Todd Energy

PROPOSED REVOCATION OF AUTHORISATION OF ARRANGEMENTS TO JOINTLY MARKET AND SELL POHOKURA GAS

SUBMISSIONS IN RESPONSE TO THE COMMERCE COMMISSION DRAFT DETERMINATION (23 FEBRUARY 2005)

A. Executive summary

1. The Commission proposes to revoke the authorisation it granted to the Pohokura Joint Venture (the "Joint Venture") under Decision 505.

2. The grounds for revocation are set out in section 65 of the Commerce Act 1986. There are two limbs to that section:

   2.1 First, the Commission must establish jurisdiction under section 65(1). The Commission asserts jurisdiction under two heads:

      (a) that the authorisation was granted on the basis of information which was false or misleading in a material particular: section 65(1)(a); and / or

      (b) that there has been a material change in circumstances since the authorisation was granted: section 65(1)(b).

   2.2 Secondly, if there is jurisdiction, the Commission is required to exercise a discretionary power in determining whether to (a) revoke the authorisation; (b) amend the authorisation; (c) enter a substituted authorisation; or (d) leave the authorisation intact.

Jurisdiction

3. The Commission does not have jurisdiction under section 65 for the following reasons:

   3.1 No false or misleading statements have been made because:

      (a) The information alleged to be false or misleading (in the case of both the Final Investment Decision and early production) relates to representations made about future events. At the time those statements were made, they were not false or misleading. The Joint Venture intended, and had the means, to jointly market and sell all the gas from the Pohokura field.

      (b) Todd has not said that joint marketing was necessary to achieve early production from the field by the end of June 2006.

      (c) It would be premature for the Commission to reach the conclusions which are forecast in the Draft Determination. The proposed findings of false or misleading statements would be

disproved if, in fact, the proposed separate delivery of gas is not achieved.

(d) The statements made about the likelihood of the Final Investment Decision being reached sooner under joint marketing than under Scenario 1 marketing are not, in the overall scheme of things, material. The Final Investment Decision is but one of a number of decision points leading up to first production. Materiality attaches to the commencement of production and the efficient exploitation of the field. No welfare assessment, as such, attaches to a comparison of the First Investment Decision dates under separate and joint marketing.

3.2 There has been no material change of circumstances because:

(a) The issue is whether there has been a material change in market circumstances since the grant of the authorisation.

(b) There have been no such changes since Decision 505. The only changes are these: (i) more has become known about the Maui reserves, and arrangements have been entered into in relation to those reserves; and (ii) a higher value now attaches to the Pohokura liquids. These are not *material* changes as contemplated under section 65.

(c) The inefficiency and welfare losses associated with separate marketing remains, principally because there is no deep liquid spot gas market. There has been no change in this, the primary cause of welfare losses. We understand the Commission accepts this fact.

(d) Alternatively if, however, the view is taken that changes in the contractual arrangements proposed by the Joint Venture may constitute changes of circumstances (i.e. not all gas may be jointly sold), there is no *material change* of circumstances *for the purposes of section 65*. The impact on the market is the same under the proposed arrangements as it was under Decision 505. In both cases the arrangements relating to the sale of gas result in public benefits which outweigh detriments.

Exercise of the discretion

4. It would be inappropriate for the Commission to exercise its discretionary powers in the manner proposed in the Draft Determination because:

4.1 There may yet be a reversion to joint arrangements in respect of tranche 1 gas.

4.2 In any event, there are likely to be joint arrangements in respect of other, as yet unsold, gas.

4.3 Revocation of the authorisation would create a risk of delay in achieving production from the field, because if the Joint Venture reverts to joint selling for the entire field, it would need to reapply for

authorisation of the very matter approved under Decision 505. That application would be likely to be made some time in 2006.

4.4 The fact that the Commission proposes to revoke existing and continuing rights to jointly market is material to the manner in which the Commission proposes to exercise its discretionary powers. The authorisation is not "dead letter" as the Commission suggests; the so-called "straight conduct test" exception does not apply here.

4.5 It follows that the Commission cannot propose revocation without first undertaking proper analysis of whether an amended or substituted authorisation is appropriate.

4.6 An amended or substituted authorisation is appropriate here because, even if there is separate delivery of gas as proposed, the basic elements of the facts and the reasoning behind Decision 505 remain relevant.

4.7 It follows that a reassessment of the standard authorisation test is required. This requires a comparative assessment of new counterfactual circumstances as follows:

(a) The new factual would include both separate selling (assuming there is delivery of gas under the proposed contracts, which account for about half of the estimated field production), while the balance of the gas may be jointly sold.

(b) The new counterfactual would involve separate selling for the entire field.

4.8 If there is separate delivery of gas, as proposed, there will be a significant reduction of the detriments found in Decision 505.

