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## QUARTERLY ACTIVITIES REPORT QUARTER ENDED 30 SEPTEMBER 2013

Following the difficult decision in March to suspend field activities, which was in response to a NSW Government announcement which severely damaged investor confidence in the CSG industry, Metgasco proceeded with its program:

- 1) To decommission unwanted water ponds and wells that were no longer necessary, and to rehabilitate the respective land;
- 2) Maintain community and government contact to highlight the importance of gas to the NSW community and that the CSG industry is a safe and environmentally attractive industry; and
- 3) evaluate the complementary benefits of new business activities outside the Clarence Moreton Basin.

Metgasco's Board has no doubt that its decision to suspend field activity and control costs was necessary and justified:

- it took the NSW Government until October to provide more definition of exclusion zones and their application, and even now there is doubt about the zones and the final implementation is some way off;
- approval of the Petroleum Onshore Amendment bill has been delayed;
- recent amendments to the SEPP merit appeals processes disadvantage CSG; and
- NSW Government agencies are still implementing their new roles and procedures.

All other CSG companies in NSW chose to take similar actions to Metgasco.

The regulatory and political environment improved to some extent during the last quarter, with:

- an increasing awareness of the almost inevitable higher gas prices NSW faces over the next few years and potential shortages, highlighted in particular at the September NSW Gas Summit; and
- the leadership shown from the new Federal Industry Minister, the Hon Ian Macfarlane MP, to resolve the NSW gas crisis.

In response to this improving NSW and federal political climate and the resulting momentum in terms of market support, Metgasco announced that it would drill Rosella E01 well next year. Metgasco, however, retains its suspension of CSG activities until the investment climate, which in turn is influenced by the NSW regulatory environment and political support, becomes acceptable.

Metgasco hopes that the opposition to the industry has bottomed out and that it will see steady improvement in community and NSW Government support, sufficient for it to restart CSG activities as well.

With the largest uncontracted CSG reserves on the eastern coast of Australia, exciting conventional / tight gas potential and a market that is in desperate need of gas, Metgasco believes that it has the opportunity to add considerable value to NSW and, in doing so, increase the value of Metgasco.

In recent months Metgasco has evaluated a number of new business opportunities outside of the Clarence Moreton Basin on the basis that they have merit in their own right and complement the ability to realise value from the Clarence Moreton Basin assets. Most have been found to be unsuitable and those which might

have some potential in the future will need to be brought to shareholders for approval, should the Board identify them as being attractive.

## Review of exploration activities

Metgasco announced plans to drill the Rosella E01 exploration well on the Greater Mackellar structure. It is proposed to drill the well to a total depth of 2,100m on a site 12 km to the northeast of Casino. The well is considered to be a commercially high risk test of the non-CSG, conventional gas potential of the structure. The prospect is interpreted to cover an area of 260 km<sup>2</sup> and hold a potential mean volume of 1,304 BCF of gas in place, comprising an estimated 456 BCF in the Ripley Road sandstone and 848 BCF in the Gatton sandstone.

The primary objective is the Ripley Road sandstone which was tested in Kingfisher-1, south of Casino, at an initial rate of 3MMcf/d. The well will also test the thick sequence of gas bearing strata in the Gatton sandstone which had low permeability in Kingfisher-1, together with the deeper Basal Bundamba Sandstone (a lateral equivalent to the Laytons Range Conglomerate), Ipswich and Nymboida Coal Measures which were below the total depth reached in Kingfisher-1.

If successful, the well will be tested to determine if an economic gas rate can be established from zones of interest and then, subject to results, suspended for further testing and evaluation. It will not be fraced in the initial drilling program. In the event that the well fails to find suitable reservoir zones, it will be plugged and abandoned and the site rehabilitated and restored to pre-drill condition.

