

# Queensland Revenue Office

## Petroleum and Gas (Royalty) Regulation 2021

### Position Paper Determination of petroleum royalty rates

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## Relevant legislation

*Petroleum and Gas (Production and Safety) Act 2004* (PG Act)

Petroleum and Gas (Royalty) Regulation 2021 (the Regulation)<sup>1</sup>

## Purpose of paper

1. This paper provides guidance on the views of the Commissioner of State Revenue (the Commissioner) on the determination of petroleum royalty rates under the Regulation from 1 October 2020.

## Background

2. From 1 October 2020 petroleum royalty is payable on the volume of petroleum produced by a petroleum producer (producer) during a return period that is liable for petroleum royalty. The royalty payable by a producer is dependent on the type of petroleum produced and the basis on which the royalty rate is determined for the producer.
3. For calculating petroleum royalty liability for a producer for a royalty return period, there are therefore three principal matters to be determined:
  - (a) the total liable volume of petroleum produced by the producer during the period
  - (b) the classification of the liable volume of petroleum as domestic gas, supply gas, project gas or liquid petroleum
  - (c) the petroleum royalty rate applicable for each petroleum type.
4. This position paper addresses the determination of petroleum royalty rates.
5. Separate position papers have also been issued dealing with the measurement of petroleum, classification of petroleum and the application of Part 2 of the Regulation to swap arrangements.

## Preliminary issues

6. Unless a contrary intention appears, words and expressions used in this paper have the same meaning as in the PG Act and the Regulation.
7. A reference to the Regulation includes a reference to the equivalent provisions of the Petroleum and Gas (Royalty) Regulation 2004 as it was in effect following commencement of the *Royalty Legislation Amendment Act 2020* on 1 October 2020 and until its expiry on 31 August 2021. The *Taxation Administration Act 2001* (the Administration Act) also applies to the administration of petroleum royalty from 1 October 2020.

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<sup>1</sup> Prior to 1 September 2021, the Petroleum and Gas (Royalty) Regulation 2004 applied.

8. In this paper:

- (a) *petroleum type* means each of domestic gas, supply gas, project gas and liquid petroleum
- (b) *relevant sales* means, for each petroleum type, the following sales:

<b>Petroleum type</b>	<b>Relevant sales</b>
Domestic gas	All gas sold in the return period, either directly by the producer or indirectly by the producer through one or more resellers for the producer, to a person who is not an LNG project buyer
Supply gas	All gas sold in the return period, either directly by the producer or indirectly by the producer through one or more resellers for the producer, to a person who is an LNG project buyer
Project gas	All LNG sold in the return period by each member of the LNG project of which the producer is a member (the LNG project)
Liquid petroleum	All oil <sup>2</sup> sold in the return period, either directly by the producer or indirectly by the producer through one or more resellers for the producer

- (c) *relevant sales data* means, for each petroleum type, the following data in relation to relevant sales:

<b>Petroleum type</b>	<b>Relevant sales data</b>
Domestic gas	Where the purchaser is: <ul style="list-style-type: none"> <li>• an independent buyer—the volume of gas sold, and the revenue from that sale</li> <li>• not an independent buyer—the volume of gas sold</li> </ul>
Supply gas	Where the purchaser is: <ul style="list-style-type: none"> <li>• an independent buyer—the volume of gas sold, and the revenue from that sale</li> <li>• not an independent buyer—the volume of gas sold</li> </ul>
Project gas	Where the purchaser is: <ul style="list-style-type: none"> <li>• a person who is neither a member of the LNG project nor a relevant entity for a member of the LNG project (an unrelated buyer)—the volume of LNG sold, and the revenue from that sale</li> <li>• a person who is not an unrelated buyer (i.e. the person is either a member of the LNG project or a relevant entity for a member of the LNG project)—the volume of LNG sold</li> </ul>
Liquid petroleum	Where the purchaser is: <ul style="list-style-type: none"> <li>• an independent buyer—the volume of oil sold, and the revenue from that sale</li> <li>• not an independent buyer—the volume of oil sold</li> </ul>

- (d) *return period* means a royalty return period as defined in the PG Act.

<sup>2</sup> Oil is petroleum in a liquid state, and may include petroleum products such as condensate: s.5 of the Regulation.

## Legislative framework

9. The PG Act requires a producer to:
  - (a) pay petroleum royalty for petroleum that the producer produces<sup>3</sup>
  - (b) lodge royalty returns in relation to such petroleum.<sup>4</sup>
10. A producer includes:
  - (a) for petroleum produced from a petroleum tenure under the PG Act or the *Petroleum Act 1923* (the 1923 Act)<sup>5</sup>—the petroleum tenure holder who produces it or for whom it is produced
  - (b) for petroleum that is incidental coal seam gas mined under s.318CM of the *Mineral Resources Act 1989*—the coal or oil shale mining lease holder who mines it or for whom it is mined
  - (c) for petroleum that is coal seam gas mined under a mineral hydrocarbon mining lease—the coal or oil shale mining lease holder who mines it or for whom it is mined.<sup>6</sup>
11. A producer also includes a person who has applied to, and been approved by, the Commissioner to be taken to be a petroleum producer for petroleum royalty purposes in relation to a stated amount of petroleum produced as part of a particular petroleum operation.<sup>7</sup>
12. Petroleum is *produced* when it is:
  - (a) recovered to ground level from a natural underground reservoir in which it has been contained  
or
  - (b) released to ground level from a natural underground reservoir from which it is extracted.<sup>8</sup>
13. Petroleum royalty is calculated, and obligations such as royalty return lodgement are imposed, on the basis of petroleum operations, rather than on the basis of individual wells or petroleum tenures.<sup>9</sup>
14. Petroleum royalty for a petroleum operation is payable on the volume of petroleum produced by the producer from that petroleum operation during a return period that is not exempt from petroleum royalty.<sup>10</sup>
15. A different royalty rate applies to each petroleum type<sup>11</sup>, with the royalty rate being determined each return period.
16. Upon lodgement of a petroleum royalty return by a producer, an assessment of royalty and each related amount<sup>12</sup> is taken to have been made by the Commissioner for the amount that, on the basis of the information stated in the return, is the producer's liability.<sup>13</sup>

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<sup>3</sup> Section 590(1) of the PG Act

<sup>4</sup> Section 592A(1) of the PG Act

<sup>5</sup> An authority to prospect or a petroleum lease granted under the relevant Act: s.18(3) of the PG Act and s.2 of the 1923 Act (definition of '1923 Act petroleum tenure')

<sup>6</sup> Schedule 2 of the PG Act, definition of 'petroleum producer'

<sup>7</sup> Part 2, Division 6 of the Regulation

<sup>8</sup> Section 15(1) of the PG Act

<sup>9</sup> Lodgement on the basis of petroleum operations is pursuant to an administrative arrangement.

