

ESG - AN ENHANCED DECOMMISSIONING FRAMEWORK IN AUSTRALIA'S OFFSHORE OIL AND GAS SECTOR

In December 2020, the Federal Government of Australia issued a Consultation Paper entitled "Enhancing Australia's decommissioning framework for offshore oil and gas activities". This is an important paper which highlights the strategic significance of the offshore oil and gas sector which has supported Australia's economic activity and energy security for decades.

INTRODUCTION

The significance of an organisation's ESG performance as a measure of success is an international trend set to continue into the future. ESG aims to integrate into an organisation's culture, strategy and daily operations, and responsible, ethical and sustainable policies, practices and procedures, so as to preserve and improve our shared future. The goal is to transition ESG from being part of an organisation's mission statement to being an integral part of its way of doing business. The emerging challenge is how best to implement that transition. Regulatory compliance is a necessary, but insufficient indicator of ESG performance. Accountability, transparency and ongoing corporate commitment to advancement are laudable and key factors in a company's ESG performance, but they alone will not secure the desired transition.

OVERVIEW

While considerable government, legislative and corporate support currently exists for ESG in principle, further practical measures are required to achieve normalisation of ESG standards across all sectors of domestic, regional and international trade and commerce. One area where ESG metrics are prominent, and of increasing importance, is decommissioning of aging offshore oil and gas facilities at end of field life.

Various international and regional conventions and guidelines prescribe decommissioning at end of life, with partial removal permitted under certain circumstances.¹

Key issues

- December 2020: Consultation Paper on "Enhancing Australia's decommissioning framework for offshore oil and gas activities" released
- Acknowledging the maturing of the Australian offshore oil and gas sector, the Australian Government has increased its focus on managing aging offshore assets
- Existing regulatory activity, whilst robust, may require reform
- Broader lessons may be learnt from Australia's experience regulating its maturing offshore oil and gas sector
- The Australian Government is responsive to the need for improvement, consistent with demands for an environmentally sustainable and responsible oil and gas sector

¹ See the 1958 United Nations Geneva Convention on the Continental Shelf (**Geneva Convention**), which mandated removal of offshore installations; 1982 United Nations Convention on the Law of the Sea (**UNCLOS**), which superseded the Geneva Convention and permitted partial removal having regard to international standards; the International Maritime Organization's (**IMO**) Guidelines for the "Removal of Offshore Installations and Structures on the Continental Shelf and in the Exclusive Economic Zone" (**IMO Guidelines**); the 1972 Convention on the Prevention of Marine Pollution by Dumping of Wastes and Other Matter (**London Convention**) and the 1996 London Protocol, and the Guidelines for Assessment of Platforms or Other Man-Made Structures at Sea (**London Convention Guidelines**); the Convention for the

Looking globally, with the uncertainty and challenges posed by COVID-19, the UK decommissioning industry has continued its emphasis on "*improv[ing] decommissioning cost-effectiveness*" in 2020.² OGUK (a representative body for the UK offshore oil and gas industry) recognises that "[i]n the future, contracts will be won based on sustainability performance as well as conventional performance indicators such as safety and cost"; "sustainability performance" might encompass re-using the assets or their component parts and re-purposing the infrastructure.³ This is reflected in the *Finance Act 2019* (UK) (the **Act**), which has received Royal Assent. The Act:

- allows companies to transfer some of their tax history and enable purchasers to obtain effective tax relief for their decommissioning expenditure that would otherwise not be available; and
- makes petroleum revenue tax relief available to the purchaser when the seller provides the purchaser with decommissioning funds.

Both changes are part of the UK Government's innovative strategy to incentivise continued investments into the UK North Sea assets. Even before the legislative change, Shell and BP, in their respective North Sea assets transfers, had agreed to retain a share of decommissioning liabilities.⁴ The emergence of such shared decommissioning liability structure signals a move away from a "clean-break" decommissioning regime. Whether COVID-19 will curb the transition, and how regional and global regulatory regimes respond, will be closely monitored by industry participants.

In the emerging ASEAN decommissioning market, changes in legal and regulatory frameworks have brought about some growing pains. One recent example is Chevron's reignited arbitration with Thailand following the breakdown of negotiations regarding decommissioning costs at the Erawan Field, one of Thailand's largest gas sites.⁵ The dispute stems from a 2016 Thai law which operated retroactively, and obliges the gas field operator to bear the costs of decommissioning assets it has installed, including those that have been, or will be, transferred to the new operator.

