

THE GROWTH AND CONTRIBUTION OF THE OIL INDUSTRY TO THE ECONOMY

Hon David Butcher
Minister of Energy

Good morning and welcome to the 1989 New Zealand Oil Exploration Conference. It is with great pleasure that I open this third major New Zealand oil exploration conference which is being hosted by the Ministry of Energy with sponsorship from the Petroleum Exploration Association of New Zealand (PEANZ). This is the most ambitious oil exploration conference hosted in New Zealand so far.

I am especially pleased to see the number of overseas representatives attending. This reflects the international nature of the New Zealand oil exploration industry. It also shows the increasing interest explorers have shown in New Zealand over the last few years and, of course, the recent successful discoveries made. The theme of this year's conference: *Towards Maturity: An Industry in Growth*, reflects this.

Today I want to discuss the growth and contribution of the industry to the economy. I believe the Government's economic reforms have had a positive effect on your industry and the energy sector in general. I will also focus on two issues of particular concern to your industry; the taxation regime for petroleum mining and the Resource Management Law Reform programme.

OIL EXPLORATION PLAYS IMPORTANT ROLE IN ECONOMY

The New Zealand oil exploration and mining industry is very small on a world scale but increasingly it is playing a more and more important role within the New Zealand economy. In the last ten years the industry has had a remarkable growth. In 1979 there were only five prospecting licences. By 1988 this had grown to 54. There are presently 44 prospecting licences. In 1979, there had been just 554 kilometres of seismic shot, compared with 3584 kilometres in 1988. This represents a 500% increase in activity in this ten year period.

In the last three years there have been 11 to 15 wells drilled annually, compared with less than four per year in the late 1970s and early 1980s. In 1979 there were just three mining licences. Today, there are ten mining licences and two applications currently being assessed. Five fields are presently producing. In 1988, New Zealand fields produced 1402 thousand tonnes of oil and 174 billion cubic feet of gas.

Indigenous gas supplies nearly 30% of the country's energy needs and indigenous oil nearly 10%. Indigenous oil and condensate produced now meet 37% of oil consumption requirements. If you add synthetic petrol and CNG and LPG supplies, between 55 to 60% of New Zealand's oil and transport fuel needs are being met by your industry. This is all to the benefit of the New Zealand economy.

A MARKET DRIVEN ECONOMY

Oil exploration is a very exciting industry, but one which involves considerable risks. There can be bonuses and unexpected outcomes. The oil and gas discovery made at Waihapa in February 1989 typifies this.

Because your industry is market driven it is responsive to economic changes both internally and internationally. In this regard, it fits in easily with the Government's overall economic policies.

Since 1984 we have introduced a series of reforms aimed at making the economy more responsive to the marketplace. Prior to 1984 there was hardly any part of the New Zealand economy that was not tied down by regulations, restrictions and red tape. Deregulation and consequent restructuring have been major policy thrusts of the Labour Government throughout all sectors of the economy.

REFORMS FOCUS ON ENERGY SECTOR

A major objective has been the *freeing up* and restructuring of the energy sector. The Government has focussed attention on the energy sector because of the key role it plays in the economy. Because it is so central to wider economic efficiency, the energy sector is the key to the rapid achievement of enhanced national efficiencies and associated social spin offs.

The Government's aim in promoting deregulation and restructuring is to improve resource use and resource investment decisions. This is done by encouraging independent, commercially orientated decisions. With this aim in mind, the Government's direct involvement in the energy sector has been wound down over the last five years. In the petroleum exploration industry, Government has decreased its involvement from a position of financing about 40 % of investment from 1979 to 1985. It participates in most of the joint ventures now exploring New Zealand's oil and gas resources but for the most part as an 11% non-contributory partner.

PETROLEUM INDUSTRY REGULATORY ENVIRONMENT

The Government has also reviewed the regulatory environment the energy sector operates in. In line with its overall reform policies, it has strived to remove unnecessary legislation which in the past may have hindered competition or directed investment into the wrong areas.

In the petroleum industry, regulations have two main functions. The first is to ensure a safe working environment.

The second is the protection of the natural environment to allow for the monitoring of exploration and mining activities and to protect the property rights of both the licence holder and land occupier. There are no regulations affecting market decisions or access opportunities.

