

6 August 2024
Hon Shane Jones
Minister of Resources

Key messages:

- *our priorities align with the Government's need to protect and grow our petroleum reserves*
- *we welcome the sensible, pragmatic changes to decommissioning legislation and financial securities outlined in the Cabinet Paper, but they are insufficient to protect the 2P reserve*
- *the best avenue to grow 2P reserves within MBIE's control is to implement a royalty credit to support appraisal/exploration activities. Other options outlined in our 8 July letter should also be investigated*
- *the legislative timetable and process does not appear to be proceeding with the necessary urgency given the magnitude of the problems that have emerged*

Urgent action is needed to incentivise rebuilding our petroleum reserves

1. The recent petroleum reserves data release showed a further reduction of gas reserves, and this year's position will likely reflect a further degradation.
2. We urgently need regulatory change, developed in partnership with industry, that will grow 2P reserves. To do this we need from the Government a firm commitment and a clear idea of timing and scope. The return back to a 'neutral' position will do nothing to alleviate security of gas supply concerns.
3. We acknowledge and welcome the vastly improve engagement from officials, but this has yet to translate into meaningful, concrete action. The royalty and tax reviews are examples of this. Changing the investment environment has real potential to attract and stimulate investment, but it remains unclear how this is being addressed and to what timetable.
4. In our last meeting we provided you with a range of other suggestions, such as changes to depreciation and tax credits. We attach an update to the table we provided you at our last meeting (see Appendix 1) that captures our assessment of how the proposals in the Cabinet Paper does or does not address these

options. We have also, through a letter dated 8 July, provided a range of gas market measures, including potential for a Crown underwrite of new exploration and appraisal, or guarantee gas off-take.

5. We believe these measures and others such as a royalty credit will realign the risk profile, mitigate sovereign risk and help create the right incentives to protect existing reserves and encourage new exploration and appraisal. We seek clear direction and a timetable from the Government on these pressing matters.

Changes to the Crown Minerals Act signalled in the Cabinet Paper

6. While appreciative of the measures proposed to amend the Crown Minerals Act to walk back many of the most egregious and disproportionate aspects of the Act introduced by the last government – we remain of the view that amending the CMA and reverting to the November 12, 2018, version would have been the expedient and cleaner approach.
7. Despite reassurance that reform would proceed at pace, we find ourselves in August, four months since our last meeting and are concerned the necessary changes – particularly the vital changes to secondary legislation - will not be implemented in time to assist in winter 2026. We are still being assured that changes will be in effect in 2024, in time for potential drilling in 2025 but the window is rapidly closing.
8. We welcome clarification of the timing and process for this legislative programme.

Next steps

9. Our priorities align with the Government's need to protect and grow our petroleum reserves base. Again, we stress this can be achieved quickly and pragmatically by working with industry to:
 - a. complete amendments to the Crown Minerals Act as quickly as possible, while ensuring the timing of additional measures, such as the review of royalty settings, aligns with this timetable; and
 - b. implement appropriate risk mitigation measures outlined in our 8 July letter, or others such as a royalty credit, to support appraisal/exploration activities to rebuild our reserves base and also align these with the legislative timetable to form a coherent overall package.

Attachments

APPENDIX 1: Industry proposed complementary measures to encourage further exploration and appraisal – updated to reflect policy proposals

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RECOVERING
INVESTOR
CONFIDENCE