<sup>10</sup> Section 590 of the PG Act

<sup>11</sup> See *Classification of petroleum* discussion paper for further details on the petroleum types.

<sup>12</sup> Assessed interest, royalty civil penalty and royalty fee: Schedule 2 of the Administration Act (definition of 'tax')

<sup>13</sup> Section 14 of the Administration Act

## Royalty rate determination

17. The royalty rate applying to a particular petroleum type produced during a return period is calculated with reference to the *average sales price* for that petroleum type for the return period.<sup>14</sup>

### **Example 1**

ABC Co produces CSG, and calculates the average sales price for domestic gas for the March 2021 return period as being \$5.00/GJ.

Section 16 of the Regulation provides that, where the average sales price for domestic gas for a return period is more than \$3.00/GJ, but less than \$8.00/GJ, the royalty rate is 6 cents per gigajoule plus 0.08 cents per gigajoule for each 1 cent per gigajoule more than \$3.00/GJ.

The royalty rate for the domestic gas produced by ABC Co during the March 2021 return period is therefore \$0.22/GJ (i.e. 6 cents per gigajoule + ((500 cents – 300 cents) × 0.08 cents per gigajoule)).

18. For a particular petroleum type for a return period, the average sales price is either:
- (a) worked out with reference to a formula (the average sales price formula) which takes into account relevant sales data<sup>15</sup> (the formula method)
  - (b) equal to the benchmark price for the petroleum type for the return period<sup>16</sup> (the benchmark price method).
19. The formula method allows a producer to set an individual reference price for determining the royalty rate, rather than using a reference price established for the petroleum type using the benchmark price.
20. The formula method applies for determining the average sales price, unless one of the circumstances exists in which the benchmark price method applies instead. That is, a producer does not need to elect to use the formula method, but may elect not to use it, or be prevented from using it, in certain circumstances.
21. Subject to eligibility requirements, a producer may use different methods to determine the average sales price:
- (a) for each petroleum type produced from a particular petroleum operation in a return period (e.g. the formula method for domestic gas and the benchmark price method for supply gas)
  - (b) for the same petroleum type produced from different petroleum operations for which the producer is required to lodge royalty returns and pay petroleum royalty (e.g. the formula method for domestic gas produced from Operation 1, and the benchmark price method for domestic gas produced from Operation 2).
22. However, one method must be used for a particular petroleum type for a petroleum operation for a return period. For instance, if the formula method is used for domestic gas, all domestic gas produced by the producer in the period will be liable for royalty using the formula method for determining the petroleum royalty rate, and data in relation to all relevant sales must be used in the average sales price formula.

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<sup>14</sup> Sections 16 (domestic gas), 20 (supply gas), 25 (project gas) and 30 (liquid petroleum) of the Regulation

<sup>15</sup> Sections 17 (domestic gas), 21 (supply gas), 26 (project gas) and 31 (liquid petroleum) of the Regulation

<sup>16</sup> Sections 18 (domestic gas), 23 (supply gas), 28 (project gas) and 32 (liquid petroleum) of the Regulation

23. If there are multiple producers in a petroleum operation, the same method must be used by all of them for a particular petroleum type produced by the operation. For instance, if there are two producers who hold petroleum tenures that form part of the one operation for petroleum royalty purposes and they produce domestic gas, it is not possible for one producer to use the formula method for determining the average sales price for the gas it sells to independent buyers and the other producer to use the benchmark price for sales it makes through resellers where the resellers refuse to provide the required sales data for applying the formula method. In this case, the benchmark price would apply.
24. Where a petroleum tenure is held by two or more persons<sup>17</sup>, one of those persons (a co-owning producer) may request that the Commissioner treats the co-owning producer as having a separate petroleum operation from any other holder of that tenure (collectively, the other producers). The consequences of the co-owning producer have a separate operation would include:
- (a) the co-owning producer would be required to lodge a separate royalty return (in respect of its operation) to the other producers (in respect of their operation)
  - (b) in that separate return, the co-owning producer's use of method to determine the average sales price for a particular petroleum type for a return period for its operation would be unaffected by the method used by the other producers in the return for their operation for that petroleum type for that return period.

## Formula method

### Relevant sales

25. The average sales price formula determines the average sales price for a particular petroleum type produced by a producer during a particular return period by dividing the total revenue or deemed sales value from all relevant sales for that petroleum type during the return period (total sales revenue), by the total volume of product (gas, LNG or oil, as the case may be) sold in those sales (total sales volume).
26. The average sales price formula only takes into account petroleum or LNG that is sold—that is, petroleum or LNG that is not sold (for example, petroleum transferred for no consideration, flared or used) is not relevant for that formula. The royalty rate determined with reference to the average sales price calculated by the formula will be applied to the total volume of petroleum produced, including the amount that is not sold.

### **Example 2**

ABC Co produces CSG. ABC Co is not a member of an LNG project.

During the March 2021 return period, ABC Co:

- produces 800,000 GJ of gas
- sells 750,000 GJ of gas to independent buyers who are not LNG project buyers
- flares 10,000 GJ of gas.

The balance 40,000 GJ of gas is in storage at the end of the period.

In applying the formula method to determine the average sales price of domestic gas for the March 2021 return period, the relevant sales will only include the 750,000 GJ of gas sold. The royalty rate determined with reference to those sales will be applied to the 800,000 GJ of domestic gas produced during the return period (being the volumes sold, flared and stored).

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<sup>17</sup> See s.30A of the PG Act.

