

**CONTACT ENERGY LIMITED: SUBMISSION TO THE COMMERCE COMMISSION****APPLICATION BY THE POHOKURA JOINT VENTURE PARTIES FOR AUTHORISATION  
OF JOINT MARKETING ACTIVITIES****1. INTRODUCTION**

- 1.1 Contact Energy Limited welcomes the opportunity to provide a submission on the Pohokura Joint Venture parties' ("JV Parties") application for authorisation of joint marketing activities.
- 1.2 Contact is a major electricity generator, wholesaler, and retailer. Contact is also a wholesaler of gas to large users such as other generators, large industrial users and petrochemicals producers, and a gas retailer.
- 1.3 Contact is therefore likely to be a major purchaser of gas produced from the Pohokura gas field by the JV Parties.  
  
*Summary*
- 1.4 Contact considers that the Application should not be authorised.
- 1.5 At least one of the JV Parties has previously told the Commission that it intended to take its equity entitlement to Pohokura gas. The Application does not explain what has changed so that the JV Parties now consider separate marketing not to be feasible.
- 1.6 The Application in effect concedes that separate marketing *is* feasible, albeit after a delay.
- 1.7 It is not credible for the JV Parties to claim that, in the absence of an authorisation for joint marketing, the development of the Pohokura gas field will be delayed by a minimum of 3 years.
- 1.8 It is uncertain whether allowing joint marketing will enable production from Pohokura to commence as early as 2004.
- 1.9 Even if the supply of gas from Pohokura is delayed, this necessarily means that more gas is available at some future point in time. For example, this could be for an additional 3 years at the end of the current estimated life of the field (i.e., after 2020). The JV Parties have not taken into account this benefit when calculating the welfare losses associated with the delay of gas production from Pohokura
- 1.10 The welfare losses calculated in the CRA Report do not take into account allocative efficiency losses which will result from allowing joint marketing.
- 1.11 Authorisation of joint marketing activities is likely to inhibit the development of "mature" market features associated with successful separate marketing.

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- 1.12 Authorisation of joint marketing has the potential to establish a precedent that acts as a disincentive on producers to enter into agreements which enable or encourage separate marketing to the extent that the inability of the New Zealand market to support separate marketing is self-fulfilling.
- 1.13 Scenario 1 discloses a feasible separate marketing regime. The difficulties identified in the Application can be overcome.
- 1.14 Contact does not consider that it is open to the JV Parties to claim exploration incentives as a public benefit flowing from the practice for which authorisation is sought. The JV Parties themselves carried out exploration in anticipation of separate marketing.
- 1.15 There are a number of distinguishing features that mean that the ACCC authorisation decisions are not directly applicable in the New Zealand context.

### *Confidentiality*

- 1.16 Contact seeks confidentiality for specific information in the submission included in square brackets and shaded. A copy of this submission with the confidential information deleted is provided to assist the Commission.
- 1.17 Contact requests that the Commission make a confidentiality order under section 100 of the Commerce Act 1986 in respect of this information.
- 1.18 Contact also requests that, on the expiry of any confidentiality order that the Commission makes, the information continues to be withheld under section 9 of the Official Information Act 1982. Contact requests that it be notified by any request made under that Act for the information, and be consulted as to whether the information remains commercially sensitive at the time that the request is made.
- 1.19 These requests for confidentiality are made because the information is commercially sensitive and disclosure would be likely to unreasonably prejudice the commercial position of Contact.

## **2. POHOKURA JOINT VENTURE**

### *JV Parties*

- 2.1 The JV Parties are prominent players in the New Zealand gas market. Shell and Todd, in particular, have a long history of involvement in the production sector.
- 2.2 It has recently been announced that OMV will purchase Preussag's interest in Pohokura. OMV is also an existing player in the New Zealand gas market. The result of this acquisition is that Shell, Todd, and OMV will together control New Zealand's two largest gas fields: Maui and Pohokura.
- 2.3 Shell and Todd are also the owners of the third largest gas field, Kapuni. Todd owns Mangahewa, the fifth largest gas field. STOS, a Shell/Todd owned entity, will also be the field operator for Pohokura and accordingly have an important role in determining the way the field is developed and operated.

### *JV agreement and separate marketing*

- 2.4 The JV Parties state in paragraph 15 of the Application that authorisation is sought for joint marketing as there is no other feasible means of marketing gas from Pohokura.

