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Statement of Preliminary Issues

Mobil/WAP and JUHI jet fuel assets

11 May 2022

Introduction

1. On 21 April 2022, the Commerce Commission registered two separate applications from Mobil Oil New Zealand Limited (Mobil) seeking clearance to separately acquire up to 100% of Z Energy Limited's (Z) ownership interest in two separate joint ventures that own assets used to supply jet fuel at Auckland International Airport.

   1.1 In the first application (the WAP Application), Mobil seeks clearance to acquire up to 100% of Z's ownership interest in the pipeline that delivers jet fuel to Auckland International Airport from storage terminals at Wiri (the Wiri to Auckland pipeline, or WAP) (the Proposed WAP Acquisition).

   1.2 In the second application (the JUHI Application), Mobil seeks clearance to acquire up to 100% of Z's ownership interest in the storage terminals and pumping facility at Auckland International Airport, which is called the Auckland Airport Joint User Hydrant Installation (JUHI) (the Proposed JUHI Acquisition).[1]

2. The WAP and JUHI are currently owned by Mobil, Z and BP Oil New Zealand Limited (BP). Both the WAP and the JUHI are run separately from one another as unincorporated joint ventures (JVs) and each JV is governed by separate ownership agreements.[2] With each of the Proposed WAP Acquisition and the Proposed JUHI Acquisition (jointly, the Proposed Acquisitions), Mobil would increase its ownership interest in each JV and Z would no longer have any ownership interest in either JV. If Mobil acquires all of Z's ownership interest, it may become the majority owner of both the WAP and JUHI.

3. The Commission will give clearance if it is satisfied that the Proposed Acquisitions will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.

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1 Public versions of the WAP Application and the JUHI Application are available on our website at: http://www.comcom.govt.nz/business-competition/mergers-and-acquisitions/clearances/clearances-register/. For both the Proposed WAP Acquisition and the Proposed JUHI Application, Mobil has sought clearance for the acquisition of "up to" 100% of Z's shares (depending on whether BP also exercises its pre-emptive rights). In order to grant clearance on this basis, the Commission must be satisfied that the acquisition of all of Z's shares (ie, 100%) will not, or will not be likely to, substantially lessen competition in any relevant market.

2 The WAP Application at [1.3] and the JUHI Application at [1.3].

4. This statement of preliminary issues sets out the issues we currently consider to be important in deciding whether or not to grant clearance to both the Proposed WAP Acquisition and the Proposed JUHI Acquisition.[3]

5. We invite interested parties to provide comments on the likely competitive effects of the Proposed Acquisitions. We request that parties who wish to make a submission do so by **25 May 2022**.

6. If you would like to make a submission but face difficulties in doing so within the timeframe, please ensure that you register your interest with the Commission at registrar@comcom.govt.nz so that we can work with you to accommodate your needs where possible.

The parties

7. Mobil is part of the ExxonMobil group of companies, which has global operations in the fuel, lubricants, and chemicals industries. In New Zealand, Mobil supplies a full range of fuel products, including jet fuel, and distributes these using storage terminals, pipelines, trucks, and other infrastructure assets that it has ownership interests in, or access to.

8. Z is a New Zealand-based fuel company that has operations across the fuel supply chain, including in relation to refining, importing, storing, distributing and supplying customers via wholesale and retail channels. Like Mobil, Z supplies a full range of fuel products, including jet fuel.

9. Mobil, Z, and BP all supply jet fuel at Auckland International Airport.

Our framework

10. Our approach to analysing the competition effects of the Proposed Acquisition is based on the principles set out in our Mergers and Acquisitions Guidelines.[4] As required by the Commerce Act 1986, we assess mergers and acquisitions using the substantial lessening of competition test.

11. We determine whether an acquisition is likely to substantially lessen competition in a market by comparing the likely state of competition if the acquisition proceeds (the scenario with the acquisition, often referred to as the factual), with the likely state of competition if the acquisition does not proceed (the scenario without the acquisition, often referred to as the counterfactual).[5] This allows us to assess the degree by which the Proposed Acquisition might lessen competition.

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[3] The issues set out in this statement are based on the information available when it was published and may change as our investigation progresses. The issues in this statement are not binding on us.

[4] Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2019. Available on our website at www.comcom.govt.nz.

