



# Molopo Australia Limited

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13 May 2005

Mr John Feil  
Executive Director  
National Competition Council  
GPO Box 250B  
Melbourne 3001

Dear Mr Feil

Re: Coverage of Dawson Valley Pipeline

Further to recent discussions with your officers, I am pleased to provide the information as listed below to clarify and expand upon matters set out in Molopo's submission of 16 March 2005.

1) Overview of activities in Dawson Valley area

This attachment provides a brief overview and history of Molopo's activities in the vicinity of the Dawson Valley Pipeline. It is noteworthy that Molopo only completed its farm-in to these prospects early in 2001 and was not in a position to provide input to the process (conducted during 2000) by which coverage of the Dawson Valley Pipeline was revoked.

2) Copy of Media Release dated 10 May 2005

This relates to the proposed sale to Ergon Energy of gas from the Mungji field.

3) DVP Capacity Calculations

This information is to provide an indication of the capacity of the Dawson Valley Pipeline and how it might be utilised.

4) Promotion of Competition

This attachment provides background on the nature of the Queensland gas market, the role that new sources of gas supply must have if true and effective competition in the Queensland gas market is to be promoted, and the potential incentive for the owner of the DVP to abuse its monopoly position (in respect of gas transportation).

It is perhaps relevant to note that the present situation (whereby the DVP might be used for transport of other than Dawson Valley gas) is significantly different from that applying, and perceived to be possible, when coverage of the DVP was revoked in 2000.

I hope this information will assist you in your deliberations.

Yours sincerely

David Casey

## Attachment 1 Overview of Activities in Dawson Valley Area

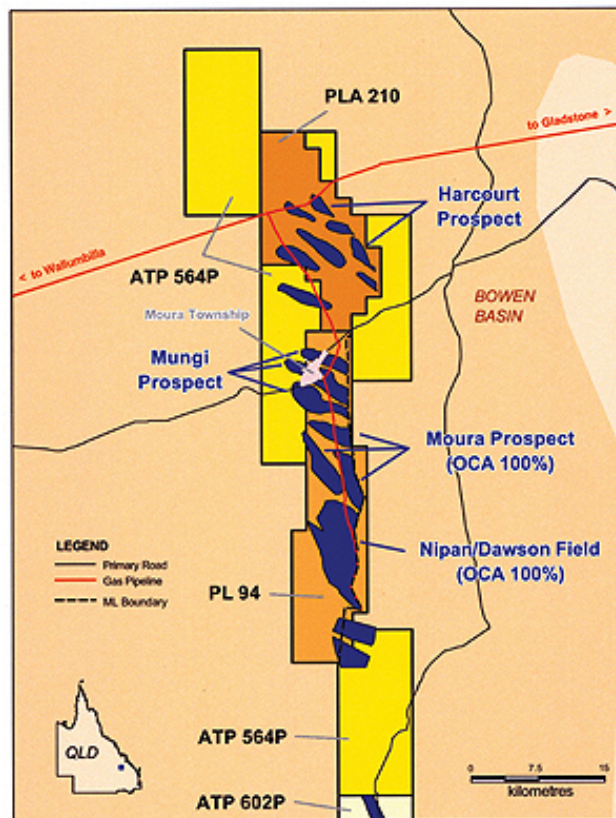
### History

On 29 March 2001, Molopo “farmed-in” to ATP 564P. The farm-in involved the acquisition from Origin Energy of a 50% interest in the Authority to Prospect (‘ATP’) in exchange for undertaking a programme of exploration activity. Molopo’s subsequently farmed-out 50% of its interest to Helm-Energy Australia LLC to provide funding for ongoing appraisal and initial development of the Mungi field. After the farm-out, Molopo’s net interest was 25%. The Mungi and Harcourt fields within ATP 564P (discussed below) have been a key focus for Molopo since this time.

