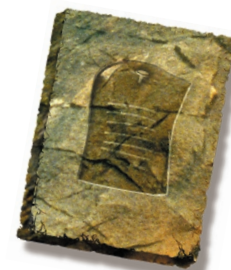


Development of a compliance policy for the Petroleum Act 2000



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Introduction

The *Petroleum Act 2000* was proclaimed on 21 September 2000 after a long consultation process which began in February 1996. As part of this process, and consistent with the openness and accountability principles the new Act embodies, it was expected that PIRSA would develop and publicly release a compliance policy.

Given the radical changes introduced in the new Act compared to the previous regulatory regime, it was felt that some time was needed to fully experience the new regulatory regime before developing a formal compliance policy. The Act has now been in operation for more than 18 months, and PIRSA has undertaken a research program to develop an appropriate compliance policy. PIRSA commissioned research on aspects of compliance and enforcement by David Cole (Cole Solicitors, Adelaide) and Dr Fiona Haines (Senior Lecturer, Department of Criminology, University of Melbourne), and this paper has relied to a significant degree on their research. These consultants provided advice on:

- the principles and current regulatory theory and strategies that should be considered when developing a compliance policy
- how the issue of conflict of regulatory aims might be addressed
- how licensees might be assessed for compliance status
- if reward-based compliance systems would be workable in this context.

It has also become evident that in some cases changes to the Act may be desirable to facilitate better compliance. Formal consultation on these changes will occur as part of a broader group of amendments to the Act proposed to be introduced in early 2003.

Principles of enforcement

The key concept underlying the enforcement of the Petroleum Act is that the basic responsibility for detecting and rectifying non-compliance lies with the licensee or individual, not the regulator.

It is also fundamental to the Act that stakeholder expectations (including building public trust) influence the setting of standards of compliance behaviour and the response to non-compliance. Consequently, PIRSA will undertake an extensive consultation process to seek acceptance of the policy by public interest groups and other government departments (see further details at the end of this paper).

PIRSA has established the following principles as a guide to developing and implementing a compliance policy:

- a commitment to review this compliance policy in consultation with appropriate stakeholders
- facilitate public access to the licensee's compliance reports and decisions relating to approval and enforcement
- taking action to maximise the future level of compliance but avoiding retribution where this will not lead to better compliance
- utilise the principal tools of education, encouragement and persuasion to achieve compliance
- be fair, predictable and consistent, but as flexible as possible
- reflect that the primary responsibility for compliance lies with the licensee or individual
- within the constraints of resources available, respond to all instances of non-compliance
- the response to non-compliance will reflect a balance between the potential or actual harm to the public good and stakeholder values

- aim to achieve licensee compliance with the minimum of resource expenditure by PIRSA.

The two major reasons a licensee may or may not comply are the licensee's capacity to comply (i.e. are sufficient knowledge and financial resources available to the licensee?) and the licensee's motivation to comply (i.e. will compliance deliver greater return to shareholders, or will public outrage to non-compliance reflect on the company?).

Capacity to comply is best assessed as an activity approval process, while motivation to comply will be assessed as the basis for the depth of PIRSA surveillance of activities being undertaken by licensees (i.e. the inspection and auditing effort directed to particular licensees and activities).

Assessment of capability (activity approvals)

PIRSA believes that a licensee's capacity in terms of professional competency of people and procedures should be assessed prior to the licensee undertaking the activities. If the licensee cannot demonstrate that it has the capacity to undertake the activity (i.e. there is an unacceptable risk of future non-compliance with requirements of the Act and conditions of the licence), then PIRSA believes that the activity should not be attempted, and approval will not be given.

At present, it is possible for certain activities undertaken by licensees to be classified as 'low supervision', which allowed the licensee up to 50% reduction in licence fees and relief from the obligation to seek approval for activities. 'High supervision' licensees are required to pay higher licence fees and seek approval for all activities. In practice, all production and pipeline licensees have been given 'low supervision' status and most exploration licensees (some

by licensee choice) ‘high supervision’ status. No discrimination to types of activities has occurred.

The original intention of this provision was to recognise that some licensees have a good track record and can be trusted to undertake future activities without PIRSA scrutiny or approval. This provision has proven to be administratively cumbersome. For instance, a high supervision licensee proposing to undertake multiple well drilling activities is required to demonstrate their ability to undertake and seek approval for each well, when it is clear that after assessing this for the first well and gaining approval, that the licensee could be trusted to drill subsequent wells. The same criteria are essentially applied generically to assess ‘low supervision’ operators.

