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New Zealand

PEPANZ Submission – Review of the Crown Minerals Act 1991 Regime

Introduction

1. This document constitutes the Petroleum Exploration and Production Association of New Zealand's (PEPANZ) submission in respect of the review of the Crown Minerals Act 1991 (the "Act") regime and the proposals set out in the March 2012 discussion paper entitled "Review of the Crown Minerals Act 1991 Regime" (the "discussion paper"). PEPANZ represents private sector companies which hold petroleum exploration and mining permits, service companies and individuals working in the industry.

Overarching Comments

2. Whilst PEPANZ agrees with the objectives of the CMA Review and many of the specific proposals, the reality is the review is limited in its scope and does of itself not address many of the issues critical to determining whether the Government achieves its objectives in relation to development of New Zealand's petroleum resources. A holistic view is required as many of the actions are not directly connected to the regime for Crown owned minerals.

3. At current level of investment in petroleum exploration New Zealand's oil and gas reserves continue to diminish and royalties have fallen from a high in 2009 - 2011. To achieve the objectives of the Government's New Zealand Energy Strategy ("NZES") we consider the Government must adopt a bolder strategy including:

   - more strongly supporting the objectives of the NZES by articulating the ways in which the development of petroleum resources is in the national interest;
   - establishing a formal advocacy role for the discovery and development of Crown owned minerals within government, and including a purpose statement into the Act that emphasises that the purpose of the Act is to "facilitate timely investment in the discovery and development of Crown owned minerals";
   - formalising shorter and aligned timelines for the various applications/consents required by industry; and
   - improving inter-agency co-ordination.

The New Zealand Energy Strategy will not be achieved under current policy settings

4. The NZES, adopted in late 2011, sets the strategic framework for the development of petroleum resources which the Government wishes New Zealand to pursue and states that *"The Government wants New Zealand be a highly attractive global destination for petroleum exploration and production investment so we can develop the full potential of our petroleum resources."*

5. The Government has stated that it wants the economy to *grow, powered by increasing energy exports*. The immediate focus is to be *on increasing exploration activity and improving the knowledge of our various petroleum basins*. To achieve these goals the NZES states that *markets must be effective and efficient, and that the Government may need to consider the provision of incentives, information and remove regulatory barriers*.

6. While the discussion paper proposes important adjustments to the legislative framework, it is silent on how the measures proposed will assist in delivering on the NZES over the next 10 years. At the current level of

investment in petroleum exploration New Zealand's oil and gas reserves continue to diminish and royalties have fallen by c$50m from '09-'10 to '10-'11. Neither the NZES, the Act, or this discussion paper provides any clarity on a reserves replacement strategy or address the issue of energy security for New Zealand.

7. The challenge facing New Zealand is that there are too few exploration companies undertaking too little exploration to ensure that existing reserves are replenished at a rate that would sustain the current royalty and tax take. Historical precedents suggest that it may take as long as 20 years from initial exploration to developing a producing asset in New Zealand (Kupe and Maari). While some fields (Tui and Pohukura) have been brought to market more quickly (5 years) it is generally accepted that 7 – 10 years is a "normal" timeframe.

8. Our reserves are being depleted in New Zealand with no substantial new discoveries currently waiting to be brought to market. Current legislative initiatives, as detailed in the discussion paper, are unlikely to result in any material increase in new exploration over a prolonged period in frontier basins. The development of a second basin to complement Taranaki is considered a "game changer" in terms of New Zealand's prospectivity. Therefore building momentum in exploration will require legislation that actively supports the establishment of new entrants and incentivises existing players to target prospective new basins.

9. There needs to be a much closer alignment between the objectives of NZES and legislation. Government must adopt a bolder strategy of legislation changes supporting to the NZES if it wishes to substantially enhance the chance of offshore discoveries, build energy security, provide cost effective energy for New Zealand's future growth, develop new employment opportunities, enhance regional New Zealand and boost royalty and tax income for New Zealand.

10. The following sections of this submission detail some opportunities for substantial changes to policy which PEPANZ recommends the Government consider.

Advocacy role for Government

11. We submit that both the Government and MED need to take a much stronger position defending the objectives of the NZES and articulating to New Zealanders the ways in which the development of petroleum resources is in the national interest.

12. The sector is currently the 4th largest earner of export revenue and gas production underpins our wider energy system. With our substantially unexplored EEZ there is a huge opportunity to realise the benefits of appropriate development for the New Zealand economy whilst protecting the environment.

13. We submit that MED should be tasked with taking an advocacy role for development of the mineral estate the Crown administers on behalf of all New Zealanders, in much the same way that the Conservation Act requires the Department of Conservation to be an advocate for conservation.

Interagency Cooperation

14. Another area where the Government must improve performance is in the area of inter-agency cooperation. With 6 central government agencies which the industry must deal with there is a need for greater cooperation between agencies to ensure decision making can be as efficient and effective as possible. Many countries we compete against for exploration and production investment have more integrated and efficient processes for managing the approvals required to undertake petroleum related activities. Formal and potentially aligned timelines for processing the various applications/consents required under legislation would also provide increased certainty to industry for decisions concerning what can be substantial investments.

