

Regulatory Assessment Statement

**for establishment of an industry levy for
petroleum tenure holders to recover costs
associated with groundwater management
functions of the Queensland Water Commission**

September 2011

An invitation to comment

Closing date for public submissions: 14 October 2011

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Executive Summary

Background

In December 2010, the Queensland Government introduced changes to legislation to strengthen the management of groundwater extraction by petroleum and gas operators (petroleum tenure holders). The changes were driven by the rapidly expanding Coal Seam Gas (CSG) sector. Although all petroleum and gas operations extract groundwater, the volumes extracted by CSG operations are large. The water extraction has the potential to affect water levels in adjacent aquifers used for water supply and the flow of water to springs. The impacts on water levels can extend well beyond the tenure and overlap with impacts generated from water extraction on other tenures.

Changes to Chapter 3 of the *Water Act 2000* (Water Act) provide for a cumulative management area (CMA) to be established in areas of intensive development where impacts are likely to overlap. The Surat CMA has been established accordingly (Figure 1). Under the legislative amendments, the Queensland Water Commission (Commission) is responsible for preparing an Underground Water Impact Report (UWIR) based on regional modelling, setting out predicted impacts and management strategies. Tenure holders outside the CMA will prepare their own UWIRs, which will include monitoring programs. The Commission will maintain a database of base line and monitoring data. The Commission will also provide advice about any future need for additional CMAs. Section 360FA of the Water Act provides for an industry levy to meet the Commission's cost in delivering its new functions.

Objectives of the Regulatory Assessment Statement (RAS)

This RAS concerns the introduction of a levy on petroleum tenure holders to meet the Commission's costs in carrying out its new functions. Policy objectives are:

- technical assessment of groundwater impacts should be of a high standard
- petroleum tenure holders have rights to extract groundwater and there are also responsibilities associated with these rights including to pay for the cost of assessment and management of groundwater impacts
- the levy structure should fairly apportion the cost of Commission activities to the groups of petroleum tenure holders according to their relative benefit
- the levy structure should be efficient, being as simple as practicable so that the administration of the levy does not add appreciably to Commission and industry costs
- the levy should only provide revenue for the Commission's new underground water management water functions, and not its other functions.

Authorising provision

Section 360FA of the Water Act is the provision under which the proposed regulation is to be made.

Options

The preparation of the UWIR for the Surat CMA is the core responsibility for the Commission. If the Commission's role did not exist then tenure holders in the CMA would need to individually prepare underground water impact reports at their own cost. For the purposes of this RAS, this is the base case.

As water extraction is the reason for establishing the Commission's new functions, basing the levy on the volume of water extracted was considered (Option 1). The difficulty with this option is that the Commission needs to carry out its activities in advance of water extraction. The timing of water extraction does not align well with the timing of the Commission's activities.

The area under tenure was also considered as the basis for charging as it provides for clear alignment between the Commission's costs and the charges applied under the levy (Option 2). Two variations were considered. The first of these involved applying the levy to the area under a petroleum lease (PL), and not applying it to areas under an authority to prospect (ATP) on the basis that water extraction is small under exploration tenures. The difficulty with this option is that the major planned CSG developments relate to land currently held under ATPs as well as PLs, so the levy would only relate to part of the planned development area. However, the water extraction impacts of these

planned developments are a major focus for the Commission. Under this option the cost burden would fall unfairly on the early developers who have a high proportion of land held under PL.

The preferred option is to use the areas under tenure as the basis for charging, but to apply the levy to lands held under a PL, and also to lands held under ATPs (granted and under application) that are within areas that are the subject of an approved environmental impact statement (EIS) for gas field development.

In order to better align charges with the Commission's costs, the preferred option also provides for different charges to apply to three groups of relevant tenures as follows. The cost of the Commission's activities outside the CMA are relatively small, and holders of relevant tenures outside the CMA should meet only those costs. Within the CMA it is the existing and planned water intensive CSG operations that are the reason for the complexity and breadth of Commission activities, rather than the less water intensive conventional petroleum and gas operations. Therefore a higher charge should apply for tenures used for CSG production than for tenures used for conventional petroleum or gas production.

Recommended option

Tenures are of different sizes but are comprised of standard sized units of land called sub-blocks. The levy would be applied per sub-block.

The levy would apply to:

- Sub-blocks under a PL; and
- Sub-blocks under an ATP (granted or under application), to the extent that the ATP is within an area that is the subject of an approved EIS for gas field development.