27. As the purpose of using the formula method is to calculate the average sales price based on relevant sales data to determine the applicable royalty rate, there is no requirement for any correlation between the volume of liable petroleum produced in a return period (which is liable for royalty) and the volume of product sold (which is only relevant for average sales price calculation purposes). In particular, as shown in the table in paragraph 8, the relevant sales for each petroleum type do not have regard to the timing or source of production, processing or purchase of the gas, LNG or oil. This means that the relevant sales for a petroleum type for a return period includes sales made in that period irrespective of whether:

- (a) for domestic gas, supply gas and liquid petroleum:
  - (i) the gas or oil is produced by the producer during the return period
  - (ii) the gas or oil is produced by the producer or by some other person (e.g. gas purchased by the producer and then re-sold)
  - (iii) the gas or oil was produced by the producer, or purchased by the producer or a reseller for the producer, prior to 1 October 2020
- (b) for project gas:
  - (i) the LNG is processed by the producer or a member of the LNG project during the return period
  - (ii) the LNG is processed by the producer, a member of the LNG project or some other person (e.g. LNG purchased by a member of the LNG project from a person outside the LNG project and then re-sold)
  - (iii) the gas that was processed into LNG was produced by the producer or some other person (e.g. feedstock gas purchased by a member of the LNG project from a person outside the LNG project, and then processed into LNG by that member)
  - (iv) the gas that was processed into LNG was produced by the producer, or was processed into LNG by the producer or a member of the LNG project, prior to 1 October 2020.

### **Example 3**

ABC Co produces CSG. ABC Co is not a member of an LNG project.

At the beginning of the March 2021 return period, ABC Co has 150,000 GJ of gas in storage that was produced in the December 2020 return period.

During the March 2021 return period, ABC Co:

- produces 800,000 GJ of gas
- sells 950,000 GJ of gas to independent buyers who are not LNG project buyers.

In applying the formula method to determine the average sales price of domestic gas for the March 2021 return period, the relevant sales will include all 950,000 GJ of gas sold (even though 150,000 GJ of that gas was produced in an earlier return period). The royalty rate determined with reference to those sales will be applied to the 800,000 GJ of gas produced during the return period.

### **Example 4**

Same facts as Example 3, but during the March 2021 return period ABC Co produces 700,000 GJ of gas and purchases 100,000 GJ.

In applying the formula method to determine the average sales price of domestic gas for the March 2021 return period, the relevant sales will include all 950,000 GJ of gas sold (even though 150,000 GJ of that gas was produced in an earlier return period, and 100,000 GJ of that gas was not produced by ABC Co at all). The royalty rate determined with reference to those sales will be applied to the 700,000 GJ of gas produced during the return period.

28. As it is a question of fact as to whether a particular sale occurred and whether it is a relevant sale, the formula method can only be used by a producer if the producer has the necessary data in relation to each relevant sale to appropriately reflect that sale in the average sales price formula. Where all necessary data is not available for making an assessment, the benchmark price method applies.<sup>18</sup>

### Resellers

29. The concept of a reseller is relevant for determining relevant sales for domestic gas, supply gas and liquid petroleum. The concept is not relevant for determining relevant sales for project gas.<sup>19</sup>
30. A reseller for a producer is a relevant entity for the producer that sells, or otherwise transfers ownership of, petroleum that is produced by the producer and owned by the reseller.<sup>20</sup>
31. The average sales price formula for domestic gas, supply gas and liquid petroleum takes into account sales by the producer directly to independent buyers, as well as sales by the producer to independent buyers through a reseller or a chain of resellers. To avoid potential distortion of the average sales price by counting sales volumes multiple times through successive sales of the same product, only the final sale by a reseller or chain of resellers is relevant for the average sales price formula.
32. In particular, for the purposes of applying the formula method:
- (a) a sale of gas or oil by the producer or a reseller for the producer to:
- (i) a relevant entity for the producer who is not a reseller for the producer<sup>21</sup> or
- (ii) an independent buyer
- is a relevant sale, and the volume and revenue<sup>22</sup> from such sales are therefore to be included in the average sales price formula
- (b) a sale of gas or oil by:
- (i) the producer to a reseller for the producer or
- (ii) a reseller for the producer to another reseller for the producer
- is not a relevant sale, and the volume and revenue from such sales are therefore not included in the average sales price formula.

### **Example 5**

ABC Co produces CSG. ABC Co is not a member of an LNG project.

During the March 2021 return period, ABC Co:

- produces 800,000 GJ of gas
- sells 500,000 GJ of gas directly to independent buyers who are not LNG project buyers
- sells 300,000 GJ to DEF Co, a relevant entity for ABC Co that was established during the period to act as a marketer.

During the return period, DEF Co sells the 300,000 GJ to GHI Co, an independent buyer who is not an LNG project buyer.

<sup>18</sup> See also the discussion commencing at paragraph 64.

<sup>19</sup> See the discussion commencing at paragraph 39.

<sup>20</sup> Schedule 1 of the Regulation (definition of 'reseller')

<sup>21</sup> See paragraph 33.

<sup>22</sup> Actual revenue for sales to independent buyers and deemed sales value for sales to persons who are not independent buyers



In ABC Co applying the formula method to determine the average sales price of domestic gas for the March 2021 return period, the relevant sales are:

- the 500,000 GJ of gas sold directly to independent buyers by ABC Co
- the 300,00 GJ of gas sold to GHI Co by DEF Co.

The 300,000 GJ of gas sold by ABC Co to DEF Co is not a relevant sale, as DEF Co is a reseller for ABC Co.

The royalty rate determined with reference to those sales will be applied to the 800,000 GJ of domestic gas produced during the return period.

### **Example 6**

Same facts as Example 5, but during the March 2021 return period, DEF Co only sells 200,000 GJ to GHI Co. The remaining 100,000 GJ that DEF Co purchased from ABC Co in that return period is sold to GHI Co in the June 2021 return period.

In ABC Co applying the formula method to determine the average sales price of domestic gas for the March 2021 return period, the relevant sales are:

- the 500,000 GJ of gas sold directly to independent buyers by ABC Co
- the 200,00 GJ of gas sold to GHI Co by DEF Co.

The 300,000 GJ of gas sold by ABC Co to DEF Co is not a relevant sale, as DEF Co is a reseller for ABC Co.

The royalty rate determined with reference to those sales will be applied to the 800,000 GJ of domestic gas produced during the return period.

The 100,000 GJ of gas sold to GHI Co by DEF Co in the June 2021 return period will be a relevant sale for the June 2021 return period if ABC Co applies the formula method in that period.

