

**COMMERCE ACT 1986: BUSINESS ACQUISITION
SECTION 66: NOTICE SEEKING CLEARANCE**

20 June 2008

By email: registrar@comcom.govt.nz
The Registrar
Market Structure Group
Commerce Commission
PO Box 2351
WELLINGTON

Pursuant to s 66 (1) of the Commerce Act 1986 notice is hereby given seeking **clearance** of a proposed business acquisition.

EXECUTIVE SUMMARY

1. Clearance is sought for Shell New Zealand Limited (**SNZ**), or an interconnected body corporate of SNZ, to acquire Mobil Oil New Zealand Limited's (**MONZ's**) "Aerostop Network" assets (**the acquisition**). MONZ's Aerostop Network comprises 48 unattended refuelling facilities at 34 local and regional airfields throughout New Zealand, which are used to supply Aviation Jet Fuel (**Jet A1**) and Aviation Gasoline (**Avgas**). The refuelling facilities consist of a fuel tank or tanks and "swipe card bowzers" (fuel pumps which are activated with customer swipe cards).
2. Jet A1 and Avgas are specialist aviation fuels. They are used in different aircraft and must be stored and transported separately. Jet A1 is a kerosene grade fuel used in turbine aircraft (such as 737s, 767s, helicopters and turbo prop aircraft). Avgas is a motor spirit based fuel used for light piston engine aircraft and helicopters.
3. The relevant supplies fall within the "General Aviation" segment of the broader Aviation Fuels market. The customers in this segment are users of light aircraft and helicopters engaged in a range of activities from recreational flying, tourism, agriculture, search and rescue, air charter and flying schools. The other segments of the Aviation Fuels market (which are not affected by the proposal) are the "Big Jet" (wide body aircraft: domestic and international carriers) and "Domestic/Special Carrier" sectors (turboprop aircraft operated by Air New Zealand Domestic, Air New Zealand Link and low cost airlines), and the "Military". There are separate product markets for the supply of Jet A1 and the supply of Avgas to the General Aviation sector.
4. Clearance is sought as the proposal could be seen as a "3 to 2" merger at the national level. In fact, the appropriate geographic market definition is arguably local given that there is relatively limited substitutability from the demand-side. The proposal results in only limited overlap (at 7 locations, out of a total of 65 locations nationally) and, when the individual markets for Jet A1 and Avgas at those sites are considered against the counterfactual scenario(s), the aggregation that would result from the acquisition is minimal (only one product at one location is impacted).
5. Importantly, the status quo is not sustainable, so the above categorisation would be incorrect. [] The assets are a legacy of infrastructure investments made in the 1980s when the government guaranteed after-tax returns on assets of 13%. The parties both face major capital expenditure in the short to medium term to replace or maintain assets which are

coming to the end of their asset lives. Profitability from the General Aviation sector has been poor, meaning that this capital expenditure is not justified by the returns at current levels. Matters will worsen with demand for Avgas declining by around [] per annum. The businesses also attract significant exposure to environmental risks and increasing compliance costs.

6. Faced with these factors, SNZ has previously considered exiting the General Aviation sector (as MONZ is doing through this sale) []

[] The New Zealand situation reflects the situation internationally, with several of the main players having announced their exit from aviation industry markets in some countries.

7. Given the nature of the assets, the risks inherent in the business, and the returns versus the capital investment that will be required, SNZ does not consider that there would be an alternative purchaser for the MONZ Aerostop Network assets. The alternative to the proposal is therefore MONZ's exit from General Aviation. Nonetheless, SNZ has considered what is likely to happen in an "alternative purchaser" scenario. []

[]

8. No counterfactual scenario offers a better outcome than the proposal, which is clearly efficiency-enhancing and pro-competitive. The parties' networks are geographically complementary, with overlap occurring at only a small number of sites. SNZ expects significant benefits through economies of scale and synergies (i.e. SNZ's future costs for the expanded network will be considerably lower if the acquisition proceeds). The proposal will result in a much stronger number two player to the dominant supplier, BP Oil New Zealand Limited (referred to in this application as **Air BP**), which currently supplies around [] of Jet A1 and [] of Avgas volumes in the relevant markets nationally.

PART I: TRANSACTION DETAILS

1. What is the business acquisition for which **clearance** is sought?

- 1.1 Clearance is sought for Shell New Zealand Limited (**SNZ**), or an interconnected body corporate of SNZ, to acquire Mobil Oil New Zealand Limited's (**MONZ's**) "Aerostop Network" assets (**the acquisition**). MONZ's Aerostop Network comprises 48 unattended refuelling facilities at 34 local and regional airfields throughout New Zealand, which are used to supply Aviation Jet Fuel (**Jet A1**) and Aviation Gasoline (**Avgas**).
- 1.2 MONZ currently supplies Jet A1 and Avgas to Kauriland Petroleum Limited and Kauriland Aviation Limited (**Kauriland**) for distribution to "homebase" customers currently serviced by Kauriland. "Homebase" customers are customers with a smaller facility located on privately-owned land such as a farm or a private airstrip. If the acquisition proceeds it will have no impact on the supply arrangements between MONZ and Kauriland.
- 1.3 The acquisition has no impact on terminal storage infrastructure and no impact on international and regional airfield infrastructure, both of which will remain the same. It therefore has no impact on MONZ's presence in the other Aviation Fuels market sectors (Big Jet, Domestic/Special Carrier and Military¹).
- 1.4 MONZ and SNZ entered into a sale and purchase agreement on 28 January 2008. The agreement is conditional upon clearance being granted by the Commerce Commission.

2. Who is the person giving this **notice**?

- 2.1 This notice is given by:

Shell New Zealand Limited
 Attention: David McGuire
 Head of Legal
 3 Queens Wharf
 PO Box 2091
 WELLINGTON

Telephone: (04) 498 0355
 Facsimile: (04) 498 4026
 Email: david.mcquire@shell.com

- 2.2 All correspondence and notices in respect of this application should be directed in the first instance to:

Minter Ellison Rudd Watts
 Lawyers
 125 The Terrace
 PO Box 2793
 WELLINGTON

Attention: Andrew Matthews / Oliver Meech
 Telephone: (09) 353 9847 / (04) 498 5095

¹ See paragraphs 11.22 to 11.28 below.

Facsimile: (04) 498 5001
Email: andrew.matthews@minterellison.co.nz
oliver.meech@minterellison.co.nz

3. Confidentiality

Do you wish to request a confidentiality order for specific information contained in or attached to the notice: If so, for how long? Why?

3.1 Confidentiality is not claimed for the fact of the proposed acquisition.

3.2 Confidentiality is sought for:

- (a) the information contained in Annex 1 to the confidential version of this application. Annex 1 is not attached to the public version of this application;
- (b) the information contained in bold square brackets in the confidential version of this application (i.e. []).

3.3 Confidentiality is sought until the relevant applicant confirms in writing to the Commission that the particular information is no longer confidential.

3.4 This request is made because the information is commercially sensitive and valuable information which is confidential to the participants, and disclosure of it would be likely to unreasonably prejudice the commercial position of the participants. Confidentiality is requested under section 100 of the Commerce Act 1986 and under section 9(2)(b) of the Official Information Act 1982.

3.5 The applicant requests that it be notified of any request made to the Commission under the Official Information Act 1982 for release of confidential information, and that the Commission seeks its views as to whether the information remains confidential and commercially sensitive, at the time a response to such a request is being considered.

4. Who are the participants (i.e. the parties involved)?

4.1 The acquirer is:

Shell New Zealand Limited
Attention: David McGuire
Head of Legal
3 Queens Wharf
PO Box 2091
WELLINGTON

Telephone: (04) 498 0355
Facsimile: (04) 498 4026
Email: david.mcquire@shell.com

4.2 The vendor is:

Mobil Oil New Zealand Limited
 Auckland Special Products Terminal
 164-188 Beaumont Street
 AUCKLAND

Attention: Sally Moon
 Telephone: (61) (3) 9270 3428
 Facsimile: (61) (3) 9270 3937
 Email: sally.f.moon@exxonmobil.com

4.3 All correspondence and notices for MONZ in respect of this application should be directed in the first instance to:

Russell McVeagh
 Vodafone on the Quay
 157 Lambton Quay
 PO Box 10-214
 WELLINGTON

Attention: Derek Johnston
 Telephone: (04) 819 7535
 Facsimile: (04) 499 9556
 Email: derek.johnston@russellmcveagh.com

5. Who is interconnected to or associated with each participant?

Acquirer group / associates

- 5.1 SNZ is part of the Royal Dutch Shell group of companies. It is ultimately owned by Royal Dutch Shell plc.
- 5.2 Royal Dutch Shell companies are involved in activities relating to oil and natural gas exploration and production, natural gas transportation and electricity generation, oil products and chemicals, and have interests in other industry segments such as renewables, hydrogen and carbon dioxide. Royal Dutch Shell companies are active in more than 130 countries.
- 5.3 Shell's aviation industry activities in New Zealand are operated by SNZ. SNZ is a subsidiary of Shell New Zealand Holding Company Limited (99.999% interest), with the remaining 0.001% interest held by Shell (Petroleum Mining) Company Limited.
- 5.4 A diagram of the Shell Group's main business activities in New Zealand is attached at confidential Annex 1.
- 5.5 For further details see www.shell.com and www.shell.com/home/contents/nz-en.

Target group / associates

- 5.6 MONZ is part of the ExxonMobil group of companies. It is ultimately owned by Exxon Mobil Corporation.
- 5.7 ExxonMobil is the world's largest publicly traded international oil and gas company. ExxonMobil companies are involved in activities relating to exploration and production,

refining and supply, lubricants and specialities, natural gas and electricity, fuels and chemicals.

- 5.8 ExxonMobil's aviation industry activities in New Zealand are owned and operated by MONZ.
- 5.9 SNZ is not aware of the detail of ExxonMobil's corporate structure and the Commission is requested to make inquiries directly of MONZ should it consider further detail is required.
- 5.10 For further details see www.mobil.co.nz, www.mobil.com and www.exxonmobil.com.

6. Does any participant, or any interconnected body corporate thereof, already have a beneficial interest in, or is it beneficially entitled to, any shares or other pecuniary interest in another participant?

- 6.1 Neither SNZ nor any of its interconnected bodies corporate has any beneficial interest in shares or other pecuniary interest in MONZ or any of its interconnected bodies corporate.
- 6.2 As far as SNZ is aware, neither MONZ nor any of its interconnected bodies corporate has any beneficial interest in shares or other pecuniary interest in SNZ or any of its interconnected bodies corporate.

7. Identify any links, formal or informal, between any participant/s including interconnected bodies corporate and other persons identified at paragraph 5 and its/their existing competitors in each market.

- 7.1 SNZ does not have any links, formal or informal, with MONZ or any other competitor in any of the markets affected by the acquisition, other than the following:
- (a) Production and transportation (Jet A1):
- (i) Shell New Zealand Holding Company Limited, MONZ, Air BP and Chevron New Zealand (**Chevron**) are shareholders in the New Zealand Refining Company Limited (**NZRC**) which, among other activities, produces Jet A1 at Marsden Point Refinery outside Whangarei;
 - (ii) SNZ, MONZ, Air BP and Chevron are shareholders in Wiri Oil Services Limited, which operates the storage terminal and distribution centre at Wiri Terminal;
 - (iii) SNZ, MONZ, Air BP and Chevron are joint owners in the pipeline from Wiri Terminal to Auckland International Airport, known as the Wiri Airport Pipeline, or "WAP". SNZ, MONZ and Air BP each hold 20%, with Chevron holding 40%;
 - (iv) SNZ, MONZ, Air BP and Chevron are equal shareholders (as to 25%) in the Joint User Hydrant Installation (**JUHI**), the fuel farm at Auckland International Airport. The JUHI is currently managed and operated by Air BP;
 - (v) SNZ and BP are joint owners (as to 50%) in one of two Joint Into-Plane Fuelling Services (**JIFS**) operating at Auckland International Airport. As the description implies, the purpose of the JIFS is to transport and pump

fuel into aircraft from the JUHI storage facility. The other JIFS is owned as to equal shares by MONZ and Chevron;

- (vi) SNZ, MONZ, Air BP and Chevron are equal shareholders in Coastal Oil Logistics Limited (**COLL**), a company specialising in petroleum product tanker scheduling. COLL uses vessels chartered from Silver Fern Shipping Limited to transport petroleum products, including Jet A1, from Marsden Point Refinery to New Zealand marine terminals;
 - (vii) at Christchurch Airport SNZ carries out into-plane fuelling and de-fuelling services for MONZ customers on behalf of MONZ when requested to do so;
- (b) Production and transportation (Avgas):
- (i) MONZ purchases Avgas from Shell's Refinery at Geelong and BP's refinery at Kwinana, Australia, for importation into New Zealand;
 - (ii) SNZ occasionally purchases Avgas from Air BP terminal storage at Mount Maunganui for distribution in the upper North Island;
 - (iii) at Wellington (Hutt City Terminal), Air BP leases one of its two Avgas terminal storage tanks from SNZ;
- (c) Borrow and loan arrangements:

In the wider petroleum industry, informal arrangements between the major players (Air BP, Shell, Mobil and Chevron) provide for the "borrowing" and loaning back of various products between the participants to facilitate the availability of products throughout the country. These "borrow and loan" arrangements are a developed industry practice. The arrangements are not documented in a formal way, other than through a national ledger of borrowed product to keep track and allow reconciliation. "Borrow and loan" arrangements cover the range of low specification and common products. The practice is becoming less used by SNZ as product differentiation increases.

