Attachment 1

1. INTRODUCTION TO CONOCOPHILLIPS

ConocoPhillips Australia is an oil and gas exploration and production company which holds a significant acreage position in the Timor Sea Joint Petroleum Development Area (JPDA) between Timor-Leste and Northern Australia. This is the site of the company's Bayu-Undan Field which is in production, and which is bringing significant income and jobs to Australia and East Timor. The gas from the Bayu-Undan Field is piped 502 kms from the offshore production facilities to the LNG Facility located at Wickham Point, Darwin. The company's other operations in Australia are located offshore Western Australia and offshore and onshore Northern Territory and ConocoPhillips has significant interests in Queensland's coal seam gas. Over 450 employees work through business centres in Perth, Western Australia; Darwin, Northern Territory; Dili, Timor-Leste; and Brisbane, Queensland.

ConocoPhillips Australasia is a subsidiary of ConocoPhillips, an international integrated energy company, headquartered in Houston, Texas. ConocoPhillips has been making LNG since 1969 (in Kenai Alaska), operates in nearly 40 countries, has approximately 33,000 employees worldwide and has assets of US$143 billion.

1.1 CONOCOPHILLIPS WORLDWIDE

It is important to note that in making this submission ConocoPhillips, as a world-wide company, recognises and takes its responsibilities to the societies in which we operate, and to the environment, very seriously.

The basic premise of our concern with the Australian Government's Carbon Pollution Reduction Scheme in so far as it relates to LNG is reflected in the principles set out in our Climate Change Position – a copy of which was attached to our submission on the Carbon Pollution Reduction Scheme Green Paper refer;
http://www.climatechange.gov.au/greenpaper/consultation/pubs/0422-conocophillips.pdf.

ConocoPhillips is also a member of the United States Climate Action Partnership (USCAP), details of which can be found at http://www.us-cap.org/. This is a group of businesses and leading environmental organisations that have come together to call on the US Federal Government to quickly enact strong national legislation to require significant reductions of greenhouse gas emissions to underscore the urgent need for a policy framework on climate change.

USCAP has issued a landmark set of principles and recommendations as follows:

- Account for the global dimensions of climate change;
- Create incentives for technology innovation;
- Be environmentally effective;
- Create economic opportunity and advantage;
- Be fair to sectors disproportionately impacted; and
- Reward early action.

1.2 DARWIN LNG

ConocoPhillips is the operator and majority interest owner of the Darwin LNG facility located at Wickham Point, Darwin. Darwin LNG and the North West Shelf LNG facility are the only two LNG export facilities in Australia. Darwin LNG was completed and began full operation in 2006. The Darwin LNG facility currently produces approximately 3.5 million tonnes of LNG per year, which is subject to an LNG Purchase and Sales Agreement to Tokyo Electric and Tokyo Gas in Japan for an initial period of 17 years. Other equity owners of the Darwin LNG plant (held through various affiliated entities) are Eni, Santos, INPEX, and Tokyo Electric and Tokyo Gas.

ConocoPhillips has plans to expand its LNG facilities in Darwin and the current site at Wickham Point has environmental approval for up to 10 million tonnes per annum.

1.2.1 INNOVATIVE TECHNOLOGY

The Darwin LNG plant uses the ConocoPhillips Optimised Cascade(RM) Process as the basis for its LNG liquefaction technology. It was first used in 1969 in ConocoPhillips' Kenai LNG plant in Alaska and since then has been licensed by owners of additional trains including Atlantic LNG, Egyptian LNG, Equatorial Guinea LNG and Angola LNG.