4.9 If there is separate delivery of gas, as proposed, a reassessment of the public benefits previously raised by the Joint Venture, and accepted by the Commission, will be required. Whereas the benefits of early production were pivotal under the original application, the new counterfactual circumstances require that closer consideration be given to the other accepted benefits (in particular, that relating to optimal pool depletion).

Process issues

5. The Commission has not yet properly followed the procedural steps prescribed under section 65(2). The Commission has failed to properly address a significant relevant consideration, namely whether there ought to be an amended or substituted authorisation on the basis of the standard authorisation test. It follows that there has not yet been a reasonable opportunity to make submissions on that subject.

6. We set out below our reasons for these conclusions.

B. Jurisdiction

7. The Commission asserts that it has two grounds upon which to assume jurisdiction under section 65:

    7.1 first, on the basis that the authorisation was granted on information that was false or misleading in a material particular; and

    7.2 secondly, on the basis that there has been a material change of circumstances since the authorisation was granted.

False or misleading information in a material particular

Legal principles

8 The Commission has on one previous occasion considered the legal framework issues applying to section 65: see *Re a Revocation of Decision 221: New Zealand Kiwifruit Exporters Association/New Zealand Kiwifruit Coolstorers Association*.[1] However, the factual circumstances of that case are different to those of the present case, and the principles enunciated in *Kiwifruit Exporters/Kiwifruit Coolstorers* are only broadly stated. Accordingly, the Commission should take a first principles approach to the matters now before it.

9 As yet, there is no case law on the meaning of the phrase "false or misleading in a material particular" under section 65. However, this phrase appears in other Acts and some guidance can be taken from the interpretation of them. The case law under the Fair Trading Act 1986 and Securities Act 1978 is of most relevance:

    9.1 The term "false" means untrue, erroneous or incorrect. It does not import any element of moral turpitude.[2]

    9.2 A statement is misleading if it leads someone into error or causes someone to err or go astray in action or conduct.[3]

    9.3 It is wrong to assume, just because a representation as to future events turns out to be wrong, that there has been a false or misleading statement. Where the maker of the statement (at the time at which the statement is made) intends to and has the means to act in the manner which is forecast, then such statement will not be false or misleading.[4]

    9.4 A range of considerations should be taken into account in determining whether statements as to future events, which do not eventuate, are false or deceptive. In general such statements will not be false or misleading if:

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1 (1989) 2 NZBLC (Com) 104,513.

2 See e.g. *Given v C V Holland (Holdings) Pty Ltd* (1977) 15 ALR 439, 443; *Commerce Commission v A & W Hamilton Ltd* (1989) 3 TCLR 398, 402.

3 *Weitman v Katies Ltd* (1977) 29 FLR 336, 343.

4 See *Commerce Commission v Chalmers* (1990) 3 TCLR 522, 553-54.

(a) they are based upon sound background knowledge (i.e. they are statements which a reasonable person with the relevant expertise would make);

(b) the maker of the statement intends to make good the forecast; and

(c) they are not made recklessly.

9.5 The inclusion of the reference to both false and misleading information requires a narrowing of the natural meaning attaching to "false" (i.e. that which is merely untrue, erroneous or incorrect). Misleading in this context suggests statements which, though literally true, lead into error.[5]

9.6 There is limited guidance on what constitutes a "material particular". There is commentary, in relation to section 22 of the Fair Trading Act, that: "A 'material particular' of a business activity is any element of the business which is essential or of importance".[6] "Material matters" also need to be disclosed under prospectus rules. In the Securities Act context this requires a consideration of whether the information in question would be likely to influence a reasonable person in making a decision to invest.[7]

9.7 These tests provide varying degrees of assistance, and need to be applied with appropriate flexibility to meet the circumstances of any given case. Further, when considering the application of terms such as "false or misleading in a material particular", it is necessary to return to the ordinary words of the section and apply them to the facts.[8]

Issues raised by the Commission

10. The Commission raises two central concerns relating to the authorisation being granted on the basis of false or misleading information in a material particular. The first relates to the Final Investment Decision and the second to early production.

Final Investment Decision

11. The Commission notes that the Joint Venture said (a) that with joint marketing the earliest Final Investment Decision would be 21 March 2004; and (b) that with Scenario 1 separate selling, the earliest date for the Final Investment Decision would be 24 August 2010.[9] Accordingly, the Commission infers that the Joint Venture's position was that the Final Investment Decision could only be achieved in 2004 if joint marketing was authorised.[10]

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5 See *Gault on Commercial Law* FT13.10(3).
6 *Gault on Commercial Law* FT22.04.
7 See e.g. Securities Commission, *A Report on aspects of the Initial Public Offering of Vertex Group Holdings Ltd in 2002* (14 March 2003) 25.
8 See *Taylor Bros Ltd v Taylor Textile Services Auckland Ltd* [1988] 2 NZLR 1, 39.
9 See e.g. paragraphs 42 and 72 of the Draft Determination.
10 See e.g. page 6 and paragraph 66.