It is important the industry is assured that this Government has virtually no restrictions on overseas companies becoming involved in New Zealand exploration and mining activities. No favouritism is shown towards the New Zealand players. It is a policy which is very different from regimes adopted by other countries.

The industry should also be aware that there are no restrictions on exporting oil. In fact, indigenous oil and synthetic petrol are both presently successfully being exported.

I would now like to turn my attention to two important reviews affecting your industry which I know there is much interest in. The first is the review of petroleum taxation and the second Resource Management Law Reform.

PETROLEUM MINING TAXATION

As you are aware, the Government has had petroleum mining taxation under review since early 1987. The present taxation regime was set in place in the early 1980s and includes considerable incentives to promote petroleum exploration.

The Government now considers tax incentives for a particular industry no longer acceptable. Our present objective with petroleum taxation reform is to tax investment in petroleum mining more neutrally, relative to investment in other sectors of the economy. The Government is opposed to taxation driving investment decisions in the same way that it is opposed to regulations driving decisions in the market place.

In 1988 the Taxation Reform No. 4 Bill was introduced which outlined the Government's thinking at the time. Strong opposition to this Bill was expressed by your industry. The Government took note of that level of concern and asked officials to consider petroleum mining taxation matters further. There has been more work done and recently the Treasury referred to the industry via PEANZ an update on its thinking about petroleum mining taxation reform. Comments are presently being sought and I would encourage the industry to be positive in its comments.

One of the most controversial matters in the taxation treatment of petroleum exploration concerns the treatment of unsuccessful wells. I can tell you that subject to a satisfactory position being reached on the other elements of the taxation reform, it is expected that the Government will agree to exploratory well costs being deductible according to the following rules.

Once a well has been sealed and abandoned and the explorer has filed a statutory declaration stating there is no intention of either utilising the well or of applying for a mining licence based upon any deposit of petroleum discovered in the sealed and abandoned well, the deduction will be available.

RESOURCE MANAGEMENT LAW REFORM

Another issue which will have direct impact on your industry is the Resource Management Law Reform process which is now nearing completion.

For the petroleum industry the new procedures being proposed are not greatly different and will involve you in fewer changes than for your colleagues in the minerals and coal industries.

You will probably have already heard of the most significant changes proposed. These include the devolution of most environmental responsibilities to local government, the changes to the rights of the surface and Crown land owners, changes to the regulations of health and safety, and a review of the management and pricing of Crown mineral and energy resources. For those of you who are not familiar with the Government's reform proposals in this area will find Joan Allin's paper most informative.

DEREGULATION AFFECTS WHOLE ENERGY SECTOR

In other energy areas, involvement by the Government in electricity generation and coal production has been transferred to corporations with independent boards making the day to day and long-term planning decisions. The Government has also announced its intention to sell the Coal Corporation.

At the retailing level, the Government has directed considerable effort to deregulation. The oil retailing industry has been fully deregulated and there has been considerable deregulation of the electricity generating and supply industry.

The latter has made it possible for Electrical Supply Authorities to establish generation facilities in competition with Electricorp. I am aware of several investigations for local gas-fired power stations. There is also considerable gas/electricity co-generation potential and I know these options are being investigated. This, of course, provides new markets for your industry. Further deregulation of electricity retailing is under review and so is the deregulation of the gas retailing industry. This is an important issue for your industry as it could have a significant effect on the future development of gas deposits.

The gas industry is presently controlled by a considerable number of regulations. Only those holding franchises are allowed to supply certain areas and franchise holders are compulsorily required to supply consumers. The Government is concerned that this situation may not be resulting in the most competitive pricing and supply and this may be hindering conversions to gas and greater use of this fuel. The main objective of the Government's drive to deregulate the gas industry is to realise the social and economic welfare gains from increased economic efficiency.

In order to achieve this we see that a vital prerequisite is a more competitively neutral environment where market forces are free to operate without the State playing favourites. It presupposes that competition from new entrants is both permitted and feasible. As a first step in this direction the Government is removing as many barriers to competition as it possibly can. This includes the removal of exclusive franchises and price controls.

These decisions are complex and the implications of them need to be fully assessed before implementation can occur. Gas supply is a natural monopoly and caution is needed in any changes proposed for this industry.

