Tenure Matters

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A column by Sue Slater, Senior Advisor Petroleum, RLMS

Welcome back. This month the topic for discussion is Land Banking or Retention – What's the difference?

There is a significant level of concern in Government around the issue of "land banking". Certainly this is not a new concern. As far back as 2002, the Council of Australian Governments Energy Market Review (COAG) frequently cited as the Parer Review, recommended that acreage management regimes in each State include the promotion of competition as a criteria for awarding exploration acreage. However, following on from recommendations in numerous more recent reports, including the MACE Report (Ministerial Advisory Committee on Exploration) released in June 2014, there seems to be a broader and more urgent desire to address the issue.

But is land banking the issue Government believes it to be? Certainly since the new petroleum legislation commenced in 2004, relinquishments have been mandatory for exploration permits every 4 years. Opportunities for land banking are therefore limited. This requirement was introduced into the 2004 Act to encourage the turnover of land. Under the 1923 Act, although relinquishment was a requirement, it was able to be waived in return for an increase in the work and/or expenditure. This recognises, albeit covertly, that the important issue is whether work is happening on the ground. If work continues to be performed, what benefit arises from the turnover of the land? The process of putting the area to bid, assessing the applications, awarding the preferred tenderer, acquisition of required Environmental Authority and perhaps Native Title, and eventual grant has, since the commencement of the 2004 Act, rarely taken less than 2 to 3 years, and often significantly longer. In this time, no work occurs on those areas.

Clearly the Government has a financial interest in creating new exploration permits, since it means additional application fees, possibly with cash bidding components. But exploration effort should be about extending the geological knowledge of the State, not increasing the cash coffers. The value-add to the Government from exploration is the increased level of geological understanding as much as it is about successfully progressing a resource to production. The former happens even when

exploration is unsuccessful; and even then the results may inform later exploration efforts and ultimately lead to successful projects. So the explorer that continues to actively explore an area should be rewarded.

A regime with fixed terms (12 years) and mandatory relinquishment (1/3 every 4 years) such as the one currently in place for petroleum, must have a system where land can be retained if value has been demonstrated, but cannot yet be realised. In the 2004 Act this was supposed to be the Potential Commercial Area (PCA), but although some ground has been made lately with respect to decreasing the number of applications (much of the decrease resulting from withdrawal by companies, but some by grants – which now total 12 declaration made out of 6 individual ATPs), the PCA concept cannot be termed a raging success. Reluctance to declare the areas, although admittedly sometimes working in the applicants favour, would appear to largely be related to perceptions around land banking issues with the implication that exploration effort would not continue. In reality though the PCA concept was merely a formalisation of the variations that used to be allowed under the 1923 Act, where relinquishment could be waived with a commitment to an increased work program (or evaluation program as it is now known in the 2004 Act with respect to PCAs).

The need for some form of retention method is greater when the area being explored is more remote. History has shown us that where pipeline infrastructure already exists, exploration efforts will be drawn to nearby areas, since the commercialisation of any discovery is likely to be easier. For large areas of the State however, there is no existing pipeline infrastructure, and any gas resource identified is likely to remain stranded for some time. The idea of a critical mass of exploration success to substantiate development comes into play in these areas. This critical mass might be held by a single proponent, or it might involve multiple proponents. Exploration success in one permit is likely to lead to more focussed efforts in areas that are either adjacent, or seen to be geologically similar, but until enough of the resource is identified, the development of infrastructure may not be commercially viable. In these cases, should early success be penalised by an inability to retain the area?

Explorers willing to take risks should be rewarded by the tenure system. Governments need to recognise that early success, particularly in remote areas, will require a mechanism to retain the areas and protect the investments already made. Turning over land in these situations is counter-productive. Turnover of land should be a priority only where no exploration effort is being made, or no resources have been established. Otherwise the priority should be that actual exploration activity continues. The success of turning over land will also depend on the economic cycle – in a boom, the chances of another company wanting to take their chance on a high risk area will be good; but in a bust there will likely be less interest in anything not considered highly prospective.

The notion that progression from exploration through appraisal to development can always fit neatly into a 12 year term does not recognise the commercial realities of our industry. Many outside influences can affect the time it takes to move through the exploration to development cycle, and the tenure system needs to be flexible enough to accommodate this. Moving from discovery to project finalisation is a complex process, with many interacting components.

A recent article in Energy News Premium on 10 July 2014, interviewed Grant King from Origin Energy, in which he made the following statements (in relation to activity on the North West Shelf, but relevant much more widely):

"The particular puzzle we were facing was that if we were to seek to explore into the North West Shelf, it would really take us a very long time and be a very expensive exercise for us."

"Just by way of benchmarking that, these Poseidon permits were first awarded … in 2001, so it's 11 or 12 years to discovery and still some years before any FID decisions we'd make… it takes a very, very, very long time to explore one's way into earnings and cash flow."

"Not only does it take a very long time, but it involves risking a very significant amount of money".

Increasingly grass roots or frontier exploration is falling to smaller players, at least in the onshore environment. Many large companies are choosing to buy into other companies discoveries rather than undertake exploration themselves, and this should by itself be seen as an indication of the inherent risk and cost of exploration. The importance of small players in new discoveries should not be underestimated; they are often the ones that make the game-changing moves. Queensland would not have the current crop of CSG to LNG projects if the then small Queensland Gas Company had not believed that CSG production was possible from the Walloon Coal Measures.

Currently there is an enormous impetus within the Government to modify, or perhaps even radically change, the current tenure regime. If we want to end up with a system that reflects the realities of our industry, and simplifies regulation, then it is incumbent upon all of us to participate in consultation when the time comes.

Thanks to those of you who have provided some feedback and suggestions, I will try to cover the topics suggested over the coming months. I am happy to hear suggestions about topics you would like covered. Feel free to email me at sue.slater@rlms.com.au with the subject heading Tenure Matters.

In the meantime, remember "Tenures make the Project; the Project doesn't make the Tenures".

Level 14, 10 Eagle St
BRISBANE QLD 4000
P. +61 7 3229 8472
E. rlms@rlms.com.au

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