Gorgon Gas Project: Application for Joint Selling Authorisation

Third submission to the ACCC
by the DomGas Alliance

27 August 2009

C/- DBP, Level 6, 12-14 The Esplanade, Perth WA 6000
Postal Address - PO Box Z5267 St Georges Terrace Perth WA 6831
Telephone: +61 8 9223 4300 Facsimile: +61 8 9223 4301
Website: www.domgas.com.au

CONTENTS

1. OVERVIEW AND THE ACCC'S ROLE

1. The ACCC's assessment is being undertaken amidst intense political interest in the Gorgon Project and intense pressure on the part of the applicants.

2. This public interest is underlined by government and media references to a "$50 billion recession busting project", "$50 billion gas deal to China" and claims that the Project will transform Australia into an "energy superpower".

3. In this highly politicised environment, the ACCC's role assumes even greater importance. The ACCC is the only independent national authority charged by the *Trade Practices Act* to promote competition and protect Australian consumers.

4. The DomGas Alliance supports the Gorgon Project and the significant investment and employment benefits it would provide to the Australian economy.

5. Issues concerning the application for joint marketing should not however be characterised as being either pro- or anti- Gorgon investment – or that refusal to grant authorisation would somehow threaten the $50 billion Project.

6. Such claims are misleading and should be dismissed by the ACCC. They have been rejected by the ACCC's own commissioned Allen Consulting Group Report.

7. A determination by the ACCC not to authorise Shell, Chevron and ExxonMobil to engage in anti-competitive conduct or price fixing could not be construed as "standing in the way" of the Project.

8. There is no justification for permitting the world's biggest oil and gas companies to sell as a cartel. Separate selling is practical and feasible and should be pursued by the Gorgon applicants.

9. The Allen Consulting Group Report confirms that cartel selling is not necessary to manage risk or to underpin Gorgon Project investment:

   - Domestic gas represents less than 5 per cent of the Gorgon gas resources;

   - Domestic gas would account for less than 5 per cent of total Gorgon revenue;

   - Shell, Chevron and ExxonMobil are three of the largest companies in the world with combined 2008 income of over $US 120 billion;

- Chevron and Shell are equity partners in the largest domestic gas seller in Western Australia;

- The domestic phase post-dates LNG export start-up by three or more years;

- Domestic gas prices will almost certainly have lower price volatility than LNG exports;

- Domestic sales will be subject to take-or-pay contract provisions;

- Chevron and Shell management are familiar with the WA gas market through their investment in the NWS project; and

- ExxonMobil is the world's largest and most profitable oil and gas company with over 40 years experience in the Australian gas market.[1]

10. As the ACG Report points out, whether the WA market is mature or immature has not prevented other gas producers from selling separately in Western Australia. The Gorgon applicants have failed to demonstrate why they would be prevented from doing so.

11. Any granting of final authorisation by the ACCC will impact businesses and households for decades through higher gas and electricity prices.

12. While cartel selling might reduce costs for Shell, Chevron and ExxonMobil, gas prices to Australian consumers will "most likely" rise "due to monopolisation effects".[2]

13. If, on the other hand, Shell, Chevron and ExxonMobil were compelled to sell separately and compete, this would reduce their bargaining power with the likelihood of lower prices for Australian consumers.[3]

14. Western Australia is already one of the most uncompetitive gas markets in Australia. Just two supply groups control close to 100 per cent of the market, with the North West Shelf Joint Venture cartel producers controlling 70 per cent of the market.

15. As a result, consumers are being asked to pay around three times or more for the price for new gas on a delivered basis compared to consumers in Victoria.

---

[1] Allen Consulting Group, 'Gorgon Gas Project Joint Venture Application for Authorisation of Joint Marketing', Final Report to the Australian Competition and Consumer Commission, July 2009.
[2] ACG Report, p.26.
[3] ACG Report, p.28.

16. At the same time, Shell, Chevron and ExxonMobil continue to compete with each other in separately marketing 95 per cent of Gorgon gas to overseas customers.[4]

17. In August, ExxonMobil separately concluded contracts to supply around $19 billion and $50 billion of gas over 20 years to Petronet in India and PetroChina in China.

18. It would be incongruous if the biggest companies in China and India should enjoy the benefits of competition in relation to 95 per cent of Gorgon gas, while this is denied to Australian consumers.