One of three charges would apply:

- Charge No 1 would apply to the sub-blocks of tenures outside the CMA.
- Charge No 2 would apply to sub-blocks of tenures inside the CMA, to the extent that the sub-blocks are used or are intended for use for conventional petroleum and gas production.
- Charge No 3 would apply to sub-blocks of tenures inside the CMA, to the extent that the sub-blocks are used or are intended for use for CSG production.

The charges would be set at the beginning of each financial year, based on the approved budget for the year and the number of relevant sub-blocks existing at 1 July in each year. The budgeted costs would be apportioned into three parts to be collected through the three charges. The apportioned charges would be divided by the number of relevant sub-blocks to which the separate charges are to apply.

The Commission has been funded during 2010-11 by the Queensland Government and this is to be recovered through the levy. For each of the first three years of the operation of the levy, in addition to the charge for the costs for the year, the charge will also include one third of the costs incurred by the Commission for 2010-11. Some amendments to the authorising provision of the Water Act will be progressed to enable a regulation to give effect to the recommended option.

Consultation

As the number of industry entities affected by the levy is small, the Commission has consulted directly with key industry stakeholders in the process of developing the levy.

1. Issue statement

1.1 Background

The Queensland CSG industry is rapidly expanding in parallel with the planned establishment of liquefied natural gas (LNG) export facilities at Gladstone. Significant volumes of water are generated as a by-product of CSG production. Petroleum and gas tenure holders, including CSG producers, have a statutory right under the *Petroleum & Gas (Production and Safety) Act 2004* (P&G Act) to extract groundwater in the process of undertaking petroleum activities. In addition, tenure holders need to hold an environmental authority under the *Environmental Protection Act 2004*, which sets conditions in relation to environmental impacts.

In December 2010, the *Water and Other Legislation Amendment Act 2010* introduced amendments to the Water Act to strengthen and expand the regulatory system for managing underground water impacts associated with the extraction of groundwater by petroleum and gas, including CSG, activities. These changes established a new role for the Commission as described below.

1.2 Cumulative management areas

A key issue for management of the impacts from CSG production is that in areas of intensive development the water level impacts from each individual CSG operation can extend beyond the tenure and overlap with impacts resulting from activities on nearby tenures. The recent amendments addressed this issue by establishing a role for the Commission in relation to the management of cumulative impacts resulting from underground water extraction by petroleum tenure holders.

The government can declare an area to be a 'cumulative management area' (CMA) if the impacts of water extraction by two or more tenure holders are likely to overlap. The legislative amendments provide for a cumulative approach to be taken to the assessment and management of CMAs, with the Commission playing the key role.

The Surat CMA has been established under these new provisions (Figure 1). The Commission will periodically prepare an Underground Water Impact Report (UWIR) for the Surat CMA. The core tool for preparation of the UWIR will be a regional groundwater flow model. This model is currently being developed and will simulate the way water moves through aquifers, allowing prediction of future reductions in water level in the coal seams and adjacent aquifers due to existing and planned petroleum and gas development.

The Surat UWIR will include maps that show predicted future water level impacts. As well as showing long term impacts, these maps will define, for each aquifer, the areas where water levels are expected to fall by more than specified trigger thresholds within three years. These areas will be termed 'immediately affected areas'. When the Surat UWIR is approved, petroleum tenure holders will need to enter into agreements with bore owners about arrangements to maintain water supply in these areas. These arrangements are designed to ensure that the agreements will be in place before any potential impairment of water supply occurs.

The Surat UWIR will include a 'spring impact mitigation strategy'. Some springs in the Great Artesian Basin are of high cultural and ecological value. The groundwater flow model will be used to assess the likely future reductions in water level in aquifers beneath springs as a result of petroleum development in the CMA, and to develop a strategy for spring management.

The Surat UWIR will include a 'water monitoring strategy'. This strategy will be an integrated strategy for the region, designed to monitor how the groundwater system responds over time, and to test how accurately the regional groundwater model is predicting water level behaviour. This approach will enable adjustments to be made to continuously improve groundwater flow modelling. The monitoring strategy will specify the bores to be monitored, frequency of measurements and standards for measurement. The strategy will also specify the water quality sampling program.

The Surat UWIR will assign individual responsibilities to tenure holders for component parts of regional programs. For example, the monitoring program will require monitoring in areas beyond the lands under tenure. Individual tenure holders will be given responsibility for specific parts of the monitoring program for those 'off-tenure' areas, and will be required to carry out that work to a specified standard.

The Commission will update the Surat UWIR every three years. The groundwater flow model will be updated incorporating new information emerging from monitoring data and other sources. Through this process, predictions about future water levels will be progressively refined.