The Company will commence preparatory work over the coming months. A final commitment to drill the well is to be made when a suitable drilling rig has been identified, regulatory permits are in hand, and consultation with the general community and key stakeholders has taken place. An agreement with the proposed landholder is close to completion.

Metgasco has identified a relatively low cost means to re-process aero-magnetic data to provide more confidence over the structure of the Greater Mackellar field. This will be completed and analysed before year-end.

Metgasco's decision to proceed with the conventional well while keeping its CSG activities suspended has been influenced by a number of factors, which include:

- 1) the political momentum created following the NSW Gas Summit and the initiative of the new Federal Industry Minister, Ian Macfarlane;
- 2) the fact that a single conventional well can demonstrate value more easily and quickly than a CSG well;
- 3) a conventional production test can be carried out conclusively within a short period of time (compared to 6 to 12 months for a CSG well); and
- 4) the approval processes for conventional exploration and development should be more straight forward than for a CSG development.

Metgasco is proceeding with the conventional well with the expectation that the regulatory and political environment will continue to improve, providing stability and support. Subject to no deterioration in this respect, the well should be drilled in the first half of 2014, depending on rig availability.

Metgasco is currently reviewing a range of options to test the IJK and other coal seams which lie deeper in the Walloon coal measures and are part of its certified reserves. Only the Richmond seam has been tested to date.

## Certified Reserves

The Company recognises the following gas reserves and resources in its tenement areas.

<b>Independently certified gas reserves – Petajoules (PJ)</b>			
<b>All reserves are 100% owned by Metgasco</b>			
<b>Reserve Category</b>	<b>PEL 13</b>	<b>PEL 16</b>	<b>Total</b>
1P (Proven)		2.7	2.7
2P (Proven + Probable)	31	307	338

3P (Proven + Probable + Possible)	437	1,618	2,055
2C Contingent Resource	1,199	1,174	2,373

The estimates of gas reserves have been prepared by Mr Tim Hower, and staff under his supervision, of MHA Petroleum Consultants (Denver). Mr Hower is chairman of MHA and has over 25 years of petroleum engineering experience and is a qualified person as defined under the ASX listing rule 5.11. Reserves have been developed within the guidelines of the SPE. MHA has consented to the use of this information.

The reserve figures above represent a downward revision of 21% for 2P reserves and 23% for 3P reserves, largely associated with the Company's assessment of the NSW Government's proposed 2 kilometre CSG drilling exclusion zone, announced in February 2013. Legislation pertaining to this has yet to be enacted and there is still some uncertainty related to the application and extent of the exclusion zones. Should the proposed exclusion zone not be adopted or local councils be given the right to opt out of the exclusion zone and choose to take this action, the reserve reductions shown below will not be required. The following table reconciles previously stated reserves and the figures above, reflecting the exclusion zone reductions and the increase associated with the Bowerbird E04 well.

### Reconciliation of Reserve Movements

Reserve Category – Petajoules (PJ)				
	1P (Proven)	2P (Proven + Probable)	3P (Proven + Probable + Possible)	2C Contingent Resource
Reserves & resources 1 July 2012	2.7	428	2,542	2,512
Additions from drilling Bowerbird E04	-	-	135	(139)
Estimated reductions from proposed 2 kilometre CSG drilling exclusion zone	-	(90)	(622)	-
Reserves & resources 30 June 2013	2.7	338	2,055	2,373

### Suspension of field operations, corresponding cost reductions and commencement of a decommissioning program

In March this year, Metgasco announced that it would suspend its Clarence Moreton Basin field activities. The decision to suspend activities was in recognition of the damage being done to the CSG industry by statements and decisions made in the lead up to the imminent federal election and the instability created by the NSW Government's announcement of further regulatory changes. In this environment of uncertainty and further costly delays to our field work, future fund raising and the attraction of quality farm-in partners would be difficult if not impossible. The company's decision to suspend was followed by other energy companies suspending or modifying their CSG operations in NSW. The industry faces a business environment characterised by delays in approvals, uncertainties over policies and the imposition of new regulations at a federal level which do no more than duplicate existing state regulation and review processes.

