Environmental Financial Mechanisms

Introduction

There are a range of financial mechanisms used in environmental laws. These mechanisms are used for a range of purposes, collectively contributing to a robust and contemporary environmental protection and management framework.

This paper outlines the various financial mechanisms that may be used in the Northern Territory's (the Territory) environmental regulatory regime and the key differences between them.

As the Northern Territory (NT) Government continues to progress its environmental regulatory reform program, it is important that the differences between the various financial mechanisms are understood, as well as where and how they may, or may not, interact and relate to other regulatory instruments, such as chain of responsibility laws.

Types of financial mechanisms

The following types of environmental financial mechanisms may be used in the Territory:

- bonds, securities and financial assurances (collectively financial assurances)
- levies
- residual risk payments
- funds
- fees.

Each financial mechanism has a specific purpose, and a range of mechanisms may be applied to a single project as part of a comprehensive and robust environmental management framework for that project.

Bonds, securities and financial assurances

The terms bond, security and financial assurance can all refer to the same type of regulatory tool - a financial assurance. The terms are used interchangeably, and typically reflect the word used in the legislation relevant to a specific project.

In the Territory, the *Environment Protection Act 2019* (the EP Act) uses the term 'environment protection bond'; the *Mining Management Act 2001* uses the word 'security', and the *Waste Management and Pollution Control Act 1998* refers to a 'financial assurance'. This paper uses the term financial assurance to refer to these types of financial mechanisms.

The overarching objective of a financial assurance is to provide to the regulator a guarantee that all statutory remediation and rehabilitation requirements will be completed by the proponent at the end of a project, or, if not completed appropriately, funding will be available to undertake the required works. If for whatever reason a proponent is unable to make good on their statutory requirements (e.g. due to

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insolvency), the financial assurance can be used by the regulator to undertake necessary remediation and rehabilitation works.

Financial assurances are made by a proponent in accordance with the financial accommodation agreed by the regulator (e.g. cash, bank guarantee). The funds are kept isolated from other government revenues and must be managed in accordance with the government framework applicable to the management of such funds. Upon the satisfactory completion of a proponent's statutory remediation and rehabilitation requirements, these funds are refunded to the proponent on application to the regulator. If the regulator has had to make a claim against a financial assurance to fund remediation and rehabilitation works, the amount refunded to the proponent is reduced accordingly.

Financial assurance amounts are determined by the regulator in accordance with the relevant legislative framework and particular funds governance arrangements. Typically a calculation for a financial assurance would consider matters such as: the level of environmental impacts or risks associated with an action, the level of disturbance expected at the project site, and likely rehabilitation requirements based on proposed disturbances. Due to the inherent differences between the risk profiles of different industries, the factors considered in the calculation of a financial assurance vary; i.e. an open cut mine is treated differently to a petroleum gas well which is treated differently to a heavy machinery industrial yard or a landfill site.

A recognised shortfall in financial assurances with respect to community expectations and environmental outcomes, is that calculations do not typically consider poor management practices and negligence throughout a project, and may not consider environmental harm that is not contained within a site, or existing disturbances at a site associated with previous activities. In addition, calculations are often limited to an expected point in time (e.g. the end of the planned project) and do not consider the implications of unexpected circumstances, such as insolvency, during a project.

This can result in the available funds being inadequate to address the level of disturbance and rehabilitation requirements at the site. In such circumstances, and if negligence and failure to adhere to environmental, social and governance standards has occurred, other regulatory instruments, such as compliance notices and chain of responsibility laws may be considered more appropriate for use.

Levies

Levies are non-refundable payments made to government, usually by industry participants (operators or consumers), to provide a revenue stream. Levies are typically applied to address a specific issue within an industry and/or support industry participants to make improvements to their practices to improve environmental outcomes and/or comply with new industry standards required by law.

The Territory's mining levy is an example of a levy imposed to address a specific environmental issue. The levy on mining industry operators was introduced to address historical and abandoned mine sites that were causing ongoing environmental and social harms in the Territory. This ensured equitable input by all industry operators who benefit economically by their mining activities in the Territory today, whilst removing the financial burden on taxpayers associated with managing the legacy mine sites and historical environmental liabilities that exist as a result of historical activities by the industry.

The Territory has committed to introducing a levy to monitor, manage and restore orphan petroleum wells in response to a recommendation of the Scientific Inquiry into Hydraulic Fracturing in the Northern Territory.

Levies can also be applied as a means to promote positive behavioural change, either amongst industry operators or consumers. For example, a waste levy increases the costs associated with disposing of waste at a landfill site. This increase in costs is typically passed down the supply chain from landfill operator to waste disposal contractor to the consumer and user of the waste disposal service. As a way to keep costs

down, the consumer will change their behaviour as much as possible to reduce how much waste they produce so the overall cost of disposing of their waste is kept as low as possible.

