



Auditor-General for Australia



31 October 2018

Senator Alex Gallacher
Chair
Senate Economics References Committee

By email: economics.sen@aph.gov.au

Dear Senator Gallacher

Australia's oil and gas reserves

The Australian National Audit Office (ANAO) has published the following performance audit report that you may find relevant to the inquiry into Australia's oil and gas reserves.

- Report No. 28 of 2016–17 [Collection of North West Shelf Royalty Revenue](#)

Information about what this audit assessed, concluded and recommended is attached. The audit report is available online at www.anao.gov.au.

Should the Committee require further information in relation to this matter, my office would be pleased to provide you with a briefing at a time convenient to you or appear as a witness at a hearing.

Yours sincerely

Grant Hehir

Report No.28 of 2016–17 *Collection of North West Shelf Royalty Revenue* assessed whether the Department of Industry, Innovation and Science had effectively and efficiently administered the collection of North West Shelf (NWS) royalty revenues. To form a conclusion against this objective, the ANAO assessed whether:

- the royalty collection framework, including the agreed administrative arrangements between the Australian Government and Western Australia, enabled efficient and effective administration;
- an adequate framework was in place for accurately calculating NWS petroleum production and sales; and
- the amounts subtracted from sales receipts to calculate the amounts of royalty payable were likely to be accurate and valid.

The audit concluded:

- The administration of the collection of NWS petroleum royalties by Department of Industry, Innovation and Science has not been sufficiently efficient or effective as the existing assurance arrangements do not effectively address key risks to the accurate calculation of royalty payable.
- NWS royalties are a considerable revenue source each year for both the Australian and Western Australian governments. But there is no formal agreement outlining the day-to-day roles and responsibilities of the respective departments involved in the collection of NWS royalty revenue. The Department of Industry, Innovation and Science also does not have a comprehensive procedure manual in place.
- There are some significant shortcomings in the framework for calculating NWS royalties. The consolidated Royalty Schedule, which governs those calculations, has not been updated in the last 10 years. In addition, the testing of the meters that are relied upon to identify production and allocate it to the appropriate field for royalty calculation purposes has not been sufficiently comprehensive or frequent.
- The amount of royalty paid is reduced by producers being permitted to claim significant deductions in areas such as operating costs and the depreciation of capital assets.¹ There has been limited scrutiny of the claimed deductions. Some errors in the claiming of deductions have been identified, but the available evidence indicates that the problems are much greater than has yet been quantified.

The ANAO recommended:

- The Department of Industry, Innovation and Science improve governance over the administration of the royalty calculation and collection function by:
 - a) implementing an appropriate accountability framework with the Western Australian Department of Mines and Petroleum that clearly sets out the roles and responsibilities of each party; and
 - b) developing a procedure manual that covers all aspects of its responsibilities in relation to the collection of North West Shelf royalties. This should include identifying the activities undertaken by the Western Australian Government that the department relies upon, and

¹ More than \$5 billion worth of deductions were claimed against petroleum revenues in the 18 months to December 2015.

the compliance and reporting procedures that are to be employed to oversee and be assured about the conduct of those activities.

- The Department of Industry, Innovation and Science, through the Joint Authority, set a timeline and regularly review progress against this timeline so as to expedite changes to the Royalty Schedule aimed at updating and improving the clarity of descriptions relating to deductible expenditure, and incorporating expenditure relating to new fields.
- The Department of Industry, Innovation and Science work with the Western Australian Department of Mines and Petroleum to implement improved controls for the verification of North West Shelf petroleum production and sales to provide increased assurance that the approach taken when allocating production to fields is complete and accurate.
- The Department of Industry, Innovation and Science work with the Western Australian Department of Mines and Petroleum to:
 - a) verify the validity of deductions claimed prior to 2014; and
 - b) develop and implement a comprehensive strategy for gaining a reasonable level of assurance that deductions claimed by the North West Shelf producers in 2015 and later years are valid and calculated in accordance with the Royalty Schedule.