As part of its suspension decision, Metgasco sought and was successful in gaining approval for reduced work programs in its three exploration licences in order to secure the value of the CSG and conventional gas potential it has established to date. Metgasco then implemented cost reduction steps consistent with the smaller work programs. Unfortunately this required the release of 21 of our 27 staff. The loss of the skills and experience developed by these people was most unfortunate, but not avoidable in the circumstances. It will be possible to regrow the organisation when the time is right.

The planned cost reductions have been realised and the well and pond decommissioning program close to being completed. All wells have been plugged and abandoned or suspended. All that remains is final site rehabilitation and recovery of bonds from government. The safety record during the decommissioning program was excellent, apart from a near-miss incident that occurred during the decommissioning of the

Kingfisher well. A full investigation report was completed, with government involvement, and safety alerts issued to industry. A further investigation is being conducted by the government's Safety Investigation Unit.

Two of the five ponds have been decommissioned and the sites rehabilitated. In addition, following detailed technical submissions, approval from government agencies has been received to permit the disposal of produced CSG water.

Work has progressed on aquifer modelling in the Clarence Moreton Basin using Parsons Brinkerhoff in preparation for the time when we restart CSG operations and to provide a sound basis for water monitoring activities. This work should be complete before year end.

## Review of commercial developments

### Gas commercialisation strategy

Little effort was focussed on commercialisation activities in the Clarence Moreton Basin given the suspension of field activities.

Metgasco retains its development approval for the Casino Gas Project / Richmond Valley Power Station. The project is currently on hold. Apart from the NSW CSG regulatory environment, changes in the eastern coast electricity market have questioned the timing for new base load power stations. Metgasco will continue to review options, which include the building of a peak load power station rather than a base load power station.

### East coast gas market opportunities

There is an increasing awareness of the need for additional gas supplies on the eastern coast of Australia. A NSW Gas Summit, initiated by the NSW Government in September, highlighted the importance of gas. There was a general consensus that the best way to lower gas prices was to increase supply, which means drilling more wells and, to do so, stimulating the industry with the application of sensible regulations.

If east coast gas demand is to be satisfied, near and long term gas supplies will need to be secured from new conventional exploration discoveries, development of CSG reserves, and exploration for and development of shale and tight gas potential. This creates an excellent opportunity for Metgasco's CSG reserves and conventional/tight gas potential.

## Review of corporate developments

### Community and Government engagement

Metgasco has maintained its active engagement program with the local community and the NSW Government. This included Community Consultation Group meetings held in Casino, an update of its website, regular advertising in local Casino newspapers and making copies of Fracknation and Switch available to the community.

Metgasco has welcomed the leadership being provided by the new federal Minister for Industry, the Hon Ian Macfarlane MP, to resolve the NSW gas crisis. Minister Macfarlane is highlighting the benefits which CSG is bringing his Queensland electorate in terms of employment, farmer security, increased farm productivity and higher land prices. He is placing a firm emphasis on science based regulatory decisions.

During the period Metgasco continued its efforts to influence the NSW Government to introduce regulations that were "smart" rather than those that penalise the industry for little gain. Regrettably, moves to place a 2 km exclusion zone around towns continue. The NSW Government's recent announcement of exclusion zones is not yet clear and introduces other features which were not expected and are unattractive to the industry. Metgasco is also disappointed by recently proposed changes to NSW's State Environmental Planning Policy (SEPP). The new SEPP draft seeks to provide more certainty for resource developments in NSW by overcoming deficiencies in the existing merit appeal process. The improvements in the draft cover mining in general but do not include petroleum (eg; CSG). This is not acceptable. The industry needs a sound regulatory system and a level playing field if NSW is going to realise the benefits a gas industry can bring.