Specifically in the aviation industry, there are several different variations of "borrow and loan" arrangements:

- (i) at Napier, SNZ will on occasion borrow Jet A1 from Air BP terminal storage;
- (ii) at Wellington:
 - (aa) SNZ borrows Jet A1 from Air BP terminal storage at Hutt City Terminal;
 - (bb) SNZ borrows Avgas from MONZ terminal storage at Seaview Terminal. SNZ replaces borrowed Avgas with its own product, imported from Australia. On occasion, SNZ will borrow Avgas from Air BP terminal storage at Hutt City Terminal;
- (iii) at Christchurch, MONZ borrows Avgas from Air BP and SNZ terminal storage. For Jet A1, all three parties will on occasion borrow from the others;

- (iv) at Dunedin, SNZ will on occasion borrow Jet A1 from Air BP terminal storage; and
- (v) at Bluff, Air BP and SNZ will on occasion borrow Jet A1 from MONZ terminal storage.

The acquisition has no impact on the ownership of terminal storage infrastructure and therefore no impact on these “borrow and loan” arrangements.

(d) Cross-indemnities in respect of certain joint activities

There is in the aviation industry globally a series of agreements (and exhibits) referred to collectively as "Tarbox" arrangements.

The essential purpose of Tarbox is to provide a mechanism for defining risk and responsibility and apportioning liabilities which may arise out of the process of Aircraft Refuelling principally from jointly owned and/or commingled storage and for this apportionment then to be backed up through indemnities and insurance.

“Aircraft Refuelling” in this context means the supply and delivery via joint facilities or storage of fuels, lubricants and related products, and defuelling, and related operations and services.

The main issue giving rise to the Tarbox principles was which party should be liable in the event of an incident arising out of an Aircraft Refuelling operation at an aviation storage or into-plane facility where the commingled Aviation Fuel at that facility was owned by more than one oil company and operated on behalf of all owners either by one of the oil companies or a third party.

Central to this issue were: (i) the fact that aviation fuel supplied and owned by individual oil companies for delivery to each of its customers was almost without exception commingled with that of all the other companies, thereby making identification of the source of off-specification product almost impossible; and (ii) that the Operator in essence carried out its duties for no arms length consideration or at a level of commercial rate which meant that it would be unwilling to be exposed to the potential liabilities that conducting Aircraft Refuelling operations might incur.

The underlying premise of the Tarbox solution is that liability falls on the party whose customer was being refuelled, regardless of where actual liability lay. This liability is apportioned by means of reciprocal indemnities entered into by the relevant parties.

Due to the very large potential exposure involved, each oil company requires to demonstrate financial resources to cover its Aircraft Refuelling liabilities in the sum of USD 1 billion. This can be done either through taking out insurance or through self-insurance. It is not possible to buy unlimited liability insurance in the aviation market, so a limit must be assessed according to the maximum likely exposure. If a party fails to demonstrate or is unable to continue to demonstrate such financial resources then it is or becomes disqualified from undertaking any further Aircraft Refuelling at that Airport.

Tarbox arrangements may be adopted/executed locally (i.e. by the participants in relevant countries), as circumstances at particular airports may require.

In New Zealand, Tarbox arrangements apply in respect of certain activities at some airports. Shell Aviation is a Tarbox participant and SNZ has adopted certain arrangements at the local level. SNZ can provide the Commission with more details if required.

- (e) For completeness it is noted that SNZ, MONZ and Air BP all utilise Gilbarco (NZ) Limited to carry out servicing and maintenance on their respective networks.

7.2 So far as SNZ is aware, MONZ does not have any links, formal or informal, with SNZ or any other competitor in any of the markets affected by the acquisition, other than the following:

- (a) See 7.1 (a)-(e) above;
- (b) MONZ supplies Jet A1 and Avgas to Kauriland. Kauriland manages the distribution of aviation fuels to “homebase” customers. “Homebase” customers are customers with a small facility located on private-owned land such as a farm or a private airstrip;
- (c) The Wellington (Miramar Terminal) Jet A1 terminal storage facility is jointly owned by Air BP and MONZ. This storage facility is used to supply Wellington International Airport;
- (d) MONZ may participate in other borrow and loan arrangements additional to those noted above and the Commission is requested to make inquiries directly of MONZ should it consider further detail is required;
- (e) SNZ understands that MONZ is also a Tarbox participant. The Commission is requested to make inquiries directly of MONZ should it consider further detail is required.

8. Do any directors of the ‘acquirer’ also hold directorships in any other companies which are involved in the markets in which the target company/business operates?

8.1 There are no common directorships between SNZ and MONZ, or any of their subsidiaries.

8.2 For completeness, SNZ notes that John Crossman is a director of SNZ and NZRC.

9. What are the business activities of each participant?
--

Shell

9.1 The primary activities of SNZ (and its related New Zealand companies) include:

- (a) the exploration for, and production of, oil and gas, including holding significant shareholdings in the Maui, Kapuni and Pohokura fields;
- (b) the production and distribution of chemicals, including petrochemicals and detergents;
- (c) the production and distribution of commercial products, including marine and aviation fuels, and lubricants;
- (d) the operation of Shell controlled branded petrol stations, with approximately 230 retail locations nationwide; and
- (e) equity investments in NZRC (17.1%), Wiri Oil Services Limited (27.7%), Coastal Oil Logistics Limited (25%), Fulton Hogan Limited (37.6%) and Loyalty New Zealand Limited (25%).

9.2 SNZ's aviation fuels activities in New Zealand involve:

Jet A1

- (a) the production of Jet A1 at Marsden Point Refinery and the importation of supplemental volumes into New Zealand, usually from Singapore²;
- (b) transportation to and terminal storage of Jet A1 at:
 - (i) Wiri Terminal, through Wiri Oil Services Limited (jointly with MONZ, Air BP and Chevron);
 - (ii) Auckland International Airport JUHI storage (jointly with MONZ, Air BP and Chevron); and
 - (iii) Port Lyttelton, Christchurch.

Avgas

- (c) the importation of Avgas from Shell's refinery at Geelong, Australia;
- (d) terminal storage of Avgas at Christchurch;

General Aviation

- (e) the distribution to and sale of Jet A1 and Avgas at 23 swipe card bowser locations throughout New Zealand.

9.3 SNZ operates into-plane refuelling facilities at Auckland and Christchurch International Airports and Nelson Regional Airport. However, the acquisition does not affect the international and regional airfield infrastructure which will remain the same. Only the General Aviation sector and the swipe card bowser networks are affected.

² The bulk of Jet A1 sold in New Zealand is produced here. Supplemental volumes are imported (to Christchurch) and meet the majority of demand in the South Island.

- 9.4 SNZ offers a range of aviation lubricants, including piston engine oils, turbine engine oils and hydraulic fluids.

MONZ

- 9.5 The primary downstream activities of MONZ (and its related companies) in New Zealand include:

- (a) the distribution of chemicals, including petrochemicals;
- (b) the production and/or distribution of commercial products, including marine and aviation fuels, and lubricants;
- (c) the supply to and/or operation of Mobil-branded petrol stations; and
- (d) equity investments in NZRC (19.2%), Wiri Oil Services Limited (27.7%), Coastal Oil Logistics Limited (25%).

- 9.6 MONZ's aviation fuels activities in New Zealand primarily involve:

Jet A1

- (a) the production of Jet A1 at Marsden Point Refinery and the importation of supplemental volumes into New Zealand;
- (b) transportation to and terminal storage of Jet A1 at:
 - (i) Wiri Terminal, through Wiri Oil Services Limited (jointly with SNZ, Air BP and Chevron);
 - (ii) Auckland International Airport JUHI storage (jointly with SNZ, Air BP and Chevron); and
 - (iii) Wellington (Miramar Terminal, jointly with Air BP);
 - (iv) Christchurch; and
 - (v) Bluff.

Avgas

- (c) the importation of Avgas primarily from Australia;
- (d) terminal storage of Avgas at Wellington (Seaview Terminal);

General Aviation

- (e) the distribution to and sale of Jet A1 and Avgas at 34 Aerostop locations throughout New Zealand.

- 9.7 MONZ's aviation industry activities also include into-plane refuelling facilities at Auckland, Wellington and Christchurch International Airports, Rotorua, Queenstown and Invercargill Regional Airports. As noted, that infrastructure is not impacted by the acquisition.

- 9.8 MONZ markets ExxonMobil's range of aviation lubricants in New Zealand, including Jet and Avgas aviation oils. That business is not part of the sale.

10. What are the reasons for the proposal and the intentions in respect of the acquired or merged business?

- 10.1 SNZ's swipe card bowser network and MONZ's Aerostop Network are legacy businesses from the regulated environment, when the government guaranteed the petroleum companies a post tax profit of 13% based on their assets.
- 10.2 Much of the infrastructure was put in place prior to deregulation of the petrol industry in May 1988. The assets at a number of the sites in the SNZ and MONZ networks are old, and in many cases at or around the end of their asset life. Sound risk management, internal standards, contemporary environmental considerations and new regulatory requirements require that the networks be maintained to high standards. In the aviation industry, the consequences of a failure to do so could be catastrophic. Replacement of these assets as they come up for renewal or upgrade will require major capital investment over the short to medium term.
- 10.3 Profitability has declined significantly post-deregulation. In 2007, SNZ's net income after tax profit for General Aviation was [] on turnover of [] Historic returns have been acceptable based on the depreciated value of the assets, but have not taken into account the forecast reinvestment. Profitability at these levels simply does not justify the capital investment that will be required to maintain SNZ's network. SNZ estimates the capital investment required for its existing network at around [] over [] years. With replacement costs of up to [] for a single fuel facility (Jet A1 or Avgas) and up to [] for a dual facility (both fuels), investment at []
- 10.4 SNZ believes that it and MONZ are currently both operating at sub-optimal scale. The relevant markets are dominated by Air BP, the clear market leader with around [] of Jet A1 sales by volume and around [] of the Avgas sales by volume nationally, and with 61 facilities at 41 locations nationwide. It is a much larger player than both SNZ and MONZ. Air BP's broad national coverage gives it significant scale advantages over SNZ and MONZ.
- 10.5 In the current operating environment, SNZ is not likely to expand its existing network further due to the costs of investment and the historically low returns. Major capital investment is needed just to maintain the current position. SNZ does not consider that investment to be justifiable. SNZ believes it is reasonable to assume the same is true for MONZ.
- 10.6 In such an environment, it is inevitable that one or other, or possibly both, of the smaller players might exit the market. SNZ has previously considered exiting the General Aviation sector (as MONZ is doing through this sale). MONZ appears to have made a strategic decision to exit the General Aviation sector. SNZ believes this is for the same reasons that led SNZ to consider exiting - they both lack the size, economies of scale and geographic coverage to compete effectively with Air BP.
- 10.7 [] The acquisition will provide SNZ with the size, economies of scale and geographic coverage that it lacks. SNZ regards the acquisition as a one-off opportunity to expand its existing network by acquiring MONZ's existing sites. SNZ sees the acquisition as the only effective way for it to gain the minimum efficient scale necessary for a long-term presence in the General Aviation sector. The acquisition will enable SNZ to offer product at more locations,

significantly improving its current customer offering and enabling it to compete more effectively with Air BP.

