Annexure 8

PNG Project as distinguished from Pohokura determination

Introduction

In September 2003, the New Zealand Commerce Commission (***NZCC***) granted authorisation to OMV New Zealand Limited, Shell Exploration New Zealand Limited, Shell (Petroleum Mining) Company Limited and Todd (Petroleum Mining Company) Limited (together referred to as the ***Pohokura joint venturers***) to enter into arrangements to jointly market and sell gas produced from the Pohokura gas field until 30 June 2006 (the ***Pohokura Project***), subject to specified conditions.

The circumstances in the Pohokura Project are clearly distinguishable from those facing the Participants in seeking to market Project gas in eastern Australia for the reasons set out below.

1. Level of supply and demand of gas in New Zealand

1.1 The supply/demand balance for gas is extremely different in New Zealand compared to Australia. At the time of the authorisation application by the Pohokura joint venturers there was a significant level of excess demand for gas in New Zealand.[1] The shortage of gas was of such a magnitude that major new electricity generation projects were put on hold due to difficulties in obtaining reliable gas supplies.[2] This excess demand was a result of a number of factors including: increased demand for electricity (electricity generation consumed 40.5% of natural gas[3]), lower than expected gas reserves in the main other New Zealand gas field (the Maui gas field) and the absence of an immediate replacement for the low Maui reserves.

1.2 This excess demand for gas meant that the participants in the Pohokura Project did not face the same difficulties that the Participants in this application face in separately underwriting their investment. The NZCC noted that as a result of the supply shortage of natural gas in the New Zealand market, it seemed 'highly unlikely' that any of the Pohokura joint venturers 'would not be able to sell their proportion of the gas at an economically attractive price.'[4]

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[1] New Zealand Commerce Commission Determination Decision 505, OMV New Zealand Limited; Shell Exploration New Zealand Limited; Shell (Petroleum Mining) Company Limited; Todd (Petroleum Mining Company) Limited (the ***Pohokura Determination***), 32 and 78. For a copy of the determination see: http://www.comcom.govt.nz/publications/GetFile.CFM?Doc_ID=428&Filename=505.pdf

[2] Ibid, 78.

[3] Ibid, 32.

[4] Ibid, 69.

1.3 Importantly, the Pohokura Project had a high degree of security in relation to their ability to dispose of project gas. The major gas buyers from the Maui gas field (NGC, Contact and Methanex[5]) are expected to be the same buyers of gas from the Pohokura field.[6] In comparison, as the ACCC is aware, over the last five years the Project has struggled to find customers willing to enter into indicative term sheets for the supply of Project gas. Several important foundation customers have left the Project for other supply sources, and since mid 2002 the Project has lost over half of the volumes previously committed. Without these volumes, the Project has been unable to justify the decision to spend approximately US$60 million on FEED. This ability to 'shop around' clearly illustrates that there is not an equivalent level of demand in Australia to that in New Zealand which can be relied on to underwrite an investment in a greenfields project.

2. Few gas suppliers

2.1 Collectively, the Pohokura joint venturers accounted for 88% of the production of natural gas in New Zealand.[7] Production of gas in New Zealand has been dominated by the Maui field since gas first flowed from the field in 1979.[8] Shell subsidiaries, Todd subsidiaries and OMV entirely own the Maui gas field which, up until September 2002, had produced 75% of the natural gas for New Zealand. Their presence in the New Zealand gas market is therefore well established. The gas field which produces the second largest amount of gas is the Kapuni field, which is the largest onshore field and the second largest gas/condensate field in New Zealand. The Kapuni field, also owned by subsidiaries of Shell and Todd, produced 11.5% of New Zealand gas.[9] Although there are seven other gas fields in New Zealand, between them they produced 13.5% of the natural gas consumed in New Zealand.[10] More importantly, 88% of gas being produced in New Zealand comes from fields owned by Shell, Todd and OMV. Swift is the only other producer which can be regarded as a major producer of gas.[11]

2.2 New suppliers are not likely to enter into the New Zealand market in the short terms as large scale discoveries of gas are likely to take several years to develop. This suggests that the owners of the Pohokura field will not face an effective competitive constraint from other gas producers before the end of the decade.[12]

2.3 By comparison, although there are a relatively limited number of gas suppliers in eastern Australia there is strong inter-basin competition. Project gas will compete against Cooper Basin gas in all eastern Australian states and against gas from Victoria in New South

[5] Ibid, 22.

[6] Ibid, 58.

[7] Ibid, 75.

[8] Ibid, 22.

[9] Ibid, 24.

[10] Ibid.

[11] Ibid, 78.

[12] Ibid, 79.

Wales and South Australia. The overlap between gas supplied by the Project and gas from other basins will result in direct price competition between gas supplies in the entire eastern Australian region.

3. Longstanding presence of suppliers

3.1 As noted above, Shell and Todd already had a long history of involvement as participants in the Maui gas field. In addition, the customer profile of the Pohokura field was likely to be largely similar to the Maui field. The fact that customers of the Pohokura field would be dealing with their established gas suppliers would obviously provide those customers with a much greater degree of commercial certainty than if the suppliers were new entrants to the supply of gas.

3.2 By contrast, Oil Search, MRDC and Merlin have never sold gas in Australia and therefore do not have the established relationships that the Pohokura joint venturers had with New Zealand customers. In this respect, the involvement of Esso Highlands in the Project has been very important in providing the Project with the commercial credibility necessary to attract serious buyer commitments.

4. Pohokura development much less complex

4.1 The Pohokura condensate and gas field is located approximately 8 kilometres off the Taranaki coast in New Zealand. The field will be developed from a single offshore platform plus three onshore development wells accessing the southern portion of the field. It is approximately 16km long by 5km wide extending offshore in a north-west direction, from close to the Methanex Motonui site near Waitara in North Taranaki.[13]

4.2 These reserves are therefore significantly closer to customer centres than in the case of the Project reserves in Papua New Guinea. The cost of pipeline infrastructure will therefore be substantially lower than in the case of the Project. Further, the Project fields in PNG are remote, the terrain is difficult and the climatic conditions are volatile. The fields are akin to 'offshore' fields such as the Pohokura fields, and this increases the risk of development compared to development of mainland or offshore Australian gas reserves.

[13] Ibid at 25.