SUBMISSION

Submission to the Ministry of Economic Development on

"REVIEW OF THE CROWN MINERALS ACT 1991 REGIME: TRANSITIONAL ARRANGEMENTS FOR EXISTING PERMIT HOLDERS: DISCUSSION PAPER (MAY 2012)"

INTRODUCTION

1. Straterra[1] welcomes the opportunity to submit on the discussion paper released on 18 May 2012, analysing options for transitional arrangements for existing permit holders[2]. As always, we do so in the interests of achieving benefits for the minerals sector[3], and for the New Zealand economy as a whole. The submission deadline of 8 June is noted.

2. Straterra submits from the point of view that New Zealand needs to consider its attractiveness for investment as a key policy criterion when developing transitional arrangements.

EXECUTIVE SUMMARY

3. The Ministry of Economic Development is urged to adopt Option A, of the three options proposed for transitional arrangements for existing permit holders. That provides for voluntary transfer to the new Minerals Programme, or for permit holders to continue complying with the relevant version of the M/P attached to their permit, if that is their wish. That arrangement would apply also in the event of changes in permit conditions, extensions in duration of permit, renewal of permits, permit appraisals, conversion to subsequent permits, transfers, and other such changes.

4. Our rationale is that Option A respects the property rights of permit holders, and helps reduce the sovereign risk of investing in, and doing business in New Zealand.

5. While Option A carries the risk of an increased administrative burden to the Crown, Straterra proposes ways of addressing that.

6. The royalty regime review should be considered separately, under appropriate criteria for that review, to achieve a regime that encourages investment in New Zealand.

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[1] Straterra represents 90 % by value of NZ minerals production, exploration, research, services, and support http://www.straterra.co.nz/About+Straterra

[2] It is noted the matter of transitional arrangements for existing permit holders was inadequately addressed in the March 2012 discussion paper, and is being addressed in the present consultation.

[3] This submission does not consider issues relating to petroleum.

DISCUSSION

Options for transition into the new Minerals Programme

7. MED has proposed three options for the transition of existing permit holders to the new Minerals Programme:

    - Option A – no forced transition into the new M/P for holders of existing permits, who will continue with the M/P applying when the permits were approved, however, may transition voluntarily into the new M/P;

    - Option B – immediate and forced transition for all holders of existing permits into the new M/P;

    - Option C – voluntary transition into the new M/P for holders of existing permits, except in the case of amendments to permit conditions, permit appraisals, subsequent permits, transfers, extensions to permit duration, renewal of permits, or other such changes where the transition would be forced and immediate.

8. The analysis provided for these Options is sound. That said, we believe there is room for improvement, which we explore below.

9. MED advises that **Option A** may suit many permit holders, however, "would not stack up well against measures of regulatory simplicity". New Zealand Petroleum & Minerals would have to administer permits under as many as eight different M/Ps, the implication being this would be an onerous task. On the face of it, that is a logical conclusion, and would need to be addressed in some way. MED notes that for the amended Crown Minerals Act to accommodate existing permits, "portions of the Act as currently written would have to be retained", e.g. for permit extensions, applications to transfer, and other changes to conditions. In places, the Act would end up providing for a "parallel regime", which, perhaps, would be undesirable.

10. **Option B** would be convenient for NZP&M, from a permit administration perspective (in the long term but not the short term), however, would impose significant obligations on permit holders. MED accepts that this option could have "significant consequences for investor perceptions of New Zealand". This can hardly be considered a serious option by anyone.

11. **Option C** offers a compromise, by providing for permit holders to move voluntarily to the new M/P, with the exception that any changes to permits, of the type already listed, would be brought compulsorily and immediately into the new M/P. The inference is that less invasion of

permit holders' property rights will occur, and the administrative burden for NZP&M will be manageable in the short term, while delivering a streamlined and fit-for-purpose M/P regime in the long term.

12. On that basis, Options A and B are presented in the discussion paper as mere "straw men", traversed to provide a rationale for adopting Option C as the only sensible course of action. There are additional considerations, however, and they lead inevitably – in Straterra's view - to preferring Option A.

13. Straterra contends that a permit is a form of valuable property right for the holder. The permit may have arisen as a result of a competition, where there can be only one winner. Significant effort and resource may have been devoted to the permit already, with build-up of intellectual property in the information associated with it. Funds may have been raised on capital markets, or from re-allocation from other projects, as a result of the holder acquiring a permit. Significant investment decisions may have been made. Furthermore, time has been expended, and time is money.

14. A permit is also a contract between the Crown and the permit holder. If the Government imposes changes in the contract framework, seemingly arbitrarily, that could send an undesirable signal to investors, regardless of whether or not the changes have merit. The signal is that the Crown is prepared to strip permit holders of rights, and vest in them those applicable under a new regime, and, therefore, is prepared to make unwarranted intrusions into the valuable property rights and investments of others[4]. As a consequence of that approach, investment capital could leave, or not arrive in, New Zealand. Some permit holders could go out of business, potentially, or have to close operations in New Zealand, and invest elsewhere (given that their financial modelling, lead times, and operational planning will have been underpinned by important assumptions as to the applicable regulatory framework).

