



COVERSHEET

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| Minister | Hon Dr Megan Woods | Portfolio | Energy and Resources |
| Title of Cabinet paper | Regulatory Framework for Decommissioning Petroleum Infrastructure and Enforcement - Strengthening the Crown Minerals Act 1991 Regime | Date to be published | 30 July 2020 |

List of documents that have been proactively released

| Date | Title | Author |
|--------------|---|--|
| 17 June 2020 | <i>Cabinet paper:</i> Regulatory Framework for Decommissioning Petroleum Infrastructure and Enforcement - Strengthening the Crown Minerals Act Regime | Office of the Minister of Energy and Resources |
| 17 June 2020 | <i>Cabinet Economic Development Committee Minute of Decision:</i> Regulatory Framework for Decommissioning Petroleum Infrastructure and Enforcement - Strengthening the Crown Minerals Act Regime | Cabinet Office |
| 17 June 2020 | <i>Regulatory Impact Assessment:</i> Regulation governing legal and financial responsibility for decommissioning petroleum infrastructure and enforcement tools under the Crown Minerals Act 1991 | MBIE |

Information redacted

YES / NO

Any information redacted in this document is redacted in accordance with MBIE's policy on Proactive Release and is labelled with the reason for redaction. This may include information that would be redacted if this information was requested under Official Information Act 1982. Where this is the case, the reasons for withholding information are listed below. Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Some information has been withheld for the reasons of confidentiality of advice to Government, legal professional privilege, free and frank advice, and commercial sensitivity.

Coversheet: Regulation governing legal and financial responsibility for decommissioning petroleum infrastructure and enforcement tools under the Crown Minerals Act 1991

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| Advising agency | Ministry of Business, Innovation & Employment |
| Decision sought | Amend the Crown Minerals Act 1991 (CMA) to strengthen legal and financial responsibility for decommissioning petroleum infrastructure and expand the current enforcement toolbox. |
| Proposing Minister | Hon Dr Megan Woods, Minister of Energy and Resources |

Section A: Summary problem and proposed approach

Problem Definition: What problem or opportunity does this proposal seek to address? Why is Government intervention required?

There is a risk that the Crown or other third parties (such as private land owners and Regional Councils) will potentially have to undertake and fund decommissioning of petroleum infrastructure. The risk arises from petroleum companies defaulting on their obligations to undertake and fund decommissioning of their petroleum infrastructure, to the required health and safety and environmental standards, or at all.

This risk is likely to increase as the ownership of late-life petroleum assets consolidates to fewer permit participants, with some being acquired by smaller private equity firms. Such firms are often less well-resourced, and therefore less able to access sufficiently large and liquid funds for decommissioning purposes, at the time decommissioning needs to be undertaken. This risk has recently materialised in relation to the first full field petroleum sector decommissioning project in New Zealand, and is likely to cost the taxpayer an estimated NZ\$155 million.

It is therefore timely to strengthen the regulatory provisions to ensure they are sufficiently robust and fit-for-purpose to help mitigate the risk of decommissioning costs potentially falling to the Crown or other third parties in the future.

Proposed Approach: How will Government intervention work to bring about the desired change? How is this the best option?

Government intervention will work to fill the regulatory gaps by creating a robust regulatory framework to impose greater discipline and strengthening the incentives for petroleum companies to undertake and fund their decommissioning activities, as an integral part of a permit to mine petroleum resources.

The package of options will be implemented through amendments to the Crown Minerals Act 1991. Regulations will be required to provide further detail on the monitoring and regulatory oversight options, as well as the infringement offence scheme. These will be subject to further policy work, consultation with stakeholders, and separate Cabinet decisions in due course.

Section B: Summary impacts: benefits and costs

Who are the main expected beneficiaries and what is the nature of the expected benefit?

The Crown and other third parties will be the main beneficiaries of these proposals. The key intended outcome is to impose greater discipline and strengthen the incentives for petroleum companies to undertake and fund their decommissioning activities to the required health and safety and environmental standards. This will mitigate undue risk that the Crown and other third parties will potentially have to step-in as the provider of last resort.

In circumstances where the Crown or other third parties may have otherwise chosen not to step-in as the provider of last resort, the health and safety and environmental outcomes will be improved. More robust regulation of the petroleum sector may also increase the sector's social licence to operate by providing greater public confidence in the regulatory system and stewardship of New Zealand's petroleum resources.

Where do the costs fall?

The most significant costs are likely to fall on the current petroleum companies that do not follow good industry practice and do not appropriately plan and provide for their decommissioning activities. The costs of decommissioning activities are substantial, with hundreds of millions of dollars typically required to decommission offshore infrastructure. These costs are an ordinary component of petroleum field exploration and mining activities, and are expected to be provided for as part of good industry practice. There will also be some increase in compliance costs for all petroleum companies (including those who already follow good industry practice), depending on their existing levels of compliance, business systems and practices. Petroleum companies may ultimately pass the additional costs to the Crown (through reduced royalties and taxes) and/or regional economies (through reduced investment and employment in the petroleum sector and its related service industries).

The regulator will incur additional administration, monitoring, enforcement and potential litigation costs, due to the expanded remit of financial capability monitoring and the enforcement toolbox. The extent of these additional costs will be driven primarily by the regulatory design choices, which will be subject to future Cabinet decisions, informed by further stakeholder consultation, and impact analysis. Confidential advice to Government

What are the likely risks and unintended impacts, how significant are they and how will they be minimised or mitigated?

There is an inherent risk of unintended consequences. The proposals will need to be implemented in a way that does not precipitate or exacerbate the very financial problems that they are designed to safeguard against (e.g. imposing a stringent financial security requirement on a company that is struggling financially could potentially lead to its default, therefore inability to undertake and fund its decommissioning obligations). To some extent, this risk will be mitigated through careful development and design of regulations, which will be subject to further policy development, impact analysis and industry consultation, and the proposed risk-based implementation approach. We do not consider that the extent of any residual risk of unintended consequences warrants a different regulatory design or form of government regulation.

The proposed package of options may also have a marginal impact of reducing New Zealand's appeal as a petroleum investment destination, as the regulatory regime may appear more onerous. The proposed package is not designed to impose more onerous obligations or set new

standards for decommissioning than is currently provided for. Instead, it is intended to provide more effective means of ensuring that existing obligations are discharged to the existing standards by those who undertake the mining and production activities, not the Crown or other third parties. However, the package will impact existing permits and licences, some of which have been in place for a number of decades. Free and frank opinions

Legal professional privilege

Identify any significant incompatibility with the Government's 'Expectations for the design of regulatory systems'.

None identified.

Section C: Evidence certainty and quality assurance

Agency rating of evidence certainty?

Overall we have a relatively high level of confidence in the evidence base for the problem definition. In addition to the recent example of the Crown stepping-in as a provider of last resort to decommissioning the Tui oil field infrastructure, there is clear evidence that New Zealand's current regulatory settings for decommissioning are lagging behind the relevant regimes in other jurisdictions. Many comparable jurisdictions already have, or are in the process of, increasing their ability to proactively manage the risks that the Crown (and therefore the taxpayer) or other third parties will potentially have to undertake and fund decommissioning of petroleum sector infrastructure.

Quality Assurance Reviewing Agency:

MBIE Regulatory Impact Analysis Review Panel

Quality Assurance Assessment:

The Panel considers that the information and analysis summarised in this Impact Statement meets the criteria necessary for Ministers to make informed decisions on the proposals in this paper.

Reviewer Comments and Recommendations:

N/A

Impact Assessment: Regulation governing legal and financial responsibility for decommissioning petroleum infrastructure and enforcement tools under the Crown Minerals Act 1991

Section 1: General information

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| Purpose |
| <p>The Ministry of Business, Innovation & Employment (MBIE) is solely responsible for the analysis and advice set out in this Regulatory Impact Assessment (RIA), except as otherwise explicitly indicated. This analysis and advice has been produced for the purpose of informing key policy decisions to be taken by Cabinet.</p> |
| Key limitations or constraints on analysis |
| <p>Not a ‘first principles’ review</p> <p>The issues and options analysed in this RIA arise from Tranche Two of the Crown Minerals Act (CMA) Review. The terms of reference for the review specify that it is not a ‘first principles’ review, with the role and function of the CMA regulatory regime in the wider regulatory system specifically excluded from its scope.</p> <p>Evidence of the problem and data quality</p> <p>The issues and options considered in this RIA have been informed by international trends and domestic evidence. There is clear evidence that New Zealand’s current regulatory settings for decommissioning petroleum infrastructure are lagging behind the relevant regimes in other jurisdictions. Many comparable jurisdictions, including Australia, the UK, Canada, the US States and Norway are increasing their ability to more effectively manage the risks that the taxpayer or other third parties will potentially have to undertake and fund decommissioning of petroleum sector infrastructure.</p> <p>In New Zealand, the cost of carrying out the first full field decommissioning project of the Tui oil field’s petroleum infrastructure has recently fallen the Crown, and is likely to cost the taxpayer around NZ\$155 million. The proposed package of options is designed to improve the Crown’s ability to more effectively mitigate the risk of potentially having to undertake and fund decommissioning in the future.</p> <p>The specific cost of decommissioning petroleum infrastructure is uncertain, and can vary significantly depending on the timing, location, extent of removal required, and other factors. We have based our analysis on a high-level estimate of a range within which the decommissioning costs could fall. We note that, due to the dynamic nature of the risk, the extent of the Crown’s risk exposure can change significantly and unexpectedly. As existing permit holders look to transfer their permits to smaller end-of-life specialist firms, the risk for the Crown of potentially having to step-in as a provider of last resort is likely to increase.</p> <p>We also note that there is a risk of unintended consequences, arising from the Crown imposing financial security requirements on companies that might already be under financial</p> |

stress; thereby exacerbating the Crown's risk of potentially having to step-in as a provider of last resort. This risk is inherent to the design of the decommissioning proposals, and will be mitigated, to some extent, by the flexibility afforded to the regulator by applying a risk-based regulatory approach. We do not consider that any residual risk of unintended consequences is sufficient to warrant a different regulatory design or form of government regulation.

There is limited quantitative data available to inform some of the compliance and enforcement related options. For example, it is unknown how often some of the proposed enforcement tools would have been used in the past, had they been available. We have based our assumptions and analysis on stakeholder feedback and MBIE's operations and compliance expert opinions and noted the limitations of this approach throughout this RIA.

Limitations on consultation

We consulted publicly from 19 November 2019 to 27 January 2020 and sought feedback on high-level policy options. Timing constraints prevented us from consulting on more detailed design characteristics of the proposed policy package. For some options, we have tested our proposed approach on the detailed design with an industry association, and note that all stakeholders will have a further opportunity to comment on those through the standard legislative change process (e.g. during the Select Committee stage). For other options, the detailed design characteristics will be developed through regulations, which will be subject to future Cabinet decisions, informed by further industry consultation and regulatory impact analysis.

Overall conclusion

Despite the above listed limitations, we consider that the regulatory impact analysis carried out is sufficient for Cabinet to base its decisions on.

Responsible Manager (signature and date):

Authorised by:



Michelle Schulz
Manager, Resource Markets Policy
Energy & Resource Markets
Ministry of Business, Innovation & Employment

May 2020

Section 2: Problem definition and objectives

2.1 What is the context within which action is proposed?

The petroleum industry is delivering significant economic benefits to the New Zealand economy...

The petroleum (oil and gas) industry is a key contributor to New Zealand's economy and overall societal wellbeing. Alongside royalties and taxes for the Crown, the sectors provide employment opportunities, profits for businesses, export earnings, and regional economic development opportunities.

Every year, the industry contributes around \$2.5 billion to the New Zealand economy, brings in around \$750 million worth of export receipts, generates approximately \$500 million in royalties and income tax for the Crown, and employs around 11,000 mostly highly skilled people, two thirds of which are in Taranaki. Oil and gas workers tend to earn twice the national average salary and create seven times the average value earned per annum, money that is spent in local communities.