12. We consider that the Commission has overstated the importance of the Final Investment Decision. The Joint Venture's welfare assessment did not flow from any comparison between Final Investment Decision dates under separate and joint marketing. Rather, that welfare assessment flowed from a comparison of (a) dates of first production; and (b) efficient exploitation of the field. While the Final Investment Decision was identified as an important decision point, it did not drive the welfare assessment on the basis of which the authorisation was granted.

13. The Joint Venture provided the Commission with a detailed analysis (in the form of a Gant chart) of the expected steps / actions required to implement each of joint and separate marketing:[11]

    13.1 The steps showed for separate selling led to a Final Investment Decision in August 2010, after a number of precedent actions had been completed, including resolution of any appeals and negotiation of necessary balancing and other arrangements.

    13.2 However, the Joint Venture carefully and responsibly advised the Commission that:

        (a) it will always be possible to debate the time allocated to individual tasks. Those times represent the best estimate of the Joint Venture parties, based on their collective experience of negotiating and contracting complex joint venture and other arrangements;

        (b) the estimates are of course made in the context of the fact that there is no previous New Zealand experience for the Joint Venture parties to draw on, either from themselves or from anyone else. As previously stated in the submission in reply, the extent of the learning curve to be traversed should not be underestimated;

        (c) the estimates are also, of course, made with reference to the resources available to the Joint Venture parties, which will always have limits; and

        (d) in the view of the Pohokura joint venture parties, the time estimates are as equally capable of being too short as they are of being too long.[12]

    13.3 As matters have transpired: (a) the Joint Venture did not reach agreement on appealing the Commission's determination;[13] and (b) despite best endeavours, the Joint Venture was not able to reach a mutually acceptable commercial position for undertaking joint selling (the reasons for this are discussed in more detail below).

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11 By e-mail dated 23 June 2003.

12 Cover note of 23 June 2003. And, as the Joint Venture pointed out, Australian precedents pointed to by other submitters were not comparable precedents in fact.

13 Todd supported appealing.

13.4 Accordingly, given the commercial incentive to develop the field, the only alternative was to proceed on a separate basis, with a view to resolving balancing arrangements at a later date.

Application of legal principles to the Final Investment Decision

14. In the case of the first allegation, that the Joint Venture represented that the Final Investment Decision could only be achieved in 2004 pursuant to joint marketing, this statement was not false or misleading because:

14.1 At the time the statement was made, the Joint Venture intended, and had the means, to pursue joint marketing for the entire field.

14.2 That intention was based upon the industry knowledge of the Joint Venture, having particular regard to the immature state of the New Zealand market.

14.3 That industry assessment was corroborated by an independent expert, Mr Agostini.[14]

14.4 Therefore, it is wrong to conclude that this representation as to future events was false or misleading, simply because a Final Investment Decision in 2004 may have been achieved by means other than joint marketing.

15. Further, the Commission's proposed conclusions are premature. If separate delivery of gas is not in fact achieved, and if the Joint Venture reverts to joint marketing (as discussed below), then the Final Investment Decision cannot properly be characterised as one achieved pursuant to separate marketing.

16. In any event, even if the statement was false or misleading, it was not so in a material particular. The Final Investment Decision is but one of a number of decision points leading up to production. In the context of the proposed separate delivery of gas, the materiality of this decision point must be viewed in light of its relationship to the achievement of first production and the efficient exploitation of the field. Many key decisions have yet to be made before there will be separate delivery. As noted above, the relevant welfare assessments do not flow from any comparison between Final Investment Decision dates under separate and joint marketing.

Early production

17. The Commission secondly alleges (a) that the Joint Venture represented that joint marketing was necessary to achieve early production of the field by the end of June 2006;[15] and (b) that this statement was false or misleading in a material particular because early production is achievable and is in fact happening, pursuant to separate rather than joint marketing.[16]

18. Todd has two responses. First and foremost, Todd considers that the Commission's statement that early production is happening to be fatally flawed. The field has not commenced production. Whether or not it does so

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14 See e.g. Conference Transcript 2 July 2003, pages 274-79.
15 See e.g. paragraph 72.
16 See e.g. paragraphs 48, 60 and 73.

in June 2006 or any other date will not be known until much closer to the time, because of the potential for delays to arise in the interim.[17]

19. The fact that separate delivery has not yet occurred is in fact recognised by the Commission, and the Commission seeks to overcome this problem by stating that: "There is no present evidence that the Pohokura Joint Venture will not meet their production target of 30 June 2006".[18] The basis for this prediction by the Commission is unsupported and entirely speculative.

