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Coal Seam Gas Exploration and Production in NSW: The new access argument

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Coal Seam Gas Exploration and Production in NSW: The new access argument[1]

As coal seam gas (CSG) and coal are by their nature co-located resources, legislative arrangements for the production of each of them requires careful thought and an appropriate and consistent legislative regime. This paper examines elements of the overlap regime in New South Wales (NSW), such as it is. We explain how we believe the regime to work from a legal point of view and then suggest some legislative reforms.

Introduction

Industry & Investment NSW (I&INSW), the NSW government department that has primary responsibility for energy, has recently expressed this view about coal and CSG in NSW:

> *The coal industry comprises a large and mature coal mining industry, and a small but emerging coal seam gas industry. While the operations of the two industries are substantially different, there is significant scope for interaction between them. The locations of both industries are defined by the State's coal resources, and therefore they will have to operate in close proximity to each other, or within the same regions.*
>
> *Consequently, there is merit in a single Strategy for both industries which will enable the potential interaction between the two to be properly considered and managed, including any potential cumulative impacts.* [2]

NSW's limited conventional oil and gas history contrasts with its position as Australia's largest potential market for energy, particularly oil and natural gas.

It is not surprising that NSW has historically favoured coal exploration and production over CSG exploration and production. This is evidenced in the legislation and the administration of the overlapping tenements regime in NSW.

That regime, for the purposes of this paper, comprises principally the *Petroleum (Onshore) Act 1991* (Petroleum Act) and the *Mining Act 1992* (Mining Act). Both are administered by I&INSW. The Petroleum Act regulates the granting of petroleum titles for CSG in NSW, and the Mining Act regulates mining titles, including for exploration and production.

In Queensland, the overlapping tenements regime is, compared to that in Petroleum Act and the Mining Act in NSW, sophisticated, not to say demanding in its complexity. Access is allowed to the co-located resources by coal and CSG explorers and producers via a complex preference process that regulates, on the basis of established resources and by reference to a public interest test, who gets access first. In Queensland the rules are very clear, but they are very complex and leave significant decisions, in particular as to which party (coal or gas) is to get preference for production titles, to the Minister. Although at present Queensland's legislation does not require the Minister to make a 'preference decision' in any given period of time, there are now proposals[3] for imposed time limits - although those time limits are reasonably generous; even though the most straightforward preference decision will have a statutory time line of at least 27 months.

In NSW, it all happens in the instruments of tenure. Rather than regulating for coal/CSG overlaps in legislation, in NSW the management of overlaps is given effect in the conditions of grant of the overlapping tenements. The problem with this approach is that access to one or other of the co-located resources can effectively be prevented for the CSG producer, and favours coal in that reciprocal provisions are not included in the Petroleum Act.

The NSW scheme also requires some significant statutory interpretation in order to be understood. This is never a good situation if all parties want access to be certain from a legal perspective.

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[1] Jonathan Fulcher and Martin Klapper, Partners, HopgoodGanim Lawyers, Brisbane
[2] *NSW Coal and Gas Strategy Scoping Paper*, February 2011, page 3
[3] Consultation paper, *Review of overlapping coal and coal seam gas tenure,* DEEDI 2011

This paper examines the coal/CSG overlap regime in NSW, such as it is. We seek to explain how we believe the regime to work from a legal point of view, and then suggest some legislative reforms to better encourage the development of a CSG industry in NSW.

In February 2011, Planning New South Wales released the scoping paper on a 'NSW Coal and Gas Strategy.'[4] Although one of the areas the strategy is intended to address will be to 'facilitate sustainable development for coal mining and CSG industries and associated activities,'[5] the tone of the paper and associated material available on Planning NSW's website appear to focus much more on land access in the traditional sense – that is, the interaction of coal or CSG activities with other key stakeholders, particularly landowners.

This is not to suggest that there is anything wrong with that focus, but rather that it remains to be seen whether the strategy leads to substantial legislative reforms relating to the competing claims to access to coal and CSG in NSW. In the meantime industry must deal the legislative regime as it stands, and it is the purpose of the next part of this paper to deal with that.