Natural gas is used by: 270,000 residential users for instant heat, energy and continuous hot water supply; 11,000 small commercial users such as restaurants; 5,000 large commercial users such as hospitals; and 300 large industrial users.¹ Gas also accounts for about 20 percent of New Zealand's total primary energy needs and fuels around 13 percent of electricity generation.²

...however, many of New Zealand's petroleum fields are nearing the end of their productive lives

The New Zealand petroleum industry has been built on the back of early exploration and development dating back to the 1950s. As the sector continues to mature an increasing number of petroleum fields (particularly those offshore) may be nearing the end of their economic lives over the next decade, and will require decommissioning and plugging and abandoning of wells.³ This is consistent with global trends, where an increasing number of petroleum fields are nearing depletion, following decades of resource recovery.

Decommissioning is the process of removing or otherwise satisfactorily dealing with petroleum assets (such as platform installations and other structures, equipment, pipelines and cables) and wells, in a safe and environmentally responsible manner, at the end of their economic life or when production ceases. This includes plugging and abandoning wells, rehabilitating the site and carrying out any necessary post-decommissioning monitoring. Plugging and abandonment (P&A) is a technical term for when a well is removed from service and made permanently inoperable. For the purposes of this document we refer to "decommissioning" as an all-encompassing term, which includes P&A activities, full or partial removal of structures and facilities, and site restoration activities.

Decommissioning is an ordinary component of petroleum field exploration and mining activities. Although parts of the facilities and infrastructure used to develop petroleum resources may be taken out of service and decommissioned at various points over the life of a petroleum

¹ <https://gasindustry.co.nz/dmsdocument/6540>

² <https://gasindustry.co.nz/dmsdocument/5806>

³ This document relates to decommissioning of petroleum infrastructure. Non-petroleum infrastructure does not present the same risks to the Crown or other third parties around potential decommissioning cost transfers. The issues of decommissioning in the minerals sector are generally dealt with through the Resource Management Act 1991.

development project, decommissioning typically coincides with the end of economic petroleum production. The exact timing of decommissioning is dependent on a range of factors including reservoir performance, redevelopment of the field, permit conditions and resource markets.

Industry information available to us indicates that there are a number of different petroleum fields with varying estimated decommissioning timeframes. New Zealand currently has five offshore petroleum mining operations and 15 offshore exploration permits, awarded under the CMA regulatory regime. **Commercial Information**

[Redacted]

Commercial Information

[Redacted]

The Government's long term vision for the petroleum and minerals sectors in New Zealand is to transition to a low emissions future and a productive, sustainable and inclusive economy. This further sharpens the focus on the sector's financial preparedness for decommissioning activities.

Decommissioning represents a substantial cost at the end of a petroleum field's economic life...

There are significant health and safety and environmental risks that could arise in the event that decommissioning is not undertaken, or, not undertaken to the required standard. At the same time, the cost of decommissioning activities are substantial and decommissioning activities often compete with other likely to be higher yielding uses of permit holders' funds.

Decommissioning is also the most significant lagging condition for petroleum mining operations. Large-scale decommissioning projects are generally undertaken at the end of field life, when there is typically little or no ongoing or future projected revenue available to directly finance or offset associated costs.

Commercial Information

[Redacted]

The estimated costs for decommissioning individual installations of petroleum infrastructure vary widely. There is also inherent uncertainty around these figures, as the cost of decommissioning is highly dependent on the standard to which decommissioning is required by other regulators, when and where the decommissioning occurs, and any technical requirements in the decommissioning process for a particular facility. In general terms, we estimate that decommissioning an onshore petroleum production facility can cost well over NZ\$50 million if a complex process is required to mitigate damage caused by any hazardous material, although the average cost to decommission an onshore facility may be considerably less. Decommissioning each of New Zealand's five existing offshore installations is likely to cost in the hundreds of millions or more.

...and there is an increasing risk that the Crown or other third parties will potentially have to undertake and fund the decommissioning of petroleum infrastructure

In the event of a petroleum company's financial default, there is a risk that the Crown or other third parties (such as private land owners and Regional Councils) will potentially have to undertake and fund decommissioning of petroleum infrastructure. Depending on the severity of the potential health and safety and environmental impacts, some decommissioning activities cannot be avoided or delayed. Such activities must take place, and the Crown is often the only party that can fund that work.

To date, company policies, rather than government regulation, have been the primary driver for ensuring that sufficient financial means are set aside, or otherwise provided for, to undertake and fund decommissioning activities in New Zealand, in the event of a company's default. There are commercial incentives for petroleum companies to do so, as it helps secure social licence to operate and preserve options for future exploration and mining projects, and is expected international best practice as part of the overall project. These are important commercial drivers, particularly during the sector's growth phase. Furthermore, petroleum assets have historically been owned by consortiums of large multinational publicly listed entities. Such firms normally have the ability to access sufficiently large and liquid funds for decommissioning purposes.

However, as the sector continues to mature and petroleum production approaches the end of its economic life, the incentives for petroleum companies to undertake and fund decommissioning of their infrastructure may weaken. Furthermore, recent experience in New Zealand and overseas has been that the ownership of late-life petroleum infrastructure tends to consolidate to fewer permit participants, with some being acquired by smaller companies, without joint venture partners, funded by private equity. Such firms are often less well-resourced, and therefore less able to access sufficiently large and liquid funds for decommissioning purposes, at the time

decommissioning needs to take place.

The risk` has recently materialised in relation to the first full field petroleum sector decommissioning project in New Zealand. In late 2019, Tamarind Taranaki Ltd (Tamarind), the operator of the Tui oil field (Tui), went into receivership and liquidation. With Tamarind's liabilities far exceeding the value of its assets, it and the other Tui participants are not able to meet any part of the decommissioning costs. To protect the marine environment (which would otherwise be severely damaged), the Crown is stepping-in as the provider of last resort to decommission the Tui infrastructure. This is estimated to cost the taxpayer around NZ\$155 million.

Tamarind's situation at the Tui oilfield is an example of the incentives and ability of smaller private equity companies to undertake and fund the decommissioning activities no longer being sufficient for the Crown to rely on as the primary source of assurance that decommissioning activities will be undertaken to the required standards, or at all.

Internationally, more proactive and strategic regulatory frameworks for funding decommissioning activities have been developed...

The degree to which overseas jurisdictions regulate and manage financial risks associated with decommissioning seems to depend on the maturity of the petroleum industry and the experience that governments have had with decommissioning. For example, the United States and Australia have experienced the cessation of numerous petroleum fields, and as a consequence have explicit, detailed and quite prescriptive decommissioning requirements embedded in their legislation. Similarly, Norway, the United Kingdom and the United States have also had to decommission a number of large scale offshore oil and gas production operations, and have therefore developed provisions for decommissioning in their governing regulatory requirements. Regulatory provisions tend to range from broad constitutional clauses to specific requirements for certain practices.

In general, over the last few decades, most comparable overseas jurisdictions have developed robust regulatory frameworks for decommissioning activities, taking a life-cycle approach to petroleum field developments. Under these frameworks impacts of petroleum field development projects are assessed, continually monitored, and mitigation measures (including decommissioning plans and financial reserves) systematically adjusted to reflect changing conditions. Overseas jurisdictions are increasingly taking a more whole-of-life view of the extractive industries, one that requires petroleum companies to consider and incorporate end-of-life stages into the initial design. This positions the end-of-life of petroleum fields' phase as a sustainable development issue, in which complex environmental, social and health and safety impacts are identified, considered and managed proactively. Such approach is seen as a means of reducing the magnitude of the impacts of decommissioning activities at lower overall costs.

The need to strengthen New Zealand's regulatory settings was highlighted by the CMA Review Tranche Two

In April 2018, the Government announced that no new offshore oil and gas exploration permits would be issued but that the issue of new oil and gas exploration permits for onshore Taranaki would continue. Tranche One of the CMA Review followed this announcement, which culminated in changes implemented through the Crown Minerals (Petroleum) Amendment Act 2018.

Tranche Two of the CMA Review was designed to consider the wider issues under the CMA with the aim of ensuring that the CMA regime remains fit-for-purpose. The Terms of Reference for Tranche Two of the CMA Review focussed on the following objectives:

- New Zealand’s petroleum and minerals sectors should contribute to the country’s productive, sustainable and inclusive economy.
- Risks and downsides associated with the sector need to be appropriately managed.
- The sector needs to be governed by a regulatory regime that is clear, coherent and fair.

The discussion document on Tranche Two of the CMA Review identified and canvassed a wide range of issues and some options for potential legislative, regulatory and operational changes and improvements. These included issues and options for clarifying and strengthening the current decommissioning and enforcement regulatory provisions of the CMA regime, as they relate directly to the second and third objectives of the review.

Recognising the need to address the petroleum decommissioning risks and liabilities in a timely manner, the proposals in this RIA aim to fast-track a small number of key areas of Tranche Two of the CMA Review. The remaining areas of Tranche Two of the CMA Review are being progressed in parallel with policy recommendations being made in due course.

2.2 What regulatory system or systems, are already in place?

New Zealand’s petroleum policies are administered under several regulatory regimes at both the central and local government level. Different regulators are responsible for managing different aspects of petroleum operations, such as the allocation of petroleum rights, environmental effects, and work health and safety.

MBIE (referred to as “the regulator” in this RIA) manages the Crown’s petroleum and minerals resources under the brand New Zealand Petroleum and Minerals (NZP&M). The Crown has owned all petroleum under New Zealand jurisdiction since its nationalisation under the Petroleum Act 1937. Crown ownership continues under the CMA, with all activities to prospect, explore and mine Crown-owned minerals requiring a permit from the Minister of Energy and Resources under the CMA. The Petroleum Act 1937 used the term ‘licences’ rather than ‘permits’, and the CMA provides for some of the licences granted under the Petroleum Act 1937 to continue to have effect as if the Petroleum Act 1937 was still in force.

Permit/licence holders are also required to comply with:

- **Health and Safety at Work Act 2015** and the Health and Safety at Work (Petroleum Exploration and Extraction) Regulations 2016: These set out work health and safety obligations applying to petroleum operations. Operators are required to have a valid safety case to account for decommissioning. WorkSafe New Zealand is responsible for overseeing the safety case acceptance process.
- **Resource Management Act 1991 (RMA):** Under the RMA, both onshore and within 12 nautical miles offshore, the appropriate regional council acts as the consenting authority for decommissioning. In practice this is the Taranaki Regional Council - as all petroleum production subject to the RMA are in that region (with some in the EEZ, as outlined below). The RMA provides flexibility for the Taranaki Regional Council to consider how to minimise the environmental effects of decommissioning. This could include complete removal of infrastructure, or consideration of leaving some infrastructure in situ (for example, pipelines under jackets or platform foundations on the seabed) where doing so may have a lower environmental impact.
- **Exclusive Economic Zone and Continental Shelf (Environmental Effects) Act 2012.** Outside 12 nautical miles, the Environmental Protection Authority (EPA) is the relevant consenting authority. In 2017, the Exclusive Economic Zone and Continental Shelf (Environmental Effects) Act (EEZ Act) was amended to strengthen the regulatory framework

for decommissioning by introducing a requirement for petroleum companies to have decommissioning plans in place. The requirement for a plan ensures that the agreed environmental outcomes (between the EPA, public, iwi and operators) are achieved in line with the purpose of the EEZ Act and New Zealand's international obligations. Detailed regulations to set out this process are currently being developed.