In 2001/02, following encouraging results from early work at Mungi, Molopo and Helm exercised an option to acquire a 50% interest in the northern section of PL 94, in which the Mungi gas field predominantly resides. Although PL 94 is the production licence area for the Dawson Valley project, Molopo/Helm’s 50% interest (acquired from Origin Energy) does not cover the Dawson field.

In 2001/02 Molopo/Helm also agreed to farm-in to ATP 602P, which lies to the south of PL 94. That farm-in was completed in 2002/03.

A Petroleum Lease Application (PLA 210) has been made to allow for production of gas from the Harcourt and Bindaree prospects within ATP 564P.



## **Size and Potential**

The permit and production areas that Molopo is involved in (particularly ATP 564P, PL 94 and PLA 210) are strategically well-located to gain access to gas markets by means of the Dawson Valley and/or Wallumbilla to Gladstone gas pipelines.

Target coal seams within these areas are the Baralaba Coal Measures, which are attractive targets for coal seam methane exploration and production. The coal measures have pay-zones around 12 to 15 metres thick and high ( $15\text{m}^3/\text{t}$ ) gas contents. In layman terms for coal of this nature, if 50% of the gas contained within the coal can be recovered almost 5.5 PJ of gas could be available for each square kilometre of production area.

Key prospects within ATP 564P, which covers  $2,538\text{ km}^2$ , include the Mungi, Harcourt and Bindaree areas and these have been a focus for Molopo.

The Mungi Gas Field itself covers an area of  $34\text{ km}^2$  and is estimated to contain 162 PJ of recoverable gas. To-date, demonstrated reserves total 51 PJ (of which 25 PJ have been independently accredited).

## **Gas Sales**

After establishing reserves of gas in the abovementioned permit areas, Molopo began discussions with several gas users and retailers in an attempt to develop stable, long-term contracts for sale of gas. Some of the potential end-users expressed negative sentiment when informed that the DVP was owned by Origin and that it was not covered. These concerns were hard to overcome for Molopo. As a small, emerging gas producer Molopo has negligible negotiating power relative to Origin. Origin is correctly seen as Molopo's competitor for sales of gas in Gladstone. Origin is also seen as a competitor to the major, incumbent gas retailers to whom Molopo was trying to sell gas. Thus, with Origin owning an uncovered pipeline upon which deliveries of gas by Molopo are dependent, Molopo's attractiveness as a prospective supplier of gas has been compromised.

On 13 March 2004 Molopo commenced gas sales of Mungi gas to Origin. Alternative buyers could not be secured and Molopo had no choice but to sell the gas to its competitor. Molopo's negotiating position with Origin was pathetically weak in terms of both gas transportation costs and gas price. Whilst the commencement of gas sales was an important milestone, it is just the beginning in terms of the envisaged potential of the field.

On 10 May 2004 Molopo announced the establishment of a Memorandum of Understanding with Ergon Energy for the sale of up to 3.5 PJ/a of gas over a 15 year period, commencing as early as 2006. Detailed sales arrangements and gas reserves certification have yet to be completed. It is hoped that fair access arrangements will be established for the DVP in accordance with the National Access Code so that the MOU with Ergon can become a binding gas sales agreement.

## **Mungi Development to Date**

To date a total of 14 wells have been drilled at Mungi, and associated gas gathering and pipeline facilities installed. Of these, 8 wells have been drilled and completed at Molopo and Helm's cost through sole-risk provisions of the Joint Operating Agreement for ATP 564P. In addition, Molopo and Helm have installed at their own cost additional compression capacity to enable the processing of up to 6 TJ of gas per day.

While the 14 existing wells have been located to appraise as much of the field as possible, further drilling based upon recent lateral well successes is proposed in order to facilitate and optimise a gas reserves re-certification. Among other things, the re-certification will allow Molopo and Helm to meet key milestones in regard to supply of gas to Ergon Energy.

**Attachment 2  
Copy of Media Release**



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10 May 2005

(ASX Code: MPO)

**MEDIA RELEASE**

**ERGON SET TO TAKE MOLOPO GAS FROM 2006**

One of Queensland's largest energy utilities has taken initial steps to source some of its future gas supplies from coalbed methane gas producer, Molopo Australia Limited's Mungi gas field in the State's Bowen Basin.