As an incentive for companies to achieve ‘low supervision’ status and to recognise that such companies would require less government resources, part of the licence fees have been refunded for ‘low supervision’ licensees. In reality, it would appear that this financial incentive is only significant for production and pipeline licensees, and that the high cost to the licensee if their status were changed from low to high supervision would suggest it is likely that significant political pressure may be exerted to maintain low supervision status, and prevent a thorough review of the capabilities of the licensee. There is no provision to reclaim licence fees if the licensee had in fact a poor compliance record for that year.

It is proposed to simplify the activity approval system, and focus on assessment of the licensee’s capability to undertake types of activities (rather than seeking approval for each individual activity), and once that approval had been given, subsequent similar activities would be allowed to occur.

Broad criteria used to assess capability to undertake activities are provided in Table 1. These criteria are largely based on AS3806 (Compliance Programs) and AS4360 (Risk Management), and licensees will be encouraged to use these standards when developing a capability to undertake activities.

Table 1 Criteria used to assess the capability to undertake petroleum-related activities.

Criteria	Acceptable level to undertake activities
Operating work practices and procedures	Practical written and well-resourced practices and procedures exist for regulatory requirements, which include roles and responsibilities of management and staff, anticipating areas at risk of non-compliance, plans to deal with non-compliances, monitoring, recording and assessment of compliance, ensuring that compliance standards are incorporated into contracts etc., summary of regulatory requirements, and practical examples.
Compliance management system	Compliance monitoring, review, reporting and remedial action processes address regulatory requirements, and adequate corrective action processes are in place.
Risk management system	A comprehensive and professional risk assessment process exists which is integrated into relevant procedures and practices; includes appropriate and effective consultation and includes emergency response drills and plans where relevant.
Management responsibility and commitment to regulatory compliance	Key senior personnel can be identified who have major responsibility for regulatory compliance. Adequate resources are allocated to the compliance system.
Training and knowledge of employees	Effective induction and training against procedures provided to relevant employees and contractors, and licensee has access to appropriate skills and experience. Employees and contractors are aware of and understand their regulatory responsibilities, even when significant non-compliances occur.

Assessment of motivation (determining appropriate surveillance level)

The seriousness of the consequences of non-compliance for the State, rather than to the licensee, will be the main consideration in determining appropriate surveillance. Critical facilities or activities that may involve very sensitive environmental issues will always be closely examined, regardless of the previous performance or motivation of the licensee.

In other cases, the surveillance level will be assessed after considering the following factors.

Past compliance record

The consistency of a past compliance record compared to recent compliance is considered the more important guide to future compliance (good or bad). Licensees who do not have a rigorous compliance reporting system will be treated as having a poor compliance record (even if past compliance levels appear to be high), as it can only be concluded that the good performance has been fortuitous.

Compliance policy and resources

Compliance will be more likely where there is a compliance policy applied

at both management and operational levels. A policy in itself is not sufficient; there also needs to be evidence that it is adequately resourced.

Shared responsibility for compliance

Compliance responsibility needs to be balanced between senior management and individual operational personnel.

Sensitivity to stakeholder outrage at non-compliance

This depends on the nature of the non-compliance; for example, public interest groups would be expected to be most sensitive to environmental damage (e.g. oil spill), but might not be so concerned with technical data reporting non-compliances. In general, PIRSA would be seeking evidence that the licensee is open and proactive with stakeholders concerning its regulatory performance.

Financial pressure

A licensee who has an area of activity or facility under severe financial pressure (i.e. reducing market share, reducing asset value), or where environmental rehabilitation liabilities have become significant, would be perceived to be more at risk of non-compliance (i.e. resources to comply may be withdrawn by senior management).

Compliance will add shareholder value

Where compliance will reduce net costs for licensee or reduce competition (e.g. reduce insurance costs), there is a clear internal motivation to comply, regardless of external pressures.

Competing regulatory regimes

If the licensee is subject to other incompatible regulatory regimes, the licensee may be forced to choose which they will comply with. The regulatory regime which is perceived to apply the least pressure to comply will be the one most likely to be compromised in this situation.

Enforcement tools available under the Petroleum Act

A range of enforcement tools is available under the Petroleum Act, and these tools can be grouped into categories of severity for the licensee. Regulatory theory suggests that these are applied in sequence of increasing severity if a licensee does not achieve compliance with lower level tools, with the most severe punitive tools being used only rarely, and education and guidelines being used the most (Fig. 1). This system relies on the licensee being aware of a consistent and transparent response to non-compliance by PIRSA (i.e. a published compliance policy), and it is expected that licensees would be able to avoid imposition of severe penalties in most cases.

