

## **In Confidence**

Office of the Minister of Energy and Resources

Chair, Cabinet

### **Final policy decisions for tranche one of the Crown Minerals Act 1991 review**

#### **Proposal**

1. To report back and seek agreement to a final approach for tranche one of the Crown Minerals Act 1991 (CMA) and associated timing considerations.

#### **Executive Summary**

2. Following the Government's announcements regarding future petroleum exploration in April, my officials have been working to give effect to these announcements. As part of this, Cabinet has previously agreed [CAB-18-MIN-0306.01] to a set of key outcomes around the Government's new petroleum exploration approach and to implement it via a two-stage legislative review.
3. Since Cabinet's previous discussion, my officials have worked with the Parliamentary Counsel Office (PCO) to develop legislative options to give effect to the Government's new petroleum exploration policies under tranche one of the CMA review.
4. I recommend Cabinet agrees to specify in the CMA that new petroleum exploration permits can only be granted over onshore Taranaki. I believe this approach provides the most certainty around the Government's aim of a managed transition away from new petroleum exploration and production in line with of our international commitments to transition to a low-carbon economy. Alongside these changes, the rights of existing permit holders would be preserved.
5. It will be necessary to resolve the tension between this approach and the current purpose of the CMA, which provides a framework under which petroleum exploration is strongly encouraged. I am recommending that the new prohibitions are made despite the current purpose or as if they do not derogate from it, without amending the existing purpose, which applies to all minerals and permit types. I consider this approach will minimise any unintended consequences and is consistent with Cabinet's previous decisions to limit the changes in tranche one to only those that are necessary.
6. When amending the CMA to prohibit new petroleum exploration permits outside of onshore Taranaki, it will be necessary to consider what would happen for onshore Taranaki beyond 2020 if no further changes are made to the CMA. I am recommending that the revised CMA, by default, allows for onshore Taranaki block offers to continue beyond 2020. This means any future change to this position would require further CMA changes.

7. Following Cabinet's agreement to this paper, my officials will work with PCO to draft a bill for tranche one as quickly as possible. In order to commence a block offer in 2018, as previously agreed, it will be necessary to have the tranche one amendments come into force by the end of September 2018.

## Background

8. On 12 April 2018, the Government announced its intention to limit the area available for new petroleum exploration permits to onshore Taranaki. Cabinet subsequently agreed on 2 July 2018 [CAB-18-MIN-0306.01] to a set of key outcomes around the Government's new petroleum exploration approach and to implement it via a two-stage legislative review.
9. This two-stage review will involve minimal changes in an initial tranche of reforms to progress quickly, followed by a second tranche of reforms following an in-depth look into issues affecting the CMA. This second tranche will involve broad public and stakeholder engagement.
10. The outcomes Cabinet agreed were:
  - 10.1. To give effect to the new offshore petroleum exploration policy while preserving the rights of existing permit holders (for either petroleum or other minerals);
  - 10.2. To hold a block offer for onshore blocks in Taranaki for 2018, and again in 2019 and 2020;
  - 10.3. To prohibit surface access to conservation land for certain activities, such as drilling, as they specifically relate to Taranaki Block Offer 2018, 2019, and 2020;
  - 10.4. To ensure the onshore Taranaki block offer processes are robust and therefore unlikely to be subject to successful judicial review proceedings; and
  - 10.5. To reduce the risk that applications for offshore Petroleum Exploration Permits (PEPs) will be made outside of the onshore block offer process, which could lead to new PEPs being granted contrary to the Government's new policy on the basis of the current law.
11. Alongside these outcomes and the two-stage approach, Cabinet:
  - 11.1. noted that decisions made to progress Block Offer 2018 are not intended to act as a precedent for the no new mines on conservation land policy work underway;
  - 11.2. authorised the Minister of Energy and Resources (the Minister) to seek advice from the Parliamentary Counsel Office (PCO) on drafting options to give effect to the agreed outcomes; and
  - 11.3. invited the Minister to report back to the Cabinet Economic Development Committee with options and timing considerations to progress the first tranche of legislative changes.

