



Queensland Government Consultation Report

Financial Assurance Framework – Providing Surety

Discussion Paper

Prepared for the Queensland Government Interdepartmental Committee on Financial Assurance for the Resource Sector

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Executive Summary

On 7 September 2017 the Queensland Government released the *Financial Assurance Framework Review – Providing Surety* discussion paper (financial assurance surety paper) for public consultation.

The financial assurance surety paper proposed *inter alia*:

- that all forms of surety will be administered by a centralised Scheme Manager
- the introduction of new forms of third party surety in favour of the State
- an expansion of the universe of acceptable third party surety providers
- the introduction of a ‘modular’ approach to enable resource operators to provide different forms and levels of surety over a life of resource operation

The paper was developed in response to the results of a recent review into the State’s financial assurance system by Queensland Treasury Corporation (QTC), industry concerns about the cost of and lack of competitiveness of third party surety providers under the current financial assurance system, and concerns about the risk to the State from the current cash holding procedures.

Over the consultation period 12 submissions were received. Submissions included industry, environmental groups, local government, insurance and financial services stakeholders.

The majority of stakeholders have generally supported the objectives of the reform package. The main concern from community stakeholders was that additional complexity from multiple forms of surety created additional risk and a single form of surety minimised the risk. Industry and financial services stakeholders were broadly supportive but sought to streamline the approval of new surety providers and had individual drafting requests on the form of surety instrument. There was uniform support for the adoption of distributed ledger technology to enhance administration of the scheme.

These concerns will be considered in further refining the scheme and its effective implementation. The Queensland Government believes that the final form of the scheme will strike an appropriate balance providing a more flexible financial assurance framework for industry, minimising the financial risk to the State, and ensuring environmental and community values are protected.

In response to consultation feedback, no changes have been made to the scheme proposed in the financial assurance paper however all relevant issues and suggestions have been or are continuing to be considered in the development of regulations and administrative processes for the scheme.

Implementation of the scheme is targeted for July 2018. New resource activities will be brought into the new financial assurance framework from 1 July 2018 onwards. Existing financial assurance will migrate to the scheme as surety on the scheme’s commencement and will be transitioned fully into the new framework over a three year period.

Financial Assurance Framework Reform Consultation Report



Purpose

The purpose of this report is to summarise the results of public consultation on the *Financial Assurance Framework Review – Providing Surety discussion paper (financial assurance surety paper)*. This report outlines the key themes raised during consultation as well as specific issues concerns/raised and the actions or responses to each.

Background

Queensland's resources industry is an important contributor to the economy—both for the revenue and jobs it generates. Last year, the resources industry contributed over \$21 billion to the state's economy, and was responsible for the direct employment of 60 000 people and the indirect employment of many more in key supporting sectors.

Industry and environmental groups have expressed concerns regarding the effectiveness of the current financial assurance surety requirements for the resources industry. These concerns cover a range of topics, including the cost of and lack of competitiveness of third party surety providers under the current financial assurance system and concerns about the risk to the State from the current cash holding procedures.

As a result, the Queensland Government commissioned a review of the financial assurance framework to better understand the advantages and disadvantages for stakeholders, and to examine options for improvements. The review was based on a range of factors that included evidence-based analysis and risk assessment; feedback from industry, government and other stakeholders; and experiences in Australia and overseas.

Review Findings

The review found that the Queensland Government relies heavily on the current financial assurance framework to protect the state against the cost of rehabilitation should a resource company not meet its rehabilitation and environmental obligations.

The review proposed a tailored, risk-based financial assurance framework for resource activities and made the following key recommendations:

- expanding the available mechanisms for providing surety
- expanding the market and competition for surety, including by increasing the permitted forms of surety
- expanding the providers of acceptable third party surety beyond the Australian regulated banking sector to include other entities (including insurance companies).

Queensland will have leading international financial assurance and rehabilitation practices that contribute to the efficient and effective management of the State's minerals and energy resources and environment.

Objectives

- Deliver a high level of environmental performance
- Protect the state's financial interest
- Provide an incentive to invest in the resources sector
- Provide an outcome that satisfies community expectations

During the course of the review, a number of options were considered as alternatives to the current financial assurance framework. After in-depth analysis, it was determined that:

- all forms of surety will be administered by a centralised Scheme Manager
- new forms of third party surety in favour of the State would be introduced
- the universe of acceptable third party surety providers would be expanded
- a 'modular' approach to enable resource operators to provide different forms and levels of surety over a life of mine would be introduced.

In contrast to the existing financial assurance framework, the tailored solution strikes a better balance between the risk to the Queensland Government and the cost burden for industry.

Components of the scheme

The Government will continue to calculate the estimated cost (Estimated Rehabilitation Cost) of rehabilitating land disturbed by the proposed resource activities.