1.3 Other Commission responsibilities

The recent change to Chapter 3 of the Water Act also established other roles for the Commission in relation to the management of water extraction by petroleum tenure holders. Outside the CMA, individual tenure holders have an individual responsibility to prepare an UWIR. Those reports will need to assess impacts on water levels and specify a water monitoring program. The Commission will maintain a database to reliably store data collected under monitoring programs set out in those UWIRs, as well as monitoring data from the Surat CMA. The database will also store baseline data.

The Commission will monitor the development under petroleum tenures and provide advice on more general matters related to the extraction of water by tenure holders, such as any emerging need for additional CMAs in Queensland.

1.4 Impacts of the government not taking action

The central role for the Commission is the assessment of regional impacts, and the development of management strategies for CMAs. If the government had not established the Commission's new role, the individual tenure holders would have each needed to carry out this work. Such an approach would be less efficient and effective than having the Commission, as an independent entity, carry out the function. It would be less efficient because the individual tenure holders would carry out work over areas that overlapped to a significant extent, and less effective because individual tenure holders would need access to data from other tenure holders. Any breakdown in cooperation would detract from the quality of the work carried out by all tenure holders. These aspects are discussed in later sections of this RAS.

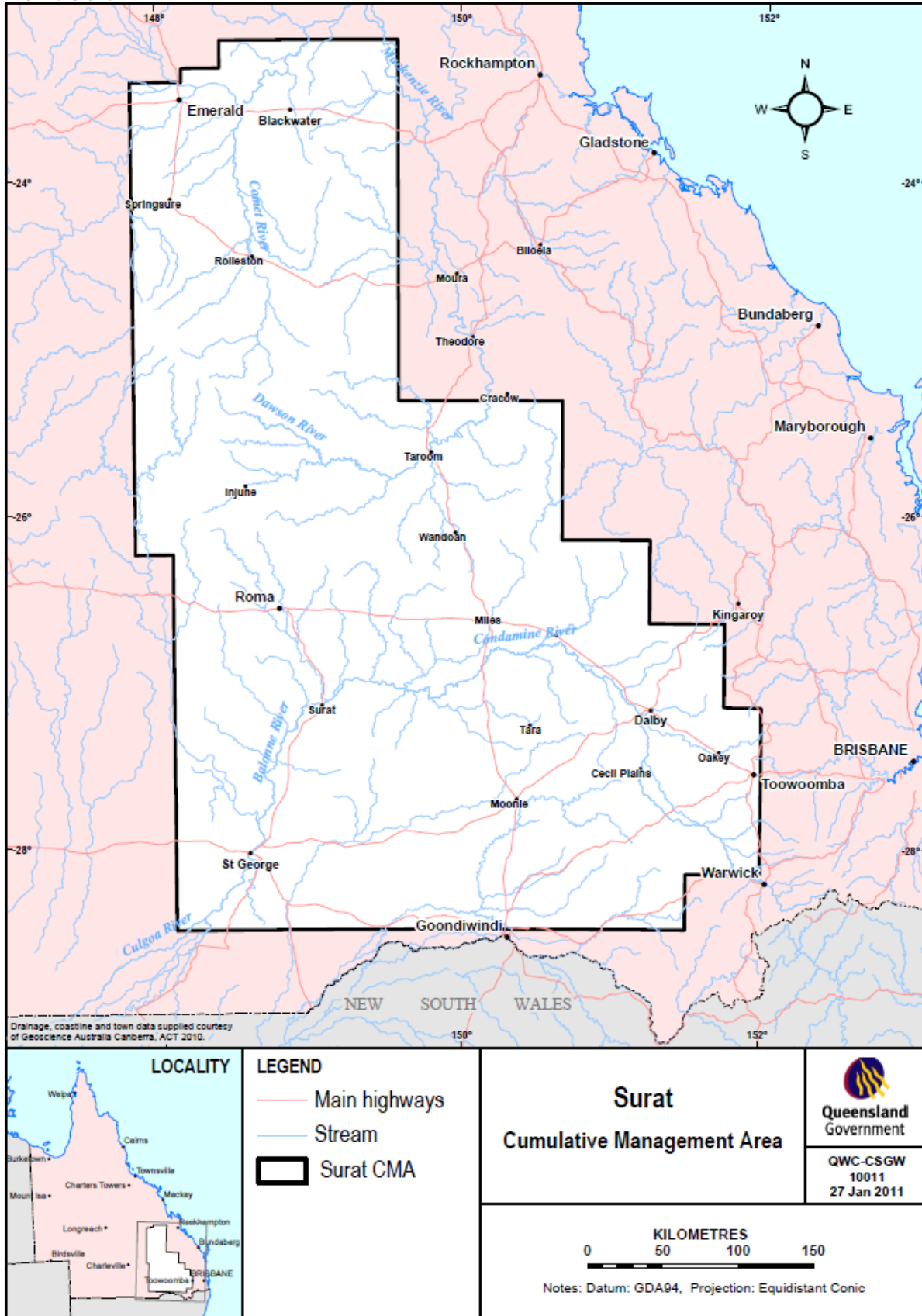


Figure 1. Surat Cumulative Management Area.