- **The Maritime Transport Act 1994:** Maritime New Zealand implements the Marine Protection Rules, under the Maritime Transport Act 1994 (which is administered by the Ministry of Transport). Marine Protection Rules Part 131 requires offshore installations operating in New Zealand waters to have marine oil spill contingency plans (OSCP) that will support an efficient and effective response to an oil spill. Marine Protection Rules Part 102 requires offshore installations operating in New Zealand waters to hold a certificate of insurance at an appropriate level of liability cover for oil pollution damage.
- **New Zealand's international obligations:** The United Nations Convention on the Law of the Sea (UNCLOS) provides that states have a general obligation to protect and preserve the marine environment and a more specific obligation to take all measures necessary to prevent, reduce and control pollution of the marine environment from any source. Article 60 of UNCLOS states that: "...any installations or structures which are abandoned or disused shall be removed to ensure safety of navigation, taking into account any generally accepted international standards established in this regard...". The International Maritime Organisation (IMO) recommends criteria for coastal states to consider when determining whether to allow an offshore installation or structure to remain on the seabed. These criteria are not binding, but reflect international good practice. Under the guidelines, the general premise is that all disused installations and structures must be entirely removed unless it can be shown special circumstances consistent with the IMO Guidelines apply.⁸
- **Tax and royalty rebates provisions:** Recognising that decommissioning costs fall at the end of a field's life when a petroleum miner makes little to no income, the tax rules allow a petroleum company to spread decommissioning costs back across previous years of income. This ex-post adjustment reduces taxable income in previous years, which reduces the amount of royalties and taxes payable. This necessitates a rebate from the Crown – effectively rebating a proportion of tax and royalties received. Since the company tax is 28 percent and the royalty rate is 20 percent of profit, the rebate rate is approximately between 42 and 48 percent of decommissioning costs. These provisions place petroleum companies' tax obligations on equal footing with other productive sectors of the economy that are able to offset their costs against future incomes.

2.3 What is the policy problem or opportunity?

The current CMA regulatory settings are no longer fit-for-purpose

Given the changes in industry dynamics, the current CMA regulatory settings do not provide sufficient assurance that decommissioning activities will be undertaken and funded by the permit/licence holders to the required health and safety and/or environmental standards, or at all. The specific issues with the current CMA regulatory provisions are outlined in detail in Section 4, as a description of the status quo, and are briefly summarised below.

⁸ 1989 Guidelines and Standards for the Removal of Offshore Installations and Structures on the Continental Shelf and in the Exclusive Economic Zone: <https://cil.nus.edu.sg/wp-content/uploads/formidable/18/1989-Guidelines-and-Standards-for-the-Removal-of-Offshore-Installations-and-Structures-on-the-Continental-Shelf-and-in-the-Exclusive-Economic-Zone.pdf>

The CMA lacks a clear strategic regulatory framework to govern legal and financial responsibility for decommissioning: The main focus of the CMA regulatory regime has, to date, been on enabling efficient entry and operation of the petroleum industry. The regulatory settings that relate to end-of-life decommissioning activities have largely evolved in an *ad hoc* manner, as it has been considered at the permit granting stage (and largely as a secondary part of the determination), in an *ad hoc* manner and in response to individual permit/licence holders' circumstances. The health and safety and environmental standards for the installation, operation and removal of petroleum infrastructure are largely governed by other regulatory regimes within the wider regulatory system (as outlined in section 2.2).

The CMA enforcement toolbox is limited: The current enforcement toolbox is effective for responding to either relatively serious breaches that warrant prosecution or relatively low-level breaches that can be dealt with through less formal compliance tools, such as requests to comply. However, it does not allow the regulator to effectively respond to mid-level breaches, which require sufficiently serious sanctions to deter non-compliant behaviour but do not warrant court action. These limitations apply equally to decommissioning-related breaches as well as other breaches of the CMA provisions.

Prior to future decommissioning activities taking place, it is timely to strengthen the CMA regulatory settings governing the legal and financial responsibility for decommissioning.

2.4 Are there any constraints on the scope for decision making?

Constraints on scope

The issues and options analysed in this RIA arise from Tranche Two of the Crown Minerals Act 1991 Review. The terms of reference for the review specify that it is not a 'first principles' review, with the role and function of the CMA in the wider regulatory system specifically excluded from its scope. The recommendations in this RIA will set out a high-level framework for financial assurance and enforcement, but the details will need to be fleshed out over time, through regulations and additional guidance by the regulator.

Connections to other ongoing work

Historic orphaned wells

The options in this RIA will not address the issue of liability and funding for historic orphaned onshore petroleum wells. Orphaned wells are those where there are outstanding P&A liabilities, but no legally responsible party that is still around to undertake these actions, and neither the Crown nor any other third party have to date deemed necessary to step-in as a provider of last resort. Confidential advice to Government

This work is ongoing.

Residual liability

Residual liability arises in situations where there is no liable permit/licence holder that can be held responsible for an issue arising from a petroleum well or infrastructure, after the permit for a decommissioned site has ended in compliance with all relevant legislation. A properly plugged and abandoned well may still carry a risk of undesirable environmental outcomes or a risk to human health and safety, arising at some point in the future. Despite taking the steps to mitigate this risk (prior to the permit expiry), the risk cannot always be eliminated. At the time such residual risk may materialise, there are no longer a permit/licence or other consent conditions in

place. This is a cross-government issue with a range of regulatory agencies involved. A cross-agency work program is currently being developed to identify issues and develop options, which may in due course lead to further regulatory changes, including to the CMA.

2.5 What do stakeholders think?

Stakeholder consultation

We consulted publicly on issues and high-level options to (among other things) clarify and strengthen the current CMA regulatory settings as they relate to decommissioning, compliance, and enforcement provisions.⁹ The consultation process took place between November 2019 and January 2020 and attracted 167 written submissions. The majority of submissions (59 percent) were from environmental groups (50 submissions) and the general public (48 submissions). Of the 50 submissions from environmental groups 30 were from submissions from Generation Zero. Ten submissions were from Iwi or hapū, nine from the oil and gas sector and nine from the minerals sector. Four submissions were from local government, three from the quarrying sector and two from research institutes. 27 submissions came from general public, organisations from the business and electricity sector.

55 submitters commented directly on the issues and high-level options that relate to decommissioning activities. All but one agreed that the CMA is currently unclear and possibly inconsistent in its application of the obligation to decommission. Many noted that the obligation needed to be carefully designed and implemented. Most submitters also strongly agreed that there should be greater visibility and assessment of permit/licence holders' ongoing financial capability, with some expressing concerns around the issues of poor visibility over the timing for upcoming decommissioning activities. There was also general support for ensuring that permit/licence holders have access to sufficient funds available for decommissioning to mitigate the risk of these activities and their associated costs being passed on to the Crown or other third parties. Some submitters were concerned about the use of some financial instruments (e.g. bonds) as they are seen as unproductive use of capital. 75 submitters commented on the current compliance enforcement tools. Most agreed that the CMA's current enforcement toolbox needs expanding. The additional compliance tools and penalties were largely supported, or supported with caveats. Some submitters, particularly environmental groups, believed that penalties for non-compliance needed to be more stringent to incentivise compliance.

Departmental consultation

The relevant government departments that were consulted on the recommended package of options included: the Treasury, the Department of Conservation, Ministry for the Environment, Ministry of Foreign Affairs and Trade, Ministry of Transport, Ministry of Justice, Ministry for Primary Industries, Office for Māori Crown Relations - Te Arawhiti, Land Information New Zealand, Environmental Protection Authority, Maritime New Zealand, WorkSafe New Zealand, and the Department of Prime Minister and Cabinet.

Limits on consultation

Due to the timing of policy development work, we did not consult publicly on detailed design characteristics of the proposed policy package. For some options, we have tested our proposed approach on the detailed design with an industry association, and note that all stakeholders will have a further opportunity to comment on those through the standard legislative change process (e.g., during the Select Committee process). For other options, the detailed design characteristics will be developed through regulations, which will be subject to future Cabinet decisions, informed by further industry consultation and regulatory impact analysis.

⁹ <https://www.mbie.govt.nz/dmsdocument/7320-discussion-document-review-of-the-crown-minerals-act-1991>

Section 3: Option identification

3.1 What options are available to address the problem?

For each specific issue with the current CMA regulatory settings we have identified and analysed a range of options. We describe the specific issues, options for addressing them, and the options' impact analysis in Section 4 below.

The preferred options are designed to work together as a coherent package in order to create a robust regulatory framework of legal and financial responsibility for decommissioning. The package of options is designed to deal with three main areas:

1. **Establishing a clear statutory obligation to decommission.** This would involve amending the CMA to:
 - impose an explicit statutory obligation on permit/licence holders to undertake and fund decommissioning activities, as an integral part of the permit to mine petroleum resources; and extend it to former permit/licence holders in the case of a transfer.
2. **Providing for more effective monitoring and regulatory oversight.** This would involve amending the CMA to:
 - require permit/licence holders to provide the regulator with sufficiently detailed and up to date planning and financial information;
 - enable the regulator to conduct periodic financial capability assessments; and
 - empower the regulator to require financial security for decommissioning to be maintained and accessed, if/when necessary.
3. **Expanding the current enforcement toolbox.** This would involve amending the CMA to:
 - introduce new enforcement powers, including: enforceable undertakings, compliance notices, and infringement fees;
 - introduce a new offence provision; and
 - clarify existing record keeping requirements.

For all three areas, there are high levels of interdependencies between options that require consideration as a package. We note these interdependencies in relation to the specific options discussed in Section 4 below.

We considered non-regulatory options. However, we concluded that legislative changes are needed to address the shortcomings of the current CMA regulatory settings. This is because they stem from existing regulatory settings, which do not provide for a clear and proactive approach to ensure that permit/licence holders, who have benefited from the petroleum exploration and production, bear the legal and financial responsibility for decommissioning.

3.2 What criteria, in addition to monetary costs and benefits, have been used to assess the likely impacts of the options under consideration?

We assessed the options against the following assessment criteria, which have been given equal weighting:

- **Effectiveness** (*the extent to which the option contributes to the desired policy outcomes*). Does the option address the problem identified with the current CMA regulatory settings effectively?
- **Proportionality** (*the extent to which the costs/risks of implementing the option are proportional to the expected benefits*). Does the option minimise the costs, risks and potential unintended consequences of addressing the problem identified with the current CMA regulatory settings?
- **Regulatory certainty** (*the extent to which the option provides clarity of regulatory requirements and predictability of regulatory outcomes*). Does the option address the problem identified with the current CMA regulatory settings in a way that makes the regulatory requirements more clear and transparent, and regulatory outcomes more predictable?
- **Practicality** (*the extent to which the option reduces any implementation risks*). Does the option minimise any implementation risks, provides for administrative simplicity, and encourages timely decision-making?

3.3 What other options have been ruled out of scope, or not considered, and why?

Given that permit/licence holders are both beneficiaries of the exploration and production permits and are best placed and expected to undertake decommissioning activities as part of their development of a petroleum field, we have ruled out options for the Crown to physically fulfil decommissioning itself as a matter of course, or arranging for a third party to do so.

We have also considered but ruled out the following options to improve compliance:

- *Making it administratively easier for the regulator to revoke a permit/licence*: This option was rejected because revocation is designed to be used as a last resort. Increasing the ease of revocation may not improve compliance and may create perverse incentives.
- *Introducing enforcement orders, as provided for in the RMA*: An enforcement order under the RMA is made by the Environment Court, compelling a person to comply with the provisions of the RMA, a rule in a regional or district plan, or the terms and conditions of a resource consent. Although there is flexibility in how the courts address a breach, they still present a relatively high-cost means of enforcing compliance.

Section 4: Specific problem definitions, option identification and impact analysis

This section describes the specific issues with the current CMA regulatory settings, identifies options for change and outlines our impact analysis.

These include:

- 4.1 Establishing a clear statutory obligation to decommission.
- 4.2 Providing for more effective monitoring and informed regulatory oversight.
- 4.3 Expanding the current enforcement toolbox.