10.8 [] Expanding the SNZ network leads to synergies from the increased volumes which SNZ believes would improve its position and reduce its costs going forward. SNZ estimates the synergy savings that would result from increased volumes through the network at []

SNZ's projections are that capital expenditure of up to [] is required over [] years for reinvestment in the maintenance and replacement of assets across the combined network. There is high confidence that approval for that capex will be forthcoming if the acquisition proceeds, to the benefit of General Aviation customers in New Zealand.

10.9 However, that investment will not otherwise be made without the acquisition. []

]

PART II: IDENTIFICATION OF MARKETS AFFECTED

11. Are there any markets in which there would be an aggregation of business activities as a result of the proposed acquisition?

Please identify for each market:

- the product(s), functional level, geographic area and (where relevant) timeframe;
- the specific parties involved;
- the relationship of those parties to the acquirer or target company as the case may be.

- 11.1 As the Commission has not previously given detailed consideration to the relevant market(s) involved here, some industry background is appropriate. Market definition is considered in the following section.

INDUSTRY BACKGROUND

- 11.2 The acquisition involves MONZ's Aerostop Network of unattended Jet A1 and Avgas refuelling facilities. Those facilities supply the General Aviation sector. General Aviation is a very small part [] of the wider Aviation Fuels industry. The other sectors of the wider industry (Big Jet, Domestic/Special Carrier and Military) and MONZ's infrastructure servicing those other sectors are not affected by the acquisition.
- 11.3 To explain the assets that are affected by the acquisition, those that are not, and the relevant markets involved it is necessary to describe the wider aviation fuels industry in some greater detail.

Aviation fuels

- 11.4 The acquisition takes place in the wider aviation fuels industry.
- 11.5 There are two distinct aviation fuel products:
- (a) Jet A1 – a kerosene grade fuel suitable for most turbine engine aircraft such as 737s, 767s, helicopters and turboprop aircraft;
 - (b) Avgas – aviation gasoline, a motor spirit-based fuel that contains lead and is used in piston engine powered aircraft and some helicopters.
- 11.6 Jet A1 and Avgas are specialist aviation fuels. Jet A1 has a strict specification and cannot be substituted for other products. Similarly, Avgas has strict product specifications. The majority of piston engine aviation customers require Avgas for their aircraft because of the quality control regime that surrounds production and handling of the fuel coupled with the high octane rating which prevents engine detonation at high power settings.

Jet A1

- 11.7 Most Jet A1 in New Zealand is produced at Marsden Point Refinery outside Whangarei by NZRC. From there it is piped through the Refinery Auckland Pipeline to terminal storage at Wiri Terminal, operated by Wiri Oil Services Limited. From Wiri

Terminal Jet A1 is pumped through the Wiri Airport Pipeline to the Joint User Hydrant Installation (JUHI), the fuel farm at Auckland International Airport.

- 11.8 Refinery product is also distributed via coastal tankers to terminal storage facilities at Napier, Wellington, Christchurch, Dunedin and Bluff.
- 11.9 Terminal storage facilities are owned by:
- (a) Wiri - Air BP, MONZ, SNZ and Chevron;
 - (b) Napier - Air BP;
 - (c) Wellington: Hutt City Terminal - Air BP, Miramar Terminal - Air BP and MONZ, Seaview Terminal - MONZ;
 - (d) Christchurch - Air BP, MONZ and SNZ;
 - (e) Dunedin - Air BP; and
 - (f) Bluff - MONZ.
- 11.10 Supplementary volumes of Jet A1 are imported from either Singapore or Australia to Lyttelton Terminal at Christchurch. The ratio of locally refined product to imported product is approximately 80:20. That ratio corresponds approximately with consumption between the North and South Islands, with the vast majority of demand for Jet A1 (around 80%) coming from the North Island and satisfied by locally refined product. Imported product makes up the balance and meets virtually the entire demand in the South Island.
- 11.11 From terminal storage, Jet A1 product is transported to facilities throughout the North and South Islands by road tanker.
- 11.12 The terminal storage facility at Miramar Terminal (jointly owned by Air BP and MONZ) supplies Wellington International Airport.
- 11.13 Jet A1 from Lyttelton Port is transported by road tanker to Christchurch Airport stock tanks.
- 11.14 From terminal storage, Jet A1 is transported to facilities throughout the North and South Islands by road tanker.
- 11.15 Industry “borrow and loan” arrangements as described in paragraph 7.1(c) above facilitate the availability of product at these terminal storage facilities when needed.

Avgas

- 11.16 Most Avgas in New Zealand is produced in Australia by Shell Company of Australia at its refinery at Geelong and by BP at its refinery at Kwinana. ExxonMobil does not produce Avgas in the South Pacific region and has not done so since early 2000. It generally relies on supply from BP and Shell out of Australia.
- 11.17 Avgas is shipped to terminal storage in New Zealand at Mt Maunganui, Wellington and Christchurch.
- 11.18 Avgas terminal storage facilities are owned by:
- (a) Mount Maunganui - Air BP;

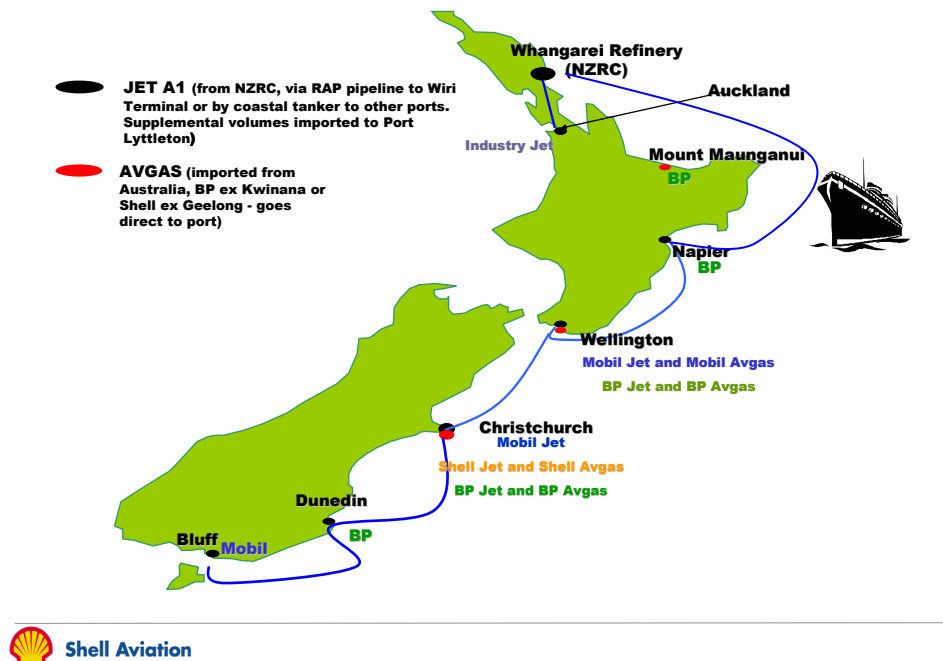
- (b) Wellington: Hutt City Terminal - Air BP, MONZ, Seaview Terminal - MONZ;
- (c) Christchurch - Air BP, SNZ.

11.19 As with Jet A1, Avgas is transported from terminal storage to facilities throughout the North and South Islands by road tanker.

11.20 Industry “borrow and loan” arrangements as described in paragraph 7.1(c) above enable SNZ and MONZ to access product from terminal storage owned by the other. Air BP, with its greater terminal storage capacity, does not need to participate in borrow and loan arrangements for Avgas.

11.21 The following diagram shows the supply chain (to terminal storage) for Jet A1 and Avgas.

Figure 1: Supply chain to terminal storage



The aviation fuels market segments

11.22 Approximately 1.4 billion litres per annum of aviation fuels are sold into four market sectors.

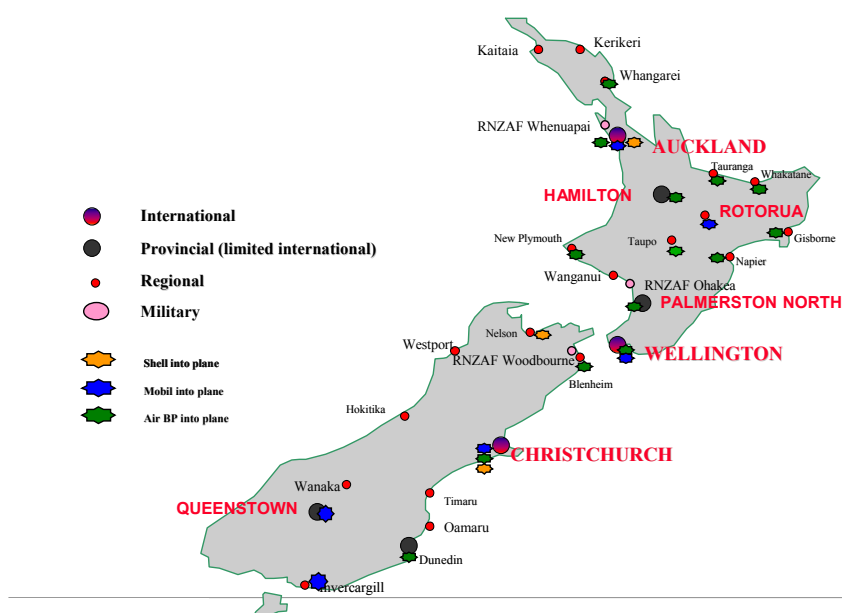
11.23 The wider aviation fuels industry comprises four market segments. They are:

- (a) “Big Jet” – wide bodied aircraft, domestic and international carriers;
- (b) “Domestic/Special Carrier” – turbine and turboprop aircraft operated by Air New Zealand Domestic, Air New Zealand Link and low cost carriers such as Pacific Blue and Jetstar;
- (c) “Military” – self explanatory and includes Royal New Zealand Air Force and Navy aircraft; and
- (d) “General Aviation” – light aircraft and helicopters engaged in a wide range of activities from recreational flying, tourism, agriculture, search and rescue, air charter and flying schools.

11.24 The infrastructure servicing the Big Jet, Domestic/Special Carrier and Military sectors is quite distinct from the swipe card bowser assets servicing the General Aviation sector. For example, at Auckland International Airport JIFS assets are used to transport and pump fuel into aircraft from the JUHI and the underground hydrant. At other airports, into-plane refuelling services are provided mainly from a tanker or from an underground hydrant, depending on the airport.

11.25 The following diagram shows the international and regional airfield infrastructure³.

Figure 2: International and regional airfield infrastructure



10

11.26 MONZ's international and regional airfield infrastructure assets and its terminal storage assets are not part of the acquisition. The airport infrastructure shown in Figure 1 will remain unchanged. The acquisition has no impact on the Big Jet, Domestic/Special Carrier and Military sectors. Also, the acquisition has no impact on the terminal storage assets in Figure 2 and the arrangements referred to above. SNZ, MONZ (and Air BP) offer a range of aviation lubricants. Again, that part of MONZ's business is not part of the acquisition.

11.27 Only the General Aviation sector is affected by this acquisition.

11.28 Jet A1 is sold into all four sectors of the Aviation Fuels industry. Avgas is only sold into the General Aviation sector. Both markets are mature. Demand for Jet A1 is steady. Demand for Avgas is declining at an average rate of around [] per annum as more turbine aircraft are being replaced and piston engine planes are being converted to Jet A1 or replaced by aircraft that use Jet A1.

General Aviation

11.29 The General Aviation sector is approximately 60 million litres annually, 40 million litres for Jet A1 and around 20 million litres for Avgas annually.

³ Military sector customers use the international and regional airfields. There are also three operational airbases at Woodbourne, Ohakea and Whenuapai. The three operational airbases are serviced by Air BP.

- 11.30 “General Aviation” refers to light aircraft and helicopters engaged in a wide range of activities from recreational flying, tourism, agriculture, search and rescue, air charter and flying schools.
- 11.31 The General Aviation sector is serviced by Air BP, MONZ and SNZ. Each of them operates a network of unattended Jet A1 and Avgas refuelling facilities.⁴ The facilities consist of a storage tank or tanks and a swipe card bowser. A swipe card bowser is a fuel pump which customers can activate using a customer swipe card issued by the relevant operator to purchase Jet A1 or Avgas for aircraft refuelling.
- 11.32 SNZ’s facilities at Motueka provide a good example.