33. Whether a relevant entity for the producer is a reseller in relation to particular petroleum is a question of fact and must be determined having regard to the circumstances—that is, the producer/reseller relationship is determined in relation to each dealing between the parties, and it is possible for an entity to be a reseller in relation to only some of the petroleum it acquires from the producer. In particular, a relevant entity for a producer will not be a reseller in relation to petroleum produced by the producer where the entity:
- (a) purchases petroleum from the producer, but does not sell or otherwise transfer ownership of it (e.g. the entity uses the petroleum)<sup>23</sup>
- or
- (b) sells, or otherwise transfers ownership of, that petroleum as an agent of the producer (i.e. without taking title to the petroleum).
34. For a producer to apply the formula method, the producer will require relevant sales data in relation to sales made by a reseller. There is no legislative requirement for the reseller to provide such information to the producer, so it is a matter for the producer to ensure (contractually or otherwise) that it is able to obtain such information if it is to use the formula method.
35. Where a reseller for the producer sells both gas or oil sourced from a particular petroleum operation of the producer (operation product) and gas or oil sourced from:
- (a) one or more of the producer's other petroleum operations
- and/or
- (b) one or more other sources (e.g. another producer's petroleum operation)

only the data in relation to relevant sales of the operation product by the reseller will be relevant for determining the average sales price for petroleum produced from the particular operation.

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<sup>23</sup> In this case, the sale by the producer to the entity will be a relevant sale.

### **Example 7**

ABC Co produces CSG from two operations, Operation 1 and Operation 2. ABC Co is not a member of an LNG project.

During the March 2021 return period, ABC Co:

- produces 500,000 GJ of gas from Operation 1
- produces 300,000 GJ of gas from Operation 2
- sells all 800,000 GJ of gas from both operations to DEF Co, a relevant entity for ABC Co that acts as a marketer.

During the return period, DEF Co sells 600,000 GJ of gas to GHI Co, an independent buyer who is not an LNG project buyer. The remaining 200,000 GJ that DEF Co purchased from ABC Co in that return period is sold to GHI Co in the June 2021 return period.

DEF Co is able to determine that, of the 600,000 GJ of gas sold to GHI Co in the March 2021 return period, 400,000 GJ was sourced from Operation 1 and 200,000 GJ from Operation 2. DEF Co advised ABC Co accordingly on the first business day after the end of the return period.

In ABC Co applying the formula method to determine the average sales price of domestic gas for the March 2021 return period for Operation 1, the only relevant sales are the 400,000 GJ of gas sold by DEF Co to GHI Co sourced from that operation. The 500,000 GJ of gas sold by ABC Co to DEF Co from Operation 1 is not a relevant sale, as DEF Co is a reseller for ABC Co.

The royalty rate determined with reference to the relevant sales for Operation 1 will be applied to the 500,000 GJ of domestic gas produced from Operation 1 during the return period.

36. Where the reseller does not provide the producer with relevant sales data in relation to operation product sold by the reseller during a return period (whether because the reseller is unable to do so, or for some other reason), the producer will not have complete data in relation to all relevant sales during the period and will therefore be required to use the benchmark price method for all of the particular petroleum type for the return period—the average sales price formula cannot be used for any petroleum for which data is available.<sup>24</sup>
37. It is acknowledged there may be cases where arrangements between a producer and a relevant entity that purchases petroleum from the producer are such that the producer does not know with certainty what the relevant entity does with the petroleum after its purchase from the producer (e.g. whether a particular volume is on-sold or used). However, it is expected the producer would or should have sufficient knowledge of the relevant entity's circumstances to know whether or not, in the ordinary course of its business, it does resell some or all of the gas or oil that it purchases such that it may be expected to act as a reseller in some cases.
38. Where a relevant entity may be a reseller but the producer is unable to determine what gas or oil sold to it has been on-sold, or any details of those on-sales for a return period, the producer would be unable to provide with certainty all revenue and volume information required under sections 17, 21 or 31 of the Regulation. Accordingly, consistent with the policy intention of the volume model, the benchmark price will apply for the period for the relevant petroleum.

### **Example 8**

Same facts as Example 7, but DEF Co is unable to apportion the 600,000 GJ of gas sold to GHI Co between Operation 1 and Operation 2 and therefore does not provide ABC Co with details of the volume on-sold from Operation 1.

As ABC Co does not have details of any relevant sales by DEF Co, the average sales price formula cannot apply and the average sales price of the domestic gas produced from Operation 1 during the March 2021 return period must be determined using the benchmark price method.

39. As noted in paragraph 29, there is no concept of a reseller for project gas.
40. The following is taken into account for applying the average sales price formula for project gas:

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<sup>24</sup> See also the discussion commencing at paragraph 64.

- (a) the revenue and volume of all sales of LNG made during a return period by a member of the LNG project to a person who is neither a member of the LNG project nor a relevant entity
  - (b) the volume of all sales of LNG made during a return period by a member of the LNG project to a person who is either a member of the LNG project or a relevant entity.<sup>25</sup>
41. If an LNG project member sells LNG to a relevant entity that is not a member of the LNG project and the relevant entity then sells the LNG to an unrelated buyer, only the volume of LNG sold to the relevant entity is taken into account for the average sales price formula. The further sale to the unrelated buyer is irrelevant as the average sales price formula does not contemplate tracing through these sales to a final sale to an unrelated purchaser.
42. If on the other hand the relevant entity was a member of the LNG project as its role was to market the project's LNG to unrelated buyers, the revenue and volume of those sales of LNG made by the LNG project marketer to the unrelated purchasers may be used for determining the average sales price.

### **Example 9**

XYZ Co produces CSG. It is a member of the Alpha LNG project, together with UVW Co which sells LNG for the project and RST Co, a relevant entity for XYZ Co, which purchases LNG from the project for sale to unrelated buyers.

During the March 2021 return period:

- XYZ Co produces 200,000 GJ of CSG
- UVW Co sells 100,000 GJ of LNG to unrelated buyers for \$400,000
- UVW Co sells 75,000 GJ of LNG to RST for \$300,000
- RST Co sells all of the LNG purchased from UVW Co for \$350,000 to unrelated buyers.

In XYZ Co applying the formula method to determine the average sales price of project gas for the March 2021 return period:

- the actual revenue of \$400,000 and the volume of 100,000 GJ of LNG sold by UVW Co to unrelated buyers is included
- the actual revenue of \$350,000 and the volume of 75,000 GJ of LNG sold by RST Co to unrelated buyers is included
- the revenue of \$300,000 and the volume of 75,000 GJ of LNG sold by UVW Co to RST Co is not included, as the sale by RST Co is relevant for the average sales price formula in this instance.