Ratings

Our impact analysis of options is set out against the status quo, which is reflected in the rating for each option against each criterion. The impact tables include the status quo, which is rated **0** reflecting no change.

| | | | | |
|--|-----------------|-------------------------|----------------|----------------------|
| Key compared with doing nothing (the status quo): | | | | |
| ++ much better | + better | 0 about the same | - worse | -- much worse |

The overall assessment for each option is essentially an average of the rating against each criterion. Judgement is applied in determining the overall rating for each option.

Section 4.1: Establishing a clear statutory obligation to decommission

4.1.1 What is the specific problem?

Status Quo: No explicit statutory obligation for permit/licence holders to undertake and fund decommissioning activities

In contrast to the Petroleum Act 1937, there is currently no explicit statutory obligation in the CMA for permit holders to undertake, and meet the financial costs of, decommissioning activities. By association, there is also no explicit statutory offence or penalty for failure to undertake and fund decommissioning activities.

As a result, the CMA is currently silent on such critical policy and regulatory design matters as to who is legally and financially responsible for ensuring decommissioning is carried out, the extent to which they are responsible, the length of time for which they are responsible, and what are the consequences for potential non-compliance

Instead, the CMA relies on a generic statutory requirement for permit holders to act “in accordance with good industry practice” and allows for specific decommissioning requirements to be imposed on permit holders as a condition of a permit.

Acting “in accordance with good industry practice” means “acting in a manner that is technically competent and at a level of diligence and prudence reasonably and ordinarily exercised by experienced operators engaged in a similar activity and under similar circumstances”. While it is generally understood and accepted that acting in this manner would include responsibilities for decommissioning activities, this implicit obligation has not been tested in court.

Reliance on permit conditions to establish legal and financial responsibility for decommissioning means that the requirements may not necessarily be worded and applied consistently across permit holders and time. This, in turn, creates additional administrative complexity, raises issues with consistency of application, and increases risks for the Crown or third parties in relation to enforcement.

Further inconsistencies arise from the legacy provisions of the Petroleum Act 1937, which was superseded by the CMA, but continues to have an effect in relation to licences issued under that Act, as if it was still in force. Under the Petroleum Act 1937, licence holders are obligated to remove buildings, machinery and equipment on the expiry, surrender or revocation of the licence and leave abandoned pipelines in a safe condition.

4.1.2 What options are available to address the problem?

We considered two options, in addition to the status quo, for addressing these problems. These are described below and include:

- **Option 4.1.1:** Amending the CMA to introduce an explicit statutory obligation for permit/licence holders to undertake and fund decommissioning activities.
- **Option 4.1.2:** Increasing the use of non-statutory means to establish legal and financial responsibility for decommissioning.

Option 4.1.1: Amending the CMA to introduce an explicit statutory obligation for permit/licence holders to undertake and fund decommissioning activities

Under this option, the CMA would be amended to establish an explicit statutory obligation for all current and future petroleum permit/licence holders to:

- carry out decommissioning activities in accordance with good industry practice and the applicable health and safety and environmental requirements in other legislation; and
- be liable for meeting the financial costs of the decommissioning activities, as an integral part of the permit to mine petroleum resources.

The legal and financial responsibility for decommissioning would rest with the current permit holders.

In the case of a permit with multiple participating interests, the legal and financial responsibility for decommissioning would apply jointly and severally to all current participating interests in the permit. This means that each permit participant could be held liable for ensuring that decommissioning obligations are met, including responsibility for meeting the total costs of decommissioning. As with other joint and several liability regimes, the individual shares of financial responsibility would be a commercial matter and would be determined and arranged for among permit participants as they see fit. The 2014 Law Commission report on the joint and several liability rule, and its application across the New Zealand legal system, concluded that none of the alternative rules were sounder in principle, or more likely to produce better policy outcomes.¹⁰ The Commission noted that while proportionate liability can deliver cost benefits to individual interests, these come at a much greater risks of not achieving adequate compensation for the affected parties.

Similar to the approach taken in the UK, the legal and financial responsibility for decommissioning would apply to a former permit holder, in the case of a transfer. This would mean that a former permit holder will continue to be held liable for decommissioning notwithstanding that they have transferred their permit interest to another entity. Recognising that it would not be appropriate to require the former permit holder to decommission infrastructure that they have neither installed nor used, their liability will be limited to decommissioning infrastructure installed before the transfer has taken place. The obligation would apply only to the extent that the current permit holder (the transferee) fails to undertake and fund decommissioning. The UK approach is designed to prevent situations where a permit holder transfers its interests to another entity to avoid decommissioning obligations and/or costs, with no consideration or concern as to whether the transferee has financial capacity to ensure that decommissioning is carried out.

Under this option, permit holders' would be required to undertake and fund their decommissioning activities prior to permit/licence expiry, surrender or revocation. This would mean that legal and financial responsibility for decommissioning would not extend beyond the life of a permit. As outlined in section 2.4 above, issues of potential residual liability are outside the scope of this RIA.

The statutory obligation to undertake and fund decommissioning would be accompanied by an offence provision, with various enforcement actions available for non-compliance (as outlined in section 4.3 below). A civil pecuniary penalty would be applied for failure to undertake and fund decommissioning. In line with other regulatory regimes regulating commercial activities (e.g. the Commerce Act 1986) the maximum penalty would be set at \$500,000 for an individual and up to \$10 million for a body corporate.

The statutory obligation would be extended to petroleum licences, originally issued under the Petroleum Act 1937. This would replace and modernise the requirements for licences under that Act and align the decommissioning obligations under both the CMA and the Petroleum Act 1937 ensuring clarity and consistency.

¹⁰ <https://www.lawcom.govt.nz/sites/default/files/projectAvailableFormats/NZLC%20R132.pdf>

The statutory obligation would apply to all current and future permit/licence holders, and as such supersede any existing decommissioning obligations set out in the permit conditions or the Petroleum Act 1937.

Option 4.1.2: Increasing the use of non-statutory means to establish legal and financial responsibility for decommissioning

Under this option, the regulator would develop an operational framework and guidance for establishing legal and financial responsibility for decommissioning through permit conditions. This would enable the regulator to apply these obligations more consistently in the future, but would rely on voluntary cooperation by existing permit/licence holders to alter existing permit/licence's conditions. Under the current CMA settings, changes to existing permit conditions cannot be imposed by the regulator, without the permit/licence holders consent.

4.1.3 Impact analysis

| Assessment criteria | Status quo/ No action | Option 4.1.1: Amending the CMA to introduce clear requirement for permit/licence holders to undertake and fund decommissioning activities | Option 4.1.2: Increasing the use of non-statutory means to establish legal and financial responsibility for decommissioning |
|--|---|---|---|
| Effectiveness: Does the option address the problem effectively? | 0 Key policy and regulatory design matters determined through permit conditions. Scope for inconsistent application, legal uncertainty and enforcement difficulties. Exposes the Crown and other third parties to the risk of potential cost transfers. | ++ Would strengthen current regulatory settings by providing for the key policy and regulatory design matters to be clearly stipulated and applied consistently. Would help mitigate the risk of potential cost transfers to the Crown or other third parties. | 0 / + Would improve clarity of expectations and consistency of application for future permits. Would also help mitigate the risk of potential cost transfers from future permits. No impact on existing permit/licence holders as permit conditions cannot be changed without permit holders' consent and the incentive to consent is likely to be weak. |
| Proportionality: Does the option minimise the costs, risks and potential unintended consequences? | 0 Unclear and inconsistent obligations may create additional compliance costs and risks for permit holders. | + No additional costs for those operating in line with good industry practice. Additional compliance cost for those who are not doing so is the intended outcome of this option. Additional risk for former permit holders, which they will need to be compensated for through the price of a transfer. | 0 / + Would provide guidance to setting individual permit conditions, and may improve consistency of application for future permits. Unlikely to have impact on existing permits/licence holders. |
| Regulatory certainty: Does the option make regulatory requirements more clear and transparent, and outcomes more predictable? | 0 Unclear and inconsistent obligations result in regulatory uncertainty and unpredictability of outcomes. | + Would produce greater clarity for permit/licence holders on their legal and financial responsibility obligations. | 0 / + Would make requirements more clear and consistent. However, outcomes may not always be predictable, as operational policies do not have the same status as legislative requirements. |
| Practicality: Does the option minimise any implementation risks, provides for administrative simplicity, and encourages timely decision-making? | 0 High risks of inconsistent application, administrative complexity. | ++ Would provide for a consistent and administratively simple treatment of all permit/licence holders' legal and financial responsibility obligations. | - The process of permit condition renegotiation would be highly resource-intensive, and could be slow and difficult. |
| Overall assessment | 0 | ++ much better than status quo. | 0 / + slightly better than status quo. |

Section 4.2: Providing for more effective monitoring and regulatory oversight

4.2.1 What is the specific problem?

Status Quo: Current monitoring and regulatory oversight provisions are not effective

The current CMA provisions in relation to monitoring and regulatory oversight significantly limit the regulator's ability to effectively identify risks and take any preventative measures to ensure that decommissioning is being appropriately provided for by the permit/licence holders. This, in turn, significantly limits the regulator's ability to mitigate the risk of potential cost transfer to the Crown or other third parties.

The regulator lacks access to sufficiently detailed and up to date planning and financial information for decommissioning

Under the current CMA provisions, planning information that permit/licence holders are required to provide to, and agree with, the regulator, as part of the permit application, lacks sufficient detail about the economic use and status of permit/licence holders' infrastructure services, as well as timing and costings of the projected decommissioning activities. In addition, there is no explicit requirement in the CMA for permit/licence holders to provide the regulator with, and seek agreement to, any updates to such planning information, over the life of the permit.

A field development plan sets out the process and timing for field development. It would typically include sufficiently detailed information about the anticipated timing, costs and scope of projected decommissioning activities, which are strongly connected to and driven by the permit/licence holders' decisions to cease production operations.¹¹ Field development plans are inherently live documents, reflecting any material changes to the originally projected timelines, costs and scope of the operations throughout the economic lifecycle of the project. While field development plans are normally submitted to, and agreed with, the regulator as part of an application for a mining permit, the CMA only explicitly refers to a "work programme" document needing to be provided to, and agreed with, the regulator, which is less detailed and separate document to a field development plan.

Similarly, while applicants for a permit must demonstrate that they have sufficient financial capability to undertake the proposed work programme (including decommissioning) before a permit can be granted, there is no requirement in the CMA for them to notify the regulator of material changes to, or impacts on, their financial capability, over the life of the permit. As a result, the regulator has no visibility over the financial status and any funding arrangements that permit holders may or may not be maintaining for decommissioning purposes, and whether deductions included in royalty returns for decommissioning can be substantiated.

Lack of access to sufficiently detailed and up to date planning and financial information throughout the life of a permit significantly limits the regulator's ability to carry out informed monitoring of permit/licence holders' decommissioning plans and funding arrangements. This, in turn, prevents the regulator from being able to effectively identify any current and emerging risks or take any preventative measures (such as requiring more robust cost estimation for decommissioning) to ensure that decommissioning is being appropriately planned for by the

¹¹ The decision to cease production will normally occur once production is no longer economically viable. A range of factors including production rates, commodity prices, and operating costs will be taken into consideration when making the decision. The timing of decommissioning infrastructure, once production has ceased, will depend on potential alternative uses, the likelihood of production being restarted, nearby resources and overall decommissioning costs.

permit/licence holders. This further means that the regulator is limited in its ability to mitigate the risk of potential cost transfer to the Crown or other third parties in an effective and proportionate manner.

The regulator lacks powers to undertake periodic assessments of financial capability

The CMA currently provides for the regulator to undertake a financial capability assessment at the time the permit is granted. At that point in time, the applicant must demonstrate that it has sufficient financial capability to undertake its overall work programme (including decommissioning) before a permit can be granted. The assessment is undertaken on the basis of the applicant's financial status at the time. Given the significant time lags between the permit being granted and the need for decommissioning activities to be undertaken, the initial financial capability assessment, as it relates to decommissioning, is made under high levels of uncertainty.