The Australian decommissioning industry is also witnessing some market-driven changes. Recent measures suggested in the Australian Government's Consultation Paper, on the "*Enhanced Decommissioning Framework for Offshore Oil and Gas Activities*" announced in December 2020 (the **2020 Consultation Paper**)⁶ reflect the increasing significance of ESG performance. The 2020 Consultation Paper is part of the Australian Government's ongoing review of Australia's offshore decommissioning framework, launched in 2018. The Australian petroleum industry's decommissioning liability was modelled by

Protection of the Marine Environment of the North East Atlantic 1992 (as amended by Decision 98/3); and the 2012 ASEAN Council on Petroleum's Decommissioning Guidelines, which supplement UNCLOS and the IMO Guidelines.

² <https://www.ogauthority.co.uk/lessons-learned/>. See also OGUK, "*Decommissioning Insight 2020*", 22, <https://oilandgasuk.co.uk/wp-content/uploads/2019/11/Decommissioning-Insight-2020-OGUK.pdf>.

³ "*Decommissioning Insight 2020*", 26.

⁴ <https://www.chrysaor.com/downloads/news/chrysaor-to-buy-north-sea-assets-final.pdf>; <https://www.enquest.com/media/press-releases/article/acquisition-of-25-of-magnus-oil-field-enquest-to-take-over-operatorship-of-magnus-sullom-voe-terminal-and-associated-infrastructure-with-no-cash-outlay>.

⁵ <https://asia.nikkei.com/Business/Energy/Chevron-and-Thailand-at-loggerheads-over-gas-field-transfer2>.

⁶ Australian Government, Department of Industry, Science Energy and Resources' consultation paper "*Enhancing Australia's Decommissioning Framework for Offshore Oil and Gas Activities*" – December 2020.

Wood Mackenzie in an industry report, dated 9 March 2020, to cost in excess of AU\$60 billion over the next 30 years, based on removal of the ageing assets. With decommissioning described as "*an inevitable activity*" which is "*planned years in advance*",⁷ the Government's initiative was well received. The review aims to assess the adequacy, suitability and adaptability of Australia's decommissioning framework to meet present and future challenges – in short, to assess the regime's fitness for purpose.⁸

In Australia, the *Offshore Petroleum and Greenhouse Gas Storage Act 2006* (Cth) (**OPGGSA**) mandates that titleholders must decommission in accordance with environmental plans, field management plans and all applicable legislation. Failure to do so can result in prosecution by the Regulatory Authority, with penalties including rectification orders and liability for remediation costs.

In 2018 the Australian Federal Government released a discussion paper titled "*Decommissioning Offshore Petroleum Infrastructure in Commonwealth Waters*" (the **2018 Discussion Paper**). It focussed principally on the liability of titleholders and security mechanisms to meet decommissioning costs. It advocated for titleholders to bear all liability associated with offshore oil and gas infrastructure, including all decommissioning costs and post-decommissioning liabilities. The latter includes environmental, tortious and statutory liability under the OPGGSA, which notably does not eliminate any common law liability concerning petroleum operations. The 2018 Discussion Paper identified a number of inadequacies in the current system, including:

- the lack of detailed information concerning decommissioning plans available to the Regulator. It contrasted the position in England, where the *Petroleum Act 1998* (UK) requires a decommissioning plan to be formally submitted for approval at or about the same time as submission for approval of the field development plan.
- Legacy issues potentially arise from holding former titleholders who had divested or surrendered their interest liable for all statutory and common law obligations in connection with the infrastructure. The transferor would be responsible for the pre-transfer interest, irrespective of whether it continues to hold title. Where security arrangements are inadequate to cover potential decommissioning costs, a possible outcome is for the government to resort to taxpayer funds to meet the community expectations and international legal requirements. The 2018 Discussion Paper considered possible security assurance, looking in particular at the UK model, which vests the UK Oil and Gas Authority with a discretion to require additional security if it is dissatisfied with the level of security provided.

LEGAL AND PRACTICAL CONSIDERATIONS UNDER REVIEW

The 2020 Consultation Paper proposes to inject certainty for potential decommissioning liability in the offshore oil and gas sector by creating an "*enhanced framework*" to ensure the Australian regime is "*clear, fit for purpose and leading practice*". The 2020 Consultation Paper

⁷ Walker Report June 2020, "*Review of the Circumstances that led to the Administration of the Northern Oil and Gas Australia (NOGA) Group of Companies*" (**the Walker Review**).

⁸ The National Energy Resources Australia (**NERA**) led development of the National Decommissioning Research Initiative and undertook a comprehensive study which was largely consistent with the Wood Mackenzie modelling.

focuses on the management of financial and environmental risks associated with decommissioning, including measures for: (a) increased oversight of changes in corporate control and of financial assurance; (b) modernising Field Development Plans; (c) early and proactive use of remedial directions powers; (d) public comment and transparent reporting; and (e) enhancing trailing liability to apply in a greater range of circumstances. The aim is to ensure "*effective regulatory oversight and robust financial safety nets to strengthen protections for the environment, the industry, the Australian Government and taxpayers*".