		Primary Impact					Post Cabinet Paper assessment		
THEME	MEASURE	High-level Summary of Energy Resources Aotearoa Position	Extend existing field life	Increase activity	Low emissions potential	Importance	Addressed in Cab Paper?	Specific comments	Overarching comments
Decommissioning	Repeal and reform decommissioning provisions	Repeal overly onerous and unnecessary decommissioning financial security and monitoring requirements for mining permits and licenses - and replace with a fairer and more proportionate regime that balances the risk to the Crown with the cost to permit holders, and more fairly reflects the risks associated with each permit holder	☑	☑	☑	Changes to New Zealand's decommissioning legislation are needed to develop an evidence based, balanced approach to manage the risk that the Crown will be required to undertake and fund another decommissioning project. Legislation introduced was a dramatic over reaction to the financial collapse of one permit holder. These changes will have the greatest impact on perceived sovereign risk and without their removal it will be extremely difficult, if not impossible, to attract overseas investors.	Partially through recommendations 8 through 19	Does not go as far as we would have liked which was a repeal back to the 2018 Act, and "build back better" from there. Does not address the root cause issue of conflating land-use issues with CMA obligations and rights. Failure to address this in a way that cuts across legislative purposes continues to add unnecessarily to administrative costs and complexity.	
	Repeal criminal liability provisions for directors	Criminalising what is normally be a civil issue unreasonably discourages suitably qualified persons from corporate governance roles	☑				No	Not addressed - Officials have advised this will not be repealed.	This is disappointing - but MBIE has advised this approach of criminalising directors' responsibilities has been creeping in across a range of other, different legislation. There is also an optics issue of repeal may look like the Government is going soft on the petroleum sector.
	Financial security requirements	These need to be based on individual operator financial risk profiles. Where required payments from the operator to escrow or bonds should be immediately deductible	☑				Addressed through recommendation 14 (including 14.1 - 14.4)	Will introduce the ability for firms with interests across multiple permits and licenses, and for related entities within a permit or license, to collectivise the financial assurance requirements. This is a significant improvement for permit and license holders.	
	Trailing Liability	Duplicative with other processes and unnecessary	☑				Partially addressed through recommendation 17	Retains the provision for trailing liability, but limits this to the most recent transaction or transfer. Officials anticipate this will be a "last resort" to manage liability as the primary means to do so is through financial securities and financial assurance assessments. Privately officials have acknowledged they expect this to be very difficult to enforce.	
	Repeal post decommissioning liability requirements	These provisions are poorly conceived and difficult to quantify and enforce.	☑				Yes through recommendation 19 (including 19.1 - 19.3)	Addressed through he removal of the requirements of the post decommissioning fund, but introduces a perpetual liability element post decommissioning for wells and infrastructure left in-situ.	

REDUCING
RISK

Tax/Accounting treatment	Enhanced exploration expenditure deductions	Allow an uplift on exploration activity expenditure tax deductions to encourage exploratory drilling. This relief might be offered on a time limited basis (say out to 2035) to encourage near term exploration		☑		We see this as a vital measure for encouraging exploration drilling, particularly if time limited.	Not addressed in Cabinet Paper	Officials have ben engaging with IRD on these matters - again we note only limited involvement from the sector, and general reluctance of IRD to contemplate derogations to the principle of a "broad low tax base" in their role as regulatory stewards.	The overall theme here is we have only very limited visibility of what is being contemplated as a means to incentivise exploration and appraisal activity, which (we hope) ultimately leads to development of additional reserves. Our concern is that IRD, in their desire to maintain a form of purity in the design and integrity of their legislation and rules is not taking direction or grasping the gravity of the situation in terms of New Zealand's energy security and therefore the productivity of the economy as a whole. We remain deeply concerned by this (apparent) indifference.
	Enhanced CAPEX depreciation	Options could include: -Introduce an irrevocable election to switch from seven year amortisation to units of production method (on a field / development basis). -Introduce a “double declining balance” method for spreading petroleum development expenditure (DV for other assets). -Allow an upfront deduction upfront for petroleum development expenditure.	☑			While important - New Zealand's security of supply risks will likely be better managed through encouraging exploration and royalty measures.	Not addressed in Cabinet Paper	Officials have ben engaging with IRD on these matters - again we note only limited involvement from the sector, and general reluctance of IRD to contemplate derogations to the principle of a "broad low tax base" in their role as regulatory stewards.	
	Offshore drilling rig exemption	Options could include: -Make the exemption a permanent exemption. -Extend the exemption to support vessels (including seismic support vessels). -Extend the exemption to on-board processing of seismic data. -Align the tax treatment with Australia by introducing a 5% final tax.		☑		The rolling nature of the exemption, since its introduction, is an unnecessary administrative burden. The exemption should also be broadened to include onboard seismic processing and support vessels mobilised to support the offshore campaign.	Not addressed in Cabinet Paper	Addressing this requires changes in tax rules, and so are not the purview of Minister Jones. We will continue to work with the Minister and officials to help create the right incentives for exploration and appraisal drilling.	

