

OIL, GAS AND NATIONAL DEVELOPMENT



This paper is an abridged version of the speech by the Prime Minister, the Rt. Hon. Harold Holt, M.P., to a conference of the Australian Petroleum Exploration Association in Sydney on Monday, 13th March, 1967.

The speech sets the Government's record and policy in the search for oil and gas in the context of its broad policies for the promotion of national development, and deals with recent criticism of certain aspects of its oil search policy.

The speech is supported by two documents to which reference was made by the Prime Minister:-

Appendix A

A statement by the Commonwealth Treasurer, the Rt. Hon. W. McMahon, M.P., on the Government "take" (royalties plus income tax) in off-shore oil and gas activities.

Appendix B

Summary of a speech at the same A.P.E.A. Conference by Sir Ian McLennan, Managing Director of B.H.P. Co. Ltd. - a partner with ESSO in the successful discovery of off-shore gas in Bass Strait, Victoria.

OIL, GAS AND NATIONAL DEVELOPMENT

ADDRESS BY THE PRIME MINISTER, THE RT. HON. HAROLD HOLT, M.P.
TO THE AUSTRALIAN PETROLEUM EXPLORATION ASSOCIATION CONFERENCE

13TH MARCH, 1967

Let me first say that I am fully conscious of the tremendous importance to Australia of an efficient, well-conducted and successful petroleum exploration and development industry. The petroleum industry provides an increasingly significant part of our total energy needs. It employs directly and indirectly an important percentage of our population. Without petroleum, life as we know it today would be, if not impossible, then certainly very different.

Fortunately, there is not much risk of a world shortage of petrol. Why then, it is often asked, should we spend so much effort in Australia in looking for more?

First, demand is rising at the rate of about 10% a year in Australia and 9% a year world-wide. Unless new reserves are being found, over-supply could turn to shortage. Second, there is always a risk that our supplies could be interrupted by events over which we have no control. It is prudent to have our own resources. Third, local supplies would help our balance of payments very much. Petroleum is our third largest import, following machinery and chemicals. In 1965-66 we imported 4,854 million gallons valued f.o.b. at about \$250 million. There are very great national rewards if we can replace much of these imports with local petroleum.

Although the quest for petroleum began in 1892 in the Coorong area of South Australia, it only commenced seriously in the years following World War II. Senior officers of the Commonwealth Bureau of Mineral Resources were among the few who maintained, despite general disbelief, that a major search was warranted. The Bureau began basic geological and geophysical mapping of the Australian sedimentary basin and we, as a Government, felt that here was a national speculation that was justified in the national interest.

When Rough Range failed to show significant resources after the find in 1953, the search had reached a low ebb by 1958. The Government, concerned at this decline in interest, introduced a Petroleum Search Subsidy Act to stimulate company enterprise and to make generally available the knowledge so gained of the geology of the basins. We also felt that the Act would demonstrate a favourable political attitude to petroleum search that would encourage experienced overseas companies to join in. The Act has been extended from time to time and is currently effective until June this year.

In the ten years of its life the subsidy scheme has stimulated exploration and led to the discovery of oil and gas in a number of areas in and around Australia.

Active exploration - geological, geophysical and drilling - has been undertaken in the 25 major basins of likely petroleum-bearing sediments. These cover some 1.7 of the 3.2 million square miles of land surface of Australia and Papua New Guinea and, about 0.6 of the 1 million square miles of the continental shelf. Total expenditure by companies and by the Commonwealth and State Governments to the end of 1966 was about \$420 million, but established reserves total only about 200 million barrels of oil. We consumed in one year, 1965-66, a total of 139 million barrels. Thus our known reserves are still less than two year's importation. So you see we still have a long, long way to go on the road to self-sufficiency.

While the discoveries of natural gas will result in cheaper domestic and industrial heating in some areas - natural gas is ready to pay handsome dividends in some localities in Australia - some of the markets are at a considerable distance from the supply. It is therefore desirable that the search should continue in an attempt to locate other fields in closer proximity to the markets. Incidentally, the current cost of finding oil in Australia of \$2 a barrel compares very favourably, I understand, with American and Canadian costs.