2. Policy objectives

2.1 Policy proposal—introducing a levy on petroleum tenure holders to fund the Commission’s underground water management activities

It is intended to introduce a levy to meet the costs incurred by the Commission in carrying out its new functions in relation to the management of the impacts of groundwater extraction by petroleum tenure holders. The Water Act provides for the introduction of the levy to be worked out in the way prescribed in a regulation..

As yet, other jurisdictions have not established a comparable management regime and therefore there is no equivalent levy in other jurisdictions that can be used for comparative purposes.

2.2 Key policy objectives

The key policy objectives are as follows:

a. Technical assessments of likely future impacts from water extraction needs to be carried out to a high standard

The volume of water planned to be extracted by CSG producers is large. Communities rely on groundwater resources and need to understand as clearly as possible the potential impact of the water extraction on water levels.

b. Petroleum tenure holders should meet the costs associated with the management of their rights to take underground water

Under the provisions of the P&G Act petroleum tenure holders have the right to take groundwater in the process of producing petroleum and gas. With that right goes responsibilities and accountabilities.

Some of those responsibilities and associated costs are met directly by individual tenure holders. Some of the responsibilities are met indirectly, through the Commission carrying out the required work collectively for tenure holders. It is appropriate that tenure holders meet the Commission’s costs as well as their own direct costs.

c. The levy structure should fairly apportion the cost of the Commission’s activities to groups of tenure holders according to their relative benefit

Some of the Commission’s activities relate specifically to particular groups of tenure holders. For example, most of the Commission’s current activities relate only to the Surat CMA. It is fair that the levy system is structured so that those costs are to be met by the tenure holders within that area.

d. The levy should be efficient

The levy structure should be as simple as possible and the data to support the levy structure should be readily available. This will ensure that the cost of administering the levy does not significantly contribute to the costs to be recovered through the levy.

e. The levy should only provide revenue for the Commission’s underground water management functions

The Commission has two separate sets of functions. One set of functions relate to water supply and demand management of urban water supply in South East Queensland. The other set of functions relate to the management of water extraction by petroleum tenure holders. The Commission has established separate business units to ensure there is transparency in relation to costs in delivering the two separate sets of functions.

The Commission has internal services (eg information technology services) that support both sets of Commission functions. The cost of these services needs to be apportioned between the two business units in accordance with sound financial management principles.

2.3 Authorising law and relationship with other legislation

The Water Act is the statute that establishes the new role for the Commission. It is the authorising law which provides the head of power for establishing the levy. Section 360FA is the relevant section. That section is part of the amendments made to the Water Act in December 2010 to strengthen arrangements for the management of water extraction by petroleum tenure holders.

Petroleum tenure holders have rights under the P&G Act to take groundwater in the process of producing petroleum and gas. In addition, under the provisions of the *Environmental Protection Act 1994*, tenure holders need to obtain an environmental authority. As a result of the recent amendments to the Water Act, tenure holders have new ongoing management responsibilities after water extraction commences that continue over the life of the project.

3. Options and alternatives

The recent amendments to the Water Act established the new functions for the Commission and provided that a levy could be established to fund the activities needed to deliver those new functions. If government now decided not to introduce the levy, it could be expected the Water Act would be amended to remove the provisions providing for the levy and to also remove the provisions establishing the underground water management functions of the Commission leaving those functions to be carried out by individual tenure holders. This option of the Commission not delivering the new functions but with those functions being carried out by individual tenure holders has been considered. This is referred to in this RAS as the 'base case'. Two other options have been considered. Option 1 is a levy based on the volume of water extracted. Option 2 is a levy based on the area of tenure held. Within Option 2 there are two variations (Option 2a and Option 2b) that differ in the types of tenures to which the levy would apply. The base case and the options are discussed below.

3.1 The base case: levy is not introduced

Under this option the Commission would not carry out cumulative assessment in CMAs nor provide advice to the Department of Environment and Resource Management (DERM) in relation to the adequacy of UWIRs prepared for operations outside the CMAs. Tenure holders would each be individually responsible for this work.

