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AUSTRALIA'S NEW OFFSHORE OIL AND GAS DECOMMISSIONING FRAMEWORK

This insight reviews recent changes to the Offshore Petroleum and Greenhouse Gas Storage Act 2006 to implement Australia's enhanced offshore oil and gas decommissioning framework, with a focus on changes in control of titleholders and trailing liability. We also consider how M&A transactions for late life Australian offshore oil and gas assets might be structured under the new framework.

This update follows on from our December 2020 article Proposed changes to the offshore oil and gas decommissioning framework: What to expect.

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KEY TAKEAWAYS FROM THE NEW DECOMMISSIONING FRAMEWORK

- Key changes have been made to Australia's offshore oil and gas decommissioning laws.
- NOPTA approval will be required for changes in control of a titleholder including changes in control occurring 'up the chain' of ownership. Failure to obtain NOPTA approval may result in civil or criminal penalties and/or cancellation of a titleholder's title(s).
- Previous titleholders (and their related parties) will retain 'trailing liability' where the current or immediate former titleholder is unable to undertake decommissioning. Trailing liability also applies to titles that have ceased to be in force.
- The Australian government and regulators have expanded decision making criteria and information-gathering powers to assess the suitability of parties wishing to participate in the offshore oil and gas sector.
- Information gathering powers commenced from 2 September 2021. The remaining changes are expected to commence on or before 3 March 2022. The trailing liability changes will take effect retrospectively from 1 January 2021.
- Sellers and buyers of Australian offshore oil and gas assets may need to consider different transaction structures to those previously used. This may include the seller retaining some liability for decommissioning costs, decommissioning security agreements, vendor financing, seller retaining a minority interest, seller consent rights and seller step-in rights.
- Coordinated and early engagement by seller and buyer with regulators (eg. NOPTA, NOPSEMA, FIRB, ACCC) remain key for successful M&A of offshore oil and gas assets. It will also be important for regulators to support transactions that effectively manage decommissioning liability.
- The Australian government should consider providing further tax relief for decommissioning. This could encourage M&A of late life assets by reducing the amount of capital required as security for decommissioning.
- The United Kingdom provides useful a precedent for trailing liability mechanisms and sale structures that could be used in Australia to effectively manage decommissioning liability, encourage M&A of late life assets and increase economic recoveries from Australia's offshore oil and gas assets.

OVERVIEW OF THE DECOMMISSIONING CHANGES

The Offshore Petroleum and Greenhouse Gas Storage Amendment (Titles Administration and Other Measures) Act 2021 was passed in both houses of Parliament on 24 August 2021 and received Royal Assent on 2 September 2021.

The Act makes a number of changes to the Offshore Petroleum and Greenhouse Gas Storage Act 2006 (**OPGGS Act**) to implement aspects of the Australian Government's enhanced decommissioning framework for offshore oil and gas activities and relevant recommendations from the Independent Review into the Circumstances Leading to the Administration and Liquidation of Northern Oil and Gas Australia.

The Australian government's objective is to ensure that the decommissioning of Australia's offshore oil and gas assets is managed effectively, and the costs of decommissioning an offshore project remain with the entity or entities who are or were responsible for, or had the capacity to influence, the carrying out of the project.

KEY CHANGES TO THE OPGGS ACT

The Australian government and regulators state the key changes to the OPGGS Act are:

+ **Changes in control of titleholders** – the government has more powers and authority regarding changes in control of a titleholder (20% or more control or ownership), including NOPTA approval being required for changes in control of a titleholder;
+ **Trailing liability** – retrospectively expanding the government's existing powers ('remedial directions') from 1 January 2021 to 'call back' previous titleholders (and their related parties) to carry out decommissioning in the title area where the current or immediate former titleholder is unable to do so;
+ **Information gathering powers** – NOPTA, NOPSEMA and the responsible federal Minister have expanded decision making criteria and information-gathering powers to assess the suitability of entities wishing to enter into or progress through Australia's offshore oil and gas regime; and
+ **Digital readiness** – minor and technical amendments to the OPGGS Act to improve the administration of titles, including enabling electronic lodgment of applications.

WHEN DO THE CHANGES TAKE EFFECT?

The information gathering powers commenced from 2 September 2021. The remaining changes are expected to commence on or before 3 March 2022. Regardless of commencement date, the trailing liability provisions will take effect retrospectively from 1 January 2021.

CHANGES IN CONTROL OF TITLEHOLDERS

The changes to the OPGGS Act are said by the Australian government to expand the transactions that will require assessment and approval from NOPTA to include changes in ownership or control of the registered holder of a title (**Titleholder**). Previously, the OPGGS Act only regulated changes in ownership of petroleum and greenhouse gas titles.

When is approval required?

A change in control of a Titleholder must be approved by NOPTA before it takes effect.

What is control?

