

Santos' summary of new proposal in relation to QGC

30 January 2007

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30th January 2007

Proposal by a subsidiary of Santos Limited ("Santos") to acquire Queensland Gas Company Limited ("QGC"), subject to implementation of the de-merger transaction.

1. Request for informal merger approval: Santos seeks informal approval from the ACCC to acquire QGC, subject to the implementation of the de-merger transaction as outlined in this submission ('new proposal'). This new proposal is in substitution for Santos' current offer to acquire control of QGC ('old proposal'). Santos will announce today that it will allow the current takeover offer to lapse next week.
2. In respect of Santos' old proposal, Santos has provided confidential submissions and information to the ACCC. The ACCC has conducted market inquiries, published a Statement of Issues, and is scheduled to announce its decision on the old proposal on 31st January 2007. In the light of this new proposal and as the old proposal will lapse, Santos has requested the ACCC to discontinue its consideration of the old proposal, which the ACCC has indicated it will do.
3. Santos' announcement of its new proposal and commencement of ACCC's market inquiries: Santos requests the ACCC to commence market inquiries, as soon as possible, as Santos will announce the new proposal on 30th January 2007. **This submission (but not the identified confidential annexures) may be published by the ACCC.**
4. Reason for the new proposal: in order to persuade the shareholders of QGC to sell their shares to Santos, and to encourage the board of QGC to give its favourable recommendation, Santos has formulated a new proposal which provides QGC's shareholders with the

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opportunity to realize significant value from QGC's success to date.¹
This will happen in two ways for QGC's shareholders-

(1) By ownership of shares in the 'new QGC'.

QGC's shareholders will be given the additional opportunity to benefit from the accelerated commercialisation of substantial parts of QGC's assets. They will be asked to approve a de-merger transaction effected through a scheme of arrangement and capital reduction by QGC. The de-merger transaction will spin out Newco, to become '*the new QGC*', as an attractive business and investment proposition in its own right.

In order to convince shareholders as to the capability of Newco to become '*the new QGC*', Newco will hold QGC's interests in certain permits and licences for about 54% of QGC's gas in place, including permits which QGC has said previously will be "the next Undulla Nose".² Newco's acreage will be about 70% of QGC's total acreage.³ As stated by QGC last week, the company "has enormous potential to expand beyond the Berwyndale South gasfield by proving-up substantial 3P gas reserves in the areas outside Berwyndale South".⁴

Newco will also have the benefit of facilitating agreements giving Newco immediate certainty and credibility for its activities as a gas supplier as it develops its own permits. The assets of Newco will include a contractual right to develop gas reserves in the Undulla Nose in ATP 648P of up to 60PJ (50% of 1P and 50% of 2P reserves) and to sell and receive the proceeds of sale of those reserves to gas buyers. Newco will be

¹ The old proposal was rejected by the QGC board, which has subsequently recommended a proposal from AGL. The ACCC has given its approval to that proposal.

² "**Both ATP 621P and ATP 651P have potential to be the next Undulla Nose**", QGC Investor presentation, 30 October 2006, slide 4.

³ " While these are exciting results, it should be remembered that the Undulla Nose region contains less than half of QGC's total estimated original gas-in-place(OGIP)...This is a huge quantity establishing the Surat Basin as a world class source of clean energy for Australia", QGC Progress Report, 8 November 2006, page 2.

⁴ QGC's ASX announcement " QGC Statement on ACCC decision", 24 January 2007.

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provided with access to drilling infrastructure and gas processing infrastructure. Newco will also have the right, but not the obligation to sell those reserves to Santos. Newco will, for instance, be able to borrow additional funds against this arrangement.

Newco will issue shares to QGC's shareholders in proportion to their existing shareholdings in QGC. Newco will also issue shares to Santos for approximately \$40 million to take Santos' total shareholding in Newco to 30% of its issued capital. This will provide Newco with capital to adequately exploit its asset base.

The overall outcome will be that the resources of Newco will enable the current QGC board and management to direct and manage Newco, and to repeat QGC's success for not only the benefit of QGC's shareholders, but also for the benefit of gas buyers and other gas industry stakeholders.

- (2) Sale of shares in QGC to Santos: it will only be after QGC's current shareholders have expressed their vote of confidence in the success of the de-merger transaction and the future of '*the new QGC*', and after obtaining Court approval of the scheme of arrangement, that Santos will be able to acquire their shares in QGC.

5. Favourable competition law outcome: the direct competition law consequence of the new proposal will be to ameliorate substantially any reasonable concerns the ACCC and some gas industry stakeholders may have had about Santos' old proposal having a possible adverse effect on competition. Their concerns may have been based on views that as the old proposal removed QGC as an independent gas supplier this could have had a material effect on competition in the relevant market as a whole, notwithstanding Santos' contrary views about the effectiveness of the competitive responses of rival suppliers, consumers and other industry stakeholders.