12. This paper provides that report back on the drafting approach and timing considerations.

### **Policy decisions for tranche one of legislative changes**

13. Cabinet has agreed that tranche one of the legislative changes to the CMA will consider only those changes necessary to give effect to the new offshore petroleum exploration policy and allow onshore block offers to be run successfully until 2020.
14. PCO has considered the Government's key outcomes for tranche one, and provided the Ministry of Business, Innovation and Employment (MBIE) with advice on legislative options to give effect to them.
15. In addition to the specific legislative approach, I consider there is merit in Cabinet also confirming the Government's desired policy outcome behind the announcements. I propose this outcome could be described as:

*"Initiating a long-term transition away from petroleum exploration and production, in line with New Zealand's international commitments to transition to a low-carbon economy".*

16. This outcome could then inform the purpose and drafting of the tranche one amendment bill to give effect to the recent policy announcements.

### *Legislative approach for tranche one*

17. From the legislative approach options proposed by PCO I recommend that we create specific legislative prohibitions or an indefinite moratorium.
  - 17.1. Option 1 – A package of amendments to alter the existing framework.
  - 17.2. Option 2 – Create specific legislative prohibitions or an indefinite moratorium.
  - 17.3. Option 3 – Create new regulatory power to make prohibitions or moratoria.
18. This approach would require associated provisions to preserve existing rights and manage any applications currently under consideration.

### *Create specific legislative prohibitions or an indefinite moratorium*

19. Under this approach, the CMA will be amended so that it prohibits granting any new PEPs either offshore or onshore outside of Taranaki. PEPs would still be available through onshore Taranaki block offers, but these would prohibit access to the surface of conservation land for certain activities such as drilling.
20. The amended CMA will also need to include a default position on what happens after 2020 if no further changes are made to the CMA.
21. I recommend that for the purposes of this legislative change, onshore Taranaki block offers can, but are not required to, run beyond 2020. I consider this position is consistent with the Government's commitment to a just transition to a low-carbon

economy. If desirable, the Government could also announce its intention to review this position around 2020.

22. This will send a strong signal that, barring further legislative change, no new offshore petroleum exploration will occur and new onshore exploration can only occur in Taranaki. This provides more enduring certainty around New Zealand's petroleum exploration policy as it would require a future Act of Parliament to change.

## **Recommended approach**

### Amending the CMA's purpose or exempting new provisions from the existing purpose

23. There is a tension between the current purpose of the CMA and the new policy outcomes. Options for addressing this tension are outlined below.
24. Section 1A states that the purpose of the CMA is to promote prospecting for, exploration for, and mining of Crown owned minerals for the benefit of New Zealand.
25. There is a clear tension between Cabinet's agreed policy outcomes and the word "promote" in section 1A of the CMA. There is also a tension between the policy outcomes and the interpretation of "for the benefit of New Zealand" in the Minerals Programme for Petroleum 2013 (the Petroleum Programme) which sets out additional direction and guidance on how New Zealand's petroleum resources are managed. The Petroleum Programme states that "the benefit of New Zealand" is best achieved by increasing New Zealand's economic wealth through maximising the economic recovery of New Zealand's petroleum resources.
26. There will need to be some additional changes to the CMA to address the tension between the current purpose and the new policies.
27. s 9(2)(h) I recommend that to address the tension I insert in the CMA a statement to the effect that the relevant new enabling provisions apply despite section 1A or must be treated as if they do not derogate from section 1A.
28. MBIE considers that having the enabling provisions apply despite section 1A is more consistent with the previous Cabinet decision to limit the changes in tranche one to only those necessary to give effect to the new offshore policy and allow onshore block offers to be run successfully. This is the case partly because a changed purpose (unless otherwise agreed) would apply not just to PEPs but to all new mineral permits, including new prospecting and mining permits.
29. In addition, with an amended purpose the Government is likely to come under increased pressure from stakeholders to, for example, intervene in individual permit or access arrangement applications for political or environmental reasons. Interventions of this nature would potentially undermine investment confidence in New Zealand. Even the possibility of such interventions could have a negative effect on investment confidence.
30. It will be necessary to highlight that it is intended as an interim approach to allow for block offers to be run until 2020 while a more permanent approach can be considered as part of the tranche two CMA review.

31. Tranche two would then involve more in-depth consideration of the purpose in relation to all Crown-owned minerals and alongside other changes like those that may arise under the “no new mines on conservation land” work stream. It will also enable this consideration to be informed by public consultation to minimise the risk of unintended consequences.