20. Secondly and in any event, at no time did Todd make the alleged representation, either in the context of written submissions made by the Joint Venture or in the context of statements made by Todd personnel during the conference. Todd has consistently taken the position that Scenario 1 separate selling would be likely to delay development of the Pohokura field, compared with joint marketing, by three to seven years. No statement was made by Todd that joint marketing was necessary to achieve early production by the end of June 2006.[19]

Application of legal principles to early production

21. As just noted, the allegation that the Joint Venture represented that joint marketing was necessary to achieve early production of the field by the end of June 2006 can be easily disposed of, because the statement was not in fact made.

22. Even if the statement had been made, the related allegation, that early production is achievable and is happening pursuant to separate marketing, is also wrong because:

    22.1 Any such conclusion is premature. Separate delivery has not yet been achieved, and the Commission's proposed conclusion may subsequently be proven wrong, should separate delivery not in fact be achieved.

    22.2 The statement would have been a representation as to future events and not false or misleading. At the relevant time the Joint Venture intended, and had the means, to jointly market gas to achieve earlier production of.the field than would be the case under Scenario 1 separate selling.

    22.3 That intention was based upon sound industry knowledge, and was again a view which was shared by the independent expert, Mr Agostini.

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17 As it happens, for technical project reasons the scheduled date for first gas is now 15 September 2006. Accordingly, an extension will be required to the 30 June 2006 target date under the conditions attaching to Decision 505.

18 At paragraph 71.

19 Refer to the following parts of the record: (1) the Joint Venture submission to the Commission, dated 21 March 2003, at page 6; (2) the Joint Venture submission in response to the Draft Determination, dated 9 June 2003, at paragraph 5.3; (3) the following references in the Conference Transcript: 1 July 2003 at pages 23, 33, 46, 100; 2 July 2003 at pages 173-74, 190, 192, 196 and 199; and (4) the Commission's file note of the meeting with Messrs Deppe and Hall on 3 November 2004.

22.4 Therefore, any such representation could not have been false or misleading in the relevant sense merely because early production may be achieved by means other than joint marketing.

Material change of circumstances

Legal principles

25. There is little in the way of legal principles on what constitutes a "material change of circumstances". In the *Kiwifruit Exporters/Kiwifruit Coolstorers* decision, the Commission said that section 65 requires something more than a merely trivial change.[20] In other contexts, such as the power of the courts to review interlocutory orders, the case law reflects that the issue of whether there has been a material change of circumstances is to be determined on a case-by-case basis, primarily having regard to the facts.[21]

26. The reference in section 65(1)(b) to a material change of circumstances is, on proper construction, a reference to changed market circumstances. Section 65(1)(b) is intended to apply to factors which are exogenous of the contractual arrangements which have been authorised. The focal point is upon market developments independent of the arrangements between the parties to the authorisation.

27. Alternatively if, however, the view is taken that certain changes to the contractual arrangements proposed by the Joint Venture may constitute a material change of circumstances (i.e. not all gas may be jointly sold), then all relevant considerations pertaining to those contractual arrangements must be taken into account. If the changed circumstances also involve overall public benefits which outweigh the detriments, as they did in Decision 505, there will be no material change of circumstances.

Issues raised by the Commission

28. The Commission asserts that:

    28.1 joint marketing has not been necessary to achieve the Final Investment Decision in 2004;[22]

    28.2 the path from the Final Investment Decision to first production will be the same under the proposed separate marketing as it would be under the authorised joint marketing;[23] and

    28.3 accordingly, joint marketing has not proved to be necessary to achieve early production of gas.[24]

No material change of circumstances

28. The Commission has suggested that there has been a change of market circumstances since the authorisation was granted. This seems to have arisen from the fact that the Joint Venture has not yet marketed and sold gas

[20] At 104,518.
[21] See *McGechan on Procedure* HR259.04.
[22] See e.g. paragraph 79.
[23] See e.g. paragraph 78.
[24] See e.g. paragraph 79.

jointly. We note, however, that an authorisation is just that and is not a prescriptive requirement to undertake the authorised activity. The fact that there has not yet been joint marketing is not, of itself, a change in market circumstance.

29. The inability to agree joint selling terms to date has occurred for a variety of reasons, to some extent reflecting the disparity of commercial interests within the Joint Venture. For example, the Strawman Contracts concluded towards the middle of 2004 required the parties to underwrite the Maui 367 PJ reserves and at least some of them will do so with Pohokura gas. Each partner undertook to take on Maui reserves risk separately. Each party has different percentages in Maui and different percentages in Pohokura. In order to discharge a separate Maui reserves risk liability a party will need an ability to access and separately market its share of gas reserves.

30. Some partners had access to other gas, whereas others only had access to Pohokura gas. Those partners that only had access to Pohokura gas suddenly had a need to gain separate access to Pohokura reserves. As a result, Shell and OMV announced to the market that they would enter into separate contracts. This meant that Todd had no choice but to do the same.