Because the impacts on water levels from water extraction on a petroleum tenure can extend well beyond the boundaries of the tenure, the impacts can extend into adjacent tenures. As a result, tenure holders in areas of intensive development such as the Surat CMA, would need to separately build models covering large areas that overlap to a significant extent. Similarly, they would need to develop monitoring and management strategies over large areas and those areas would overlap to a significant extent. This option is therefore less efficient than having the Commission carry out modelling and assessment and developing integrated management strategies.

The option would also pose difficulties for individual tenure holders as they would need to obtain information from other tenure holders in order to carry out their individual responsibilities. There is a risk that the high level of cooperation required between tenure holders could not be achieved or maintained over time, and that as a result the quality of outcomes would be compromised.

Under this option there is the potential for conflict of interest issues. There could be a perception that tenure holders may not bring the independence needed to provide stakeholder confidence in the outcomes of technical assessments.

The base case does not meet the key policy objectives and is not preferred.

3.2 Option 1: levy based on water extraction

As the impacts resulting from water extraction is the issue that has led to the Commission's new functions, basing the levy on the volume of water extracted has been considered.

A key limitation of this option is that the timing of water extraction would not align well with the costs incurred by the Commission. For the developing CSG industry, the Commission needs to assess the likely impacts of future water extraction at an early stage, before large scale water extraction commences. Commission costs are therefore driven more by planned development than by existing development. As a result, a levy based on water extraction would fall unfairly heavily on the earliest CSG developers. Later developers would significantly avoid the costs of initial model development and initial assessment.

A further limitation of this option is that when CSG water extraction does commence, the volume extracted varies significantly over time. For any bore the volume of water extracted peaks early and then reduces over the production life of the well. As a result the charge per unit volume of water would vary substantially from year to year, depending on the volume of water extracted, making it difficult for tenure holders to predict their exposure to the levy from year to year.

This option does not meet some of the key policy objectives and is not considered further.

3.3 Option 2: levy based on area under tenure

This option uses the area of land under tenure as the basis of the levy as it provides the best alignment between the Commission's costs and the charges applied under the levy. Tenures are of different sizes but they are comprised of a number of standard sized units of land area called sub-blocks. One of three separate charges would apply for each sub-block of a tenure, calculated as follows.

For tenures outside the CMA a single charge per sub-block would apply. For these areas the Commission's activities and associated costs are relatively small. The relevant activities relate to management of the monitoring data and the provision of advice in relation to such matters as the adequacy of UWIRs prepared by individual tenure holders. For indirect costs, activity based costing was used to allocate the costs to the different cost pools. For any year the levy per sub-block would be the Commission's costs relating to work outside the CMA divided by the number of sub-blocks.

For tenures inside the Surat CMA a similar approach would be taken. However, a differential charge would apply depending on whether the tenure was used for CSG production or for conventional petroleum or gas production. This approach would be needed for the following reasons:

- Conventional production extracts a relatively small amount of water, the operations are mature and the impacts are well understood. By comparison, CSG development will extract more water, and is in new areas where impacts need to be assessed for the first time. As a result, it is the CSG industry that is the main cost driver for the Commission's activities in the Surat CMA and it should meet the major share of the cost of the Commission's activities in the CMA.
- The tenures on which conventional production is carried out tend to be relatively large because they were established at an earlier point of time when a different approach applied to the granting of tenures. To charge for the sub-blocks of tenures on which conventional production is carried out at the same rate as for tenures on which CSG production is carried out, would result in an unfair share being paid by tenure holders using conventional production.

Although there is a strong reason to differentiate between CSG and conventional production inside the CMA, the same need does not exist outside the CMA for the following reason. Inside the CMA the Commission will be carrying out the modelling and assessment activities. Outside the CMA the individual tenure holders will carry out that work. Although the cost associated with assessing the impacts of new water intensive CSG developments may be higher, those costs will be met directly by the tenure holders. The Commission's activities will consist of checking the technical work carried out by the tenure holder, and the storage of monitoring data. As a result, there is not the same need to differentiate between CSG and conventional production.

Option 2 therefore provides for three annual charges:

- Charge No 1 would apply to the sub-blocks of tenures outside the CMA.
- Charge No 2 would apply to the sub-blocks of tenures inside the CMA, to the extent that the sub-blocks are used or are intended for use for conventional petroleum and gas production.
- Charge No 3 would apply to the sub-blocks of tenures inside the CMA, to the extent that the sub-blocks are used or are intended for use for CSG production.

Tenures can be exploration tenures called an 'authority to prospect' (ATP) or 'petroleum leases' (PLs). Two variations of option 2 have been considered having regard to the cost drivers for the Commission's activities.

Option 2a—levy based on area under tenure—applies to petroleum lease tenures

Under this option the Commission's costs would be shared by the holders of PLs, but not the holders of ATPs. This rationale is because generally the holders of ATPs for the most part do not extract water and do not affect groundwater levels. ATPs exist over large areas of the state and often exploration does not proceed to production.