In the design and construction of the Darwin LNG plant (which commenced construction in 2003), ConocoPhillips took the opportunity to incorporate the best available emission reduction technology. Innovative solutions for optimising environmental outcomes were developed with the result that Darwin LNG includes:

- The use of high efficiency, low emission, aero-derivative gas turbines for refrigerant drivers. It should be noted that the Darwin LNG plant is the first to use these turbines in this application. Improved thermal efficiency reduces fuel requirements that result in a reduction of greenhouse gas emissions (3.7% as compared to the original design case for the project).
- The installation of waste heat recovery units on the gas turbine stacks, which has minimised the usage of a dedicated boiler for plant heating requirements and resulted in a greenhouse gas reduction of 9.3%.
- Vapour recovery during LNG ship loading has reduced emissions associated with flaring this stream, resulting in a reduction in greenhouse gas emissions of 4.4%

Collectively, these technologies reduce emissions at Darwin LNG in the order of 20% compared with what could have been built at the time.

ConocoPhillips is maximising ongoing opportunities to minimise venting, such as the arrangement with BOC to establish a helium plant (currently in construction) alongside our Darwin LNG facility to utilise the vent stream from our nitrogen rejection unit as feedstock for helium.

The innovations and technology improvements at Darwin LNG were undertaken at considerable expense. However, the Carbon Pollution Reduction Scheme not only does not take account of improvements in design and actions undertaken, but by improving efficiency and minimising emissions, it actually penalises such activity.

1.2.2 GREENHOUSE CHALLENGE PLUS

In Australia, the management of greenhouse gas emissions has continued to be in the forefront of our operations. For example, in 2006 we joined the Greenhouse Challenge Plus Programme, with our first report being submitted in 2007. We also elected to take a "beyond compliance approach" in our participation in the government's energy efficiency opportunities programme.

1.2.3 WAFMA

In the first agreement of its kind, ConocoPhillips (through Darwin LNG) signed an agreement with the Northern Territory Government and the indigenous landowners in a wildfire (i.e. savannah burning) management programme that reduces greenhouse gas emissions while preserving the cultural traditions of indigenous landowners. This programme which is administered by the NT Government is known as the West Arnhem Fire Management Agreement (WAFMA).

The WAFMA Project has been exceptionally innovative and, in the context of statements made in the White Paper, WAFMA:

- Is certified by the Australian Greenhouse Office as an offset;
- Has already been (for several years) providing indigenous jobs; and

- For several years has been providing a Greenhouse offset, with approximately 180,000 tonnes CO2-e/year for the calendar year of 2007 alone, which is in the order of 10% of Darwin LNG's emissions. An abatement certificate was attached to our submission to the Senate Economics Committee and is available on the web at http://www.aph.gov.au/senate/committee/economics_ctte/cprs_09/submissions/sublist.htm, as submission No 68. The results for calendar year 2008 are not yet officially available but are understood to be a comparable order of magnitude.

In August 2007, the WAFMA project won the IAG Eureka Prize for Innovative Solutions to Climate Change presented by the Australian Museum. Further details on WAFMA are available at http://www.atns.net.au/agreement.asp?EntityID=3638 while details on this award are available at http://www.austmus.gov.au/eureka/index.cfm?objectid=55A0F975-EAA1-4C4E-5506CBAC18FDEA41.

Additional details on WAFMA are available from NT Bushfires or from ConocoPhillips.

2. CRITIQUE OF THE CPRS

In light of the above demonstrated commitment to greenhouse emissions reductions and innovation, we believe we are well placed to provide a rational critique of the CPRS. Our critique is divided into the following key areas:

- CPRS Design;
- Savannah Burning;
- JPDA/Sunrise;
- Timeline;
- Regulations; and
- Climate Change Action Fund.

2.1 CPRS DESIGN

During the 2007 election campaign the Australian Labor Party canvassed on the premise in its Resource Sector Policy Paper, which is available at http://www.alp.org.au/download/now/071122___labors_plan_for_a_stronger_resources_sector222_xx.pdf, the following:

> *"Labor recognises that the transition to a more carbon constrained economy has the potential to disadvantage emissions intensive trade exposed industries. There is no global environmental benefit to simply shutting down LNG plants or aluminium smelters in Australia only to have new plants open up in other countries which may have inferior environmental protection standards and higher emission intensities.*
>
> *A Rudd Labor Government will:*
> - ***Ensure that Australia's international competitiveness is not compromised by the introduction of emissions trading**.*
> - *Consult with industry about the potential impact of emissions trading on their operations to ensure they are **not disadvantaged**.*
> - *Establish specific mechanisms to ensure that Australian operations of emissions intensive trade exposed firms are not disadvantaged by emissions trading.*