31. This does not mean, however, that the purpose of the original application – to allow joint marketing to occur – has changed. It has not. The Joint Venture still considers joint marketing to be the best option for:

- commissioning gas, to avoid unnecessary complexities arising from the unpredictable and fluctuating nature of gas supply and the difficulty of getting purchasers to contract for that with a joint seller let alone a separate one;
- peaking gas, to maximise use of the facilities; and
- subsequent tranches, particularly when volumes decline and deliverability becomes less certain.[25]

32. The Joint Venture also considers that it may need to revert to joint marketing:

- if gas balancing arrangements cannot be negotiated or require some form of joint arrangement;
- if separate marketing results in significant unutilised capacity or other inefficiencies (separate marketing requires that separate volumes are notified ahead of time but capacity at the time is by definition determined instantaneously);
- when further investment becomes necessary to recover residual gas.

[25] Ongoing expenditure and investment is necessary to maintain deliverability in all fields (e.g. perforations, work-overs etc.). Without such expenditure, deliverability declines. A party that is not able to sell its share of production will have no incentive to invest to maintain deliverability. When there are more parties selling the same gas production there is a higher risk that at least one party will at some point in time have some difficulty selling all its entitlement. In the absence of detailed gas balancing arrangements (which will include rights to unsold entitlement) unsold entitlements will result in lower production and deferred liquids for all parties. This results in a lower supply to the market and hence welfare losses.

33. Accordingly, absence of ability to jointly market might still cause a delay in commencement of production and/or other welfare losses. It would therefore not be appropriate for the authorisation to be revoked at this point.

34. The only significant change since the authorisation is the 50% plus increase in the liquids price:

- The Pohokura field is a liquids rich field. Maximising early access to liquids is the overriding objective of the Joint Venture. Gas has to be disposed of in order to gain access to the more valuable liquids.

- The Joint Venture's decision to go ahead with the development despite the fact that gas balancing arrangements have not been negotiated and remain a significant risk is an illustration of this.

- The Joint Venture has not changed its view that separate marketing is a significant barrier to the maximisation of gas and liquids volume over the life of the field. This is particularly the case later in field life when the recovery of incremental or bypassed reserves inevitably becomes an issue, especially if gas balancing arrangements, still to be negotiated, result in the parties being able to shift reserves risks and costs at the end of field life to other Joint Venture parties.

35. Finally, there is no material change of circumstances even if the focus is upon changes to the proposed contracting approach. There will be no material change to the competition law assessment of the contracts for the sale of Pohokura gas if not all the gas is jointly marketed. In both the case of Decision 505, and the changed counterfactual circumstances which are now potentially before us, the standard authorisation test will reach the same result. The benefits will outweigh the detriments (as outlined below), and accordingly, there will be no material change in circumstances.

C. Exercise of the discretion

36. Even if there was jurisdiction, it would be inappropriate for the Commission to exercise its discretion under section 65, as proposed in the Draft Determination, because:

36.1 There is, as yet, no separate delivery of gas and it cannot be assumed that there will be. Even if the proposed separate delivery of gas is achieved, joint marketing remains likely.

36.2 Revocation of the authorisation may create a risk of delay.

36.3 The Commission has not taken into account relevant considerations which apply to the proposed exercise of the discretion. In particular, the Commission is in error in asserting that there are no grounds requiring it to consider an amended or substituted authorisation.

No separate marketing; joint marketing remains likely

37. As noted above, the proposed separate delivery of gas is primarily being driven by the incentive to maximise early access to the liquids in the Pohokura field (as well as address the Maui issues discussed in paragraph 29 above). Gas needs to be disposed of in order to gain access to the highly

valuable liquids. Only collective maximisation of gas production maximises liquids. Hence the Joint Venture has the incentive to jointly sell residual volumes to maximise production. Preventing joint selling will mean that the most obvious and efficient way of maximising production and minimising residual unsold production will not be possible. If production is lower, the market supply is lower and market prices will be higher. It is therefore in the interests of consumers that joint marketing (or joint balancing arrangements) to maximise efficiency are allowed.

38. It cannot be assumed that the proposed separate delivery will be achieved. For example, in practice gas balancing or related arrangements are likely to be complex, both in terms of the conclusion and performance of any such arrangements. This is illustrated by reference to the recent experience with separate marketing at Kapuni. In that case a rudimentary gas splitting arrangement has not overcome continuing disputes and litigation. The dysfunctional nature of these separate marketing arrangements has diverted the field owners from maximising the field capacity.

39. Accordingly, in the absence of arrangements necessary to support field development (such as gas balancing arrangements), the prospect remains that the Joint Venture parties may need to revert to joint selling for all or part of the gas presently the subject of the separate contracts.