15. We support the proposals for an annual work plan review of permit holders operations be included in the Act. Those meetings should be led by MED and attended by all relevant agencies to plan and prepare for future consent applications which might flow from a permit holder's activities.

16. To industry it also appears that there has traditionally been inadequate discussion between agencies about the planning or timing of future legislative or regulatory changes, although we note some positive signs recently.

Royalties

17. The discussion paper was released with a companion paper examining royalty matters. It concludes that the existing regime is generally fit for purpose with no significant changes proposed. This recommendation is at odds with discussions that have occurred over the past 3 years where officials have indicated a potential willingness to remove the AVR component of the existing royalty regime.

18. PEPANZ notes that the current petroleum royalty regime can be burdensome, particularly the Ad Valorem Royalty ("AVR"). This is because AVR is determined based on a company's net sales revenue rather than its profits and, as such, is levied irrespective of the cost associated with production. This results in projects that were economically feasible becoming uneconomic to develop after the AVR is levied. The AUPEC Report, released by MED in 2009 noted that this was a concern for marginal gas projects and recommended the AVR be significantly reduced or, alternatively, replaced with a different regime.

19. A less significant change would be to adjust the regime so that AVR could be paid initially but if a permit moved to paying an Accounting Profits Royalty ("APR") it would not return to paying AVR. This would ensure that the Crown receives a royalty from initial production but removes the risk of the application of the AVR leading to fields being abandoned earlier, with more hydrocarbons left in the ground than would be the case under a continuing APR. This can be significant as once a field is abandoned it is highly unlikely that it would be re-entered, whereas if a field remains in production there remains the possibility that new investments will be made to increase or prolong operation that could not have been foreseen at an earlier time.

20. PEPANZ submits that the existing APR should be retained at the rate of 20%. However, we note the current royalty regime is based on Generally Accepted Accounting Practice ("GAAP") and there are no transitional rules in the event that there are changes in GAAP. Further, NZPM has indicated that, in some circumstances, GAAP for financial reporting purposes will not necessarily dictate the treatment under the royalty regime, as it is the "intention" of the legislation which is the paramount consideration. This creates uncertainty for petroleum mining companies and leads to disputes with NZPM.

21. Accordingly, PEPANZ recommends that the Accounting Profits Royalty ("APR") methodology should be amended so that the starting point is the concept of "taxable profits" for income tax purposes (with adjustments to allow "front ending" of development costs). This would remove the existing problems associated with GAAP interpretation and would lower the compliance costs associated with performing separate detailed calculations for both tax and royalty purposes.

22. In addition, the use of taxable profit as a starting point for the APR calculation would mean that deductions are available for general administration costs, financing costs and exploration expenditure incurred in and outside the relevant permit area.

23. If the Government were of a mind to open a dialogue with industry over more substantive changes to the royalty regime there are other changes to the royalty regime that could be considered to stimulate investment. For example, options might include re-introducing the royalty concessions that applied between 2004 and 2009 or introducing new concessions such as a royalty holiday for the first 20% of reserves.

Petroleum taxation

24. The discussion paper is silent on anything to do with petroleum taxation. Of these, the most important from an industry perspective is the need for further consideration to the tax deductibility of exploration expenses incurred in deep water frontier basins.

25. The Association suggests the Government give serious consideration to adopting a refundable tax credit for exploration. Companies who already have a tax base in New Zealand are entitled to corporate tax relief at 28% of their exploration costs, thus the net cost of unsuccessful exploration is 78% of the total costs. However, new or existing entrants who do not have a tax base in New Zealand obtain no relief. A refundable tax credit would "level the playing field" and make oil exploration in New Zealand more fiscally attractive to petroleum mining companies who are not currently taxpayers.

26. This is but one of many possible changes that could be considered to improve the likelihood of attracting new entrants. Whilst we recognise the current seriousness of the Government's fiscal position it may require Government to invest some money up front to stimulate investment to ensure a better, and earlier, royalty return in future.

Specific Comments on the Discussion Paper

Review Objectives

27. PEPANZ generally supports the objectives of the review, namely:

- to encourage the development of Crown-owned minerals so that they contribute more to New Zealand's economic development.
- to streamline and simplify the regime where appropriate, ensuring it is in line with the regulatory reform agenda, and make it better able to deal with future developments.
- to ensure that better coordination of regulatory agencies can contribute to stringent health, safety and environmental standards in exploration and production activities.

With respect to the last of these objectives PEPANZ made extensive submissions to MED in February 2011, responding to a discussion paper on proposed changes to the offshore health, safety and environmental regime. At that time we expressed some reservations about the wisdom of NZPM (Crown Minerals as it then was) taking on a broader mandate to consider the health, safety and environmental track record of companies wishing to bid during a blocks offer round.

