BARNZ

VOICE OF THE AIRLINE INDUSTRY

SUBMISSION

Mobil acquisition application – WAP / JUHI assets - [redacted version]

Commerce Commission

8 June 2022

BARNZ is the respected and trusted voice of the airline industry in New Zealand

We work closely with the Government, regulators, airports and local communities to create an environment that fosters continued, sustainable growth for the airline industry in New Zealand. We do this through advocating for service quality and fair prices, which help our airlines grow their international and domestic services.

The 30 BARNZ members keep New Zealand connected to the world, directly enabling our tourism industry and delivering $8 billion of exports. They bring together families, friends and businesses, as well as the free flow of ideas, information and innovation that only happen when people come together face-to-face.

We champion the airline industry and its contribution to travel, trade and tourism in New Zealand.

We strive for fair-priced, customer-focussed airport, border agency services and infrastructure for our members and their passengers.

We help to win the airline industry's ability to grow and operate in New Zealand through consultation and engagement with the wider community.

EXECUTIVE SUMMARY

1. The Wiri to Auckland Pipeline (WAP) and the Joint User Hydrant Installation (JUHI) make up a critical part of the infrastructure delivering 100% of jet fuel to Auckland Airport today. Therefore how they are owned and made available for the sale of jet fuel are of critical importance to airlines and the running of Auckland Airport. Getting jet fuel to Auckland Airport by other means such as trucking is expensive, less reliable and could only meet a small amount of total daily demand.
2. The airport is the principal gateway to New Zealand, serving over 70% of our air routes keeping us connected to the world. As we have learned through the Covid-19 pandemic, these airlinks are a strategic enabler for our economy and wider societal wellbeing. It is on this basis the application by Mobil to acquire the Z Energy share of these assets deserves the utmost scrutiny.
3. The public version of the application to acquire the Z Energy share of the WAP and JUHI provided by Mobil is heavily redacted on the grounds of commercial sensitivity. This lack of transparency, especially on how the ownership split will sit between Mobil and BP, make it difficult for BARNZ to support without fuller information.
4. In particular, significant detail about the open access model, and the proposed access fee is missing. This information is material, because it determines how effective (or not) the proposed ownership structure could be at driving competition between jet fuel providers. Without this critical information, BARNZ is unable to give a full response as to the likelihood of reduced competition should the acquisition be approved by the Commerce Commission.

BARNZ SUBMISSION

Introduction

5. BARNZ makes this submission in response to the Commerce Commission Statement of Preliminary Issues – Mobil / WAP and JUHI Jet Fuel Assets. This submission is made on behalf of our 26 member airlines, and our non-airline members which are listed in the Appendix. Some members may also make their own submissions on the Bill.
6. This submission is set out based on the key issues of consideration identified by the Commerce Commission.
7. This version of the document has commercially sensitive information redacted, identified as [redacted] in the relevant portions. A confidential, unredacted version of this document has also been provided to the Commerce Commission.
8. BARNZ's contact person for this submission is:

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Why WAP and JUHI access are essential for driving jet fuel competition at Auckland Airport

9. The WAP and JUHI deliver 100% of jet fuel to Auckland Airport. Combined with the RAP and Wiri tank farm, they make up the most cost-effective means of getting jet fuel at the scale and efficiency required into Auckland Airport.
10. As they make up key components of the fuel pipeline linear network from Marsden point to the airport (effectively the last 7 km of a 170km network), it is artificial to consider them in isolation. The 2017 jet fuel pipeline outage showed how reliant Auckland Airport is on this fuel infrastructure. An alternative trucking solution to Auckland Airport was attempted to be stood up while the RAP pipeline was inoperable, but it was unable to deliver more than a very small proportion of the daily fuel usage required by airlines.
11. Since 2017 rather than improving, this reliance on the pipeline has grown even greater. The Wynyard Wharf fuel wharf has been decommissioned and removed, meaning Auckland no longer has any port facility for the delivery of fuel.
12. The WAP and JUHI are essential for currently providing the only viable means for delivering fuel in the volumes and at the cost needed by airline customers at Auckland Airport.

