Gas landmark

Indonesia's first project under the new oil and gas regime

The Tangguh liquid natural gas (LNG) project in Indonesia has signed and closed long-term financings for $2.6 billion. The greenfield project demonstrates the interest and growing confidence the international financing community has in both Indonesia and the oil and gas sector under the new oil and gas upstream implementation agency, Badan Pelaksana Kegiatan Usaha Hulu Minyak Dan Gas Bumi (BPMIGAS).

The Tangguh project has a lifespan of more than 30 years, to produce LNG in the remote Bintuni Bay area in Indonesia's eastern-most province of Irian Jaya Barat (Papua). The project is being led by energy company BP, with partners including China National Offshore Oil Company (CNOOC), Mitsubishi, INPEX, Kanematsu, LNG Japan and Nippon Oil. The overall project is expected to cost approximately $5.2 billion. This includes associated upstream development, marine infrastructure to transport gas from offshore gas fields, and construction of a processing plant. The gas reserves in the area were discovered in the mid-1990s and the project has proven reserves of 14.4 trillion cubic feet.

The financing includes loans from the Japan Bank for International Cooperation (JBIC), the Asian Development Bank and a group of international commercial banks including The Bank of Tokyo Mitsubishi UFJ, BNP Paribas, Fortis Bank, ING Bank, Mizuho Corporate Bank, Sumitomo Mitsui Banking Corporation and Standard Chartered Bank. An additional tranche provided by Chinese banks is expected to be signed in the near future.

The $350 million ADB tranche is ADB's first private sector project in Indonesia's oil and gas sector. JBIC is providing $1.2 billion and the international commercial bank tranche is approximately $1.07 billion.

When the Tangguh project begins production in 2008, it will become the third major LNG facility in Indonesia (after Arun in North Sumatra and Bontang in East Kalimantan). The plant will initially consist of two trains, producing 7.6 million metric tons of LNG a year. Over time, plant capacity may be expanded to support new sales. The Tangguh site is capable of supporting up to eight LNG trains without additional land.

The loan financing involves a complex multi-tranche Indonesian trustee borrowing structure. Repayment of the loans is supported by revenues from long-term LNG sale and purchase agreements with K-Power in South Korea, POSCO in South Korea and Sempra Energy via a receiving terminal in Mexico. The tranche from the Chinese banks will be supported by an agreement for 2.6 million tons a year with the Fujian LNG-receiving terminal project in China.

The project's strong economics and cashflows contributed to the lenders' positive perception of the financing. The improving political and economic environment in Indonesia provided an excellent backdrop. The lenders also drew comfort from the offshore borrower structure.

The Tangguh project is the first LNG project to be developed and financed in Indonesia since the regulatory changes brought on by the new oil and gas law in 2001. While the loan structuring paralleled previous trustee financings, the project's scope, location and timing required new forms of legal and commercial due diligence, new structural approaches and innovative solutions for a diverse group of lender and sponsors.

The decentralization process between Jakarta and the central governmental authorities and local governments required modifications to the revenue-sharing arrangements, and there were political and geographical issues around the location of the project in Irian Jaya Barat (Papua). Also, offtaker risks arose from the gas sales to certain frontier-market offtakers such as China and Mexico.

The project's legal structure will serve as a precedent for future national LNG projects in Indonesia. Among other firsts, the deal is the largest private sector project in Indonesia since the Asian financial crisis, the first greenfield LNG plant financing in Indonesia in nearly 30 years, the first financing completed under the new oil and gas upstream implementation regime with BPMIGAS and the first LNG financing successfully completed with ADB, JBIC and a syndicate of banks simultaneously.

Under the trustee borrowing structure (see diagram), loans are repaid from an agreed portion of gross proceeds under identified offtake contracts. The buyers make payments directly to the trustee and paying agent. The trustee is also the borrower under the loan agreement with the lenders, and the debt service payments are made from the trustee accounts. Except as otherwise provided, the lenders look to this source of debt service for all loans, with no recourse to the project and no security interest in the project assets or contracts.

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Extract of trustee borrowing structure: contractual overview