28. We were not opposed to the Government having regard to those matters, but expressed doubts about whether giving those powers to the Minister of Energy and Resources would conflict and or complicate the Minister's functions in his/her decision making role under the Act. This matter is again canvassed in detail later in this submission in our responses to questions 1, 7 and 8.

Review Principles

29. We support the 6 broad principles which underpin the review and the view expressed by officials that regulatory efforts should focus on operations that have the highest technical and geological complexity, and which have the greatest potential to generate royalty revenue for the Crown. Proactive management of these types of operations support the broad purpose of the Act which is to ensure a fair financial return to the Crown.

30. We also support greater coordination among regulatory agencies, iwi and other stakeholders. There has been a significant improvement in cross agency dialogue in recent months and we would like to see this continue. PEPANZ would welcome more significant involvement with officials on interagency cooperation.

Chapter 2 - Health, safety and environmental (HSE) matters

31. The industry places significant emphasis on executing operations in a manner which protects the health and safety of both its employees and the environment. In New Zealand, there have been no fatalities in the industry for over 15 years, very few lost time injuries, and only 2 minor spills of oil to the environment – both of which were quickly cleaned up and created no permanent damage.

32. Ensuring we continue to deliver good outcomes in this area is critical to maintaining the industry's "social licence to operate".

Q1. ***(a) Do you agree that including assessment of applicants' HSE policies, capability and record in the initial stages of the permit allocation process is desirable?***

33. PEPANZ agrees that it is desirable to consider the HSE policies, capability and track record of applicants in the initial stages of the permit allocation process along with the current consideration of technical and financial capability and prior activities in New Zealand and globally. This will help to ensure that acreage is not allocated to a company that cannot give effect to the permit (for example, because they will fail to meet the

requirements of HSE legislation to carry out activities under the permit) and provides a level of assurance to the public that a company awarded a permit to undertake exploration activities in New Zealand has demonstrated a certain level of capability to carry out those activities in a safe and environmentally sound manner.

34. We do, however, have reservations that the clear decision making process under the Act and Minerals Programme which exists at present could be complicated by introducing HSE considerations, which are currently dealt with by other agencies with the requisite expertise, under other regulatory frameworks, ahead of a particular activity being carried out.

35. Given the significance of being excluded from the blocks offer process or permit award, there will need to be clear guidelines for industry in terms of information to be submitted and the factors that will be taken into account in approving or declining prequalification or a permit award based on HSE capability. In particular, how will a company with no track record of carrying out certain activities be assessed or a company who has a long history of carrying out relevant activities but which may have suffered some adverse HSE incidents in the past?

36. The discussion paper anticipates that the Department of Labour would advise on an applicant's health and safety record. The proposed merging of the Department of Labour with MED (and two other agencies) would seem to imply that this assessment will be done within a single agency in future. The discussion paper states an "agency with appropriate expertise in environmental resource management" will assess the environmental information. We note that currently only one regulatory body at a regional level has this expertise, the Taranaki Regional Council. At central government Maritime NZ, DOC and the Environmental Protection Authority all have different roles in consenting to some aspects of a development. There needs to some centralised oversight of this process to ensure consistency.

37. It is unclear what level of discussion and consultation will occur between the respective agencies and the applicant, or by MED on their behalf, ahead of a decision to decline prequalification or decline the award of a permit based on HSE capability. In the interests of natural justice, we expect that an applicant would have an opportunity to meet with officials to discuss the grounds of any proposed decline and be afforded an opportunity to submit further information or reapply.

Q1. (b) Which of the two options presented do you prefer? (Paragraphs 29/46)

38. We prefer a pre-qualification system (option 1).

39. Granting a prequalified company a five year qualification to participate in blocks offers, avoids duplication of effort in subsequent blocks offers and should reduce costs for most industry members, particularly those likely to apply for multiple permits over a five year period. We recognise this option has the disadvantage of involving officials in examining the policies, capability and track record of companies who may subsequently be unsuccessful in having a permit awarded to them.

40. It is unclear from the discussion paper whether the intention is that a potential permit applicant could apply for prequalification at any time or only at the time of a block offer. Our view is that companies should be able to apply to become prequalified at any stage. We suggest there could be merit in establishing a public register of companies which have achieved pre-qualification status as this would increase transparency.

41. The proposal for pre-qualification also doesn't indicate whether companies will be pre-qualified for specific operations – for example onshore operations, nearshore or deepwater and/or whether there would be a different approach to those firms intending only to apply for prospecting permits. We would have thought this may be appropriate.

42. Whereas option 2 would presumably be given effect to under section 27 of the Act it is unclear from the discussion paper what legal status a pre-qualification decision would have and exactly who would make it, i.e. the Minister or MED, and if so who within MED. Further consideration may also need to be given to the parameters around a five year qualification period – what happens for example if an operator has a significant HSE incident during that period or a change in ownership?