SNZ Motueka – Jet A1 facility



SNZ Motueka – Avgas facility



Industry history

- 11.33 A substantial part of the General Aviation infrastructure is the legacy of the regulated petroleum industry environment in New Zealand prior to May 1988. Prior to deregulation, the New Zealand government guaranteed industry players a post-tax profit of 13% based on their assets. At that time the government also controlled the price of petrol, diesel and aviation fuels. That situation led to a proliferation of assets at the retail level. General Aviation infrastructure was no exception.
- 11.34 Following deregulation, industry players were forced to evaluate investments in New Zealand on a purely commercial basis and investment criteria were set. The new commercial reality naturally led to a process of rationalisation as assets came up for renewal. The objective was greater volume through fewer facilities. That trend was particularly pronounced for the retail and commercial networks, but also affected the aviation networks.
- 11.35 From the early 1990’s, SNZ decided to rationalise its General Aviation facilities as assets came up for renewal. All investments were considered against Shell Aviation Group investment criteria. For New Zealand, the investment hurdle is [

] For Australia the same investment hurdle is set at [] Only limited investment was made in expanding SNZ’s General Aviation network over this period.

⁴ MONZ also supplies Jet A1 and Avgas to Kauriland for distribution to homebase customers. At one of these sites, Piriaka, Kauriland has installed a swipe card bowser.

- 11.36 Air BP, in contrast, continued reinvestment and expansion of its General Aviation network at a significant rate.
- 11.37 SNZ lost market share to Air BP. SNZ also found that its fixed cost unit rates and transport costs began to escalate. SNZ believes MONZ will have been in a similar position.

The need to replace ageing assets

- 11.38 The assets at many General Aviation sites in SNZ's network are old, in some cases at or around the end of their asset life. Storage tanks have an asset life of up to approximately 30 years. In the time since the assets were first installed, environmental considerations have gained in prominence. Sustainability and minimising environmental impacts have become key considerations for many businesses. New regulatory requirements impose new obligations on the industry players and higher internal standards have been introduced.
- 11.39 In November 2006, the Environmental Risk Management Authority (**ERMA**) developed and approved a Code of Practice for the Management of Existing Stationary Container Systems up to 60,000 Litres Capacity (the **Code**) pursuant to the Hazardous Substances and New Organisms Act 1996.
- 11.40 The Code provides standards against which test certificates for stationary tanks can be issued. All underground stationary tanks must be designed, constructed and installed in accordance with the Code. Underground stationary tanks installed in Zone A (highly sensitive areas) must have a secondary containment system with the space between the stationary tank and the secondary containment periodically monitored.
- 11.41 For existing underground tanks which do not have secondary containment, operators were required to submit a compliance plan endorsed by a test certifier to ERMA by 31 March 2008. The compliance plan was to detail how those tanks will be made compliant with the Code and the timeframe within which they will be made compliant. The compliance costs associated with the exercise will obviously be considerable. It is thought likely that regulatory requirements will continue to become even more stringent in the future due to environmental concerns and therefore that regulatory costs will continue to increase.
- 11.42 SNZ operates under Shell Aviation group compliance standards. Under this system, called the Global Environmental Management System (**GEMS**), SNZ is required to have in place a programme for cathodic protection for all underground tanks by the end of [], at an estimated cost of around [].
- 11.43 These regulatory and internal compliance standards, and environmental considerations, create real impetus to upgrade facilities from old underground storage tanks to new, fully protected, accessible sites that are much easier to maintain. To illustrate, SNZ would envisage upgrading the MONZ facility at Stratford (see photo below) to a facility similar to that in operation at Motueka (see photo of SNZ's Jet A1 facility at Motueka in paragraph 11.32 above).

MONZ Stratford - Jet A1 facility



11.44 The replacement costs for such an upgrade are considerable, especially relative to revenue at individual sites. The costs of a new single fuel facility (Jet A1 or Avgas) can be up to [] and up to [] for a dual facility (both fuels).

11.45 Replacement of these assets across the network will require significant capital investment over the medium term. SNZ's projections are that:

- (a) [] will be required for the GEMS cathodic protection programme in [];
- (b) [] investment is required at [] sites over the next [] years;
- (c) a further [] investment is required at [] sites over the following [] years;
- (d) in total, over [] investment is required across its existing network over the next [] years.

Low profitability

11.46 Volumes in General Aviation are low compared to other segments of the Aviation Fuels market, Big Jet and Domestic/Special Carrier in particular, and to petrol volumes at retail service station outlets. As noted, General Aviation volumes are less than [] of the wider Aviation Fuels market. Moreover, a large General Aviation site (e.g. []) would have volumes of approximately [] litres per annum. In contrast, a large retail service station (e.g. []) would have volumes of approximately [] litres per annum. The largest General Aviation location in New Zealand is [] airport, with volumes of around [] litres per annum (Jet A1 and Avgas). Most General Aviation sites are much smaller than this. Total annual volumes in General Aviation are approximately equal to the volumes through [] large retail service stations.

11.47 Profitability from General Aviation has been limited. SNZ's net income after tax profit from General Aviation for 2007 was [] on turnover of []

Historic returns have been acceptable based on the depreciated value of the assets, but have not taken into account forecast reinvestment. Figures for the last three years were as follows:

Year	Turnover	NIAT
2007	[]	[]
2006	[]	[]
2005	[]	[]

11.48 There are, in this current environment of significant costs and historically low returns, limited incentives for re-investment in existing sites, let alone expansion of SNZ's General Aviation network.

11.49 Unsurprisingly, SNZ has considered exiting the General Aviation sector.

SNZ has considered exiting General Aviation

11.50 In February 2004, SNZ conducted a strategic review of its General Aviation and Domestic/Special Carrier business. The outcome of that review was to identify an exit strategy. Consideration was also given at the time to approaching MONZ to acquire its Aerostop Network, but that strategy was dismissed because it was assumed that the acquisition cost would be too high.

11.51 In December 2005, MONZ approached SNZ with an offer to sell most of its Aerostop Network to SNZ.

11.52 SNZ considers that it is currently operating at sub-optimum scale. SNZ is not likely to expand its network further in the current operating environment due to the costs of investment and the historically low returns. SNZ is looking at significant capital investment even to maintain the current position. That investment is not considered justifiable under current market conditions. SNZ believes it is reasonable to assume the same is true for MONZ.

11.53 The situation in New Zealand is reflective of the situation internationally:

- (a) Air BP has publicly announced its withdrawal from 22 countries, the most recent ones announced being Canada, Spain, Portugal and Tuvalu (Pacific Islands);
- (b) In April 2008, ExxonMobil announced its withdrawal from Brazil with the sale of 100% of its interests in Esso Brasileira de Petroleo Ltda (including aviation fuels) to Cosan S.A. Industria e Comercio;⁵
- (c) In late 2006, Shell Aviation announced its withdrawal from the South West Pacific.

11.54 It is against this background that the relevant counterfactual scenario(s) should be considered.

FACTUAL AND COUNTERFACTUAL SCENARIOS

The factual

11.55 In the factual, SNZ would acquire MONZ's Aerostop Network assets. These would be integrated into SNZ's swipe card bowser network.

⁵ Cosan's press release of 24 April 2008 was at www.cosan.com.br. See also www.marketwatch.com/news/story/cosan-ltd-buys-exxon-mobil

11.56 The proposal:

- (a) generates economies of scale from increased volumes across the combined network, resulting in lower unit costs and synergy savings which SNZ estimates at []
- (b) enhances SNZ's presence in the Jet A1 markets;
- (c) assists the business case for maintaining SNZ's presence in General Aviation in New Zealand, in particular enabling SNZ to conduct future investment in its network;
- (d) would see SNZ become a stronger number two competitor through an enhanced network and increased economies of scale, better able to compete against Air BP (by far the largest player, with network and cost advantages).

11.57 SNZ's projections are that capital expenditure of up to [] is required over [] years for reinvestment in the maintenance and replacement of assets across the combined network. There is high confidence that approval for that capital investment will be forthcoming if the acquisition proceeds. That capital investment will not be made under any of the relevant counterfactual scenario(s).

The counterfactual scenario(s)

11.58 SNZ has considered the possible counterfactual scenarios. They are:

- (a) a continuation of the status quo;
- (b) a sale of the MONZ network to an alternative purchaser; and
- (c) MONZ's exit from the market.

11.59 SNZ believes that the status quo is not sustainable and will not continue.

11.60 It appears that MONZ has made a strategic decision to exit the General Aviation sector. If clearance is declined and a sale to SNZ cannot proceed, SNZ considers that MONZ would look to sell its Aerostop assets to another purchaser. SNZ considers that the reason for this is self-evident – SNZ believes that, like itself, MONZ has sub-optimal scale and faces significant network upgrade costs which are not justifiable based on expected returns.

11.61 The nature of the assets and the risks inherent in the business mean that they are only likely to be of interest to petroleum industry players. SNZ believes none would be interested, given the risks, the limited rewards and the significant capital investment that would be required for an ongoing presence in General Aviation.

11.62 The only conceivable purchaser is Kauriland, which has a peripheral involvement in aviation fuels through its operation of "homebase" supplies. For the reasons explained below, SNZ considers an acquisition by Kauriland to be unlikely and that the appropriate counterfactual against which the proposal should be considered is MONZ's exit from the General Aviation sector.

11.63 Even though SNZ does not regard an acquisition by Kauriland as a likely counterfactual scenario, it has assessed how that scenario would be likely to play out. In short, SNZ believes that the market dynamics would, in this scenario, change quite

radically from what they are now, to the detriment of competition in the General Aviation sector.

11.64 The implications under each of the possible counterfactual scenarios are considered in more detail in the following section, but in summary:

- (a) the proposal offers synergies and a stronger number two competitor;
- (b) the proposal would see reinvestment in the improvement of the combined (SNZ and MONZ) network;
- (c) all of the counterfactual scenarios lead to worse outcomes than under the proposal because:
 - (i) Air BP's market power would be enhanced. If clearance is declined, Air BP might look to "cherry pick" by acquiring facilities at locations where it is not currently present or look to expand aggressively and would in any event benefit from additional volumes at sites where it is already present;
 - (ii) [] The reinvestment that SNZ has earmarked for the combined network under the proposal would not be made;
 - (iii) under a "Kauriland alternative purchaser" counterfactual scenario, the number three player would be likely to decline and might ultimately be forced to exit;
 - (iv) sites would close under the counterfactual that would remain open under the factual i.e. under the counterfactual there would be harm outside the areas of overlap.

The status quo is unsustainable and will not continue

11.65 SNZ considers that the status quo in the General Aviation sector is not sustainable and will not continue:

- (a) MONZ appears to have made a strategic decision to exit the General Aviation sector and, if it cannot sell to SNZ or another party, would likely close down its Aerostop Network;
- (b) SNZ does not regard its current position as sustainable. If the sale cannot proceed, SNZ would reassess its presence in the General Aviation sector. The need for approval for capital investment in its GEMS (cathodic protection) compliance programme would likely force a determination as to whether SNZ would remain in General Aviation in New Zealand. [

]

11.66 Put simply, the rewards for SNZ (returns) do not justify the risks and capital investment need for an ongoing presence in General Aviation. As described above, major capital investment is required for maintenance and the replacement of assets across SNZ's swipe card bowser network. Profitability from General Aviation has been limited historically and simply does not sustain the capital investment required.

11.67 [] SNZ believes that the most likely result, if clearance is declined and the proposal cannot proceed, is a decision that no further capital investment will be made in the General Aviation sector in New Zealand. []

[] On a site-by-site basis, the investment required to upgrade one site (around [] (for a single fuel, up to [] for a dual facility)) means that investment in []

[] SNZ estimates that margins would need to increase by [] for that investment to otherwise be made, which would mean significant price increases for General Aviation customers, estimated by SNZ to be in the region of [] per litre (excluding GST).