The royalty rate determined with reference to those sales will be applied to the 200,000 GJ of project gas produced during the return period.

43. As is clear from section 26 of the Regulation, sales of gas made by a producer who is a member of an LNG project, whether directly or through a reseller, are not taken into account for determining the average sales price of project gas. Therefore, where such a producer sells gas to an LNG project buyer, neither the revenue from those sales nor the volume of gas sold is relevant for section 26. It is only the LNG sold by members of the LNG project that is relevant for determining the average sales price of the project gas produced.

### **Measuring relevant sales data—total sales revenue**

44. For a relevant sale made to an independent buyer, the average sales price formula uses (subject to paragraph 47) the actual revenue from that sale. For a relevant sale made to a person who is not an independent buyer, the average sales price formula instead uses the benchmark price as the basis of a deemed value for that sale, irrespective of whether the actual sale price was negotiated on an arm's length basis.

45. The deemed sales value of sales to persons who are not independent buyers or unrelated buyers for a return period is determined by multiplying the total volume sold in relevant sales to such persons in the period by the benchmark price for the particular petroleum type for the return period.<sup>26</sup> That is, a separate deemed sales value is not calculated for each individual sale to a person who is not an independent buyer or an unrelated buyer.
46. The total sales revenue for a particular petroleum type for a return period is:
- (a) for domestic gas, supply gas and liquid petroleum—the total revenue from all relevant sales in a return period to independent buyers, plus the deemed sales value of all relevant sales in a return period to persons who are not independent buyers
  - (b) for project gas—the total revenue from all relevant sales (i.e. sales of LNG by members of the LNG project, and not sales of gas) in a return period to unrelated buyers, plus the deemed sales value of all relevant sales (i.e. sales of LNG by members of the LNG project, and not sales of gas) in a return period to persons who are not unrelated buyers.<sup>27</sup>

### **Example 10**

ABC Co produces CSG. ABC Co is a member of the ABC LNG project.

During the March 2021 return period, ABC Co:

- produces 850,000 GJ of gas
- sells 50,000 GJ of gas at \$4/GJ (i.e. a total of \$200,000) to DEF Co, a relevant entity for ABC Co that is not an LNG project buyer, who uses the gas
- sells 500,000 GJ of gas to GHI Co, an independent buyer who is not an LNG project buyer, at \$5/GJ (i.e. a total of \$2,500,000)
- sells 250,000 GJ of gas to JKL Co, an independent buyer who is an LNG project buyer, at \$5.25/GJ (i.e. a total of \$1,312,500)
- has a balance of 50,000 GJ of gas in storage at the end of the period

During the March 2021 return period, the ABC LNG Project sells 1,000,000 GJ of LNG for \$7,000,000 to unrelated buyers.

As DEF Co uses the gas purchased from ABC Co, it is not a reseller for ABC Co in relation to the gas.

The benchmark price for domestic gas for the March 2021 return period is \$5/GJ.

In ABC Co applying the formula method to determine the average sales price of domestic gas for the March 2021 return period, the total sales revenue is \$2,750,000, being the sum of:

- the total revenue from all relevant sales to independent buyers (i.e. \$2,500,000 revenue from sales to GHI Co)
- the deemed sales value of all relevant sales to persons who are not independent buyers (i.e. \$250,000, being the volume of gas sold to DEF Co (50,000 GJ) multiplied by the benchmark price for domestic gas for the period (\$5/GJ)).

To determine the average sales price for domestic gas, this total revenue is divided by the total volume of gas sold to persons who are not LNG project buyers (i.e. 550,000 GJ).

In ABC Co applying the formula method to determine the average sales price of project gas for the March 2021 return period, the total sales revenue of LNG sold by LNG project members to persons who are neither members of the LNG project nor relevant entities for any member of the LNG project is \$7,000,000.

To determine the average sales price for project gas, this total revenue is divided by the total volume of LNG sold by members of the LNG project during the period (i.e. 1,000,000 GJ).

The revenue (\$1,312,500) and volume (250,000 GJ) relating to the sales of gas made to JKL Co is irrelevant for determining the average sales price of the project gas.

<sup>26</sup> Sections 17(2) (domestic gas), 21(2) (supply gas), 26(2) (project gas) and 31(2) (liquid petroleum) of the Regulation

<sup>27</sup> Sections 17(1) (domestic gas), 21(1) (supply gas), 26(1) (project gas) and 31(1) (liquid petroleum) of the Regulation

47. For the purposes of the average sales price formula, the revenue from a relevant sale to an independent buyer:
- (a) subject to paragraph 47(b), includes all amounts paid or payable by the purchaser in relation to the sale (including, but not limited to, transportation or other costs of the producer that are explicitly recovered from the purchaser in addition to the stated sales price), even if such amounts are invoiced separately
  - (b) does not include any amounts paid by a purchaser to a producer or a reseller for the producer on account of the recovery of the producer or reseller's liability for goods and services tax (GST) on taxable supplies made to the purchaser<sup>28</sup>—that is, the revenue is to be expressed on a GST-exclusive basis
  - (c) is not reduced by:
    - (i) any costs of the producer, or a reseller for the producer, in relation to the particular gas, LNG or oil (e.g. costs of production, processing or purchase)
    - (ii) any amount payable by the producer, or a reseller for the producer, to a purchaser, irrespective of whether the parties agree to offset such amounts against the amount payable to the producer or reseller
    - (iii) any amount invoiced by the producer, or a reseller for the producer, to a purchaser but not recovered from the purchaser (i.e. a bad debt).

### **Example 11**

ABC Co produces CSG. ABC Co is not a member of an LNG project.

During the March 2021 return period:

- ABC Co sells a total of 10,000 GJ of gas to GHI Co, an independent buyer, for \$5/GJ (excluding GST)
- ABC Co and GHI Co settle an existing commercial dispute on the basis that ABC Co will pay GHI Co \$20,000.

ABC Co and GHI Co agree to offset the \$20,000 settlement payment by ABC Co against the \$50,000 payable by GHI Co. Accordingly, it is agreed that GHI Co will only pay ABC Co \$30,000 for the gas purchased during the period.

GHI Co ultimately only pays ABC Co \$20,000 before GHI Co is wound up.

Despite the settlement agreement and the underpayment by GHI Co, the revenue from the sale of gas to GHI Co for the purposes of the average sales price formula is \$50,000.