In August we appointed a new director, Mr Greg Short, bringing a wealth of geoscience experience to a Board with strong engineering and commercial experience. Mr Short will help us maximise the value of our Clarence Moreton Basin CSG and conventional gas assets, and can also advise on any external exploration opportunities.

## Opportunities outside the Clarence Moreton Basin

A small number of potential opportunities were reviewed during the quarter, but none have been identified as having the potential to bring meaningful value to the Company. These opportunities continue to be assessed on their individual technical and commercial merits and their ability to complement Metgasco's Clarence Moreton Basin assets.

Metgasco is aware that it can take considerable time to identify suitable projects and to negotiate acceptable entry terms. While we are keen to broaden our interests beyond the Clarence Moreton Basin, we are also aware of the need to be thorough in our assessments, to ensure that risks as well as potential benefits are understood fully and that participation terms are acceptable. As a consequence, it could take time before new opportunities are presented to shareholders.

## Cash position

The Company ended the quarter with a cash balance of \$16.5 million and no debt.

## Shareholder base

At 30 June 2013 Metgasco had 445 million shares on issue and 1.6 million options outstanding.

## Outlook – planned forward work program next quarter

Metgasco's focus for the December quarter will be as follows:

- completing its decommissioning activities for wells and water storage ponds;
- implementing a proactive community relations program for the Richmond Valley and Clarence River council areas;
- preparing for the drilling of Rosella E01 to test the Greater Mackellar structure; and
- evaluating exploration and development opportunities outside the Clarence Moreton Basin.

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### Background on Metgasco

[www.metgasco.com.au](http://www.metgasco.com.au)

Metgasco has a 100% interest in PEL 16, 13 and 426 in the Clarence Moreton Basin in NSW where it operates the largest acreage position in the basin. Metgasco currently has 2P gas reserves of 338 Petajoules and 3P gas reserves of 2,055 Petajoules (based on Metgasco's current understanding of the impact of the NSW Government's proposed exclusion zones). The Company is exploring for conventional and unconventional gas. Metgasco's has identified natural gas commercialisation opportunities that include local sales in the Northern Rivers Region, domestic sales to eastern coast domestic markets and LNG exports.

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# Appendix 5B

## Mining exploration entity quarterly report

Introduced 1/7/96. Origin: Appendix 8. Amended 1/7/97, 1/7/98, 30/9/2001, 01/6/10.

Name of entity

**METGASCO LIMITED**

ABN

24 088 196 383

Quarter ended ("current quarter")

30 September 2013

### Consolidated statement of cash flows

<b>Cash flows related to operating activities</b>	Curent quarter \$A'000	Year to date (3 months) \$A'000
1.1 Receipts from product sales and related debtors	-	-
1.2 Payments for:		
(a) exploration and evaluation	(4,031)	(4,031)
(b) development	-	-
(c) production	-	-
(d) administration	(546)	(546)
1.3 Dividends received		
1.4 Interest and other items of a similar nature received	199	199
1.5 Interest and other costs of finance paid	(7)	(7)
1.6 Income taxes paid	-	-
1.7 Other	28	28
<b>Net Operating Cash Flows</b>	<b>(4,357)</b>	<b>(4,357)</b>
<b>Cash flows related to investing activities</b>		
1.8 Payment for purchases of:		
(a) prospects	-	-
(b) equity investments	-	-
(c) other fixed assets	(1)	(1)
1.9 Proceeds from sale of:		
(a) prospects	-	-
(b) equity investments	-	-
(c) other fixed assets	22	22
1.10 Loans to other entities	-	-
1.11 Security deposits (paid)/returned	13	13
1.12 Other (provide details if material)	-	-
<b>Net investing cash flows</b>	<b>34</b>	<b>34</b>
1.13 Total operating and investing cash flows (carried forward)	<b>(4,323)</b>	<b>(4,323)</b>

+ See chapter 19 for defined terms.