43. Should option 2 be progressed we recommend that assessment of HSE capability is undertaken as part of the blocks offer process, but only in relation to the preferred bidder for a block. This would reduce costs for government and industry as only the preferred bidder(s) for a block would be required to undergo HSE assessment.

Q2. ***(a) Do you think that annual review meetings would provide a better mechanism for permit holders and the Ministry to exchange information and discuss work programmes than the current paper-based approach? (b) Do you consider that a regular meeting with the Ministry and other appropriate agencies would improve coordination between permit holders and the various parts of government?***

44. Yes to 2(a). There is however a need to ensure that MED avoids micro managing permit holders and their obligations. We note that annual review meetings will impose resourcing/capability issues on MED which need to be clearly thought through as there are 82 active petroleum permits. If these face to face meetings are all to be conducted in the 2nd quarter each year it suggests a heavy workload for NZ Petroleum and Minerals staff, with more than 1 meeting per day to complete the review within a 3 month timeframe. We recommend that a portfolio type approach is taken to increase the efficiency of interactions between those industry players with interests in multiple permits. There also needs to be some focus and structure to these meetings with attendees limited to those with specific interests in the relevant permit/s.

45. Yes to 2(b). However it is important that there is some structure and formality established around such meetings. They need to have specific objectives and a clear understanding among the parties about who is attending and why. In particular, it will need to be clear to how information supplied by permit holders in these meetings is used by the participating agencies (please also refer to our response to questions 44 and 45).

Q3. ***Do you agree with the proposal to distinguish in the Act between permit operators and non-operators?***

46. Yes. However, it will be important to make clear what the Operator status means in terms of administering the permit and the regime, for example, what the Operator can and cannot do without the signature of the other permit holders (in terms of permit applications and changes etc). Any formal notices under the permit or the Act or regulations (such as in the event of non-compliance) should continue to be served on all permit holders.

Chapter 3 - Iwi Engagement on Crown Minerals (Paragraphs 58/77)

47. The WAI 796 report identified a number of shortcomings in the management of the petroleum resource. Concern was expressed at the lack of resourcing within iwi and hapu to respond to proposed petroleum minerals programmes, permit consultation and RMA consent applications. We note Iwi have also expressed concern that their submissions seeking land be excluded from an operative minerals programme are not always acted on.

48. In general we support better resourcing of iwi and hapu by central government because it facilitates positive engagement with industry. In paragraph 74 of the discussion paper there is a suggestion that industry work with government and iwi to develop guidelines and case studies on effective engagement. Industry would welcome involvement in such an initiative. Industry considers that a set of guidelines, even at the most general of levels, would help signal to new entrants what is expected around iwi consultation.

Chapter 4 - Petroleum

Q4. ***Do you consider the proposed changes would better incentivise non-exclusive geophysical survey activity? (Paragraphs 80/83)***

49. Yes, particularly if a longer confidentiality period is introduced. The longer that the company has exclusive ownership of the information collected the more likely it is a speculative survey will be conducted.

Q5. ***Do you consider that additional changes are necessary to encourage non-exclusive geophysical surveys to be conducted more frequently?***

50. We note that the requirement for iwi consultation ahead of grant of a PPP may mean that for large scale surveys, particularly onshore, there may be protracted consultation with a number of different iwi and hapu groups. Also, the potential for areas of importance to iwi and hapu to be excluded as part of that process may complicate the acquisition of data. Further consideration may need to be given as to how the Ministry could ensure this process is facilitated so that it does not become a disincentive to companies conducting speculative surveys in New Zealand.

51. As noted below, we would like further engagement with the Ministry on how speculative survey data is expected to play a part in future block offers.

Q6. ***Should PPPs be granted over currently-permitted areas? (Paragraphs 89/90) If so, should the consent of the existing exploration or mining permit holder be required before a PPP is granted?***

52. We recognise that the ability to acquire data irrespective of underlying permit rights may increase the attractiveness of conducting speculative surveys in New Zealand. However, we have a number of concerns in relation to this proposal.

53. We consider that data acquired over a permitted area by a speculative survey company could create an unfair advantage for those who choose to purchase it, for example, in the context of a block offer on expiry, farm down surrender or revocation of the permit. We would like to discuss with MED how such data is expected to play a part in future block offers and whether the Crown intends to continue its seismic acquisition programme to promote block offers by making information freely available.

54. It is currently common practice for operators to enter into trespass agreements with other permit holders to acquire data over neighbouring permit areas, often in exchange for release of that 'trespass' data to the underlying permit holder. It is unclear from the discussion paper whether the PPP holder would be required to provide data acquired in a permitted area to the permit holder and how this would be treated for release under section 90 of the Act upon the expiry, surrender or revocation of the underlying permit.