48. Where gas, LNG or oil is sold in a currency other than Australian dollars, for the purposes of the average sales price formula the conversion of foreign currency into Australian dollars should use an exchange rate obtained from a consistent, reasonable external source. Examples of an exchange rate that is considered reasonable include:
- (a) the hedge settlement rate
  - (b) the WM/Reuters Australian Fix 4.00pm rate
  - (c) a rate published by a major Australian commercial bank or financial institution
  - (d) an exchange rate referred to in Schedule 2 of the Income Tax Assessment Regulations 1997 (Cwlth), subject to:
    - (i) any limitations contained in that Schedule in relation to the calculation or use of such exchange rate
    - (ii) the period selected for calculation of an average exchange rate being no longer than the return period.

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<sup>28</sup> See section 9-5 A New Tax System (Goods and Services Tax) Act 1999 (Cwlth).

## Measuring relevant sales data—total sales volume

49. The total sales volume for a particular petroleum type for a return period is:
- (a) for domestic gas, supply gas and liquid petroleum—the total volume sold in all relevant sales in the return period to independent buyers, plus the total volume sold in all relevant sales in the return period to persons who are not independent buyers
  - (b) for project gas—the total volume sold in all relevant sales (i.e. sales of LNG by members of the LNG project, and not sales of gas) to unrelated buyers, plus the total volume sold in all relevant sales (i.e. sales of LNG by members of the LNG project, and not sales of gas) to persons who are not unrelated buyers.<sup>29</sup>

### **Example 12**

Same facts as example 10.

In ABC Co applying the formula method to determine the average sales price of domestic gas for the March 2021 return period, the total sales volume is 550,000 GJ, being the sum of:

- the total volume of gas sold in all relevant sales to independent buyers (i.e. 500,000 GJ of gas sold to GHI Co)
- the total volume sold in all relevant sales to persons who are not independent buyers (i.e. 50,000 GJ of gas sold to DEF Co).

In ABC Co applying the formula method to determine the average sales price of project gas for the March 2021 return period, the total sales volume is 1,000,000 GJ of LNG, being the volume of LNG sold by members of the LNG project to unrelated buyers.

50. For the purposes of the average sales price formula, the volumes of:
- (a) gas and LNG sold in relevant sales are to be expressed in gigajoules
  - (b) oil sold in relevant sales is to be expressed in barrels.<sup>30</sup>
51. Where:
- (a) gas or LNG is sold in units other than gigajoules  
or
  - (b) oil is sold in units other than barrels
- the producer must:
- (c) convert the units into gigajoules or barrels (as appropriate) using a consistent, reasonable conversion factor each return period
  - (d) keep records to support the conversion.
52. As relevant sales involve the transfer of title to petroleum, the Commissioner expects that the measurement of the volume sold in each relevant sale should be verifiable by a meter that meets the error tolerances required by the PG Act and the Petroleum and Gas (General Provisions) Regulation 2017.

## Take or pay arrangements

53. A producer, or a reseller for the producer, may enter into an arrangement with a purchaser under which the purchaser agrees to purchase a stated quantity of gas, LNG or oil during one or more stated return periods, but the purchaser has the option of paying for but not taking delivery of some or all of that quantity each return period (a take or pay arrangement).

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<sup>29</sup> Sections 17(1) (domestic gas), 21(1) (supply gas), 26(1) (project gas) and 31(1) (liquid petroleum) of the Regulation

<sup>30</sup> Section 14 of the Regulation

54. For each return period, the volume and revenue or deemed sales value (as the case may be) of gas, LNG or oil sold under a take or pay arrangement in that period must be included in the average sales price formula, irrespective of whether or not the purchaser decides to take delivery of some or all of that volume in the period or a subsequent period.
55. If, under the take or pay arrangement, the purchaser can defer taking delivery of some or all of the volume for a particular return period until a subsequent return period, the volume and revenue or deemed sales value of such gas, LNG or oil:
- (a) must be included in the average sales price formula for the return period in which the purchaser was originally entitled to take it
  - (b) will not be included in the average sales price formula for the return period in which the purchaser ultimately takes it.
56. The positions described in paragraphs 54 and 55 affect only the calculation of the average sales price for each return period. They do not affect the volume of petroleum that is subject to royalty each return period.

### **Example 13**

ABC Co produces CSG. ABC Co is not a member of an LNG project.

On 1 January 2021, ABC Co enters into an agreement with GHI Co, an independent buyer who is not an LNG project buyer. Under that agreement:

- ABC Co agrees to sell GHI Co 50,000 GJ of gas each month until 31 December 2022 for \$5/GJ
- in any given month, GHI Co can decline to take some or all of the 50,000 GJ, but must pay ABC Co at the rate of \$5/GJ for any gas not taken
- any quantity of gas that GHI Co declines to take in a given month can be taken in a future month without additional payment in that future month.

During January, February and March 2021, GHI Co takes 45,000 GJ of gas each month pursuant to the agreement (i.e. GHI Co declines 5,000 GJ of gas each month). In April 2021, GHI Co takes the full 50,000 GJ of gas for that month, as well as the 15,000 GJ not previously taken in January, February and March 2021.

In ABC Co applying the formula method to determine the average sales price of domestic gas for the March 2021 return period, ABC Co will include the total volume (150,000 GJ) and revenue (\$750,000) from the sales to GHI Co, despite the fact that GHI Co only accepted 135,000 GJ of gas.

In ABC Co applying the formula method to determine the average sales price of domestic gas for the June 2021 return period, ABC will not include the additional 15,000 GJ of gas (nor any revenue in relation to it) supplied in April 2021.