	Deductibility of development expenditure	Allow permit holders to claim an uplift on development CAPEX for new developments or changes to existing operations that contribute to growing the 2P reserves base.	☑			Important to encourage the development of new reserves or for converting contingent resources to reserves - particularly if time limited.	Not addressed in Cabinet Paper	Officials have ben engaging with IRD on these matters - again we note only limited involvement from the sector, and general reluctance of IRD to contemplate derogations to the principle of a "broad low tax base" in their role as regulatory stewards.	
	Research and design tax credit scheme	Apply a 30% tax credit to new projects or initiatives that reduce emissions and/or accelerate the transition to a lower carbon economy (e.g. hydrogen, offshore wind, CCUS, etc.)			☑	Encourages innovation and reutilising existing infrastructure to meet net zero targets and reduce emissions.	Not addressed in Cabinet Paper	Officials have ben engaging with IRD on these matters - again we note only limited involvement from the sector, and general reluctance of IRD to contemplate derogations to the principle of a "broad low tax base" in their role as regulatory stewards.	
	Tax exemption for drilling rig and support vessel employees	Introduce a tax exemption for income derived by employees working on seismic ships, drilling rigs or support vessels in New Zealand. Extend the “92 day exemption” to 183 days for employees working on seismic ships, drilling rigs or support vessels.		☑		For consistency we would like to see a similar tax exemption for foreign crew mobilised to support offshore activities.	Not addressed in Cabinet Paper	Officials have ben engaging with IRD on these matters - again we note only limited involvement from the sector, and general reluctance of IRD to contemplate derogations to the principle of a "broad low tax base" in their role as regulatory stewards.	
Royalties	Differential royalty rates for frontier basins	Offer differential (lower) royalty terms for early movers exploring frontier basins to encourage drilling of exploration wells.		☑		It might be appropriate to offer a differential basin-specific royalty regime	Addressed through recommendation 29 - Officials will review the royalty regime with a report back to Cabinet Q3 2024 seeking decisions on the recommendations.	Will be examined as part of a royalty regime review -see comment below.	Tentative green on the basis that this will happen - judgement on the process, level of engagement, and of course outcome is reserved.
	Royalty regime concessions	Options might include: - Remove the AVR component (5% of revenue) and retaining the APR component (20% of account profits) only. - Introduce new concessions (e.g. a royalty holiday for the first 20% of reserves). - Lower royalty rates for first movers in frontier basins - Remove ERL requirements for PMLs	☑	☑		Adjusting the royalty regime to manage security of supply concerns has been effectively tried before. We believe this could be an effective means to encourage bringing additional and new reserves to market.	Addressed through recommendation 29 - Officials will review the royalty regime with a report back to Cabinet Q3 2024 seeking decisions on the recommendations.	Advises Cabinet the Minister intends to undertake a review of the royalty regime as a means to encourage further exploration - we expect full and close collaboration with officials on the review - and we should recommend engaging outside expertise such as WoodMac.	
Reducing sovereign risk	Repeal ban on new exploration outside of onshore Taranaki	Will add to the overall resilience of NZs energy system, and help secure a smooth low emissions journey		☑	☑	Reversing this poorly conceived legislation is a necessary step in regaining our reputation as an investment destination.	Fully addressed in recommendation 7	Fully addressed - no further comment (other than to thank the Minister for his courage).	
	Streamlined consenting processes for exploration wells	Setting consent conditions for exploration well drilling can be an open ended and drawn out affair. The process and risks for this activity are well traversed and understood.		☑		The risks and mitigations for exploration well drilling in New Zealand are widely known and understood. This should be reflected in the consenting process, which has become unnecessarily drawn out and costly.	Not addressed in the Cabinet Paper	It is unclear if this is on anyone's radar as a priority issue - particularly in the offshore. We will again need to highlight this as a necessary step to facilitate the protection and rebuilding of our petroleum reserves through appraisal and exploratory drilling. Our preference would be to not rely on the fast track process as this legislation is deliberately broad in its application. Petroleum appraisal and exploration drilling is a specific and well defined activity, and the process should be able to be streamlined in specific regulations - including the need for public, stakeholder, and iwi engagement and consultation. But, the costly and open ended nature of the consenting process needs to be reviewed.	
Measures to Improve Administrative Efficiency	Clarify priority in time (PIT) processes for producing basins	Encourage near field exploration through a PIT regime for producing basins.	☑	☑		Any efforts to increase clarity around the availability of new exploration acreage is welcome.	Addressed in Cabinet Paper through recommendations 23 and 25.	Changes to the CMA and the Petroleum Programme will enable both a Block Offer and PIT approach for allocating acreage. Our preference was to ensure incumbent producers will have the opportunity to protect and rebuild our petroleum reserves in the short term, while retaining the option of a block offer process for frontier acreage. This appears to meet these requirements.	