[5] *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

12. If the lessening of competition as a result of the Proposed Acquisition is likely to be substantial, we will not give clearance. When making that assessment, we consider, among other matters:

    12.1 constraint from existing competitors – the extent to which current competitors compete and the degree to which they would expand their sales if prices increased;

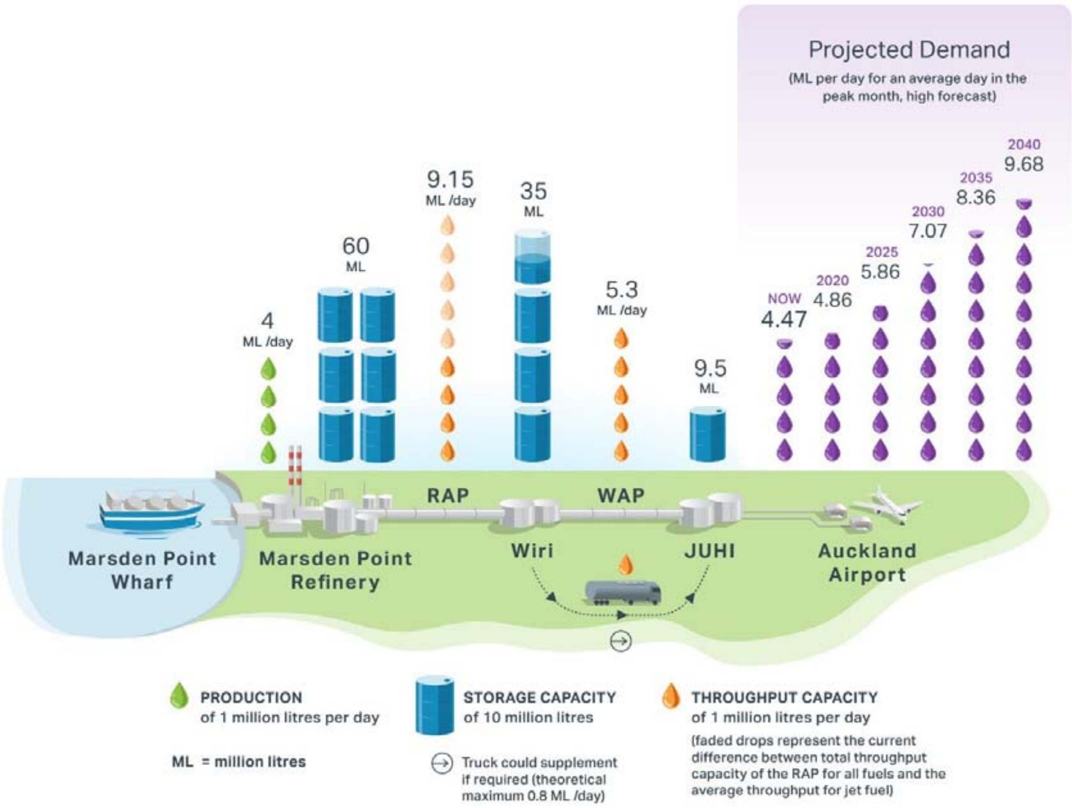
    12.2 constraint from potential new entry – the extent to which new competitors would enter the market and compete if prices increased; and

    12.3 the countervailing market power of buyers – the potential constraint on a business from the purchaser's ability to exert substantial influence on negotiations.

The Proposed Acquisitions and relevant background

13. Figure 1 depicts all key infrastructure currently used to deliver jet fuel to Auckland International Airport, including the WAP and the JUHI.

Figure 1: Infrastructure delivering jet fuel to Auckland International Airport[6] [7]



6 Final Report of the Government Inquiry into the Auckland Fuel Supply Disruption (August 2019) at 87. Although the Marsden Point Refinery has transitioned to an import terminal, the jet fuel delivery infrastructure illustrated in Figure 1 remains the same. The RAP is the pipeline that runs from the refinery to storage terminals at Wiri and is called the Refinery to Auckland Pipeline.

7 The Proposed Acquisitions do not include the storage terminals at Wiri (and other upstream infrastructure from those terminals) and the assets downstream from the JUHI used to deliver fuel to, and physically

14. Mobil advises that the completion of the proposed sale of Z to Ampol Limited (Ampol) will trigger change in control provisions in the ownership agreements for each of the WAP and JUHI. These provisions —along with pre-emptive rights in the ownership agreements— will require Z to give Mobil and BP the option to buy Z's shares in each of the JVs.

