AUSTRALIAN CONSERVATION FOUNDATION

8 November 2017

Submission: Horizontal Fiscal Equalisation

Productivity Commission Draft Report

The Australian Conservation Foundation (ACF) welcomes the chance to provide feedback on the Productivity Commission's (PC) Draft Report into Horizontal Fiscal Equalisation (HFE).

Key Points

- ACF welcomes draft finding 4.3 and its implication that the PC won't be recommending adjusting the HFE system to add incentives for resource exploration.
- The final report should acknowledge that resource exploration policies come at an environmental cost which will have financial implications.
- Discussion of state spending on natural disaster recovery versus mitigation spending should be expanded to consider climate change mitigation as part of the discussion.
- Current rehabilitation bonds for mines do not adequately cover the cost for government if owners are unable to adequately rehabilitate sites.
- Resource projects bring governance risks around corruption that need to be identified and managed.

Environmental Risks

From the analysis presented in the draft report it is clear that environmental issues around HFE and state government revenue haven't been considered in any detail, despite their relevance to government revenue and expenditure.

The PC rightly has a reputation for rigorous and sober analysis and research. Therefore, it is disappointing that the long-term health of the environment and its importance to the economic resilience of Australia is absent from parts of its draft report where it would relevant.

We welcome the statement in draft finding 4.3 in reference to mineral and energy resources that "there is no direct evidence that GST effects have influenced specific policy decisions" and that "making adjustments to the HFE system specifically to add incentives for resource exploration policies that are deemed to be desirable would be an intentional breach of policy neutrality and State autonomy."

However, we remain concerned the PC continues to make statements such as "the distortions arising from the treatment of resource restrictions could have large financial implications for some States, especially over the long term" without any discussion about the financial and environmental implications from continuing fossil fuel extraction and combustion. These implications include more frequent natural disasters and degradation of natural infrastructure which will have an impact on state government revenue and expenditure.

Resource royalties play a minor role in state budgets and environmental impacts of fossil fuel extraction and combustion have long term far reaching impacts that are not adequately priced or understood by all levels of government.[1] It would enhance the final report if there was acknowledgment that resource exploitation comes at an environmental cost.

As is acknowledged in the draft report:

> "the Productivity Commission has previously found that the equalisation of spending on natural disaster recovery, but not of mitigation expenses, biases States' incentives to effectively manage natural disaster risks."[2]

States that allow continued unfettered exploitation of fossil fuels or put up regulatory barriers to the production of pollution free energy despite evidence of increased extreme weather events such as cyclones and droughts are not accounting for the full financial risk of these decisions, discussion should be extended to acknowledge this. As acknowledged above, equalisation "biases States' incentives to effectively manage natural disaster risks" - the same logic applies to the effective management of climate risks.

For example, jurisdictions that continue to rely on older more traditional centralised energy systems with large scale transmission infrastructure may find themselves suffering more interruption to their power supply owing to climate related weather events than jurisdictions who embrace decentralisation of energy supply.[3]

This will interrupt economic activity and therefore revenue potential. This is an important mitigation issue that could be explored in the final report.

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[1] Draft Report, p.106
[2] Draft Report, p.104
[3] Engineers Australia, *The Future of Australian Electricity Generation*, 2017, p. 20 https://www.engineersaustralia.org.au/sites/default/files/resources/Public%20Affairs/The%20Future%20of%20Australian%20Electricity.pdf
Union of Concerned Scientists, *Power Failure: How Climate Change Puts our Electricity at risk – and What We Can Do*, April 2014, p. 2 http://www.ucsusa.org/sites/default/files/legacy/assets/documents/Power-Failure-How-Climate-Change-Puts-Our-Electricity-at-Risk-and-What-We-Can-Do.pdf

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Rehabilitation Risks

As outlined above there is no discussion in the draft report of the environmental cost to jurisdictions of resource exploration. There is also no discussion of the liabilities that rehabilitation of mines places on state governments. The NSW Auditor General conducted an audit of Mining Rehabilitation Security Deposits that was presented to Parliament on the 11th May this year. The audit concluded that:

> "The security deposits the Department [NSW Department of Planning and the Environment] holds are not likely to be sufficient to cover the full costs of each mine's rehabilitation in the event of a default."
>
> "Security deposits also do not include sufficient contingency given the substantial risks and uncertainties associated with mine rehabilitation and closure, particularly in the absence of a detailed closure plan. This risk is exacerbated by the limited independent verification of mining company claims about the size of the outstanding rehabilitation task, which remains the case despite recent improvements to monitoring and review procedures and practices.
>
> There is also no financial assurance held over the risk of significant unexpected environmental degradation in the long-term after a mine is deemed to be rehabilitated and the security deposit is returned. A security deposit is not an appropriate vehicle for covering this risk. "[4]

This is a concern across jurisdictions and it should be incorporated into the cost and benefits of resource extraction for state and territory governments in the PC's analysis.[5]

Corruption Risks

Recent work by Transparency International Australia has also highlighted the Corruption Risks inherent in mining approvals. Their research into the resource approval processes across Western Australia and Queensland found that of the 9 risk categories they profiled 5 categories are in the high or very high category. With 2 being low and 2 being medium risk.[6]

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[4] New South Wales Auditor-General's Report Performance Audit, Mining Rehabilitation Security Deposits, May 2017, p. 2 http://www.audit.nsw.gov.au/ArticleDocuments/993/01_Mining_Rehabilitation_Security_Deposits_Final_Report.pdf.aspx

[5] Ground Truths: Taking Responsibility for Australia's Mining Legacies, 2016 https://d3n8a8pro7vhmx.cloudfront.net/auscon/pages/847/attachments/original/1466127496/MPI_mine_rehab_report.pdf?1466127496

[6] Transparency International Australia, 'Corruption Risks in Mining Approvals: Australian Snapshot, October 2017, p.19. http://transparency.org.au/tia/wp-content/uploads/2017/09/M4SD-Australia-Summary-Report_Final_Web.pdf

Conclusion

It would enhance this report if both the costs and benefits of resource exploration to jurisdictions, and therefore their impacts on HFE were equally considered.

Analysis in the draft report should be expanded to include the costs of resource exploration and development for jurisdictions as well as potential benefits. Costs include localised environmental risks as well as climate risks if resource exploration leads to fossil fuel combustion. Costs borne by state governments including potential mine site rehabilitation costs and corruption costs should also be considered.

For more information:

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The Australian Conservation Foundation is Australia's national environment organisation. We stand up, speak out and act for a world where reefs, rivers, forests and wildlife thrive.

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