**Appendix 5B**  
**Mining exploration entity quarterly report**

1.13	Total operating and investing cash flows (brought forward)	(4,323)	(4,323)
	<b>Cash flows related to financing activities</b>		
1.14	Proceeds from issues of shares, options, etc.	-	-
1.15	Proceeds from sale of forfeited shares	-	-
1.16	Proceeds from borrowings	-	-
1.17	Repayment of borrowings	(39)	(39)
1.18	Dividends paid	-	-
1.19	Other (cost of share placement)	-	-
	<b>Net financing cash flows</b>	(39)	(39)
	<b>Net increase (decrease) in cash held</b>	(4,362)	(4,362)
1.20	Cash at beginning of quarter/year to date	20,856	20,856
1.21	Exchange rate adjustments to item 1.20	-	-
1.22	<b>Cash at end of quarter</b>	16,494	16,494

**Payments to Directors of the entity & associates of the Directors.**  
**Payments to related entities of the entity & associates of the related entities**

		Current quarter \$A'000
1.23	Aggregate amount of payments to the parties included in item 1.2	177
1.24	Aggregate amount of loans to the parties included in item 1.10	-
1.25	Explanation necessary for an understanding of the transactions	
N/A		

**Non-cash financing and investing activities**

2.1 Details of financing and investing transactions which have had a material effect on consolidated assets and liabilities but did not involve cash flows

N/A
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+ See chapter 19 for defined terms.

- 2.2 Details of outlays made by other entities to establish or increase their share in projects in which the reporting entity has an interest

N/A
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### Financing facilities available

*Add notes as necessary for an understanding of the position.*

		Amount available \$A'000	Amount used \$A'000
3.1	Loan facilities	-	-
3.2	Credit standby arrangements	-	-

### Estimated cash outflows for next quarter

		\$A'000
4.1	Exploration and evaluation (Note A)	2,103
4.2	Development	
4.3	Production	
4.4	Administration	729
<b>Total</b>		<b>2,832</b>

#### Note A

This expenditure includes the company's well decommissioning program.

### Reconciliation of cash

Reconciliation of cash at the end of the quarter (as shown in the consolidated statement of cash flows) to the related items in the accounts is as follows.	Curent quarter \$A'000	Previous quarter \$A'000
5.1 Cash on hand and at bank	570	1,100
5.2 Term deposits	15,924	19,756
5.3 Bank overdraft	-	-
5.4 Other (provide details)	-	-
<b>Total: cash at end of quarter</b> (item 1.22)	<b>16,494</b>	<b>20,856</b>

+ See chapter 19 for defined terms.

### Changes in interests in mining tenements

	Tenement reference	Nature of interest (note (2))	Interest at beginning of quarter	Interest at end of quarter
6.1	Interests in mining tenements relinquished, reduced or lapsed			
6.2	Interests in mining tenements acquired or increased			

### Issued and quoted securities at end of current quarter

*Description includes rate of interest & any redemption or conversion rights together with prices and dates.*

	Total number	Number quoted	Issue price per security (see note 3) (cents)	Amount paid up per security (see note 3) (cents)
7.1	NIL			
7.2	NIL			
7.3	451,348,141	451,348,141		
7.4	6,189,339	6,189,339		
7.5	NIL			
7.6	NIL			
	NIL			

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+ See chapter 19 for defined terms.



**Appendix 5B**  
**Mining exploration entity quarterly report**

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- 3      **Issued and quoted securities** The issue price and amount paid up is not required in items 7.1 and 7.3 for fully paid securities.
- 4      The definitions in, and provisions of, *AASB 1022: Accounting for Extractive Industries* and *AASB 1026: Statement of Cash Flows* apply to this report.
- 5      **Accounting Standards** ASX will accept, for example, the use of International Accounting Standards for foreign entities. If the standards used do not address a topic, the Australian standard on that topic (if any) must be complied with.

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