11.68 SNZ therefore believes that if the acquisition cannot proceed further capital investment in New Zealand is unlikely to be approved. []

]

11.69 []

]

Sale of MONZ's Aerostop Network assets to an alternative purchaser (Kauriland)

11.70 SNZ's view is that there would be few interested purchasers given the nature of the assets. In fact, SNZ's view is that there are no alternative purchasers who could be regarded as "likely" to acquire MONZ's assets.

11.71 Kauriland might be considered a possible option as Kauriland has previously acquired some assets from MONZ.⁶ However, SNZ does not regard Kauriland as a likely purchaser, for a number of reasons:

- (a) Kauriland is not a major oil industry player. It would be getting into a business where the risks are high, the returns historically low and substantial capital investment will be required over the medium term;
- (b) SNZ doubts Kauriland could offer MONZ the "clean break" in respect of environmental liabilities, which was a key factor for MONZ in the negotiations with SNZ;
- (c) Kauriland would face supply chain vulnerability, particularly for Avgas. It would need a Supply and Technical Services Agreement with an oil industry company and would therefore be at a cost disadvantage to an integrated producer, as MONZ is currently;
- (d) Kauriland would face compliance, maintenance, replacement and quality control costs in the knowledge that a major incident (involving closing tanks and/or recalling product) could cause serious financial hardship to their business;
- (e) although Kauriland has previously acquired some assets from MONZ, those were assets associated with MONZ's "homebase" customers.⁷ "Homebase"

⁶ See 11.71(e) below.

customers are customers with a smaller facility (a storage tank of up to 15,000 litres) located on privately-owned land such as a farm or a private airstrip. Typically homebase sites are used by a single customer, who has a vested interest in keeping the assets maintained. In contrast, Aerostop sites are unattended swipe card bowzers at sometimes remote locations. They are larger facilities (at least twice the size), used by multiple customers and must be maintained by the supplier as the ramifications of a failure to do so are very significant.⁸

11.72 The MONZ Aerostop Network assets would be an entirely different proposition for Kauriland to the ‘homebase assets’ previously acquired, and have a significantly increased risk profile associated with them. SNZ believes that Kauriland is unlikely to be interested.

11.73 Even if Kauriland was interested (and able to negotiate a deal with MONZ), Kauriland would face the same capital investment issues and profitability concerns that SNZ believes MONZ faces currently (because SNZ faces the same issues and concerns), but it would not derive the network benefits and efficiencies that SNZ would in an acquisition of the same assets. SNZ estimates the capital investment required for the replacement of assets in MONZ’s existing network at over [] over [] years.

11.74 SNZ considers that concerns over profitability, required capital investment, a desire to reduce potential liabilities, supply chain vulnerability and potentially lower margins would lead to Kauriland:

- (a) rationalising the former MONZ network by immediately closing low contribution sites; and
- (b) focusing efforts on Jet A1, converting some Avgas locations to Jet A1 and ultimately exiting from the supply of Avgas, most likely over a two to three year period.

11.75 This scenario would see:

- (a) Air BP maintaining its market leadership;
- (a) Kauriland consolidating to a considerably smaller model supplying Jet A1 only; and
- (b) SNZ making no further capital investment and closing sites as the assets come up for replacement.

11.76 The party most likely to benefit in this scenario would be Air BP. Where it has a presence at a location and SNZ or Kauriland shut down their facility, Air BP would capture the incremental volume without needing to do anything. At other sites (where Air BP does not currently have a presence), the exit of one or other of SNZ or Kauriland could present an opportunity for Air BP, either to acquire the facility being closed down or to enter with a new facility (e.g. to enter with an Avgas facility where Kauriland has closed down). SNZ believes Air BP would examine other possibilities to expand by putting in a dual facility where it was already entering with Avgas. That could lead to Air BP putting still further pressure on Kauriland.

⁷ SNZ understands that Kauriland has converted one “homebase” site, at Piriaka, to a swipe card bowzer.

⁸ The risks range from environmental liabilities for leaking tanks, compensation claims for poorly maintained concrete pads which could cause damage to aircraft, quality control issues in respect of product, product recalls or, worst case, a crash due to engine failure.

11.77 SNZ believes this scenario would lead to a downward spiral, with Air BP continuing to increase its market share and Kauriland getting smaller. [

]

11.78 [

] Air BP would end up with unilateral market power as SNZ and Kauriland exerted an increasingly small competitive constraint.

MONZ's exit – the most likely outcome

11.79 This is, in SNZ's view, the most likely of the counterfactual scenarios identified.

11.80 It appears that MONZ has made a strategic decision to exit the General Aviation sector in New Zealand. If it cannot sell its Aerostop Network assets to SNZ, then no doubt it would try to realise some value by selling those assets to another player.

11.81 For the reasons noted above, SNZ seriously doubts that there is an alternative purchaser for these assets, in which case MONZ would be left with no option but to shut down its existing sites and exit the market.

11.82 That scenario would be three to two in any event, but also a worse outcome than under the proposal as the market would lose the network benefits from the sale to SNZ. Two players would remain, but SNZ would miss out of the synergies from the proposal and Air BP might look to "cherry pick" by acquiring facilities at locations where it does not currently have a presence. [

]

11.83 [

]

Factual versus counterfactual

11.84 All the counterfactual scenarios identified would lead to worse outcomes than the proposal as the synergies that would result from the proposal would be lost and SNZ would not make further investment in General Aviation in New Zealand.

11.85 Were Kauriland to acquire the MONZ assets, it would be in a similar situation to SNZ and MONZ currently. Rationalisation/consolidation is virtually certain, and Kauriland might consider exiting Avgas. Either counterfactual leads to harm outside the areas of overlap in the proposal through:

(a) [];

(b) closure of Kauriland sites and/or conversion of Avgas locations to Jet A1; or

(c) a shutdown of the MONZ Aerostop Network.

11.86 Compared against any of the counterfactual scenarios, the proposal is pro-competitive.

MARKET DEFINITION

11.87 The Commission has not previously given detailed consideration to the definition of the relevant market(s) in this industry. In Decision 434, *Caltex New Zealand/Challenge Petroleum*⁹, the Commission noted that crude oil can be refined to produce a range of petroleum products, including gasoline, diesel, jet fuel, fuel oils, bitumen and sulphur. However, it did not give closer consideration to market definition in respect of “jet fuel” in that case as aggregation only took place in the gasoline and diesel product markets.¹⁰

11.88 The applicant is not aware of any overseas decisions on point.

Product dimension

11.89 Jet A1 and Avgas are specialist aviation fuels. They are not substitutes for each other on the demand side, nor can they be substituted by other products. As they obviously cannot be mixed together, they are required to be transported and stored separately. The infrastructure and assets for Jet A1 are therefore distinct from those for Avgas. For present purposes the applicant has treated them as separate product markets.

Functional level

11.90 Shell Group companies, Mobil Group companies and BP Group companies are engaged in the:

(a) production and importation; and

(b) distribution and sale,

of Jet A1.

11.91 In respect of Avgas:

(a) Shell Group companies and BP Group companies are engaged in the production of Avgas; and

(b) SNZ, MONZ and Air BP are engaged in the:

(i) importation; and

(ii) distribution and sale,

of Avgas.

11.92 The applicant considers the relevant functional markets to be the production and/or importation and supply of Jet A1 and Avgas.

⁹ Decision No. 434, *Caltex New Zealand Limited/Challenge Petroleum Limited*, 28 June 2001. The reference to “jet fuel” in this decision must be taken as a reference to Jet A1 as neither of the merging parties was involved in the supply of Avgas.

¹⁰ Ibid at paragraph 74.

Geographic area

- 11.93 Local airfields (at which General Aviation sites are located) are unlikely to be substitutable for each other on the demand-side. Typically, a pilot would wish to take on fuel prior to take-off. Operators based at a particular location (e.g. a tourist operator) will take fuel at the location where they are based. En route, the pilot may have a choice of locations at which to land and re-fuel, depending upon a range of factors including the flight plan, the weather, load (including cargo and passengers), altitude and fuel capacity. This permits some degree of choice between airfield and re-fuelling locations. The nature of the activity means that a large number of customers fly out of more than one location. In general, however, customers based at a particular airfield will take at least initial fuel there and would be unlikely to view other airfields as immediately substitutable.¹¹
- 11.94 On the supply side, there are three suppliers servicing the General Aviation sector. They operate national networks and view this as a network business.
- 11.95 In terms of geographic scope, there is on the demand-side some limited scope for substitutability between airfields. On the supply-side, the network nature of the business supports defining the geographic market as national.
- 11.96 On balance, and to assist the Commission's analysis, the applicant has defined the relevant geographic from the demand-side, with the geographic markets being local.

Customer dimension

- 11.97 There are four distinct market sectors: Big Jet, Domestic/Special Carrier, Military and General Aviation. The customers in each sector have different requirements.
- 11.98 Big Jet and Domestic/Special Carrier customers require high volumes of Jet A1 and into-plane service at the international and regional airfields. The customers are the major international and domestic airlines. Military customers also have significant volume requirements for Jet A1. They use predominantly the same infrastructure as well as that at their operational bases at Woodbourne, Ohakea and Whenuapai, which are serviced by Air BP.
- 11.99 General Aviation customers have smaller volume requirements for Jet A1 and a number require Avgas.
- 11.100 On the supply-side, some substitutability is possible for Jet A1, in that some General Aviation customers would have the option of an into-plane service for Jet A1 from Domestic/Special Carrier infrastructure at regional airfields. Avgas customers mainly use the swipe card bowser networks, although MONZ offers an into-plane Avgas service at Queenstown airport (not part of the sale). Air BP offers into-plane Avgas services at Auckland, Wellington and Christchurch International Airports. SNZ offers an into-plane Avgas service at Auckland International Airport.
- 11.101 Differences in customer requirements and the infrastructure required to service customers in the Big Jet, Domestic/Special Carrier and Military sectors, as distinct from those in the General Aviation sector, point to a separate market for General Aviation customers.
- 11.102 Different customer requirements and infrastructure also point to a separate market for supplies to "homebase" customers (currently supplied MONZ fuel by Kauriland).

¹¹ For completeness, SNZ notes that a number of helicopter operators working in remote locations away from an airfield will use a fuel trailer (1,300-1,500 litre capacity) or a fuel tanker (up to 13,000 litre capacity) to ensure they have fuel close to their operating zone.

Conclusion on market definition

11.103 As noted, there are three suppliers nationally and each operates the business as a national network. The acquisition might therefore be seen as a 3 to 2 merger at the national level.

11.104 However, for the reasons noted above, the applicant has taken a narrower, demand-side approach to market definition. For the purposes of analysis, it has defined local markets (defined by the relevant airfield) for the supply of:

- (a) Jet A1; and
- (b) Avgas,

to General Aviation customers (and excluding supplies to “homebase” customers).

11.105 On that basis, there are 48 local markets for Jet A1 throughout New Zealand and 61 local markets for Avgas. The number of suppliers in each market ranges from three to one.

11.106 The acquisition would result in the integration of MONZ’s Aerostop Network into SNZ’s swipe card bowser network.

11.107 Shell’s swipe card bowser network comprises 32 facilities at 23 locations throughout New Zealand:

Ardmore	Jet A1	Avgas
Bridge Pa	Jet A1	Avgas
Fielding		Avgas
Foxton		Avgas
Gisborne		Avgas
Hokitika	Jet A1	
Motueka	Jet A1	Avgas
Napier	Jet A1	
Nelson	Jet A1	Avgas
Oamaru		Avgas
Palmerston North		Avgas
Paraparaumu	Jet A1	Avgas
Rangiora		Avgas
Taupo	Jet A1	Avgas
Tauranga		Avgas
Tekapo	Jet A1	Avgas
Timaru	Jet A1	Avgas
Wairoa	Jet A1	
Wanaka		Avgas
Wellington West Apron		Avgas
Whakatane	Jet A1	Avgas
Whitianga		Avgas
Wigram		Avgas

11.108 MONZ’s Aerostop Network comprises 48 facilities at 34 locations throughout New Zealand:

Albany	Jet A1	
Alexandra	Jet A1	Avgas
Ardmore	Jet A1	Avgas x 2

Ardmore Flying School		Avgas
Dargaville		Avgas
Dunedin (Momona)		Avgas
Franz Joseph	Jet A1	Avgas
Gisborne	Jet A1	
Greymouth	Jet A1	Avgas
Haast		Avgas
Hamilton	Jet A1	
Invercargill		Avgas
Kaitaia		Avgas
Kerikeri	Jet A1	Avgas
Mechanics Bay	Jet A1	
New Plymouth	Jet A1 x 2	
Omarama		Avgas
Opotiki		Avgas
Palmerston North	Jet A1	
Paraparaumu	Jet A1	
Rotorua		Avgas
Rotorua Hospital	Jet A1	
Stratford	Jet A1	Avgas
Taieri		Avgas
Taihape	Jet A1	Avgas
Taumarunui	Jet A1	Avgas
Taupo	Jet A1	Avgas
Te Anau		Avgas
Te Kuiti	Jet A1	Avgas
Thames	Jet A1	Avgas
Wairarapa		Avgas
Wanganui	Jet A1	Avgas
Wellington	Jet A1	
Whakatane	Jet A1	

Aggregation

11.109 There is limited aggregation on a site-by-site basis as there are only seven locations in the North Island where SNZ and MONZ are both present. Those locations are:

- (a) Ardmore;
- (b) Gisborne;
- (c) Palmerston North;
- (d) Paraparaumu;
- (e) Taupo;
- (f) Wellington; and
- (g) Whakatane.