15. It is acknowledged the Crown is confronted with the problem of administering permits under multiple M/Ps. The situation is analogous to a landlord who owns many rental properties, with eight variations in the tenancy agreements, arising over changes in approach over time. But the landlord cannot arbitrarily change the template for tenancy agreements (leaving to one side for a moment the matter of rent). That would have to occur by agreement with the tenant. Even if it

[4] Refer also to the Law Society of NZ submission to MED on the Crown Minerals Act Regime Review 2012, paragraphs 20 and 21:
http://www.lawsociety.org.nz/__data/assets/pdf_file/0020/51680/Crown_Minerals_Act_Review-23_04_12.pdf

were advantageous to the tenant to make the change, the overarching principle has to be contract law. That is for a very good reason. If the landlord is able to make arbitrary changes to the agreement, people would become reluctant to enter into such agreements, a lose-lose situation for landlord and potential tenant. (The landlord would retain the ability to review the rent from time to time, subject to criteria, as a separate matter (refer to **para. 20** on royalties).)

16. The Crown, therefore, is faced with the conundrum of wishing to make life easier for itself, at the risk of elevating New Zealand's sovereign risk, driving businesses away from New Zealand, and less economic activity occurring in New Zealand than would and should otherwise occur.

17. It is accepted that every investor must take on an element of sovereign risk, anywhere in the world. That does not provide an excuse, however, for increasing it. As matter stand, New Zealand's indifferent Fraser Institute rankings[5] caution against complacency in this regard. The new Overseas Investment Office test in relation to proposed investment in "sensitive land"[6] stands to make matters less favourable for New Zealand's attractiveness for investment. As well, the red tape, regulatory delays and thus uncertainty being experienced by major resource projects is having a discouraging effect on investor confidence. We have heard reports of major overseas investors saying that had they known of the regulatory uncertainty in New Zealand, they would not have invested.

18. Straterra proposes the adoption of Option A, with care needed in the design to make it workable from the Crown's perspective. The rationale is that the Crown should respect the property rights of permit holders, and invite permit holders to join the new M/P voluntarily. If the new M/P is better than previous M/Ps – e.g., more equitable criteria for approving work programmes, more flexibility in managing compliance with work programmes, set time frames for permit processing, the ability to amalgamate permits in specified circumstances, proactive engagement by the Crown with permit holders and applicants, streamlined processes for extending the duration of permits or changing conditions on permits - the permit holders will have a strong incentive to join the new M/P. NZP&M will wish to promote to industry the benefits of joining the new M/P. New entrants would enter the new M/P in any event.

19. On the concern that the amended Act would end up providing a parallel regime, in having to accommodate existing permit holders, Straterra believes there are simple expedients for

[5] Straterra submission to MED on the CMA Regime Review 2012, para. 11
http://www.straterra.co.nz/uploads/files/straterra_submission_cma_review_20_apr_2012_final.pdf
[6] International Law Office comment on changes to NZ overseas investment law
http://www.internationallawoffice.com/newsletters/detail.aspx?g=f9cf003f-46fd-45c9-a0f6-4becbc428a11

addressing that issue (refer to the recommendations below). This simple tool is to provide in the body of the CMA one regime applying to permits going forward, prefaced (where relevant) by exception wording that refers the reader to a schedule, in which are set out provisions applicable to older permits. Thus the body of the Act is not rendered inaccessible, or difficult to interpret.

Royalty regime

20. Straterra believes that royalty regime matters should be addressed separately to that of the transition or otherwise of existing permit holders into a new M/P. The Crown is entitled to review the royalty regime applying to minerals owned by the Crown, however, the criteria for that review are unlikely to be the same as those applying to the transition to a new M/P. Straterra has advocated previously for criteria that should govern the royalties review, and on the outcome that should be sought from the review, namely, a competitive regime that encourages investment in New Zealand[7].

RECOMMENDATIONS

a) Note that the discussion document's Options A and B appear to be "straw men" to promote Option C, which provides for a combination of voluntary and forced transition into the new Minerals Programme;

b) Note that while Option C is an improvement on Option B, it entails interference with valuable property rights, and presents to investors considering New Zealand, nonetheless, with unnecessary, elevated sovereign risk;

c) Agree to adopt Option A, as the option most likely to promote continued or increased investment in New Zealand, and as the option that adequately respects property rights, with Recs. (d) – (g) providing for workability from the Crown's perspective;

d) Agree to preface relevant provisions in the Act with wording such as "other than in respect of an existing permit, in respect of which the provisions in Part [x] or Schedule [X] apply...", This will avoid confusion or difficulties in administering the Act, and leaves the core body of the Act easy to interpret and apply;

e) Agree to develop Part [X] of, or Schedule [X] to the Act, to set out the different rules on relevant matters, for existing permits under different M/Ps;

[7] Straterra submission to MED on the CMA Regime Review 2012, paras. 21, and 105-108.

f) Agree to define "existing permit" in the Act to mean any permit under a M/P for minerals, coal or petroleum, other than that entering into force following the amendment to the Act;

g) Agree to develop a new M/P in such a way to ensure that it invites and encourages a voluntary transition on the part of existing permit holders into the new M/P; and

h) Agree to consider the review of the royalty regime separately from Recs. (a) – (g), under fit-for-purpose criteria, e.g. as proposed previously by Straterra.