## **Benchmark price method**

### General points

57. The benchmark price method will apply for determining the royalty rate for a return period (that is, the average sales price will be equal to the benchmark price) where:
- (a) an election made by the producer to use the benchmark price method is in effect
  - (b) the producer does not provide, for an assessment, the information required to work out the average sales price using the average sales price formula
  - (c) for domestic gas, supply gas or liquid petroleum—no relevant sales occur during the return period to an independent buyer (i.e. either there are no sales at all, or the only relevant sales are to persons who are not independent buyers)
  - (d) for project gas—no relevant sales occur during the return period to a person who is an unrelated buyer (i.e. either there are no sales at all, or the only relevant sales are to persons who are either a member of the LNG project or a relevant entity for a member of the LNG project)

- (e) the Commissioner considers it is appropriate, for the protection of the public revenue, for the benchmark price method to apply.<sup>31</sup>

#### Election by the producer

58. A producer may elect to use the benchmark price method to determine the average sales price for a particular petroleum type. An election (a *benchmark election*) will be effected by the producer in the royalty return for the return period.<sup>32</sup>
59. There are no pre-requisites to a producer making a benchmark election. In particular, the producer may make an election even where the benchmark price is lower than the average sales price would be if the formula method were to apply.
60. A benchmark election:
- (a) starts on the first day of the return period for the royalty return in which the election is made
  - (b) continues in effect for each subsequent return period unless and until the Commissioner ends the election.<sup>33</sup>
61. The Commissioner may only end an election:
- (a) following receipt of an application in the approved form by the producer<sup>34</sup>
  - (b) if the Commissioner considers it appropriate to do so, having regard to all the circumstances including, for example, the protection of the public revenue.<sup>35</sup>
62. The Commissioner must give the producer notice of the ending of an election, including the day on which the election ends (which may be a day before the day on which the producer made the application referred to in paragraph 61(a)).<sup>36</sup>
63. There is no minimum number of return periods for which a benchmark election must apply before the Commissioner may end it. However, in considering whether to end an election, the Commissioner will have regard to the principle underpinning the legislative framework that the election is not intended to be made return period by return period to reduce royalty liability.

#### Non-provision of information for the formula method

64. For a producer to use the formula method to calculate the average sales price in the royalty return for the return period, the producer must necessarily have complete relevant sales data (i.e. relevant sales data for all relevant sales made in the period) by the time the royalty return is lodged.
65. The Commissioner would generally expect that, where a relevant sale is made directly by the producer, the producer would have the relevant sales data in relation to that sale.
66. The Commissioner acknowledges that the producer may be reliant on other entities to provide it with details of relevant sales in situations such as the following:
- (a) in relation to domestic gas or supply gas—where gas is sold by an agent or a reseller for the producer
  - (b) in relation to project gas—where LNG is sold by an agent, or another member of the LNG project
  - (c) in relation to liquid petroleum—where oil is sold by an agent or a reseller for the producer.

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<sup>31</sup> Sections 18(1) (domestic gas), 23(1) (supply gas), 28(1) (project gas) and 32(1) (liquid petroleum) of the Regulation

<sup>32</sup> Sections 18(3) (domestic gas), 23(3) (supply gas), 28(3) (project gas) and 32(3) (liquid petroleum) of the Regulation

<sup>33</sup> Sections 18(4) (domestic gas), 23(4) (supply gas), 28(4) (project gas) and 32(4) (liquid petroleum) of the Regulation

<sup>34</sup> Sections 18(5) (domestic gas), 23(5) (supply gas), 28(5) (project gas) and 32(5) (liquid petroleum) of the Regulation. The approved form is Form QRO R02.10.

<sup>35</sup> Sections 18(6) (domestic gas), 23(6) (supply gas), 28(6) (project gas) and 32(6) (liquid petroleum) of the Regulation

<sup>36</sup> Sections 18(7)-(9) (domestic gas), 23(7)-(9) (supply gas), 28(7)-(9) (project gas) and 32(7)-(9) (liquid petroleum) of the Regulation



67. Where a relevant sale has occurred for a particular petroleum type, but the producer does not have the relevant sales data in relation to that sale by the time the royalty return is lodged, the producer cannot provide all relevant sales data for the formula method to apply and the benchmark price method must therefore be applied for the return period for that petroleum type.<sup>37</sup>

No relevant sales to independent buyer or unrelated buyer

68. Where the only relevant sales of a particular petroleum type that occur during a return period are to persons who are not independent buyers or unrelated buyers, the average sales price determined under the average sales price formula (were it to apply) would be equal to the benchmark price. For ease of administration, the benchmark price method will apply automatically in this situation.
69. Where no relevant sales of a particular petroleum type occur during a return period, the average sales price formula cannot be used as there is no relevant sales data to input into the formula. It is therefore necessary for the benchmark price method to apply in this situation.

Decision by the Commissioner

70. In making a decision that it is appropriate for the average sales price to be equal to the benchmark price, the Commissioner may have regard to any of the following matters:
- (a) for domestic gas, supply gas or liquid petroleum:
- (i) any arrangements existing between the producer, or one or more resellers for the producer, and a person who purchases the petroleum type from the producer or reseller
  - (ii) the number of sales in the return period of the petroleum type produced by the producer
  - (iii) the volume of the petroleum type provided by the producer in the return period that is sold to:
    - an independent buyer
    - a person other than an independent buyer
  - (iv) any other matter the Commissioner considers relevant<sup>38</sup>
- (b) for project gas:
- (i) any arrangements existing between a member of the LNG project and a person who purchases LNG from a member of the LNG project
  - (ii) the number of sales of LNG in the return period by all members of the LNG project
  - (iii) the volume of LNG sold in the return period by all members of the LNG project to a person who is:
    - neither a member of, nor a relevant entity for a member of, the LNG project
    - either a member of, or a relevant entity for a member of, the LNG project
  - (iv) any other matter the Commissioner considers relevant.<sup>39</sup>

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<sup>37</sup> See the discussion commencing at paragraph 73 in relation to the consequences of the producer subsequently obtaining the missing relevant sales data.

<sup>38</sup> Sections 18(10) (domestic gas), 23(10) (supply gas) and 32(10) (liquid petroleum) of the Regulation

<sup>39</sup> Section 28(10) of the Regulation

## Example 14

ABC Co produces CSG. ABC Co is not a member of an LNG project, and sells CSG to independent buyers who are not LNG project buyers via DEF Co, a reseller for ABC Co.

In the royalty return for the March 2021 royalty return period, ABC Co uses the formula method to determine the average sales price for domestic gas produced during the period. The average sales price so determined is less than the benchmark price.

In the royalty return for the June 2021 royalty return period, ABC Co indicates that it does not have all relevant sales data for relevant sales of domestic gas, and therefore must use the benchmark price method to determine the average sales price for domestic gas produced during the period.

Over the next four royalty return periods (i.e. the September 2021 to June 2022 periods), ABC Co:

- uses the formula method to determine the average sales price for domestic gas in three return periods, and in each case the average sales price so determined is less than the benchmark price for domestic gas for the period
- uses the benchmark price method to determine the average sales price for domestic gas for one return period, again on the basis that it does not have all relevant sales data for relevant sales of domestic gas.