- 2.5 As recognised by the Commission in *Decision 408*, JV agreement “permits the JV partners to ‘take in kind’ – that is, to take ownership of the share of the output of the field that equates to their share of the JV, and to market that gas independently of the other partners”.<sup>1</sup>
- 2.6 *Decision 408* also states that Shell “[pointed] out ... that the provisions of the joint venture agreement imply that equity selling is intended to be a feature of the marketing arrangements in respect of Pohokura gas”.<sup>2</sup>
- 2.7 In addition, in *Decision 411* it is stated that:
- “Todd has provided evidence to the Commission that it has informed the Pohokura Offtake Committee that it expects to take, at least in part, its equity entitlement to the Pohokura product. ... The gas it takes, if it is significant, could provide competition to the JV/Shell”.*
- 2.8 It is clear that, as recently as the middle of 2000, the JV Parties anticipated that at least one JV party would exercise its right to take in kind, and separately market gas produced from Pohokura. From the discussion contained in *Decision 408* and *Decision 411*, it seems that separate marketing was not only viewed as “feasible” by the JV Parties, but also as likely.
- 2.9 The Application does not explain what has changed so that the JV Parties no longer consider this to be the case.
- 2.10 Contact considers it disingenuous of the JV Parties to now claim that separate marketing is not “feasible”.

### 3. TIMELY DEVELOPMENT

#### *3 year delay not credible*

- 3.1 A significant public benefit claimed by the JV Parties is that joint marketing will result in the “timely” development of Pohokura. Section 8.2.1 of the CRA Report says that if joint marketing is authorised, production from Pohokura can be expected to commence in 2004.
- 3.2 It is also claimed that separate marketing in the form of Scenario 1 would result in a delay of at least 3 years, with production not commencing until 2007. Contact does not consider that the claim of a 3 year delay is credible.

#### *Steps to establish framework*

- 3.3 The steps that the JV Parties must take in respect of establishing the legal framework for both joint marketing and separate marketing are identical. They are:
- (a) negotiating a field development plan and production schedule between themselves;
  - (b) obtaining a mining permit;
  - (c) obtaining the necessary resource consents; and
  - (d) negotiating contracts of supply with purchasers.

<sup>1</sup> Paragraph 233, *Decision 408*.

<sup>2</sup> Paragraph 235, *Decision 408*.

- 3.4 In relation to obtaining a mining permit, paragraph 5.4.10 of the Minerals Programme for Petroleum states that the Minister of Energy must take into account the proposed production profile and the proposed commencement date for production when the Minister assesses the acceptability of the work programme prior to granting a mining permit. Having regard to recent publicity regarding gas shortages, Contact finds it difficult to believe that the Minister would be satisfied with a proposed production profile which includes a delay of 3 years.
- 3.5 Negotiating a field development plan and production schedule and obtaining a mining permit can be undertaken at the same time in either the joint marketing or separate marketing context.
- 3.6 One of the JV parties has indicated that obtaining the necessary resource consents may be a difficult hurdle.<sup>3</sup> However, resource consents are required irrespective of whether gas is to be jointly or separately marketed, and accordingly this cannot be claimed as a factor that contributes to the delay that the JV Parties argue would be a result of separate marketing.
- 3.7 Some extra negotiation will be needed between the JV Parties at stage (a). This would involve addressing the optimal depletion path, balancing etc, if the JV parties are required to market separately. It is not credible for the JV Parties to claim that the additional time associated with those negotiations would require the development of Pohokura to be delayed for 3 years before production under separate marketing arrangements would occur.

*Economic Losses*

- 3.8 The Application fails to take into account that delay leads to a severe loss of economic value to the JV Parties.
- 3.9 The Commission should be sceptical of the claim that a 3 year delay would be an necessary consequence of separately marketing the gas given the obvious incentive on the JV Parties to avoid a large economic loss.

*Competitive Tension*

- 3.10 There is already a lack of competitive tension in the producer sector. [ ]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

