
C International comparisons

The Commission has drawn on several external studies to examine structural and circumstantial influences on regulatory performance from an international perspective. Two issues of regulatory structure are identified as particularly relevant to this study, namely:

- the legal nature of the state–business relationship — specifically, the choice between rule-based and negotiation-based regulation (section C.1)
- the constitutional constraints that a federation places on designing a cooperative multi-jurisdictional regulatory framework (section C.2).

C.1 Introducing flexibility with negotiation-based regulation

The legal framework governing upstream petroleum activities can have crucial implications for the level of regulatory burden faced by project proponents. In particular, the question arises as to whether such framework should be defined by general legislation or based on *ad hoc* agreements between governments and individual businesses.

According to Hossain (1979), the regulation of petroleum projects in different countries falls broadly under three systems, namely:

- a sector-specific legislative system — with legislation predetermining conditions under which the rights to explore for and exploit petroleum resources are granted by means of standard licences or leases, including royalty taxes and other payments to be made by licensees or lessees
- a negotiation-based system — with the government granting the rights to explore for and exploit petroleum resources on the basis of individually negotiated agreements with petroleum businesses in the absence of comprehensive petroleum legislation
- a hybrid system — with general legislation setting out certain provisions and minimum standards or conditions for the grant of rights to explore for and exploit petroleum resources, but also providing for certain important matters to be settled by negotiation between government and individual businesses.

Australia primarily depends on a sector-specific legislative system for regulating upstream petroleum activities. In a few cases, contractual agreements have been negotiated and subsequently codified into legislation. Some others are based on ‘major project’ provisions of the legislation. Canada and the United States adopt a similar legal system.

Petroleum concessions were typically negotiated between host governments and multinational businesses in traditional petroleum provinces such as Saudi Arabia and some other Middle East countries. More recent examples include Indonesia and Papua New Guinea, where petroleum legislation lays down broad principles for contracting businesses in the private sector to develop petroleum resources, while leaving detailed terms and conditions to be determined through contract negotiation (Asmus 2000; Yalapan 2003).

The Netherlands, New Zealand, Norway and the United Kingdom are among the countries that have adopted a hybrid system to regulate upstream petroleum activities. Typically, these countries have legislation governing petroleum development activities that contains provisions enabling governments to negotiate with petroleum businesses on crucial contractual matters. For example, Norway’s regulatory framework is outlined in box C.1.

A key advantage of a sector-specific legislative approach (from a government’s perspective) is that the terms (including fiscal terms) can be varied by subsequent legislative changes. This helps avoid the situation where an individually negotiated agreement ‘freezes’ contract terms over the project life, without any legal recourse to enable adjustment to changing market conditions.

Another advantage of the legislative approach is that it allows policy objectives to be incorporated into the legal framework. Setting out overarching policy strategies for petroleum development in legislation can provide guidance on the design and administration of regulatory arrangements.

Further, minimum standards and basic conditions for the grant of rights of resource exploration and extraction can be laid down in legislation. This helps promote transparency and accountability in the administration of the regulatory regime. To leave such licensing standards and conditions to administrative discretion or negotiation could expose the regulatory agency concerned to undue pressure exerted by petroleum businesses individually or collectively.

On the other hand, to include excessive project details into legislation could lead to a lack of contracting flexibility. Moreover, including detailed rules into legislation can add to compliance obligations.

Box C.1 The Norwegian regulatory framework

The Norwegian petroleum resource management regime is characterised by the use of principle-based legislation, as currently reflected in the *Petroleum Activities Act 1996* (Norway). This law sets out framework conditions to guide the formulation of acceptable commercial incentives in concession contracts granted to private businesses for undertaking exploration and extraction.

Among the matters prescribed by the legislation are the initial duration of an exploration licence (3 years) and a production licence (10 years), as well as the mandatory obligation for project proponents to submit field development plans for approval by authorities before extraction activities can commence. The legislation also prescribes that '[t]he King may decide that the Norwegian State shall participate in petroleum activities' (*Petroleum Activities Act 1996* (Norway), s. 3.6).

