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Dear David

Submission Proposed Changes to Minerals Program for Petroleum

Introduction

The Petroleum Exploration and Production Association of New Zealand (the "Association") welcomes the opportunity to comment on the proposal to amend the Minerals Programme for Petroleum 2005 ("MPP") to remove to PIT method of allocating petroleum exploration permits (PEPs) from the MPP.

The Association is an incorporated society, operating as a trade association, to promote the interests of companies actively involved in petroleum exploration and production in New Zealand and services companies offering technical and other business support to the sector.

Most of the E&P companies operating in New Zealand are members of the Association. The Association's mission is to promote a legislative, administrative, economic and social framework which efficiently and effectively facilitates safe, environmentally responsible and profitable oil and gas exploration, development and production.

Removal of PIT allocation method

A clear majority of the E&P companies who are members of the Association are generally supportive of the proposal to remove the PIT allocation method for PEPs.

Accordingly, this submission proceeds on that basis and sets out a number of points for the Ministry of Economic Development ("MED") to consider in connection with the implementation of the proposed change and the consequential operation of, and necessary changes to, the Block Offer allocation process.

Implementation of the proposed change

The Government has consulted on and is currently undertaking further review work on the proposed changes to the Crown Minerals Act 1991 ("Act") and the MPP. It is expected that a revised discussion document, addressing both the proposed changes to the Act and the MPP, is to be released in December 2011 for public consultation. It is also expected that such consultation process will result in amendments to the Act and a new Minerals Programme for Petroleum being issued pursuant to the Act.

In the Association's submission on the original August 2010 discussion document relating to the review of the Act, the point was made that it was critically important that the review of New Zealand's petroleum legislation be undertaken in a co-ordinated manner rather than on a piece meal or ad-hoc basis. A review of all the submissions received on that discussion document indicates the same concern running through many of the submissions.

The Government clearly appreciated the problems the proposed disjointed review would have caused and announced on 16 December 2010 that the review of the Act and the MPP was to be delayed and undertaken as a co-ordinated whole. The Association considers such an approach to be clearly correct and intended to ensure optimal regulatory outcomes are achieved.

In the context of the proposed removal of the PIT allocation method, the Association considers the same approach should be followed and the removal of PITs from the MPP should form part of the more wide-

ranging changes to the MPP to be proposed at the end of the year. The Association considers this to be important in order to ensure the permit allocation framework remains coherent, appropriate and that there are no unintended consequences in other parts of the permit allocation framework or the MPP more generally as a result of the removal of PITs.

Accordingly, the Association considers that the relevant changes to the Minerals Programme for Petroleum to remove the PIT allocation method should only be made once the overall implications of the proposed changes (and any “flow on” effect on the MPP that will result from them) have been considered in a comprehensive manner. The obvious opportunity to do that in the (very) near future is in the context of the overall review of the MPP set to be released in December 2011.

This is particularly the case given the consequential proposals the Association makes in relation to the Blocks Offer allocation method set out below (and the suggested inclusion of certain of those proposals in the MPP). It is clear the Crown considers the removal of PIT allocation to be part of a wider strategy in relation to permit allocation via an expanded Blocks Offer process (and, in this regard, the 30 August 2011 notice specifically contemplates PIT allocation being replaced by the Blocks Offer process). This strongly suggests the changes to the MPP should address both the removal of PIT allocation and considerations relating to the expanded Blocks Offer process

The Association notes that such an approach is not only consistent with the approach taken to the review of New Zealand’s petroleum legislation to date as contemplated by the Petroleum Action Plan (November 2009) but is also consistent with the existing requirements under the MPP to ensure the efficient allocation of petroleum rights (see in particular the policies identified in section 2.18 of the MPP).

The Association is mindful of the MED’s concerns in seeking to remove the PIT allocation method. Until such time as the changes to the allocation methodologies become effective, the MED’s concerns relating to unsuitable companies applying for acreage and “low ball” applications can be dealt with by:

- the existing allocation and assessment procedures in the MPP; and/or
- the inclusion of acreage in the Indicative Petroleum Exploration Permit Block Offer Schedule.

The Association would also note that the approach suggested above would not in any way affect the ability of the Crown to undertake its proposed Block Offer round at the end of 2011/start of 2012 (which Block Offer round is strongly supported by the Association).

Flow on changes to the Blocks Offer process

The notice of proposed change to the MPP dated 30 August 2011 foreshadowed changes to the current Blocks Offer process in light of the removal of PITs. The Association agrees that changes to the Blocks Offer allocation methodology will be required in light of the removal of PIT allocation.