Generally, the Commission's activities are not driven by exploration activities of tenure holders. If the levy were to apply to ATPs and PLs equally, the holders of ATPs as a group would be unfairly burdened with payment for costs for activities from which they would not benefit.

However, a difficulty with this option is that within the CMA some ATPs are part of planned major CSG developments. The Commission's modelling and assessment activities within the CMA are directed at assessing the impacts of major planned CSG development as well as existing development. If the Commission's costs within the CMA were met by holders of PLs only and not the holders of ATPs that are part of planned development, then the cost burden would fall unfairly on the existing early developers. The ATPs in the areas of planned development will eventually become PLs as planned development is progressively implemented, but the cost of the Commission's modelling and assessment activities in the CMA would have already been met by the early developers.

This option does not meet some of the key policy objectives and is not recommended.

Option 2b—levy based on area under tenure—applies to petroleum lease tenures and also exploration tenures that are approved for petroleum development.

Under this option, the Commission's costs within the CMA would be shared by both the holders of PLs and the holders of those ATPs (granted or under application) within areas that are the subject of an approved environmental impact statement (EIS) for gas field development. These particular ATPs have been signalled as being on a planned path to commercialisation and therefore are a focus for activity by the Commission.

This option achieves a high degree of alignment between charges under the levy and the benefits to tenure holders.

This option best meets the key policy objectives and is the recommended option.

3.4 Levy for 2011–12 under Option 2b

The Commission is currently operating under a budget approved by government, and funds provided by government. The approved budget for 2010–11 is \$3.32 million (a part year) and the approved budget for 2011–12 is \$4.52 million (a full year).

The levy is to commence for the 2011–12 year. The government costs for the 2010–11 year are to be recovered from tenure holders through the levy, with one third of the 2010-11 costs recovered in each of the first three years of operation of the levy. Table 1 provides an estimate of the levy for 2011–12.

Table 1. Indicative charges for 2011-12 based on approved budget and current tenure status

	Charge No 1 Outside the CMA	Charge No2 Inside CMA Conventional Production	Charge No3 Inside CMA CSG production
Cost 2011-12	\$226 000	\$213 000	\$4 082 000
Cost recovery 2010-11 (33% of 2010-11 costs)	\$ 57 000	\$ 53 000	\$1 035 000
TOTAL	\$283 000	\$266 000	\$5 117 000
No. of sub-blocks	2 792	1 390	6 680
Charge (per sub-block)	\$101	\$191	\$766

4. Impact assessment

4.1 Methodology

The primary issue for impact assessment is the comparison of the base case with the options that involve the Commission carrying out its role and recovering costs from tenure holders through a levy. This assessment considers the economic, environmental and social impacts associated with the proposed levy structure.

4.2 Economic costs and benefits

Under the recommended option, the Commission will carry out modelling and assessment of impacts inside the CMA. This work involves the development of geological understanding of the aquifer system and construction of models based on that understanding. It involves a survey of springs to assess values and an assessment of the vulnerability of springs. It also involves the development of a regional monitoring program. The Commission expects to spend some \$3.99 million on these activities in 2011–12. The expenditure provides for staff salaries and the purchase of specialist services. The Commission's total planned expenditure on its new underground water management functions is \$4.52 million in 2011–12. Expenditure within the CMA therefore accounts for some 88 per cent of the Commission's total expenditure.

Under the base case, each tenure holder in the CMA would need to carry out the same range of work for the area affected by their individual operations. There are four major CSG projects of similar size that are planned for development in the Surat CMA. The impacts from the four planned projects overlap substantially. As a result, each of the four project proponents would need to carry out the same scope of work as will be carried out by the Commission under the preferred option, and do so over an area nearly as large. There are clear economic efficiencies for tenure holders in paying for a portion of the Commission's costs through the levy, rather than needing to fully fund costs that would be of the same order as the Commission's costs.

This logic is demonstrated as follows. The proportion of the Commission's cost for CMA related activities that each of the four major project proponents would meet would depend on the amount of land under relevant tenure at the time. However, for the purpose of this demonstration it is assumed that they would each pay a charge that met 25 per cent of the Commission's costs. On this basis, the charge for each tenure holder would be some 25 per cent of the costs that the tenure holder would incur in carrying out the work that it could need to carry out under the base case.

For tenures outside the CMA, under the preferred option the Commission can advise DERM about the adequacy of the UWIRs prepared by the tenure holders. Under the base case, in the absence of the Commission providing that function, it could be expected that tenure holders would be required to pay for detailed peer review of reports. Therefore, the recommended option would not materially increase the economic cost to these tenure holders.