19. The ACCC should not endorse an outcome which will give authorisation for the world's biggest oil and gas companies to impose higher gas and electricity bills on Australian industry, small business and households.

2. THE ALLEN CONSULTING GROUP REPORT

20. The Alliance welcomes the ACG Report which provides a balanced and considered assessment of the claims asserted by the Gorgon applicants.

21. While the Alliance does not agree with some of the Report's findings, it strongly agrees with the Report's findings that:

- cartel selling is not required to manage risk or to underpin investment in the Gorgon Project;
- the Gorgon applicants have failed to demonstrate why they are unable to sell separately to Australian consumers; and
- authorisation would result in higher gas prices for Australian consumers, while separate selling would result in lower gas prices.

2.1 Interim authorisation

22. The Alliance does not agree with the reasoning behind the Report's conclusion that the ACCC's grant of interim authorisation is unlikely to have a material impact on competition in the short term.

23. The Report correctly points out that buyers might not provide anything more than expressions of interest and would be reluctant to divulge commercially sensitive information.

24. Gas consumers are therefore seeking to limit the anti-competitive detriment that has arisen from the ACCC's grant of interim

---

[4] As the ACG Report points out, LNG exports will account 95 per cent of Gorgon resources and 95 per cent of expected project revenue.

authorisation. It is incorrect to conclude that the interim authorisation decision has no material impact on competition.

25. Furthermore, ExxonMobil has separately concluded 20 year LNG contracts with India and China – estimated to be worth $19 billion and $50 billion each.

26. It is unreasonable for the applicants to continue to claim that cartel marketing for domestic gas is necessary to enable a Final Investment Decision on the Gorgon Project.

27. They have been separately selling Gorgon gas to overseas customers since 2005, with LNG expected to account for over 95 per cent of expected Project revenue.

2.2 WA domestic gas market and separate selling

28. The Alliance does not agree with the Report's findings on the relative immaturity of the WA domestic gas market, compared to international markets.[5]

29. However, as the ACG Report points out, whether the WA market is mature or immature has not prevented other gas producers from selling separately in Western Australia. The Gorgon applicants have failed to demonstrate why they are unable to sell separately:

    "Accepting that Gorgon will have a larger market presence, it could be asked why it is that medium-large fields like Harriet, John Brookes and possibly some of Reindeer and Macedon can be and are marketed separately, but the Applicants believe that the market conditions will not be conducive for Gorgon to be separately marketed for many years."[6]

30. The ACG Report dismisses the applicants' claims that gas balancing or nominations arrangements are unfeasible for the Project:

    "Separate marketing of hydrocarbons is commonplace, so the principles of overlift and underlift are well established in project operating agreements. In fungible products like oil, condensate, LPG and LNG, imbalances are generally easily resolved and are therefore immaterial. Most petroleum joint ventures have operating agreements and/or lifting agreements which set out the principles under which entitlement imbalances can occur and how they must be resolved."[7]

---

[5] The Alliance has provided detailed evidence on the significant transformation of the WA gas market since the 1990s including the significant increase in the number of customers, additional transport and storage options, significant short-term and spot markets, etc.

[6] ACG Report, p.21.
[7] ACG Report, p.22.

31. The Alliance agrees with the Report's conclusion that "it is difficult to accept the argument put forward by the Applicants that joint marketing is required as a risk mitigation tool" because:

- Domestic supply represents a small proportion of the total Gorgon Project;
- the domestic phase post-dates the export phase start-up by three or more years;
- domestic gas prices will almost certainly have lower price volatility than the export and liquids phase;
- domestic sales will be subject to take-or-pay contract provisions;
- Chevron and Shell management are familiar with the WA gas market through their investment in the NWS project; and
- ExxonMobil is the world's largest and most profitable oil and gas company, with over 40 years experience in the Australian gas marketed.[8]

32. There is therefore no justification for permitting the world's biggest oil and gas companies to sell as a cartel to Australian consumers.

33. It is not required to manage risk or to underpin investment in the Gorgon Project. Separate selling is practical and feasible and should be pursued by the Gorgon applicants.