11.110 There is no overlap at the other 27 locations to be acquired from MONZ as SNZ does not have a presence there.

11.111 The seven locations affected by the acquisition are considered in further detail in Section 16 below. When the separate markets for Jet A1 and Avgas at each site are considered individually, the level of concentration that would result from the acquisition is shown to be very low.

Differentiated product markets

12. Please indicate whether the products in each market identified in question 11 are standardised (buyers make their purchases largely on the basis of price) or differentiated (buyers make their purchases largely on the basis of product characteristics as well as price).

12.1 Jet A1 and Avgas, while distinct from each other, are generally undifferentiated.

12.2 The principal points on which the suppliers differentiate themselves are noted in 13.1 below.

12.3 General Aviation customers make their purchases largely on the basis of the location at which they wish to refuel. Many, if not most, customers are customers of all three suppliers and will hold a swipe card for each. Volume discounts, offered by the suppliers, and value adds such as Fly Buys (SNZ) may influence the purchasing decisions where a customer flies to/from a number of locations throughout New Zealand.

13. For differentiated product markets:

- Please indicate the principal characteristics of products that cause them to be differentiated one from another.
- To what extent does product differentiation lead firms to tailor and market their products to particular buyer groups or market niches?
- Of the various products in the market, which are close substitutes for the products of the proposed combined entity? – which are more distant substitutes?
- Given the level of product differentiation, to what extent do you consider that the merged entity would be constrained in its actions by the presence of other suppliers in the market(s) affected?

13.1 The principal points on which the suppliers differentiate themselves are:

- (a) geographic coverage – presence at a number of locations;
- (b) service, equipment reliability, servicing and frequency of supply and ease of use (e.g. having a convenient location at an airfield, with easy access from two sides. At some sites a player may be disadvantaged by being located up against a fence, a shed or some other structure, in which case access is limited to one side); and
- (c) price.

13.2 SNZ offers customers Fly Buys points for aviation fuel purchases. This is the only available award scheme for aviation fuels. SNZ understands that Air BP accepts

payment by credit card, which may offer opportunities to accumulate loyalty points under schemes operated by the credit card issuers.

- 13.3 Fly Buys has proved attractive and a point of difference for SNZ. SNZ has acquired [] new accounts since Fly Buys was introduced in February 2002.

Vertical integration

14. Will the proposal result in vertical integration between firms involved at different functional levels?

14.1 The acquisition will not result in vertical integration.

14.2 For completeness it is noted that:

- (a) SNZ and Air BP are already vertically integrated into the production and importation, and the distribution and sale of Jet A1 and Avgas;
- (b) MONZ is vertically integrated into the production and distribution of Jet A1. That position, insofar as it relates to MONZ's international and regional airfield infrastructure, will remain unchanged. In respect of Avgas, ExxonMobil does not produce Avgas in the South Pacific region and has not done so since early 2000. MONZ purchases the majority of its Avgas requirements from Shell Group companies and BP Group companies out of Australia.

15. In respect of each market identified in questions 11 and/or 14 identify briefly:

- all proposed acquisitions of assets of a business or shares involving either participant (or any interconnected body corporate thereof) notified to the Commission in the last three years and, in each case:
 - the outcome of the notification (e.g. cleared, authorised, declined, withdrawn)
 - whether the proposed acquisition has occurred.
- any other acquisition of assets of a business or shares which either participant (or any interconnected body corporate) has undertaken in the last three years.

15.1 The only relevant acquisitions involving either participant in the last three years are that in 2006 SNZ, MONZ and Air BP each acquired a portion of the shares in the JUHI at Auckland International Airport from Chevron. Clearance was not sought in relation to those acquisitions.

PARTS III, IV AND V: CONSTRAINTS ON MARKET POWER BY EXISTING AND POTENTIAL COMPETITION AND OTHER POTENTIAL CONSTRAINTS

16. Existing competitors

16.1 This applicant treats the relevant markets to be local markets for the supply of:

- (a) Jet A1; and
- (b) Avgas,

to General Aviation customers (and excluding supplies to “homebase” customers).

16.2 In total there are 65 locations throughout New Zealand at which either or both Jet A1 and Avgas are offered. Specifically, at these locations:

- (a) Jet A1 is offered at 48 sites;
- (b) Avgas is offered at 61 sites.

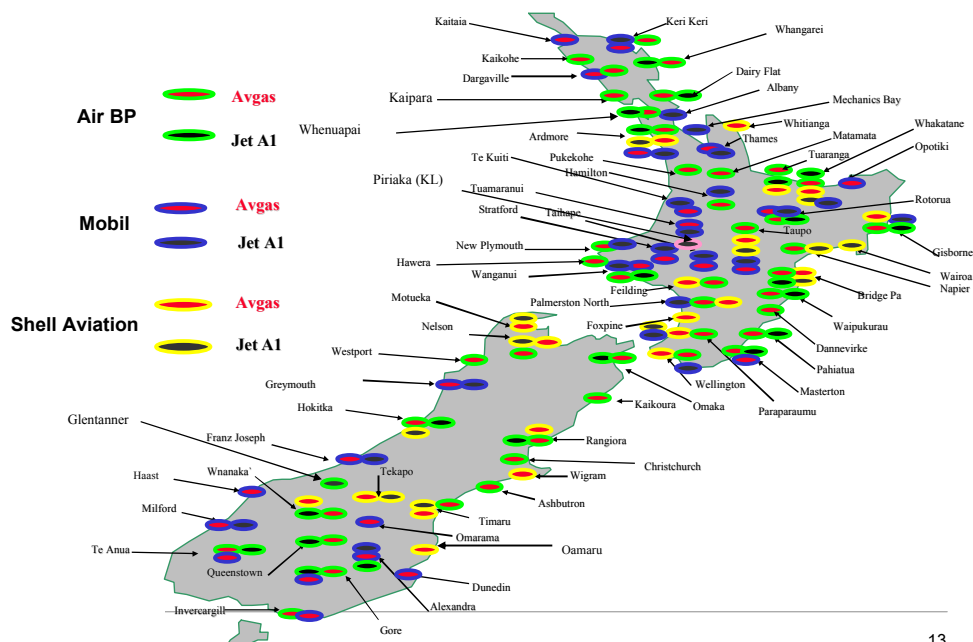
16.3 On the market definition which the applicant has adopted, there are 48 local markets for Jet A1 and 61 local markets for Avgas throughout New Zealand, with the number of suppliers in each market ranging from three to one.

16.4 At the national level, there are three suppliers, each of which operates its General Aviation business as a national network.

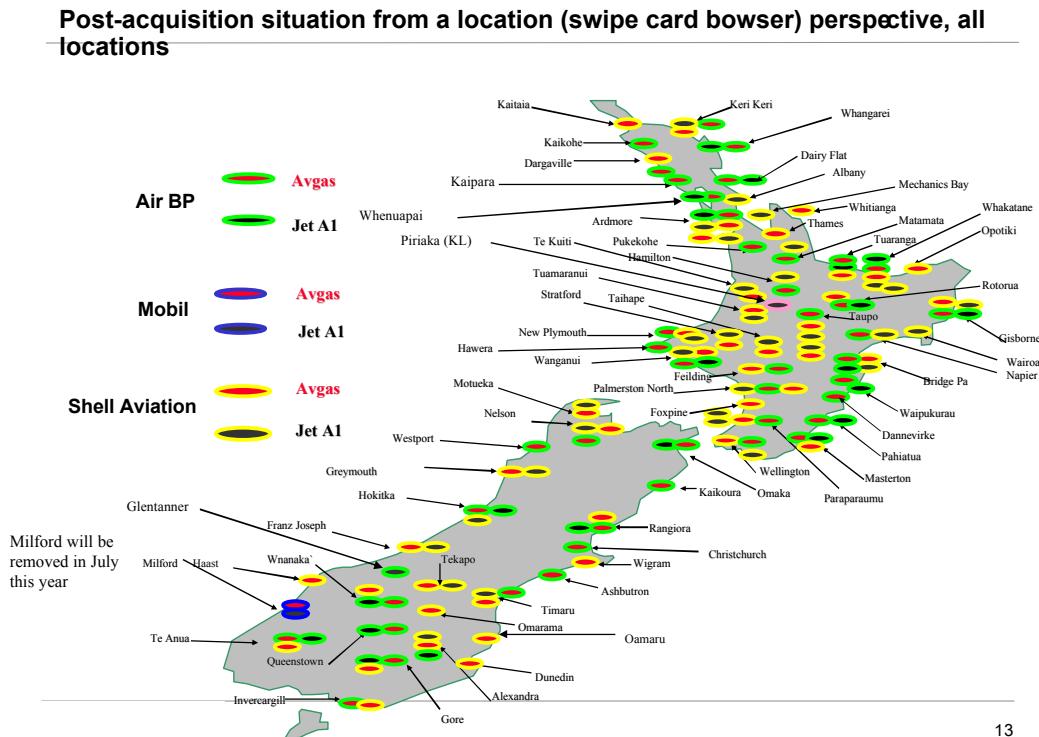
16.5 A spreadsheet of all locations throughout New Zealand is attached at Annex 2. This shows which player or players are present at each location for each of Jet A1 and Avgas.

16.6 The following diagram shows the current locations of the players’ respective facilities.

Current situation from a location (swipe card bowser) perspective, all locations



16.7 The following diagram shows the position post-acquisition.



13

16.8 As can be seen, there is only limited aggregation on a site-by-site basis as a result of the acquisition. There are only seven locations in the North Island where SNZ and MONZ are both present. Those locations are:

- Ardmore;
- Gisborne;
- Palmerston North;
- Paraparaumu;
- Taupo;
- Wellington; and
- Whakatane.

16.9 There is no net change at the other 27 locations to be acquired as SNZ does not have a presence there.

16.10 Insofar as those seven locations are concerned, and examining the position in respect of the Jet A1 and Avgas markets individually, the level of concentration is even lower. This is because SNZ and MONZ do not presently offer both products at all sites.

16.11 The following table summarizes the concentration that would result in the local markets for Jet A1 and Avgas.

Table 1: concentration levels in the affected markets (Jet A1 and Avgas)

Location	Concentration – number of suppliers	
	Jet A1	Avgas
Ardmore	3-2	3-2
Gisborne	No change	No change
Palmerston North	No change	No change
Paraparaumu	2-1	No change
Taupo	2-1	3-2
Wellington	No change	No change
Whakatane	3-2	No change

16.12 As can be seen from the above:

- (a) there is no change to the number of suppliers in the markets for either fuel at Gisborne, Palmerston North and Wellington. The acquisition is complementary at those sites as, pre-acquisition, SNZ currently offers Avgas but not Jet A1 while MONZ offers Jet A1 but not Avgas. Post-acquisition SNZ would offer both fuels, but there is no reduction in the number of existing suppliers for either fuel at those locations;
- (b) the same applies in respect of Avgas at Paraparaumu and Whakatane. While SNZ currently offers both products, MONZ offers Jet A1 but not Avgas. The acquisition therefore does not reduce the number of existing suppliers in the market for Avgas at either location.