15. The ownership agreements for each JV will require Z to offer its interest in each of the WAP and JUHI to Mobil and BP pro rata to their current shareholdings. Mobil intends to exercise its pre-emptive rights in relation to both JVs. Depending on whether BP also opts to exercise its rights, Mobil intends to acquire either all or part of Z's stake.[8] It seeks clearance to buy up to 100% of Z's stake in each JV.

16. Mobil submits that its decision to exercise its pre-emptive rights is motivated by its intention to modernise the ownership agreements for each of the WAP and JUHI, and how the WAP and JUHI are owned and operated, in a way that would:[9]

   16.1 facilitate new entry in the supply of jet fuel at Auckland International Airport by removing the requirement that new users need to acquire an ownership interest in the WAP and JUHI to be able to use them;

   16.2 encourage and remove the barriers to future investment in the quality and capacity of each of the WAP and JUHI by enabling the JVs to generate a return on investment; and

   16.3 address the concerns raised by, and recommendations of, the Government Inquiry into the Auckland Fuel Supply Disruption.[10]

17. Post-acquisition, Mobil intends to renegotiate the ownership agreements for the WAP and JUHI with BP, and convert both JVs to an 'open access' model, which Mobil says is consistent with best practice. This open access model would mean that any party wanting to supply jet fuel at Auckland International Airport could access the WAP and JUHI, rather than just JV shareholders which is currently the case. Under this model, all users (including Mobil and BP) would pay a non-discriminatory fee for usage of the WAP and JUHI.[11]

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refuel, aircraft at Auckland International Airport. The downstream assets include a pipeline and hydrant dispenser vehicle owned by Auckland International Airport Limited (AIAL) and refuelling trucks that are filled up at the JUHI and drive out to refuel aircraft on the tarmac. Mobil operates refuelling trucks on its own, while BP and Z jointly own refuelling trucks through a Joint Into-Place Fuelling Services joint venture. The WAP Application at [8.2(d)] and the JUHI Application at [8.2(d)].

8 The WAP Application at [1.4]-[1.5] and [5.2] and the JUHI Application at [1.4]-[1.5] and [5.2].

9 The WAP Application at [1.6] and the JUHI Application at [1.6].

10 Final Report of the Government Inquiry into the Auckland Fuel Supply Disruption (August 2019) at Part E. The concerns included the extent of storage capacity at the JUHI and the capacity of the WAP, which added to a general concern about the resilience of the jet fuel supply chain (given forecast demand for jet fuel). The report expressed some concern about whether Mobil, BP and Z would make timely decisions to make necessary investments in the supply chain. The report suggested that that open access to infrastructure would likely reduce the barriers for new entrants.

11 The WAP Application at [5.7] and the JUHI Application at [5.7].

18. At this stage it is unclear whether such a renegotiation will be successful and, if it is, what the key aspects of an open access regime will be. Similarly, it is unclear whether BP will also seek to exercise its own pre-emptive rights in relation to one or both JVs. We are considering the implications of these unknowns for our analysis.

Market definition

19. We define markets in the way that we consider best isolates the key competition issues that arise from the Proposed Acquisition. In many cases this may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Commerce Act, as a matter of fact and commercial common sense.[12]

20. Mobil submits that the only potentially relevant markets that may be affected by the Proposed Acquisitions are downstream markets for the sale of jet fuel at Auckland International Airport, noting that the Commission in Z/Chevron defined downstream markets for:[13]

    20.1 the supply of Jet A-1 to Air New Zealand at Auckland International Airport; and

    20.2 the supply of Jet A-1 to all other (non-Air New Zealand) customers at Auckland International Airport.

21. We will consider whether these are the appropriate markets for considering the competition effects of the Proposed Acquisition, and whether there are other relevant markets, including upstream functional markets for access to the relevant midstream infrastructure (ie, the WAP and JUHI).

Without the acquisition

22. Mobil submits that, in the counterfactual, it is most likely that Z (and its new owner Ampol) would retain any shares of the WAP and JUHI not acquired by Mobil or BP.[14] This would result in Z remaining a participant in the JVs with respect to the WAP and JUHI. In other words, the counterfactual would be the status quo.

