

Rehabilitation Bond Policy for the Latrobe Valley Coal Mines

Introduction

Communities and government expect that the full costs of mine rehabilitation are borne by the mine operator and not left to the taxpayer. To this end, the State expects to be financially assured for these costs through a rehabilitation bond.

Under the *Mineral Resources (Sustainable Development) Act 1990* and the associated *Mineral Resources (Sustainable Development) (Mineral Industries) Regulations 2013*, mine operators are obligated to:

- rehabilitate land that has been mined in accordance with an approved rehabilitation plan
- enter into a rehabilitation bond with the form and amount to be determined by the Minister for Resources.

Rehabilitation Bond Policy Review 2016/17

The 2015/16 Hazelwood Mine Fire Inquiry (the Inquiry) identified policy implementation issues that resulted in the government holding insufficient rehabilitation bonds for the Latrobe Valley coal mines.

In late 2016, the Victorian Government undertook a review of its rehabilitation bond policy as applied to the Latrobe Valley coal mines (the Review), a key commitment in response to the Inquiry.

The Review was undertaken in consultation with key stakeholders, including the Latrobe Valley mine operators, local government and Environment Victoria.

Two overarching objectives guided the review process:

- Ensuring that the State of Victoria is financially assured against the risk of rehabilitation default and the costs of rehabilitation are borne by the operator and do not fall to the taxpayer.
- Encouraging progressive rehabilitation and improved rehabilitation planning by mine operators.

The following Rehabilitation Bond Policy framework for the Latrobe Valley coal mines was informed by the outputs of the Review.

The Rehabilitation Bond Policy framework for the Latrobe Valley coal mines

Rehabilitation bonds will be based on an assessment of rehabilitation liability using a new Rehabilitation Liability Assessment Framework

The State will set bonds based on an assessment of rehabilitation liabilities using its Rehabilitation Liability Assessment Framework (RLA Framework) and Cost Calculator¹, developed by DEDJTR Earth Resources Regulation (ERR) in response to the Inquiry.

The RLA Framework specifies the ‘manner and form’ of liability assessments and applies a probabilistic approach to provide a risk-adjusted estimate of rehabilitation liabilities. The RLA Framework will be applied to produce independent rehabilitation liability assessments, informing consideration of a third stage rehabilitation bond increase for the Latrobe Valley coal mines, in line with the recommendations of the Inquiry.

The RLA Framework and Cost Calculator produce a range of estimates of rehabilitation liability that reflect the estimated rehabilitation base cost plus a risk cost. This allows the assessed rehabilitation liability amount to be adjusted to reflect an estimate of risk and uncertainty associated with the base cost reliability estimate. Adopting this approach provides an incentive for mine operators to improve their rehabilitation planning. This confidence level, or ‘P-value’, represents the degree of confidence that the estimate will reflect actual rehabilitation costs – indicative of the risk appetite of the user (government) in setting rehabilitation bonds. A P-value of P50 represents an estimate of the most likely costs, as there is an equal chance that actual costs will be higher or lower than the estimate. A higher P-value represents a more conservative approach, as the higher the P-value, the smaller the likelihood that actual rehabilitation costs will exceed the estimate.

Consistent with the objectives of the rehabilitation bond policy review, the State places an appropriate price on risk and uncertainty. This will be achieved by setting a confidence level that provides an incentive for mine operators to improve rehabilitation planning, reduce uncertainty in the model and ultimately, bring down liability estimates. The confidence level reflects government’s risk appetite and provides an estimate to guide the setting of bonds that assure the State against the risk of default.

This outcome will be achieved by the application of a P80 confidence level.

Liabilities will be assessed independently no less frequently than every five years

Regular review of a rehabilitation liability assessment is critical to the effective operation of the rehabilitation bond policy consistent with the objectives of the Review. Periodic review of the assessment amount reduces uncertainty and ensures that risk-adjusted estimated liabilities best reflect actual rehabilitation costs.

