FUTURE PATTERNS OF LEGISLATION FOR THE PETROLEUM INDUSTRY

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INTRODUCTION

In this paper it is proposed first to summarise the known provisions of the proposed offshore petroleum legislation. Then I will outline the amendments now proposed to present on-shore legislation. Finally, in the light of the legislation now contemplated, I will endeavour to forecast what will be the trend of future petroleum legislation.

OFFSHORE LEGISLATION

In April 1964 it was agreed at a meeting of Federal and State Ministers that the constitutional questions of jurisdiction over the petroleum resources of the sea-bed be settled by joint arrangements between the Commonwealth and the States.

A year or so later an agreement on a uniform code covering offshore petroleum exploration and exploitation was considered at a joint meeting of State and Commonwealth Attorneys-General.

This agreement was ratified in principle at the Premiers' Conference in Canberra during June 1965. Pursuant to this agreement it was decided that royalties payable on offshore production would be shared 50-50 by the Commonwealth and the States, but such fees as rentals would be retained by the States.

On 16th November, 1965 a joint statement of Commonwealth and State Ministers was tabled in the Federal Parliament by the Minister for National Development.[1]

The statement traced in brief outline the history of discussions between the Commonwealth Minister for National Development, the State Mines Ministers and the Commonwealth and State Attorneys-General which had extended over the previous two years or so.

The objectives of these discussions, it was stated, had been to work out a scheme that would give certainty of legal title to operators in offshore areas who undertake the substantial expenditures involved in offshore exploration and exploitation, and to enable constitutional issues to be put on one side so as to avoid constitutional litigation of the kind which had been going on in the United States for many years.

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[1] Commonwealth of Australia Parliamentary Debates, 25th Parliament, First Session 1965, House of Representatives, p. 2741.

It was further stated that the several Governments had mutually agreed that, without abating any of their constitutional claims, they should try to arrive at a concerted policy with common administration and with complete agreement between them as to what would happen. This, said the Ministers, had now been achieved.

The scheme agreed to by the Governments was to be effected by Commonwealth and State legislation in similar terms which would be presented to the several Parliaments pursuant to a formal agreement between the Commonwealth and States setting out details of the agreed arrangements.

The following is a brief outline of the contents of the legislation proposed in November 1965:

1. Provisions would be made for the application in offshore areas of the general body of law in force in the adjacent State or Territory.
2. There would be a code providing for a common set of principles to apply to all offshore petroleum operations anywhere around the Australian coast, but at the same time allowing sufficient flexibility to enable the peculiar problems offshore from any individual State or Territory to be met.
3. The administration of the legislation was to be in the hands of the States and Territories, but the States had agreed that the Commonwealth would be consulted on all aspects affecting the Commonwealth's own special constitutional responsibilities, e.g. defence and external affairs.
4. There would be a two-stage system — a permit to cover all stages of exploration including drilling, and a licence to cover production.
5. The permit would be issued initially for a period of up to 10 years or if issued initially for a lesser period could be extended to a total life of 10 years. If its duration exceeded 2 years, either by way of grant or extension, such duration would be divided into successive specific periods and there would be provisions for reduction of the areas of the permit at the end of such periods.

   This, said the Ministers, was to encourage companies to concentrate their efforts on the most prospective areas which they discovered but not at the same time to hold large offshore areas which were not being effectively explored.

   The company holding permits would be required to carry out exploration work in accordance with programmes approved by the State Ministers or the appropriate authorities in the Commonwealth Territories.

   Other provisions requiring operations to be carried out in such manner as would not interfere unjustifiably with navigation or

fishing or with the conservation of the living resources of the sea and the sea-bed, with underwater cables or pipelines, or with mining operations for minerals other than petroleum would also be included.

Annual rentals at the rate of 20 cents per square mile but not exceeding the sum of $2,000 for any permit area would be payable to the States or Territories. Rentals would be kept by the States.

Other provisions dealing with such matters as safety procedures, submission of reports, provisions for voluntary relinquishment and for cancellation would be also included.