The changes the Association believes are necessary or desirable are set out below. An important associated matter is that the changes or processes relating to the expanded Blocks Offer process must be reflected in the MPP (at the same time as the PIT allocation methodology is removed).

While the Association is not in favour of rigid rules or processes being included in the MPP which could have the effect of undermining an expanded Blocks Offer process, it does believe it is very important that the general principles set out below be reflected in the MPP (together with ensuring there is sufficient operational flexibility for the Crown to ensure the expanded Blocks Offer process remains workable for both the Crown, industry and relevant stakeholders).

The inclusion of the points below in the MPP is in accordance with the policy framework set out in the MPP (see in particular Chapter 2) and more generally is consistent with ensuring a certain, stable, transparent and predictable regulatory framework for the Crown and operating environment for industry participants. Such an approach also accords with the Government’s key policy objective of making New Zealand a highly desirable destination for international petroleum investment as articulated in the recently released Energy Strategy 2011.

A summary of the proposed changes or clarifications to the Blocks Offer process for inclusion in the MPP is as follows:

1 Annual Blocks Offers

There should be a general requirement that Blocks Offers should be undertaken on (at least) an annual basis. The Association would not object to some flexibility in relation to this requirement to take into account operational or practical considerations, but strongly believes there should be a clear requirement for annual Blocks Offer rounds (given this will effectively be the only mechanism for making acreage available to industry).

2 Taranaki Acreage available

There should be a general requirement that all unallocated acreage onshore Taranaki should be included in the next available scheduled Blocks Offer round. This is consistent with maximising the investment opportunities in New Zealand's petroleum industry. This requirement could, in the interests of operational efficiency and ensuring the most efficient allocation of acreage, be subject to the exceptions identified immediately below in relation to recently surrendered acreage.

3 Surrendered acreage

Where acreage is surrendered or otherwise becomes available it should be included in the next available scheduled Blocks Offer round. This is mostly likely to result from the surrender of acreage resulting from a permit holder moving to the second five year term of its PEP or where an operator determines to surrender a permit area it no longer wants to pursue.

The Association does, however, believe it would be appropriate to qualify this general requirement by allowing a (say) three or six month period to ensure that all the relevant data in respect of the surrendered area has been provided to the Crown. It may also be appropriate to hold back a surrendered area where it is too small to be separately offered under a Blocks Offer or where it could be combined with adjacent acreage that may be surrendered in the immediate future. Otherwise, recently surrendered acreage should be made available for re-allocation as soon as possible (especially given it is likely to be some of the more prospective acreage).

4 Consultation

Although the notice of proposed change to the MPP specifically mentions the expectation that communities will have an opportunity to comment on areas to be included in a Blocks Offer, it is not clear to the Association whether this will differ from the consultation requirement currently included in the MPP in relation to Blocks Offers. The Association believes the existing consultation requirements contained in the MPP which the Crown must observe in connection with Blocks Offers are sufficient.

The Association also believes that it is appropriate for the Crown (through the MED), as the owner of the petroleum resource, to undertake the required consultation with associated involvement from industry as part of the overall process. The Association considers the most efficient and meaningful stakeholder consultation process would be consultation undertaken by one party (i.e. the Crown) rather than a number of different groups or interests. If the Crown proposes to change the existing consultation processes for Blocks Offers, the Association believes any such revised consultation process/requirement should be included in the MPP.

As a practical matter, the Association notes the consultation requirement should be precisely that. In other words, the Association believes that while the Crown should consult with affected communities and stakeholders (and where appropriate have regard to their views in relation to what acreage should be included in a Blocks Offer where the relevant community/stakeholder would be specifically affected by the Blocks Offer proposal), the relevant communities/stakeholders should not have any form of veto or approval right as to what is (or is not) included in a Blocks Offer. That is a decision for the Crown as the owner of New Zealand's petroleum resource.

5. Competing bids addressing different resources/targets

It is not clear how the expanded Blocks Offer process will apply in respect of competing bids which address different resources/targets. For example, a particular block could attract a bid relating to conventional petroleum activity or a gas hydrate operation. Similarly, a particular block could be the subject of bids relating to both deep and shallow plays.

This is similar to the issue identified in the August 2010 discussion document relating to the review of the Act, and the Association believes should also be considered in the context of the PEP allocation methodology (especially since the Blocks Offer methodology will be the only allocation method available in practice). This is an example of the point made above relating to the importance of changes to the allocation methodologies being considered in the context of the wider review of the MPP.

