

Submission to the Senate Select Committee on the Taxation of Gas Resources April 2026

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This short submission addresses several issues relevant to the Committee's terms of reference. It does not directly address all items.

Context

Because of energy supply disruptions caused by recent conflict in the Middle East, the prices of fluid fossil fuels have risen strongly. As a consequence, shareholders in multinational entities engaged in the extraction of Australian-sourced LNG have benefited from substantial windfall gains. These gains have come entirely from consumers, both domestic and foreign. On other occasions this century, resource price increases have come from surging demand, especially from Asian customers. These also generated windfall gains to shareholders in entities engaged in the extraction of Australian energy resources.

Global energy prices are notoriously volatile. Current prices are unlikely to be sustained. Yet they will rise again at some future time.

The energy resources generating windfall gains belong to the people of Australia, yet the people of Australia are big losers, forced to pay higher energy prices. The sole beneficiaries of higher energy prices are shareholders in multinational energy companies. Given that these companies are not state owned, as they would be in some other resource rich nations, the tax and transfer systems provide the only mechanisms to redistribute some part of the gains in favour of Australians. This was what motivated the Rudd Government's proposal, 16 years ago, to legislate a Resources Super Profits Tax (RSPT). We've had 16 years to learn the heavy cost of its defeat. But have we learned anything?

And the public policy issues go beyond the distributional. Resource security also matters. Here, too, Australian policy settings could benefit from the application of some basic economics. Australia sits among the top five fossil fuel exporters in the world, yet its leaders are perpetually concerned about gas shortages on the east coast of the country. Except for the domestic gas reservation policy operating in Western Australia, Australian policy settings appear geared to the maximisation of exports, with little to no value being placed on domestic energy security. Domestic users pay world prices, with no guarantee of supply, and are thus fully exposed to any and every international disturbance that impacts global energy supply chains, even in those products in which we are, from time to time, the world's largest exporter.

Climate impacts also matter. Australia is also one of the world's major exporters of carbon emissions. The carbon embedded in fossil fuel exports is about three times domestic net emissions from all sources. Australia accepts no responsibility for carbon emitted into the atmosphere when these fossil fuels are used by foreign customers. But there could be domestic economic advantage in doing so. Now would be a good time to consider available options.

The general principle here is that if a resource rich country relies upon foreign-owned, private capital to exploit those resources, then the tax system will have to play a major role in the achievement of distributional goals, resource security and climate policy. To date, the Australian tax system has achieved little in any of these areas.

Windfall gains are an ideal tax base

In markets featuring perfect competition, marginal investments will generate returns that just cover the opportunity cost of capital; that is, the highest return available from an alternative investment with similar risk characteristics. Windfall gains, supernormal profits and economic rents are forms of income above the opportunity cost of capital. They share a common feature: the level of income generating activity (measured in terms of output, employment or invested capital) is insensitive to the rate at which the excess returns are taxed. Thus, a tax rate of even 100 per cent applied to a windfall gain would have no impact on the underlying level of activity. Like land and anything else in perfectly inelastic supply, windfall gains present tax bases that offer tax revenue with no adverse consequences for economic efficiency. These constitute a special set of tax bases that avoid the oft-quoted maxim that the more you tax something, the less you have of it. Thus, taxing the windfall profits of gas producers would have no impact on gas supply. Neither would it affect prices paid by consumers. It would, therefore, have no impact on export contracts.

The socially optimal tax rate is approximately 100 per cent

Since a tax applied to windfall gains has no adverse economic efficiency consequences, the choice of tax rate is principally an equity, or distributional, matter. However, the use made of the additional tax revenue can also have important consequences for economic efficiency and future levels of economic activity. Thus, there is a 'double dividend' opportunity available.

Of course, some part of any windfall gains will be absorbed by existing state-imposed royalties and company tax. But this is the minor part. Given the composition of the share registers of the major gas producers, the principal beneficiaries of windfall gains are foreign shareholders. A windfall gains tax provides the Australian Parliament with the opportunity to decide how the windfall gains should be distributed among Australian residents, who are the owners of the natural resources from which the windfall gains have been derived.

In evaluating distributional options, consideration might be given to three dimensions: public debt management; nature repair; and boosting productivity. All three dimensions are highly significant for the living standards of future generations and thus offer the opportunity to address sources of intergenerational inequity.