6. Turning to the question of production licences, the statement went on:

"In the event of a permittee discovering payable petroleum he will have a preferential right to a licence for production. Licences will issue for periods of 21 years, with the licensee having the right of extension, providing he has satisfactorily carried out the conditions and covenants of his licence, for a further period of 21 years. During the first 21 years royalty will be payable at the rate of 10 per cent. of value of production at the well head. The second 21 years will be divided into three seven-year periods, during each of which the royalty may be varied by agreement between the several Governments. Further extensions of the licence may be granted. The effect of this is that an operator is assured, providing he carries out his side of the bargain, of holding his licence area for at least 42 years and that during the first half of this the royalty rate will be fixed on a 50-50 basis between the Commonwealth and the adjacent State. The disposition of royalties in the case of the Territories will depend on the general financial relationships between the Commonwealth and the particular Territory concerned."

The statement then outlined the method by which areas of a production licence would be determined. There was to be established over offshore areas a graticular system of block areas, each of a size of five minutes of arc of latitude by five minutes of arc of longitude.

Following a discovery within a permit area the permittee would be asked to nominate a graticular block which would then become the centre of a group of nine graticular blocks to be known as a location. Each side of the location would be three blocks in length. From within the location of nine blocks a permittee would be entitled to select any four blocks and to be granted a production licence covering such blocks. He would have at least two years in

which to make his selection with possible extension to four years with the approval of the Minister or authority concerned.

Those five blocks not selected would be excised from the permit area and could be disposed of by the States or Territories by tender. However, the original permittee would have the right of first option over any such blocks at the top price offered by any other tenderer. Proceeds from the sales of these blocks would be retained by adjacent States or Territories. There would be no limit to the number of licences that could be granted to any one company.

7. The statement then went on to deal with the position of tenements already issued by the States or Territories. Provisions were to be made in the legislation relating to the confirmation of existing tenements for the unexpired period of their life and accordingly confirmatory permits could be issued temporarily with boundaries that did not confirm to the graticular system.

8. In conclusion, the Ministers emphasized that the proposed system had been designed to ensure security of title and tenure to offshore operators, to avoid costly and time consuming litigation, and to establish an effective and legally sound administrative regime supported co-operatively by the Commonwealth and the States.

The Petroleum Industry, however, did not agree that the legislation in fact ensured security of title and tenure to offshore operators, and on the 21st February, 1966 the Offshore Oil Industry Committee made representations in Canberra to officers representing all States and Territories and the Commonwealth Government.

Subsequently on 30th June, 1966 the State Ministers for Mines and the Acting Minister for National Development issued a joint press statement announcing certain modifications to the proposed offshore legislation.

Again, it was stated that the objective of the Commonwealth and States was to give certainty of legal title to operators in offshore areas.

They went on to say that, after careful consideration of the proposed legislation, the Ministers were confirmed in their view that it was a fair and reasonable code, compared favourably with overseas practices and established a reasonable balance between the public and the industry interest. However, they had agreed that some modifications could be made to the original scheme within its basic framework and principles which should go a long way to allaying the anxieties voiced by the Industry's representatives.

The modifications outlined in the statement are briefly as follows:

1. Permits to explore would be issued for an initial period of six years with rights of renewal for further successive periods each

of five years subject to satisfactory compliance with the conditions of the permit and to the permittee surrendering half of the permit area at the end of each period.

2. The maximum permit area would be 400 blocks giving a maximum permit size of approximately 10,000 square miles.
3. There would be no statutory limitation on the number of permits which could be granted to any individual company.
4. The royalty to apply to the second 21-year period of a licence would be fixed by the Parliaments at or before the time of granting a renewal, and the rates so determined would apply for the whole of the second period. In the absence of Parliamentary action to fix a new rate the 10% rate would continue to apply.
5. The holder of an exploration permit would be allowed to retain five out of the nine graticular blocks with four reverting to the Crown for auction to the highest bidder subject to the permittee's right of first option.

Industry still objected to some provisions of the proposed legislation and on the 25th August, 1966 submissions were made in Canberra to Senior Cabinet Ministers and Heads of Departments.