Apart from the Subsidy Act, the Commonwealth Government has provided various inducements and basic technical services in order to create a favourable climate in which private enterprise will provide the greater part of the expenditure required and be responsible for detailed exploration, development and exploitation. We clearly recognise the need to maintain continuing incentives in this field, and I can safely assure you that the general attitude of my own Government is to recognise the difficulties the industry faces because of the long term character of its investment and the freaks of development which are a feature of the oil industry.

The principle measures taken by the Commonwealth Government, with which you are all familiar, include taxation concessions, subsidies to exploration companies, basic surveys and investigations in the field and laboratory by the Bureau of Mineral Resources, other forms of assistance such as relief from duty for essential equipment, accelerated map production by the Department of National Development and the assistance of highly qualified consultants.

Despite all this there has recently been a definite pause in the rate of exploration due to an absence of significant discoveries of new areas on-shore and delays in obtaining rigs to drill structural areas off-shore. This latter problem will be largely overcome late in 1967 when five and possibly six rigs will be drilling on our continental shelf. As Sir Ian McLennan has said, the production activity of these rigs, and other by-products of the mineral oil exploration programme, affect the economy over a wide range of activities.

I was appreciative of what Sir Ian McLennan had to say about the co-operative and helpful attitude he had found in the Governments concerned in his negotiations - this, of course, is as it should be. There have been extensive Commonwealth/State discussions on the proposed off-shore legislation, and the Governments concerned have given their careful consideration to the views expressed by the companies engaged in off-shore operations. The object of the Governments has been to reach agreement on a legislative scheme that would give certainty of title to operators in off-shore areas who undertake to bear very high expenditures, and at the same time to avoid wasteful and costly litigation of a kind which has beset the United States for many years and is now starting to show up in Canada. We confidently expect that our legislation will be brought before the Parliament during the course of this year.

Much interest in the continental shelf has been generated by the discovery of large supplies of natural gas. Although natural gas provides only one-hundredth part of one per cent of Australia's primary energy market, this share could increase to as much as 10% within a few years. The change from one energy source to another is an expensive step, but where it can be shown that it is in the interest of the Australian people to make a change, my Government will view constructively and in a helpful spirit any scheme suggested. I am happy to say that through the Australian Loan Council we have been able to arrange for the necessary funds to cover the \$40 million cost of piping gas to Adelaide.

As a background to the changes which your own industry is bringing to Australia's growing economy, let me mention that there are now 60,000 factories in Australia - double the number at the beginning of World War II. Employment in these factories represents an increase of 125% since 1939. Manufacturing now absorbs 28% of our work force and contributes 13% of the value of our total exports - and that percentage is tending to increase. We are now exporting to countries some products which we formerly imported, including steel to the United States and the United Kingdom.

Our manufacturing nowadays includes some highly sophisticated products like radio-telephone equipment, transistorised airways beacons, the pilotless jet aircraft Jindivik, the anti-submarine guided missile Ikara and the anti-tank guided weapon Malkara. These have all found markets abroad.

Another aspect of the changing economic pattern - reflecting largely the impact of petroleum and mineral developments - is the emergence of new towns. Though small in size, the contribution to national development, and in particular to development of the north of such towns as Weipa, Dampier, Mount Tom Price, Gove and Barrow Island, will become increasingly important as time goes by. This is decentralisation in a practical way stemming from private industry developments. We recognise that there is a role for Governments in all this, but Australia has benefited, and will benefit increasingly in the years ahead, from the practical decentralisation of activity and industry occurring through these private industrial developments, and others like them.

Vast quantities of capital are required for these projects and in the main this is being found by the firms themselves. Nevertheless, Government action has contributed much to the mineral development of the north. Direct financial contributions totalling \$44 million have been made by the Government towards the Townsville-Mount Isa Railway, the Gladstone coal loader, the Weipa wharf and township, the Darwin wharf and railway facilities in the Northern Territory. The Commonwealth Government has also arranged that, in addition to the mining activity in the Gove bauxite deposits, processing to alumina will take place in the Northern Territory. The Bureau of Mineral Resources has, in fact, spent 80% of its annual budget of nearly \$5.4 million on securing basic data on mineral resources in Northern Australia.