The Mining Act and the grant of petroleum rights and coal leases

First, let's be clear about the terminology. Under the Petroleum Act, 'petroleum' is defined in this way:

> *(a) any naturally occurring hydrocarbon, whether in a gaseous, liquid or solid state; or*
>
> *(b) any naturally occurring mixture of hydrocarbons, whether in a gaseous, liquid or solid state; or*
>
> *(c) any naturally occurring mixture of one or more hydrocarbons, whether in a gaseous, liquid or solid state, and one or more of the following, that is to say, hydrogen sulphide, nitrogen or helium, carbon dioxide and water,*
>
> *and includes any substance referred in paragraph (a), (b) or (c) that has been returned to a natural reservoir, but does include coal or oil shale or any such substance prescribed to be a mineral for the purpose of the Mining Act 1992*[6]

Correspondingly, 'mineral' is defined as 'any substance prescribed by the regulations as a mineral for the purposes of this definition, and includes coal and oil shale, but does not include uranium or petroleum'. 'Petroleum' has the same meaning as it has in the Petroleum Act.[7]

The *Mining Regulation 2010* (section 4 and schedule 1) lists the substances that are to be regarded as 'minerals' for the purpose of the Mining Act. Neither CSG nor petroleum are mentioned.[8] So, at the outset, at least from a definitional perspective, the rules are clear - petroleum includes (by reference to the extensive definitions listed above) CSG.

The complication to which the NSW legislative regime gives rise, and that is the subject of this paper, arises from section 78 of the Mining Act. Section 78(1) says this:

> *'The holder of a mining lease for coal may apply for the inclusion in the lease of petroleum'*

That, fundamentally, is why we say that the legislative regime for coal/CSG overlaps in NSW favours coal. There is no reciprocal provision in the Petroleum Act. The coal mining lease holder is simply entitled to apply and (with limited exceptions) to have the right to mine petroleum under a coal mining lease.

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[4] Available on www.planning.nsw.gov.au
[5] Strategy, page 8
[6] Petroleum Act, section 3
[7] Mining Act, dictionary
[8] 'Geothermal energy' is prescribed as a mineral for the purposes of the Mining Act, but that is a topic for another paper

The process works this way:

(a) Under section 78(1), the holder of the coal mining lease applies for inclusion in the lease of petroleum.[9]

(b) The Minister **must** refuse the application if 'the land to which the application relates' is within the NSW adjacent area (essentially, offshore land) or if it is 'is subject to a petroleum exploration licence or a petroleum mining lease granted under the' Petroleum Act.[10]

(c) The Minister can impose conditions on a direction that a mining lease include petroleum.[11]

It is therefore possible for the Minister to (for example) direct that petroleum be added to a coal mining lease for the purpose of enabling the coal mining lease holder to explore for and extract CSG that is found in association with coal in mineable coal seams, but that this right is not to extend to conventional oil and gas reserves.

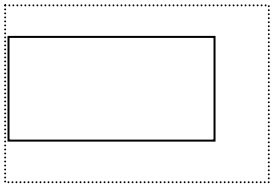
An immediate difficulty arises in interpreting section 78(4)(b) of the Mining Act which says that:

> *'the Minister must refuse an application if the land to which the application relates... is subject to a petroleum exploration licence or a petroleum mining lease granted under the' Petroleum Act.*

It is not clear whether the phrase 'the land to which the application (for the inclusion in the coal mining lease of petroleum) relates' in the first part of section 78(4) is a reference to the **whole** of the land in the coal mining lease area, or only to a **part** of it.

If the first meaning is correct - that is, if the whole of the coal mining lease must be subject to the petroleum tenure - then the Minister **must** refuse an application under section 78(1) **only if** the entire coal mining lease is subject to some form of petroleum tenure. Consider this example:

Example 1



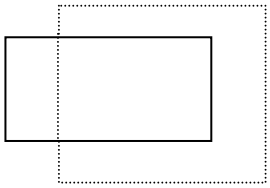
In example 1, the entire coal mining lease is subject to a petroleum exploration licence granted under the Petroleum Act, and consequently the Minister must refuse an application by the coal mining lease holder under section 78(1) of the Mining Act for the coal mining lease to extend to petroleum.

Consequently, if the Minister in response to an application under section 78(1) of the Mining Act were to direct that a coal mining lease applies to petroleum then the direction would be invalid because under section 78(4)(b) the Minister must refuse the application.

However, on this same interpretation the Minister can properly direct that a coal mining lease that only partially overlaps with petroleum tenure extend to petroleum. Consider examples 2 and 3.

[9] Mining Act, section 78(1)
[10] Mining Act, section 78(4)
[11] Mining Act, section 78(5) including the types of conditions mentioned in section 78(6)

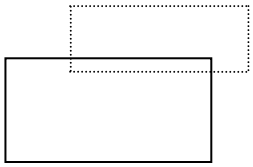
Example 2



Coal mining lease ————

Petroleum exploration licence ·····

Example 3



Coal mining lease ————

Petroleum exploration licence ·····

On an interpretation of section 78(4) based on this first meaning, because less than the whole of the coal mining lease overlaps with a petroleum tenement, the Minister is not constrained under section 78(4) of the Mining Act from making the declaration and the Minister could quite properly direct under section 78(3) that the coal mining lease apply to petroleum – notwithstanding the partial overlap with the petroleum exploration tenement.