A number of critical matters are determined by mutual agreement of the parties concerned, which often requires intensive negotiations. These matters include the size of the exploration program and the extent of state participation in the project. In effect, state participation involves negotiating a joint-venture agreement covering a number of contractual issues such as the percentage of equity to be held by each party, the management structure and control of operations, and the conditions under which the obligation to invest in resource development would increase.

Despite its contractual basis of regulation, the Norwegian petroleum regime includes mechanisms that enhance transparency through a set of criteria for reporting on concession terms and project incomes. For example, there is public information on the tax payments from individual businesses operating in the Norwegian continental shelf. Further, model contract terms are accessible to the public.

Sources: Hossain (1979); Norwegian Ministry of Foreign Affairs (2006); Tina Hunter (sub. 9).

Hossain (1979) suggested that the most effective way to introduce contractual flexibility would be to leave room for negotiation on matters for which some variation could be expected. Variation could stem from differences in location or other geological and geophysical features of petroleum projects. Consequently, this approach underpins a key advantage of the hybrid system.

Onorato (1995), while serving as the World Bank's principal advisor on petroleum development matters, suggested that best practice regulation in this area should involve integrating the legal, contractual and fiscal arrangements into a self-contained legislative framework. Further, Onorato argued that such an integral framework would give both the host government and the petroleum business a clear legal and contractual basis on which to negotiate mutually advantageous arrangements for developing petroleum resources. Under this approach, the regulatory framework comprises broad, and not overly detailed, petroleum law

complemented by enabling regulations and one or several variants of a model contract (box C.2).

According to a study by Daintith (2005), the Australian regulatory regime for upstream petroleum activities involves administrative rules embedded in legislation. The regime operates by prohibiting certain activities and then granting businesses the administrative authority to carry out operations under the relevant regulatory provisions.

In almost all other concession systems worldwide, the state concludes a contract with the business within a regulated environment on the basis of the state's complete sovereign rights to the petroleum resources (Daintith 2005). In the United Kingdom, for example, the state–business relationship is wholly expressed in a contractual form.

Box C.2 An effective legislative framework for petroleum development

According to World Bank practices of legal reform in the petroleum sector, an effective legislative framework for attracting investment should be comprised of a generic petroleum legislation, a set of subsidiary regulations, and a model contract.

The petroleum legislation would assert the state's property rights to petroleum resources. It would also identify an agency to be vested with the exclusive mandate to implement government policies for developing petroleum resources within its jurisdiction. This agency would represent the state in negotiating and contracting with investors, and subsequently in regulating and administering contract compliance activities.

To maintain its generic property, the petroleum legislation should be couched in terms of minimal permissive contents of a model contract — without including excessively detailed legal provisions. For example, the recommended practice in respect of environmental protection and safety is to include a comprehensive obligation for these policy goals in the petroleum legislation, and then to detail specific actions and requirements in the subsidiary regulations and the contract.

For regulating petroleum projects, a self-contained and coherent legislative framework is considered more appropriate than piecing together legislative provisions in both the petroleum legislation and other related and relevant laws such as those on taxation, land use and environmental protection. Accordingly, Onorato concluded that it is inadvisable to make petroleum operations subject to broad, general environmental protection law, except to the extent that the principles of law are applicable to specific practices of the petroleum sector.

Source: Onorato (1995).

In the 1960s, Australian governments avoided using a concession system to regulate oil and gas exploration and extraction, in part to avoid conflict between the

Commonwealth and States and Territories over resource rights (Daintith 2005). Australian governments maintained a non-contractual basis of petroleum laws even after the resource rights issue was resolved through the Offshore Constitutional Settlement in the late 1970s.

Tina Hunter argued that the history of Australia's offshore petroleum legislation produced 'a combination of painstaking detail and grand scale delegation' (sub. 9, p. 20). Daintith (2005) found the system of petroleum titles under the *Petroleum (Submerged Lands) Act 1967* (Cwlth), and the detailed rules surrounding them, limited the flexibility of Australia's petroleum regime to adjust to different or changing circumstances.

The Australian regime has been described as involving broad delegation of regulatory powers to government departments or agencies (Daintith 2005). These authorities are given appreciable discretionary powers, particularly in interpreting and determining regulatory requirements, although these administrative powers are sometimes exercised through the issuance of regulatory guidelines that confine the decision making of the authorities.

