
1 What is this study about?

Key points

- In response to a request from the Australian Government, this study was undertaken to review Australia's regulatory framework for upstream petroleum activities.
 - Its objective is to identify ways to improve the regulatory arrangements and reduce unnecessary regulatory burdens on the upstream petroleum sector.
- This study is concerned with the regulation of conventional upstream petroleum projects that involve more than one jurisdiction.
 - The terms of reference exclude downstream activities, as well as coal seam methane and other mineral resource projects.
- This study focuses on burdens that may arise from deviation from best practice regulation, or from poor administration of regulatory arrangements.
 - Such burdens can result in delays and uncertainties in obtaining approvals, duplication of compliance requirements and inconsistent administration of regulatory processes, particularly affecting cross-jurisdictional projects.

On 10 April 2008, the Assistant Treasurer asked the Productivity Commission (the Commission) to undertake a research study of regulatory burdens on the upstream petroleum (oil and gas) sector. The Commission was given 12 months to prepare and submit a report for consideration by all Australian governments. The terms of reference are reproduced at the front of this report.

1.1 Background to this study

On 12 October 2005, the Prime Minister appointed a Taskforce on Reducing the Regulatory Burdens on Business (the Regulation Taskforce) to identify options to reduce the compliance burden on business from government regulation. The report of the Regulation Taskforce (2006) stressed the importance of continual reform to reduce regulatory burdens on business and the community. Since the release of this report, the Australian Government has focused its regulatory reform initiatives on addressing excessive, inconsistent or duplicative regulation. As part of this process, the Commission has been asked to conduct a series of reviews of burdens stemming from the regulatory requirements of the Australian Government.

In 2007, the Commission undertook a review of regulatory burdens on business in the primary sector, including upstream petroleum. In response to this review, the Australian Petroleum Production and Exploration Association indicated that significant burdens have resulted from delays and uncertainties in obtaining approvals, duplication of compliance requirements, and inconsistent administration of regulatory processes across jurisdictions. The burdens were claimed to be particularly large for cross-jurisdictional projects (APPEA 2007b, 2007c).

The Commission concluded that there was scope for improving the regulation of upstream petroleum activities, but that this required an examination of the totality of regulation, not just that of the Australian Government (PC 2007a). Consequently, the Commission recommended a broad review of the whole Australian onshore and offshore petroleum regulatory framework.

Governments in Australia have taken some steps to harmonise relevant legislation and streamline administrative arrangements governing upstream petroleum operations. However, COAG has recognised that there is scope for further improvement in this area.

In its meeting on 26 March 2008, COAG agreed to a far-reaching regulatory reform agenda, with the upstream petroleum sector identified as one of the numerous ‘hotspots’ where overlapping and inconsistent regulation threatens to impede economic activity (box 1.1). The present study was commissioned to assist Australian governments to identify ways of improving the regulation of upstream petroleum activities and reducing regulatory burdens on the upstream petroleum sector.

1.2 What the Commission has been asked to do

The Commission has been asked to review Australia’s framework for regulating upstream petroleum activities, and consider opportunities to streamline regulatory approvals, provide clear timeframes and remove duplication between jurisdictions. Specifically, the terms of reference require the Commission to:

- assess the impact of the current regulatory framework on the international competitiveness and economic performance of Australia’s petroleum sector and on the performance of the economy as a whole
- report on regulatory impediments to improved performance, including inconsistencies and duplication across jurisdictions, and ways in which governments in Australia could address them

Box 1.1 **COAG's regulatory reform agenda**

In February 2006, COAG launched a National Reform Agenda that included a stream of reform commitments aimed at reducing regulatory burdens on business and the community. Ten areas were originally identified for reform, namely: rail safety; occupational health and safety; trade measurement; chemicals and plastics; development assessment arrangements; building regulation; business regulation; environmental assessment and approval; personal property security; and product safety.

In December 2007, COAG established the Business Regulation and Competition Working Group to devise strategies and implementation plans for accelerating and broadening the regulation reduction agenda. The Working Group proposed to include 27 areas in an expanded reform agenda, which COAG subsequently endorsed at its 26 March 2008 meeting. These reform areas were prioritised as follows:

- Top priority — occupational health and safety.
- Requiring early action — environmental assessment and approval bilaterals; payroll tax administration; trade licences; Health Workforce Intergovernmental Agreement; national trade measurement; rail safety; consumer policy framework; product safety; trustee companies; mortgage credit and advice; margin lending; and non-deposit taking institutions.
- Accelerating progress — development assessment; building regulation; chemicals and plastics; Australian Business Number and business name registration; and personal property security.
- New reforms — standard business reporting; food regulation; mine safety; electronic conveyancing; upstream petroleum (oil and gas); maritime safety; wine labelling; directors' liabilities; and financial service delivery.

Sources: COAG (2008); PC (2006a).

- consider options for a national regulatory authority (for example, along the lines of the National Offshore Petroleum Safety Authority) to manage all regulatory approvals for the upstream petroleum sector as a means of addressing issues of regulatory duplication and inconsistencies.