Although financial capability is re-assessed if a permit holder initiates a transfer, or there is a change of control or a change of operator, there is currently no provision in the CMA for the regulator to re-assess a permit holder's financial capability once a permit has been granted.

Significant changes can occur to a company's financial capability over the life of a permit, due to circumstances such as potential changes in corporate structure, the impact of international events, commodity prices, or poor exploration success across a permit/licence holder's portfolio. For example, offshore petroleum wells can cost up to US\$250 million to drill, with no guaranteed return on this investment. Several dry wells can negatively affect the financial capability of a company to meet its statutory obligations around decommissioning of petroleum infrastructure. There is no guarantee that the permit holder's capability that exists at that time will be available in the future to meet its obligations when they fall due. The initial assessment would also not account for any additional obligations or activities the permit holder might take on following the assessment and/or granting of a permit.

As a result, the regulator does not have the ongoing visibility of changes in permit/licence holders' financial status, and is therefore unable to effectively identify any current or emerging financial risks or take any preventative measures (such as accessing some form of financial security) to ensure that funding for decommissioning is being appropriately provided for by the permit/licence holders. This further means that the regulator is limited in its ability to mitigate the risk of potential cost transfer to the Crown or other third parties, in an effective and proportionate manner.

The regulator lacks powers to require permit/licence holders to maintain appropriate financial security for decommissioning

With decommissioning taking place at the end of the oil field's economic life, the costs of decommissioning activities cannot be recovered from future production revenues. Consequently, appropriate financial security instruments need to be in place for permit/licence holders to cover their decommissioning costs.

As a matter of good business practice, many permit/licence holders maintain various financial security instruments to fund their decommissioning activities. However, there is currently no direct mechanism in the CMA for the regulator to require them to do so, over the life of the permit.

As outlined above, the CMA currently relies on the initial financial capability assessment, undertaken at the time the permit is granted or transferred, for assurance that permit/licence holders have sufficient financial capability to undertake their overall work programme (including decommissioning). Although financial capability can change significantly during the life of a permit, there is currently no provision in the CMA to enable the regulator to proactively re-assess it during the life of a permit.

In addition, when granting a permit, the regulator can require a monetary deposit or bond to be paid as security for compliance with permit conditions. However, bonds can only be used to pay off any outstanding fees or royalties. Furthermore, bonds are a very blunt and sometimes ineffective security mechanism, as the bond amount is often not sufficient to cover the full costs of the decommissioning activities and it ties up capital, which forgoes a likely higher rate of return if deployed for other purposes. Therefore, bonds are rarely required.

Imposing other types of financial security instruments can often provide a better balance. However, with decommissioning not being an explicit statutory obligation in the CMA, there is legal uncertainty as to whether any financial security instruments (other than bonds) can be legitimately imposed by the regulator as part of permit conditions.

Furthermore, even in situations where permit holders may choose to maintain appropriate financial security instruments over the life of a permit, there are no provisions in the CMA to enable the Crown to directly access the financial security instruments of the permit holder, if it becomes necessary to do so (e.g. if the permit interest were to vest in the Crown in the event of a company default).

The lack of regulatory powers to require appropriate financial security arrangements to be maintained, and possibly accessed by the Crown, significantly limits the regulator's ability to take effective preventative measures and ensure that decommissioning is being appropriately provided for by the permit/licence holders. This means that the regulator is limited in its ability to mitigate the risk of potential cost transfer to the Crown or other third parties, in an effective and proportionate manner.

Requirements to have financial security instruments in place are common in other jurisdictions as a safeguard against damages and costs.¹² International experience suggests that imposing such requirements also facilitates better cost estimations, improves project planning by industry, and encourages early engagement with regulatory agencies on decommissioning projects. The fundamental features of an effective financial security instrument appear to be that it is sufficiently liquid, accessible by the Crown if necessary, payable on demand, and assigned to the permit, rather than a permit interest holder.

4.2.2 What options are available to address the problem?

We considered two broad options, in addition to the status quo, for addressing these problems. These are described below and include:

- **Option 4.2.1:** Amending the CMA to provide for more effective monitoring and regulatory oversight, including the application of financial security instruments.
- **Option 4.2.2:** Increasing the use of non-regulatory means to improve monitoring and regulatory oversight.

Option 4.2.1: Amending the CMA to provide for more effective monitoring and regulatory oversight

Under this option the CMA would be amended to require permit/licence holders to provide the regulator with sufficiently detailed and up to date planning and financial information; enable the regulator to conduct periodic financial capability assessments; and empower the regulator to require financial security for decommissioning to be maintained and accessed, if necessary. Each of these aspects is described below.

¹² https://consult.industry.gov.au/offshore-resources-branch/decommissioning-discussion-paper/supporting_documents/Decommissioning%20Discussion%20Paper.pdf

Requiring permit/licence holders to provide the regulator with sufficiently detailed and up to date planning and financial information

Under this option, the CMA would be amended to require permit/licence holders to provide the regulator with, and seek its agreement to, the field development plans that set out projected decommissioning costs, risks and timing. The provisions of the field development plans would be required both at the initial permit application stage and subsequently if/when material changes to decommissioning-related activities or decisions are contemplated, and in any event at regular (e.g. three or four yearly) time intervals as part of the regular periodic financial capability assessments (as outlined below).

The permit/licence holders would also be required to notify the regulator of any material changes to, or impacts on, their financial capability, over the life of the permit, and provide the regulator with relevant financial information (including as set out in the options 4.3.1 below).

This would ensure that sufficiently detailed and up to date planning and financial information forms an integral part of the regulator's financial capability assessments (both at the time the permit is granted and periodically over the life of a permit, as outlined below). This would also enable the regulator to more accurately estimate decommissioning costs (and therefore establish a more accurate type and quantum of financial security requirements, as outlined below) and increase the regulator's ability to ensure that decommissioning is undertaken prior to permit expiry, revocation or surrender.

Enabling the regulator to conduct periodic financial capability assessments

Under this option, the CMA would be amended to empower the regulator to conduct periodic financial capability assessments over the life of a permit. This would enable the regulator to routinely monitor changes to decommissioning plans and funding arrangements, thus putting the regulator into an informed position to identify and respond early and preventatively to any current or emerging risks to decommissioning not being adequately provided for by permit/licence holders. Ongoing monitoring and regulatory oversight would also strengthen permit/licence holders' commercial incentives to provide for decommissioning at early stages of project development and to reassess their decommissioning options and cost estimates on an ongoing basis, including as part of the overall field development plans.

To be effective, periodic assessments would need to be based on reliable information and conducted at a frequency sufficient to provide a reasonable assurance of permit/licence holders' ability to undertake and fund their decommissioning obligations. Regulations will be developed to stipulate the scope and substance of information requirements and frequency of periodic financial capability assessments. These would need to carefully balance the administrative effort and compliance costs associated with the provision of information and periodic assessments with the extent of potential cost transfer various permits may present for the Crown and other third parties.

Under this option, the key guiding principle for developing regulations would be to avoid prescribing detailed information requirements or setting the frequency of periodic assessments too rigidly. While prescriptive and rigid requirements can provide a high degree of certainty for permit/licence holders, they can also be highly inflexible as they would apply to all permit/licence holders, irrespective of their individual circumstances, compliance history, and levels of expertise. All permit/licence holders would then need to submit all of the information even if it was not strictly necessary to inform an assessment, and be subjected to periodic assessments even if there has not been a material change in their circumstances.

Our preferred risk-based approach would see the regulations stipulate the minimum necessary requirements, supported by information gathering powers and guidance for permit/licence holders. Setting minimum requirements in regulations would keep the compliance costs down for the majority of permit/licence holders for whom this information will be sufficient to enable the

regulator to undertake the assessments. We expect that for most permit/licence holders the assessments would be based primarily on their current and up to date field development planning and financial information (as outlined above). This would include information and documentation about permit/licence holders' capability to carry out decommissioning activities (such a detailed estimate of the costs of decommissioning, predictions of future revenues, the costs and benefits of any plans for future development), and financial arrangements (such as up to date management accounts, forward financial planning, and lending and debt capacity).

The list of minimum information requirements would be supported by guidance published on the ministry's website (providing examples of what specific requirements might entail) and an iterative process whereby the regulator could request additional information during the assessment. This would ensure that in circumstances where the minimum information requirements do not provide an adequate information base, further more targeted information can be gathered to fill the gap.

Recognising there are significant information asymmetries between permit/licence holders and the regulator, the onus would be for the permit/licence holders to demonstrate, and for the regulator to assess the validity of, their ability to give effect to the permit including meeting the decommissioning obligations satisfactorily. Furthermore, the information would need to be provided within a specified timeframe, and, to ensure that it is sufficiently robust, the regulator may require permit/licence holders to engage an independent third party expert, approved by the regulator, to verify the estimates.

With regard to the frequency of periodic assessments, the regulations would set indicative time-bound intervals (e.g. every three or four years). However, the regulator would have the flexibility to conduct out-of-cycle assessments (e.g. annually) or defer a regular assessment (e.g. by a year or two) depending on the project size, timeframes and levels of risk and complexity associated with individual decommissioning activities. This would provide for a risk-based approach to monitoring and enable the regulator to establish an adequate case-by-case monitoring scheme, whereby higher risk projects would be subjected to higher levels and more frequent monitoring and regulatory oversight.

If, when assessed, it was found a permit/licence holder did not have sufficient capability to carry out and fund its decommissioning activities, a range of compliance and enforcement actions would be available (including requiring financial security to be established, as set out in below).

Empowering the regulator to require financial security for decommissioning to be maintained and accessed, if necessary

Under this option, the regulator would be empowered to require permit/licence holders to establish and provide financial security sufficient to discharge their decommissioning obligations, if/when deemed necessary to do so. To guide the regulator's exercise of this discretionary power, regulations will be developed to establish the relevant processes and procedures. The key guiding principles for developing these regulations are set out below.

The requirement for financial security to be established would follow the financial capability assessment, and be based on information regarding the permit holder's financial status, projected decommissioning costs, risks and timing (as set out above). The regulator would have the flexibility to also take into account other matters, such as the permit holders' financial strength and compliance history, so that to balance the impact of the financial burden on the permit/licence holder with the need to ensure that sufficient financial assurance in place.

Financial security would be assigned to the permit, rather than any individual participating interest in a permit. This is consistent with the joint and several liability approach, as outlined above. This would mean that the value of the financial security would be incorporated into the value of the permit, and could therefore be recovered by the transferor from the transferee as part of the purchase price for the permit, or shared appropriately among the permit's participating interests

based on their commercial arrangements.

The type and quantum of financial security would be determined (and could be updated periodically throughout the life of the permit) to reflect the current and emerging risks to undertaking decommissioning activities, at any given point in time.

Types of financial security often required in other comparable jurisdictions and sectors, include, but not limited to, insurance, self-insurance, bonds, deposits as security with a financial institution, an indemnity or other surety, a letter of credit from a financial institution, or a mortgage. These types of security tend to be sufficiently liquid, allowing permit holders to draw on their financial assurance at the time that costs, expenses or liabilities are likely to arise. They also tend to provide for the security to be payable to the Crown on demand, in the event or high risk of company default. The types of financial security would be specified as examples of acceptable forms of financial security, with the ability for the regulator to accept other types of security, if deemed appropriate in the given circumstances. Additional guidance as to what could constitute acceptable form of financial security in different circumstances would be provided for in regulations.

The quantum of financial security required would be determined on a case-by-case basis, guided by the regulations and based on an estimate of future decommissioning costs, taking into account the number and type of facilities, wells and other infrastructure in the permit area. These would need to be carefully estimated, to ensure the financial security required accurately reflects the amount needed for decommissioning, and may therefore warrant a conservative approach.