Preventive enforcement tools available to obtain compliance

Education and guidelines

As noted above, it is the primary responsibility of the licensee or individual to comply with regulatory obligations. To assist this, guidelines and verbal advice can be given on what the regulatory obligations are before the activity is undertaken. It is not appropriate that PIRSA provide 'Codes of Practice' or specific procedures on how compliance might be achieved. Expert assistance in this regard may be obtained in the marketplace.

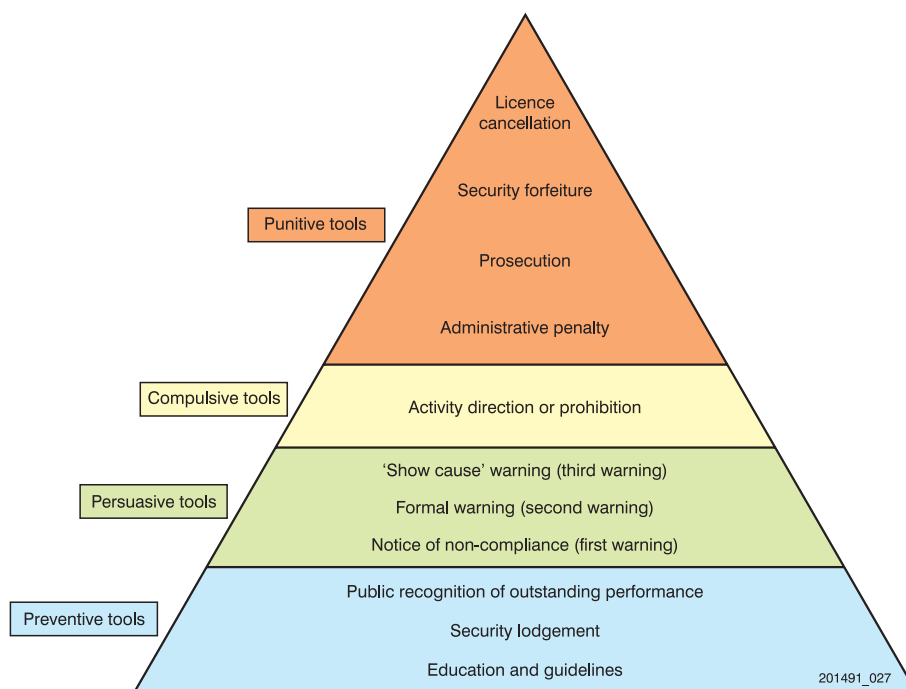


Fig. 1 Enforcement pyramid for petroleum compliance in South Australia.

Involvement of PIRSA in such advice may compromise enforcement if non-compliances are detected which partially resulted from PIRSA-approved procedures. However, if requested by the licensee, PIRSA may advise on whether or not a draft document proposed to be submitted to PIRSA is likely to result in compliance with the Act.

Security lodgement

It is current policy that licensees lodge a security of \$50 000 to cover obligations arising under the licence. This security is required to be lodged prior to entering any year in which seismic acquisition or well drilling or other on-ground activities are planned. If the licensee is fully aware that non-compliance may put this security at risk, it is believed that this will act as an incentive to comply with regulatory obligations.

Recognition of outstanding licensees

PIRSA will publicly report the names of those licensees who have demonstrated outstanding motivation and performance to comply during the year (as judged during the assessment of surveillance level). This recognition will not be for the 'best' performer, but will be given to all licensees who meet a high level of compliance and can demonstrate a high commitment and motivation to comply.

Persuasive enforcement tools available to obtain compliance

A three-step warning process has been developed to persuade non-compliant licensees that failing to take action to correct non-compliances will result in more severe consequences. These persuasive tools are most likely to be used for low-level breaches of the Act and regulations, where public harm results more from the frequency of the non-compliance rather than the seriousness of individual breach. Where the non-compliance is of a nature that further such non-compliance cannot be tolerated, the 'show cause' notice may be given in the first instance.

Notice of non-compliance (first warning)

This notice will clearly identify the nature and time of a detected non-compliance, and request that the licensee detail the events leading to non-compliance and actions intended to be taken by the licensee to prevent a recurrence.