Melbourne-based Molopo (ASX code: "MPO") announced today that a Memorandum of Understanding (MOU) signed with Ergon Energy Pty Ltd could see gas being supplied to Ergon as early as 2006.

Fully commercialised, the agreement has the potential to add a share of 3.5 petajoules (PJ) to Molopo's annual sales volumes from Mungi – more than eight times the Company's current annualised sales.

"Should those volumes be attained, it would represent a significant step-up for Molopo's production, sales, revenue and earnings outlook," the Company's Managing Director, Mr Stephen Mitchell, said today.

"The Ergon MOU is in addition to our current supply agreements with Origin Energy and Queensland Cotton Corporation and goes a long way to underpinning a founding customer base," Mr Mitchell said.

"The MOU provides for Molopo to work towards providing gas from the Mungi field to a potential new power generation project that would be established by Ergon in the vicinity of the Mungi field.

"The agreement contemplates the installation initially of one 43MW unit, with scope to explore the feasibility for an additional unit to be added at a subsequent date.

"Baseload gas requirements are currently estimated at 3.5PJ/annum per unit over a 15 year period.

"Molopo and Helm have the opportunity to provide a significant share of the eventual gas requirement with the potential to supply the total volume subject to the adequacy of gas reserves."

Mr Mitchell said Molopo and Ergon would now work collaboratively on the technical and financial feasibility of the projects and are expected to negotiate a term sheet later this year for the supply of the Mungi gas.

Following successful completion of a final feasibility study, reserve certification and a detailed engineering design, final formal documentation would then be entered into.

Mr Mitchell cautioned that much needed to be accomplished before a final binding Sales Agreement could be entered into, but said "The MOU represents a further opportunity to accelerate development of Mungi, including expanding our recent early successes with horizontal wells to boost production results."

Mr Mitchell said Molopo was in a unique position in that all new Mungi wells drilled would prove up additional reserves to satisfy the requirements for Ergon, with the gas produced from these interim wells being sold into existing infrastructure through contracts in place with other parties with strong financial credentials.

"This considerably enhances the returns from the Mungi project," he said.

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**Kevin Skinner**  
**Field Public Relations**  
**0414 822 631**

Molopo Australia Limited is an ASX listed gas producer focused primarily on the development of coalbed methane. Molopo holds a 25% interest in several gas fields located in the Bowen Basin, Queensland, a 25% interest in CBM operations located in the Gloucester Basin (NSW), a 15% interest in two permits in the Clarence Moreton Basin (NSW) and a 50% interest in the Liulin project in China.

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## **Attachment 3**

### **DVP Capacity Calculations and Potential Usage**

#### **Basis of Calculations**

Full technical details of the Dawson Valley pipeline are not publicly available. For capacity assessment purposes the following have therefore been conservatively assumed:

- Pipeline operating (inlet) pressure: 14 MPa (source: OCA submission to NCC dated 10 March 2000)
- Pipeline internal diameter: 156 mm (external diameter is 168.3 mm)
- Heating value of gas to be transported: 35 MJ/m<sup>3</sup> (being the lowest allowable heating value that will be accepted for delivery into the Wallumbilla to Gladstone gas pipeline). In comparison, the heating value of methane is 37.7 MJ/m<sup>3</sup>.
- Pipeline outlet pressure: maximum 10.5 MPa being the MAOP of the Wallumbilla to Gladstone gas pipeline (10.2 MPa) plus an allowance for pressure loss through custody transfer facilities. Note that the typical operating pressure of the Wallumbilla to Gladstone gas pipeline at the interconnection with the DVP is 8.06 MPa (source: Alinta web-site).

There are other factors (such as the internal roughness of the pipeline) that also have an impact, albeit second-order in magnitude, upon the capacity of a gas pipeline. Industry indicative values have been assumed for these factors.