Further, in the Renewable Energy Policy Document which is available at http://www.alp.org.au/download/now/071030_renewable_energy_policy___xx.pdf, the ALP quoted similar sentiments "*As part of its comprehensive approach to climate change, Labor has already indicated that it will develop mechanisms to **ensure that Australian operations of emissions-intensive trade-exposed firms are not disadvantaged before an effective global regime is in place**."*

The CPRS in all of its evolutions, including the current version, does not meet the two primary tests of “compromised” nor “disadvantaged” before an effective global regime is in place.

In the context of no global agreement, the CPRS (in all of its evolutions to date) will adversely affect the international competitiveness of Australian industries which are trade exposed, including the LNG industry. We therefore call upon the Government to focus on trade-exposure.

The White Paper notes that business “can afford” 2.5% loss of revenue. This arbitrary figure of “2.5% of revenue” is premised on the current “eligibility” criteria for 60% assistance being 1000 tonnes CO2e/$million revenue, and assuming an initial CO2e permit cost of $25. It should also be noted that LNG is very capital intensive and so in this context revenue is not the most appropriate measure of cost impact.

The arbitrariness of this figure was demonstrated when the eligibility criteria were significantly reduced between publication of the Green Paper and publication of the White Paper

The criteria were called into question by the Government considering a value-add “option” after release of the Green Paper. The value-add concept does not represent a true value of doing business; hence it made little difference to many trade exposed industries, like the LNG industry.

In its release of the White Paper, the Government referred to the CPRS with the statement “*Implementing the Scheme represents the biggest structural economic reform since the opening up of Australia's economy in the 1980s and 1990s.”* This was repeated at the National Press Club release of the CPRS when Mr Rudd said “*Today, the Australian Government announces one of the largest and most important structural reforms to our economy in a generation - the introduction of a national Carbon Pollution Reduction Scheme.”*

Given that this is such a large economic reform proper due diligence and consultation should be conducted to ensure the Scheme’s efficacy and that it meets the criteria laid out by the Government. Current indications raise considerable concern that the fundamental design of the Scheme does not meet these criteria as premised by the Government and that the time should be taken to properly address and evaluate these concerns rather than simply pushing for an outcome (i.e. to have a scheme, any scheme, in place by 1 July 2010) regardless what it really means to business or the environment.

It should be noted that Australia represents in the order of 1.5% of global GHG emissions and so even if Australia turned everything off, we would have a miniscule effect on reducing global emissions which will continue to rise strongly in most forecasts – a position echoed by Professor Garnaut. In such a case Australia will still be potentially adversely affected in spite of a 100% reduction of our emissions. That is not to say that Australia should not take its place as a leader in reducing global greenhouse gas emissions but should do so in a manner that meets the Government’s own criteria of not damaging Australia’s international competiveness and of reducing carbon pollution.

If Australia’s LNG/gas exports were reduced, global GHG emissions may actually increase, as less clean burning fuels such as coal would make up the shortfall in the world’s energy demand. This is because, as is widely published, coal emits in the order of twice the emissions of an LNG development over its lifecycle to meet a given electrical demand. This point is acknowledged by the Australian Labour Party
http://www.alp.org.au/download/now/071122___securing_a_sustainable_energy_supply_for_australias_future_xx.pdf.

Therefore, if Australia has the wrong system in place it will have a significant negative effect on business and the Australian community.

We wish to now turn to the actual impacts of the CPRS on the LNG industry.