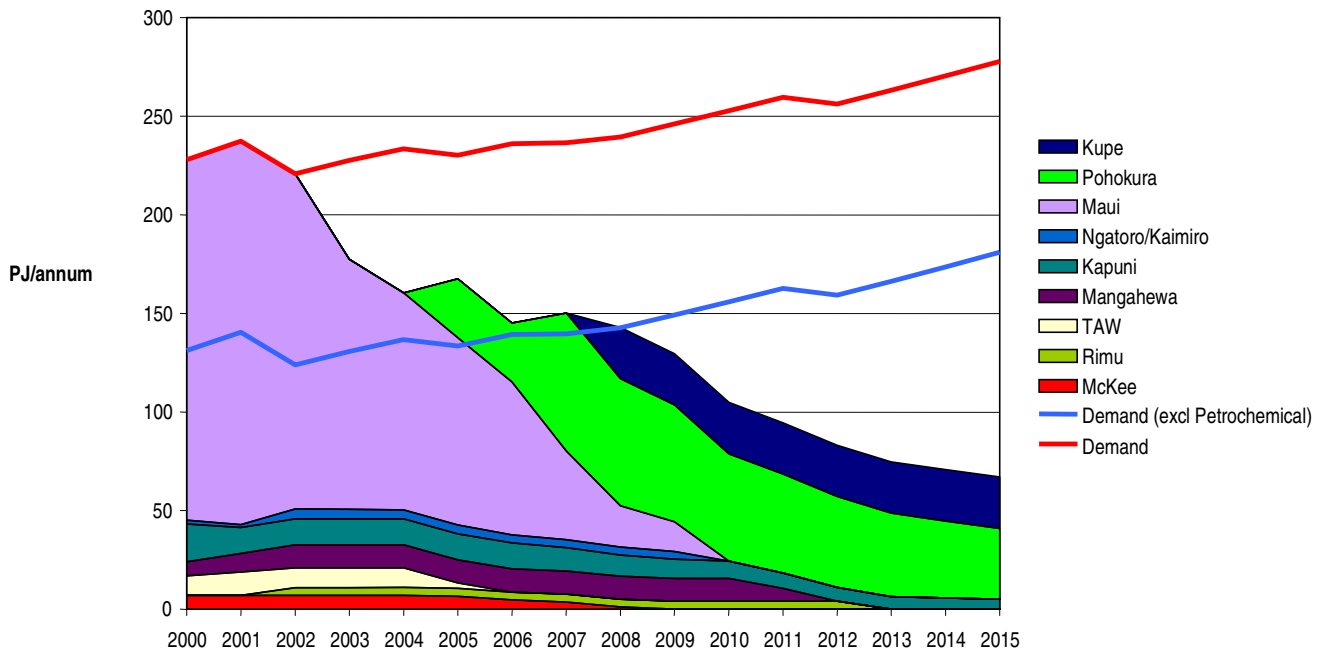
[REDACTED]

*Supply and demand mismatch*

- 3.11 Given the increasing mismatch between gas supply and demand (as illustrated by the Figure 1 below), it is highly unlikely that buyers would seek to add to any delay or engage in protracted negotiations for the gas because of the short supply of gas anticipated over the next 10 to 12 years. In fact, purchasers are likely to be anxious to conclude deals swiftly, and certainly take no longer than the time they would take in the context of joint marketing.

<sup>3</sup> The Independent, 26 February 2003, page 8.

Figure 1: NZ Gas Supply/Demand



3.12 [ [REDACTED]  
[REDACTED]  
[REDACTED] ]

[ [REDACTED] ]

3.13 [ [REDACTED]  
[REDACTED]  
[REDACTED] ]

3.14 [ [REDACTED]  
[REDACTED]  
[REDACTED] ]

3.15 [ [REDACTED] ]

3.16 [ [REDACTED]  
[REDACTED]  
[REDACTED] ]

*Actual Delay*

- 3.17 The JV Parties state in the Application that, if joint marketing is authorised, gas may be produced from Pohokura in 2004. In contrast, recent statements from one of the JV parties indicated that, even with joint marketing, the first gas may not be produced until 2006.<sup>4</sup>
- 3.18 Contact is unsure why the commencement of production, even under a joint marketing scenario is now predicted to be 2006. However, this being the case, if production under separate marketing arrangements is still expected to commence in 2007, and joint marketing will only result in production commencing one year earlier, then the welfare losses calculated in the CRA Report should be significantly reduced.

**4. CALCULATION OF WELFARE LOSSES**

- 4.1 As discussed above, the JV Parties have submitted that, without authorisation, the development of the Pohokura field will be delayed by 3 years. The JV Parties argue that this in turn implies higher gas prices and welfare losses in the form of reductions in consumers' and producers' surplus.
- 4.2 These welfare losses have been quantified in the CRA Report. The welfare losses, and therefore the public benefits of authorisation, are claimed to be \$204.1 million in CRA's base case scenario. To put these claimed welfare losses in context, they are equivalent to \$0.52 per GJ of gas to be recovered from Pohokura.<sup>5</sup>

*3 Year Delay*

- 4.3 The CRA analysis is wholly dependent upon the premise that, without joint marketing, there will be a 3 year delay in production of gas from Pohokura. As discussed elsewhere in this submission, Contact does not accept that this is credible.

*Welfare losses and allocative efficiency*

- 4.4 The analysis undertaken by CRA assesses the allocative efficiency losses associated with higher gas prices as a consequence of Pohokura supply being delayed. Normally, anti-competitive practices have allocative, productive and dynamic efficiency losses. These are the competitive detriments which the public benefits need to outweigh for authorisation to be granted.
- 4.5 The estimated welfare losses from the CRA Report analysis are allocative efficiency losses from higher gas prices stated to result from the inability of the JV Parties to jointly market the gas.
- 4.6 However, if joint marketing itself results in higher gas prices, then allocative efficiency losses will actually be a consequence of *allowing* joint marketing, and will not be avoided by the authorisation of joint marketing, contrary to the JV Parties' claims.
- 4.7 This is illustrated by some of the sensitivity testing conducted by CRA and summarised in Table 19 on pages 100 and 101 of their Report. The table shows that welfare losses are sensitive to changes in the supply of gas assumed from other fields.