There are three main reasons as to why the new proposal will not offend the merger provisions of the Trade Practices Act 1974 :-

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(a) Compared with the old proposal, the implementation of the new proposal will halve the gas in place assets being acquired by Santos to be added to its existing coal seam gas interests at Fairview. The physical split of the assets is depicted on the attached map, and the split of QGC's "gas in place" is set out in the following table-

<u>Permits</u>	<u>Original Gas in Place (PJ)</u>	
	<u>New QGC</u>	<u>QGC (Santos)</u>
ATP 574P	1774	0
ATP 610P	0	254
PLs 179,180,228,229 ⁵	0	2271
ATP 621P	2771	0
PLs 201,211, 212	0	924
ATP 632P	806	0
ATP 647P	971	0
ATP 648P	200	4175
ATP 651P	2484	532
ATP 676P	639	0
TOTAL	9644	8155
	54%	46%

Santos will assume QGC's obligations under existing gas supply agreements and commitments (other than the conditional AGL gas supply agreement) under which most of QGC's existing 2P reserves are committed. Santos acknowledges that the direct outcome of its new proposal will be to create and facilitate a vigorous, independent and highly effective competitor in the form of '*the new QGC*'.

(b) As noted above, the new proposal will create '*the new QGC*' with board, management and company personnel, resources, funding and facilitating arrangements which will enable the new QGC to step quickly into the shoes of the old QGC as a supplier of coal seam gas to consumers. QGC's management team has a detailed understanding of the geology of the areas

⁵ PLs out of previous ATP 620P.

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and the completion techniques required to effectively exploit the reserves of coal seam gas within the areas. QGC has itself suggested that the production and supply of coal seam gas is more akin to a steady manufacturing operation once these techniques are applied.

The approval of the scheme of arrangement by shareholders, and the participation of the board, management and staff of QGC in the direction and management of Newco, will be their vote of confidence that '*the new QGC*' will be a successful business as an independent and highly effective competitor of Santos and all other Queensland gas suppliers.

It can be expected that industrial and wholesale consumers will be supportive of '*the new QGC*' by early entry into gas purchase arrangements.

- (c) As a result of Santos developing the permits retained by QGC to perform existing gas supply agreements and to compete to win new gas contracts, and with Newco developing and supplying gas from its permits to win new gas contracts, more gas will become available for competitive supply much sooner to many more consumers (and not just AGL) than if QGC had remained independent.⁶

6. Further implementation details:-

- (1) Acquisition of QGC: Santos, with the co-operation of QGC, proposes to effect a scheme of arrangement under which Santos will acquire all of the shares in QGC, on the condition that the de-merger transaction outlined below is first implemented. Newco will be de-merged from QGC, as part of the same scheme of arrangement, pursuant to which Santos will acquire **all of the shares of QGC.**
- (2) Establishment of Newco: Newco will be established by QGC initially as a wholly-owned subsidiary of QGC. In connection

⁶ " With a potentially very large resource base of coal seam gas still to be developed, QGC will be well placed *to expand and grow quickly*, in an environment that increasingly values clean energy", QGC Announcement, 5 December 2006, page 1 (emphasis added).

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with the de-merger, Newco will assume the name "Queensland Gas Company Limited" and will list on the ASX.

- (3) De-merger transaction: Subject to a scheme of arrangement under Part 5.1 of the Corporations Act between QGC and its shareholders becoming effective, QGC will transfer to Newco the assets, liabilities, obligations, personnel and enter into the associated arrangements in accordance with the scheme proposal and de-merger arrangements for the establishment of Newco, including as follows:-
- (a) Permits and related assets: QGC's interests in ATP 574P, ATP 621P, ATP 632P, ATP 647P, ATP 647 farm-out, ATP 651P and ATP 785P being about 70% of QGC's acreage and 54% of QGC's gas in place: refer to Confidential Annexure "A".
 - (b) Transitional services, assistance, records and information agreement for the purpose of establishing Newco's operations independently from Santos as soon as possible: refer to Part A of Confidential Annexure "B".
 - (c) Pipeline consent agreement to enable Newco to construct and operate a pipeline connecting ATP 621 to the Roma to Brisbane pipeline: refer to Part B of Confidential Annexure "B".
 - (d) Drilling Rig access agreement for the purpose of enabling Newco to use such drilling rigs that QGC owns or has a contractual right to use, including associated personnel and services: refer to Part C of Confidential Annexure "B".
 - (e) Pipeline and Plant Infrastructure Access Agreement for the purpose of enabling Newco to use spare capacity in upstream pipeline and plant infrastructure owned by QGC: refer to Part D of Confidential Annexure "B".

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- (f) Arrangements in relation to ATP 648P, which will enable Newco to conduct operations there to meet a reserves target for itself of 60PJ, 50% of which must be 1P reserves and 50 % must be 2P reserves, for sale to consumers, or at Newco's election for possible sale to Santos at an agreed price: refer to Confidential Annexure "C".
- (4) QGC's scheme of arrangement: QGC will undertake a scheme of arrangement and a capital reduction, pursuant to which QGC's shareholders will receive all of the shares held by QGC in Newco in proportion to the number of shares they hold in QGC.
- (5) Santos' shareholding in Newco: Santos will subscribe for shares in Newco, in the order of 200 million shares at 20 cents per share, at a total subscription price of approximately \$40 million, which will give Newco, in conjunction with the benefit of the arrangements in relation to ATP 648P set out in annexure "C", sufficient capital to adequately exploit Newco's asset base. Santos' total shareholding in Newco will be 30% of the issued capital of Newco, including its pro rata entitlement to Newco shares through its existing QGC shareholding).