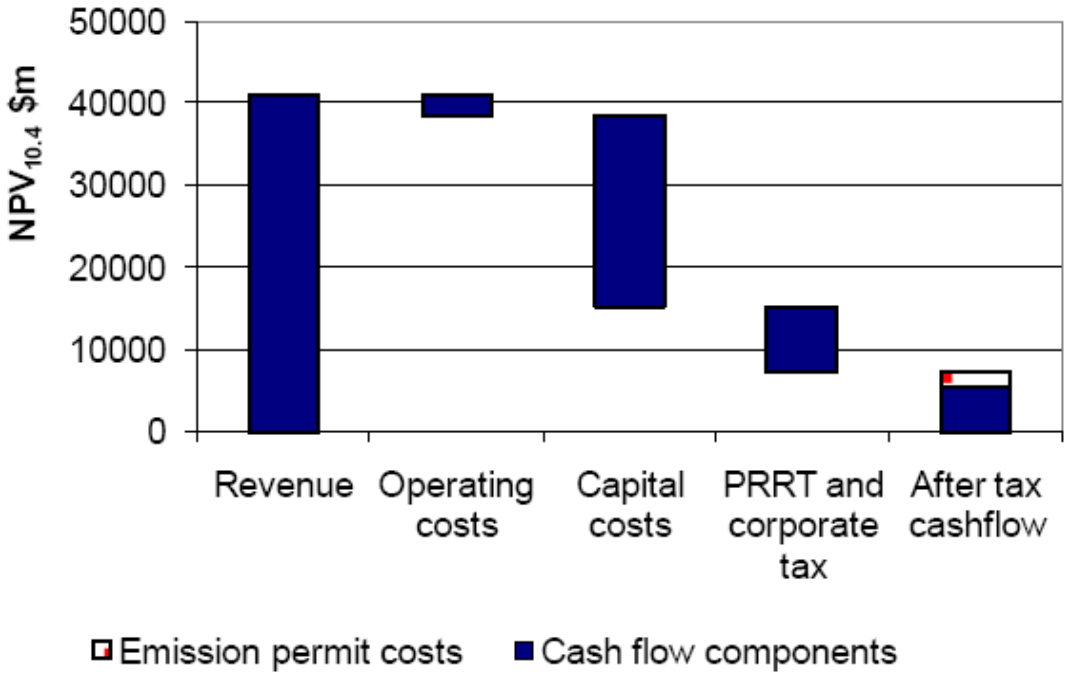
AcilTasman prepared a report on behalf of the LNG industry after the Green Paper was released and prior to release of the White Paper. That assessment (available publically at http://www.aciltasman.com.au/images/pdf/LNG_CPRS_report_081008.pdf) was premised on 3 typical LNG developments of various sizes, and assumed no assistance at all.

The following is an extract from the Executive Summary of that report:

> *"The paper concludes that a carbon charge starting at between $20 to $40 per tonne in 2010 – and escalating over time in real terms – would reduce significantly returns to a typical green fields two train, 10 million tonnes per annum (Mtpa) LNG development by:*
> *• increasing operating costs by up to 130 per cent*
> *• increasing direct government payments by as much as $3.4 billion in Net Present Value terms over the life of a typical development, taking the effective tax rate from 36 to 43 per cent of earnings before taxes and charges*
> *• reducing the Net Present Value of after-tax cash flows by up to 29 per cent.*
>
> *In consequence, a carbon charge has the potential to push final investment decision metrics – which are already marginal – into negative territory."*

The report demonstrates pictorially in Figure ES1 (copied below as Figure 1) that most (~84%) of the "revenue" is absorbed by "capital costs", "taxes" and "operating costs".