Formal warning (second warning)

Following detection of a similar non-compliance, a formal written warning will be issued which notes the non-compliance, refers to the earlier 'Notice of non-compliance', warns of consequences of further non-compliance, and formally requests

an appropriate forward plan (with milestones) that will lead to the licensee becoming compliant.

‘Show cause’ notice (third warning)

Following a further detection of similar non-compliance, the licensee will be requested to show cause why one or more of the following compulsive or punitive tools should not be applied:

- direction to cease or undertake specific activities to rectify non-compliance
- prohibit further activities of the type resulting in the non-compliance
- imposition of an appropriate penalty
- prosecution for the offence (civil or criminal)
- cancel the licence.

The licensee may avoid punitive action if it can be demonstrated to PIRSA that they have already taken significant action which is likely to result in compliance at the next occurrence of the activity and that, where possible, previous non-compliances have already been corrected.

Compulsive enforcement tools

Directions

Under various sections of the Act, direction may be issued to licensees to carry out specified obligations under the Act or to cease activities that are contrary to the Act. The licensee may be prosecuted for non-compliance and be fined up to \$120 000, and the Government may recover the cost of fulfilling the obligation as a debt.

Restrictions on activities

Under Section 105 of the Act, licensees may be prohibited or restricted in undertaking activities if the licensee has failed to meet the criteria for good environmental performance included in the Statement of Environmental Objectives for the activity. The licensee may be prosecuted for non-compliance with the restriction and be fined up to \$120 000.

Punitive enforcement tools

Security forfeiture

As noted above, all licences where regulated activities are carried out will have a security lodged against them,

generally \$50 000 per licence. This security can be called upon when either:

- a licensee has failed to comply with a direction, and the security may be used by the State to remedy the non-compliance, or
- a licensee is in breach of licence work program conditions and the licence is to be cancelled.

Administrative and other penalties

Various penalties may be imposed under the Act, including ‘Administrative Penalties’ for defined offences. Administrative Penalties are imposed without recourse to a court (similar to fines levied on drivers detected exceeding the speed limit) and may be up to \$10 000 plus up to a further \$1000/day if the offence continues. Most of these offences relate to regulations and involve the late or incomplete submission of reports and technical data. The amount of penalty imposed is not discretionary and is fixed by regulation for each type of offence. If an Administrative Penalty is imposed, the offence cannot subsequently be prosecuted.

Prosecution

The main deterrent value of pursuing prosecution is not the amount of fine that may be imposed (maximum \$120 000) but the public attention that is drawn to a licensee’s poor compliance. There are considerable costs and risks borne by Government associated with prosecution that need to be considered when this option is to be pursued. It is felt that this would be considered only where there is public outrage at the non-compliance (i.e. significant environmental damage), such that further non-compliances could not be tolerated, and this needs to be clearly communicated to other licensees.

Licence cancellation

Licence cancellation represents the most severe penalty available under the Act. In the case of a pipeline or production licence, potentially assets of significant value (\$100+ million) are at risk if the licence were cancelled.

Consultation

As noted above, a key element of development and implementation of a

compliance policy is consultation with stakeholders to facilitate a sense of ownership and to ensure their support of the policy. Hames Sharley, a local multidisciplinary market and social research company, has been engaged to research the issues of maximising the effectiveness of consultation and the resulting level of understanding among stakeholders, and to obtain meaningful feedback from stakeholders in relation to the draft policy.

It is intended that the research program will achieve a definition of understanding, establish how understanding is best achieved or enhanced through consultation, how it is to be accurately measured, and to what extent suggested modifications of the policy are based on sufficient understanding, and not on other information or prejudice.

A crucial element to the evaluation will be to go beyond the initial reaction or ‘gut feel’ and penetrate the underlying motivations for opinions and attitudes. To achieve this, in-depth interviewing or focus group methodology will be used. The relevant stakeholders to be involved in these focus groups include:

- petroleum industry
 - environmental groups
 - other government departments
 - impacted people such as landowners.
- Some of the issues that will be tabled for discussion in the focus groups are:
- overall impression of the ‘Draft Compliance Policy’ document
 - awareness, behaviours, attitudes and opinions
 - identification of the perceived strengths and weaknesses of the policy
 - reasons for the strengths and weaknesses (prompted and unprompted)
 - their recommendations for an improved approach to the compliance policy
 - what modifications to policy would satisfy the group?
 - how can these modifications be compromised to meet with the demands of other stakeholders?

For further information contact John Morton (ph 08 8463 3225).