In all these ways, the Government is helping to shape the new pattern of economic activity. We can also help by providing a favourable climate for decentralisation, and this applies in particular to your own industry through the economic and general policies we pursue. An illustration that comes quickly to mind of practical help to areas remote from the cities is the legislation that brought the price of petrol for people outside the city areas to a level close to city prices. Other measures include the amounts to be expended on rural roads under the Commonwealth Aid Road legislation, the activities of my colleague, the Postmaster-General in ensuring that television services stretch out as widely as possible, the decentralisation of air services and the provision of other amenities.

From what I have already said, you will appreciate that mining and oil development are but a part of the overall story. May I mention particularly the recent publication brought out under the aegis of my colleague, the Minister for National Development. It costs only \$2 and shows the major development work under construction in Australia at the end of June last year to have a value on completion of \$2,327 million. By any standard this is a huge investment programme with a nation of less than 12 million people - and the total does not include

such things as expenditure on housing, hospitals and education facilities or the Commonwealth's \$600 million expenditure on the Snowy Scheme. The publication shows that we now have in hand investment and developments amounting to some \$200 a head of our population.

New arrangements and facilities for the provision of capital will need to be devised to help finance this and new developments, and we have been working actively and earnestly on the problem for some time. We are confident that we will find a practical means to achieve this objective.

Nobody living in this country so subject to the hazards of the seasons and risk of drought, flood or fire, can expect that the course ahead is ever likely to be easy. But we believe our plans are soundly laid and that the political and economic stability we are maintaining is one of the strongest incentives for investment in Australia and provides a favourable environment for development and growth.

Before I conclude, perhaps I should deal a little more specifically with some of the matters that were raised by your Chairman, Mr. Earl Abbott in his thoughtful and extremely interesting speech. The most serious point I want to take up with you is the question of the availability of Governments for consultation. I have no hesitation in stating that there is no agreement whatsoever among the Governments concerned that they will not consult with the industry. Indeed, there have been several consultations, and I have taken part in two of them myself. To mention only the more recent occasions, there were three meetings with the industry last year - in February, June and August, - as well as a number of written exchanges.

At the meeting in February there were lengthy discussions between senior Commonwealth and State officers and representatives of eleven off-shore companies, many of whom are prominent members of APEA. At a meeting of Commonwealth Ministers in June, the APEA request for permission to send a deputation was granted and in August five senior Commonwealth Ministers received a further deputation which presented a written case and took several hours in explaining its point of view and discussing it. I therefore think it is fair to say that the Government has given the APEA wide opportunity to present its views: it has certainly taken these into account in determining its policies, and will continue to do so. Far from our adopting policies which would discourage the industry or kill the goose that we hope will lay us many golden eggs, it is our object to assist it in its tasks and to encourage it to go ahead with its investment, exploration and development.

I did have it in mind to go in some detail into the percentage of "take" by Governments in Australia and how this compares with the percentages in other countries. For lack of time, I now just want to make it clear that we do not accept - and this has been the matter of a quite thorough study - the table of percentages which have been publicly presented as a basis of comparison for the Australian "take" and that of countries overseas. Rather than weary you with going over the ground again, may I direct your attention to the press statement of 27th January which went out from my colleague, the Treasurer. It is admittedly difficult to find a realistic basis for comparison between the tax structures of the different countries, but we have to recognise that the responsible Commonwealth and State Governments have an entitlement to a proportion of the return from the exploitation of our natural resources, just as have those who hazard their capital and skill in the effort. These things are all in our consciousness and I would hope that the experience of the industry generally can be that we will always be seeking good co-operation between Government and industry in the exciting task of the development of our country and its resources.

OFF-SHORE OIL AND GAS:
ROYALTIES AND TAX

by

The Rt. Hon. William McMahon, M.P.

Treasurer of the Commonwealth
of Australia

The petroleum industry has claimed that the Government "take" (royalty plus income tax) in Australia in the proposed joint off-shore petroleum legislation by the Commonwealth and the States will be higher than in five of the six other countries with recent off-shore legislation. The comparative figures that have been quoted are:-

<u>Country</u>	<u>Govt. "take" as percentage of "divisible profit" (a)</u>
United Kingdom	50.4 per cent
Denmark	45.8 " "
Germany	50.6 " "
Norway	55.2 " "
France	47.72 " "
United States	46.8 " "
Australia	52.8 " "

(a) on a "present-day value" basis.