23. For each of the Proposed WAP Acquisition and the Proposed JUHI Acquisition, we will consider what Mobil, Z and BP (and third parties) would do if it did not go ahead. We will consider the evidence on whether the without-the-acquisition scenario is best characterised by the status quo, or whether the counterfactual may be something other than the status quo.

24. For the counterfactual to each of the Proposed WAP Acquisition and the Proposed JUHI Acquisition, we will consider whether:

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12 Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

13 The WAP Application at [9.1]-[9.3] and the JUHI Application at [9.1]-[9.3] citing Z Energy Limited and Chevron New Zealand [2016] NZCC 10 at [278].

14 The WAP Application at [7.4] and the JUHI Application at [7.4].

24.1 BP would be likely to exercise its pre-emptive rights to buy all or some of Z's shares; and

24.2 Mobil, BP and Z would revise the structure, ownership and/or operation of the JV.

Preliminary issues

25. We will investigate whether the Proposed Acquisitions would be likely to substantially lessen competition in the relevant markets by assessing whether the Proposed Acquisitions might result in vertical, horizontal unilateral, or coordinated effects:

25.1 vertical effects: whether the Proposed Acquisitions would increase the merged entity's ability and/or incentive to engage in either partial or total foreclosure of actual or potential rivals;

25.2 unilateral effects: whether the loss of competition would enable the merged entity to profitably raise prices and/or reduce quality or innovation by itself;[15] and

25.3 coordinated effects: whether the Proposed Acquisitions would change the conditions in the relevant markets so that coordination is more likely, more complete, or more sustainable.

26. The main focus of our investigation is likely to be on vertical effects.

27. While we will need to undertake this assessment separately for the Proposed WAP Acquisition and the Proposed JUHI Acquisition, the considerations and assessment may be broadly similar for each of the WAP and JUHI.

Vertical effects: would the merged entity be able to foreclose rivals?

28. A merger between suppliers (or buyers) who are not competitors but who operate in related markets can result in a substantial lessening of competition due to vertical effects. This can occur where a merger gives the merged entity a greater ability or incentive to engage in conduct that prevents or hinders rivals from competing effectively.[16]

29. We will investigate whether the Proposed Acquisitions would be likely to substantially lessen competition in a relevant downstream market due to vertical effects. This could be the case if the WAP or JUHI are necessary infrastructure to compete in that market and the Proposed Acquisitions give Mobil the ability and incentive to foreclose (either fully or partially) rivals' access to that infrastructure. Foreclosure may result from raising rivals' costs thus preventing or hindering rivals from competing effectively in the relevant downstream market.

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15 For ease of reference, we only refer to the ability of the merged entity to "raise prices" from this point on. This should be taken to include the possibility that the merged entity could reduce quality or innovation, or worsen an element of service or any other element of competition (ie, it could increase quality-adjusted prices).

16 Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2019) at [5.1]-[5.2].

30. Mobil submits that the Proposed Acquisitions would not result in any lessening of competition due to vertical effects. Mobil submits that it would have neither the ability, nor incentive, to foreclose access to the relevant downstream markets by restricting access to the WAP or JUHI. Further, even if Mobil did have both the ability and incentive to foreclose access, it submits that the Proposed Acquisitions could not plausibly have the likely effect of substantially lessening competition in those markets due to vertical effects.[17]

31. We discuss below:

    31.1 the ability to foreclose;

    31.2 the incentives to foreclose; and

    31.3 the potential effects of foreclosure on competition in the relevant downstream markets.

Ability to foreclose

32. Mobil submits that post-acquisition, it would not have the ability to foreclose access to the WAP and JUHI on the basis that:[18]

    32.1 access to the WAP is not essential to supply jet fuel in the relevant downstream markets, as the WAP can be bypassed by a supplier trucking fuel to Auckland International Airport;

    32.2 BP would continue to be a joint owner of the WAP and JUHI, and remain a vigorous competitor in the relevant downstream markets;

    32.3 AIAL has countervailing power over the JUHI in its capacity as owner of the land where the JUHI is situated. AIAL is incentivised to ensure that airlines can obtain reasonably priced jet fuel at Auckland International Airport (so as not to risk losing flights to other airports) and could impose conditions on any JUHI lease to preserve competition as some airports have done in Australia;

    32.4 airlines and/or AIAL can integrate up the supply chain to establish alternative supply infrastructure; and

    32.5 any hypothetical ability to foreclose in the relevant downstream markets is likely to be transitory because attempts to foreclose would provide a catalyst for alternative supply chain infrastructure being established (which would then remove any ability to foreclose).