4.3 Environmental costs and benefits

Under the preferred option, the Commission will carry out the modelling and assessment functions within the CMA. The Commission is an independent authority with power to obtain the data the Commission needs to carry out its functions from tenure holders. This arrangement provides the best potential to ensure that the most accurate assessment possible is made of environmental impacts.

Under the base case, tenure holders within the CMA would need to provide data to each other to enable modelling and assessment in areas of overlapping impacts. Any lack of cooperation between the tenure holders could reduce the accuracy of the assessments carried out. If the assessments are inaccurate then the need for management responses may not be identified and management action may not be taken or may not be taken in a timely way. This could result in damage to springs.

The preferred option provides clear environmental benefits in comparison to the base case.

4.4 Social costs and benefits

Under the recommended option, the Commission as an independent authority will carry out modelling and assessment functions within the CMA. It will store monitoring data in a secure database, and will provide advice to government on any emerging need for additional CMAs. This work can be expected to provide greater community confidence that long term structural arrangements are in place to support decision making, than would be provided under the base case.

5. Consultation

The proposed levy impacts the holders of petroleum tenures. In developing the regulatory arrangements for strengthening the management of water extraction by tenure holders, the petroleum and gas industry was consulted through the Water Working Group of the Australian Petroleum Production and Exploration Association (APPEA). This group includes representatives from the major CSG companies with APPEA providing representation for smaller companies. The new regulatory arrangements were specified in the Water and Other Legislation Amendment Bill 2010. An exposure draft of the Bill was provided to industry for comment. The Bill provided for the new functions of the Commission in relation to the impacts of water extraction by tenure holders on groundwater levels, and for the costs of the Commission to be met by a levy paid by tenure holders. The legislative changes came into effect in December 2010.

Following the changes to legislation, the Commission consulted with petroleum industry representatives in the process of developing levy options. Options were discussed with industry representatives on 27 January 2011. As the proposed arrangements essentially impact a small number of tenure holders, individual meetings were held with those companies to discuss and further develop options during February and March 2011. These included meetings with Santos Ltd, Origin Energy Ltd, Queensland Gas Company Ltd and Arrow Energy Ltd. Meetings were also held with APPEA to gain broader industry perspectives.

Through the consultation meetings the Commission formed the following understanding of industry views:

- Industry supports the need for the Commission's central role and does not resist the introduction of a levy.
- Industry seeks stability in the levy to allow budgeting for future charges.
- Industry seeks the levy to be structured so as to distinguish between the holders of tenures used for CSG production and the tenures used for conventional production, so as to not unfairly burden conventional production.
- While acknowledging that the budget through to 2011–12 were set by government in establishing the Commission's new role and that the planned expenditure is not unreasonable, industry seeks assurance that tenure holders exposed to the levy will be consulted in the development of budgets for future years.
- Industry seeks confidence that financial management arrangements within the Commission support clear separation of costs incurred in delivery of the Commission's new underground water management functions from its other functions.

The preferred option addresses the issues raised by industry in relation to the structure of the levy. Financial management arrangements within the Commission have been established to ensure that only costs associated with the underground water management functions are recovered through the industry levy. The Commission is committed to consultation on the Commission's work plan and future budgets and is exploring options with industry and other stakeholders.

6. Preferred option

It is proposed to charge petroleum tenure holders an annual levy based on the number of sub-blocks comprising the tenure. A sub-block is a standard sized area of land some number of which comprises any one tenure.

The levy would apply to PL tenures, and also to those ATP tenures (granted or under application) within areas specified in an approved EIS for gas field development. There would be no levy for ATPs other than those specified above, as they do not generate significant costs for the Commission.

In order to fairly apportion costs between the tenure holders, the levy structure would comprise three separate charges, only one of which would apply for any sub-block. The differentiation is proposed in order to align the charges paid with the extent to which the water extraction activity or planned activity on the tenures impacts on the cost of activities that the Commission needs to carry out. The bulk of the Commission's costs relate to the CMA.

Within the CMA, the bulk of the Commission's activities relate to recent or planned CSG development, rather than the less water intensive conventional gas developments. In summary the three charges would apply as follows:

- Charge No 1 would apply to the sub-blocks of tenures outside the CMA.
- Charge No 2 would apply to sub-blocks of tenures inside the CMA, to the extent that the sub-blocks are used or are intended for use for conventional petroleum and gas production.
- Charge No 3 would apply to sub-blocks of tenures inside the CMA, to the extent that the sub-blocks are used or are intended for use for CSG production.