#### **Pipeline Capacity**

For the assumptions set out above, the estimated capacity of the DVP to transport gas over 47 km (from inlet to outlet) is 35 TJ/d. This of course assumes that sufficient compressor capacity is available to ensure a gas pressure of 14 MPa at the inlet of the pipeline.

If the outlet pressure requirement is reduced to 8.4 MPa (a margin above the typical outlet pressure requirement of 8.06 MPa) the capacity of the DVP would be around 47 TJ/d.

#### **Pipeline Utilisation**

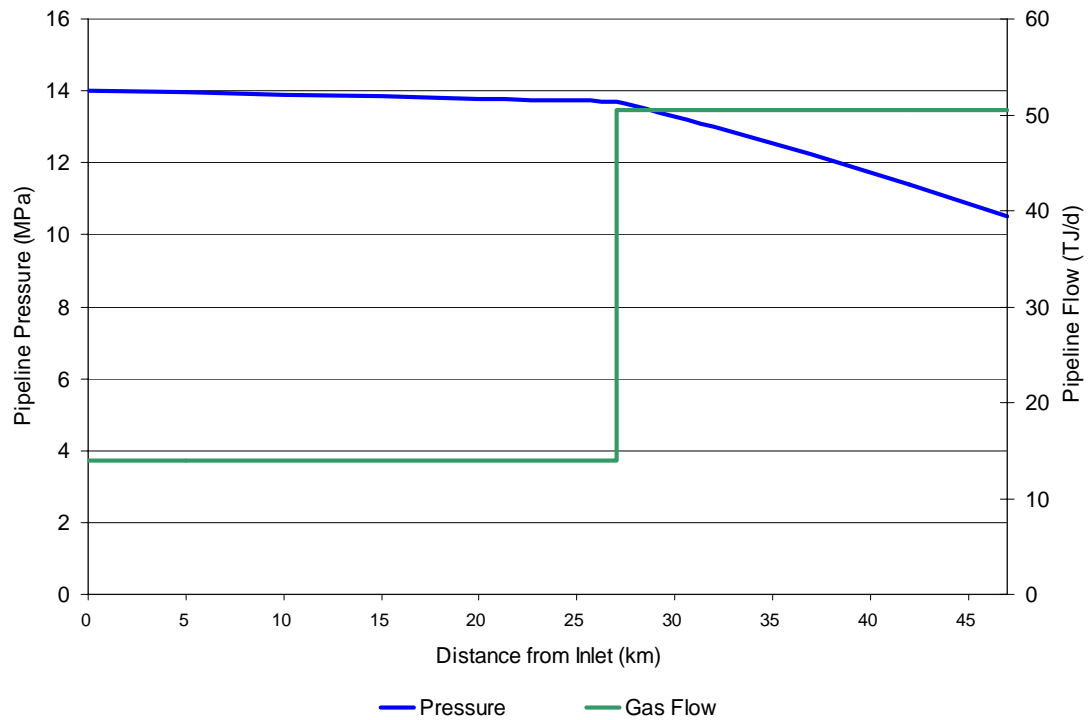
OCA has advised (submission to NCC dated 10 March 2000) that the requirement for capacity for transport of Dawson Valley gas may reach 14 TJ/d<sup>1</sup>. This leaves considerable capacity available for other users.

The following chart illustrates the performance of the DVP on the basis that it is used to transport:

- 14 TJ/d of gas over the full length of the pipeline; and
- additional gas over the final 20 km of the pipeline.

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<sup>1</sup> OCA referred to a capacity requirement totalling 70% of 20 TJ/d.



Indications are that, in addition to 14 TJ/d of gas from Dawson Valley, the DVP could transport around 35 TJ/d of gas from the Mungi location (27 km from the inlet of the pipeline) to the Wallumbilla to Gladstone pipeline. For this scenario, the maximum pipeline outlet pressure requirement (10.5 MPa) would be satisfied. As may be seen in the chart above, the rate of pressure decline in the DVP would increase after the injection of Mungi gas.