33. For each of the Proposed WAP Acquisition and the Proposed JUHI Acquisition, we will consider whether Mobil would have the ability to foreclose access to the relevant assets. Central to this assessment will be considering whether Mobil would have market power with respect to the WAP and JUHI because rivals need to access this

[17] The WAP Application at [10.1] and the JUHI Application at [10.1].
[18] The WAP Application at [1.8] and 26-29 and the JUHI Application at [1.8] and 26-29.

infrastructure to compete effectively downstream (ie, for the supply of jet fuel at Auckland International Airport). Our assessment for each of the Proposed WAP Acquisition and the Proposed JUHI Acquisition may be different if:

33.1 rivals are able to bypass the WAP but cannot bypass the JUHI; and

33.2 any countervailing power of AIAL is different for the JUHI versus the WAP.

Incentives to foreclose

34. Mobil submits that post-acquisition, it would also not have the incentive to foreclose access to the WAP and JUHI on the basis that:[19]

34.1 the rationale for the Proposed Acquisitions is to implement a model that would facilitate open access to the WAP and JUHI (and thus the relevant downstream markets) and foreclosure would run contrary to that rationale; and

34.2 Mobil globally has strict firewalls in place between staff who are responsible for participation in the JVs and those selling jet fuel to airlines. This is to ensure that decisions are made to maximise utilisation of the WAP and JUHI (irrespective of which supplier is selling the jet fuel downstream) in order to spread the fixed costs of the infrastructure over the largest possible volume to drive the most efficient per-litre cost of jet fuel.

35. We will consider whether the Proposed Acquisitions would give Mobil the incentive to engage in foreclosure. Central to this assessment will be profitability of such a strategy and, in particular, whether the profits that Mobil would earn from the additional airline customers it wins from foreclosing rivals would outweigh any loss of profits associated with the WAP and JUHI.

Effect of foreclosure on competition in the relevant downstream markets

36. Mobil also submits that even if it did hypothetically have both the ability and incentive to foreclose access to the WAP and JUHI, neither of the Proposed Acquisitions could plausibly have the likely effect of substantially lessening competition in the relevant downstream markets. Mobil submits that the dynamics of the relevant downstream markets are such that it would face material competitive constraints post-acquisition. Mobil submits that this is due to the fact that:[20]

36.1 Z would remain a vigorous competitor in the relevant downstream markets;

36.2 even if Z is foreclosed, BP would remain a vigorous competitor to Mobil;

36.3 airlines can, and do, negotiate region-wide arrangements with fuel suppliers, and may constrain any attempt by Mobil to increase jet fuel prices at Auckland International Airport by shifting volumes to rival fuel suppliers at other airports;

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19 The WAP Application at [1.8] and 29-30 and the JUHI Application at [1.8] and 29-30.

20 The WAP Application at [1.8] and 30-33 and the JUHI Application at [1.8] and 30-33.

36.4 airlines have flexibility to alter their fuelling schedules to bypass Auckland International Airport (or minimise their need to refuel at the airport) if prices are not competitive with other airports;

36.5 the rationale for the Proposed Acquisitions is to shift to an open access model for the WAP and JUHI, where all suppliers can access the assets at throughput fees that generate a return to fund further investment in that infrastructure. Overseas experience suggests that an open access model would lead to more (rather than less) competition in the relevant downstream markets; and

36.6 as the largest purchaser of jet fuel at Auckland International Airport, Air New Zealand has countervailing buyer power, and could therefore defeat any purported attempt by Mobil to increase prices. Air New Zealand would be able to threaten to sponsor new entry either by integrating up the supply chain and/or committing large volumes to a potential new entrant. Air New Zealand could also look to self-supply.

37. We will consider whether any competition lost from foreclosed competitors in the relevant downstream markets would have the likely effect of substantially lessening competition. This could occur if any foreclosure made entry by rivals more difficult or otherwise reduced a competitor's ability to compete in the relevant downstream markets.

Unilateral effects: would the merged entity be able to profitably raise prices by itself?