The levy would be set at the beginning of each year, based on the approved budget for the year and the number of relevant sub-blocks existing at July 1 of the year. The budgeted costs would be apportioned into three parts to be collected through the three charges. The apportioned charges would be divided by the number of sub-blocks to which the separate charges would apply.

Where the amount of the levy apportioned to a petroleum tenure holder is more than nil, the chief executive officer of the Commission would send a notice to the relevant petroleum tenure holders as soon as practicable after 1 July each year. The notice would state:

- The tenures and number of sub-blocks to which the levy is being applied;
- The relevant financial year;
- The levy period to which the notice applies;
- The amount of levy payable by the relevant petroleum tenure holder;
- The day by which the levy amount must be paid (the due date); and
- The way in which the levy must be paid.

The levy would be invoiced quarterly.

There would be a delay in the sending out of invoices for the 2011–2012 financial year until the regulation is finalised. Consequently the above notice would be given as soon as practicable after the regulation takes effect and the levy would be payable on the remaining quarters for the financial year on a pro rata basis (i.e. if for example there are two quarters remaining in the 2011–2012 financial year after the notice is given half the levy would be payable on each quarter).

The Water Act requires that the budgets for the underground water functions of the Commission are determined in consultation with a relevant advisory body and approved by the Minister. However, the Commission is currently operating under a budget approved by government, and funds provided by government. The approved budget for 2010–11 is \$3.32 million (a part year) and the approved budget for 2011–12 is \$4.52 million (a full year).

The levy is to commence in the 2011–12 financial year. It is proposed that the regulation specify the Commission's estimated costs for the financial years 2010–2011 and 2011–2012 in the amounts of the approved budgets for those financial years and that the consultation and approval process in section 360FA(5) of the Water Act be followed in relation to the financial year 2012–2013 and thereafter.

For each of the first three years of the operation of the levy, in addition to the charge for the costs for the year, the charge will include a charge for one third of the charge of the costs incurred by the Commission for 2010–11. Table 1 provides an estimate of the levy for 2011–2012.

Amendments to Section 360FA of the Water Act will be promoted separately to enable the regulation to provide for these arrangements for the commencement of the levy. The proposed amendments are as follows:

- Provide that the Commission be enabled to recover its costs for carrying out its functions under Chapter 3 of the Water Act for the 2010–2011 and 2011–2012 financial years by way of the levy and that the estimated costs for those years are not subject to the requirements under section 360FA(5) of the Water Act.
- Provide that the Commission's estimated costs for the 2010–2011 and 2011–2012 financial years will be as prescribed in the regulation.
- Provide that, in the event that further funding is required for the financial year 2011–2012 the Commission may obtain that extra funding by following the existing process set out in Section 360FA including section 360FA(5).
- The levy to be imposed on tenure holders for the financial years 2011–2012, 2012–2013, and 2014–2015 may include in each year one third of the costs of the Commission's functions under Chapter 3 of the Water Act for the financial year 2010–2011, and a regulation may impose the obligation to pay the levy accordingly.

The Commission will establish an advisory body in accordance with s360FA of the Water Act to consult on budget matters and planned expenditure for 2012–13 and future years. Should supplementary funding be required during a year, consultation and approval would be carried out in accordance with s360FA, and a supplementary levy would be applied over the remaining quarters of the year.

7. Consistency with other policies and regulation

7.1 National Competition Policy

The guiding principle of the Competition Principles Agreement, under the National Competition Policy, is that legislation should not restrict competition unless it can be demonstrated that the:

- Benefits of the restriction to the community as a whole outweigh the costs; and
- Objectives of the legislation can only be achieved by restricting competition.

The proposed industry levy does not restrict competition and is consistent with the Competition Principles Agreement. The impacts of water extraction by petroleum tenure holders can affect groundwater resources that support water users and environmental assets such as springs. There is a strong community interest in the long term impacts being carefully assessed and management strategies developed on a regional basis. The proposed levy of tenure holders applies to tenure holders on the basis of costs, and applies equally to groups of tenures.

7.2 Fundamental legislative principles

The Legislative Standards Act 1992 requires that legislation has sufficient regard to rights and liberties of individuals and the institutions of Parliament. The proposed levy framework is consistent with fundamental legislative principles.

8. Implementation, evaluation and compliance support strategy

The government would establish the levy by amending the *Water Regulation 2002* in accordance with the provisions of the Water Act.

In relation to the 2012–2013 financial years onward, the Commission would consult with key stakeholders on the proposed budget, and on any need to change the ratio of apportionment of costs into the three component charges.

If a new CMA was established at any time, new charges would be established following the established principles.

The levy structure will be reviewed every three years.