The 2020 Consultation Paper was well timed, given the unprecedented liquidation in February 2020 of Northern Oil & Gas Australia, which resulted in the Australian Government having to ensure the safety and protection of the marine environment in respect of the FPSO Northern Endeavour on cessation of production. The Minister for Resources, Water and Northern Australia, the Honourable Keith Pitt MP, ordered a review into the surrounding circumstances (the **Walker Review**). This review identified areas for potential improvement in the current regime and made nine recommendations for improvement, including:

- Greater accountability, and the adoption of "*trailing liability*", whereby a titleholder would continue to be liable for decommissioning and removal of its offshore assets, even after ceasing to be a titleholder. Such a regime has been successfully adopted in a number of jurisdictions, albeit as a backstop for decommissioning liabilities, with the "*prime liability*" for decommissioning resting with existing titleholders. The enhanced framework proposed by the 2020 Consultation Paper would see the proactive use of remedial directions under the OPGGSA to achieve greater accountability. According to the 2020 Consultation Paper, the existing trailing liability provisions were inadequate, as the government's ability to "*call back*" is limited to when a title is terminated, has expired, is revoked, cancelled or surrendered. The enhanced framework would increase the scope of the government's power to "*call back*" a previous titleholder to remediate the title area or undertake other activities. As part of the accountability requirement, the enhanced framework would also provide for information to be made publicly available to stakeholders so that they are aware of steps taken by the titleholder to meet its decommissioning obligations and to be satisfied as to the remediation undertaken.
- Greater financial oversight by the National Offshore Petroleum Titles Administrator (**NOPTA**), greater transparency in change of control or ownership of titleholders, and increased scrutiny of titleholders' ongoing financial stability throughout the lifecycle of the title. The enhanced framework recognises the significance of "*titleholder governance*", including the need for an effective Board, clear demarcation of corporate responsibilities, and rigorous business risk management and transparency. The 2020 Consultation Paper proposes expanding the types of transactions subject to scrutiny and approval to include change of ownership or control of the titleholder entity whether through corporate merger, acquisition or takeover. This is aimed at ensuring that titleholders demonstrate their continuing technical and financial capacity throughout the entire lifecycle of the title, including when transitioning from one title to another, and at renewals. Under the enhanced framework proposed by the 2020 Consultation Paper, titleholders would be required to provide financial assurance, such as bonds or securities, to demonstrate they can

continue to fulfil their obligations and liabilities. This is consistent with the international standards requiring stronger corporate governance to ensure liabilities and obligations related to petroleum activities, including decommissioning, are adequately covered.

- Enhanced planning and management. The Walker Review recognised that "[d]ifferent facilities and dutyholders ought to require different strategies for inspection",⁹ having regard to their past performance, the type and condition of the facility in issue, and corporate governance factors. In short, one size does not fit all dutyholders. The Walker Review recognised the importance of "titleholder governance" as a "crucial issue worthy of NOPTA...oversight".¹⁰ It recommended more strategic planning of interventions, with the suitability and adequacy of the inspection regime being regularly assessed and incorporated into a long-term plan. The enhanced framework is said to modernise the requirement for a Field Development Plan "to reflect a maturing industry and to include early stage planning for decommissioning".¹¹ This aims to optimise the prospects of titleholders being able to meet their decommissioning obligations, having regard to the economic viability of the project. The 2020 Consultation Paper advocates for increased oversight of planning activities to capitalise on opportunities for "broad-scale efficiencies and cost reductions across the industry and the scope to grow new capability in an Australian decommissioning services sector to support the forecast increase of activity over the next 30 years".

Consultations for the enhanced framework close on 22 January 2021. Experiences from the UK and ASEAN markets indicate that for the enhanced decommissioning framework to succeed, government-led changes should be based on and reflect market-oriented calls for cost reductions and optimisation towards a more efficient, environmentally sustainable and responsible decommissioning regime.

CONCLUSION

The enhanced decommissioning framework, as proposed by the 2020 Consultation Paper and echoed in the Walker Review, is generally consistent with the principles reflected in ESG performance, with emphasis on environmental protection, sustainability, accountability, transparency and ongoing corporate commitment to such goals. The 2020 Consultation Paper underscores the need for certainty in respect of decommissioning costs and associated liabilities including on asset transfers. It provides an opportunity for legislative reform which may align Australia's decommissioning regime with international standards, and may facilitate the ongoing evolution of regional decommissioning standards.

⁹ Walker Report, page 6.

¹⁰ Walker Report, page 7. NOPTA is the National Offshore Petroleum Titles Administrator responsible for the daily administration of petroleum and greenhouse gas titles in Commonwealth waters in Australia.

¹¹ 2020 Consultation Paper, page 5.

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