources sector currently provides a major contribution to STEM related initiatives, such as Earth Science Western Australia (ESWA), which are critical for continuing to ensure the foundation for careers in the resources sector. CME has also recently supported the proposal for the pilot STEM-WA initiative, which is modelled on the ESWA experience. The initiative aims to actively engage all stakeholders in the reinvigoration of STEM education and is designed to raise teacher confidence and capability, and increase student participation and achievement.

The 2016-17 budget should include specific funding support for STEM related programs in schools, including the industry-led STEM-WA initiative.

Due to the ongoing automation of the resources sector, programs must prepare Aboriginal Australians for future higher technology employment opportunities in the resources sector beyond machine operator roles, which will decline over time. In particular, programs targeted at career development and leadership positions, not solely entry level positions, and programs to promote the growth of Aboriginal businesses are necessary for sustained economic development of Aboriginal people.

Funding should be allocated and prioritised to further support the resources sector in its education, training and employment programs aimed at fostering sustainable participation of Aboriginal Australians in the workforce.

¹¹ Chief Scientist, *Science, Technology, Engineering and Mathematics: Australia's Future*, September 2014, p.7

¹² Committee for Economic Development of Australia, *Australia's future workforce?*, June 2015, p.6

Gender diversity

The resources sector is also implementing measures to redress the gender imbalance in the workforce, including implementing flexible work practices, conducting gender pay gap audits and instigating programs to attract more women.

Access to childcare and parental leave arrangements are important initiatives for attracting women to the resources sector workforce. Sixty-five percent of companies in the Western Australian resources sector offer paid parental leave over and above legislated requirements. For these programs to be effective, they must be based on a solid government paid scheme to ensure returning to the workforce is an attractive proposition for women, not seen as duplicative.

The budget should include funding measures to ensure appropriate childcare support is in place to facilitate greater participation of women in the workforce.

Labour mobility

Labour mobility is an important part of the success of Australia's resources sector. Fly-in fly-out work arrangements and an effective skilled migration program provide the flexibility that allows Australia, particularly regional and remote areas in Western Australia, to secure major resources sector project investments.

Changes to remove exemptions for fly-in fly-out work arrangements will increase the cost for companies using these arrangements and be counter to the intent of the exemptions, which are to recognise certain goods and services are required as part of performing a role, rather than benefits of the role. In the case of the resources sector, any such changes would ultimately penalise industry growth, development and returns to governments and communities.

There should be no change to current fringe benefits tax arrangements given the adverse impact any changes will have on company costs and labour mobility.

Industrial relations

CME welcomes the ongoing Productivity Commission public inquiry into the Workplace Relations Framework. To drive organisations and an industry which can be competitive, the workplace relations system must foster innovation and employment opportunities, ensure confidence to investors to back new projects, feature clarity for all parties, and reflect the current and future needs of the economy.

At present, the cost of doing business in Australia is hampering further development for the resources sector. This is illustrated by Australian iron ore industry wages being 21 per cent higher than the global average, Australian resources construction wages rising 2.5 times the national average from 2001-12, and LNG production costs being 26 to 30 per cent higher than future competitor, Canada.¹³

Analysis undertaken by KPMG for AMMA indicates up to an additional \$30.9 billion in GDP for Australia could be earned if changes recommended by the resource industry are adopted.¹⁴ This would be generated as a result of productivity gains and an increase in investment in the sector. It does not include the flow-on benefits for other industries which could be also be generated due to these changes. **Workplace relations policy changes, as suggested by the AMMA, should be implemented to deliver increased revenue to the budget.**


¹³ KPMG, *Workplace Relations and the Competitiveness of the Australian Resources Sector*, 2015, pp. 8-9

¹⁴ *Ibid*, p. 14

Conclusion

CME looks forward to your response to this submission and ongoing engagement across the government on these important issues to ensure the success and viability of the resources sector and, in turn, both the Western Australian and Australian economies.

Should you have any questions regarding the issues raised in this submission, please contact Ms Nicole Roocke, Deputy Chief Executive, on 08 9220 8513 or n.roocke@cmewa.com.

Authorised by	Position	Date	Signed
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