The requirement to establish financial security, as well as the form and quantum of security required, would be set out either in the permit conditions or a separate direction (e.g. a notice issued to the permit holder). Non-compliance would be grounds for regulator to take enforcement action (including using the expanded compliance and enforcement toolbox outlined in section 4.3 below).

Option 4.2.2: Increasing the use of non-regulatory means to improve monitoring and regulatory oversight

Under this option, the regulator would develop an operational framework for requiring more detailed and up to date planning and financial information to be provided as part of its existing compliance function. It may also be able to require financial security for decommissioning to be maintained, although there is a degree of legal risk in doing so. This would enable the regulator to carry out more informed monitoring and regulatory oversight more effectively in the future, but would rely on voluntary cooperation by existing permit/licence holders to alter requirements set out in existing permit conditions. Under the current CMA settings, changes to existing permit conditions cannot be imposed by the regulator, instead and the permit holder has to consent to any change.

4.2.3 Impact analysis

| Assessment criteria | Status quo/ No action | Option 4.2.1: Amending the CMA to provide for more effective monitoring and regulatory oversight, including application of financial security instruments | Option 4.2.2: Increasing the use of non-statutory means to improve monitoring and regulatory oversight |
|--|--|---|--|
| Effectiveness: Does the option address the problem effectively? | 0 Limited access to sufficiently detailed and up to date planning and financial information. Lack of powers to carry out periodic financial capability assessment, and require financial security arrangements to be maintained and accessed. | ++ Would improve effectiveness of monitoring and regulatory oversight. Would enable the regulator to identify and mitigate the risks of potential cost transfers to the Crown or other third parties, in an effective and proportionate manner. | 0 / + May improve effectiveness of monitoring and regulatory oversight of future permits. No impact on existing permit/licence holders- permit conditions cannot be changed without permit holders' consent and the incentives to consent are likely to be weak. |
| Proportionality: Does the option minimise the costs, risks and potential unintended consequences? | 0 Minimal/no compliance costs and risks for permit/licence holders. | 0 / + No additional costs arising from the requirement to provide planning and financial information, as the information is already being produced for business purposes. Future development of regulations and design of clear processes and requirements will aim to minimise additional compliance costs for permit/licence holders and administrative costs for the regulator. Flexibility, afforded by enabling the regulator to use discretion, would provide for the financial burden on individual permit holders to be taken into account when determining the type and estimating the quantum of financial security required. | 0 / + Would provide guidance to setting individual permit conditions, and may improve consistency of application for future permits. However, legal uncertainty over imposition of financial securities (other than bonds) would continue to exist. Unlikely to have impact on existing permits/licence holders. |
| Regulatory certainty: Does the option make regulatory requirements more clear and transparent, and outcomes more predictable? | 0 Inconsistent treatment of information requirements in permit conditions creates a degree of regulatory uncertainty and unpredictability of outcomes. | + Would produce greater clarity of expectations for permit/licence holders. The regulator's discretion presents a degree of regulatory uncertainty, which may impact investment decisions. This will be managed by guiding the regulator's exercise of discretion through regulations. | 0 / + Would make requirements more clear and consistent. However, outcomes may not always be predictable, as operational policies do not have the same status as legislative requirements. |

| | | | |
|---|--|--|--|
| <p>Practicality: Does the option minimise any implementation risks, provides for administrative simplicity, and encourages timely decision-making?</p> | <p>0 Risk of inconsistent application, and administrative complexity.</p> | <p>++ Would improve the regulator's visibility of current and emerging risks, and improve its ability to respond in a timely and preventative manner. The complexity involved in assessing financial capability would vary across permit/licence holders. These would be assessed on a risk-based basis. The complexity involved in administering financial securities would vary with the instrument and approach selected. These would be managed through careful planning and cost estimation.</p> | <p>- The process of permit condition renegotiation would be highly resource-intensive, and could be slow and difficult.</p> |
| <p>Overall assessment</p> | <p>0</p> | <p>++ much better than status quo.</p> | <p>0 / + slightly better than status quo.</p> |

Section 4.3: Expanding the current enforcement toolbox

4.3.1 What is the specific problem?

Status Quo: Limited enforcement toolbox

The current CMA enforcement provisions (as they apply to decommissioning-related breaches and all other breaches of the CMA), significantly limit the regulator's ability to manage, deter, and/or respond to instances of non-compliance in a timely, effective and proportionate manner.

Ineffective compliance and enforcement tools to respond to mid-level breaches

The regulator currently does not have an effective suite of enforcement tools for responding to mid-level breaches of the CMA and permit conditions. This limits its ability to manage the risks of non-compliance effectively. Mid-level breaches are those serious enough to warrant a sanction to deter further non-compliant behaviour, but which are not serious enough to reach the threshold for a court-ordered remedy, such as a criminal prosecution or the imposition of civil penalties.

Under the current CMA provisions, the enforcement tools available to the regulator are limited to:

- taking no action;
- requesting the permit/licence holder to address non-compliance (which does not legally compel action);
- taking action through the courts; and
- initiating the permit revocation process (which involves notifying an intention to revoke a permit and following through with revocation if non-compliant behaviour is not rectified).

There are significant limits to the effectiveness of each of these tools. In some circumstances, taking no action would significantly undermine the key objectives of the CMA regime. This includes situations where royalty returns are not filed or royalties are not paid; where a person is mining without a permit effectively expropriating the Crown's resources; or where a permit holder is regularly non-compliant with its reporting obligations, creating uncertainty around key reporting metrics, e.g. the Crown's reserves.

Requests to permit/licence holders to address non-compliant behaviour are heavily dependent on the permit holder's voluntary cooperation. Such requests are not directly enforceable, meaning that where a permit holder does not comply with the request, the regulator's only recourse is to the court in respect of the original breach. For mid-level breaches court action is often time-intensive and cost prohibitive. This leads to lack of consequences for continued non-compliance, which does little to address the conduct of the non-compliant parties who are habitually non-compliant.

Taking court action, while often effective in addressing non-compliance, represents a significant escalation and it is also the most time-intensive and costly option, reserved for serious and intentional non-compliant behaviour. Diversion (settling in the early stages of the court process) through the courts is often a preferable approach (once proceedings are initiated) but the initiation of proceedings is also time-intensive and costly.

Seeking to revoke the permit to incentivise compliance can also be highly disproportionate to the level of non-compliance. It can also create perverse incentives in some cases, as once a permit is revoked the permit holder has few responsibilities under the CMA, and the regulator has few enforcement powers.

When considered as a package, the current enforcement toolbox is blunt in application, with little provision for the regulator to achieve compliance outcomes that are effective and proportionate relative to the breach that occurred in a given situation.

While requests to comply can be effective at supporting voluntary compliance where there are unintentional and low-level breaches (by making it easier for permit holders willing to do the right thing through information provisions) and court action and revocation can ensure enforced compliance in situations of intentional and serious breaches (by using the full force of the law); - neither of these tools are effective at assisting and directing compliant behaviour for mid-level breaches where permit holders may lack capability to comply and/or have propensity for non-compliance. The enforcement tools suitable for this type of mid-level breaches would typically aim to improve the regulator's visibility of the operator's practices (through increased monitoring and targeted assessments), allow the regulator to compel action (through legally enforceable mechanisms), and may also provide for immediate corrective action (through the imposition of fines).

In the context of potential failure to undertake and fund decommissioning activities, the regulator is currently restricted to prosecuting permit/licence holders (for a breach of 'good industry practice' or for a breach of the specific permit condition) or proceeding with the permit revocation procedures. If prosecution is successful, this would mean that a permit holder would be convicted of a crime under the CMA and may find it difficult obtain permits in the future. If a permit is revoked or transferred to the Crown, the permit holder would not be released of any liability for actions or omissions before the revocation or transfer date. However, there could be difficulties in practically compelling a former permit holder to fulfil an obligation if they are owned by one or more foreign companies, headquartered overseas, or if the company ceases to exist. In essence, the regulator is currently unable to compel action and/or order permit holders to compensate the Crown if the Crown ends up undertaking decommissioning because the permit holder did.

More generally, the lack of suitable compliance and enforcement tools to address a diverse range of non-compliant behaviour means that the regulator is unable to take a proportionate enforcement action, using fit for purpose enforcement tools, while taking into account the individual circumstances of each case. If the CMA compliance and enforcement toolbox is not expanded:

- significant resources could be spent on taking disproportionate enforcement action relative to the breach that occurred; and
- incidents of mid-level non-compliance may increase if no enforcement action is taken due to cost, probability of success, and public interest concerns; and
- confidence and trust in the CMA regime, as well as the overall levels of compliance, may reduce if currently compliant operators perceive that there is a not a level playing field in the market, where non-compliant operators are able to get away with breaches and continue to operate unaffected.

Weak incentives for non-permit holders to comply with the regulator's information requests

The CMA currently contains a general provision that enables the regulator to require information from any person for the purposes of administering the CMA. This provision is typically used to seek information from permit holders, and can also be used for ex-permit and non-permit holders (such as other interested or affected parties). Generally, information requests are made about active permits, and the operation and capabilities relating to those permits and permit holders.

However, while it is an offence (with a corresponding financial penalty) for a permit holder not to comply with a request for information, there is currently no offence (nor any corresponding financial penalty) for non-permit holders (including ex-permit holders) not to provide information requested under this section.¹³ This means there can be little/no incentive for non-permit holders to comply

¹³ This is exercised through section 33 which requires permit holders to "co-operate with the Minister, the chief executive, and enforcement officers for the purpose of complying with the conditions of the permit, this Act, and the regulations". This section does not apply to non-permit holders.

with an information request and no ability for the regulator to enforce compliance.

The information gap can be significant and may at times inhibit the regulator's ability to detect, investigate and incentivise compliance in some circumstances, e.g. where non-permit holders hold information relevant to an investigation of a permit holder, or where a person has never been a permit holder and is illegally mining Crown-owned minerals.¹⁴ In some situations, not having access to such information may also delay or prevent permit holders from being released from their permit, potentially tying up land that could otherwise be re-permitted.

Unclear record keeping requirements

The CMA currently requires detailed records and reports to be kept in respect of all prospecting, exploration, and mining activities conducted by or on behalf of the permit holder for at least seven years after the year to which they relate or for at least two years after the permit to which they relate ceases to be in force, whichever is the longer.

However, we understand that there is some uncertainty among permit holders about the scope and measures of adequacy in relation to these record keeping requirements. The CMA is currently silent on these.

This has in the past prevented the regulator from obtaining access to financial information (such as financial records), as well as the documents and calculations that feed into creating this information. Being able to request such information from time to time would enable the regulator to verify information such as royalty returns and other aspects of compliance with the CMA regulatory requirements.

4.3.2 What options are available to address the problem?

We considered two broad options, in addition to the status quo, for addressing these problems. These are described below and include:

- **Option 4.3.1:** Amending the CMA to provide the regulator with new enforcement powers, strengthen incentives to comply, and clarify existing requirements.
- **Option 4.3.2:** Increasing the use of non-statutory means to improve compliance.

Option 4.3.1: Amending the CMA to provide the regulator with new enforcement powers, strengthen incentives to comply, and clarify existing requirements

Under this option the CMA would be amended to provide the regulator with new enforcement powers to impose enforceable undertakings and issue compliance notices. The CMA would also be amended to provide an authority to develop an infringement offence scheme, strengthen the incentives of non-permit holders to comply with the regulator's information requests, and clarify existing record keeping requirements. These tools will be available to the regulator to use across all types of potential breaches of the CMA provisions, not just the decommissioning-related ones. Each of these tools is described below.

¹⁴ In one instance, MBIE became aware of a person mining aggregate without a permit (or associated resource consents and other regulatory approvals). In this case, information needed to launch proceedings was obtained from the land owner after a request was made under section 99F of the CMA. However, had the land owner not complied with the request, MBIE would have been unable to compel them to comply. Given this uncertainty, MBIE initially tried to obtain the information without making a request under section 99F, and only resorted to the section 99F request after this initial request was not complied with.