One of the most important considerations is access to pipelines, both high pressure and those for local reticulation. Officials have been working on gas deregulation for some time and I am hoping that final recommendations will be with me shortly. Deregulation of this industry has been delayed in order to take account of other reviews going on in parallel which affect gas sector activity. These include the Resource Management Law Reform programme and the reviews of the Commerce Act and Occupational Health and Safety Legislation.

GOVERNMENT REORGANISATION LEADS TO REFORMS

Many of the reforms have been prompted by the Government's reorganisation of its core responsibilities. The government's aim is for an integrated approach to be taken across sectors on matters such as occupational health and safety and for like land uses to be similarly assessed. At the moment, resource uses are all differently assessed and there is no consistency of treatment. Many resources have their use regulated by one Act and one agency.

The petroleum exploration and mining industry on the other hand has always required multiple consents before development proceeds. The government considers it more appropriate to regulate aspects of all resource uses consistently and neutrally, by having agencies regulating on a function basis. Your industry will notice the changes most in the areas of health and safety and the control of pollution and hazardous substances.

One agency and one Act will regulate occupational health and safety and another one will regulate pollution and hazardous substances. These separate agencies will regulate all industries which require the application of these constraints. This will improve the neutrality with which activities are regulated. It will also ensure that the people managing those activities in the public sector are accountable for the achievement of one objective which does not conflict with any other regulatory objective.

DISESTABLISHMENT OF THE MINISTRY OF ENERGY

The disestablishment of the Ministry of Energy is part of this overall rationalisation of Government activities. From December 1, the Ministry will be merged with the Ministry of Commerce. However, there will continue to be an Energy Division and a Minister of Energy. This will ensure a continuing source of advice on energy and minerals issues and will allow the government to remain well briefed on issues of concern to the sector. It reflects the fact that the competition and market analysis work undertaken by the MOE has a close parallel in the work of the new Ministry of Commerce.

The key reason for the merger has been the Government's continuing drive to reduce the cost of Government by reducing corporate overheads rather than reducing the range and standard of services which are provided. In particular, the information base held within the Ministry of Energy will continue as a necessary adjunct to its role in mineral and energy resource management.

PETROLEUM RESOURCE MANAGEMENT IN THE NEW DIVISION

Under the new Resource Management legislation, the new Energy Division's role in resource management will be more active. Resource managers will be publicly accountable for the achievement of the objectives of their legislation. Those objectives include the allocation of rights in a way which will create an efficient market and the recovery of an equitable share of the economic rent arising from the development of the Crown's mineral and energy resources. The division will be required to prepare Resource Management Strategies which will specify the methods by which particular resources are priced and allocated. In preparing these strategies, they will be required to have regard to the depletion rate implications of their choices. This will be more important for some resources than for others.

Flexibility in the choice of allocation and pricing methods is necessary to take account of the diverse characteristics of the Crown resources being managed under the one Act and the different characteristics of the markets for them. You will have the opportunity to be involved in strategy formulation. This reform typifies the changes the Government is making to New Zealand's business environment. We are creating an economy where business decisions will not be distorted by Government policies.

ECONOMIC REFORMS ARE WORKING

These policies are working. The latest National Bank Business Outlook survey shows that for the fifth month in a row there has been an improvement in business confidence. It notes that the tone of David Caygill's recent Budget and the expectation of political stability until the next election have resulted in greater certainty with respect to economic policy and the outlook for business activity. It is very encouraging to see that all five sectors of the business community have indicated a rise in confidence for the second time in recent months. I agree with the Bank's prediction that political stability, falling interest rates and the expectations of a steady increase in domestic economic activity should add up to a period of sustained economic recovery.

CONCLUSION

I want to end today on a positive note by looking at future prospects for your industry in New Zealand. I am sure the petroleum exploration industry will benefit from the economic recovery I have just outlined. I expect that by this time next year there will be a new resource management regime in place. I am also hopeful that deregulation of the gas industry will be in place and that the petroleum taxation regime will be defined.

I look forward to the continuation of the constructive input which has typified your industry's submissions to date. They have made an impact on those responsible for the preparation of the new legislation and on Ministers, and will continue to do so in the future.

Once again, it is with great pleasure that I welcome you here to Queenstown. I wish the conference every success and hope you all benefit greatly from meeting with colleagues and listening to the papers being delivered.