40. Further, joint marketing remains likely, even if the proposed separate delivery of gas is achieved. For example, there may be joint marketing of the following gas from the field:

    40.1 *Commissioning gas*: Commissioning gas sold to a single buyer allows all production to be sold without prior notice, despite the fact that it is uncertain and a variable volume. The commissioning programme may be highly inefficient or be jeopardised under separate marketing because each seller's multiple buyers will need to guarantee that they can take uncertain, variable volume without notice. Commissioning requires that the capacity of facilities is tested. Very few buyers can take the large and unpredictable volumes associated with commissioning. For three sellers to separately negotiate large, variable, short-notice volume contracts with three or more buyers would be very complex, such that joint marketing will remain the preferred strategy for the sale of commissioning gas.

    40.2 *Unsold gas*: From the public announcements surrounding the proposed separate sales, it is evident that each Joint Venture party has only sold sufficient gas to support the development of the field. Accordingly, there are significant volumes of gas, accounting potentially for around [ ], which may yet be jointly marketed.

    40.3 *Capacity above nameplate*: STOS has confirmed that it is normal for the design limit of the plant capacity to be [ ] above nameplate. The Joint Venture parties have not yet sold any of the capacity above nameplate, which represents about [ ] per annum.

40.4 *Peaking gas*: The demand for peaking gas can result in one seller infringing on the rights of another seller in any given hour. A requirement to ad here to separate hourly entitlements would necessarily mean that joint peaking flexibility would be lost. Separate sales are a barrier to meeting the demand for peaking gas. Joint marketing remains the best option for the sale of such gas.

40.5 *Imbalance gas*: The current proposed Maui open access arrangements require that the three Pohokura sellers, who are joint owners of the Welded Point, be jointly liable for any imbalance and penalties at the Welded Point. If a positive imbalance occurs, Maui will cash out the welded party. This will be a joint sale by the Joint Venture parties to Maui. Alternatively, the parties may want to buy or sell gas to efficiently maintain imbalance within pipeline tolerances. Without the ability to jointly sell or buy this will not be possible. Open access requires that a welded party be able to jointly sell and/or buy gas without restriction.

41. A further driver for joint marketing (e.g. in the case of unsold gas and capacity above nameplate) is that separate marketing will not maximise the volume of the gas produced over the life of the field (as explained elsewhere in this submission). This is particularly the case later in field life when the recovery of incremental or bypassed reserves becomes an issue. Joint contracts linked to the limited volumes of residual gas are likely to become necessary to support investment for extra capacity. Further, smaller uncertain quantities are harder to sell towards the end of a field's life. The pooling of quantities under joint marketing is often necessary to meet minimum quantity demands of purchasers. In short, there are strong efficiency grounds to pursue joint as opposed to separate marketing, and for this reason joint marketing can be anticipated.

Risk of delay

42. The uncertainty which exists relating to the actual achievement of separate delivery points to a further issue of real practical concern. What if the Commission revokes the authorisation, without amendment or substitution?

43. If the proposed separate delivery is not in fact achieved, then there is the strong prospect that the Joint Venture will need to revert to joint selling for the entire field. In those circumstances the Commission would presumably expect the Joint Venture to reapply for the restoration of the revoked rights under Decision 505 to jointly market gas. This very prospect alone reveals that it would be inappropriate for the Commission to exercise its discretionary powers as proposed.

44. Further, if the Joint Venture was required to reapply for authorisation, it is likely that this would not occur until some point in 2006. Such a prospect would place the timely development of the Pohokura field seriously at risk. Even if the application for authorisation was fast tracked to the extent possible, timing problems would be inevitable.

45. Therefore, the prospect of revocation exposes the Joint Venture and the Commission to:

45.1 the unnecessary duplication of significant costs which are inherent in any authorisation application; and

45.2 a process which could well delay first production from the field.

Proper application of section 65

Background and relevant framework

46. Decision 505 has conferred authorisation upon the Joint Venture to jointly market all gas from the Pohokura gas field, subject to the fulfilment of certain conditions.

47. In terms of the current conditions, contracts entered into by the Joint Venture prior to 30 June 2006 are authorised even if the field is not fully operational by 30 June 2006.[26]

48. Contracts entered into by the Joint Venture after 30 June 2006 are only authorised if the field is "fully operational before 30 June 2006". In order to satisfy this requirement, gas production equipment must be installed, commissioned and capable of producing at least 60 PJ of gas per annum.

49. Assuming that the field is fully operational before 30 June 2006, this authorisation still confers rights upon the Joint Venture to jointly market gas, even if the proposed separate delivery of gas does in fact take place.

50. The fact that the Commission proposes to revoke existing and ongoing rights under the authorisation it has granted is material to the manner in which the Commission must exercise its discretionary powers under section 65.

51. If the Commission concludes that it has jurisdiction under section 65(1)(a) or (b), it must properly assess the impact of the changes in question on the detriments and benefits before it can exercise its discretionary powers under section 65. It is plain from the wording of section 65 that the Commission must consider the prospect of an amended or substituted authorisation before it can exercise powers of revocation. This approach is also the accepted methodology under the equivalent provision of the Australian Trade Practices Act.[27]

52. It therefore follows that the Commission must reassess the detriments and benefits at this time. The relevant changes which need to be taken into account, whether the Commission assumes jurisdiction under either section 65(1)(a) or (b), are as follows:

52.1 reduced detriments in the event that the proposed separate delivery does in fact occur; and

52.2 reduced benefits in the event that early production is achieved pursuant to separate delivery.