16.13 The table above compares the proposal against the status quo. As explained, the status quo is not sustainable. When the proposal is compared against even the most favourable counterfactual (with Kauriland acquiring the MONZ's Aerostop Network assets and SNZ remaining in the market (but declining)), it can be shown that there is only one local market where there would be a reduction in the number of players as a result of the merger, namely Whakatane (Jet A1).

Ardmore

16.14 At Ardmore Airport, MONZ currently operates two Avgas facilities and one Jet A1 facility. The larger of the two Avgas facilities services Ardmore Flying School, with current volumes of around 600,000 litres per annum. MONZ's other Avgas bowser and its Jet A1 bowser are situated at the other end of the airfield, some 600 to 700 metres away, and have considerably lower annual volumes, of 46,000 and 74,000 litres per annum respectively. All three sites are old and due for replacement.

16.15 In SNZ's view, the volume at the two smaller sites would not justify their replacement costs and, if Kauriland were to acquire the sites from MONZ, it would be likely to close them within two to three years post acquisition rather than incur the replacement costs.

16.16 Kauriland could be expected to maintain the other, larger, Avgas facility for long as it remained in Avgas. SNZ considers that Kauriland would exit Avgas within [] years.

16.17 With or without the acquisition, it appears likely that the number of suppliers in both markets would reduce from three to two in any event. This would be the outcome in the event that no alternative purchaser for MONZ Aerostop Network could be found, and MONZ subsequently decided to close down its network immediately.

16.18 Jet A1 customers are currently very well serviced by SNZ and Air BP, which both operate successful into-plane services at Ardmore Airport.

Paraparaumu

16.19 Though under the proposal there would nominally be a reduction in the number of suppliers of Jet A1 from two to one, there is currently no throughput through the MONZ asset at this location. SNZ understands that MONZ was about to remove the storage tanks. The major customer at the site is Helipro. Helipro is a Kauriland customer. Kauriland purchases Jet A1 from SNZ and on-sells to Helipro.¹² That situation would be very likely to continue post a Kauriland acquisition and so the proposal really results in no change as compared with the counterfactual. To supply this customer directly, Kauriland would need to invest in replacing MONZ's assets at the site and it is hard to see why it would do so when the current arrangements are workable.

16.20 Moreover, there is speculation that Air New Zealand may start a Domestic/Special Carrier service out of Paraparaumu Airport, making Paraparaumu a regional airport. If that development were to go ahead, it would create a new opportunity to offer an into-plane Jet A1 service at this location. SNZ is currently the only player with a functioning Jet A1 storage facility. However, the larger volumes for a Domestic/Special Carrier service would be attractive to any of the other players. SNZ considers that Air BP, Kauriland and MONZ would all potentially be interested. The proposal has no impact on the potential for future competition to establish such a service at Paraparaumu.

Taupo

16.21 The Jet A1 storage tank at this site is owned by SNZ. MONZ's bowser is connected to SNZ's tank. SNZ transports product to the site. If Kauriland were to purchase the MONZ Aerostop bowser at Taupo, it would have to consider capital investment in its own storage facility at this location. SNZ considers this unlikely. Otherwise, for the current arrangements (with MONZ) to continue, Kauriland would have to satisfy SNZ that it had the required financial resource to support the indemnities that SNZ would normally require for such arrangements.

16.22 As regards Avgas, SNZ considers that Kauriland would exit Avgas within five years.

16.23 Therefore, there would be a reduction in the number of suppliers for both products at this location in any event under the counterfactual.

Whakatane

16.24 There is only one General Aviation customer at Whakatane Airport, namely Superair. SNZ believes Superair is currently a MONZ customer. Were Kauriland to acquire the MONZ facility, it could be expected that Superair would transition to Kauriland.

16.25 This is the only site where there would be a reduction in the number of players as a result of the proposed acquisition as compared with even the most favourable counterfactual scenario.

¹² To clarify, these are not "homebase" supplies. [

16.26 Finally, SNZ notes that Air BP is present at all of these locations, specifically:

- (a) Ardmore (both products);
- (b) Gisborne (both products);
- (c) Palmerston North (both products);
- (d) Paraparaumu (Avgas);
- (e) Taupo (Avgas);
- (f) Wellington (both products); and
- (g) Whakatane (both products).

16.27 Paraparaumu and Taupo are the only locations where Air BP would not be present for both products.

Market shares

16.28 SNZ has not attempted to provide market share estimates by volume on a site-by-site basis.

16.29 SNZ's estimates of market shares on a national basis, by volume, for each of Jet A1 and Avgas pre- and post-acquisition are as follows:

Table 2: General Aviation volumes and market shares, national basis, Jet A1 and Avgas

Supplier	Jet A1		Avgas	
	Volume	%	Volume	%
Pre-acquisition				
Air BP	[]	[]	[]	[]
Mobil	[]	[]	[]	[]
Shell	[]	[]	[]	[]
Total	[]	[]	[]	[]
Post-acquisition				
Air BP	[]	[]	[]	[]
SNZ	[]	[]	[]	[]
Total	[]	[]	[]	[]

Source: SNZ's estimates. Volumes are litres x1000

16.30 These figures are SNZ's estimates. They exclude, as outside the relevant market, Jet A1 and Avgas volumes currently supplied by MONZ to Kauriland for distribution to homebase customers.

16.31 SNZ estimates the annual volumes for these supplies, which will continue post-acquisition, at approximately [] for Jet A1 and [] for Avgas. This brings total annual supplies to General Aviation customers to approximately 40 million litres for Jet A1 and 20 million litres for Avgas, as noted in paragraph 11.29 above.

16.32 The acquisition would have a *de minimis* impact on the overall position in the aviation fuels industry as General Aviation is such a small part [] of the wider

industry including supplies to the Big Jet, Domestic/Special Carrier and Military sectors.

16.33 Moreover, given that:

- (a) if the acquisition cannot proceed SNZ believes that one or other, or conceivably both, of SNZ and MONZ would exit the General Aviation sector;
- (b) there is no alternative purchaser who would be likely to offer a more competitive scenario to an acquisition by SNZ;
- (c) expanding SNZ's network through the acquisition of MONZ sites will give SNZ the size, geographic coverage and economies of scale that it currently lacks and mean that it is better placed to compete against Air BP;
- (d) the acquisition does not remove a "maverick" or an important and vigorous competitor,

SNZ considers that the acquisition would be beneficial to competition in the General Aviation sector.

Air BP

16.34 The General Aviation sector is dominated by Air BP which has:

- (a) facilities at 41 locations nationwide, compared with Shell (23) and MONZ (34);
- (b) over [] of the annual volume for Jet A1 on a national basis;
- (c) over [] of the annual volume for Avgas on a national basis.

16.35 Air BP is a much larger player than both SNZ and MONZ. Air BP's broad national coverage gives it significant scale advantages over SNZ and MONZ.

16.36 Air BP's network comprises 61 facilities at 41 locations throughout New Zealand:

Ardmore	Jet A1	Avgas
Christchurch Airport		Avgas
Dannevirke		Avgas
Dargaville		Avgas
Feilding		Avgas
Gore	Jet A1	Avgas
Gisborne	Jet A1	Avgas
Hamilton	Jet A1	Avgas
Hastings	Jet A1	Avgas
Hawera		Avgas
Hokitika	Jet A1	Avgas
Invercargill		Avgas
Kaikohe		Avgas
Kaikoura		Avgas
Kaipara		Avgas
Kerikeri		Avgas
Masterton	Jet A1	Avgas
Matamata		Avgas
Napier		Avgas
Nelson		Avgas
New Plymouth		Avgas

North Shore	Jet A1	Avgas
Omaka	Jet A1	Avgas
Paihiatua	Jet A1	Avgas
Palmerston North		Avgas
Paraparaumu		Avgas
Pukekohe		Avgas
Rangiora	Jet A1	Avgas
Rotorua	Jet A1	Avgas
Taupo		Avgas
Tauranga	Jet A1	Avgas
Timaru		Avgas
Te Anau	Jet A1	Avgas
Waipukurau	Jet A1	Avgas
Wanaka	Jet A1	Avgas
Wanganui	Jet A1	Avgas
Wellington		Avgas
Westport		Avgas
Whakatane	Jet A1	Avgas
Whenuapai	Jet A1	Avgas
Whangarei	Jet A1	Avgas

16.37 Air BP's size and broad national coverage give it significant advantages over SNZ (and, SNZ believes, over MONZ also) through:

- (a) a presence at a larger number of locations nationwide;
- (b) the ability to offer a single source of supply to customers who purchase fuel over a large geographic area. Air BP's slogan is "everywhere you want us to be";
- (c) the ability to capture more volume, and the corresponding ability to offer greater volume-related discounts;
- (d) economies of scale;
- (e) lower unit costs for terminal storage and transportation;
- (f) more frequent supply of Avgas (6 shipments of Avgas per annum ex Australia compared with SNZ (3 per annum)), meaning it can respond more quickly if the cost of product falls.

16.38 In Avgas, Air BP's terminal storage capacity means that it does not need to participate in borrow and loan arrangements. Importantly, Air BP has Avgas terminal storage capacity at Wellington (Hutt City Terminal) and Mount Maunganui. As over 65% of Avgas supplies in New Zealand are to the Upper North Island above Taupo/Turangi/Taranaki, Avgas terminal storage capacity at Mount Maunganui provides Air BP with a significant transport cost advantage over SNZ (and, SNZ believes, over MONZ), which must transport product from MONZ terminal storage at Wellington. Another major advantage is the ability to maximise transport capacity in delivering fuels to a larger number of locations, given Air BP's extensive coverage.

16.39 Air BP also:

- (a) offers an into-plane Jet A1 service at 10 of New Zealand's regional airports (see Figure 2 in paragraph 11.25 above);

- (b) services all three international airports at Auckland, Wellington and Christchurch; and
- (c) continues to service the Military sector. Air BP has held the Royal New Zealand Airforce contract for over 40 years.

16.40 Air BP is a vigorous competitor. Air BP has a history of entering at locations that SNZ would not regard as viable which suggests that it does not appear to face the same capital investment constraints as SNZ. For example:

- (a) At Waipukarau, SNZ removed an Avgas tank that had had annual volumes of 85,000 litres per annum. Air BP installed an Avgas tank at an estimated cost of over [], then installed a Jet A1 facility one year later. SNZ did not consider the site viable for re-investment;
- (b) Air BP targeted SNZ's locations at:
 - (i) Whakatane – Air BP installed a dual facility in 2000/2001;
 - (ii) Bridge Pa – Air BP installed an Avgas facility in 2000/2001;
- (c) Air BP continues to expand its network with recent investments in greenfields sites at:
 - (aa) Kaipara Flats (Avgas) in 2002;
 - (bb) Dargaville (Avgas) in 2001;
 - (cc) Alexandra (Jet A1) in 2002;
 - (dd) Te Kowhai (Avgas) in 2007.

16.41 There is no reason to expect that Air BP's behaviour would change, with or without the acquisition.

Conditions of expansion

16.42 Establishing a facility at a new location might be regarded as either:

- (a) expansion of an existing network; or
- (b) new entry,

depending on how the relevant markets are defined (whether local or national).

16.43 In any event, the requirements for expansion through the establishment of a site at a new location are the same as for reinvestment (i.e. asset replacement). The process is relatively straightforward but reasonably capital intensive, and any decision to invest must take into account the likely returns on a site-by-site basis, and hence volumes at individual sites.

16.44 Greenfields entry at a new location requires:

- (a) resource consent;
- (b) site and tank certification;
- (c) ERMA/HSNO compliance;

- (d) a lease, licence or less formal access rights.
- 16.45 Investments costs are up to [] for a single fuel (Jet A1 or Avgas) to [] for a dual facility (both fuels), for the installation of a tank or tanks, a swipe card bowser and the associated hoses and pumps. Tanks must then be stocked and re-filled on an ongoing basis, and the equipment serviced and maintained.
- 16.46 SNZ's view is that a site requires at least [] litres throughput per annum to be a viable financial proposition, based on its current investment criteria []. If there is already an existing competitor at a location, SNZ's planning assumption would be based on capturing a maximum of [] of the volume available. The relevant markets are mature.
- 16.47 SNZ is currently limited in its ability to expand its existing network by the difficulty in justifying capital investment on a site-by-site basis. SNZ is already challenged to make out the business case for the asset replacement required to maintain their existing networks. Air BP appears to face less restriction in this regard and has a history of expansion and new entry, including at sites that SNZ would not consider viable.
- 16.48 The acquisition should not be regarded as removing potential competition, as neither SNZ nor, in SNZ's view, MONZ, is presently likely to expand. Even the most favourable counterfactual would likely see contraction (closure of sites) through rationalisation of low-contributing sites and, potentially (in a Kauriland acquisition scenario), the conversion of Avgas sites to Jet A1 within [] years.
- 16.49 SNZ's position improves if the acquisition goes ahead, with the result that sites would stay open that would otherwise close under the counterfactual. Increased confidence in the ability to invest in its network would give greater ability to explore opportunities to then expand the network in competing against Air BP.

