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The Secretary
Ministry for the Environment
PO Box 10362
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Our ref 090709gassubmission.doc

13 July 2009

Dear Sir

Submission on Climate Change (Stationery Energy and Industrial Processes) Regulations 2008

We write on behalf of our client, Australian Worldwide Exploration Limited (“AWE”), to provide a submission on the draft Climate Change (Stationary Energy and Industrial Processes) Regulations 2009 (“draft SEIP”). AWE welcomes the chance to submit on the draft SEIP.

AWE is an Australian based oil and gas exploration company listed on the Australian Stock Exchange.

AWE currently has a 42.5% share in the Tui oil field, for which it is operator of the Tui Joint Venture Partners (“the Tui JV”). AWE is also the operator for several exploration permits, (PEP38481/2/3, 38401, 38499 and 385240), offshore Taranaki and the South Island.

At present gas produced from the Tui Field is not sold into the New Zealand pipeline. Between 35-45% is currently used for fuel gas and the remainder is flared. As production diminishes the percentage of flared gas will also reduce (as the fuel gas usage is constant) to a point where there will be minimal gas flared.

The Tui JV is currently investigating the viability of constructing an export pipeline to a neighbouring facility to minimize flaring and make the gas available to the New Zealand pipeline.

1 Overview

AWE has a number of concerns about the proposed regulations, in particular:

- That the factor for losses should be removed or, alternatively, gas which is flared or used for fuel should be excluded from the basis for allocation of the national losses;
- Measurement of the quantity of natural gas by fiscal meter and gas chromatography and the frequency of the measurement required;

- The participant being the Tui JV itself, and the Tui JV partners each being joint and severally liability for its other JV partners emissions liabilities; and
- The ability for a purchaser of gas from AWE to become an opt-in participant and the ability for the opt-in participant to rely on information supplied by AWE.

These concerns are elaborated upon below.

2 Distribution Losses

2.1 *Inequity of including “own use” and flaring*

In the draft SEIP a new factor for ‘losses’ has been included.

Losses from the transmission and distribution network and from unaccounted-for gas (which are largely metering inaccuracies in the transmission and distribution network) are included in New Zealand’s Greenhouse Gas Inventory and therefore form a part of New Zealand’s overall emissions liability.

AWE understands that due to the difficulty in measuring the losses, the current proposal in the draft SEIP regulations allocates a share of the national losses to each participant in proportion to their share of the total national gas production. The current losses factor is 1.75%, which has the effect of increasing each gas producer’s carbon liability by the same percentage.

The proposed method of arbitrarily allocating the national losses to each gas producer will mean that a portion of the national gas loss is attributed to gas producers who only flare and/or use their own production for fuel.

AWE recommends that if the factor for losses is retained (which, as discussed below, AWE recommends it is not) then gas that is flared and/or used as fuel should escape an allocation of the national losses on the basis that the production never enters the transmission and distribution network.

2.2 *Distribution losses – double counting*

We understand that the formula as it stands is based on the European calculation, which defines the ‘point of sale’ as when the gas leaves the pipeline. Therefore, under the European model, a gas loss adjustment is required, as the losses will typically have occurred prior to the ‘point of sale’.

Under the draft SEIP the formula for calculating the liability of participants (which is set out in clauses 16 and 49 for mandatory and opt-in participants respectively) requires measurement of the quantity of gas produced to occur at the ‘point of sale’.

However, the New Zealand ‘point of sale’ differs from European ‘point of sale’. New Zealand ‘point of sale’ is effectively the point where the gas leaves the processing plant and immediately before it enters the pipeline, which for most fields is at the fiscal gas sales meter(s) at the plant boundary, i.e. before the ‘losses’ have typically occurred.

However, an adjustment is then added for the gas producer’s share of national gas losses.

AWE considers that the inclusion of the losses in the formula results in double counting. This is because the unit obligation is now imposed on volumes of gas measured at a point upstream of the point(s) where the gas losses (metering inaccuracies) occur.

Therefore, to avoid this double counting, AWE recommends that either:

- 1 The gas loss adjustment is removed; or
- 2 The point of sale definition is amended (i.e. moved downstream to where the gas leaves the pipeline’).

Given that the move to a point of sale at the processing plant appears to have gained widespread support within the industry, AWE recommends the best approach is to remove the gas loss adjustment. Especially as this reduces any arbitrary allocation as the actual gas entering the pipeline is accurately measured.

3 Emission Factors – measurement by fiscal meter and gas chromatography

3.1 Measurement in GJ

As the draft SEIP currently stands, the quantity of gas produced is measured at the point of sale by fiscal meter in tonnes and the composition of the gas, by gas chromatography.

However, we note that gas is usually sold in GJ. Therefore, for ease of compliance AWE recommends that the formula be changed to allow measurement in GJ rather than tonnes.

3.2 Sampling and testing using gas chromatographic analysis

The draft SEIP specify that the total mass of CO₂, mass of the gas and total terajoules of the gas is to be determined using gas chromatography in accordance with certain standards by a person who is accredited according to ISO 17025:2005.