### **Legal advice on timing of Block Offer 2018**

32. s 9(2)(h)

33. s 9(2)(h)

### **Timing implications for tranche one**

34. The Government has previously made a public commitment to commence a block offer in 2018.
35. To achieve this, the legislation will need to progress all stages by the end of September 2018. This would allow a new iwi consultation period to commence on 1 October 2018 and following this, Block Offer 2018 to commence in December 2018.
36. To accommodate this timeframe, following decisions in this paper, MBIE and PCO will work together to draft a bill for tranche one as quickly as possible.
37. I am aiming to return to Cabinet with a draft Bill in September 2018.
38. My office has also begun liaising with the Leader of the House’s office to prepare for the bill’s passage through the House in September.

### **Relationship between tranche one and tranche two and associated Petroleum Programme changes for Block Offer 2018**

39. To meet the Government’s policy outcomes, the changes made in tranche one must be made quickly and with little or no consultation. This approach is likely to attract some criticism.
40. To help address such concerns, it will be necessary to inform stakeholders that the tranche one changes are intended as an interim measure to give effect to the new offshore policy and allow block offers to run successfully until 2020. A wider review of the CMA will then follow to consider the long-term settings for managing the Crown’s petroleum and minerals estate.



41. In particular, it will be important to highlight the Government's intention to release a discussion document in the coming months that will canvas a range of issues around the CMA and the management of the Crown minerals estate.
42. In addition, my officials are looking at whether or not subsequent changes to the Petroleum Programme are desirable to support the amended CMA and associated block offers. Any such changes would be seen as an interim step while the wider review of the CMA progresses.

## **Consultation**

43. The following agencies have been consulted: Department of Prime Minister and Cabinet, the Treasury, Parliamentary Council Office, Crown Law Office, Ministry for the Environment, Department of Conservation, Te Puni Kōkiri, Ministry for Primary Industries (Fisheries), Ministry of Justice (Post Settlement Unit), and the Environment Protection Authority.
44. Te Puni Kōkiri (TPK) raised concerns regarding the proposed level of engagement with Māori on the policy changes proposed in tranche one and the potential for unintended consequences that could impact Māori. TPK suggests consideration of some form of consultation with Māori authorities (for example, an exposure draft of the bill). TPK welcomes the intention to consult more fully, including with Māori, on the wider CMA review under tranche two.
45. The Department of Conservation considers progressing non-legislative matters associated with this work should be considered irrespective of the legislative option chosen. For example, the tension identified in paragraph 25, regarding the current minerals programme and the government's desired policy outcome (identified in paragraph 10) could be at least partially resolved through a review of the current Minerals Programme for Petroleum.

## **Fiscal and Financial Implications**

### *Fiscal implications*

46. When the new offshore policy was first discussed at Cabinet, it noted that I would report back on the fiscal implications of the new offshore exploration policy. It is important to distinguish between direct fiscal implications for the Crown and the economic implications for the whole New Zealand economy.
47. The announcement of the policy needs to be seen in the context of global commodity cycles. Global exploration development expenditure was in steady decline following the sharp drop in oil prices in 2014. Participants focused on strategies to optimise production while deferring exploration investment. The impact of this locally was a decline in jobs and investment. The global trajectory shifted from around 2017 with increased expenditure in exploration activities and an increase in development projects being approved. Over the coming decades the ability to predict the time and magnitude of oil and gas commodity cycles will be increasingly difficult and inaccurate.