Introducing a new enforcement power by enabling the regulator to accept enforceable undertakings

This option would amend the CMA to provide the regulator with a power to accept enforceable undertakings, following a contravention of the CMA requirements. Generally used as an alternative to prosecution, it would allow a permit/licence holder to voluntarily enter into a binding agreement with the regulator. The regulator would have broad discretion to accept an undertaking from the permit/licence holder to take specific actions to address the contravention, in exchange for the regulator agreeing not to bring court proceedings. The parties can agree actions that are wider and more tailored than those that a court might impose, thus allowing bespoke solutions that address breaches in a proportionate manner.¹⁵ Examples of enforceable undertakings powers are contained in the Commerce Act 1986, the Financial Markets Authority Act 2011 and the Health and Safety at Work Act 2015 (HSWA).

Once accepted, the undertaking would become legally binding and its terms would be directly enforceable by application to the court. The penalty for breach of an undertaking would be set at the maximum level of \$200,000, which is broadly in line with the maximum penalties provided for other breaches of the CMA, and other legislation within the wider regulatory system (e.g. the RMA and HSWA). This level of penalty strikes the right balance between the deterrent value of the penalty and the incentives on a permit/licence holder to bear the risk of the cost of proceedings. The incentives for the permit/licence holder to enter into enforceable undertakings would depend on there being a credible threat of court action should they decline to cooperate. This means enforceable undertakings need to also be supported by continued use of litigation, where appropriate.

In general, enforceable undertakings allow greater flexibility for the regulator to address non-compliance, improve incentives to comply, and allow a more cost-effective enforcement response, as well as improving consistency with modern regulatory practice.

Introducing a new enforcement power by enabling the regulator to issue compliance notices

This option would amend the CMA to provide the regulator with a power to issue an enforceable compliance notice. A compliance notice is a formal notification from a regulator that states that the regulator has reasonable grounds to believe that there is a level of non-compliance, specifies exact requirements that the regulator believes are not being met, stipulates specific actions to address the non-compliance, and sets firm deadlines by which these actions must be completed.

The validity and reasonableness of the content of the compliance notice would be able to be challenged in court by the recipient, which would provide the necessary checks and balances. The court will be able to direct the content of the compliance notice to be either complied with, overturned, or modified as the courts see fit.

Failure to comply with a compliance notice would be made an offence under the CMA and attract a maximum penalty of \$200,000, by application to the court. As with the proposed maximum penalty for breaches of enforceable undertakings, this is broadly in line with the maximum penalties provided for other breaches of the CMA, and other legislation within the wider regulatory system (e.g. the RMA and HSWA).

¹⁵ Permit holders are obliged to adhere to their permit conditions. However, the regulator can only take action *after* a permit holder has failed to do so. This means a permit holder could be granted an exploration permit of five years duration and surrender after four years and 11 months without having completed the obligations that needed to be met within five years and remain “in good standing”. With enforceable undertakings, the regulator could observe a lack of progress after two years and intervene early to ensure the work programme is progressed (or the permit is surrendered earlier, allowing the acreage to be reallocated more promptly).

Ability to issue enforceable compliance notices would allow greater flexibility for the regulator to address mid-level non-compliance, improve incentives to comply, and allow a more cost-effective regulatory response.

Introducing a regulation-making power to establish an infringement offence scheme

Under this option, the CMA would be amended to include a new regulation-making power to enable a new infringement offence scheme to be developed in regulations. An infringement offence scheme provides an administratively efficient method of encouraging compliance with the law by imposing a set financial penalty following relatively minor breaches of the law. It effectively enables the enforcement officer to issue instant fee where there are reasonable grounds to believe that there has been clear, relatively low-level, breaches (such as the failure to file an annual royalty return or annual summary report by the due date). Infringement offence schemes are a common feature of many other regulatory regimes, including fisheries, resource management, and telecommunications.

Under this option, the authority establishing an infringement offence scheme would be supported by the amendments in the CMA that would set the maximum fee to \$1,000 for an individual and \$3,000 for a body corporate, per infringement.

Under this option, the detailed design of an infringement offence scheme would be set in regulations, as is the case with other regulatory regimes, and in line with guidance issued by the Ministry of Justice.¹⁶ The regulations would specify such provisions as the form of the infringement notice, the specific action or omission constituting an infringement offence, and the specific penalty levels for each infringement offence. The development of these regulations would be subject to a separate stakeholder consultation and Cabinet decision making processes.

Introducing a new offence and penalty provision

Under this option, the CMA will be amended to make it an offence for non-permit holders to not comply with the regulator's reasonable information requests made under section 99F of the CMA.

Failure to respond to an information request is often a lower level breach, and does not generally represent serious or reckless offending, unless there is a deliberate intent to mislead, obstruct or deceive the regulator. The maximum level of penalty would therefore be set at the same level as the penalty for a breach of permit holder's obligations under section 100(2) of the CMA, which is \$20,000, or \$2,000 per day for an ongoing offence. This maximum penalty level provides an upper limit for the courts to determine the level of actual penalty based on the individual circumstances.

Clarifying existing record keeping requirements

Under this option the CMA would be amended to provide for a specific definition of the term "records" as it applies to permit/licence holders' record keeping requirements, and a new regulation making power to further specify the details of the record keeping requirements in specific circumstances if necessary.

The definition would be modelled on the provisions in the Tax Administration Act 1994, while building in some sector specific (decommissioning related) information. The CMA would be amended to clarify that all permit/licence holders, and in respect of each permit, would need to keep records (both electronically and in hard copies) of the following nature:

- a record of the assets and liabilities of the permit holder;
- a record of the income and expenditure of the permit holder;

¹⁶ <https://www.justice.govt.nz/assets/Documents/Publications/infringement-governance-guidelines.pdf>

- a record of all entries from day to day of all sums of money received and expended by the person (in relation to that permit) and the matters in respect of which the receipt and expenditure takes place;
- the charts and codes of accounts, the accounting instruction manuals, and the system and programme documentation which describes the accounting system used in each permit year in the carrying on of that permit activity;
- books of account (whether contained in a manual, mechanical, or electronic format) recording receipts or payments or income or expenditure;
- vouchers, bank statements, invoices, receipts, and such other documents as are necessary to verify the entries in the books of account referred to above; and
- documents in respect of financial, economic, scientific or other technical data and information, including underlying calculations.

In addition to these generic record keeping requirements, this option would also provide for some specific financial information requirements (drawing on the provisions of the Financial Reporting Act 1993) that would need to be provided to the regulator as part of the initial and periodic financial capability assessments. These specific requirements would differentiate between Tier 1 and Tier 2 permits¹⁷ and include:

- **Tier 1 permits:** financial statements that have been prepared in accordance with Generally Accepted Accounting Practice (GAAP) as defined in section 6 of the Financial Reporting Act 2013.
- **Tier 2 permits:** any financial statements that have been prepared in accordance with GAAP as required by any statute or regulation; or where the above does not apply, financial statements prepared in accordance with other non-GAAP financial reporting standards or authoritative notices and guidance as is promulgated by the accounting profession from time to time.

The clarification of the record keeping requirements would allow the regulator to access the components that make up the permit holder's financial information, as well as providing useful context within which the information is provided. For example, documents in respect of financial, economic and scientific data might relate to estimating the costs of decommissioning activities and/or provide context for items that go into royalty returns to help the regulator understand the origin of costs and revenues. In line with other legislation, and to ensure that records can be easily accessed by the regulator, the CMA would also provide for the records to be kept in New Zealand; kept in English, Te Reo Māori, or another written official New Zealand language; and be clear as to which permit(s) they relate to, and differentiate between activities undertaken under different permits.

Option 4.3.2: Increasing the use of non-statutory means to improve compliance

Under this option, the regulator would make greater use of its existing tools coupled with enhanced guidance, sector education and outreach. This option would involve building on the regulator's existing sector engagement and education function, by issuing further, more detailed policy and guidance documents, direct outreach to permit/licence holders, publicising the outcomes of compliance activities, and using traditional and social media to increase awareness of the CMA regime, including compliance obligations and regulatory enforcement.

¹⁷ The CMA separates permits into two tiers to reduce the administrative burden for the majority of permit holders but increase the scrutiny applied to high-value or high-risk permits. Tier 1 permits are defined as complex, higher risk and return mineral operations, based on expenditure or production thresholds set out in Schedule 5 of the CMA. They are subject to closer assessment, monitoring and management. Tier 2 permits are lower risk and return industrial, small business, and hobby mineral operations, which are managed in a pragmatic streamlined process incurring less time and effort for all parties.

4.3.3 Impact analysis

| Assessment criteria | Status quo/ No action | Option 1: Amending the CMA to provide the regulator with new enforcement powers, strengthen incentives to comply, and clarify existing requirements | Option 2: Increasing the use of non-statutory means to improve compliance |
|--|---|--|--|
| Effectiveness: Does the option address the problem effectively? | 0 Current toolbox is ineffective for mid-level breaches. Incentives to comply are weak and some regulatory requirements are unclear. | ++ Would improve the regulator's ability to incentivise and enforce compliance in a much more effective and proportionate manner, especially for mid-level breaches. Incentives to comply would be strengthened by a new offence provision. Clarification of statutory terms would improve clarity and consistency of application. | 0 / + May improve awareness and provide some clarity of statutory terms, but is highly unlikely to provide any further deterrence for mid-level breaches. No change to the current weak incentives to comply. |
| Proportionality: Does the option minimise the costs, risks and potential unintended consequences? | 0 Creates risk of non-compliant behaviour. | 0 / + No implications for compliant permit/licence holders. Checks and balances designed into the option would safeguard against the regulator's potential over-reach. | 0 / - No implications for compliant and non-compliant permit/licence holders. Regulator's interpretation of unclear regulatory terms may be challenged in courts. |
| Regulatory certainty: Does the option address the problem in a way that makes the regulatory requirements more clear and transparent, and policy outcomes more predictable? | 0 Some requirements are unclear and enforcement outcomes may not be predictable. | ++ Would provide more predictable range of responses to mid-level breaches and clear define statutory terms. Would enable the scope and process around enforceable undertakings, compliance notices, and infringement fees to be clearly prescribed, creating more certainty, transparency and predictability of regulatory outcomes. | 0 May provide more clarity and predictability of the regulator's approach to enforcement, but no substantive change. |
| Practicality: Does the option minimise any implementation risks, provides for administrative simplicity, and encourages timely decision-making? | 0 Creates risk of non-compliant behaviour and does not encourage timely and proportionate enforcement action. | ++ Implementation risks are low, as the new enforcement tools are modelled on other regimes. Enforcement action is likely to be more administratively simple and decision-making more timely, as fewer breaches would need to be taken to court. | 0 / - Would divert the regulator's focus and resources away from other functions, and create additional administrative burden for no/little benefit. |
| Overall assessment | 0 | ++ much better than status quo. | 0 the same as status quo. |

Section 5: Conclusions

5.1 What option, or combination of options, is likely best to address the problem, meet the policy objectives, and deliver the highest net benefits?

Recommended package of options

Our preferred approach is a combination of the following three options:

1. **Option 4.1.1:** Amending the CMA to introduce an explicit statutory obligation for permit/licence holders to undertake and fund decommissioning activities, as an integral part of the permit to mine petroleum resources.
2. **Option 4.2.1:** Amending the CMA to:
 - require permit/licence holders to provide the regulator with sufficiently detailed and up to date planning and financial information;
 - enable the regulator to conduct periodic financial capability assessments; and
 - empower the regulator to require financial security for decommissioning to be maintained and accessed, if necessary.
3. **Option 4.3.1** Amending the CMA to:
 - introduce new enforcement powers, including: enforceable undertakings, compliance notices, and infringement fees;
 - introduce a new offence and penalty provision; and
 - clarify existing record keeping requirements.