A person controls the Titleholder if the person (whether alone or together with one or more other persons the person acts jointly with):

+ holds the power to exercise, or control the exercise of, 20% or more of the voting rights in the registered holder; or
+ holds, or holds an interest in, 20% or more of the issued securities in the registered holder.

The definition of control incorporates two key concepts: control and ownership. A change in control of a Titleholder applies not only to persons who propose to be in a position to exercise control or influence over the Titleholder, but also to those who propose to hold a substantial interest in the Titleholder but may not be able to exercise such control or influence.

What is a change in control?

A change of control will occur if a person begins, or ceases, to control 20% of the Titleholder.

Factors that NOPTA can consider

When assessing a change in control of a Titleholder, NOPTA must consider whether technical and financial resources available to the Titleholder after the change in control are sufficient to carry out the operations and works authorised by the titles, and can discharge those obligations imposed under the OPGGS Act.

NOPTA may also consider:

+ the compliance history and experience in offshore petroleum operations of the person or persons who will begin controlling the Titleholder (including any officers if the person is a body corporate);
+ matters that go to the adequacy of the corporate governance of a person who will begin to control the Titleholder; and
+ any other matters NOPTA considers relevant.

This criterion ensures that the broad decision-making discretion that currently applies at similar decision points in the OPGGS Act (eg. grant of a petroleum exploration permit) continues to apply.

Consultation with other decision makers

In deciding whether to approve a change in control application, NOPTA may consult with other decision makers including the Joint Authority, NOPSEMA and the responsible federal Minister.

Approval period

Once approved, the Titleholder must complete the change of control within 9 months of the notice of approval. If the approval period expires, another application for the approval of the change in control must be made and further information or documents may be requested by NOPTA.

Revocation of approval

NOPTA may revoke an approval during the nine-month approval period if there has been a change in the circumstances of a person who is approved to begin or cease controlling a Titleholder and NOPTA considers it appropriate to revoke the approval.

Consequences of a change in control without NOPTA approval

If a change in control occurs without NOPTA approval, the person who begins or ceases to control the Titleholder may be liable for civil or criminal penalties. Contravention of these provisions is also grounds for cancellation of a title.

Tracing provisions

Tracing provisions prevent parties avoiding the change of control provisions through indirect holdings.

Under these provisions, a person (jointly or alone) is taken to control 20% of a Titleholder if it holds the power to exercise, or controls the exercise of, 20% or more of the voting rights in a party that has the power to exercise, or controls the exercise of, 20% or more of the voting power in the Titleholder.

The tracing provision may be applied multiple times so that a change in control of a Titleholder may be traced to a change in control of a higher party, regardless of how 'high up' in the corporate group the higher party is.

The same tracing provisions apply to interests in trusts and partnerships (including beneficial interests and interests in a unit trust).

Anti-avoidance

Anti-avoidance provisions create a fault-based offence and civil penalty where a person, either alone or with one or more persons, enters into a scheme, begins to carry out a scheme or carries out a scheme for the sole or dominant purpose of avoiding the change of control provisions.

Defence for civil penalty

If the Titleholder did not know, and could not reasonably be expected to have known, that the person begun to control or ceased to control the Titleholder, this is a defence to the civil penalty provision. However, the Titleholder will bear an evidential burden of proving the defence applies.

TRAILING LIABILITY

Call back of former titleholders

NOPSEMA's existing powers are said by the Australian government to have been expanded to enable it to 'call back' (via remedial directions) former Titleholders to decommission infrastructure and remediate the marine environment in the title area where the current or immediate former Titleholder is unable to do so (known as 'trailing liability').

Call back of holders of titles no longer in force

NOPSEMA may also call back the person who was, or is, the holder of a title that has ceased to be in force.

Scope of persons who may be called back

The definition of 'persons' who may be called back is broad and includes a related body corporate of a Titleholder (or former Titleholder) and any entity that NOPSEMA or the responsible federal Minister determines:

- is capable of, or has, significantly benefitted financially from the operations;
- has been at any time in a position to influence the extent to which a person has complied with their obligations under the OPGGS Act; and
- acted jointly with the Titleholder (or former Titleholder) in relation to the operations.

Circumstances where trailing liability may apply

Circumstances where decommissioning might be imposed on a previous Titleholder include:

- where a title expires prior to undertaking or completing decommissioning activities;
- where a Titleholder goes into liquidation; or
- where a previous decommissioning has developed a residual problem.

Last resort power

The Explanatory Memorandum to the Offshore Petroleum and Greenhouse Gas Storage Amendment (Titles Administration and Other Measures) Act 2021 states that the power to give a remedial direction to a person other than the current or immediate former Titleholder is intended to be an option of last resort where the current or immediate former Titleholder cannot meet their decommissioning obligations and all other regulatory options have been exhausted. This is not explicitly noted in the OPGGS Act.