48. There is no immediate fiscal impact because the policy only affects new PEPs, and it typically takes several years from making a new discovery to bringing production online. This forward activity is not reflected in the Government's books.
49. The new policy is likely to have both an economic impact in the medium-term, and a long-term fiscal impact in terms of forgone royalties and tax revenue that might have been collected from future permit holders. It is difficult to accurately quantify these impacts, as while the benefits of a new discovery can be estimated, it is difficult to predict when (if ever) a new commercial discovery might have been made.
50. MBIE has undertaken modelling to provide a range for the long-term fiscal impact as part of assessing the regulatory impact of the proposals in this paper. This is discussed in more detail in the impact analysis section below. The modelling should be treated with caution for the reasons outlined.
51. It is also difficult to quantify the impact on the economy if no new discovery is made from the existing PEPs. At present, remaining gas reserves equate to 10.2 years of current demand. Natural gas is used in a number of commercial and industrial applications from methanol or fertiliser production, to electricity generation, to providing heat for hospitals and schools. There are also approximately 280,000 homes that use natural gas for hot water heating and cooking. Historically, over 70 per cent of this natural gas has been provided from offshore permits.
52. There are likely to be opportunities for gas users to switch to electricity or other sources as part of the country's long-term transition to a low emissions' future. To allow sufficient time for a transition to renewable sources, it is important to ensure the policy settings for existing petroleum exploration and mining permits are sufficient to encourage investment in extending the life of existing gas fields while new fields are discovered.
53. The new offshore policy may also result in existing asset owners choosing not to invest to extend the life of assets (particularly of "late in life" assets), bringing forward the decommissioning of these assets. The Crown is liable for up to 42 per cent of decommissioning costs for royalties and taxes that have effectively been overpaid during the course of field production.

#### *Financial implications*

54. There are no immediate financial implications as a result of this paper.
55. There may be financial implications in the future as a result of lower overall petroleum permit fees paid to MBIE under the new offshore policy. These permit fees are collected to recover costs from activities associated with managing permits and promoting mineral exploration in New Zealand. In 2016, when the fees were last reviewed, the memorandum account was in deficit. Cabinet agreed at the time that this deficit should be stabilised in the short-term but that the fees would be reviewed again in 2019 with a view to bringing the memorandum account back into balance.
56. MBIE intends to review permit fees in 2019 as part of the wider review of the Act under Tranche two. There may be some additional challenges to increase permit fees given that offshore PEPs, which typically incur the highest fees, will no longer

be granted. Should this result in financial implications for the Crown, they will be addressed at the time.

### **Legislative Implications**

57. Legislation is required to give effect to the decisions in this paper. The proposed legislation will bind the Crown.
58. Consequential/related changes to the Programme Petroleum are also anticipated.

### **Impact Analysis**

59. A Regulatory Impact Statement is attached as Annex Two to this paper. MBIE has attempted to model the direct monetised costs of the regulatory changes proposed in this paper. However as this is a complex area to model MBIE has not been able to accurately model precise outcomes. This means the figures provided are not sufficiently robust to use to guide decision making.
60. The impact analysis shows potential costs to the Crown of not offering future offshore petroleum exploration and continuing to offer onshore petroleum exploration in Taranaki range \$1.2 billion through to \$23.5 billion using a three per cent discount rate. As GNS Science states in their study that MBIE relied upon for some modelling assumptions, “this study attempts to quantify what is almost unquantifiable, and the numerical results must be treated with caution.”<sup>1</sup>
61. For the Government’s preferred option, MBIE has modelled the net present value potential fiscal impact to the Crown relative to the counterfactual using a three per cent discount rate of \$7.9 billion (real) as a mid-point estimate. This impact is modelled to occur over the period 2027 to 2050. The model does not factor in existing exploration permits which will continue under the Government’s policy. The success rates are modelled to be higher than recent historical trends so may not eventuate. For instance, the actual success rate in the Taranaki Basin (offshore and Cape Farewell) since 2006 was 13 per cent. The GNS Science study adopted a 15 per cent success rate in the Taranaki Basin, acknowledging the basin has moderate maturity in terms of exploration and the success rate over the last few years has dropped away. These rates compare to MBIE’s model, which uses a 20 per cent success rate. The impact of the transition to a low carbon economy and uses of alternatives to oil and gas have also not been fully modelled.
62. I acknowledge that there are likely to be some costs for the existing industry in Taranaki as part of the transition over the long term, which is why we have begun work on the Just Transition to mitigate those costs and the impact on the community.
63. A Just Transition Unit has been established within MBIE and is working collaboratively with industry, workforce, local leadership and the community to begin mapping out the transition plan. Good progress has been made and I look forward to updating colleagues in more detail in the near future.