<sup>4</sup> The Independent, 26 February 2003, page 8.

<sup>5</sup> This assumes that gas production from Pohokura will commence in 2004, plateau at 70PJ/annum from 2007 for 4 years, and then decline at 10% per annum thereafter with a 10% real discount rate.

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- 4.8 Contact is concerned that, rather than allocative efficiency gains as a consequence of joint marketing, there will be allocative efficiency losses if joint marketing provides scope for higher gas prices from Pohokura and other sources than would otherwise be the case.
- 4.9 In addition, consideration needs to be given to the potential for reductions in productive and dynamic efficiency as a consequence of joint marketing. The JV Parties appear to argue that joint marketing will enhance dynamic efficiency by encouraging greater exploration (paragraph 75 of the application). As discussed in Part 7, Contact disagrees with this.

*Additional supply later*

- 4.10 Even supposing that separate marketing of gas by the JV Parties delays production from Pohokura, any such delay necessarily means more gas is available at some future date. This could be for an additional 3 years at the end of the current estimated life of the field (i.e. after 2020) or could mean a higher extraction rate from 2007 to 2020.
- 4.11 This additional gas supply would have a similar effect to that claimed in the CRA Report in terms of putting downward pressure on gas prices and consequent gains in producer and consumer surplus. These need to be deducted from the benefits quantified by CRA. Because they accrue later, discounting means they will have a lower value in present value terms although this could be offset to the extent that their real value increases over time.

*Common prices do not mean no competition*

- 4.12 The JV Parties argue that separate marketing of Pohokura gas will not result in any greater price competition, since all prices will tend to the same level via parallel behaviour (paragraph 69 of the Application).
- 4.13 Contact agrees that common prices may indeed result, even with separate marketing.
- 4.14 However, if this occurred, it does not mean that there will have been no additional competition in the separate marketing context. Many competitive markets have common prices. The issue is whether there will be any additional downward pressure on prices in general as a consequence of separate marketing.

[REDACTED]

4.15 [REDACTED]

4.16 [REDACTED]

4.17 [REDACTED]

4.18 [REDACTED]

4.19 [

[REDACTED]

4.20 [

[REDACTED]

## 5. MATURITY OF THE NEW ZEALAND GAS MARKET

5.1 The Application places significant emphasis on a number of the characteristics identified by the ACCC as being features of more “mature” markets where separate marketing is the norm. In particular, at paragraph 21 of the Application, it is stated that “The ACCC in the *North West Shelf Project - Determination* identified the market features **necessary** to support separate marketing.” (emphasis added).

5.2 This interpretation is not correct. In fact, in the *North West Shelf Project - Determination*, the ACCC specifically stated that “it is **impossible to be prescriptive** about exactly what market features need to develop before separate marketing will become viable in WA”<sup>6</sup> (emphasis added).

5.3 In addition, the factors listed in paragraph 21 of the Application seem to have been taken from the ACCC's submission to the Gas Reform Implementation Group on Upstream Issues, rather than the ACCC's *North West Shelf Project - Determination*.

5.4 In the *North West Shelf Project - Determination*, the ACCC actually said:

*“... the greater the number of the following list of market developments that are introduced, the greater the likelihood that separate marketing will be viable:*

- *a significant increase in the number of customers;*
- *the entry of new competitive suppliers;*
- *additional transportation options;*
- *development of storage facilities;*
- *the entry of brokers/aggregators*
- *the creation of gas related financial markets; and*
- *the development of significant short term and spot markets.”*

5.5 These comments were made specifically in relation to the Western Australian market, as it existed at that time. However, in *Mereenie Producers – Gasgo Sales Agreement – Determination*<sup>7</sup> the ACCC repeated these market features and indicated that they may be applied to other geographic markets.

5.6 The Australian decisions are considered in greater detail in Part 8 of this submission.

5.7 It is a circular exercise to try to determine whether separate marketing is feasible by reference to a list of market characteristics. In fact, separate marketing may facilitate the development of the characteristics of

<sup>6</sup> *North West Shelf Project Determination*, page v

<sup>7</sup> 7 April 1999.



markets, like those in the US and the UK, that are considered more developed or “mature” than those in New Zealand or Australia.

5.8 A risk of identifying market features which are typically present in markets where separate marketing occurs is that those features may come to be regarded as pre-requisites for separate marketing.