These figures do not give a true picture - the worth of the figures depends heavily on:-

- a) the basis on which the calculations of "present-day values" of "divisible profits" have been made. (These calculations involve the estimating of gross sales proceeds and capital and operating production costs over a given future long-term period, and the reduction of the resulting figures to a present-day value basis by the application of a discount interest rate); and
- b) the assumptions used in the measurement of the incidence of income taxation in the respective countries.

The information that has been provided on how the figures are compiled is very meagre. The starting point is an assumption that, on a present-day value basis, gross sales proceeds will be double capital and operating production costs in the case of all the countries mentioned.

This is obviously a very generalised assumption; it certainly cannot be accepted without question so far as Australia is concerned. The period and discount interest rate used in the calculation of the present-day value figures have not been indicated and the use of different periods and different interest rates can produce vastly different results in terms of comparative present-day values.

It is not sufficient only to look at tax rates; the comparisons must have regard to the taxation laws as a whole of

those countries. These laws differ considerably in relation to deductions allowable and the time when those deductions may be claimed.

The tax figures included in the calculation of the quoted percentages for the other countries may be significantly understated in some cases while the tax figures included in the calculation of the quoted Australian percentage, on the other hand, seem to be substantially overstated. This is because the figures take no account of the special deductions allowable under our income tax laws which are designed to free the proceeds from the sale of petroleum and its products from income tax until all allowable capital expenditure has been fully recouped.

If in the present-day value calculations allowance were made for this feature of Australian income tax law, the tax figures included in the Australian calculation would be considerably reduced - perhaps even to the point where the figure for the Australian government "take" would fall below the percentage figures quoted for other countries.

The only comparison that can be made of any real meaning is between rates of royalty and these represent only one area of government involvement. For instance, the Commonwealth Government has given special stimulus and assistance to oil search, at times when the risks are highest by the petroleum search subsidy scheme, under which the Commonwealth has already paid out or committed a total of \$59.6 million; by making capital subscribed to an oil exploration company by Australian resident shareholders fully tax deductible, and by fixing a special incentive price for five years from 1965 for crude oil produced in Australia.

The standard royalty rate of 10% in the proposed joint off-shore legislation is relatively low on international standards. It compares with rates of 15-2/3% and 12½% generally applicable in off-shore areas in the United States and the United Kingdom respectively.

Furthermore the industry has been treated more generously in this country with the proposed legislation on the sizes of exploration and production areas.

Canberra

27th January, 1967.

AN AUSTRALIAN LOOKS AT PETROLEUM EXPLORATION

by

Sir Ian McLennan

Managing Director of B.H.P. Co. Ltd.

Petroleum exploration activities in Australia represent a unique combination of local and foreign private enterprise, activities combined with effective and practical Government support in tangible form.

Expenditure on petroleum exploration in Australia had reached a total of some \$370 million by December 1965 of which \$234 million had been spent in the last 10 years. The current rate of expenditure is of the order of \$60 - \$70 million per annum.

These figures are substantial, even alongside the Snowy Mountains scheme where approximately \$600 million has been spent at the rate of \$40 - \$50 million a year, and the steel industry where \$794 million has been spent in the last 10 years.

The \$370 million spent to December, 1965 -was made up this way:-

Funds provided by Private Enterprise	\$294 million
Direct Government Subsidies	\$ 42 "
Other direct Commonwealth and State Expenditure	\$ 34 "

This is enlightening and shows that while Governments do play a significant role in the matter of subsidies, direct expenditure and by other incentives, it is still for private enterprise, to the greatest extent, to provide the necessary stimulus, funds and know how.

There is, of course, a further great stimulus provided by the Commonwealth Government in the form of relief from taxation, but I know of no way of putting a precise figure to this.

A breakdown of the \$70.8 million spent on petroleum exploration activities during 1965 shows that the major investment was by overseas organisations which accounted for \$34.3 million, followed by Australian private enterprise investment and re-investment amounting to \$21.6 million, Government subsidy of \$10.4 million and Direct Government expenditure of approximately \$4.5 million.

One of the intangibles which has not been listed in the expenditures, but which is very real, is the value which should be placed on the experience represented by the personnel engaged in such activities, and the influence that they can exert to see that the money is spent wisely.

In the field of off-shore legislation in particular there have been many international and constitutional problems to overcome and many points of view to consider.

This is not just a simple government/industry relations problem. Both government and industry are working together in an uncharted field and the degree of progress and mutual understanding is heartening.