55. If speculative surveys are allowed to be conducted over permitted land, we do consider that consent from the underlying permit holder should be required. The reasons for this are primarily:

    a. In onshore areas, operators often have numerous landowner access agreements and stakeholder engagement protocols with iwi and hapu that have been developed over a number of years and are essential to the operator's 'licence to operate' in the community. It is therefore critical that these relationships are maintained and are not compromised by third party acquisition companies who will not have a continued engagement with the community after completion of the speculative survey and whose drivers are therefore not necessarily aligned with the operator's in managing the stakeholder engagement process.

    b. In both onshore and offshore areas, it will be essential that activities of a speculative survey company are undertaken at a time and in a manner that does not interfere with a permit holder's activities in the permit area. This is likely to require coordination and may include undertakings that personnel undertaking the survey will comply with an operator's HSE policies in respect to access to certain permit areas etc.

56. Finally, we think consideration may need to be given to whether acquisition companies conducting one-off onshore speculative surveys could give rise to land access payments that create unreasonably high expectations in the community, which would be difficult for companies maintaining long-term relationships to meet.

Q7. ***Do you have any comments on the proposal to introduce HSE considerations for petroleum – either through a prequalification process or through a consideration of HSE matters during the evaluation of permit applications? (Paragraphs 91/97)***

57. We support a prequalification process. Please see our response to question 1.

Q8. ***Do you consider that such considerations should be made for all petroleum operations or for a subset of them?***

58. We see no reason why the HSE capability requirements should not apply to all petroleum operation. Whether through a prequalification or permit application process it is however important that applicants HSE capabilities are fairly judged against what they are intending to apply for in terms of acerage.

Q9. ***Do you consider that longer exploration permit durations are necessary for thorough work programmes to be delivered? (Paragraphs 98/109)***

59. Yes based on historical experience in New Zealand.

Q10. ***Do you agree with the proposed shift from a single five-year permit to a structure that distinguishes between different exploration contexts?***

60. Yes. We support the proposed phased approach to exploration permits and the distinction between onshore, shallow water and deep water offshore permits and the proposed terms of 9, 12 and 15 years.

61. It is not clear from the discussion paper whether the new permit phase durations will be specified in the Act as maximum permit durations (as is currently the case) or whether there will be Ministerial discretion for the term to be extended. For example, if a permit holder is prevented from carrying out activities in a particular phase for reasons beyond its control, is that phase able to be extended rather than reducing the time available for activities in the next phase (or at the end of 9, 12 or 15 years)?

62. Whilst there is no universally agreed definition for the boundary between shallow water, deep water and ultra-deep water drilling 500m is an appropriate delineation between shallow and deep water areas. Water depth is only one factor. Other factors such as formation pressure, geological structures, equipment capability and logistics all contribute to and can accumulate to increase the complexity of undertaking exploration, particularly drilling.

Q11. ***Do you think that annual review meetings would provide a better mechanism for permit holders and the Ministry to exchange information and discuss work programmes than the current approach? (Paragraphs 110/114)***

63. Yes. See our response to question 2 above.

Q12. ***Should the annual review process be adopted only for new permits or should it also be adopted for existing permit holders?***

64. We submit that it should apply to existing as well as new permit holders. It would seem inconsistent to have two different regimes operating.

Q13. ***Do you agree that judgements about compliance with work programmes should be made at the end of particular phases and at intervals of at least three years? (Paragraphs 115/122)***

65. PEPANZ welcomes commitment dates which allow greater flexibility to manage the work programme within a particular phase. While we are not opposed to the removal of "reasonable efforts" from section 39 it is important that some flexibility remains in the regime to provide for force majeure or where permit holders can provide good reasons for why they have not met commitments within agreed timelines.

66. However, it is not clear whether it is intended that a permit would be able to be revoked within a phase if it was apparent from the annual review meetings, or otherwise, that a permit holder was not making reasonable efforts to carry out the work programme. The concern is the possibility of having a permit area unavailable for the full 3, 4 or 5 year phase before revocation action could commence.

Q14. ***Do you agree with the proposals on primary and secondary work programmes and the expectations on the change of conditions? (Paragraphs 123/135)***

67. PEPANZ supports the proposed approach in principle. We support the stated policy that where permits are awarded by competitive bidding a permit holder will be expected to carry out its bid work programme unless factors outside of its control make this unachievable.

68. We note that the discussion paper proposes to exclude extension of land applications except where a discovery extends beyond the permit area (although no specific question is provided in the paper). It is not clear whether this is intended to apply only to new permits granted under the new regime, or is intended to cut across existing permit holders rights (which we submit would be unreasonable).

69. This would be a significant change from the current policy which recognises that the ability to extend the area of a permit may facilitate a more rational carrying out of activities under the permit. We consider the ability should be retained and competing interests considered as part of the block offer process. For example, a permit holder may have identified a lead or prospect extending beyond the boundary of the permit but may not wish to bid for a new exploration permit over the area as the prospect can be drilled most efficiently from the existing permit. To 'outlaw' such applications seems to assume to competitive processes will always lead to the best results and may run counter to the policy of allocating permits to the person who is most likely to effectively and efficiently prospect or explore and develop the petroleum resource.

