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Inquiry into the privatisation of state and territory assets and new infrastructure

Senate Standing Committee on Economics

Contact
Andrew Winter
a.winter@cmewa.com

The Chamber of Minerals and Energy of Western Australia Level 10, 2 Mill Street, Perth, Western Australia
Locked Bag N984, Perth WA 6844 **p** +61 8 9220 8500 **f** +61 8 9221 3701 **e** chamber@cmewa.com **w** cmewa.com

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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 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 2013-14, the value of Western Australia's mineral and petroleum production was $121.6 billion, accounting for 91 per cent of the state's total merchandise exports. Furthermore, the value of royalties received by the Western Australian government from the resources sector increased by 33 per cent from the 2012-13 financial year to reach a record $6.98 billion in 2013-14.

Recommendations

Long term planning and evaluation of projects

- A coordinated interface for planning and funding of infrastructure between all levels of government, and across agencies within the same level of government, should be developed.
- The federal government should consider how it can incentivise state governments to develop state infrastructure plans which should be collaboratively developed by the government and private sector, and include prioritisation of the state's economic and infrastructure needs.
- The federal government should consider how it can assist states to establish an state arm's length body to advise on infrastructure strategies and improve the level of coordination between the government and private sector for longer term infrastructure planning.
- The state government's strategic asset review is supported by CME; however, this should be undertaken in consultation with industry.
- Capital recycling should be used as a means of developing the state's infrastructure requirements.

Increasing and deepening the competitive market for infrastructure provision and funding in Australia

- Where a project has broader economic benefits, but is unlikely to be financially viable for private investors, hybrid and alternative funding models should be considered to support the project's development.
- An unsolicited proposal process should be established to encourage the private sector to approach government with innovative solutions to fund infrastructure.

Taxation treatment of upfront contributions

- The government and resources sector should work collaboratively to consider alternative commercial solutions to mitigate the tax impost associated with resources sector companies contributing towards the cost of state-owned infrastructure.
- CME considers any incentives provided by government for future asset sales needs to be excluded from the GST distribution process.

Context

Long term planning and evaluation of projects

Good practice governance principles and reforms to institutional arrangements would assist in promoting efficiencies in long term planning, provision, financing and funding of infrastructure. To improve long term planning and to deal with infrastructure challenges in the state, CME's Investment in Resources Sector Infrastructure report[1] recommended:

- infrastructure plans and a project pipeline be developed;
- an economic infrastructure unit be established;
- blended project delivery teams be used;
- the Western Australian state government's asset review be undertaken in consultation with industry; and
- capital recycling be facilitated.

Independent infrastructure planning

Long term, coordinated infrastructure planning frameworks are important for addressing the nation's infrastructure requirements. There is a range of infrastructure planning delivery models within the states and territories, as well as at the national level through Infrastructure Australia. Without coordinated planning and identification of jurisdictional infrastructure needs, ad hoc approaches to infrastructure development and delivery will continue. Ideally bi-partisan and support across different levels of government should be sought for infrastructure development and delivery.

A coordinated interface for planning and funding of infrastructure between all levels of government, and across agencies within the same level of government, should be developed.

Long term, coordinated planning around infrastructure requirements can help avoid duplication and delays, ensuring state infrastructure needs are met at an efficient cost. In Western Australia there are recent advances in the state's infrastructure related planning, evidenced by the State Planning Strategy, the Regional Freight Network Transport Plan and draft State Aviation Strategy. However, there still remains a shortage of detailed planning across asset classes, and implementation of existing plans.

Coordination of planning across all levels of government and amongst agencies needs to be improved. For example, in Western Australia there are several regional planning and infrastructure documents such as regional blueprints, planning and infrastructure frameworks, and strategic plans, currently being developed by the Department of Planning, the state's Regional Development Commissions and Regional Development Australia. There is a lack of clarity on the uses of, and linkages between, these documents. The documents appear to duplicate effort, potentially resulting in conflicting views amongst agencies as to the intent of the plans, 'buy in' to implement the plans, and therefore failing to deliver outcomes over the longer term.

The federal government should consider how it can incentivise state governments to develop state infrastructure plans which should be collaboratively developed by the government and private sector, and include prioritisation of the state's economic and infrastructure needs.

Infrastructure providers have indicated several benefits that could result from the development and maintenance of a pipeline of priority projects, including:

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[1] CME & PwC, 2014, *Investment in Resources Sector Infrastructure,* Perth, http://www.cmewa.com/UserDir/CMEPublications/140116-INF-FINAL%20designer%20report-v0602.pdf.

- assisting construction companies and investors to prepare for priority infrastructure projects, thereby ensuring both strong delivery capability and strong competition;
- assisting resources sector companies to include access to shared infrastructure in their planning;
- aligning private sector and local government planning with the state government's priority projects; and
- better positioning the state for federal government support.

The federal government should consider how it can assist states to establish an arm's length body to advise on infrastructure strategies and improve the level of coordination between the government and private sector for longer term infrastructure planning.

The arm's length body would fill the gap in Western Australia's current planning and budget processes, and should work closely with Infrastructure Australia at the national level. Whereas projects within the four year government forward estimates period (the state government's budget outlook) receive significant attention from the Department of Treasury, projects proposed in five to ten years are typically not subject to detailed central scrutiny and coordination.

The benefits of establishing an independent body, responsible for long term infrastructure planning and coordination, include:

- improved collaboration between the various levels of government and the private sector to deliver strategic infrastructure planning;
- better decision making through a structured, evidence-based assessment of needs and priorities;
- greater sophistication in the way infrastructure is procured, financed and maintained; and
- the attraction of private investment through a clearly defined pipeline of projects.