Under the terms of reference, the Commission is required to have regard to:

- any other current or recent reviews commissioned by Australian governments affecting the regulatory burden faced by businesses in the upstream petroleum sector
- the underlying policy intent of government regulation on the upstream petroleum sector.

In addition, the *Productivity Commission Act 1998* (Cwlth) underpins broad policy guidelines to which the Commission must have regard in conducting this study. Those guidelines oblige the Commission to, among other things, adopt a community-wide perspective, promote reducing unnecessary regulation, encourage the development of efficient and internationally competitive Australian industries, and ensure that Australian industry develops in an ecologically sustainable way.

1.3 Scope of the study

This study is concerned with all forms of regulation governing conventional upstream petroleum projects that involve more than one jurisdiction (excluding coal seam methane and other mineral resource projects). Emphasis has been placed on regulatory arrangements that are potentially inconsistent and duplicative, or create burdens in their own right.

What *regulation* is within scope?

A broad definition of ‘regulation’ is adopted in this study, referring to any laws, government policies and rules that are intended to control or influence specific aspects of the regulated activity. Such regulation encompasses a range of legal instruments including statutes, subordinate legislation (regulations) and ministerial orders, as well as less formal instruments such as standards, guidelines and codes of conduct for which there is a reasonable expectation of compliance on the part of business (box 1.2).

Moreover, regulation can be implemented by contractual agreements between businesses and governments that provide the basis for governing business conduct. Under this approach, contract terms are negotiated with governments — possibly involving community stakeholders — on a facility- or project-specific basis. Such negotiated agreements are legally binding although they may or may not be codified into law.

What *activities* are within scope?

The Australian upstream petroleum sector produces a range of products including crude oil, condensate, natural gas, liquefied natural gas (LNG) and liquefied petroleum gas. The terms of reference explicitly exclude coal seam methane projects and other mineral resource projects such as oil shale extraction.

Box 1.2 **Business regulation in various forms**

Formal regulation involves governments exerting control or influence over business conduct through legal requirements, monitoring or inspection programs and, in the case of non-compliance, punitive sanctions. This form of regulation is generally based on:

- primary legislation — which consists of Acts of Parliament that set out the regulation-making authority
- subordinate legislation — which comprises laws and rules made by authorities under the delegated powers of the legislature to spell out details of policy decisions embodied in primary legislation, as exemplified by statutory rules, ordinances, by-laws, and disallowable instruments
- administrative decisions or discretions — which are requirements imposed by public officials entrusted with the relevant powers and duties
- international treaties and agreements — which can be ratified with legislative backing.

Apart from formal regulation, governments can influence business conduct by means of *quasi-regulation*. This encompasses policies, rules, standards and other instruments that do not have the force of law but effectively impose compliance requirements on business through government involvement in their development. Examples include government-endorsed industry codes of practice, government-issued guidance notes, government–industry agreements, and national accreditation schemes. Quasi-regulation is also implicit in licensing and government procurement requirements.

Further, business conduct can be subject to *co-regulation*. This involves industry and other non-government stakeholders jointly developing and administering particular codes, standards or rules, with government providing legislative support for the enforcement of those arrangements.

Sources: Banks (2001); Commonwealth of Australia (1997); OECD (2003).

In line with the terms of reference, the study has been confined to the upstream activities of the oil and gas supply chain — namely, exploration, development and production. These are distinguished from downstream activities associated with the refining, distribution, wholesaling and retailing of petroleum products.

Specifically, the delineation of upstream activities extends from the exploration for hydrocarbon deposits to the production and on-site storage of marketable crude petroleum commodities. In the upstream production stage, crude oil, condensate or gas is delivered from the wellhead, typically by pipeline, to a processing plant for primary purification or processing. These processes remove unwanted chemical compounds, making the petroleum products suitable for shipment to a refinery.

They sometimes take place on a floating export terminal for offshore projects. In the case of LNG, the upstream stage is taken to include the LNG purification and liquification trains and all activities up to the export terminal for LNG.

The regulation of a range of onshore and offshore project activities is examined in this study. A project can involve the development of a new single hydrocarbon reservoir or field, or an incremental development of an existing producing field. The integrated development of a group of several fields and associated facilities also constitutes a project (World Petroleum Council 2008). Regulated project activities include conducting exploration and seismic surveys, drilling wells (both for exploration and later for production), laying pipelines, constructing oil and gas extraction equipment and subsequent processing equipment, operating transport and storage facilities, and eventually decommissioning end-of-life installations.