Mobil's Proposed Open Access Model

13. BARNZ supports open access to jet fuel pipeline infrastructure as a way to increase supply competition.
14. However, the open access model proposed by Mobil is lacking in important detail, without which BARNZ cannot offer a view of support. In particular, the following information is critical for determining whether the open-access model will positively effect competition:
    a. Infrastructure scope – appears to be limited to the WAP and JUHI. If this is the case, this limits the supply model for non-equity suppliers to trucking only, which has significant practical limitations. An effective open access model would need to apply to the entire jet fuel network, from Marsden Point through to Auckland Airport.
    b. Non-discrimination access fee – little detail is provided as to how this would work. An open book model would be required to ensure that the equity partners are not over-recovering the cost to maintain and operate the infrastructure from non-equity suppliers. BARNZ considers information disclosure to the Commerce Commission would be required to provide adequate transparency.
    c. Technical criteria in the User Access Services Agreement – such as testing laboratory access, operating procedures and standards, quality control procedures and ability to provide continuous supply all need to be consistent with global standards and practical, to ensure they do not become proxy barriers to entry for new entrant suppliers.
    d. Section 5.9 under "The proposed new operating model" is redacted and therefore impossible to tell if it is material to a well-functioning open access model.
15. Mobil asserts that a new operating model will "incentivise and expedite future investments in the WAP and JUHI..." by providing a reasonable rate of return on capital investment".
16. No evidence is presented that the current WAP and JUHI owners are failing to make a reasonable rate of return. We note that the three current owners of the WAP and JUHI all sell jet fuel at Auckland Airport, and can recover their opex and capex costs with margin through the fuel charge they negotiate with airline customers. The Commission is encouraged not to take this inference at face value and ask Mobil to provide evidence of the failure of the current ownership model.
17. A key issue to date has been that for investment in capacity or additional assets requires all three WAP and JUHI equity shareholders agreement. It only requires one party vetoing to halt investment. This will still be the case under an open access model, so it is unclear how the proposed model will "incentivise and expedite future investments".

18. We also understand the RAP and Wiri storage facilities remain [redacted]. Any throughput or storage capacity upgrades still need to be completed in synch throughout the entire pipeline asset. So how changing the ownership structure of only some parts of the network will lead to increased and faster investment in jet fuel infrastructure is not immediately clear.

Likelihood of new jet fuel suppliers at AKL Airport

19. Mobil submits that the new operating model would facilitate even further competition in the Auckland Airport jet fuel market by virtue of removing the requirement that new suppliers need to acquire a share in the WAP and JUHI assets.
20. For jet fuel new entrants to be able to provide effective competition at Auckland Airport, they have to be able to sell at a competitive rate and volume. This means:
    a. Non-discrimination access fee must not disadvantage non-equity suppliers versus equity suppliers; and
    b. New entrant suppliers must be able to provide the volume of jet fuel that airline customers demand
21. **Non-discrimination access fee** as previously stated must not allow the equity-holding suppliers to push the cost to operate and maintain the WAP and JUHI onto non-equity suppliers. Mobil has said equity-holding suppliers would be required to pay the non-discrimination access fee along with new entrants. [redacted].
22. The only way to adequately address this risk is to have an open book information disclosure regime, ideally to the Commerce Commission. This would ensure that opex and capex spent on the pipeline is not over-recovered from customers. However, as it is not within the powers of the Commerce Commission to grant conditional approval to merger and acquisition applications, BARNZ would be concerned about this risk of potential anti-competitive behaviour should the Commission approve the acquisition.
23. **The ability of new entrants to supply jet fuel at significant volume would remain constrained** if open access only applied to the WAP and JUHI, and not the RAP and Wiri tank facilities. Such restriction would mean that new entrant suppliers can only provide jet fuel to Auckland Airport by first trucking it to the WAP or JUHI.
24. If the open access model does not apply to the wider jet fuel infrastructure, jet fuel importers would be forced to drive the 170km from Marsden Wharf, or even further from Mount Maunganui. There is no ability to land jet fuel closer to Auckland since the recent closure of the Wynyard Wharf terminal.

25. Therefore significant cost barriers to entry would remain for new entrants: investment in tank storage facility for jet fuel at either Marsden Point or Mt Maunganui, along with a substantial truck fleet that can provide the daily volume needed to adequately compete with jet fuel delivered by the pipeline. All of this upfront investment and additional cost to operate would likely make it difficult for new entrants to be able to offer competitive fuel bids.

26. On this basis, BARNZ submits that a functioning upstream market allowing access to the RAP and Wiri storage facilities is also necessary to drive competition. Allowing new entrants access to the full jet fuel pipeline for a non-discriminatory access fee that is monitored under an information disclosure regime would overcome this issue and provide a level playing field for competition.

27. Vertical effects – the Commerce Commission asks whether the ownership arrangements applied for would increase the merged entity's ability to foreclose rivals. The ability to foreclose new entrants already exists today, with the current requirement that any fuel company wishing to use the jet fuel infrastructure must be an equity owner (currently the only feasible way to sell jet fuel to Auckland Airport). No additional equity owners have been approved, so competition has remained limited at the airport to the current three fuel providers.