2.3 Separate marketing will increase the number of competitive sellers

34. The ACG Report considers that if all of WA's gas is marketed separately, there may be seven sellers with equity shares of 50 TJ/day or more with each of Woodside, Chevron, BHP Billiton and Apache controlling more than 200 TJ/day.[9]

35. This demonstrates the competitive benefits of separate selling. It will result in seven sellers each with significant quantities of gas to market to the domestic market.

36. If on the other hand final authorisation is granted, the WA domestic gas market will continue to be dominated by just two supply groups: (1) the NWSJV and Gorgon participants ; and (2) Apache-led JVs. It will continue to be one of the most uncompetitive gas markets in Australia.

[8] ACG Report, p.24.
[9] ACG Report, p.24.

2.4 Separate marketing and Gorgon Project investment

37. The DomGas Alliance supports the Gorgon Project and the significant investment and employment benefits it would provide to the Australian economy.

38. Issues concerning the application for joint marketing should not however be characterised as being either pro- or anti- Gorgon investment – or that refusal to grant authorisation would somehow threaten the $50 billion Project.

39. Such claims are misleading and should be dismissed by the ACCC. They have been dismissed as "misleading" by the ACCC's own commissioned Allen Consulting Group Report:[10]

"Gorgon project risk emanates from various geological, engineering (offshore and onshore), market, environmental, political and financial exposures. Domestic gas is therefore a comparative small component of total risk. The question regarding joint marketing versus separate marketing is an even smaller proportion of total risk.

It may therefore be misleading to consider the question of joint versus separate marketing from a 'whole of project' perspective as outlined in the arguments detailed in the Lateral Economics and Concept Economics reports.

They discuss price determination, market power and risks from a 'whole of project' perspective but the issues pertaining to the request for authorisation of joint marketing are a sub-set of the Gorgon investment decision."[11]

40. Furthermore, as the ACG Report points out, domestic gas represents a very small proportion of the total project - less than 5 per cent of the Greater Gorgon gas resource, and less than 5 per cent of total project revenue.[12]

41. It is unreasonable for the applicants to argue that cartel selling is necessary to underpin Gorgon investment when they continue to sell separately to overseas customers in relation to 95 per cent of Gorgon gas.

42. The Alliance is hopeful that the ACCC remains firm against attempts by Shell, Chevron and ExxonMobil to characterise a decision not to grant authorisation as somehow "standing in the way" of the $50 billion Gorgon Project.

---

[10] ACG Report, p.27.
[11] ACG Report, p.27.
[12] ACG Report, p.23.

43. Authorisation for cartel selling is not necessary to manage risk or to underpin investment in the Gorgon Project.

3. PRODUCERS CONTINUE TO SELL SEPARATELY IN WA

44. The Alliance agrees with the ACG Report that the next three gas projects in WA may be separately marketed.

45. As the Report notes, Reindeer (2011), Macedon (2012) and Julimar (2014) are all possible / likely to be separately marketed based on the actions of Apache, Santos and Kufpec in other joint ventures.[13]

46. Recent developments reinforce that separate selling in WA continues to be commercially practical and feasible.

47. In July 2009, Santos announced it had entered into a new arrangement to extend its existing gas supply contract with Santos. Total sales revenue under the four year contract will be approximately $100 million.

48. The gas will be sourced from Santos' 45 per cent production share of the John Brookes field. As Santos points out in its announcement, gas from John Brookes is marketed separately by the partners Santos and Apache.[14]

49. The fact that Santos continues to successfully sell separately disproves the claims that separate selling is not commercially practical or feasible in WA.

50. The $100 million agreement with Newmont also disproves claims that the WA domestic market is a "small" or immature market. The WA domestic gas market is in fact a $1 billion dollar market, where more than 30 customers buy directly from just two producer groups.

4. SHELL, CHEVRON AND EXXONMOBIL CONTINUE TO SELL SEPARATELY TO OVERSEAS CUSTOMERS

51. As discussed above, Shell, Chevron and ExxonMobil continue to sell separately to overseas customers, entering into long-term contracts with a very small number of very large customers.

52. On 10 August 2009, ExxonMobil announced it had entered into a 20 year agreement with India's Petronet LNG for the separate sale of Gorgon gas.

---

[13] ACG Report, p.25.

[14] Santos, "Santos secures $100 million Newmont gas supply extension in Western Australia", ASX / Media Release, 27 July 2009.