Figure ES 1 **Development economics – net present value of cash flows for a 10 Mtpa project with emissions charge starting at $20 per tonne**



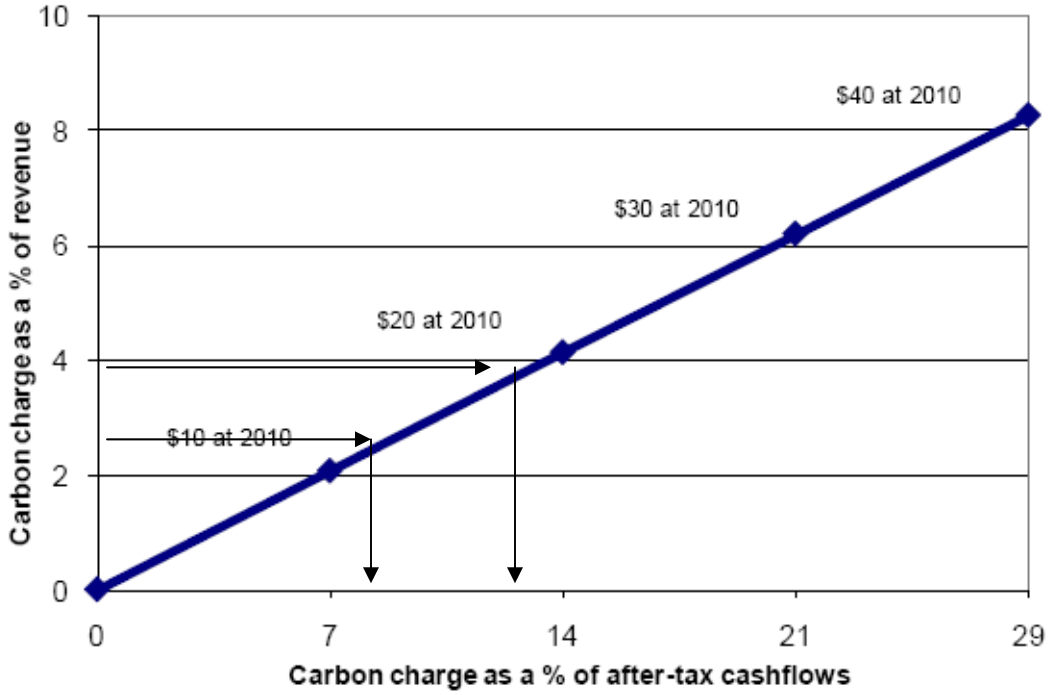
Notes: $NPV_{10.4}$ refers to Net Present Value of post tax cash flows discounted by a nominal 10.4 per cent post-tax discount rate. The analysis presented in this figure assumes central estimates for LNG prices, capital expenditures and field performance.

Data source: ACIL Tasman

Figure 1 – Typical LNG Development Cost Breakdown.

The report demonstrates in Figure ES2 (copied below as Figure 2) the effects of "loss of revenue" on "loss of after tax cash flow".

Figure ES 2 **Impact of increasing the carbon price – 10 Mtpa development**



Note: The analysis assumes central estimates for LNG prices, capital expenditures and field performance.

Data source: ACIL Tasman analysis

Figure 2 – Carbon Cost Impact on Revenue and After Tax cash Flow

The Green Paper proposed that 3.75% loss of revenue[1] was considered "acceptable", however Figure 2 translates this to nearly 13% loss of after tax cash flow as being considered "acceptable" to the Government. This is a fundamentally flawed assessment of the capacity of businesses (such as LNG) to absorb arbitrarily assigned costs and this flaw lies at the core of the CPRS design since the Green Paper.

Figure 2 shows that under the White Paper 2.5% effect on revenue[2] has approximately an 8+% effect on "after tax cash flow", which is still a fundamentally flawed assessment of the capacity of businesses (such as LNG) to absorb arbitrarily assigned costs.

In the current design of the CPRS under the White Paper the LNG industry may possibly obtain 60% assistance based on historical industry average emissions intensity and subject to formal review. It must be emphasised that there is no certainty that LNG will receive any assistance at all.

[1] 3.75% is premised on 1500 tonnes CO2-e/million revenue and assuming a permit cost of $25.
[2] 2.5% is premised on 1000 tonnes CO2-e/million revenue and assuming a permit cost of $25.