Under the proposed new financial assurance framework there will be a Scheme Manager who will manage the scheme. The Scheme Manager will decide if the holder of an environmental authority will be required to provide surety or if a contribution to the scheme fund will be required. Surety will equate to the estimated rehabilitation cost related to the proposed resource activities.

Environmental authority holders that are required to provide surety will be entitled to adopt a 'modular' approach and provide a combination of any of the acceptable forms of surety in order to provide the total Surety Amount. The types of surety which may be provided is expanded to include Insurance Bonds .

As the Surety Amount is varied (for example by progressive rehabilitation of disturbed land) the environmental authority holder will be entitled to request that the Scheme Manager release an existing financial assurance and replace it with different forms of surety. This process allows greater flexibility. For example a 'cash float' consisting of cash held in security may be utilised to cover short term financial assurance requirements. Resource operators will be better able to address their liquidity requirements as rehabilitation is completed under the modular approach.

Public consultation

Public consultation on the financial assurance paper was held from 7 September 2017 to 22 September 2017. Some extensions were given on a case by case basis.

A notice inviting written submissions on the paper was provided on the Queensland Government's Get Involved and Queensland Treasury's websites.



Results of consultation and responses

Submissions were received from a total of 12 stakeholders.

All submissions relating to the financial assurance paper were reviewed and their contents summarised and collated by themes as well as issues.

Table 1 provides a summary of the key themes identified in the submissions and presentations/ meetings for the financial assurance surety paper, and the Queensland Government’s responses to each issue.

All relevant issues and suggestions have been or are continuing to be considered in the development of legislation, regulations and administrative processes for the scheme.

Table 1: Summary of key themes raised during consultation period and Queensland Government’s response

Issue	Issue description	Response
Risk associated with the ‘modular’ approach	Community stakeholders made the observation that allowing multiple forms of types of surety may give rise to an increased risk to the State due to the complexity associated with more than one form. One proponent advocated that cash was the least risky form of surety and therefore should be the only form permitted, whereas another proponent adopted a similar position in respect of bank guarantees and suggested cash surety be eliminated.	<p>As noted in the financial assurance surety paper one objective of the new scheme is to enable resources operators greater flexibility without increasing the risk to the State.</p> <p>A single form of surety would potentially reduce competitiveness in the market for third party surety (in the case of bank guarantees/insurance bonds), increase concentration risk on the providers and/or limit the ability of resources operators to provide surety (given different balance sheet and liquidity profiles of resource operators).</p> <p>The State believes that it is essential to manage the financial risk associated with third party sureties to provide a scheme which encourages the increase the number of potential acceptable providers (including insurance companies).</p> <p>By centralising the administration of surety to the scheme administrator, the State believes it will significantly reduce the operational risk associated with all forms of surety, particularly the risk the State currently has in respect of cash.</p> <p>Enabling simplified adjustments to the amount of surety held (for example by utilising cash surety) will act as an incentive to resource operators to undertake progressive rehabilitation and allow them to better to manage liquidity.</p> <p>The State has conducted a risk analysis of all options and is of the opinion that the three forms of proposed surety balance the need to ensure the State is adequately secured and resource operators are provided flexibility in meeting surety requirements.</p>

Separation of third party surety provider and resource operator	Some resource operators currently provide third party surety by way of surety providers who are within the same corporate group. Such surety providers are subject to prudential and rating requirements. Community stakeholders were strongly of the view that in all cases there should be a strict separation between resource operator and surety provider. Industry/financial services stakeholders were of the view that provided the surety provider met the prudential benchmarks then such surety was acceptable.	The State will consider the suggestions as it develops the regulations and guidelines for approval.
Process for approval of acceptable surety providers	Several financial services and industry participants suggested changes and additional criteria in relation to the approval of acceptable insurers for the purposes of third party surety. This included providing for additional rating agency benchmarks and the approval of certain jurisdictions as being <i>prima facie</i> acceptable regulatory regimes for the purposes of insurance company prudential regulation.	The State will consider the suggestions as it develops the regulations and guidelines for approval.
Risk associated with insolvency of EA holder and insurance bonds	One participant sought clarification on the status of insurance bonds in the case of default by the resource operator who would be unable to pay ongoing premiums.	The proposed form of surety contemplates an instrument which would be issued by either acceptable banks or insurance companies. In all cases the surety instrument is irrevocable, on demand and unconditional. In other words, once the surety instrument has been issued the rights of the State to call for payment are not impacted by any subsequent failure of the EA holder to pay any amount to the relevant insurer or financial institution.
Wording of surety instrument	Several financial services and industry participants suggested changes to wording of standard surety instrument.	The suggested changes will be carefully considered by the Scheme Manager when determining the approved form of surety.
Use of technology in respect of administration of the surety scheme	All respondents were in favour of the use of technology in relation to the administration of the surety scheme. In particular respondents endorsed the use of distributed ledgers and other 'blockchain' type technologies in the administration of surety instruments.	The State will further consider the introduction of technological solutions to ensure best practice administration of the scheme.

