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Business Tax Working Group Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

Via email: BTWG@treasury.gov.au

Dear Mr Jordan

Submission on Business Tax Working Group (BTWG) Discussion Paper

BP welcomes the opportunity to contribute to the consultation on how Australia's business tax system can be improved to help promote equity, efficiency and investment. BP has undertaken a thorough review of the BTWG's discussion paper, including the impacts that the identified "offsets" would have on our business and makes the following comments.

Scope of review

First, the scope of review (to identify incentives or distortions ("offsets") within the business tax system that can be abolished to fund a company income tax cut) is too limited to have any real positive impact on economic growth or investment. BP believes that a wider community debate is necessary about the tax system as a whole to ensure that the changes made are appropriate. Specifically, we would encourage debate around what structural tax mix changes are necessary to create a tax system that meets the unique domestic challenges of Australia's Federal and State Governments. The Henry Review, a valuable attempt to commence the debate but which appears at risk of stalling, should not be forgotten. It is critical to consider changes to the rate and base on which the GST is levied, and the removal of inefficient State taxes. This would enable genuine reform of the tax system as a whole to deliver international competitiveness and to continue to attract foreign direct investment whilst at the same time meet the revenue needs of all levels of Government. The scope of the present BTWG review, whilst narrow, also poses significant risk to investment in the oil and gas sector which is not in Australia's national interest.

Second, and of most concern to BP, the terms of reference require the BTWG to make recommendations to meet a stated objective that is not based on sound economic analysis. To illustrate, the terms of reference cited in the discussion paper include;

"make recommendations on how the business tax system can be improved to make the most of the challenges and opportunities arising from transformations in the broader

economy, including the patchwork economy, and that aim to increase productivity while delivering relief to struggling businesses".¹

This premise is entirely inconsistent with long held and widely accepted objectives of business tax reform, that were perhaps best described up in the 2008 AFTS Consultation Paper as:

"Attracting investment to Australia, directed to activities with the greatest national return, will improve the returns to Australians from working and saving."²

In this regard BP rejects outright the notion that the objective of tax reform should be to dampen the allocative signals presented by the fundamentals of the economy. Rather for Australia our tax system should support our comparative advantage, wherever it exists, by seeking to allow economic fundamentals to be efficiently transmitted into investment signals whilst neither dampening nor exaggerating them. While we recognise some sectors of the economy face challenges, in aggregate Australia's economy needs to accommodate the expansion of growth sectors such as resources in order to underpin the long term prosperity of the nation. Therefore, changes which endeavour to provide relief to struggling business sectors risk our aggregate prosperity by failing to make the space for our current competitive advantages to flourish.

Importance of a robust capital allowance regime

BP is specifically concerned that amendments to the capital allowance regime proposed by the BTWG will restrain investment at a critical moment for the LNG sector. There are several major LNG projects at various stages of appraisal readying themselves for investment decision, and these are typically characterised by deep capital intensity, long flat revenue streams, high technology, reserve and market risks, and increasingly a series of (usually State-originated) regulatory risks that are restrictive (or could be seen as 'implicit taxes') on the sector such as domestic gas reservations, environmental offsets and local content requirements. In this overall context, it would be extremely retrograde for the deceleration of capital allowances to be imposed on the sector.

As evidenced by recent deferrals in major resource projects, investment in the resource sector appears to be slowing down due to weaker commodity prices and rising costs. Tax reform which defers our capital payback periods will continue this trend, particularly the removal of effective life caps on oil and gas plant.

Capital investment is subject to supply and demand like all other business decisions. While many projects are close to final investment decisions, deferral of decisions, may mean that available capital is invested in competing projects in other countries. This will reduce the ability of international companies to invest in Australia when the conditions for investment improve. In this sense, any deferral is a significant risk to actual investment.

BP also believes the window of opportunity for Australian conventional offshore LNG is now. Although not certain, we believe the rise of unconventional gas (particularly in the US), and conventional gas from East Africa, may in future years reduce our competitive advantage that we now have with conventional offshore LNG. Therefore, it is critical that Government not act to discourage investment in conventional offshore oil and gas at this important time.

¹ Business Tax Working Group Discussion Paper, 13 August 2012, Pg 1

² Australia's Future Tax System Consultation Paper, December 2008, Pg 123

Specifically, changes to the capital allowance regime, either to remove effective life caps for the oil and gas sector or to reduce the rate of depreciation, would put further pressure on the economics of marginal LNG projects and risk major investments that are approaching sanction. BP opposes any change to the rates of depreciation of oil and gas plant which are already anomalous when compared internationally with other tax systems benefitting from significant LNG activity.

Encouraging investment in the renewal of Australia's sovereign resource base

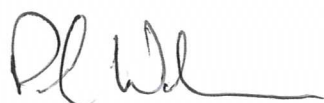
BP also notes that the treatment of exploration expenditure has been a trademark feature of Australia's tax system for decades and considers it vital to encourage further exploration activity, which underpins the renewal of Australia's sovereign resource base. With this in mind we would encourage ongoing consultation on the review of the definition of exploration expenditure, acknowledging the separate review which is occurring in tandem with the BTWG's review. In our view disputes with ATO are less likely if there is clarity on what is normal revenue expenditure of an exploration company, what is deductible capital exploration expenditure of an exploration company under the specific provisions, and what is other capital expenditure deductible over either the life of the field or life of plant. The tax treatment of exploration expenditure should reflect the major risks taken on by investors and whether enduring benefits are derived from such work. Without such investment and risk taking, developing Australia's resource base would never materialise.

Conclusion

As in previous submissions to Government, BP advocates stability of the business tax system and an end to ad-hoc reform in response to short term budgetary pressures. BP believes the Government should consider any BTWG's recommendation as part of a tax policy platform for the next Federal election and resist rushing amendments. Implementing material changes, within the business tax system alone, prior to the election would increase investor uncertainty at a time when major projects are approaching final investment decisions. Moreover, any material change on resources tax at a time when the window of opportunity for Australian conventional LNG investment is under threat would not be in Australia's national interest.

If you have any questions on this submission, please contact John Condon on 03 9268 3219 or myself.

Yours sincerely,



Paul Waterman

Cc Hon Wayne Swan MP, Treasurer and Deputy Prime Minister, Government of
Australia

Hon Martin Ferguson MP AO, Minister for Resources Energy and Tourism,
Government of Australia