In reviewing ABC Co's affairs, the Commissioner identifies that in each of the two periods in which the benchmark price was used for domestic gas:

- ABC Co had relevant sales information in relation to all relevant sales by DEF Co during the period except for one sale
- in contrast to the return periods where the formula method was used, ABC Co did not request DEF Co to provide any outstanding relevant sales data within one week of the end of the return period
- on the basis of the relevant sales information that was available to ABC Co, the average sales price calculated using the formula method likely would have been significantly higher than the benchmark price.

The Commissioner considers that ABC Co's failure to obtain relevant sales data in return periods in which doing so would likely result in a higher average sales price than if the benchmark price applied is a relevant consideration in determining whether the average sales price should be equal to the benchmark price for the protection of the public revenue. The Commissioner therefore determines that the benchmark price method will apply to ABC Co for domestic gas for the September 2022 and all subsequent return periods.

71. The Commissioner must give the producer notice of the decision, including the day on which the decision takes effect (which may be a day before the day on which the Commissioner makes the decision).<sup>40</sup>
72. A decision by the Commissioner may apply to one or more petroleum types for one or more specified return periods, or may apply for all future return periods unless withdrawn by the Commissioner.

## Incorrect calculation of average sales price

### Incorrect relevant sales data

73. Where a producer believes that it has complete relevant sales data in relation to a particular petroleum type at the time of lodgement of the royalty return for a return period, and uses the formula method on that basis<sup>41</sup>, the producer may subsequently discover that:
  - (a) one or more additional relevant sales occurred during the royalty return period, but were not included when the average sales price was being calculated (e.g. due to accidental omission, or information about the occurrence of the sale not having been provided by a reseller until after the royalty return was lodged)

<sup>40</sup> Sections 18(11)-(13) (domestic gas), 23(11)-(13) (supply gas), 28(11)-(13) (project gas) and 32(11)-(13) (liquid petroleum) of the Regulation

<sup>41</sup> If the producer does not believe that it has complete relevant sales data in relation to a particular petroleum type at the time of lodgement of the royalty return for a return period, the producer would be required to use the benchmark price method: see discussion commencing at paragraph 64.

- (b) the revenue or volume from a particular sale included in the average sales price formula was incorrect at the time of return lodgement or subsequently becomes incorrect (e.g. due to a transposition error when calculations were being performed, or a retrospective change to an external index upon which the sale price was based to correct an error in the index) or
  - (c) a particular relevant sale, although included in the average sales price formula, was miscategorised (e.g. the producer incorrectly treated a sale to a relevant entity for the producer as a sale to an independent buyer).
74. Subject to paragraph 77, if the average sales price calculated using the formula method reflecting the corrected or previously omitted relevant sales data (recalculated average sales price) is greater than the average sales price calculated at the time of return lodgement (original average sales price):
- (a) the correct royalty rate for that petroleum type for the return period will increase, such that the producer's petroleum royalty liability will be greater than the amount assessed upon lodgement of the royalty return
  - (b) the producer must advise the Commissioner of the understatement within 30 days after becoming aware of the understatement<sup>42</sup>
  - (c) irrespective of whether the producer so advises the Commissioner, subject to limitation periods<sup>43</sup> the Commissioner may make a reassessment increasing the producer's petroleum royalty liability.
75. Subject to paragraph 77, if the recalculated average sales price is less than the original average sales price:
- (a) the correct royalty rate for that petroleum type for the return period will decrease, such that the producer's petroleum royalty liability will be less than the amount assessed upon lodgement of the royalty return
  - (b) subject to the limitation period on lodging an objection<sup>44</sup>, the producer may object against the assessment made when the royalty return was lodged on the basis that that assessment overstates the producer's petroleum royalty liability
  - (c) the producer may request the Commissioner to make a reassessment decreasing the producer's petroleum royalty liability and, subject to the limitation period<sup>45</sup>, the Commissioner may, but is not compelled to, make such a reassessment.<sup>46</sup>
76. Subject to paragraph 77, if the recalculated average sales price is equal to the original average sales price, the petroleum royalty liability would be unchanged and no further action would be required by the producer.
77. As noted in paragraphs 57(c) and 57(d), where the only relevant sales during the return period are to persons who are not independent buyers (for domestic gas, supply gas or liquid petroleum) or unrelated buyers (for project gas), the Regulation provides that the average sales price for the petroleum type will be the benchmark price.

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<sup>42</sup> Section 28 of the Administration Act

<sup>43</sup> Section 22 of the Administration Act

<sup>44</sup> Section 65 of the Administration Act

<sup>45</sup> Section 21 of the Administration Act

<sup>46</sup> Section 17(4) of the Administration Act. A decision to not make a reassessment is a non-reviewable decision: s.17(5) of the Administration Act

78. Where:

- (a) one or more such sales were incorrectly classified as being to a person who was an independent buyer or an unrelated buyer
  - (b) the formula method was used at the time of royalty return lodgement
- and
- (c) it is subsequently discovered by the producer or the Commissioner that the benchmark price method should have applied

then, if the benchmark price is:

- (d) greater than the original average sales price—the consequences in paragraphs 74(a) to 74(c) would follow
- (e) less than the original average sales price—the consequences in paragraphs 75(a) to 75(c) would follow
- (f) equal to the original average sales price—the petroleum royalty liability would be unchanged and no further action would be required by the producer.

Incorrect application of benchmark price method

79. Where a producer believes that the circumstances in paragraph 57(b), 57(c) or 57(d) apply at the time of lodgement of the royalty return for a return period, and uses the benchmark price method on that basis, the producer may subsequently discover that:

- (a) the producer did have complete relevant sales data at the time of return lodgement
- or
- (b) there were actually sales to independent buyers or unrelated buyers during the return period.

80. If no benchmark election was in force for the return period, and the Commissioner has not decided that the benchmark price method should apply for the return period, the producer should have used the formula method to determine the average sales price. Accordingly, if the average sales price determined under the formula method is:

- (a) greater than the benchmark price—the consequences in paragraphs 74(a) to 74(c) would follow
- (b) less than the benchmark price—the consequences in paragraphs 75(a) to 75(c) would follow
- (c) equal to the benchmark price—the petroleum royalty liability would be unchanged and no further action would be required by the producer.