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1 Assessment of New Zealand’s Undiscovered Petroleum Resources by Delphi Panel, September 2015



64. The Treasury Regulatory Quality Team (RQT) has reviewed the Regulatory Impact Analysis (RIA) prepared by MBIE and considers that the information and analysis summarised in the RIA partially meets the quality assurance criteria.
65. Due to time limitations and analytical constraints arising from Cabinet's previous decisions, MBIE has not consulted the petroleum industry and the public on the proposals. As such, RQT is not possible to be confident that all potential impacts have been identified. The consultation criterion has therefore not been satisfactorily addressed.
66. Treasury concluded that within these limitations, however, they believe the RIA comprehensively sets out the current state, how it is expected to develop without further intervention and under different policy scenarios, and explores how and why the options meet the assessment criteria. Limitations and uncertainties in the modelling, and the assumptions used to inform it, are carefully explained.

### Human Rights

67. There are no human rights implications with this paper.

### Gender Implications

68. There are no gender implications with this paper.

### Disability Perspective

69. There are no disability implications with this paper.

### Publicity

70. There is no publicity planned as a result of this paper.

### Proactive Release


71. I intend for this paper to be published on the MBIE website, with redactions consistent with the Official Information Act 1982, once the new legislation has been introduced in Parliament.

### Recommendations

The Minister of Energy and Resources recommends that the Committee:

1. **Note** on 12 April 2018, the Government announced its intention to limit the area available for future petroleum exploration permits to onshore Taranaki.
2. **Note** Cabinet subsequently agreed on 2 July 2018 [CAB-18-MIN-0306.01] to a set of key outcomes around the Government's new petroleum exploration approach and to implement it via a two-stage legislative review of the Crown Minerals Act 1991 (CMA).
3. **Note** Cabinet also authorised the Minister of Energy and Resources to seek advice from the Parliamentary Counsel Office (PCO) on drafting options to give effect to the

agreed outcomes and invited the Minister to report back to the Cabinet Economic Development Committee with options and timing considerations to progress the first tranche of the legislative review.

4. **Note** the updated legal risks outlined in this paper since Cabinet's previous discussion on 2 July 2018.
5. **Agree** that the high-level outcome behind the proposed legislative changes is:  
*"to initiate a long-term transition away from petroleum exploration and production, in line with New Zealand's international commitments to transition to a low-carbon economy"*.
6. **Agree** to create specific legislative prohibitions or an indefinite moratorium for tranche one.
7. **Agree**, in addition to one of the approaches above, to include associated provisions to preserve the rights of existing permit holders and manage any permit applications currently under consideration.
8. **Note** under recommendation 6, the current CMA framework will be altered so that the Government can then give effect to the new policy as a statutory decision.
9. **Note** under recommendation 6, only an Act of Parliament could amend or rescind the prohibition on new petroleum exploration.
10. **Note** under recommendation 6, the revised CMA will need to include a default position for onshore Taranaki block offers beyond 2020 (i.e. what will occur after 2020 if no further changes to the CMA are made).
11. **Agree** to amend the CMA so that onshore Taranaki block offers can, but are not required to, continue beyond 2020.
12. **Note** there is a clear tension between the current purpose of the CMA and the Government's new policy outcomes.
13. **Agree** to ensure the new provisions apply despite or as if they do not derogate from the current purpose.
14. **Note** the Government has previously publicly committed to commencing an onshore Taranaki block offer in 2018.
15. **Note** <sup>s 9(2)(h)</sup>  

16. **Note** to Commence a block offer in 2018, without relying on existing preparatory work and consultation with iwi and hapū, the Ministry of Business Innovation and Employment considers the revised CMA must commence by the end of September 2018 at the latest.

17. **Note** to allow time for PCO to draft the bill following the decisions in this paper, the amendment bill will need to return to Cabinet in September 2018 and progress through all stages in the House by the end of September 2018, which may require the use of urgency.
18. **Invite** the Minister of Energy and Resources to issue drafting instructions to PCO to give effect to the recommendations in this Cabinet paper.
19. **Authorise** the Minister of Energy and Resources to consider any issues that may arise during the drafting process and to approve any necessary changes provided they are consistent with the policy proposals in this paper.
20. **Agree** the new bill will have a category two priority (must be passed this year) under the 2018 Legislation Programme.

Authorised for lodgement

Hon Dr Megan Woods

**Minister of Energy and Resources**

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