5.9 These concerns are acknowledged in the recent paper produced for the CoAG energy market review in Australia regarding the separate marketing of natural gas. While the paper concedes that examination of the relative state of “maturity” of given markets (and attempts to identify the hallmarks of what constitutes such maturity) may well be a valid exercise, it was sceptical about the true value of identifying such features. It was stated that:<sup>8</sup>

*“The process of seeking to define relative market maturity simply by reference to a list of attributes can be akin to self-fulfilling prophecy. For example, the existence, of say, secondary markets, intermediary trading, spot markets and financial hedges are outcomes of a mature market, rather than prerequisites for separate marketing”.*

5.10 The paper goes on to say that separate marketing could itself be regarded as one of the ingredients that, in the appropriate circumstances, helps to create competition and therefore a more mature market.<sup>9</sup> Contact agrees.

5.11 In addition, CoAG’s November 2002 report, “Towards a Truly National and Efficient Energy Market” concluded that not all of the features of a mature market need to be present for separate marketing to be feasible. The report rightly points out that, if this were the case, “separate marketing itself would probably only be of academic interest, as a high degree of competition would already be achieved”.<sup>10</sup>

5.12 These observations are consistent with the development of the UK gas markets. In the UK between 1988 and 1995 contracts tended towards “supply type” arrangements with no dedicated source of supply. In addition, contracts developed where upstream companies would sell gas from a combination of sources.

5.13 In that period, separate “lifting” of gas field entitlements became the norm, developing to meet the requirements of the emerging market. This took place well before the development of a liquid spot market.

5.14 In addition, there is a real danger that authorisation of the present application will provide a significant disincentive for producers to ever put in place arrangements that would make separate marketing “feasible”, and therefore inhibit the development of a so-called “mature” market.

## 6. FEASIBILITY

6.1 Contact considers that scenario 1 (the second counterfactual) describes a feasible separate marketing programme.

6.2 [REDACTED]

<sup>8</sup> CoAG Energy Market Review “Separate Marketing of Natural Gas in Australia”, page 24.

<sup>9</sup> Ibid.

<sup>10</sup> CoAG “Towards a Truly National and Efficient Energy Market”, page 117.

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- 6.3 As Figure 1 (in Part 3, above) demonstrates, there does not appear to be any scenario in which all gas produced from Pohokura could not be accommodated by the New Zealand market, as early as 2004/2005.
- 6.4 The JV Parties are in a strong position to devise a field development plan and production schedule that optimises overall hydrocarbon recovery, and accelerates the rate of condensate and LPG production, without having to be concerned that they will be unable to sell the gas produced. This is a luxury that did not exist when Maui dominated the market, nor in Western Australia when the North West Shelf Project sought authorisation for joint marketing
- 6.5 As discussed in Part 3, the JV Parties are heavily incentivised to complete a field development plan and production plan provided they are of a common mind to develop the resource as soon as possible.
- 6.6 Contact does not agree with the JV Parties' contention in paragraph 26 of the Application that selling jointly produced gas under individually negotiated contracts would present insurmountable problems for the JV Parties.
- 6.7 The apportionment of the cost of appraisal, development and operation would be able to be overcome if the parties separately marketed gas. Such matters must also be addressed in the context of joint marketing, although there may be an added level of complexity in a separate marketing scenario.

### *Lifting and balancing arrangements*

- 6.8 The most common issue faced by an individual joint venture party that takes its separate entitlement is the tension between maximising field production and providing flexibility to meet that joint venture party's purchasers' nominations/needs.
- 6.9 Lifting and balancing arrangements only allow a limited amount of flexibility for the purchaser to overlift before curtailment of further liftings within a specified period. Similarly, underlifting may breach minimum production requirements, and will result in loss of the entitlement that is not lifted, or deferral of lifting until later in the field's life.
- 6.10 There are a number of feasible approaches to lifting and balancing issues. They are:
- daily quantity and capacity sharing;
  - profile sharing; and
  - whole/life of field balancing.

### *Daily quantity and capacity sharing*

- 6.11 Daily quantity and capacity sharing is the most simple arrangement. It involves the available maximum daily quantity producible from a field in any year being allocated on the basis of equity shares.
- 6.12 Each joint venturer would be able to nominate and use as much or as little of the maximum daily quantity as they like, either with no restriction on total take, or with some annual lifting limit set by that joint venture party's share of the annual contract quantity (typically 110 to 120%).
- 6.13 The drawbacks of the daily quantity and capacity sharing arrangements, however, may be that recovery of underlifting is not addressed, or there may be a limited ability to lift underlifted quantities in the following year or years, depending on the field profile.