28. If the open access model remains limited in scope to the WAP / JUHI infrastructure only, then we believe there is increased ability to foreclose. Only two equity shareholders would remain, and it is not immediately clear that Z Energy would continue to sell jet fuel at Auckland. Rational economic behaviour suggests this would depend on the terms offered in the access fee, and whether Z Energy could continue to use the Marsden terminal to maintain current volumes sold.

29. Unilateral effects – could the merger see less competition in jet fuel providers at Auckland Airport? Yes, if new entrants do not enter the market due to barriers to entry already outlined. If Z Energy decided to no longer sell jet fuel as a non-equity supplier, then the number of providers at Auckland Airport would drop from 3 to 2. The challenge for airline customers at airports where there are only 2 providers is when only one provider bids to provide services. In such a scenario there would be no commercial or negotiating leverage for the airline customer – it is then a case of being forced to take the price offered or withdraw flights to that airport.

30. The Commerce Commission asks would the merged entity be able to profitably rise prices by itself? Demand for jet fuel is largely inelastic – airlines have no choice but to purchase fuel from the available providers at a given port. In a scenario where open access fails to deliver increased competition, adding an access fee to use the WAP and JUHI could allow the equity-holders to over-recover cost to maintain and operate. This would increase profitability on jet fuel, and is why it is so important an open access model is subject to information disclosure.

Countervailing powers of airlines and Auckland Airport

31. Mobil submits that even in the event of restricted competition at Auckland Airport, airlines and airports have countervailing powers that will offset this. BARNZ disagrees with a number of these assertions.

32. Shifting fuel volumes - Mobil states that airlines have an ability to respond to attempts to increase jet fuel prices at Auckland Airport by "shifting more significant volumes to competitors at other airports". International airlines, particularly those flying long haul, have no such ability, and would not respond in this way as it is completely impractical. Any such effort ultimately costs more in fuel and emissions.

33. The practice referred to is known as tankering, and is really only viable during jet fuel supply disruptions. As described, it would involve filling up with cheaper fuel at the last port of departure prior to Auckland, and carrying it to Auckland. More fuel means the aircraft is heavier, and has to burn more fuel to carry the extra weight. The extra fuel burned would erode any savings in fuel purchase costs, and also lead to more emissions, something which airlines are working very hard to minimise as part of their sustainability initiatives.

34. This practice is not available for long haul flights, or even many mid-haul flights, as aircraft flying these routes would need fuel-tanks large enough to carry fuel for more than twice the route distance, so they can return to the departure port without refuelling in Auckland. Aircraft flying mid-to-long haul are not equipped to carry fuel loads of this size, even if it were economic.

35. Airline purchasing power - Mobil points to the NERA report which notes that airlines have greater bargaining power through the "prospect of reprisals in other geographic locations", i.e. using the purchasing power of their global networks. This may be partially true of some of the larger international airlines, but Auckland Airport also serves a significant number of much-smaller, Pacific-based airlines who do not have such power.

36. The opposite dynamic that NERA highlights also applies. International airlines are unlikely to walk away from a favourable international contract with an oil company on the basis of a very small port responsible for less than one percent of their fuel purchases. This would be a case of the tail wagging the dog - airlines are simply far more likely to stop flying there. Furthermore, larger airlines tend to purchase fuel from multiple providers internationally, rather than just one, which waters down the overall purchasing power.

37. Countervailing power of airlines to set up alternate suppliers – Mobil submits that national carriers such as Air NZ have enough countervailing power to develop new jet fuel supplies if competition is not adequate. This could be done through measures such as building a new pipeline, sponsoring a new entrant or arranging for jet fuel to be trucked in.

38. While some of these options may have theoretically possible at the outside margins prior to the pandemic, there is no ability for airlines struggling for survival to contemplate them. With the border closures, IATA estimates airlines have lost over $200b during the Covid-19 pandemic, and many are in record debt and managing cashflow crises. There is no balance sheet ability for airlines to invest in anything other than core business at this time.

APPENDIX – LIST OF BARNZ MEMBERS

Airline Members	
Air Calin	Air Chathams
Air China	Air New Zealand
Air Tahiti Nui	Air Vanuatu
Airwork	American Airlines
Cathay Pacific Airways	China Airlines
China Eastern Airlines	China Southern Airlines
Emirates	Fiji Airways
Jetstar	Korean Air
LATAM Airlines	Malaysia Airlines
Philippine Airlines	Qantas Airways
Qatar Airways	Singapore Airlines
Tasman Cargo Airlines	Thai Airways International
United Airlines	Virgin Australia Airlines

Non-Airline Members	
Menzies Aviation (NZ)	OCS Group NZ
Swissport	