Currently, it is unclear from the regulations what the requirement to test the gas (by gas chromatography) will mean in practice, how frequent this testing will be required and how the composition of the gas will be measured. Consideration needs to be given to these requirements and the frequency of the testing. AWE notes that frequent testing would result in a substantial

cost to AWE and other small-scale miners with little benefit to the accuracy of the emissions calculations.

AWE also notes that chromatographic analysis, while appropriate for the gas sold to the New Zealand pipeline, is not appropriate for AWE's gas, which is used currently as fuel gas or is flared. AWE recommends that an alternative method, which is not cost prohibitive, needs to be discussed and agreed for small-scale gas miners such as AWE. AWE notes that, currently, there is only one test laboratory in New Zealand and understand that the cost of testing each sample is \$275-\$300.

AWE proposes that an alternative method is agreed through consultation on a field-by-field basis to determine the composition of each gas field.

AWE notes that the cost of implementing a gas chromatography system would be significant, (potentially in the millions) when the loss of revenue from ceasing production to implement such a system was taken into consideration.

AWE recommends instead a testing regime that is not prohibitively expensive - perhaps quarterly.

Once the composition of the gas is determined, the volume of the gas can be measured by gas meter each year.

3.3 *Appropriate Verification Regime*

At present, the draft SEIP require that a person who is accredited according to ISO 17025:20 tests the gas but there are no verification requirements for the sampling and testing regime prescribed. AWE understands that consideration is being given to what an appropriate verification regime might be and whether verification should be by an approved verifier.

AWE understands that the only approved New Zealand verifier laboratory has advised that the cost would increase to approximately \$500 per sample if the samples were required to be verified. AWE sees little value in requiring the verification of tests especially where the composition of the gas does not shift (as noted above).

3.4 *Unique Emission Factor*

The draft SEIP contain a provision for participants to elect to use a unique emission factor in place of the default emissions factor for unprocessed gas, flaring, venting, processed gas, LPG, specification gas, and geothermal fluid. This unique emission factor can be used to calculate and report on emissions in accordance with the SEIP regulations and the Unique Emission Factor regulations.

AWE see the ability to elect a unique emission factor as a positive step as the emission factors for the various fields differ substantially and the default emission factor may overestimate emissions by the Tui JV.

4 Opt In – Joint Venture is the Participant

Wholesalers or end users of natural gas who purchase more than two petajoules of natural gas per annum may wish to opt in to participate within the NZ ETS as a natural gas purchaser in order to ensure that they retain control over the cost to them of the NZ ETS scheme.

However, to opt in, the opt-in participant needs to purchase the gas from one or more “participants” who mine the natural gas. In this context, a “participant” as outlined in section 157 of the Climate Change Response Act 2002 (“CCRA”) appears to be the joint venture as a whole, not the individual joint venture parties.

There is a potential issue as, in practice, each producer usually sells gas individually rather than by the joint venture as a whole. Therefore, a purchaser who, typically, is acquiring gas from an individual joint venturer is arguably not purchasing gas from a mandatory participant and, therefore, cannot opt-in. Although AWE does not currently sell gas, AWE may in the future sell gas and wishes to see the issue rectified on this basis. It was apparent from the discussion at the gas sector workshop on NZETS Reporting Requirements that this was also the view of officials.

AWE proposes that the Act requires amendment to give rise to its intended effect that the wholesalers and end users should be able to opt-in and control the cost of the emission liability arising from the gas purchased.

Alternatively, amending the law, as outlined below, to make each producer the mandatory participant would suffice.

5 Liability at Joint Venture Level

A further issue of the joint venture being the mandatory participant is that the joint venture is jointly and severally liable for the emissions produced by the activities of the joint venture as a whole under section 157 of the CCRA.

AWE considers that the individual producers should be the mandatory participants, rather than the joint venture for two reasons:

- The first reason is that it removes a contingent liability, which will need to be recorded for accounting purposes in relation to the other Tui JV party’s emissions liabilities and which could crystallise if any of the other Tui JV parties failed to meet their unit obligations at any time in the future.

- A second reason is that it would then be considerably simpler for each producer to control the acquisition of emission units to cover their share of the total surrender obligations, and would enable producers to adopt a “portfolio” approach to managing their obligations when they have interests in multiple joint ventures.

AWE therefore proposes that section 157 of the CCRA is amended so that the parties to an unincorporated joint venture such as the Tui JV are not aggregated as the participant and are not jointly and severally liable for the obligations of the other JV parties.

6 Opt In – provision of information and penalty exposure

The draft SEIP require the opt-in participant to report emissions using the same information as an obligation participant (i.e., the gas producer). This requires that the opt-in participant be able to access the required data from the producers.

At present, there appears to be no information sharing obligations imposed by the CCRA or the draft SEIP.

AWE is concerned that the draft SEIP will be amended to require the provision of information to opt-in participants but without any provision for limitation of liability for the gas producer in the event that the information is incorrect and penalties are imposed on the opt-in participant.

AWE submits that if information sharing obligations are included in the draft SEIP, there should also be provisions to the effect that, if a producer provides information in error (but in good faith), then that is a complete defence against penalties for the opt-in participant.

7 General

I hope these comments are of some assistance. Please do not hesitate to contact AWE or myself if there are any matters that you would like to discuss. AWE and KPMG look forward to discussing these comments with you in the near future.

Yours sincerely



Greg Bishop
Partner