6. Financial assessment of bidders

Has the MED considered the implication of an expanded Blocks Offer process on the requirement that it assess the financial capability of bidders? Under a PIT allocation model, this is relatively straight forward as the applicant for a PIT area will typically only be applying for one area (rather than several) and the financial capability assessment can be undertaken in respect of that block.

This compares with the situation where under an expanded Blocks Offer process a bidder may apply for several blocks (knowing that it may only get one or otherwise less than all the blocks applied for). The Association believes that the MPP should be expanded to include guidelines as to how the Crown will undertake the financial capability assessment when an applicant applies for several blocks under a particular Blocks Offer (especially given the annual Blocks Offer round will be the only opportunity each year for industry participants to obtain acreage).

7. Extension of land application

The Association considers that the relationship between the expanded Blocks Offer process and extension of land ("EOL") applications needs to be considered further. The rationale for an EOL is to facilitate a more rational carrying out of activities under the permit, including where a prospect may extend across the permit boundary. The Association believes that, where a Blocks Offer is effectively the only allocation mechanism, the possibility of an upcoming Blocks Offer should not limit or preclude a person holding a permit from extending the areas of that permit where it is appropriate to do so and the relevant MPP requirements are met. The particular concern here is given the new primacy (and expanded role) afforded Blocks Offers, they should not unnecessarily restrict EOL applications. This will require the relevant provisions of the MPP (see, for example, sections 5.5.11 and 5.1.6) to be revisited in order to ensure that the EOL-related provisions continue to "fit" with the expanded Blocks Offer process. It also shows (again) the importance of ensuring any changes to the MPP to reflect the removal of PITs and the expanded role for Blocks Offer take place in the context of the wider review of the MPP currently proposed for December 2011.

8. Subsequent change of conditions applications

Given the expanded role for the Blocks Offer allocation method, the Association believes that the provisions of the MPP which relate permit changes of conditions (specifically, section 5.5.7) need to be revisited (and in all likelihood further review and policy work undertaken in relation to them) in order to ensure that they do not undermine or "cut across" the expanded role the MED sees for Block Offers as the primary permit allocation methodology. The Association believes that in the years since the MPP was written the petroleum industry in New Zealand has developed significantly (including as a result of numerous new participants entering the industry) such that the workability of section 5.5.7 and related provisions of the MPP needs to be revisited.

Indications of attractive acreage

The Association understands the MED will welcome individual companies identifying to the Crown in advance of a Blocks Offer particular acreage they would like to see included in the forthcoming Blocks Offer and that the Crown will consider including such acreage in the next Blocks Offer. The Association generally supports the MED adopting a proactive approach in this regard with a view to ensuring that the Blocks Offer process is a meaningful one for industry and accommodates the commercial and practical drivers facing industry. The Association would also expect that any such acreage identified by a company would, in fact, be included in the

next available Blocks Offer unless there was a very clear and compelling reason why it should not be. In addition, the Association would expect that where any acreage is identified by an operator, the fact or existence of that identification would remain confidential to the MED due to its commercially sensitive nature.

NZPM resourcing

By way of a concluding comment, the Association would like to reiterate its support for an expanded Blocks Offer process. However, the Association cautions that such an expanded process will involve a very significant commitment of resources by NZPM. The Association believes it is crucial for the continued successful development of New Zealand's petroleum sector that:

1. NZPM has available to it, and devotes, sufficient personnel and other resources to ensure the efficient, transparent and successful conduct of each and every Blocks Offer; and
2. Just as importantly, there are sufficient other resources available for NZPM to be able to timely execute its other permit governance and management activities (i.e., there must be sufficient resources available so that day-to-day operational and management requirements are not compromised or "put on the back burner").

We are aware this is a key focus for NZPM, but believe this is a crucial consideration going forward as failure to deliver in relation to either aspect above could seriously and adversely affect New Zealand's attractiveness as a destination for international petroleum investment.

Consultation

Given the fundamental significance of the proposed changes to the permit allocation methodology proposed in (and contemplated by) the 30 August 2011 notice, the Association respectfully requests the opportunity to meet with MED representatives to further discuss the proposal set out above before any changes are made to the MPP. In particular, the Association is very concerned to ensure that any such changes are fully considered as an integrated whole and address both the removal of PITs but also changes required to the MPP to accommodate the successful implantation of the expanded Blocks Offer process contemplated by the notice.

Yours sincerely

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