53. As discussed below, this reassessment is based upon matters previously raised by the Joint Venture, and considered by the Commission, in the

[26] As noted above, this date will need to be extended.

[27] See *Re Media Council* (1996) ATPR 41-261, at 42,261; *Re AGL Cooper Basin* (1997) ATPR 41-593, at 44,172-73; *Re 7-Eleven Stores* [1998] ACompT 3, at 11.

context of Decision 505. It is merely a question of adjusting the analysis to account for a potential change in facts, should there be separate delivery of gas in the case of the cornerstone contracts supporting development of the field. The Commission's methodology for the assessment of detriments remains relevant, but would require adjustment taking into account the separate delivery of gas. Greater emphasis will also need to attach to the public benefits other than earlier development of the field. These are public benefits which the Commission has already recognised in Decision 505.

54. The Commission can only properly undertake this reassessment by applying the standard authorisation test. Therefore, consideration needs to be given to the correct factual and counterfactual which would apply to the changed circumstances, followed by a comparative assessment of the detriments and benefits applying to those redefined counterfactual circumstances.

"Straight conduct test" does not apply

55. The Commission accepts this methodology, at paragraph 88 of the Draft Determination. However, it seeks to depart from this accepted approach here on the basis of the so-called "straight conduct test", as described by the Australian Trade Practices Tribunal in *Re Media Council*.[28]

56. It is helpful to set out the full text of the Tribunal's discussion of that test:

> It was the Commission's submission that it will sometimes be the case that no elaborate analysis is required when the very conduct that was originally authorized is currently not being undertaken. The Commission submitted that the present application is such a case. As Mr Comans put it in oral address, "our primary submission is the simple fact they have moved away from the rules is enough and there is no detriment benefit or economic analysis involved in that at all". It was the Commission's submission that a straight conduct test is then sufficient, not only to establish "material change of circumstances" but also to warrant revocation. Various possibilities were envisaged at the level of principle. It could be that the conduct was never in fact undertaken; it could be that the parties have moved away from the conduct; it could be that the evidence shows that the parties do not intend in future to engage in conduct that is authorized or intend to engage in conduct that is inconsistent with the conduct which is authorized. If so, such a "dead letter authorisation" should be removed from the books.
>
> We accept this submission in principle but defer consideration of whether it applies to the present matter.[29]

57. The "straight conduct test", which at most has only been accepted in principle, does not apply here because:

    57.1 the parties have not moved away from the authorised conduct, which relates to all of the gas in the Pohokura field;

    57.2 the Joint Venture has every intention to engage in the authorised conduct;

    57.3 there remains the likelihood of joint marketing; and

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28 (1996) ATPR 41-497.
29 At 42,261.

57.4 the fact that there may be some separate delivery of gas from the field is not inconsistent with joint marketing, in particular where joint marketing results in optimum production from the field.

58. Accordingly, this authorisation cannot be characterised as "dead letter", and the so-called "straight conduct test" does not apply.

Factual and counterfactual

59. In undertaking the reassessment of standard authorisation analysis in relation to the changed circumstances, there is an obvious change to the factual which was adopted in Decision 505. The new factual will involve both separate and joint marketing of the field. As noted above, around half of the expected reserves of the field may be jointly sold.

60. The most likely counterfactual will be for separate marketing for the entire production from the field.

Detriments

61. The onus is upon the Commission to establish detriments.[30]

62. The Commission's findings on detriments are set out in paragraphs 424-450 of Decision 505. Those findings are based upon the factual of joint marketing for all of the Pohokura gas. The counterfactual used was so-called Scenario 1 separate marketing. Should the proposed separate delivery of gas be achieved, those factual/counterfactual terms of reference will no longer be appropriate. The new factual and counterfactual circumstances described above will necessarily require a reassessment of detriments.

63. The Commission's reasoning in this part of Decision 505 remains problematic. The Commission's main concerns related to allocative and dynamic inefficiencies.

64. The Commission had two concerns in its discussion of allocative efficiency. It asserted that output may be more limited under joint marketing than may be the case under Scenario 1 marketing.[31] It also asserted that price discrimination may be facilitated under joint marketing, with the result that some purchasers may face higher prices.[32]

65. Turning to dynamic efficiencies, the Commission appeared to attach significant weight to the fact that, under joint marketing there would not be the range of terms and conditions of contract which would apply under separate selling. This the Commission identified as an "important detriment".[33] The remaining concerns of the Commission appeared to be based on the assertion that joint marketing would slow down the development of an efficient and competitive market.[34]

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30 Decision 505, paragraph 397.
31 Paragraphs 426 and 428.
32 Paragraph 429.
33 Paragraph 443.
34 See e.g. paragraph 438.