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- 6.14 Accounting principles would also have to be amended in a standard joint venture operating agreement to allocate revenue streams separately against actual liftings, whereas field costs remain allocated on an equity basis.
- 6.15 However, Contact considers that greater flexibility could be gained by the joint venture parties by swapping or buying/selling gas at the wellhead.

### *Profile sharing*

- 6.16 Where the plateau period of a field is able to be confidently predicted, or a given level of reserves carved out for this purpose, the joint venture parties may agree to take different shares of the profile, in particular years.
- 6.17 Over the plateau period, the joint venture parties' expected off-takes would be equal to their equity shares in the joint venture. Some complexity exists in terms of balancing the present value of differential off-takes over time if the joint venture parties lift different shares. This may or may not be addressed in the original profile share.
- 6.18 Risks of unexpected reservoir or production problems will lie with those who are lifting later in the life of the field and with those who chose to uplift their production later in the life of the field. Accordingly, restrictions on the ability to recover an underlifted position, and caps on overlifting, need to be developed.

### *Whole/life of field balancing*

- 6.19 The whole/life of field balancing approach involves the joint venture parties differentially nominating and lifting, with the added feature of over/under liftings against the annual contracted quantity being carried forward and rebalanced over successive years, resulting in the lifting entitlements being varied from year to year.
- 6.20 In essence, this means that equity participation for the joint venture parties is continuously variable. Accordingly, restrictions on the ability to recover an underlifted position, and caps on overlifting, need to be developed.
- 6.21 In practice, setting up a whole/life of field balancing arrangement would involve the following steps:
- the operator would set a profile for annual production for the life of the field based on an agreed set of principles;
  - joint venture parties' underlift or overlift position would be established against the nominal lifting entitlement by deducting cumulative actual take from the equity share of cumulative production;
  - successive years' entitlement would be recalculated to rebalance joint venture parties' positions over the agreed period (i.e., reduced entitlement for overlifters, and increased entitlement for underlifters);
  - joint venture parties would make a daily nomination on the basis of their adjusted lifting entitlement;
  - any spare production capacity would normally be offered to joint venture parties who had underlifted, in preference to joint venture parties in an overlifted position;
  - once a joint venture party has lifted its full field entitlement, the remaining production is handed to the underlifted parties, along with their remaining costs (except for abandonment costs).

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- 6.22 The issues described in the above approaches have not proved insurmountable to UK producers. In fact, as discussed elsewhere in this submission, separate lifting of gas field entitlements from the UK continental shelf fields became commonplace between 1988 and 1995, well before a liquid spot market developed.
- 6.23 In the absence of a spot market, flexible, short term sales agreements, interruptible sales agreements, and storage can all provide alternative solutions. Upstream gas trading arrangements with other field joint venturers can also provide flexibility, as can asset trades to rebalance an individual joint venture party's position.
- 6.24 With only three joint venture parties, an equity-owned pipeline, and on-shore processing facility, concluding individual lifting arrangements and sales in respect of Pohokura should be relatively straightforward.

### *Tendering Process*

- 6.25 The sale process itself would not be overly onerous if the JV Parties separately marketed gas.
- 6.26 Each of the JV Parties would be likely to run their own tendering process along the following lines:
- the JV Parties would presumably research the requirements of purchasers in terms of flexibility, reliability, etc;
  - the JV Parties would decide on a development plan and production schedule (including balancing rules);
  - individual selling parties, if they wished, would then offer their share of production determined in accordance with the development plan and production schedule;
  - due to lifting and balancing arrangements, the sum of the offerings made by each JV party would probably be the same. However, this does not mean that each selling party would offer the same terms to all buyers. For example, some buyers may prefer more flexibility than others.

### *Spot market in New Zealand*

- 6.27 As described elsewhere in this submission, the lack of a spot market has been suggested as a factor that inhibits separate marketing.
- 6.28 A gas spot market in NZ would probably take the form of a simple overs and unders market, and would not need the complexity that exists, for example, in respect of the electricity spot market.
- 6.29 Trades of gas would be made at the entry point into a major pipeline (such as the Maui pipeline), with the buyer usually paying for transport to the point of demand. Trading parties would therefore just use the market to balance their daily off-takes with supply. Settlement is just as likely to be volumetric as financial.
- 6.30 The development of a spot market of the nature described above is likely to be encouraged by separate marketing. Conversely, it is unlikely that a spot market will develop if joint marketing predominates.

## **7. EXPLORATION INCENTIVES**

- 7.1 Contact does not consider that it is open to the JV Parties to claim that benefits relating to exploration incentives accrue as a result of the authorisation of joint marketing by the Parties. The JV Parties have already completed their exploration.