Santos will enter into undertakings with the ACCC pursuant to section 87B of the Trade Practices Act 1974 stating that, until Santos is released by the ACCC from its obligation to do so, it will not, without first obtaining the ACCC's prior written consent, seek to-

- (a) *appoint any director representing it to the board of Newco,*
- (b) *acquire from another shareholder any shares in the issued capital of Newco, or*
- (c) *remove any director from the board of Newco, unless the proposal is recommended by a majority of the board of Newco.*

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- (6) Approval of the de-merger transaction: upon approval of the de-merger transaction, Santos will then acquire all of the shares in QGC subject to implementation of the de-merger transaction agreements.

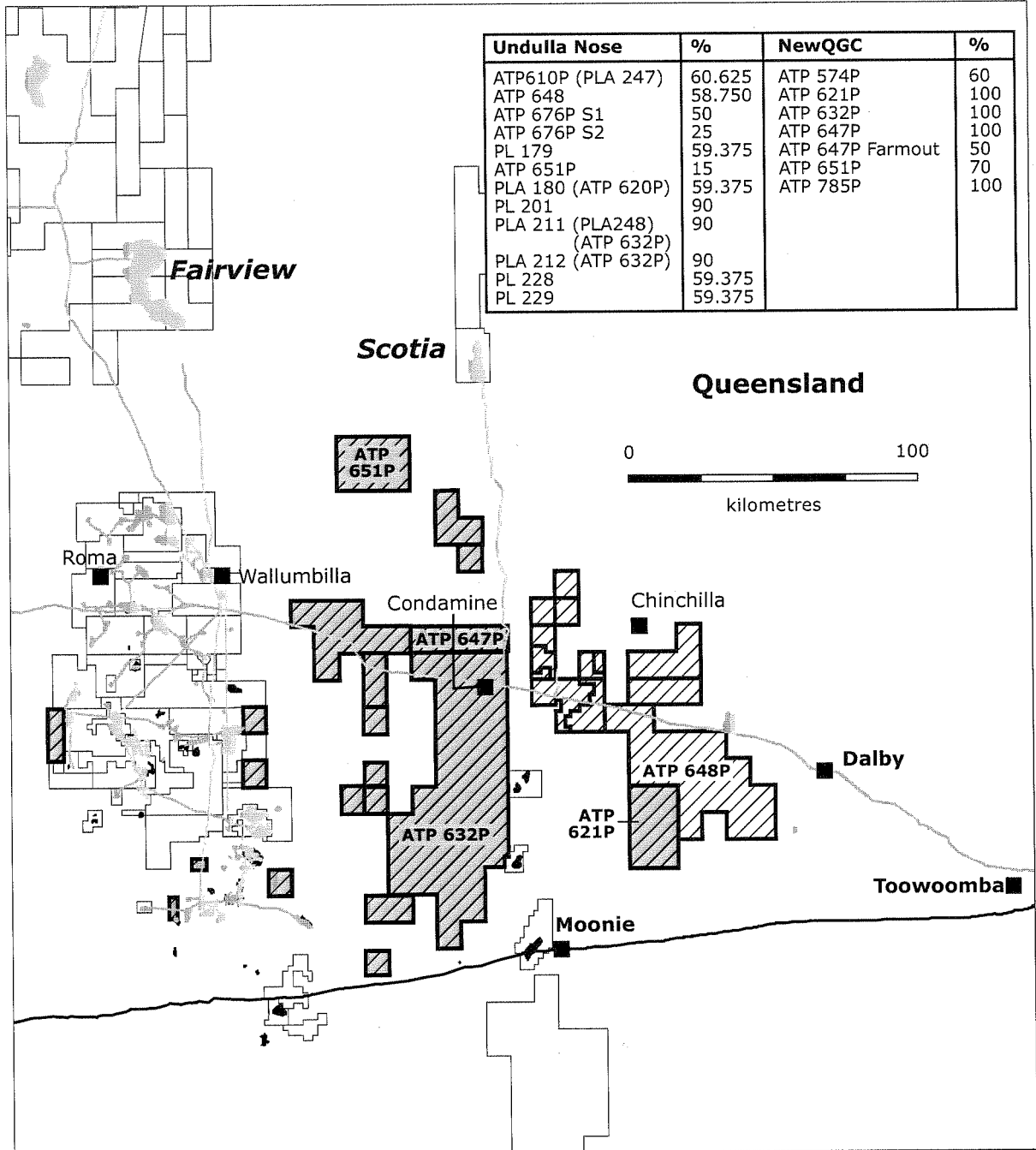
Santos will enter into undertakings with the ACCC to observe and perform the de-merger transaction agreements.

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ASX/Media Release

Santos

Surat/Bowen Basins



Legend

- Santos acreage
- Oil Field
- Gas Field
- Oil Pipeline
- Gas Pipeline
- Undulla Nose
- NewQGC