66. This is not a time at which it is appropriate or necessary to relitigate those findings. However, we record that we continue to strongly disagree with them. The lack of detail in the Commission's reasoning, and the absence of quantification, also makes it difficult to engage in an informed debate on the findings.

67. For present purposes, however, the important point is that if the proposed separate delivery of gas is achieved under the new factual, then even on the Commission's own analysis there will need to be a significant reassessment of detriments. For example, the following factors would, again on the basis of the Commission's own reasoning, point to a significant reduction of the detriments which were found to exist in Decision 505:

    67.1 The concern about the uniformity of contracts is largely removed. As noted above, around half of the field may be separately marketed under the new counterfactual, assuming there will be separate delivery of this gas.

    67.2 The fact that such separate delivery is proposed serves to answer what appeared to be a central concern of the Commission, namely that prices would be higher under joint marketing than they would be under separate marketing.

    67.3 The concerns about the development of an efficient and competitive market will also need significant revision.

    67.4 The assumptions about limitations in output will require revision.

Public benefits

68. Similarly, it is obvious that the new counterfactual circumstances which would necessarily arise, should the Commission assume jurisdiction under section 65, involve different public benefit assessments.

69. In the context of the application leading to the authorisation of joint marketing in Decision 505, the focal public benefit was the timely development of the Pohokura field. Others benefits were identified by the Joint Venture, and accepted by the Commission.[35] Those benefits included:

    69.1 lower production and transaction costs;

    69.2 optimal pool depletion;

    69.3 increased exploration incentives; and

    69.4 reduction in the adverse effects on the environment.

70. Given the magnitude of the benefits of timely development of the field under the original application, it was unnecessary for the Joint Venture and for the Commission to engage in detailed analysis of those other benefits.

[35] Decision 505, paragraphs 496 to 514.

71. Clearly, these "other benefits" assume considerable importance in the revocation context. In particular, the potential for joint marketing now attaches to the latter tranches of gas from the field. In this context, the benefits of optimal pool depletion assume particular importance.

72. In the time made available to us to prepare our submission of 18 October 2004 in response to the Commission's letter of 1 October 2004, it was not possible to undertake a detailed reassessment of public benefit issues. In paragraph 18 of our submission, we noted that detailed consideration needed to be given to this issue.

73. The only further communication between the Commission and Todd since this date was the meeting held on 3 November between Commission staff and Messrs Deppe and Hall. The Commission's file note of this meeting reflects that Mr Hall again stated that the Commission should undertake a reassessment of detriments and benefits. The Commission rejected this view at that meeting, and the Draft Determination reflects that the Commission does not consider this to be a relevant consideration in the current context. Accordingly, Todd has not at this time undertaken further detailed analysis of the public benefits.

74. Clearly, however, public benefits are a relevant issue to be taken into account, and detailed consideration needs to be given to the public benefits which assume particular relevance in this new setting.

D. Grounds for consideration of an amended or substituted authorisation

75. The Commission takes the position in the Draft Determination that there is "insufficient evidence of grounds" for it to be required to consider an amended or substituted authorisation.[36] This conclusion is incorrect because:

75.1 The Commission has failed to give appropriate consideration to the likelihood that there will continue to be joint marketing in accordance with the rights conferred under Decision 505.

75.2 The basic elements of the facts and the reasoning behind Decision 505 remain relevant. No new arguments are being introduced in this submission; rather it is a matter of adjusting the analysis to account for a potential change in the facts, namely that not all of the gas from the field may be jointly sold.

75.3 The Commission has given no consideration to the changed counterfactual circumstances which would necessarily arise from a finding of jurisdiction under section 65.

75.4 Further, the Commission has failed to turn its mind to the reassessment of detriments and public benefits, as it is required to do in the circumstances of this case.

[36] At paragraph 95.

E. Process issues

76. It follows that the Draft Determination is defective in a material way. The Commission has failed to address a relevant consideration, namely the reassessment of the standard authorisation test.

77. Section 65(2) requires that the Commission give a reasonable opportunity for the making of submissions, and the Commission must have regard to those submissions before it can enter a decision. This obligation has not been discharged by the Commission, and the Commission cannot now safely proceed to a final determination of this matter.

78. It is submitted that if the Commission wishes to proceed with this matter then an appropriate way forward will be for the Commission to:

    78.1 invite the Joint Venture parties to make detailed submissions on the authorisation test;

    78.2 issue a revised Draft Determination which addresses the additional matters which need to be considered in the context of a proper reassessment of the standard authorisation exercise, as discussed above; and

    78.3 provide a further opportunity for written submissions in response to the revised Draft Determination.

79. Todd does not request that the Commission hold a conference in relation to this matter.

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Todd Petroleum Mining Company Limited