Coordinated market power

- 16.50 These markets are highly competitive. That will not change as a result of the transaction. As noted, the three national supplier model is an unsustainable market structure, so the proposal simply affects the timing of the change in market structure while enabling major efficiency gains and creating a strong "number two" player.
- 16.51 The proposal results in very limited aggregation on a site-by-site basis and, for the reasons explained, should not be regarded as taking out a potential entrant given the extent to which SNZ is constrained in its ability to expand. On that basis it is not necessary to consider potential coordination issues.
- 16.52 Even if the proposal was regarded as resulting in increased market concentration at a small number of locations, it would not materially enhance the possibility for tacit collusion. This is because:
- (a) SNZ's pricing is cost-based and transparent to customers (but not to Air BP). This will not change with the acquisition;
 - (b) the industry is small and many customers are sophisticated purchasers with visibility over pricing at a number of locations. Many, if not most, are customers of all suppliers and can easily switch. They could easily observe attempts at co-ordinated behaviour and respond to it;
 - (c) supply is already highly competitive, even in sites where there are only one or two suppliers. When prices are adjusted for transportation costs, there is no

material difference between the prices at “solus” or two supplier locations, compared with three supplier locations;

- (d) on that basis there is no reason to expect that the pricing at the seven sites of overlap would be adversely impacted;
- (e) there is differentiation in service and the product offering (e.g. site positioning);
- (f) the parties differentiate their offerings in other ways, e.g. SNZ offers Fly Buys;
- (g) activities in related markets (i.e. the broader fuel market) provide some price comparison and also options for some customers (e.g. Jet A1 into-plane at some locations);
- (h) MONZ’s continuing presence in the Big Jet, Domestic/Special Carrier and Military segments of the wider industry will provide some constraint on the expanded SNZ and Air BP by providing an additional price/service comparison.

Pricing is cost-based and transparent to customers

16.53 Customers purchase fuel using a swipe card issued by the relevant supplier. They are invoiced at the Posted Airfield Price (**PAP**) less any negotiated discount.

16.54 [

]

16.55 [

]

16.56 [

]

16.57 [

]

16.58 [

]

(a) [

]

(b) [

]

16.59 [

]

16.60 [

]

16.61 Differences in the PAP at different locations throughout the SNZ network reflect the differing costs of transportation of product to the different locations. The cost of transporting product to remote locations such as Motueka or Hokitika is significantly more than those for delivery to e.g. Wigram or Paraparaumu.

16.62 SNZ's pricing methodology is unlikely to change with or without the acquisition.

The industry is small

16.63 The General Aviation sector is small. Many of the customers, particularly the commercial pilots, know each other. There is an industry association, the NZ Agricultural Aviation Association (**NZAAA**), which is a division of the Aviation Industry Association (**AIA**).¹³ Co-ordination between SNZ and Air BP could be easily detected. SNZ believes that most General Aviation customers are customers of all three suppliers currently. Switching between them is easy.

No tacit co-ordination currently

16.64 On the basis of the Commission's criteria, despite the industry's tight oligopoly structure, tacit collusion does not currently occur. There are currently 36 "solus" locations, being a location at which only one supplier is present, and 22 locations at which only two suppliers are present.

16.65 As noted, there is no evidence that either unilateral or co-ordinated market power is being exercised currently. In particular:

(a) []

(b) []

16.66 There is no reason to consider that this will change with the acquisition.

MONZ will continue to provide a comparison

16.67 MONZ will continue to supply Jet A1 and Avgas to Kauriland for distribution to "homebase" customers. This will provide a price point comparison.

16.68 MONZ will also continue to supply the Big Jet, Domestic/Special Carrier and Military segments. Through that infrastructure, MONZ will continue to be able to offer General Aviation customers:

(a) a Jet A1 into-plane service at:

- (i) Auckland;
- (ii) Rotorua;
- (iii) Wellington;
- (iv) Christchurch;
- (v) Queenstown;
- (vi) Invercargill; and

¹³ See www.nzaaa.co.nz.

(b) an Avgas into-plane service at Queenstown.

16.69 MONZ's continuing presence in General Aviation and the wider industry will provide customers of the expanded SNZ network with an additional price/service comparison and will continue to be some constraint on SNZ.

16.70 SNZ considers that all Jet A1 customers could potentially access a MONZ into-plane service at a regional airfield. This is because all Jet A1 customers would be within flying range of a regional airport and could pick up fuel there. For Avgas, this option is more limited (to Queenstown).

17. Potential competition

Conditions of entry

17.1 Establishing a facility at a new location might be regarded as either:

- (a) expansion of an existing network; or
- (b) new entry,

depending on how the relevant markets are defined.

17.2 However the relevant markets are viewed, the requirements for entry at a new location are the same and are outlined at paragraphs 16.42 and following above.

17.3 SNZ is currently limited in its ability to expand its existing network by the difficulty in justifying capital investment on a site-by-site basis. SNZ is already challenged to make out the business case for the asset replacement required to maintain its existing networks. Air BP appears to face less restriction in this regard and has a history of expansion and new entry, including at sites that SNZ would not consider viable.

17.4 Of the sites of overlap under the proposal, Paraparaumu and Taupo are the only sites where Air BP does not currently have a presence in both fuels. Air BP has a presence in Avgas at both locations and could easily establish a Jet A1 facility. The costs of establishing a Jet A1 facility would not be prohibitive for Air BP and entry could be effected inside 18 months.

Likelihood, Sufficiency and Timeliness of Entry

17.5 New entry at multiple locations (on a network basis) is not regarded as "likely".

18. Other potential constraints

18.1 The customer base for General Aviation breaks down into several groups:

- (a) Agricultural – pilots engaged in top dressing and forestry-related flying activities;
- (b) Flying schools – pilot training;
- (c) Tourist operators – charter, air taxi, tourism, postal and freight;

- (d) Search & Rescue and other commercial operators (construction-related flying activities, power line laying etc.);
- (e) Resellers – resellers buy fuel from the suppliers and on-sell to their own customers. This category of customer includes a number of overhaul and maintenance companies that repair and maintain aircraft. They buy fuel from SNZ and charge their customers when they pick up their aircraft; and
- (f) Recreational pilots.

18.2 SNZ's customer base, by volume and by value, appears as follows:

- (a) For Jet A1: [

]

- (b) For Avgas: [

]

18.3 Approximately [] of SNZ's customer base, by number, would be commercial operators (i.e. not Recreational pilots). Such customers are repeat purchasers with high annual volume requirements (by General Aviation standards). An average Jet A1 uplift would be 200-250 litres. An average Avgas uplift would be 70 litres.

18.4 Recreational pilots make up the balance. They are occasional purchasers with much lower annual volume requirements.

18.5 While some customers will be based at or near a particular fuelling location, all will have access to more than one fuelling location and can pick up fuel where it best suits them on their journey. This enables some choice between locations e.g. for a customer who may prefer Shell Jet A1 because of an agreed discount or the added benefit of collecting Fly Buys points.

18.6 The larger customers will fly out of a number of locations and have considerable visibility of price differences between suppliers.

18.7 Many are customers of all three suppliers currently. This gives them security of supply through the ability to take fuel at any landing site, whichever supplier has a presence there.

18.8 Volume discounts are common. Contracts are the exception rather than the rule. SNZ has only [] customers on contracts. Air BP and MONZ may have more.

This notice is given by:

Shell New Zealand Limited

The company hereby confirms that:

- all information specified by the Commission has been supplied;
- all information known to the company which is relevant to the consideration and determination of this application/notice has been supplied; and
- all information supplied by the company is correct as at the date of this application/notice.

The company undertakes to advise the Commission immediately of any material change in circumstances relating to the application/notice.

Dated this 20th day of June 2008.

Signed by: David McGuire

Head of Legal

Shell New Zealand Limited

I am duly authorised to make this application on behalf of Shell New Zealand Limited

CONFIDENTIAL ANNEX 1

ANNEX 2

Current locations, all three players: Jet A1

	JET A1		
	MONZ	SNZ	AIR BP
ALBANY			
ALEXANDRA			
ARDMORE			
BLENHEIM (OMAKA)			
BRIDGE PA (HASTINGS)			
CHRISTCHURCH AIRPORT			
DANNEVIRKE			
DARGAVILLE			
DUNEDIN			
FOXTON			
FIELDING			
FRANZ JOSEF			
GORE			
GISBORNE			
GLENTANNER			
GREYMOUTH			
HAAST			
HAMILTON			
HAWERA			
HOKITIKA			
INVERCARGILL			
KAITAIA			
KAIKOHE			
KAIKOURA			
KAIPARA			
KERIKERI			
MASTERTON			
MATAMATA			
MECHANICS BAY			
MOTUEKA			
NAPIER			
NELSON			
NEW PLYMOUTH			
NORTH SHORE			
OMARAMA			
OAMARU			
OPOTIKI			
PAHIATUA			
PALMERSTON NORTH			
PARAPARAUMU			
PUKEKOHE			
RANGIORA			
ROTORUA			
STRATFORD			
TAIERE			
TAUPO			
TAUMARUNUI			
TAIHAPE			
TAURANGA			
TIMARU			
TE ANAU			
TE KUITI			
TEKAPO			
THAMES			
WAIPUKARAU			
WANAKA			
WANGANUI			
WELLINGTON			
WESTPORT			
WAIROA			
WHAKATANE			
WHANGERAI			
WHENUAPAI			
WHITIANGA			
WIGRAM			

Current locations, all three players: Avgas

	AVGAS		
	MONZ	SNZ	AIR BP
ALBANY			
ALEXANDRA	Blue		
ARDMORE	Blue	Yellow	Green
BLENHEIM (OMAKA)			Green
BRIDGE PA (HASTINGS)		Yellow	Green
CHRISTCHURCH AIRPORT			Green
DANNEVIRKE			Green
DARGAVILLE	Blue		Green
DUNEDIN	Blue		
FOXTON		Yellow	
FIELDING		Yellow	Green
FRANZ JOSEF	Blue		
GORE			Green
GISBORNE		Yellow	
GLENTANNER			
GREYMOUTH	Blue		
HAAST	Blue		
HAMILTON			Green
HAWERA			
HOKITIKA			Green
INVERCARGILL	Blue		Green
KAITAIA	Blue		
KAIKOHE			Green
KAIKOURA			Green
Kaipara			
Kerikeri	Blue		Green
MASTERTON	Blue		
MATAMATA			Green
MECHANICS BAY			
MOTUEKA		Yellow	
NAPIER			Green
NELSON		Yellow	
NEW PLYMOUTH			Green
NORTH SHORE			Green
OMARAMA	Blue		
OAMARU		Yellow	
OPOTIKI	Blue		
PAHIATUA			Green
PALMERSTON NORTH		Yellow	Green
PARAPARAUMU		Yellow	Green
PUKEKOHE			Green
RANGIORA		Yellow	Green
ROTORUA	Blue		Green
STRATFORD	Blue		
TAIERE	Blue		
TAUPO	Blue	Yellow	Green
TAUMARUNUI	Blue		
TAIHAPE	Blue		
TAURANGA		Yellow	Green
TIMARU		Yellow	Green
TE ANAU	Blue		
TE KUITI	Blue		
TEKAPO		Yellow	
THAMES	Blue		
WAIPUKARAU			Green
WANAKA		Yellow	Green
WANGANUI	Blue		Green
WELLINGTON		Yellow	Green
WESTPORT			Green
WAIROA			
WHAKATANE		Yellow	Green
WHANGERAI			Green
WHENUAPAI			Green
WHITIANGA		Yellow	
WIGRAM		Yellow	