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Horizontal Fiscal Equalisation Inquiry
Productivity Commission
Locked Bag 2
Collins Street East Vic 8003

Dear Commissioners Chester and Coppel,

BHP welcomes the opportunity to share its views on Australia's system of horizontal fiscal equalisation (HFE).

We are proud of the contribution we make to the Australian economy and the benefits this contribution brings to Australia's standard of living. In FY2016, we paid US$2.5 billion in taxes and royalties to Australian governments, including US$1.4 billion in payments to State governments.

These latter payments, and those made by other resources companies, are a key input to the Commonwealth Grants Commission's (CGC) determinations on how GST revenue should be distributed across the jurisdictions. Broadly speaking, States that have stimulated above average resources production are assessed as having above average revenue capacity, which reduces their GST share. States with below average resources production, meanwhile, are assessed as having below average revenue capacity, which increases their GST share.

We recognise there is a need for the HFE system to account for differences in the fiscal strength of the States. The system's treatment of resources revenue, however, is problematic for the economy in that it dulls the incentives for States to stimulate development of their resource endowment. Over time, this is likely to result in less investment in the resources sector than would otherwise be the case. This translates to lost opportunity for jobs (including flow on opportunities for other businesses that support the resources sector), less activity in regional communities and, in turn, a less productive, efficient and robust national economy.

This dilemma is not unique to Australia. Other jurisdictions have sought to address it by quarantining a portion of resources revenue for the purposes of HFE. For example, in Canada, another resource rich nation, the Federal Government applies a 50 per cent discount to provincial mining revenue when making its HFE determinations.

Adopting a similar mechanism in Australia would increase the benefits that accrue to the States from facilitating the development of their mineral and energy resources, while still allowing the CGC to account for differences in jurisdictional revenue capacity.

The benefits of such a change would not be limited to those jurisdictions that are able to attract additional resource projects. Greater investment in the resources sector would be beneficial for the national economy. The broader base of economic activity that it would stimulate would bring with it more jobs and more opportunities for small and medium businesses, well beyond the borders of the State in question. Incremental economic activity would lead to growth in the tax base for all governments. Research commissioned by the Minerals Council of Australia (MCA) found that changing policy and regulatory settings to facilitate the development of new resource projects could (over a 12 year period):

- Increase real GDP by between A$160 billion and A$280 billion (2014 dollars)
- Create between 384,000 and 690,000 new jobs.[1]

Furthermore, allowing States to retain a share of resources revenue outside of the HFE system has the potential to have a positive effect on energy security and affordability. Those jurisdictional governments that have imposed blanket restrictions on onshore gas exploration and development would have greater financial incentive to re-assess opportunities to reduce or remove them. Any measure that brings with it increased likelihood of a key current constraint to effective market balancing being alleviated would be in the interest of manufacturers and other gas-intensive users serviced by the east coast gas market, as well as all household energy users.

We believe the model proposed in the MCA submission to this inquiry provides a practical solution, which has already been proven elsewhere, to progress reform. The MCA has proposed the adoption of a 25 per cent discount to the mining revenue assessment in the GST distribution calculations, but with a 'safety net' so that no jurisdiction would receive less GST funding than their previous year allocation.

We are committed to working with all Australian governments to create a policy and regulatory environment that maximises investment and the living standards of ordinary Australians. We would be happy to have further discussions with the Inquiry team on any issue raised in our submission.

Yours sincerely

Mike Henry
President Operations, Minerals Australia

[1] BAEconomics (2014), *The economic gains from streamlining the process of resource projects approval*, prepared for MCA.