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- 7.2 Even if the Application is authorised, new exploration cannot be on the basis that the explorers expect to obtain authorisation from the Commission or will not need an authorisation for joint marketing. Parties undertaking new exploration must be aware of the fact that the Commission must address each request for authorisation of joint marketing activities on the merits of the Application at the relevant time, in the context of the prevailing market circumstances.
- 7.3 Even if the authorisation of this Application provides some encouragement, or comfort to prospective explorers, then, in Contact's submission, the degree to which this increases the incentive on parties to explore is negligible.
- 7.4 Specifically in relation to the Pohokura JV, as described above, the JV agreement is drafted in a way that contemplates separate marketing by the JV Parties. Obviously, at the time the JV agreement was entered into, the JV Parties had no assurance that they would be able to jointly market the gas produced from Pohokura.
- 7.5 Accordingly, Contact does not consider that it is open to the JV Parties to claim that increased exploration is a benefit that would be a result of authorising the Application.

### 8. AUSTRALIAN AUTHORITY

- 8.1 The JV Parties place considerable emphasis on Australian decisions of the late 1990s. In particular, the JV Parties rely on the ACCC's determinations in respect of the North West Shelf Project (July 1998), and the Mereenie Producers Gasgo Sales Agreement (April 1999).
- 8.2 While Contact agrees that these decisions provide guidance for the Commission in its investigation, the Commission should keep in mind the particular facts of the Australian cases. We discuss the facts underlying the *North West Shelf Project – Determination*, and the *Mereenie Producers – Gasgo Sales Agreement – Determination* below.
- North West Shelf Project – Determination*
- 8.3 The *North West Shelf Project – Determination* related to the production of gas from the North West Shelf in Western Australia.
- 8.4 Authorisation was sought by the North West Shelf Project ("NWS Project") for a proposal to discuss and agree the common terms and conditions, including price, at which gas produced by the Incremental Venture (a member of the NWS Project) would be offered for sale by the NWS project, and to discuss and agree on methods for marketing and selling such gas (co-ordinated marketing).
- 8.5 The NWS Project consisted of five production joint ventures, including the Domgas Venture. The Domgas Venture already had an authorisation for joint marketing of gas produced by it for sales in Australia.
- 8.6 The ACCC described the Western Australian market as a "contract" or "project" market. It was characterised by few producers and buyers, a predominance of long-term contracts, and an absence of spot and secondary markets.
- 8.7 Annual production and consumption in Western Australia had increased from approximately 31PJ per annum in 1973/74 to 261PJ per annum in 1994/1995. From 1985 to 1994, there was only one purchaser of gas from

the NWS project. This was a statutory body which was subsequently disaggregated into five separate entities.

- 8.8 Each joint venture participant in the NWS Project had a right to take and separately dispose of its production entitlement. At the time of the determination, the participants in the NWS project had the capacity to supply 550TJ/day of natural gas. If authorisation was granted, the NWS project intended to increase capacity to 1100TJ/day. Two additional pipelines were also to be constructed.
- 8.9 The ACCC recognised that in the context of the Western Australian market, if one producer within a joint venture won a contract to supply, but the other joint venture parties did not have buyers for their share of the gas produced, there was an issue as to what the other producers were to do with their gas.<sup>11</sup>
- 8.10 The ACCC considered that it had to “form a view as to whether the expansion of the NWS Project would proceed if the co-ordinated marketing activities of the applicants were not granted authorisation.”<sup>12</sup>
- 8.11 It is crucial to remember that, in their submissions, the NWS Project were “emphatic” that the expansion would not proceed without co-ordinated marketing.<sup>13</sup>
- 8.12 The circumstances of the New Zealand market differ in material ways from those that existed in the Western Australian gas market at the time the ACCC determined the NWS Project’s application.
- 8.13 As described above, there is currently a gas shortage in New Zealand. The gas supply situation will get tighter over the next few years as Maui is further depleted. Unlike in the *North West Shelf Project – Determination*, the Commission need not consider whether there is a risk that separate marketing will mean that the individual JV Parties will not be able to sell their gas.
- 8.14 Based on Contact’s understanding of Pohokura’s projected production rates, Contact or Methanex would be capable of purchasing all the gas produced by the JV Parties. In addition, Genesis could also take a substantial portion of the gas produced (if not all the gas).
- 8.15 Accordingly, Contact finds it difficult to believe that the JV Parties will have any difficulties in securing purchasers for gas produced from Pohokura (whether production commences in 2004, or 2006/7).
- 8.16 In addition, it cannot be said that the JV Parties would not proceed without co-ordinated marketing. In fact, the Application implicitly accepts that separate marketing could proceed, albeit after a delay.
- 8.17 Contact appreciates that in a market like Western Australia where substantial investment in both production facilities and transmission pipelines was required, and in which producers have no guarantee of being able to sell all their product, co-ordinated marketing gives a greater level of comfort to the producers that they will recover at least some of their costs. However, these same concerns do not exist in the New Zealand market.