The submissions made may be summarised as follows:

1. In view of the cost and time required in offshore drilling (as compared with on-shore drilling) to evaluate a permit area, the compulsory relinquishment of 50% of the permit area at the end of six years was unduly restrictive.
2. The proposal that, on discovery, an explorer should be bound to select a location of nine blocks and within two to four years to relinquish to the Crown four of the blocks in the location was objectionable for the following reasons:
   (a) The search for oil was a hazardous and highly speculative undertaking. The explorers needed to have "know-how", modern technical resources and facilities and substantial risk capital available.
   (b) The amount of risk capital required for offshore drilling was not available from Australian sources except in association with overseas oil companies. The cost of drilling offshore was estimated at between $15,000 and $20,000 per day and substantial losses could occur where shutdowns are caused for long periods because of weather conditions.
3. In determining the desirability of possible oil exploration in another country, international oil companies invariably had regard to the following factors:

(a) *The Geological Factor.* The probable success ratio, the probable size of the fields and the depth at which oil was likely to be found.

(b) *The Geographical Factor.* The logistics of exploration and development in the country and the distance of discoveries from refineries and markets.

(c) *The Political Factor.* The support of the government and the attraction of its petroleum legislation.

(d) The stability of the country's economy.

It was further submitted that as the geological factor was still highly speculative in Australia and the geographical factor was marginal, oil exploration was less attractive in Australia than many other countries. On the other hand the political and economical factors were unusually favourable.

4. As there was little geological information available in respect of the Continental Shelf area (approximately 3 million square miles in extent), there was a pressing need for intensive exploration of the Continental Shelf. However, only the full reward from discovery could justify the high risk and cost of offshore exploration and drilling. The probable effect of the proposed legislation would be to concentrate exploration in regional areas where oil or gas had been found.

5. Forfeiture to the Crown of 44% of the discovery area or in lieu thereof, the payment to the Crown of an undetermined penalty sum on auction as a condition to the issue of his lease ran contrary to a fundamental principle long recognised in Australian mining legislation that the discoverer who paid his rent and royalty and fulfilled the conditions of his lease, was entitled to exploit the discovery for his own benefit.

6. In no oil producing country, to the Industry's knowledge, was there any offshore legislation providing for restrictive selection of the discovery area together with a relinquishment programme in the permit stage.

7. The auction system, while giving the Crown a temporary advantage by way of revenue, would divert to the Crown risk capital which would otherwise be expended in further exploration, disregarded the need for the expenditure of maximum available capital risk in exploration, so as to build up a viable and profitable producing industry from which royalty and taxes could be collected and was unfair to the discoverer and benefited a third party taking no risk.

8. Legislation in other countries where there were rich oil fields were not necessarily a guide for offshore legislation in Australia.

9. The proposed legislation ignored the need for encouragement of offshore exploration in a world situation where there was intense competition for limited offshore drilling equipment and available finance, and where more satisfactory titles could be obtained in much closer proximity to major markets.

Accordingly, Industry recommended:

1. That the Governments defer the proposed legislation until such time as the Oil and Gas Producing Industry became viable.
2. In the meantime discoverers should be entitled to exclusive production rights over the discovery area, and
3. A Committee be appointed to discuss the common problems relating to offshore exploration and production of oil and gas.

The Government representatives agreed to consider these submissions.

In January, 1967 a further meeting of State and Commonwealth Ministers was held in Adelaide. It was announced that it had been agreed by all Ministers that following a discovery an explorer would have the option of taking a production licence over five blocks at the standard royalty rate of 10%, or of taking all nine blocks on payment of an over-riding royalty on all nine blocks. In the latter event separate production licences would be granted over the five blocks and the four blocks respectively.

At a further joint meeting of State and Commonwealth Attorneys-General and Mines Ministers held in Sydney on 7th April, 1967 it was announced that the additional royalty to be payable by an explorer who took all nine blocks would be negotiated by the States between a floor of 1% and a ceiling of 2½%. These additional royalties would be retained in full by the States. In addition it was agreed that the basic 10% royalty (which previously was to be split on a 50-50 basis) would be split 60-40 between the States and the Commonwealth respectively.

The Ministers reiterated their previous view that the legislative scheme devised by them would result in the Governments being in a position to ensure that the interests of the nation were secure while allowing those who faced the commercial and financial risks involved in offshore exploration and production a proper chance to obtain reasonable returns for their enterprise.

In reply to a question asked of him in the House of Representatives on 12th April, 1967, Mr. Fairbairn stated that agreement had been reached at the April meeting in Sydney on all outstanding matters with the exception of two minor matters concerning the boundaries between some States.

He further stated that the Commonwealth Bill was "80% prepared"

and would be completed by about mid-May. He hoped that Bills would be introduced into all State Parliaments and the Commonwealth Parliament in the Spring sessions.[2] The latest information I have is that the legislation will be introduced on 1st October this year.