Q15. ***Do you agree with the proposals on notification of discoveries and the subsequent definition of the appraisal permit? (Paragraphs 136/142)***

70. Yes

Q16. ***Do you agree with the proposals on relinquishment and surrender of acreage? (Paragraphs 143/146)***

71. It is unclear from the discussion paper the likely size of the blocks that will be allocated in the future. It is therefore uncertain as to whether a 25%/25% relinquishment will be appropriate. The concern here is whether in the timeframes allowed a permit holder will have been able to sufficiently acquire, process and interpret data to make informed decisions on surrender of acreage. For example with large deep water blocks with multiple leads it could be hard to prove up before 50% of the block would have to be relinquished.

72. We also suggest that where a permit holder has identified leads and prospects across the full permit area, it is not in the Crown's best interest to have to wait for someone else to take that acreage up in a subsequent blocks offer and carry out its own exploration programme before those leads and prospects are developed.

Q17. ***Do you agree with the proposals on the regular review of production permits? (Paragraphs 147/152)***

73. Yes. We understand the Crown's objective in ensuring that production rates are not damaging the ultimately recoverable reserves from the field, allowing the Crown to maximise its economic return over time. However, what is not clear from the discussion paper is how production rates might be incorporated into the mining permit conditions and whether the Crown might seek to unilaterally change such conditions.

74. The concern here is the risk of creating uncertainty at the point a decision is made to develop a resource based on a particular production model. We also note that actual reservoir performance can of course differ from original production modelling.

Q18. ***Do you agree with the proposals to have separate parts within new minerals programmes in order to accommodate distinct mineral types? (Paragraphs 153/160)***

75. We agree that there is a need to develop policy concerning the permitting of coal seam gas and methane hydrates. Proposed amendments to section 15(2) of the Act and the new parts within the Minerals Programme for Petroleum to provide for coal seam gas and methane hydrates seem appropriate.

76. As we noted in our submissions in 2010, PEPANZ believes that a significant amount of further work needs to be done in relation to the technical and HSE issues that may arise if methane hydrate activity and conventional petroleum activities are undertaken in the same land area. We look forward to working with officials on development of that policy. This work needs to be undertaken before granting overlapping permits for methane hydrates and conventional petroleum activities in the same land area.

77. Despite advances in the understanding of the formation of gas hydrates, PEPANZ is of the view that the means of commercially recovering gas from hydrates is far from proven. In light of this, we support the development of policy on methane hydrates, but suggest government exercises caution so as not to delay or impede the exploration for and development of conventional petroleum resources in the intervening period. The Association would not support policy development which allows areas to be permitted on an exclusive basis where the work programme targets methane hydrate activity to the exclusion of conventional petroleum activities.

78. Further consideration and guidance on how MED will approach evaluation of block offer bids for different hydrocarbon mineral types would be welcomed.

Chapters 5 and 6 - Tier 1 & Tier 2 minerals

79. These chapters relate to non-petroleum minerals and are not commented on by PEPANZ.

Chapter 7 - Royalties

Q41. ***What changes, if any, would make royalty administration, assessment and collection more efficient for the government and make compliance easier for permit holders?***

80. The discussion paper examines in Paragraphs 327/339 various administrative arrangements for managing the royalty regime going forward, including that of transferring the function to IRD. PEPANZ supports royalties continuing to be administered by MED.

81. We have made comments in paragraphs 19 to 25 of our submission above regarding substantive policy settings for royalties (Paragraphs 319/326 of the discussion paper).

Chapter 8 - Other matters

Q42. ***Do you agree with the proposals for the objectives to be set out in a purpose statement for the CMA? (Paragraphs 341/346)***

82. PEPANZ agrees the concepts underlying the two statements listed in paragraph 345 should be incorporated in a purpose statement although we question whether efficient allocation is more a method than an objective in itself.

83. We also recommend that ensuring that New Zealand's petroleum regime will attract investment, thereby facilitating discovery and development of the Crown's resources, should also be clearly reflected in a purpose statement. A fundamental purpose of the Act is to facilitate and promote the discovery and development of the Crown's mineral resources, which it administers on behalf of all New Zealanders.

84. Issues expressly provided for through other legislation such as the Resource Management Act do not need to be provided for in the purpose statement as they do not relate to the purpose of the Act.

85. We suggest the following wording as a purpose statement:

"An Act to facilitate timely investment in the discovery and development of Crown owned minerals"

Q43. ***Do you agree with the proposals on alignment of permitting provisions across the relevant legislation?***

86. This proposal relates to non-petroleum minerals and is not commented on by PEPANZ

Crown Use of Information Provided by Permit Holder

Q44. ***(a) Should the Act be amended to clarify when information about an operation should be able to be shared with, and used by, another government agency or regional authority that has functions and powers that apply to the same permitted operation? (b) If so, what information/agencies should the legislative change apply to? (Paragraphs 358/360)***

87. Yes. However only data that is relevant to decision making by the receiving agency should be shared and permit holders should be made aware in advance what information will be required. There also needs to be strict rules (subject to the provisions of the Official Information Act) concerning information being shared, particularly where that information is commercially confidential.