For the purpose of this study, there are four classes of jurisdiction which are relevant — namely: (i) local governments; (ii) State and Territory Governments; (iii) the Australian Government; and (iv) the Joint Petroleum Development Area established under the 2002 Timor Sea Treaty between the Australian Government and the Government of East Timor. Accordingly, the Commission has considered a range of circumstances in which a project could be identified as cross-jurisdictional. These include, but are not limited to, cases where a project:

- crosses from Commonwealth waters into a State or Territory area (including coastal waters) such as in building a pipeline to bring gas onshore
- takes place wholly within a State or Territory but is subject to regulation by different levels of government, which could include federal, state or local government
- is subject to legislation jointly administered by agencies or departments at different levels of government
- crosses from the Joint Petroleum Development Area into Commonwealth waters.

1.4 Approach of the study

The Commission has reviewed the regulatory framework by considering the questions of whether it is achieving policy objectives and whether the resulting burdens are the minimum necessary to achieve those objectives. Where it is clearly articulated, the Commission has taken the underlying policy intent as given and, on that basis, sought to identify and distinguish between:

- the extent to which particular policy objectives explain the significance of regulatory burdens — that is, the policy creates a burden in its own right

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- the extent to which particular policy objectives might be attained with a reduction in burden through improving the design and/or administration of regulation.

In some instances, however, the Commission has commented on the lack of clarity regarding the underlying policy intent of regulation. Lack of clarity in this respect creates uncertainty and, sometimes, inconsistency as different regulators put their own interpretations on what the policy is intended to achieve. All these contribute to unnecessary regulatory burdens.

In line with the broad definition of regulation outlined earlier, the regulatory framework has been reviewed as a collection of:

- policies
- laws and rules
- incentives
- decision-making processes
- licensing conditions
- compliance mechanisms
- administrative procedures
- institutional arrangements.

The Commission has drawn on broad principles of best practice regulation and governance when assessing the regulatory framework. Best practice regulation depends on rules and laws that have clear objectives, and are well designed, properly administered and duly enforced. Moreover, it requires the support of robust and adequate governance arrangements — a set of institutions, processes and systems by which policy decisions are made, roles and responsibilities are assigned, regulatory tasks and functions are carried out, and the relationships of authorities within and between jurisdictions are organised.

In addition, the Commission has examined the regulatory frameworks governing petroleum resource development in a selection of overseas countries. Identifying key similarities and differences in the form and content of regulation from an international perspective has been aimed at shedding light on the scope and focus of reforms that might bring improvement to the Australian regime.

The Commission has examined both the practice of regulators and the reaction of businesses to the regulation of project activities. To this end, empirical and anecdotal evidence has been obtained from meetings with petroleum companies, industry bodies, government departments and regulatory agencies.

Particular attention has been paid to how regulators act on and interpret their regulatory mandates. This behavioural aspect is important because any rule or law has an impact on business that is influenced by the way the regulators choose to interpret and apply that regulation.

The Commission also recognises the importance of appropriate resourcing to the organisational and administrative efficiency of regulation. Difficulties in attracting and retaining appropriately skilled and experienced staff to carry out regulatory functions has been frequently cited by participants in this study.

The Commission, in its issues paper, called for credible evidence and quantification of unnecessary regulatory costs borne by the upstream petroleum sector. Some participants provided information on burdens and associated costs, although the evidence presented was largely anecdotal or qualitative in nature with limited empirical data on burden indicators or costs. This qualitative information helped identify particular priorities and reveal the complexity of certain regulatory challenges.

1.5 The conduct of this study

On receipt of the terms of reference on 10 April 2008, the Commission advertised in major newspapers and issued a circular announcing the study to interested parties.

The Commission held informal discussions in Adelaide, Brisbane, Canberra, Darwin, Karratha, Melbourne and Perth with various interested parties, including representatives from petroleum companies, industry associations, government departments and regulatory agencies, as well as researchers with expertise in the regulation of petroleum projects.

In July 2008, the Commission released an issues paper to assist those preparing submissions. A total of 20 submissions were received in response to the issues paper. A draft report was released in December 2008, to enable participants to provide comments on the Commission's preliminary analysis through a further round of public submissions. Following the release of the draft report, a further 15 submissions were received.

In October 2008 the Commission held two roundtables, in Canberra and Perth, to elicit views on key issues relevant to the Commission's study. Further roundtables were held in February 2009, in Melbourne and Perth, following the release of the draft report.

All individuals and organisations consulted, roundtable attendees, and submissions received are listed in appendix A.

1.6 Report structure

The structure and economic significance of the upstream petroleum sector in Australia is described in chapter 2. Chapter 3 discusses the rationales for regulating upstream petroleum activities, as well as the general causes and implications of unnecessary regulatory burdens. Chapter 4 provides an overview of the regulatory framework, including its historical background, existing legislative and institutional arrangements, and recent and current reviews of those arrangements.

The next few chapters are devoted to detailed discussion of regulatory arrangements and issues in specific areas: resource management and land access (chapter 5); environmental and heritage protection (chapter 6); and occupational health and safety (chapter 7). This is followed by an empirical assessment of unnecessary regulatory burdens in chapter 8. Models for a national regulator are examined in chapter 9. Finally, the way forward on future regulatory arrangements is presented in chapter 10.