Neither the Petroleum Act nor the Mining Act says what happens then. In theory each of the coal mining lease holder and the petroleum tenement holder have concurrent rights to explore for and (subject to the type of petroleum tenure that has been issued) produce CSG.

There is another interpretation that can be placed on section 78(4). This is that, if a coal mining lease holder makes an application under section 78(1), and **any part** of the coal mining lease is subject to a petroleum tenement, then the Minister must refuse the application.

To apply that to example 2 above, because the petroleum exploration licence overlaps only a part of the area of the coal mining lease, on this interpretation the Minister must refuse the application under section 78(1) for the coal mining lease to extend to petroleum.

The consequence of this interpretation is that the coal mining lease holder cannot apply under section 78(1) for the coal mining lease to extend to petroleum where even **the smallest part** of the coal mining lease overlaps with a petroleum tenement, and if the Minister purports to make a direction contrary to this reading of section 78(4) that direction would be invalid because the subsection says that the Minister must refuse the application. It would be beyond power (on this interpretation) for the Minister to make any variation.

Though the arguments and alternative approaches to the interpretation of section 78 that we have described so far in this paper appear legalistic in nature, they have a very direct and practical effect for both coal mining lease holders and CSG explorers and potential producers.

Both of the interpretations discussed above create adverse and probably unintended consequences for both the coal miner and the CSG explorer/potential producer that can make it more difficult for each of them to access resources in their tenement areas and create significant levels of uncertainty, in particular in the circumstances described in examples 2 and 3.

The 'new' access argument that is in the title of this paper proposes an interpretation of section 78 that resolves that uncertainty.

We think that it is important to address the uncertainty, from the perspective of each of the coal mine and CSG explorer/producer.

The coal miner can have a genuine and proper interest in having its coal mining lease extend to petroleum. Methane gas must be removed from underground coal seams before mining in those coal seams can commence, and methane removal must continue while the coal mine operates. There is nothing intrinsically wrong with the concept that a coal mining lease holder should have rights to extract and commercialise CSG from mineable coal seams - indeed that concept is also enshrined in Queensland in the more complex and prescriptive Queensland legislative regime.

The coal mining lease holder will, however, wish to have certainty about the circumstances in which it is entitled to have the coal mining lease apply to petroleum, and it will want to be sure that if the Minister makes a direction under section 78(3) that the direction is valid. This is more than a sterile legal argument: if a coal mining lease holder extracts and commercialises CSG on the strength of a Ministerial direction under section 78(3) that is invalid, then that extraction and commercialisation of that CSG is at the very least a breach of the Petroleum Act (and perhaps the Mining Act) and can even be characterised as theft of the State's CSG resources.

Conversely, the CSG explorer and producer will want to know that its access to CSG resources is not unreasonably or unduly limited in circumstances where for example it might have invested considerable sums of money in exploring for petroleum in areas that are potentially affected by a declaration of section 78(3). Neither the CSG explorer/producer nor the coal miner benefits from the uncertainly inherent in the two alternative approaches to the interpretation of section 78(4) that are discussed earlier in this paper.

Statutory interpretation: a dynamic purposive approach

The now familiar *Project Blue Sky* case gives us this guidance about how the interpretation of a statute is properly approached.

> *(It is necessary) 'to give the words of a statutory provision the meaning that the legislation is taken to have intended them to have. Ordinarily, that meaning (the legal meaning) will correspond with the grammatical meaning of the provision. But not always. The context of the words, the consequences of the literal or grammatical construction, the purpose of the statute or the canons of construction require the words of a legislative provision to be read in a way that does not correspond with the literal or grammatical meaning.*[12]

Reference to 'intention of the legislature' here is not to any particular state of mind of the parliamentary draftsperson or individual legislators, or even of the legislature as a whole. It refers to what the words of the statute mean, not what the legislature might have intended them to mean.[13] In other words, we have to construe the words of section 78 of the Mining Act without attempting to insert or infer words to aid in the interpretation of the provision.

