

Submission of NSW Government agencies to IPART's review of *Landholder benchmark compensation rates for gas exploration and production in NSW*

As part of the NSW Gas Plan, the NSW Government commissioned the Independent Pricing and Regulatory Tribunal (IPART) to develop a framework to set benchmarks for landholder compensation for gas exploration and production. NSW government agencies welcome the Issues Paper released by IPART on 20 April 2015, which sets out a series of questions for IPART, the Government and the community to consider.

NSW Government agencies support the three principles of transparency, adaptability and practicability which IPART proposes to guide the review. In particular, it is important that the framework is easy to use, provides an even playing field for landholders and gas companies to negotiate compensation and does not unduly increase the length and cost of negotiations.

This submission has been prepared by the NSW Department of Premier and Cabinet, the Division of Resources and Energy within NSW Trade and Investment, and NSW Treasury and reflects the views of NSW Government agencies.

The purpose of this submission is to provide further information on the NSW Gas Plan and how it will support landholders and local communities where gas activities take place and identify some issues for further consideration by IPART as part of the review.

NSW Gas Plan

The NSW Gas Plan will reset the approach to regulating gas in NSW through five priority pathways:

1. Better science and information to deliver world's best practice regulation
2. Pause, reset and recommence gas exploration on our terms
3. Strong and certain regulation
4. Sharing the benefits
5. Securing gas supply needs.

Specifically, under Priority 4, the NSW Government will introduce legislation to require gas companies to agree land access arrangements with landholders at both the exploration and production stages. Compensation will be a mandatory component of these arrangements.

Benchmarks set by IPART will give landholders the information they need as a guide to negotiate a fair deal.

The Government will also introduce legislation to implement the recommendations of the independent review of the arbitration system conducted by Bret Walker SC. This will make arbitration processes more efficient, balanced and transparent, and ensure the costs of negotiating an access arrangement are borne by the gas companies, not landholders.

The Government will also establish a Community Benefits Fund with voluntary contributions from gas companies to fund local projects in communities where gas development takes

place. The Government will refund \$1 from its natural gas royalty take for every \$2 provided to the Fund by industry, capped at 10% of royalty take.

The Walker review and Community Benefits Fund are discussed further below.

Grounds for compensation

The Issues Paper sets out comprehensive grounds for calculating compensation for the potential impacts of gas activities on landholders, based on compulsory land acquisitions. This is one potential model. IPART could consider whether there are any other models that provide further guidance.

Where possible, IPART could also consider how this compares with the experience of landholders in other jurisdictions. To support the review, IPART could consider land access arrangements for exploration and production in comparable Australian jurisdictions, including the heads of consideration and rates used for determining compensation.

Costs of entering into an access arrangement

In 2014, Bret Walker SC reviewed the land access arbitration framework under the *Mining Act 1992* and the *Petroleum (Onshore) Act 1991*. The NSW Government endorsed all of the Walker review's 32 recommendations, which were informed by targeted stakeholder consultation. While the focus of the review is on the dispute resolution aspects of land access arrangements, it also makes several recommendations about landholder compensation (see recommendations 25, 26, 27 and 28).

Recommendation 25 of the Walker review proposed that explorers be required to pay landholder costs relating to the negotiation and arbitration of land access arrangements, up to a capped amount, including the cost of time spent, legal costs and expert advice.

The Government Response to the Walker review committed to engage an independent expert to set reasonable and efficient cost and fee structures and caps, informed by further consultation with stakeholders. It is anticipated these requirements will be reflected in legislation in 2015.

Compensation for neighbours and the broader community

The Issues Paper expresses a preliminary view that neighbouring landholders who are affected by noise or other impacts from gas activities should receive compensation.

However, it does not consider possible vehicles for payment of compensation, how compensation could be calculated, whether it would be time limited or practice in other jurisdictions. It also does not consider how it would relate to other existing measures to ensure that local communities benefit from gas activities, including Resources for Regions payments, the Community Benefits Fund, local council rates, local council developer contributions and Voluntary Planning Agreements. It is important to consider the cumulative community benefits of these payments by industry, the risk of duplication and inconsistency across these initiatives, as well as the implication that it could discourage companies from making voluntary contributions or investing in development at all.

The NSW Government has released a discussion paper seeking input on the design and implementation of the Community Benefits Fund, which can be downloaded from www.haveyoursay.nsw.gov.au. We welcome submissions from interested groups and individuals, by 5pm 17 July 2015.

Economic benefit payments

The Issues Paper suggests that, in addition to compensation, landholders could also be given a share of the value of production as a benefit payment. This raises a number of complex issues that warrant further consideration including:

- **Compensation and benefit payments are distinct from each other:** The benchmarks sought from IPART are intended to provide information to guide landholders in their compensation negotiations with gas companies. As set out in the Issues Paper, the specific elements to be considered as part of compensation are set out in the resources legislation. To avoid confusing landholders and to ensure consistency with this legislation, the Government suggests that published compensation benchmarks should incorporate only these specified elements.

While benefit payments are likely to be a confidential matter between parties, IPART could consider whether it is possible to produce a benchmark for benefit payments based on experience in other jurisdictions. This benchmark would need to be clearly separate from the benchmarks for compensation, but would ensure that NSW landholders were aware of payments made in other jurisdictions.

- **Gas production is uncertain and has a long lead time:** There are many factors that influence whether exploration activities lead to production, including entering into land access arrangements with all relevant landholders, finding viable gas reserves, access to suitable infrastructure and market conditions. Even if production eventuates, gas flows and associated profits are likely to have a long lead time.

To manage these uncertainties, the Issues Paper raises two possible strategies: i) pooling benefit payments among landholders, and ii) making benefits payments upfront based on forecast production value, with a discount rate. Both of these proposals shift risks between the parties and should be considered in greater detail.

- **Impact on royalties:** IPART suggests that economic benefits payments could be funded through a gas company contribution to the value of 1% of production and a government contribution to the value of 1% of production drawn from royalties. However, the Issues Paper does not provide evidence of how such payments would support the goal of creating benchmarks to assist parties to negotiate compensation. Additionally, the rationale for these figures and an analysis of the implications is not provided in the Issues Paper.

It is also not clear whether it is appropriate for taxpayers to fund half of the cost of economic benefit payments to landholders. There does not appear to be a clear role for government as both companies and landholders have incentives to privately negotiate the best combination of compensation and benefit payments for their specific circumstances.

Royalties are collected from gas companies by government because natural resources are owned collectively by the people of NSW. Royalties are used to fund essential services like health and education. Diverting a proportion of these funds to private individuals would be out of step with the treatment of other resources in NSW and in other jurisdictions across Australia.

This would be on top of the 'royalty refund' contribution the NSW Government has already committed to make to encourage contributions to the Community Benefits Fund.

- **Potential perverse incentives:** In its recent paper, *Examining barriers to more efficient gas markets*, the Productivity Commission flags that any reallocation of the benefits of existing property rights (for example, through the establishment of landholder benefit payments) could create an incentive for rent-seeking and other unproductive behaviour, as well as disruption and uncertainty (pp.83-84). The Issues Paper briefly acknowledges, but does not accept, this analysis. It is important that this is considered in detail to mitigate any potential risks.

Consultation

NSW Government agencies support IPART's proposal to undertake extensive public consultation on the review, including public hearings in Sydney and country areas (particularly Gloucester and Narrabri, where Strategic Energy Projects are in progress). We suggest that landholders, gas companies and any other interested members of the community be encouraged to participate in the process.