The proposed package will establish a clear and explicit statutory obligation on all current and future permit and licence holders to undertake and fund their decommissioning activities, and provide for more effective monitoring and informed regulatory oversight of permit holders' actions. Importantly, it will enable the regulator to take preventative measures, such as requiring financial security to be established for decommissioning purposes that could be accessed by the Crown in the event or high risk of company default. The proposed package will also enable timely and proportionate enforcement action to be taken, if necessary.

Together, this package of options represents an improvement to the status quo, and provides for the greatest effectiveness in creating a robust outcome-focused risk-based regulatory framework. Whereby, the overarching statutory obligation is supported by sufficient regulatory flexibility to impose specific requirements that are proportionate and can be applied to individual circumstances across a range of business models and practices. Recognising that this level of flexibility may reduce regulatory certainty and impact investment decisions, additional regulation-making powers will be provided to enable the provision of further guidance on how such flexibility will be applied in practice. The detailed design of the regulations is currently being developed and will be subject to future Cabinet decisions.

As outlined in section 2.5 above, stakeholders were generally supportive of the high-level policy options that formed the basis of our preferred approach. Due to the timing of policy development work, we were unable to consult widely on detailed design characteristics of the proposed policy package. However, we have tested the detailed design features of the proposed options with an industry association, and note that all industry stakeholders will have a further opportunity to comment on the proposed package of options through the Select Committee process for any legislative changes. Furthermore, for some options, the detailed design characteristics will be developed through regulations, which will be subject to future Cabinet decisions, informed by further industry consultation and regulatory impact analysis.

5.2 Summary table of costs and benefits of the preferred approach

| Affected parties | Comment | Impact | Evidence certainty |
|---|--|---|--|
| Additional costs of proposed approach, compared to taking no action | | | |
| Regulated parties – permit/licence holders | Some additional cost would be imposed on those permit/licence holders who follow good industry practice and appropriately plan for their decommissioning activities. The costs would arise from having to engage with the regulator. | <i>Low - Medium</i> | <i>High</i> |
| | Some, quite significant, additional costs would be imposed on those permit/licence holders who do not follow good industry practice and do not appropriately plan for their decommissioning activities. The costs would arise from both having to plan and fund their decommissioning activities and from engaging with the regulator. Additional costs could also arise from the proposal to extend the decommissioning obligation to former permit and licence holders in a case of a transfer. The proposal may raise the costs of acquiring late life assets, resulting in a field being decommissioned in a state where economic reserves are still available. | <i>High</i> The direct costs of decommissioning can be significant, with hundreds of millions of dollars needing to be provided for decommissioning of offshore infrastructure. | <i>High (within significant range)</i> |
| Regulator – MBIE | The regulator will incur additional administration, monitoring and enforcement costs, due to the expanded remit of financial capability monitoring and the enforcement toolbox. | <i>Medium</i> We expect that additional FTEs with specialised financial markets expertise will be required. The extent of the additional costs will be driven primarily by the regulatory design choices, which will be subject to future Cabinet decisions. Confidential advice to Government | <i>Medium</i> |
| Wider government – the Crown and Other parties – other third parties (ie. private land owners and Regional councils) | Permit/licence holders may ultimately pass the additional costs to the Crown (through reduced royalties and taxes) and/or regional economies (through reduced investment and employment in the petroleum sector and its related service industries). Free and frank opinions | <i>Low to Medium</i> The impact is difficult to estimate as it would depend on individual companies' alternative rates of return on the funds that would now be reserved for decommissioning, rather than those funds being returned to shareholders as dividends, used to repay debt, or be re-invested in the business | <i>Medium</i> |

| | | | |
|---|--|---|---------------|
| Total Monetised Cost | Without accurate quantifiable evidence, it is difficult to provide an accurate estimate. Detailed costings of the additional administration, monitoring, enforcement and litigation resources will be developed during policy development for the supporting regulations. | <i>Medium</i> | <i>Medium</i> |
| Total Non-monetised costs | We anticipate a medium increase in overall costs, mainly for compliance, enforcement and potential litigation. | <i>Medium</i> | <i>Medium</i> |
| Expected benefits of proposed approach, compared to taking no action | | | |
| Regulated parties – permit/licence holders | Potentially reduced overall decommissioning costs, arising from a stronger discipline and incentive to plan for decommissioning early and often. More transparent and consistent requirements would reduce regulatory uncertainty and improve predictability of outcomes for the permit/licence holders. | <i>Medium</i> | <i>Medium</i> |
| Regulators – MBIE | The regulator will benefit from simplified administration of the CMA regime, as compliance will no longer need to be monitored against various standards and obligations set out across a wide range of permits and licences. The regulator will also have a clear mandate and new powers and tools to ensure compliance and take appropriate enforcement actions if necessary. | <i>Medium</i> | <i>Medium</i> |
| Wider government – the Crown and Other parties – other third parties (ie. private land owners and Regional councils) | Benefits would arise from potential avoided costs to the Crown and other third parties of potentially having to undertake and fund decommissioning activities in the event of a permit/licence holders' financial default. | <i>High</i> The avoided costs of decommissioning can be significant, particularly as they relate to offshore infrastructure. | <i>High</i> |
| Health and safety and environmental outcomes | In circumstances where the Crown or other third parties may have otherwise chosen not to undertake or fund decommissioning, the health and safety and environmental outcomes will be improved. The exact nature of any environmental outcome is determined by other regulatory regimes that set these standards. | <i>Medium</i> | <i>Medium</i> |
| Total Monetised Benefit | Without accurate quantifiable evidence, it is difficult to provide an estimate. | <i>High</i> | <i>High</i> |
| Total Non-monetised benefits | We anticipate a high level of benefits from avoided costs for the Crown and other third parties from potentially having to fund decommissioning activities. | <i>High</i> | <i>Medium</i> |

5.3 What other impacts is this approach likely to have?

The proposed package of options is expected to strengthen permit/licence holders' commercial incentives to plan for decommissioning at early stages of project development and to reassess their decommissioning options on an ongoing basis, including as part of the overall field development plans. International evidence suggests that planning for decommissioning early and often is likely to improve environmental outcomes at lesser overall costs.

The risk that the Crown or other third parties will potentially have to undertake and fund decommissioning is the highest in relation to existing permit and licence holders, as it is the existing, rather than future, oil fields that will soon require decommissioning. The proposed package will therefore affect existing permits and licences, some of which have been in place for a number of decades, Confidential advice to Government

The proposals are not designed to impose more onerous obligations or set new standards for decommissioning than is currently provided for. Instead, they will provide for more effective means of ensuring that existing obligations are discharged to the existing standards by those who undertake the mining and production activities, not the Crown or other third parties.

The proposals will also bring New Zealand more in line with comparable overseas jurisdictions. Countries such as Australia, the UK, Canada, the US, and Norway have over the years been increasing their ability to more effectively manage the risks to the taxpayer and other third parties of potentially having to fund decommissioning.

The proposed package of options may also have a marginal impact of reducing New Zealand's appeal as a petroleum investment destination as the regulatory regime may appear more onerous. The proposed package is not designed to impose more onerous obligations or set new standards for decommissioning than is currently provided for. Instead, it is intended to provide more effective means of ensuring that existing obligations are discharged to the existing standards by those who undertake the mining and production activities, not the Crown or other third parties. However, the package will impact existing permits and licences, some of which have been in place for a number of decades. Confidential advice to Government

Legal professional privilege

Alternatively, more robust regulation of the petroleum sector may increase its social licence to operate by providing greater public confidence in the regulatory system and stewardship of New Zealand's petroleum resources.

5.4 Is the preferred option compatible with the Government's 'Expectations for the design of regulatory systems'?

We consider the preferred package of options is compatible with the Government's 'Expectations for the design of regulatory systems'.

This package sets out a robust regulatory framework, along with mechanisms to provide further guidance to achieve sufficient level of regulatory certainty and predictability. There are no significant areas of incompatibility, but we note there is further work to design more detailed features of effective monitoring and regulatory oversight provisions, once the framework is established in law.

Section 6: Implementation and operation

6.1 How will the new arrangements work in practice?

The preferred package of options will be implemented through amendments to the Crown Minerals Act 1991. Regulations will be required to provide further detail on the monitoring and regulatory oversight options, along with additional guidance from the regulator. These are subject to further policy work, consultation with stakeholders, and Cabinet decisions, at a later date.

Consideration will be given to the timing of when the amendments should be brought into effect, taking into account the wider changes that are currently taking place (e.g. Covid-19) and the impact these changes will have on the industry. Exact timing will be confirmed on introduction of the legislation to Parliament. The implementation of the options may also involve some transitional period to allow permit/licence holders to make necessary changes to their practices.

The preferred package of options will be enforced by MBIE as the relevant regulator for the CMA regime. MBIE is an experienced regulator, but the proposed package of options is an extension of its existing remit. As set out in the cost/benefit analysis in section 5.2 above, we expect the package to impose additional administrative cost on MBIE as the regulator. While, we do not expect significant impacts on IT systems to arise from the proposed package of options, specialist financial markets expertise will need to be hired and operational monitoring systems established for the administration of financial security instruments (if and when imposed) and for the assessment of financial information and field development plans.

6.2 What are the implementation risks?

There is an inherent risk of unintended consequences. The regulations giving effect to the proposed new financial security tools will need to be designed and implemented in a way that does not precipitate or exacerbate the very financial problems that they are designed to safeguard against (e.g. imposing a stringent financial security requirement on a company that is struggling financially could potentially lead to its default, therefore inability to undertake and fund its decommissioning obligations).

Additionally, even for a financially-healthy company, the requirement of financial security could constrain capital and thereby constrain ability to invest and operate efficiently. This could mean a field is less developed than the Crown would consider optimal (or that the pace of investment is slowed). Implementation of this aspect of the proposed package would need to be very careful and cognisant of the implications of constraining capital.

There is also a risk that permit/licence holders could have difficulty obtaining appropriate financial security, particularly if their finances are strained at the time financial security is sought.

To some extent, this risk will be mitigated through careful development and design of regulations, which will be subject to further policy development, impact analysis and industry consultation, and the proposed risk-based implementation approach. We do not consider that the extent of any residual risk of unintended consequences warrants a different regulatory design or form of government regulation.

The development of the regulations would also require careful consideration of the interdependencies with other regulatory regimes responsible for managing different aspects of the decommissioning activities, such as the decommissioning planning process under the Exclusive Economic Zone and Continental Shelf (Environmental Effects) Act 2012.

Section 7: Monitoring, evaluation and review

7.1 How will the impact of the new arrangements be monitored?

The anticipated impacts will be clearly able to be identified as the proposed approach will involve greater monitoring and oversight of the regulated entities. As the relevant regulator, we will be able to monitor to what extent permit/licence holders are complying with the obligations.

We plan to incorporate monitoring of the effectiveness of the proposed package into our existing monitoring and evaluation programmes and processes. This includes such channels as:

- annual reports provided by permit/licence holders;
- annual review meetings with permit/licence holders;
- the recording system for MBIE to monitor compliance with work programme commitments over time;
- periodic field reviews; and
- other periodic interactions with permit/licence holders.

The system-level impacts will be monitored as part of our wider regulatory stewardship obligations.

7.2 When and how will the new arrangements be reviewed?

There is no plan to conduct a formal review of the proposed package of options within a particular timeframe. However, the interaction with stakeholders following implementation of the amendments, as well as the regulator's ongoing monitoring and enforcement functions, should assist to uncover whether there are any issues that need addressing.

MBIE regularly evaluates and reviews amendments to the law it administers. The changes could, for example, be reviewed and evaluated two to three years after coming into force (subject to resource constraints). An evaluation or review at this time would allow the changes to have bedded in and any initial impacts to show.