Fortuitously, the NSW parliament gives us some further guidance about the way the interpretation of section 78 should be approached. The *Acts Interpretation Act 1987* (NSW) provides:

> *'in the interpretation of a provision of an Act or statutory rule, a construction that would promote the purpose or object underlying the Act or statutory rule (whether or not that purpose or object is expressly stated in the Act or statutory rule or, in the case of a statutory rule in the Act under which the rule was made) shall be preferred to a construction that would not promote that purpose or object'.* [14]

So what, then, is the **purpose** of section 78 of the Mining Act?

The purpose of section 78 of the Mining Act

The Mining Act, section 3A says that:

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[12] *Project Blue Sky v Australian Broadcasting Authority* (1998) 194 CLR 355 at 384
[13] *Wik v State of Queensland* (186) 141 ALR 129 at 220
[14] *Acts Interpretation Act 1987* (NSW), section 33

'the objects of this Act are to encourage and facilitate the discovery and development of mineral resources in New South Wales, having regard to the need to encourage ecologically sustainable development, and in particular:

To provide an integrated framework for the effective regulation of authorisations for prospecting and mining operations; and

To ensure an appropriate return to the State for mineral resources.'

Unfortunately the Petroleum Act does not contain the statement of objects or purpose. For present purposes, however, section 3A gives us enough to be getting on with.

Considering section 78 specifically, its purpose clearly is to allow a coal miner to apply to include within the coal mining lease the right to produce petroleum.

Sections 78(4), (5) and (6) are designed, at least in part, to enable the Minister to deal with the prospect that overlapping petroleum interests exist by prohibiting the Minister from making a direction in at least some overlap situations, and by placing conditions on a direction for a coal mining lease to extend to petroleum where the direction would impact adversely upon rights granted under a petroleum tenement that overlaps a coal mining lease.

In this sense, section 78 constitutes the overlapping coal and CSG regime in NSW. It is significant to note that section 78(4) has not been amended since 1996. Up to that time, the CSG industry was in its infancy. Little overlap in practice could then have been expected between conventional petroleum and coal.

The problem identified above in construing section 78(4) has perhaps not therefore arisen until recently. Since 1996, CSG exploration and development has expanded exponentially and overlaps between practical, on the ground petroleum and CSG interests have become more prevalent.

In Queensland, a new and complex regime was enacted in 2004 to address such overlaps. In NSW, where the CSG industry has lagged well behind Queensland, legislative development has not kept pace with the new technology. As a result, it is necessary to interpret section 78 in a way that takes account of the new circumstances.

We propose that the problem to be solved in interpretation of section 78(4) - that is, whether the Minister **must** refuse any and all applications under section 78(1) for a variation of the coal mining lease when **a part, but not the whole**, of the coal mining lease is subject to petroleum tenure can be addressed by applying section 33 of the Acts Interpretation Act, the High Court's comments in the Project Blue Sky case and the objects of the Mining Act section 3A.

Adopting a purposive approach to section 78, we consider that the purpose of the provision is to allow the efficient extraction of both coal and CSG resources, while at the same time ensuring that different tenement holders are not granted access to the same petroleum resource. Any other outcome results in arguments about who has rights to claim property in petroleum once it is extracted, and indeed to conduct operations to extract that petroleum in the first place.

The access argument that we describe below applies only where a coal mining lease holder makes an application under section 78(1) of the Mining Act for a coal mine lease to extend to petroleum, and where part but not the whole of the coal mining lease overlaps with a petroleum tenement granted that is granted under the Petroleum Act.

If there is no overlap with a petroleum tenement, section 78(4) cannot apply and the Minister can obviously give the direction.

Where the entire coal mining lease is overlapped by a petroleum tenement, section 78(4) will clearly apply (example 1 above) and the Minister cannot make the variation (and if the Minister purports to do so, then the variation will be invalid).

The focus, then, is where a partial overlap exists (examples 2 and 3 above).

The interpretation of section 78 that we propose is this:

- Under section 78(3)(a), the Minister can give a direction only that 'the mining lease apply to petroleum' - the Minister cannot, for example, direct that the mining lease extend to petroleum over only part of its area. It is a once and for all direction.

- The Minister can, however, impose conditions under section 78(6). One of the conditions that the Minister can impose is 'the limitation of the right to prospect or drill for petroleum to part only of the mining area'.[15]

- Consequently we are of the opinion that section 78 operates so as to allow the grant of an application for variation to a coal mining lease that is partly overlapped by a petroleum tenement, providing the Minister imposes a condition under section 78(6)(a) that prohibits the coal miner from prospecting or drilling for petroleum in those parts of the coal mining lease that are subject to the overlapping petroleum tenement.