State asset review in consultation with industry

The Western Australian state government's strategic asset review is supported by CME; however, this should be undertaken in consultation with industry.

As part of the review, consideration of future long term leasing or privatisation of assets should be accompanied by suitable contractual or legislative frameworks to prevent abuse of any monopolistic position. Timely access for all users at reasonable commercial rates must be enshrined in any lease or privatisation arrangement.

Capital recycling to develop infrastructure

Capital recycling should be used as a means of developing the state's infrastructure requirements.

Capital recycling can attract competition from a larger pool of capital by offering projects already established and operating. As some infrastructure investors, such as superannuation funds, do not accept construction risk, the pool for new projects can be narrowed. Focusing instead on proven projects with an established demand profile can alleviate this narrowing of the pool.

CME supports the federal Treasurer's announcement, on 28 March 2014, of an asset recycling initiative, which sees the federal government offer financial incentives to states that sell assets and recycle the proceeds of these sales into new, productive infrastructure. This will see a federal incentive of 15 per cent of the assessed value of the proposed asset being sold for capital recycling being provided to the state government. It is encouraging the state government is considering this offer as part of its asset review.

For Western Australia, the benefit of a capital recycling strategy is potentially greater than for other states given investment in new resources sector infrastructure is likely to stimulate additional royalty revenue through the development or expansion of resources sector projects. This will also create national benefits through increases in taxation and employment opportunities.

Increasing and deepening the competitive market for infrastructure provision and funding in Australia

Where a project has broader economic benefits, but is unlikely to be financially viable for private investors, hybrid and alternative funding models should be considered to support the project's development.

Hybrid and alternative funding models can assist to make a project financially viable, secure private finance and reduce the financial impact on governments. There are also alternative solutions where government packages existing revenues, or delays the transfer of demand risk, which can assist in developing projects without a long term impact on net debt.

There are four approaches enabling governments to support resources sector infrastructure that could be structured in a manner that avoids governments being exposed to the full debt impact over the life of a project. These approaches are:

- viability gap funding;
- minimum guarantees;
- existing revenue streams as a funding source;
- delaying demand risk transfer.

An unsolicited proposal process should be established to encourage the private sector to approach governments with innovative solutions to fund infrastructure.

The assessment of unsolicited proposals should be conducted in line with probity principles designed to maintain impartiality, accountability, transparency and confidentiality. The probity principles also relate to managing conflicts of interest and obtaining a value for money outcome.

Taxation treatment of upfront contributions

The taxation treatment of gifted assets creates a barrier to developing new infrastructure. In a number of cases resources sector companies have financed infrastructure improvements however, when gifting the asset to the state, companies are required to contribute beyond the cost of the asset in order to cover intra-government tax cash flows.

Capital contributions or gifted assets from resources sector companies creates a taxable income for the recipient of that asset equivalent to the arms length value of any monetary or non-monetary consideration, which is usually assessable at the time of receipt.

While state-owned entities are typically (but not in all instances) entitled to depreciation deductions over the life of the asset (typically 20 to 40 years depending on the type of asset), there is no matching revenue stream to cover the cost of the income tax liability. As a result some entities seek to recover the additional cost from the companies which financed the infrastructure initially to ensure the transaction is tax neutral. Further, the additional contribution is generally taxable to the recipient further increasing the tax cost of the gifted infrastructure to the state-owned entity.

The additional taxation impost can be managed through appropriate commercial structuring, and by working collaboratively with resources sector companies to evaluate alternative models for delivering infrastructure at the lowest cost.

The government and resources sector should work collaboratively to consider alternative commercial solutions to mitigate the tax impost associated with resources sector companies contributing towards the cost of state-owned infrastructure.

GST

Government will need to consider the equity impacts between states and territories arising from Commonwealth incentives for future asset sales and the interaction this has with the GST distribution process.

Western Australia is already heavily penalised for its economic success, receiving only 37 per cent of its equal per capita share of GST distributed back to the State. CME does not support GST distribution mechanisms that discourage the Western Australian Government from independently and efficiently managing their royalty regimes for fear of a reduced GST distribution share.

For example, it is imperative the Western Australian Government maintains a suite of policy instruments to effectively manage its economy; royalties can be adjusted to attract investment or to increase state revenue, to fund services and infrastructure. However, under the current interaction between state royalties and federal taxes, this policy is blunted for the key commodities of iron ore and coal.

Any government incentives for privatisation of assets will need to be evaluated in the context of GST distribution; will the incentives be included as state's own income? Does every state have the same capacity to earn this same revenue? Will the incentives be deemed specific grants outside of the distribution mechanism?

These and other questions will need to be resolved with consultation of the states prior to any recommendations being formed.

CME considers any incentives provided by government for future asset sales needs to be excluded from the GST distribution process.

CME will outline our arguments for why a greater return of GST to Western Australia is required for the benefit of all state in its submission to the Federation white paper process throughout 2015.

Conclusion

CME welcomes the Senate Standing Committee's inquiry into the privatisation of state and territory assets and new infrastructure and looks forward to ongoing engagement throughout the inquiry process.

If you have any further queries regarding the above matters, please do not hesitate to contact Andrew Winter, Manager – Infrastructure on (08) 9220 8525 or a.winter@cmewa.com.

Authorised by	**Position**	**Date**	**Signed**
Reg Howard-Smith	Chief Executive	29 January 2015	
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