38. Unilateral effects arise when a firm merges with a competitor that would otherwise provide a significant competitive constraint (particularly relative to remaining competitors) such that the merged firm can profitably increase prices above the level that would prevail without a merger, without the profitability of that increase being thwarted by rival firms' competitive responses.[21]

39. Mobil submits that the Proposed Acquisitions do not result in the removal or acquisition of a competitor to Mobil. Given this, and that Mobil would have neither the ability nor incentive to foreclose access to the relevant downstream markets by restricting access to the WAP or the JUHI, Mobil submits the Proposed Acquisitions do not result in any increased risk of unilateral effects arising.[22]

40. Mobil further submits the Proposed Acquisitions would be procompetitive in that they would facilitate new entry into the relevant downstream markets as well as allow for an appropriate return on the infrastructure to incentivise further investment in the infrastructure. These factors will become increasingly necessary and urgent when demand for air travel returns to pre-pandemic levels.[23]

41. We will consider whether any horizontal unilateral effects might arise from the Proposed Acquisitions. We will consider:

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[21] Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2019) at [3.62]

[22] The WAP Application at [12.1] and the JUHI Application at [12.1].

[23] The WAP Application at [5.14] and the JUHI Application at [5.14].

41.1 *closeness of competition*: the degree of constraint that Mobil and Z impose upon one another in any relevant market, and the extent of competition that might be lost with the Proposed Acquisitions;

41.2 *remaining competitive constraints*: the degree of constraint that existing competitors would impose on the merged entity;

41.3 *entry and expansion*: how easily rivals could enter and/or expand, including the ability to secure access to infrastructure, or to establish the alternative infrastructure needed for entry/expansion; and

41.4 *countervailing power*: whether AIAL or airlines have special characteristics that would enable them to resist an exercise of market power by Mobil.

Coordinated effects: would the Proposed Acquisitions make coordination more likely?

42. An acquisition can substantially lessen competition if it increases the potential for the merged entity and all or some of its remaining competitors to coordinate their behaviour and collectively exercise market power or divide up the market such that output reduces and/or prices increase.[24] Unlike a substantial lessening of competition which can arise from the merged entity acting on its own, coordinated effects require some or all of the firms in the market to be acting in a coordinated way.

43. Mobil submits that the Proposed Acquisitions would not change the conditions of the relevant downstream markets in such a way that would increase the potential for coordinated effects to arise. Mobil submits that this is because:[25]

43.1 there would be no decrease in the number of suppliers in the relevant downstream markets with the Proposed Acquisitions (instead there may be an increase in the number of suppliers with a change to an open access model);

43.2 the relevant downstream markets lack transparency around price and volumes;

43.3 customers are sophisticated purchasers with countervailing buyer power; and

43.4 suppliers need to secure volume to spread the costs of the infrastructure used to supply jet fuel to Auckland International Airport.

44. We will assess whether any of the relevant markets are vulnerable to coordination, and whether the Proposed Acquisitions would change the conditions in the relevant markets so that coordination is more likely, more complete, or more sustainable.

Next steps in our investigation

45. The Commission is currently scheduled to make a decision on whether or not to give clearance to the Proposed Acquisition by **20 June 2022**. However, this date may

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[24] Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2019) at [3.84].

[25] The WAP Application at [11.1]-[11.2] and the JUHI Application at [11.1]-[11.2].

change as our investigation progresses.[26] In particular, if we need to test and consider the issues identified above further, the decision date is likely to extend.

46. As part of our investigation, we will be identifying and contacting parties that we consider will be able to help us assess the preliminary issues identified above.

Making a submission

47. If you wish to make a submission, please send it to us at registrar@comcom.govt.nz with the reference "Mobil jet fuel" in the subject line of your email, or by mail to The Registrar, PO Box 2351, Wellington 6140. Please do so by close of business on **25 May 2022**.

48. Please clearly identify any confidential information contained in your submission and provide both a confidential and a public version. We will be publishing the public versions of all submissions on the Commission's website.

49. All information we receive is subject to the Official Information Act 1982 (OIA), under which there is a principle of availability. We recognise, however, that there may be good reason to withhold certain information contained in a submission under the OIA, for example in circumstances where disclosure would unreasonably prejudice the supplier or subject of the information.

[26] The Commission maintains a clearance register on our website at http://www.comcom.govt.nz/clearances-register/ where we update any changes to our deadlines and provide relevant documents.