88. If the Crown decides to proceed with pre-qualification, legislation should anticipate the sharing of information before a permit is awarded and have strict rules/policies in place regarding the distribution and use of the information.

89. Relevant agencies would seem to be the Department of Labour for health and safety information; DOC, Maritime NZ, the EPA/MFE and Regional/Territorial Councils for environmental information. Which agency is involved will be determined by where the proposed permit is located. Outside the Territorial sea it will be the EPA, inside the Territorial Sea the relevant Regional and/or District Council. We note that most local authorities in New Zealand have no experience in assessing resource consent applications for our sector.

Q45. ***(a) Do you agree that the Act should be amended to clarify what, and when, information received by the Ministry should be confidential? (b) If so, to what information, and in what circumstances, should confidentiality apply?***

90. Yes, please see comments above about information received during the prequalification phase. All that information needs to be kept confidential until the final decisions on applicants are made, including that information shared with other agencies – which may require appropriate changes to the legislation of the agencies receiving data from MED.

91. We consider that the information shared can be limited to that provided in respect of a particular aspect of the application. For example, we would expect the block offer notice to ask for specific documents to evidence HSE capabilities (company policies, track record etc.) we would expect only this specific information to be provided to the relevant assessing agency, not the full application. Apart from information already in the public domain, we would expect that information in a permit application would be treated by all agencies as confidential and commercially sensitive and consultation with the applicant would be expected before release under the OIA in every case.

Q46. ***Do you agree/disagree with the series of proposals to address the release of data and reports? (Paragraphs 363/367)***

92. We disagree. Unless we have misunderstood the proposals outlined in Paragraph 366, this would mean that data pertaining to a permit that had not been surrendered would be released. It seems to us that this is an

internal issue for MED to resolve given that section 90 is clear as to when data becomes publicly available. MED just needs to set and enforce clear rules about the release of data for permits that are surrendered, especially if data is collected across several permits but lodged only under one permit.

Q47. ***Are current offences and penalties the most appropriate mechanisms to promote compliance? If so, at what level should fines be set; if not, what alternate or additional mechanisms might be more effective and efficient? (Paragraphs 368/369)***

93. PEPANZ considers it appropriate that penalties are inflation adjusted as proposed in paragraph 368. It is not apparent why other sanctions drawn from civil and/or criminal systems are appropriate or necessary to promote compliance under the Act.

Removing the Statement of Reasons (Paragraphs 370/371)

94. PEPANZ supports the proposal to remove the statements of reason for the adoption of certain polices from Minerals Programme for Petroleum.

Removing section 25(2) - Crown Participation (Paragraph 372)

95. PEPANZ supports the repeal of this provision.

Q48. ***How should potential conflicts between minerals programmes be resolved? (Paragraphs 373/374)***

96. PEPANZ believes that the rights granted to the first permit holder must have priority over those created by the grant of a right under any subsequent minerals programme.

Q49. ***Do you agree with the proposals related to processes around transfers and dealings? (Paragraphs 375/380)***

97. Yes. We support the proposal to change the existing procedures for permit transfers and dealings so that parties can assume that Ministerial consent is not required, unless advised to the contrary. We consider however that a period of 20 working days (effectively one month) following notification to the Ministry would be a more appropriate period than 40 working days.

Annex 1: Petroleum Data and Reporting

Notices (Paragraphs 382/393)

Add new regulations to ensure that the Ministry is notified about relevant activities by permit holders

98. PEPANZ supports broadening the range of notifiable activities to include:

- the discovery of a hydrocarbon accumulation
- the commencement and conclusion of well stimulation operations (including hydraulic fracturing)
- the commencement and conclusion of well workover operations
- the abandonment of a well.

Amend regulations requiring survey and drilling notices to be provided to the Ministry to additionally require proposed names for surveys or wells to be included in the notice

99. PEPANZ supports this proposal.

Reports (Paragraphs 394/437)

Reduce the six-monthly reporting timeframes for petroleum permit holders to annual timeframes and align with royalty reporting dates

100. PEPANZ supports this proposal.

Amend the expenditure reporting regulation to clarify that annual expenditure totals are required for the items listed in the expenditure report regulation

101. Agree

Amend the prospecting and exploration regulations to include, for each well, any well stimulation activities carried out and their purpose

102. The purpose of collecting this information is not clear. There are many activities undertaken when drilling a well which are not reported on. It would be helpful if the Ministry could explain why this information is required.