There is intense world wide competition for capital for petroleum exploration and the development of petroleum production capacity. Other countries may offer certain incentives in the competition for such capital but in the overall analysis Australia has a great deal to offer.

The development of the large super tanker and of pipeline transportation have done much to ease our joint problems of isolation and small local markets.

In the local scene, Australia is rapidly becoming industrialised, and its population mobile, with a high standard of living and increasing demands for energy. Our energy resources in black and brown coal are quite significant, but the growth factor is in the field of readily transportable energy. The sources of primary energy, for the statistical year 1965-66, expressed in tons of black coal equivalent, are:-

Coal	48.7%
Petroleum	44.2%
Firewood	1.4%
Hydro electric power	5.7%

This clearly shows the importance of petroleum in the energy market.

There are areas where competition exists between these sources of primary energy, particularly in power generation and perhaps in some types of industrial market, and the natural forces of competition will give each source its place in the market.

However, there are major sections of the energy market where the alternative types of fuel are not interchangeable and one result is the rapidly increasing demand for energy in the form of petroleum.

The petroleum industry is well aware of the continual expansion of the demands for its products. In the United States, for example, the 61% share of the total energy requirements of the United States held by oil and natural gas in 1950 rose to 76% by 1965. In Western Europe, the share rose from 15% in 1950 to 52% in 1965 with an expected increase to 72% in 1975.

Is there any doubt that Australia's energy requirements will follow similar trends?

In Australia we offer stability of Government and have Governments fully alive to the advantages which can accrue from the development of a local petroleum industry. I would emphasise the intangible incentives that stable Government offers, notwithstanding the various shades of Government opinion.

The lack of restrictions placed on foreign investment in Australia, compared with restrictions, both written and unwritten, which the petroleum exploration and production industry has encountered elsewhere, reflects an enlightened Australian attitude offering considerable encouragement.

In matters such as taxation, remittance abroad of earnings and repatriation of capital, the attitude of the Commonwealth Government and the various authorities concerned can only be classified as highly co-operative.

From time to time there may be some criticism levelled at remittance abroad of earnings and repatriation of capital in the case of foreign controlled organisations, but usually such criticism is saved up for those organisations which are successful. However, there is, no doubt, on the other side of such criticism, a whole-hearted respect for such organisations and a realisation of their value to a country like ours.

One very important aspect of Government policies, is no discrimination between national and foreign ownership in the application of laws and regulations. Another incentive to the petroleum exploration industry for continual and expanded exploration in Australia is the potential that exists.

Our own experience in petroleum exploration has shown that a painstaking and detailed step by step programme under expert and experienced guidance with adequate resources in capital and know-how, can result in discoveries and also maintain a high proportion of local equity.

I would not venture to predict the anticipated ratio of success in both continental and off shore exploration in Australia, but I imagine you will all agree that the potential for further discoveries in the Australian area is good.

I am not sure if we are doing all we can in Australia to take full advantage of this petroleum age and our educational activities will need to be developed further so that our young people can play their full part in just the same way as they have in the development of our other industries. We need geologists, chemical engineers, construction engineers, physicists, chemists, and so on, all oriented in their training towards the petroleum industry.

The coming of the petroleum exploration industry and its prospect of success has brought other developments to Australia which would not have been contemplated even a few years ago.

Who would have thought that the State Dockyard at Newcastle would have played a major part in reconstructing an off-shore drilling rig and who would have thought that at Whyalla we would be constructing a semi-submersible rig of the most highly sophisticated nature using very largely Australian raw materials and Australian people?

The imported content of this rig will be confined to specialised machinery not made in this country. Further, it is hoped that soon we will be building platforms for erection in Bass Strait and already there has gone into operation at Port Kembla a new tube mill capable of producing the very high grade pipes necessary for gas and oil distribution. These are just some of the things that have happened and others of course may well occur and are in fact already under way.

So far very little income has been derived in Australia from petroleum activities. It is all with an eye to the future and it is most heartening indeed that there are so many people prepared to "chance their arm" in an endeavour to bring the great benefits of oil and natural gas production to this country.

Surely they deserve their just rewards if success comes their way. It is essential that these rewards be there to provide incentive for further exploration because up to the present we have only scratched the surface.

Sydney

13th March, 1967.