¹ The RLA Framework was provided to mine operators in December 2016

ERR will undertake an independent assessment of rehabilitation liabilities no less frequently than every five years or in response to a Work Plan variation, that includes substantial updates to the rehabilitation plan. This increased frequency reflects that:

- there are a number of identified knowledge gaps in existing Work Plans that need to be addressed by the mines through their rehabilitation planning
- the mines are likely to develop a clearer view of their rehabilitation plans as they move closer to closure and there are likely further changes to Work Plans as the Latrobe Valley Regional Rehabilitation Strategy is developed and finalised.

Rehabilitation bond amounts will reflect the full value of a risk-adjusted liability assessment, discounted for progressive rehabilitation

The State will continue to set bond amounts that are equal to 100 per cent of a rehabilitation liability assessment determined using the RLA Framework and appropriate confidence interval, discussed above.

The Inquiry recommends risk-based ‘discount bond models’ be considered as a method to encourage progressive rehabilitation.

The Department of Economic Development, Jobs, Transport and Resources will work with the three Latrobe Valley coal mine operators to develop principles and administrative arrangements for detailed rehabilitation planning and define progressive rehabilitation milestones. This will include clarifying the requirements for progressive rehabilitation and objectives as part of the review of the regulatory framework, which will address rehabilitation issues identified by the Inquiry.

Any reductions to rehabilitation bond amounts will reflect the progressive rehabilitation milestones in a respective approved Work Plan. The progressive rehabilitation to be considered for bond discounts must be consistent with achieving the agreed final landform, thereby reducing long term rehabilitation liabilities. This approach also strengthens rehabilitation planning and annual reporting, as these are the basis for determining bond reductions.

Performance against progressive rehabilitation milestones linked to discounts under the framework would be assessed using existing annual requirements for mine operators, which include a self-assessment of rehabilitation liability and details of progressive rehabilitation undertaken during the period. Earth Resources Regulation will use these reports to monitor significant changes to risk levels or rehabilitation liability.

Regular review of bond amounts using a consistent and transparent tool (the RLA Framework) provides the best incentive for operators to undertake progressive rehabilitation and thereby reduce the bond. The completion of progressive rehabilitation that contributes to the final landform will be directly reflected in a reduction in liability assessments, translating to a reduction in the bond amount.

Rehabilitation bonds must be provided in the form of a bank guarantee

Rehabilitation bonds must be in the form of a bank guarantee that meets conditions approved by the Minister for Resources.

While there are costs to operators associated with servicing a bank guarantee, this approach best meets the State's objective to provide financial assurance against the risk of operators defaulting on rehabilitation. Bank guarantees provide a strong level of assurance, particularly when the guarantee is provided by an Australian, or similarly regulated, financial institution.

The conditions for acceptance of a bank guarantee, include that a bank guarantee must:

1. be from a recognised OECD financial institution (bank, building society or credit union) with a risk rating of at least A- or A3 for Standard and Poor's and Moody's respectively
2. be payable immediately at an office of the issuer in an Australian capital city on any business day
3. have an expiry date of no less than three (3) years from the date of issue and if applicable, be suitably replaced twenty (20) days prior to expiry. A bank guarantee cannot be terminated by the bank without prior approval of Earth Resources Regulation
4. be in favour of the Minister for Resources
5. state the name of the tenement holder
6. state the tenement type and number
7. relate to a single tenement only (i.e. each tenement must have a separate bond)
8. be on Bank, Building Society or Credit Union letterhead or have a recognised stamp to indicate authenticity
9. be an original document
10. be signed and dated by an authorised officer of the financial institution.

The Minister for Resources will consider rehabilitation bonds in a hybrid form, where the bank guarantee is complemented by a portion of the bond in the form of a parent company guarantee (PCG) from an entity acceptable to the State, where:

- the value of the PCG portion is no more than 20 per cent of the total risk-adjusted rehabilitation liability estimate
- the terms and conditions of the PCG are set by the State and must satisfy the following minimum conditions:
 - all costs associated with establishing and maintaining the PCG are borne by the relevant mine operator
 - the guarantee is secured against an appropriately rated entity (at least Standard and Poor's BBB or Moody's Baa2) and a positive trading outlook
 - the entity has appropriate Australian asset coverage to conservatively cover any potential requirement for the repayment of funds
 - the parent company guarantee is governed under Australian law
 - there is no ability to seek an injunction to legal proceedings.