## **Attachment 4 Promotion of Competition**

***For a gas market to be truly competitive there must be competition between gas producers.***

A necessary pre-condition to the development of a competitive gas market is that gas users have the right to purchase gas from their supplier(s) of choice. But having this right does not, of itself, make a gas market competitive.

For a gas market to be truly competitive there must be competition between producers of gas that supply into the relevant market. Regardless of whether there may be multiple retailers of gas, if there is no competition between producers the prices at which end-users can purchase gas will reflect the wholesale price required by the producer(s) plus downstream delivery and market costs. In the absence of competition between producers, the wholesale price will be that which maximises the producers' revenue, and may tend toward the user's costs of competing fuels less the costs of gas delivery (that is, what the market can bear).

***Competition is only effective if supply is not constrained.***

Similarly, the presence of multiple gas producers does not make for effective competition in a gas market unless those producers have reserves of gas available for supply. This is evidenced in the US where, because there are shortages of gas, gas prices are high despite the presence of many gas producers, many retailers and many customers.

For competition to be effective, there needs to be some gas available in excess of market requirements. The extent of the excess need not be large since, through innovative ('building-block' type) purchasing strategies, all gas-users can benefit from effective producer competition

***The benefits of true and effective competition are potentially significant.***

The benefits of true and effective competition have been evident in the Western Australian gas market, where there have been multiple producers of gas with and ability to supply gas at rates that exceed the total market requirement. After Western Australian gas markets were opened to competition in the 1990's, the physical availability of gas from multiple producers meant that competition within the market was both true and effective.

During the 1990's, wholesale gas prices in Western

Australia fell in nominal terms from the levels that had prevailed after the introduction of Northwest Shelf gas in the mid 1980's.

***There is not yet effective competition in the Queensland gas market.***

The foundations are in place for effective competition in the Queensland gas market in that:

- gas users have choice of supplier; and
- there are multiple (albeit small) gas producers.

However, Queensland gas users do not yet enjoy effective competition. Despite the presence of multiple gas producers, gas supply is constrained. Clear evidence of this is the nature of the gas purchase arrangements that prospective gas users have entered – that is, contracts that are dependent upon gas reserves being proven.

There are no uncommitted sources of gas presently available for delivery in Queensland. Therefore, the Queensland gas market does not have effective competition.

***Competition between developers of prospective reserves of gas is desirable but not ideal.***

Prospective gas users in Queensland have made commitments to purchase gas from prospective (rather than proven) reserves. To the extent, if any, that multiple parties (or 'developers') may be able to formulate programmes to meet the prospective purchaser's gas requirements, the purchaser may enjoy some competition for supply.

Competition between developers of prospective reserves is not as effective as competition between producers of gas from proven reserves. This is because, inherent in the purchase of gas from a developer, there is some transfer reserves risk to the gas purchaser. There is no certainty that gas will be available in the time-frame and quantities to meet the users' needs.

Gas users in the Queensland gas market do not yet enjoy the benefits of effective competition.

***Additional supplies of gas are essential in order to promote competition in the Queensland gas market.***

True and effective competition in the Queensland gas market will only be achieved if, and when, there is sufficient gas available from gas producers to allow gas-users and retailers to have a real (rather than a theoretical) choice of supplier.

Facilitation and development of new sources of gas production is essential.

***The Mungi gas resource may be small but it is nonetheless important***

Mungi and surrounding gas resources, that may be delivered through the DVP, already play an important role in the Queensland gas market. The prospective gas resources of these markets can be offered for development and supply as a competitive alternative to other prospective resources. The recently (10 May 2005) announced potential sale of gas from the Mungi field to Ergon Energy is a perfect example of this.

However, the key to effective competition (that is, a competitive environment where gas users rather than gas producers enjoy the benefits of competition in the market place) is to have gas available from producers at an aggregate rate that exceeds the market requirement for gas.