	Defined block offer in frontier basins	Institute a new block offer process where the Crown calls for bids on a defined block in a frontier basin. Permit conditions would leverage some of the other measures offered here, such as reduced royalty rates.		☑		Considered a low priority to meet energy security concerns, but should be a consideration for future exploration.	Likely addressed in recommendation 23	Changes to the CMA signal the potential for a Block offer process, but the details of the process do not belong in primary legislation. We welcome the opportunity to work with officials to design a new process. We note that the previous Block Offer was premised on a highly competitive bidding environment. It is very unlikely this will be the case now or in the future - so the process and the allocation needs to be carefully designed to promote interest, and more importantly prioritise exploratory drilling.	Green on the basis that both PIT and Block Offer will be on the table for allocation of exploration acreage. We look forward to working with officials to ensure block offer in particular is fit for purpose.
	improve process efficiency and accountability	The activities in the upstream sector are well documented and understood. The efficiency and timeliness of approvals and consenting processes could be systematised and improved through standardised information and consenting timelines.		☑		Similar to the issues encountered for exploration well drilling, consenting and approvals processes have become unnecessarily time consuming and costly.	Not addressed in the Cabinet Paper	This will remain an ongoing and live issue for multiple sectors. Ultimately this will need to be addressed in resource management reforms . Our preference aligns with the recommendations of the Infrastructure Commission which moves the consenting authority from a consenting (approvals) based role to a monitoring based role for certain activities. A clear example of this is sediment control for earthworks. Currently a consent is required that explicitly details the provisions and measures an applicant will take to manage sediment. This in turn requires significant expertise on behalf of the consenting authority to assess these measures prior to granting consent. A far more efficient, cheaper, and widely adopted approach is to have specific standards and make the consent conditional on meeting these standards. Councils will then have powers of inspection and the ability to fine consent holders in the event of non-compliance.	These are cost reduction measures that make undertaking work less costly and more certain - they cannot be addressed through the CMA hence the red traffic-light.

Other	CCUS legislation	Establish a clear regulatory pathway for the handling, storage, and monitoring of CCUS projects that also establishes a clear liability regime for project proponents.	☑		☑	Clarification on the treatment of a reinjected separated carbon stream is a priority for the sector to improve emissions performance.	Not addressed in the Cabinet Paper - but sign posted in recommendation 33	Proactive release of this Cabinet Paper coincided with MBIE opening consultation on developing a CCUS regime for New Zealand - key for the upstream sector will be the treatment under the ETS and any post closure monitoring - for what is widely regarded as normal oil field practice.	Green as legislation is being advanced on the basis of recently released consultation by MBIE. Reserve the right to revisit the ranking as we progress!
	Gas storage	Amend decommissioning legislation to accommodate change of service from resource extraction to gas storage more attractive for fields at their end-of-life.	☑		☑	Worthy changes, but lower priority for addressing energy security and sovereign risk issues.	Not addressed in the Cabinet Paper	The confused and overlapping nature of the CMA obligations (intended to bring about decommissioning at the earliest convenience) and repurposing oil and gas infrastructure - including well pads, roads, water treatment pits etc. - still requires an exemption from decommissioning obligations by the Minister. This approach does not appear to address any issues with the transfer of obligation to decommissioning (depending on what has been repurposed). Again - we submit that addressing land use issues in the CMA undermines it's primary legislative purpose and the efficacy of environmental effects management legislation.	This will continue to be a part of our advocacy - the ongoing undermining of the legislative intent of the enabling legislation (CMA) and effects management legislation (EEZ and RM Acts).
	ETS reform	Maintain existing levels of industrial allocation to EITE to ensure carbon price doesn't get ahead of those of our trade competitors		☑	☑	Worthy changes, but lower priority for addressing energy security and sovereign risk issues.	Not addressed in the Cabinet Paper	Check with Angela on ETS reform and the ERP2 treatment	It remains highly unlikely we will be able to get upstream oil and gas as an exemption from the NZETS - particularly with agriculture remaining outside of the system. Our submission on the CCUS consultation (due 6 August) will look to address this from a post closure monitoring POV, and designation of reinjection of own CO2 is a normal oil field practice, so outside of the ETS if never emitted, and treatment of this as an avoided costs. We will also argue for appropriate depreciation and other incentives for these projects as a means to avoid emissions (gross reduction).

LEGEND HIGH MEDIUM LOW