Revenue raised from a windfall gains tax could be invested in a sovereign wealth fund for the benefit of future generations. But paying down public debt has much the same consequences. Since the burning of fossil fuels has been a major, and increasing, cause of nature loss, there is a strong case for using some of the proceeds of a windfall gains tax to undertake nature repair. And a windfall gains tax provides the opportunity to develop a broader tax reform package, including reforms to personal income tax rates and company tax, lifting flagging rates of productivity growth.

There are several tax design options available

If the size of the windfall gain is known (i.e., independently estimated), then it can be taxed simply at any determined rate. There are other options that avoid the need to estimate the size of the windfall gain and which are, therefore, well suited to the taxation of incomes prone to price volatility. These include a cashflow tax, a so-called 'Brown tax' (an example of which was the proposed Resources Super Profits Tax), an allowance for corporate equity (ACE) and an allowance for corporate capital (ACC). The principal design features of these various options are discussed in the tax review commissioned by the Rudd Government, *A Future Tax System*, published in 2010. All are designed to tax only supernormal profits, thus being economically neutral.

In each of these models, supernormal profits are revealed by the specific tax treatment accorded project expenses. Each model taxes windfall gains automatically. There is no need for independent estimation of the size of a windfall gain.

Thus, whilst there is an obvious case for levying a 'standalone' windfall gains tax on gas right now, it may be better to take the opportunity to develop one of the other options as an ongoing feature of the Australian tax system, recognising that there will be future shocks that also generate substantial supernormal profits, economic rents, and windfall gains for entities engaged in the extraction of Australia's gas reserves, and other stocks of Australian natural resources.

Taxing gas exports is another option

An alternative reform option is simply to levy a tax on gas exports. The tax could be applied on an ad valorem (per cent of value) or specific (\$ per unit of volume or weight) basis. One option presently being discussed is of the ad valorem type; specifically, a 25 per cent export tax. An alternative is to apply the export tax at a rate equivalent to the (shadow) price of carbon applying in the domestic economy. A sensible benchmark tax rate is the spot price of Australian Carbon Credit Units (ACCUs), expressed in \$ per tonne of embedded carbon. It would make sense to apply such a tax to fossil fuel exports of all types, including thermal coal. Levied at the current spot price of ACCUs, the tax would raise tens of billions of dollars of additional tax revenue annually.

An export tax would not be neutral in its economic impact, however. Over time, because it exempts domestic sales, it would redirect some part of exports to the domestic market. And it would reduce the domestic prices of both gas and thermal coal below their world prices. The larger the tax rate, the bigger the gap between world prices and domestic prices. Thus, an export tax has some of the same impacts as the more interventionist policy of domestic reservation. Unlike domestic reservation, however, it has the advantage of raising substantial amounts of revenue for the budget.

Despite their favouring domestic supply over export, an export tax would not introduce any additional obstacle to the Australia Government's ability to direct supply to particular export markets if it considered that necessary for strategic reasons.

Self-serving claims of elevated 'sovereign risk' and a freeze in investment should be ignored

Any proposal to generate more tax revenue from windfall gains accruing to foreign owners of capital will draw self-serving criticism from those supplying the capital, for the most part, the CEOs of multinational corporations. Invariably, it will be asserted that the proposal elevates 'sovereign risk'. The precise nature of the risk will not be explained. But it will be asserted that its elevation raises the cost to the Australian economy of foreign sourced capital, that there will be less foreign investment, and less foreign investment means lower productivity.

These assertions are self-serving and, in respect of proposals to tax windfall gains, reveal a lack of understanding of basic economic principles. Any investment proposal that at least meets its cost of capital in the absence of a windfall gains tax, or any of the other options for taxing supernormal profits, will still do so in the presence of such a tax. For those with an understanding of economics, this is merely a tautology.

What, then, should be made of claims of elevated sovereign risk? Suppose a windfall tax of, say, 25 per cent is applied. What, precisely, is the increment to sovereign risk? Is it that the tax rate might be lifted, at some future time? If so, then the remedy is obvious. Apply the tax at the rate of 100 per cent from day one. As noted earlier, because a windfall tax does not apply to that part of the return on capital that covers its opportunity cost, it has no impact on the volume of capital invested,

whether the rate is 25 per cent or 100 per cent. If the higher rate carries less sovereign risk, then it should be preferred.

If the sovereign risk is, rather, that the Australian Parliament might from time to time, and quite unexpectedly, make laws that are in the national interest, then this is obviously a risk premium worth paying. Avoiding reforms that are in the national interest merely in the hope of securing a lower risk premium on foreign sourced capital makes no sense.