M&A AND TRAILING LIABILITY IN THE UNITED KINGDOM

Decommissioning liability has been one of the single biggest concerns for the Australian government in recent years, particularly given the outcome of the liquidation of Northern Oil & Gas Australia in 2020. It has also been a major barrier to recent offshore oil and gas M&A activity in Australia.

Decommissioning liability is also a key issue in the United Kingdom (**UK**) on the UK continental shelf. The UK government, buyers and sellers have developed industry accepted mechanisms to deal with this issue. These include the buyer agreeing to provide the seller with security for decommissioning liabilities under a decommissioning security agreement (**DSA**) where secured amounts may change as the field matures and the UK government providing tax relief for decommissioning under a decommissioning relief deed. DSAs are generally entered into on a 'post tax' basis (ie. reflecting the cost of decommissioning after taking into account available tax relief). The UK government also allows a seller to transfer some of their tax history to the buyer to enable the buyer to obtain effective tax relief for their decommissioning costs. These mechanisms have facilitated successful M&A by reducing the amount of capital tied up as security, while addressing government concerns about funding decommissioning.

Recently, some sellers of UK assets have agreed to retain some share of decommissioning liabilities (eg. Shell/Chrysaor; BP/Enquest). Such a shared decommissioning liability structure signals a move away from a 'clean-break' decommissioning regime.

Other transactions in the UK have included vendor financing, the seller retaining a minority interest, contingent consideration and the seller having operator step-in rights.

We suggest that sellers, buyers and the Australian Government look to how trailing liability has been dealt with in UK M&A transactions when structuring future M&A transactions in Australia. In particular, sellers may need to consider moving away from a 'clean break' approach and the Australian Government should consider whether further tax relief could be provided for decommissioning. M&A of Australia's late life offshore oil and gas assets is key to increasing economic recoveries from these assets.

KEY CONSIDERATIONS AND RECOMMENDATIONS

There are a number of issues arising from the changes that require further consideration by key stakeholders. These include:

- The 20% threshold for a change in control, tracing provisions and broad definition of control may catch out some parties, particularly where the change in control occurs 'up the chain' of ownership and/or involves global M&A transactions.
- Joint operating agreements may need to be reviewed to ensure that the parties obligations and liabilities under the joint operating agreement are consistent with the new laws. For example, amendments may be required to deal with changes in control of a party.
- It will be important for former titleholders who ceased to be a titleholder on or after 1 January 2021 to determine their potential exposure to trailing liability under the new regime and to implement strategies to mitigate that risk.
- Sellers and buyers of late life assets may need to consider different transaction structures to those previously used. This may include the seller retaining some liability for decommissioning costs, decommissioning security agreements, vendor financing, contingent consideration, the seller retaining a minority interest, seller consent rights to future sales and/or seller operator step-in rights.
- Coordinated and early engagement by both sellers and buyers with the government and regulators (including NOPSEMA, NOPTA, FIRB, ACCC) remain key to successful transactions.
- The objective of the new regime is to effectively manage decommissioning liability – and not in itself to constrain transactions in the oil and gas sector. It will be important for regulators (NOPSEMA and NOPTA) to be a facilitator of transaction structures that give effect to that objective.
- The government may wish to consider providing further tax relief for decommissioning costs to assist with reducing the amount of capital tied up as security.
- Trailing liability mechanisms used in the UK may provide a useful precedent for Australian transactions. For example, 'post-tax' decommissioning security agreements enabled by decommissioning relief deeds/tax relief may offer an appropriate balance of decommissioning risks while increasing economic recoveries from late life assets.

Despite most changes not coming into effect until March 2022, we would encourage owners, sellers and buyers of Australian offshore oil and gas assets to become familiar with the changes, and consider the issues discussed above, before all the laws take effect. We expect that NOPTA and NOPSEMA will release guidance prior to March 2022 that will also assist in understanding the changes.

As more Australian offshore oil and gas assets move into their late life, there are opportunities for these assets to be transferred to new operators who are more incentivised to maximise economic recoveries. This is particularly important for east coast domestic gas assets. However, for this to occur, buyers and sellers may need to accept different transaction structures that effectively manage decommissioning liability under the new decommissioning framework.

CONTACT

BEN MACDONALD
Partner
T +61 3 8656 3351
M +61 418 524 724
E bmacdonald@gtlaw.com.au

BEN FULLER
Partner
T +61 2 9263 4171
M +61 459 200 037
E bfuller@gtlaw.com.au

CHRISTOPHER MARCHESI
Special Counsel
T +61 8 9413 8503
M +61 458 333 309
E cmarchesi@gtlaw.com.au

TOM CARBERRY
Lawyer
T +61 3 8656 3323
E tcarberry@gtlaw.com.au

GILBERT +TOBIN

GTLAW.COM.AU