

NEW ZEALAND

RECENT CHANGES AND DEVELOPMENTS IN THE NEW ZEALAND PETROLEUM INDUSTRY*

Government Review of Petroleum Exploration Regime

The recently announced 2006 government budget allocated an additional NZ\$6 million to the geotechnical data acquisition programme across prospective petroleum basins. This funding boost is proposed as a way to encourage more petroleum exploration in New Zealand. On 22 May 2006 the government subsequently announced that this additional funding would partly be used to finance work aimed at gaining a greater understanding of the known fields within onshore Taranaki.

On 25 May 2006, the Ministry of Economic Development convened a meeting with members of the industry to discuss industry proposals for new initiatives to encourage increased exploration. At the meeting the government noted that while the long term focus remained on large exploration in offshore frontier basins to replace Taranaki reserves there was also a need to consider shorter term initiatives in onshore or nearshore Taranaki which could be brought into production quickly and, therefore, defer the need for any decision on imported gas (CNG or LNG).

Members of the industry present at the meeting pointed out some of the barriers to petroleum exploration in New Zealand. The high cost of exploring and developing petroleum discoveries was compared to other countries like the United States. This difference was attributed to the economic impact of comparatively higher costs and lower revenue from domestic gas in New Zealand.

Industry participants highlighted ways in which the government could improve the petroleum exploration regime in New Zealand, including:

- Bringing down barriers to exploration and production, especially economic barriers;
- Eliminating discriminatory tax provisions which are unique to the petroleum industry, for example reviewing and updating the amortisation methodology;
- Improving access to equipment (in particular, the potential for the government to be involved in the acquisition of rigs was mooted);
- Changing permit conditions to be more flexible and allow more seismic exploration before drilling decisions need to be made;
- Clarifying and, where necessary, adopting legislative amendments to remove commercial uncertainties associated with section 41 of the Crown Minerals Act 1991;
- Improving the royalties regime, for example by eliminating the ad valorem royalty (AVR) rate;
- Stimulating infrastructure development in remote exploration and production areas;

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- Expanding the number of skilled workers available to the industry; and
- Providing a better and more reliable database of gas reserves.

Gas Industry – Pending Release of Policy Papers

Three major policy papers are close to release by the Gas Industry Company (GIC), the industry body of the gas sector (established under the Gas Act 1992). The papers are part of GIC's work programme required by the Government Policy Statement on Gas Governance of October 2004. They are:

- An updated paper, following industry feedback to an initial paper released last December, which examines the best mechanism (rules versus contracts) for switching customers between gas suppliers (released on 19 June 2006).
- A discussion paper on options to improve current reconciliation arrangements; and
- An options paper on open access to the gas network.

These papers will generate much debate within the industry and will be the subject of a future update.

Proposed Changes to the Tax Treatment of Expenditure on Geothermal Wells

The Taxation (Annual Rates, Savings Investment, and Miscellaneous Provisions) Bill introduces changes to the tax treatment of expenditure on geothermal wells. These amendments are designed to remove uncertainty about the deductibility of capital losses arising from unsuccessful wells drilled in New Zealand. The proposed changes respond to tax-related problems identified by the industry.

The Bill proposes that the owner of a geothermal well makes a decision whether the well is a "failure" i.e. whether there is a reasonable prospect of the well being used in an income-earning process. This decision determines the tax treatment of the costs of the well, as outlined below.

If the well is a failure:

- A deduction for its cost or the remaining book value will be allowed;
- If it is subsequently sold or used, the value of the well will be written back and will be assessable for income tax;
- When sold, the write-back value will be the lesser of its original cost or the price received; and
- When subsequently used, the write-back value will be the amount of the previously allowed deduction.

If the well is a success:

- The costs will be depreciated over the estimated useful life of the well from the date the well is completed;
- If it is subsequently sold or written off, a deduction for any losses will be allowed; and

- If the price received for the well exceeds its tax book value, the excess up to the original costs of the well will be assessable for income tax.

Submissions on the Bill are due on 7 July 2006.

Conclusion

These proposed changes and developments in the energy industry in New Zealand provide an exciting platform for business investment and development. From oil and gas exploration to geothermal to gas distribution, the government and the relevant industries are working hard to create vibrant, profitable industries.