The difficulty with this approach is that, at first glance it appears inconsistent with section 78(4):

> *'the Minister must refuse an* ***application if the land to which the application relates... is subject to a*** *' petroleum tenement granted under the Petroleum Act.* (emphasis added)

As explained earlier in this paper, we consider that the purpose of section 78 is specifically to enable the Minister to deal with overlapping coal mining and petroleum interests where a variation to a coal mining lease would impact adversely upon rights granted under a petroleum tenement overlapping the coal mining lease. This interpretation of section 78 satisfies that purpose without straining the language of section 78(4)(b).

It is also consistent with the more general purposes of the Mining Act described in section 3A, particularly these objects:

- *'to encourage and facilitate the discovery and development of mineral resources in New South Wales'*

- *'to recognise and foster the significant social and economic benefits to New South Wales that result from the efficient development of mineral resources'*

- *'to provide an integrated framework for the effective regulation of authorisations for prospecting and mining operations'*

- *'to ensure an appropriate return to the state for mineral resources'*

The interpretation that we advance allows for the efficient extraction of resources in not prohibiting a coal miner from accessing petroleum over the area of the coal mining lease other than to the extent that another person has rights of access relating to petroleum, by imposing section 78(6)(a) conditions on the grant: at no time will two different tenement holders have access to the same resource.

It is a consequence, however, of this interpretation of section 78 that a variation to a coal mining lease which does not contain a condition prohibiting the prospecting or drilling for petroleum over those parts of the coal mining lease which are subject to an overlapping petroleum tenement will be invalid.

A case for legislative reform

Currently, I&INSW and its relevant Minister manage the conflict inherent in the current coal and CSG tenement overlap scheme by excluding from the petroleum tenure any land which is included in the coal tenure. A recent amendment to the standard conditions for grants of coal exploration tenements has included a requirement for the tenure holder to use reasonable endeavours to work cooperatively with any overlapping tenure holder. The coal tenure holder must try its

[15] Mining Act, section 78(6)(a)

best to enter into a commercial agreement (referred to in the conditions as a 'cooperation agreement' - see clause 33 of section E of the Exploration Licence Conditions 2010) about the following matters, which are not meant to be limiting:

- Access arrangements
- Operational interaction procedures
- Dispute resolution
- Information exchange
- Well location
- Timing of drilling
- Potential resource extraction conflicts
- Rehabilitation issues

We suggest that such 'best endeavours' arrangements have limited value in a commercial context. The lack of such an agreement despite 'every reasonable attempt' does not lead to any express consequences, nor does it address the issue central to this paper: access by different producers to the same land at the same time for the purposes of exploitation of different products, CSG and coal.

Our proposal, on the other hand, suggests there should be at least some consequences. It involves a 'use it or lose it' approach. We see no problem with keeping condition 33 of section E at the exploration stage. However, we propose that, if no such agreement is entered into by the coal explorer for the purposes of that condition, the consequence should be at production. If, at that time:

- the coal explorer (now producer) decides to seek inclusion of petroleum in the coal lease; and
- no agreement of the kind contemplated by condition 33 of section E of the standard Exploration Licence Conditions has been entered into;

then the coal producer should be given three options to choose from:

- Elect within a certain period, say, six months to exploit the petroleum resource.
- Farm out the petroleum rights to a CSG producer, within a certain period, say, six months.
- Lose the rights to a tender process to be commenced by the Government after that period.

Such consequences should not, of course, adversely affect the coal producer's ongoing rights to mine coal.

The benefits of this policy change would include the following:

- It represents incremental change on the current law, not a radical departure from it. The coal tenure holder would still be in the 'driver's seat'.
- It has built-in commercial incentives to reaching agreement and for the exploitation of both CSG and coal.
- It allows the Government to argue that both resources are being produced for the benefit of NSW.

- It requires limited Ministerial involvement (unlike the Queensland scheme) and allows maximum flexibility for the commercial players, within the parameters of a 'use it or lose it' approach.

The adverse consequences of such a policy change might include:

- concerns on the part of coal producers at the perceived loss of preferential access to CSG;
- landholders may object to the advent of two development interests with different exploration programs wanting access to the same land; and
- increased administration costs for the sector.

Summary

We set out examining the overlap regime for simultaneous access to coal and CSG by the different producers, and noted that these issues are managed at the tenement level. We examined what we think is the proper approach to the main provision dealing with this issue, section 78 of the Mining Act in NSW. We noted that any issue which requires extensive statutory interpretation to resolve the rights of the parties does not provide optimum certainty for coal and CSG producers in NSW. We then finished by suggesting some law reforms which may provide one possible solution to a problem which in other States has involved great statutory complexity and commercial attention.