Gas supplies available to the Queensland gas market are presently less than the potential market requirement, as evidenced by the conditional gas purchase arrangements, or similar, entered into by parties including Energex (from QGC), CS Energy (from QGC and Arrow Energy) and Ergon (from Molopo).

The expanded availability of gas from any producer is of value in changing the supply-demand balance.

***Effective competition may be opposed by major producers.***

As was the case in WA, should competition in the Queensland gas market become effective (through competition at the producer level) there is little doubt that wholesale gas prices will either fall or be constrained (ie, prevented from rising). This may compromise the earnings potential of major gas producers.

***Origin Energy is the dominant supplier of CSM in Queensland.***

Origin Energy, through Oil Company of Australia ('OCA') subsidiaries, is the pre-eminent producer of coal seam methane within Queensland<sup>2</sup>, producing 25 TJ/d (or 60% of the coal seam methane sold within the state).

***There is a significant incentive for OCA to abuse its monopoly powers in respect of the DVP.***

Any decline of or constraint to the wholesale price of gas for the Queensland gas market will erode the earnings potential of OCA's coal seam methane production activities.

A small reduction in the price that is achievable for sales of large quantities of coal seam methane would

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<sup>2</sup> Source: Queensland Government:

[http://www.nrm.qld.gov.au/mines/petroleum\\_gas/csg/review.html](http://www.nrm.qld.gov.au/mines/petroleum_gas/csg/review.html)

OCA produces at least 25 TJ/d of gas for supply into the Queensland gas market.

far outweigh any financial benefit that might be realised through transportation of modest quantities of gas from the Mungi project. To put this into perspective, a mere 3 cents per Gigajoule decrease in the wholesale price of gas in the Queensland gas market would reduce OCA revenue by around \$275,000 pa.

There can be no doubt that OCA would benefit from sustained, high wholesale gas prices. There is therefore a potential incentive to exercise monopoly powers to restrict, or to increase the cost of, delivering gas from the Mungi field to the Queensland gas market.

***The NCC has identified how Coverage Criterion (a) should be assessed.***

In the final recommendations made by the NCC<sup>3</sup> in relation to applications for revocation of certain gas pipelines in Western Australia from coverage under the WA Gas Access Regime, the NCC made the following statement regarding Coverage Criterion (a):

“In general, while a trivial increase in competition would not be sufficient, the Council considers access would not need to substantially promote competition in order to satisfy this test. The Council’s approach is to:

- verify that the market in which competition is said to be promoted is separate from the market for the service; and (if so) then
- determine if access (or increased access) would promote competition in this separate market.

In the case of the 44 km Kalgoorlie to Kambalda gas lateral in Western Australia, the NCC determined that Coverage Criterion (a) was satisfied because access to the lateral would facilitate development of a gas pipeline between Kambalda and Esperance<sup>4</sup> (a distance of about 330 km) and, in turn, could promote competition in the markets for water and energy.

***The availability of Mungi gas promotes competition.***

The prospective gas reserves of the Mungi and surrounding gas resources are significant in that they already play an important role in providing a competitive alternative for gas users in a market place where gas supply is constrained. This was clearly demonstrated by the recently announced MOU with Ergon Energy.

Proving up and development of the Mungi and surrounding gas reserves (despite their small size relative to the total Queensland market) may give rise

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<sup>3</sup> June 1999

<sup>4</sup> A gas pipeline between Kambalda and Esperance has now been developed.

to, and will at least contribute to, development of effective competition in the Queensland gas market.

***Mungi gas is delivered through the DVP.***

The availability of Mungi gas to gas users in the Queensland gas market is dependent upon the availability of access to the DVP. The DVP is owned by a competitor of Molopo and a competitor of some of Molopo's prospective customers. This has proved to be a constraining factor in securing contracts to allow sales of gas.

***Access to the services provided by the DVP will promote competition.***

Access to the DVP will facilitate deliveries of gas as development of the Mungi and surrounding gas fields proceeds and, in accordance with the NCC's stated requirement, will promote competition in the Queensland gas market.