The monetary amount applied for a levy is dependent on the industry and reason for the levy. The calculation is usually based on an agreed rate or percentage of something (e.g. weight or volume of a type of waste multiplied by agreed rate; or percentage of output/turnover of a factor within a financial year). When determining the amount of a levy, the increased financial burden on industry and/or consumers is weighted against the broader economic impacts, and the social and environmental costs and benefits likely to be achieved by the introduction of the levy.

Revenue collected by governments from levies is generally isolated from other government revenue streams and only permitted to be used for specific matters related to the industry that paid the levy.

Residual risk payments

Residual risks are the risks that remain at a site once it has been fully remediated or rehabilitated. Residual risks are most commonly associated with in-situ infrastructure which is allowed to remain on site as part of agreed remediation and rehabilitation.

A residual risk payment is a non-refundable payment that provides the financial resources for the long term monitoring and maintenance of a site's residual risks to ensure the continual protection of the surrounding environment, human health and community safety. For example, perimeter fencing, shaft caps, dam walls, leachate barriers and /or other engineered containment systems used to restrict/close access or for tailings storage will need to be monitored and repaired periodically to maintain functional integrity. Alternatively, site inspections and repairs may be required following extreme weather events that has likely caused damage. These payments are typically only required where there is an intention to transfer liability for a site with residual risks from one entity to another (typically from a site operator to a regulatory body). They are only considered once a period of post-closure monitoring has demonstrated the site is safe, stable and non-polluting.

Residual risk payments differ from other non-refundable financial mechanisms, such as levies, in that the allocation of funding is specific to the site for which the payment is made.

Residual risk payments provide an avenue for an operator to surrender an industry activity site and to 'walk away' from the site without further liability. The payments also provide assurance to government and the community that financial resources have been allocated to facilitate scheduled monitoring and maintenance programs for a site with residual risks over the long term.

Residual risk payments enable regulators to confidently refund any financial assurances that are being held for the site. This can increase certainty for the operator and alleviate financial pressures associated with a requirement to maintain a financial assurance for a site with residual risks that is no longer operating and generating an income. Such a financial impost can limit an operator's ability to secure credit, invest, and establish new projects.

The Queensland Government has introduced a residual risk payments scheme[1] to protect the State's financial interest following a review[2] of Queensland's overall financial assurance framework. This was in response to its increasing financial burdens associated with legacy and orphaned contaminated land sites and moth-balled mines. The Australian Government also applies a residual risk payment scheme as part of transferring liability from a licensee of a carbon capture and storage project to the Australian Government.

[1] https://www.business.qld.gov.au/running-business/environment/licences-permits/rehabilitation/residual
[2] https://s3.treasury.qld.gov.au/files/review-of-queenslands-financial-assurance-framework.pdf

To be granted a site closure certificate associated with a carbon capture and storage project's greenhouse gas injection licence, a licensee must provide a security to cover the costs of carrying out an ongoing monitoring program of the injection site to ensure the greenhouse gases are not re-released into the atmosphere.

Environmental fees

Governments can charge fees for specific government activities. This can include the provision of goods, services or regulation, or a combination of these activities. Fees provide a revenue stream to resource the regulator and support it to perform its essential tasks and functions for the community. Fees support the implementation and administration of legislation. Application of fees are based on a number of policy factors, and may reflect a simple fee for service structure, or a more complex full/partial cost-recovery structure.

Fees may be applied at the front end of a regulatory system (e.g. on lodgement of an application), or periodically (e.g. licence renewal fees). Fees can also be applied at each or some stages of a process (e.g. at the referral stage for an application, or at the actual assessment stage of a project's Environmental Impact Statement). In some cases, fees are charged at a nominal rate (e.g. small one-off payment for a permit to conduct an activity or renew an operator's licence), or at a rate that reflects the quantum of an activity (e.g. time required to complete a review and assessment of a project's referral, or an annual waste discharge licence fee based on estimated or actual outputs over a set period of time).

Examples of fees in place for environmental legislation in the Territory include:

- waste discharge licence renewal fees
- petroleum titles annual rent registration fees
- new water extraction licence application advertising fees
- extractive mineral lease administration fees.

The Australian Government provides guidance on cost recovery and governments charging of fees[3]. When applying fees for government activities, one of the key considerations is whether the activity is benefitting a specific individual or organisation, as opposed to the general public. It is not considered appropriate for the general public to be paying for government activities when the benefits of the activity will only be received by an individual or company (e.g. issue of a mineral title provides a benefit for the title holder only, so it would be appropriate to charge a fee for this government activity).

Environment protection funds

Environment protection funds are secure trust accounts that provide a transparent mechanism to hold money paid to governments through applied financial mechanisms. They are established to isolate, or 'quarantine' the revenue collected.

The primary purpose of environment protection funds is to hold revenue monies in trust, to be used only for the environmental management purposes permitted by the funds governance structure. For example, the Northern Territory's 'Mining Remediation Fund' holds money obtained through the mining levy imposed on the mining industry. The money in the fund can only be spent on activities associated with the rehabilitation of legacy mining sites.

[3] https://www.finance.gov.au/publications/resource-management-guides/australian-government-cost-recovery-guidelines-rmg-304