Amend the supply deadline for a number of reports and records to better reflect the reasonable timeframes required for permit holders to be able to supply certain information to the Ministry

103. Agree

Amend the well completion reporting regulation to additionally require permit holders to report on any well stimulation activities that are undertaken down hole

104. Agree

Remove the core analysis and microfossil record regulations and include the requirement to supply these records as Paragraphs in the well completion regulation

105. Agree

Amend regulation 45 so that the relevant schedule also requires daily drilling reports to include details of any work-over activities and well stimulation that have been undertaken in the relevant reporting period

106. Agree

Amend petroleum regulations (as detailed in this chapter) to improve the quality of published information on gas reserves as well as that provided by industry to government about the Crown's petroleum resources

107. PEPANZ made detailed submissions on this issue to MED in September 2010. The proposal to proceed with the collection of P10 reserves estimates is noted. Our position has not changed.

108. We do not understand the purpose of publishing P10 numbers. P50/90 reserves tend to be a realistic expression of field performance in the long term. Provided a standard is used to ensure all operators are consistent in their methods of estimation, P50/90 reserves provide the best reserves for use in policy and decision making by the market. It is standard practice for companies to report both P50 and P90.

109. The options paper released in 2010 suggests that moving to P10 reporting would provide visibility of upside potential at existing fields. Whilst most companies collect P10 numbers and report them internally, it must be understood that the technical rigour applied to the estimation of P10 reserves and Contingent Resources is far less than that applied to P2 reserve estimates. If MED were to simply add P10 estimates together by field it would, in our opinion, provide a far too optimistic forward scenario. (In much the same way that applying the same approach to P90 reserves would result in too pessimistic a forward view of reserves).

110. In our opinion the options paper released in 2010 did not justify why P10 reporting was required. It is still not clear to us what the problem is.

111. The options paper was predicated on the assertion that there are significant annual swings in reserves which is said to erode confidence in the figures being supplied, and undermines the ability of officials to use the data for planning purposes. The implication was that the industry is responsible for this situation.

112. Some of the variability of reserves predictions is due to 4 very real facts of the NZ oil and gas environment:

- there is a small population of large fields near the end of field life where a small variation in recovery has a large influence on remaining reserves;
- there is a relatively large number of small fields, with no convincing analogues in the area, in their early stages of life where reserve predictions are subject to large fluctuations as events develop;
- product price fluctuations change the reserves to a large extent as they change the expected economic life of fields, thus the reserves that may be booked. In all cases the inaccuracy is unavoidable no matter what reporting standard is invoked;
- on-going reservoir management activities in producing fields, like reservoir modelling (including history matching pressures and water), fraccing, work-overs, infill drilling, etc. mean that reserves are reassessed regularly, and that the resulting reserves revisions are the natural consequence of active reservoir management. In fact it would be more of a concern if the numbers did not change (except for removal of historical production) because it could mean that a field is not being actively managed.

113. While it is understandable that downstream gas users wish to have certainty about New Zealand gas reserves for the purposes of planning and investment, the above features of our industry cannot be avoided. Nor will the introduction of P10 reporting reduce that uncertainty for them.

114. In our view including P50 and P90 numbers in the published reserves best reflect the "expected" and "reasonably certain" view of the world. They have also been proven by the stock markets as the most relevant in determining oil and gas companies' future production levels.

115. If MED wishes to pursue P10 reserves reporting we will make further submissions at the Select Committee stage on this matter.

Streamline section 41 of the CMA by placing a specific requirement in the annual expenditure reports to the Ministry

116. Agree

Adopt a consistent approach to the use of individual regulations and schedules when the next regulations are made

117. Agree

Publish annual production data on a well-by-well basis

118. The unintended consequence of his may be to disclose data about field performance which is not currently available to a competitor. The Association is opposed to the proposal.

Make survey and well header information publicly available immediately

119. Yes.

Long-term gas sales agreements

Q50. ***Do you agree/disagree with the proposal to make permit holders submit any long-term gas sales agreements to the Ministry?***

120. We oppose this proposed requirement.

121. This is a commercial matter between the parties to the contract. The proposal to require this information to be disclosed in annual expenditure reports seems out of place and the discussion document does not provide compelling reasons for why this information is required from permit holders under Act.

122. Should this proposal nonetheless be progressed we consider a six month threshold is too short and suggest, if this is to be introduced, only gas sales agreements in excess of 3 years duration. Short duration contracts are commercially sensitive and do not paint a material picture. Long-term contracts of greater than 3 years will provide the government with a clear position on the allocation of resources.

Publication of annual production data

Q51. ***Do you think that annual production data should be made available on a well-by-well basis in addition to the current field production totals published in the Energy Data File?***

123. PEPANZ is opposed to this proposal, as it would provide much greater detail on field performance to non-permit holders than is currently the situation. The discussion paper gives no compelling reasons for why this information should be disclosed.

Make survey and well header information publicly available immediately

Q52. ***Do you agree with the proposal to make survey and well information publicly available immediately?***

124. Yes

Annex 2: Mineral data and reporting

125. This Annex does not affect the petroleum industry and no comment is provided.

Annex 3: Proposals considered but not pursued

126. Noted, no comment required.

David Robinson
Chief Executive