The Governments have not made public what will be the content of the other provisions to be included in the legislation dealing with such matters as conservation, safety etc., but these should be known within the next couple of months.

That is the offshore picture as it now stands.

ON SHORE LEGISLATION

On shore, with certain exceptions, the position has been fairly static. With the exception of South Australia and Western Australia, no major amendments to the present legislation are contemplated.

The Queensland Government appears to be quite happy with the way its legislation is working, notwithstanding that last year Mr. I. W. Morley, the State Mining Engineer spent several months in North America examining petroleum legislation.

In New South Wales, I understand, some amending legislation is in the course of preparation. This will provide for the deletion of the petroleum prospecting licence stage, leaving a two stage system of tenure (the petroleum exploration licence and the petroleum mining lease). In addition, a Pipelines Bill will be introduced into Parliament in the near future, and from indications given by the government it should be satisfactory to industry.

In South Australia extensive amendments are expected to be made in the foreseeable future to the Mining (Petroleum) Act 1940-1963.

In September, 1966 the South Australian Government circularised a draft of proposed amendments to the Act and later in 1966, following representations by members of industry and other interested parties, a second draft of the proposed legislation was circulated.

The basic provisions of this draft were as follows:

1. The second licence stage, the oil prospecting stage, would be deleted. The exploration licence, the first stage, would remain substantially intact except that renewals beyond the initial five year term for further periods of five years would be subject to relinquishment of 25% of the original licence area at each renewal and there would be a rental increase on each renewal. In addition an obligatory scale of expenditures on approved works would be imposed.

[2] Commonwealth of Australia Parliamentary Debates (Hansard), 26th Parliament, First Session 1967 (First Period), House of Representatives No. 6, p. 1146.

2. There would be completely new provisions for pipeline construction and operation requiring the issue of a licence for pipeline construction and a further licence for pipeline operation. In addition, the Minister would be empowered to require a pipeline operator to be a common carrier.
3. The Minister would be empowered to make certain orders for the purpose of preventing waste and regulating operations for production of petroleum to ensure optimum recovery. For such purposes the Minister could, inter alia,
   (a) regulate and make provision in respect of any pool or field for well spacing and designation of drainage units, maximum rates of production of wells, secondary recovery and pressure maintenance schemes and disposal of oil field wastes.
   (b) regulate, limit and allocate the production of oil and gas.
   (c) limit the amount of gas or water to be produced with oil and from wells and limit the production of oil from any gas well.
   (d) designate pools or fields.
4. In addition the Governor would be empowered, inter alia, to make regulations and orders of general application for the prevention of waste and to ensure optimum recovery.
5. A Petroleum Appeal Committee would be set up. Any person claiming to be prejudiced by any decision or direction or any order made under the Act would have the right to have the objection referred to this Committee, provided that the Minister was satisfied that the objection was not vexatious or frivolous.

As yet the amending legislation has not gone before the South Australian Parliament and it is not known at the moment whether any further redrafting is contemplated prior to its introduction.

In August, 1966 the Western Australia Mines Department announced proposals for the amendment of the Petroleum Act 1936-1954. These proposals may be summarised as follows:

1. Two forms of title would be used—
   (a) A permit to explore which would be exclusive or non-exclusive, and
   (b) a production lease.
2. The area of the State would be divided into five minute graticules in line with offshore provisions.
3. The maximum area of an exclusive permit to explore would be 5,000 square miles, i.e., half of the proposed area of an offshore permit.