On the current preliminary estimation of LNG activity emissions intensity, and assuming the 60% assistance threshold can be met (which is not a given), approximately 0.3 permits per tonne LNG will be allocated free. The AcilTasman report was premised on an LNG facility with an emissions intensity of 0.71 tonnes CO2e/tonne LNG, so the effective allocation of free permits is ~40%. This means that "60% assistance in the CPRS" actually means "~40% assistance" and 60% of the permits (or approximately 0.4 permits per tonne LNG) will still have to be obtained from the market.

To obtain 0.4 permits per tonne LNG for a 10 MTPA facility used in the AcilTasman report will require 4 million permits per annum, and at $25 per permit will initially cost in the order of $100 million per annum. This cost will rise with time for two reasons, namely (1) the expectation that the cost of a permit will increase with time, possibly in the order of 7.5 -10% per annum, and (2) the decay of assistance referred to in the White Paper as the "carbon productivity contribution".

The AcilTasman report indicated that the effect of "no assistance" would be as shown above. Assuming an effective assistance package of ~40% free permits a first order assessment indicates the effect of the current scheme will be approximately 60% of the effects stated in the Acil Tasman report, or in other words:

- Increased operating costs by approximately 80%;
- Increase in the effective tax rate from 36% to approximately 40%, or in other words a 10% greater tax take by Government; and
- Reducing the NPV of after tax cash flows by up to 17%.

The result of such massive effects (in spite of limited assistance under the White Paper) would be similar to that concluded by AcilTasman, namely: "*In consequence, a carbon charge has the potential to push final investment decision metrics – which are already marginal – into negative territory* "

The potential effects of this are that LNG projects may not occur in Australia. This could make an LNG project in a competitor country go ahead, or perversely make a coal fired facility go ahead, and so the effect will be little or no global environmental benefit and at massive cost to Australia.

The CPRS, and in particular its treatment of trade-exposed industries, will have a substantial negative effect on business confidence in general and in particular the LNG industry, decreasing Australian jobs and increasing Government take, and for little or no positive global environmental effect. This is clearly contrary to the election commitments that Australia's international competitiveness will not be "compromised" nor "disadvantaged" and that a Rudd Government will "*Encourage the development of the gas industry to open up additional supply for export and domestic use*" refer
http://www.alp.org.au/download/now/071122___securing_a_sustainable_energy_supply_for_australias_future_xx.pdf

2.2 SAVANNAH BURNING

The White Paper puts off discussion about savannah burning, but ConocoPhillips and the Northern Territory Government already have one such scheme operating efficiently and effectively for several years. The CPRS must recognise and allow WAFMA as an official offset from scheme commencement, and not delay it by at least 5 years as is the current plan.

2.3 JPDA/SUNRISE

The Commentary Paper on the main Bill Page 80 Section 1.282 states:

> "*The Government is considering whether the Scheme should include specific provisions relating to activities in the Joint Petroleum Development Area and the Greater Sunrise Oil and Gas Field (and pipelines associated with them) in the light of Australia's international obligations. The final decision on this issue will be included in the final bill prepared for introduction."*

ConocoPhillips (and its Co-venturers) has a significant interest in the Joint Petroleum Development Area (JPDA) with its Bayu-Undan operations. ConocoPhillips also currently employs many East Timorese people such as on the Bayu-Undan facilities and in Dili at the heliport. ConocoPhillips also sponsors many other initiatives to support the East-Timorese people.

ConocoPhillips is a Co-venturer with Shell and Woodside in the Greater Sunrise Fields, and so ConocoPhillips has a strong interest in any discussions regarding the Greater Sunrise area.

The ramifications of including the JPDA and Sunrise Project must be more closely considered including the potential cost implications for the Timor-Leste people.

ConocoPhillips encourages the Government to consult widely on any such intentions so that all parties can fully understand any and all ramifications. ConocoPhillips suggests that a comprehensive stakeholder engagement plan and timeline must be developed as this affects many, including ConocoPhillips.

2.4 TIMELINE

As mentioned above ConocoPhillips has included many greenhouse gas emission reduction aspects in its activities without legislation, and supports global action to reduce greenhouse gas emissions. However, unilateral action by Australia in all likelihood won't have a significant impact on global emissions. It is important for Australia to show leadership, commitment and the courage to take the lead, but if the fundamental design of any such scheme is not absolutely correct, the potential to negatively impact jobs, growth, investment and our competitiveness could be significant.