*Mereenie Producers – Gasgo Sales Agreement – Determination*

- 8.18 The Mereenie producers were active in the Northern Territory, a relatively small market with annual demand of approximately 18PJ. The Mereenie Joint Venture produced 9 – 10PJ per annum. The Palm Valley field (owned by the same parties that constituted the Mereenie Joint Venture) supplied 8 – 9PJ per annum. The Mereenie Joint Venture also held an interest in a licence over a field that was, at that time, undeveloped.

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<sup>11</sup> *North West Shelf Project – Determination*, page 46.

<sup>12</sup> *North West Shelf Project – Determination*, page 34.

<sup>13</sup> *North West Shelf Project – Determination*, page 26.

- 8.19 As well as there being few producers in a small Northern Territory market, there was, in essence, only one purchaser. The Mereenie Joint Venture sold only 0.1PJ per annum to a pipeline operator (which then on-sold the gas to a small number of industrial customers). The remaining gas produced from the Mereenie field was sold to Gasgo under the Gasgo Sales Agreement.
- 8.20 The gas purchased by Gasgo was ultimately sold to the Northern Territory Power and Water Authority (“PAWA”). PAWA was a statutory body in charge of the supply of electricity and evaluating fuel and electricity needs of the Northern Territory. Gasgo had a pre-emptive right over gas produced by the Mereenie producers – i.e. the Mereenie producers were obliged to offer Gasgo gas produced from the Mereenie field prior to offering it to any other party.
- 8.21 The Northern Territory government itself had no objection to joint marketing by the Mereenie Joint Venture.<sup>14</sup>
- 8.22 The gas market in New Zealand is very different from that of the Northern Territory, which, as described above, was characterised by a sole gas producer, and one dominant purchaser holding a pre-emptive right over the supply of gas to other purchasers.
- 8.23 In circumstances such as those in the Northern Territory, Contact agrees that long-term contracts similar to the Gasgo Agreement could be necessary to ensure the requisite cash flow to underwrite the investment and deliver the associated public benefits.
- 8.24 However, as discussed above, Contact does not envisage a situation where the individual JV Parties in Pohokura will have any difficulty in securing the sale of gas produced from Pohokura. In addition, the quantity of gas which is to be produced from Pohokura far exceeds that from the Mereenie field.

*Recent separate marketing*

- 8.25 Woodside Energy Limited announced in August 2002 that it has already sold its separate entitlement to gas from the Geographe and Thylacine gas fields.<sup>15</sup> Like Pohokura, these are offshore fields, with initial estimates suggesting that the fields together contain approximately 0.8 TCF (800PJ).
- 8.26 In February, Woodside and its partners in the Geographe and Thylacine fields announced that they had agreed commercial terms for joint development.<sup>16</sup>

*Market characteristics*

- 8.27 As already discussed, Contact already considers there is a risk that features commonly associated with mature markets may be turned into pre-requisites for considering a market to be “mature”.
- 8.28 In addition, Contact considers that focussing on the features listed in the *North West Shelf Project – Determination*, may detract from the competition analysis that the Commission is required to make.
- 8.29 For example, the feature which requires an examination of the number of gas customers, and suggests (in relation to Western Australia in the *North West Shelf Project – Determination*) that a “significant increase” in the number of customers will make separate marketing more likely, may disguise the fact that the relevant enquiry is the level of competition between competitors, not the number of competitors.

<sup>14</sup> *Mereenie Producers – Gasgo Sales Agreement – Determination*, page 21.

<sup>15</sup> Press release, 14 August 2002, [www.otway.woodside.com.au](http://www.otway.woodside.com.au)

<sup>16</sup> Press release, 5 February 2003, [www.otway.woodside.com.au](http://www.otway.woodside.com.au)

*Other decisions*

- 8.30 The JV Parties list a number of other decisions by the ACCC and the Australian Competition Tribunal in an appendix to the Application. However, the JV Parties do not seem to rely on these cases or otherwise refer to them in the Application and accordingly Contact does not intend to address these cases.

**9. CONCLUSION**

- 9.1 Contact does not consider that the Application should be authorised.
- 9.2 Separate marketing is feasible in the New Zealand market. The JV Parties in effect also concede that separate marketing is feasible, albeit after a delay. The delay claimed by the JV Parties as resulting from not being able to jointly market is not credible.
- 9.3 Contact does not consider that the net public benefits have been accurately quantified. As a result, in addition to the other matters identified above, the competitive benefits outweigh the competitive detriments flowing from the joint marketing of Pohokura gas.

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