4. The shape of an exclusive permit to explore would follow the five minute graticular boundaries excepting where the offshore line was followed, but one minute boundaries could be approved by the Minister in special circumstances.
5. There would be no limit on the number of exclusive permits to explore which could be held by any one person or company.
6. The initial term of an exclusive permit to explore would be five years (a year shorter than the initial term of an offshore permit).
7. A second term of five years would be granted to the permittee subject to relinquishment of 50% of the area held at the date of granting of the permit.
8. A third term of five years would be granted subject to a further relinquishment of 50% of the area held at the end of the second five-year term.
9. The relinquishment provisions would not apply to areas of 500 square miles or less. In these cases, provided that work obligations had been complied with, the holder could continue to hold his area of 500 square miles or less through the second and third five-year terms.
10. Exclusive permits would be terminated at the end of fifteen years. If discoveries were made during this period petroleum leases would be granted in respect of each discovery. Following a discovery an exclusive permit holder would nominate a location of nine graticules, one of which must include the discovery well and choose any five of those nine graticules within one year of the discovery as the petroleum lease area. The remaining four graticules would be reserved to the Crown for disposal by tender at a later date to be determined.
11. Section 59 of the present Act, which provides for an initial lease term of twenty-one years with extensions for any further period during which petroleum in payable quantities is produced from at least one well, would be extended to provide for renewals in periods of twenty-one years subject to the continuation of production.
12. Annual rentals for exclusive permits to explore would be based on the area of the permit in square miles and years in force. The State would be divided into zones. The zoning would be based on the prospectiveness and geographical situations of various areas. Rentals payable would depend on the zoning.
13. Exclusive permit holders would be expected to expend a certain amount annually on approved works. The legislation at the present time imposes no obligation upon a permit holder to undertake any

extensive programme of work. The amount to be expended annually in exploration on work obligations also would be determined by the zoning.

14. Non-exclusive permits to explore could be granted for a period to be determined according to the existing circumstances. These would permit operators to carry out preliminary investigations in free lands excluding test drilling. Free land would be land not previously explored or an area relinquished from an exclusive permit area. After the period of the permit had expired the Minister could then determine the method to be employed to make the area available for exclusive exploration. This would be done by either calling applications or by putting an area up for auction or private bidding. The granting of a non-exclusive permit to explore would be purely at the discretion of the Minister.

Later in 1966 the Western Australia Government decided not to proceed with the proposed amendments pending agreement as to the content of the offshore legislation.

Industry objected to certain of the proposed amendments. Whilst Industry had no objection to the two forms of title, it objected to the double relinquishment proposals. Whilst Industry accepted the five-year term for a permit it felt that 5,000 square miles maximum area was insufficient, and considered that a 10,000 square mile maximum was more desirable.

At present it is not known whether Industry's represensations have been successful or when the proposed legislation will be introduced.

That is the present status of onshore legislation.

THE FUTURE

What will be the guide lines for future legislation?

An examination of the proposed offshore legislation and the amendments proposed to their onshore legislation by the South Australian and Western Australia Governments, indicate three new trends. These, I think, will be reflected and developed in future legislation, but to what extent must be a matter for conjecture at this stage. These trends are—

1. A desire on the part of government to increase exploration activity by ensuring a more rapid turnover of land. The present method of assuring a more rapid turnover, so the Australian Governments seem to be saying, is to provide for a two-stage system of title, relinquishment of a large proportion of an area held under licence both during and at the end of the second stage, the imposition of more strict and well-defined work obligations during the exploration stage.

2. An awareness of the need to ensure that all petroleum production operations are carried out in such a way as to prevent waste and ensure maximum recovery by the introduction of more comprehensive conservation legislation than presently exists.
   It is not yet known what will be the content of the offshore conservation provisions. We do know, however, what the South Australian government proposes.
3. Recognition, as evidenced by the Ministerial Statement of November, 1965, and the zoning provisions of the proposed Western Australian legislation, of the principle, long recognised in Canada, that some areas because of their inaccessibility and the nature of their topography call for special treatment.

CONCLUSION

The various governments have not always sought the views and recommendations of the petroleum industry before proceeding with new legislation. However, it is felt that considerable progress is being made in developing a climate in which this will be the case.

In a country where Government acts in a dual capacity with respect to petroleum resources, firstly as a lessor and secondly as a legislative or regulatory body, it is important that it exercise its very wide powers in such a manner as not to discriminate either against the public or industry. The Commonwealth and State Ministers in recognition of this necessity expressed the view in their June 1966 statement that the proposed offshore legislation established a reasonable balance between the public interest and the industry interest.

There will, of course, be differences of opinion from time to time as to what is the public interest, what is the industry interest and whether a reasonable balance has been established between the two.

If government, in considering future legislation, honestly endeavours to strike this balance and is flexible in its approach to the peculiar problems of the petroleum industry, and if an atmosphere of mutual co-operation and trust continues to develop, I have no doubt that in the long run Australia's petroleum legislation should prove satisfactory to all sections of the community.