C.2 A cooperative multi-jurisdictional framework

Evans and Bailey (1997) found that the Australian offshore regime appeared to be effective in averting the potential conflicts of interest between jurisdictions. This was in contrast with the US framework, which is based on the traditional three-mile separation offshore of the state from federal authority. In the United States, the administration of the petroleum regime is largely entrusted to the Secretary of the Interior, with no delegation to state authorities and limited scope for federal–state joint decision making (Daintith 2005).

On the US west coast, for example, the tension between governments pursuing differing, or even conflicting, policy goals within their respective coastal zones was noted to have 'broken down' the offshore oil leasing program (the US petroleum acreage allocation process) (Evans and Bailey 1997). Such a problem reflects the asymmetric distribution of costs and benefits involved in developing petroleum resources — that is, the beneficial aspects of offshore development accrue mainly to the federal government as resource-driven revenues, whereas the costs of onshore infrastructure, environmental damage and disruption of lifestyle are incurred at a more localised level.

Evans and Bailey (1997) suggested that two factors contribute to the relative effectiveness of the Australian regime. First, the use of mirror legislation in different jurisdictions provides legal consistency and continuity, enabling

compatible resource titles to be granted for all offshore areas. Second, the joint decision-making structure promotes cooperative governance of offshore petroleum activities, allowing the Australian Government and the State and Territory Governments to set consistent policies for the development of petroleum resources in offshore areas.

Hunt (1990), after comparing the petroleum regimes of Australia and Canada, concluded that Australia's Offshore Constitutional Settlement has worked well in resolving the competing jurisdictional claims over offshore petroleum resources of the two levels of government (box C.3). Nevertheless, it was noted that common petroleum codes could be 'more an illusion than reality' in Australia because the *Coastal Waters (State Powers) Act 1980* (Cwlth) allows each State to alter its petroleum laws in its coastal waters without having to seek the agreement of other governments. Consequently, a lack of uniformity in petroleum laws could complicate the regulation of projects in cross-jurisdictional areas (chapter 5).

Box C.3 Comparing the Australian and Canadian petroleum regimes

The Australian and Canadian petroleum regimes are both characterised by federal–state (province) involvement in decision making about the development of petroleum resources in offshore areas. Nevertheless, they have some notable differences.

Australia has a multilateral inter-jurisdictional system covering all water areas adjacent to the States and the Northern Territory. By contrast, Canada has a bilateral system. This is represented by the 1985 Atlantic Accord and the 1986 Resources Accord signed between the Canadian Government and, respectively, the provinces of Newfoundland and Nova Scotia.

Further, unlike Australia's Offshore Constitutional Settlement, the Canadian Accords do not differentiate between the territorial sea and the continental shelf. For areas where no intergovernmental management arrangements have been agreed to, the Canadian Government has jurisdiction over the regulation of petroleum development.

Australia's regime has the advantage of a single Commonwealth statute governing the entire continental shelf. Yet, it also has the potential disadvantage of different State statutes governing the territorial seas.

Sources: Brownsey (2007); Hunt (1990).

The Australian regime, notwithstanding its strengths as discussed above, was viewed by Evans and Bailey (1997) as having a narrow focus on resource management, while giving less consideration to environmental issues. It is primarily based on the mandate for governments to manage the economic relationship between the jurisdiction (as resource owner) and the project proponent (as the entity entrusted with the development of petroleum resources), although this mandate also

includes broader responsibilities of government such as environmental protection and public safety. Reflecting this, there is scope for governments to pursue differing environmental policies within their own jurisdictions (chapters 4 and 6). This has led to different approaches to environmental regulation across Australia.

The absence of fully cooperative marine protection policy at different levels of government is not unique to Australia but also applies to other federations such as Canada (Bowal 2003). This is in large part because environmental protection law has been a relatively recent initiative. As a consequence, the legal jurisdiction over such issues has been interpreted and declared from a constitutional structure that did not foresee the natural environment as a discrete subject for regulation. In practice, the diverse nature of environmental protection renders it difficult to assign all relevant regulatory responsibilities to one level of government.