Therefore, it is imperative to get any local scheme right. The time required to consider the ramifications, to deal with them and implement the inherently noble intent of the Scheme should be provided for and not be a victim of a schedule which is too short. The timelines with which the CPRS, including the Draft Legislation to effect it, are being progressed do not allow the ramifications to be properly considered, discussed and effectively dealt with.

A rushed review may result in unforeseen aspects slipping through with dire consequences. It is noted that a major review is planned for 5 years after scheme commencement but ConocoPhillips suggests that (in any scheme) it should be legislated that a significant review must be scheduled one year after the start of any scheme and again after another year to pickup any unwanted/unexpected consequences as 5 years is potentially far too long if such circumstances arise.

2.5 REGULATIONS

The Draft Legislation puts off many key aspects to Regulations, but it appears as if the plan is to release these Regulations after the key legislation goes to Parliament. This makes it very difficult to see the whole package, to consider the Scheme in its entirety and therefore appreciate and understand its ramifications.

The Australian LNG industry currently intends to expand to meet world energy demands - for example ConocoPhillips is a 50/50 Co-venturer with Origin in coal seam gas opportunities in Queensland with potentially 4 LNG trains of comparable size to Darwin LNG with billions of dollars of investment and thousands of jobs. In addition, Chevron and its Co-venturers have Gorgon and Wheatstone, while various other companies are looking at LNG developments in the Gladstone region in Queensland and off the Kimberley Coast of Western Australia. All care should be taken to ensure that such proposals are not negatively impacted by a Scheme that has been rushed and has not been fully designed, with potential loss of jobs and adverse impact on investment with little or no positive global environmental effect.

2.6 CLIMATE CHANGE ACTION FUND

The White Paper refers to the Climate Change Action Fund (CCAF) in the context of providing funding to assist companies to implement greenhouse gas reduction initiatives. There is currently little information available to describe how the CCAF will work. It is imperative that any such scheme provides assistance on the basis of cost effectiveness (e.g. $ per tonne CO2-e) of the proposed mitigations as this will provide the most emissions reduction for any given scheme cost. ConocoPhillips encourages all concerned to make this guidance available soonest so we can see the whole picture of the proposed CPRS and understand how the CCAF fits into the big picture of the scheme.

2.7 CONCLUSION

ConocoPhillips has made its position clear with respect to greenhouse gas emissions and has implemented many innovative ways to reduce/offset emissions without legislation.

ConocoPhillips supports the intention of the CPRS. However, as a minimum, the CPRS should consider and take account of, the following USCAP principles and recommendations, namely to:

- Account for the global dimensions of climate change;
- Create incentives for technology innovation;
- Be environmentally effective;
- Create economic opportunity and advantage;
- Be fair to sectors disproportionately impacted; and
- Reward early action.

The CPRS should also take into account the ALP's election commitments to:

- *Ensure that Australia's international competitiveness is not compromised by the introduction of emissions trading.*
- *Consult with industry about the potential impact of emissions trading on their operations to ensure they are not disadvantaged.*
- *Establish specific mechanisms to ensure that Australian operations of emissions intensive trade exposed firms are not disadvantaged by emissions trading."*

The negative impact on the international competiveness of trade exposed Australian industry, such as the LNG industry, in an international market has the potential to cost Australian jobs and tax revenues, not have the intended effect on reducing global emissions and in fact potentially (and perversely) increase global GHG emissions.

ConocoPhillips strongly urges the Australian Government to reassess its assistance to trade exposed industries, especially the LNG export industry as LNG is an intermediate fuel to assist the planet on its quest to a carbon-less economy.

ConocoPhillips has demonstrated its commitment to reducing/offsetting GHG emissions and is committed to working with the Government to achieve an outcome that is satisfactory to, and workable for, the whole of Australia and the globe.