53. Under the agreement, ExxonMobil will supply about 1.5 million tonnes per year from its share of Gorgon LNG production for 20 years.[15] The deal has been estimated to be worth $19 billion.[16]

54. On 17 August 2009, ExxonMobil announced it had entered into a 20 year agreement with PetroChina for the separate sale of Gorgon gas.

55. Under the agreement, ExxonMobil will supply about 2.25 million tonnes per year from its share of Gorgon LNG production for 20 years.[17] PetroChina is the listed arm of state-owned China National Petroleum Corporation (CNPC), China's biggest oil producer.

56. In welcoming the PetroChina agreement, the Federal Government has referred to a $50 billion contract. The ABC reports that the deal "virtually guarantees that the Gorgon project will go ahead".[18]

57. It is telling that ExxonMobil has, in the space of a week, successfully concluded two highly complex international sales agreements, involving $19 billion and $50 billion of gas, over 20 years, supplying some of the world's biggest and most powerful companies.

58. Furthermore, these contracts have been concluded at a time when "international" LNG prices have fallen significantly (as outlined in the Alliance's previous submissions to the ACCC).

59. They were also concluded in the almost complete absence of an Asian "spot market". The North West Shelf Joint Venture (which Shell and Chevron are participants in) has reported as recently as 10 August 2009 that "spot demand for LNG in Asia, and Japan in particular, has almost disappeared".[19]

60. There is therefore no basis to the Gorgon applicants' claims that the characteristics of the WA gas market or domestic gas supply make separate marketing unviable.

61. It is illogical for the Gorgon applicants to claim that a small number of domestic customers, long term contracts, an illiquid market or the lack of spot markets prevents separate selling in WA, while at the same time:

---

[15] ExxonMobil, 'ExxonMobil and Petronet sign Gorgon LNG supply agreement', media release, 10 August 2009, available at: http://www.exxonmobil.com.au/Australia-English/PA/news_release_20090810.aspx

[16] The Australian, 'Huge gas project on target', 11 August 2009.

[17] ExxonMobil, 'ExxonMobil and PetroChina sign Gorgon LNG supply agreement', media release, 17 August 2009, available at: http://www.exxonmobil.com.au/Australia-English/PA/news_release_20080818.aspx

[18] ABC News, 'Massive sale from Gorgon Gas Project', 19 August 2009, available at: http://www.abc.net.au/rural/content/2008/s2660434.htm

[19] Dow Jones Newswires and The Australian, 'LNG spot Asian demand hit by global downturn', 10 August 2009, available at: http://www.theaustralian.news.com.au/business/story/0,28124,25908572-5005200,00.html

- separately negotiating and concluding $19 billion and $50 billion overseas gas contracts;

- covering 20 year terms;

- to supply a very small number of very large customers;

- at a time when the spot market "has almost disappeared".

62. In fact, to the extent there are commercial risks attached to gas marketing, these lie heavily in relation to the international marketing of LNG as opposed to domestic gas:

"[T]he relative impact of differing modes of Gorgon domestic marketing on price outcomes is almost certainly less than the price volatility which LNG sales will encounter. While each of the Applicants are attempting to secure term contracts for some or all of their expected LNG entitlements from Gorgon, pricing will be heavily exposed to oil price volatility and probably spread across less than four customers. Domestic pricing is likely to be linked to less volatile indices and to multiple customer contracts."[20]

63. As the ACG Report points out, domestic sales will be subject to take-or-pay contract provisions which would transfer much of the risk associated with domestic supply to customers.[21] Such provisions are also typically contained in LNG contracts.

64. It would be incongruous if the biggest companies in China and India should enjoy the benefits of competition between the Gorgon applicants, while this is denied to Australian consumers.

5. IMPACT ON COMPETITION AND AUSTRALIAN CONSUMERS

5.1 Cartel selling with increase prices for Australian consumers

65. Any granting of final authorisation by the ACCC will have profound consequences for businesses and households in Western Australia for decades through higher gas and electricity prices.

66. The ACG Report concludes that while cartel selling might reduce costs for Shell, Chevron and ExxonMobil, gas prices to WA consumers will "most likely" rise "due to monopolisation effects".[22]

[20] ACG Report, p.24.
[21] ACG Report, p.24.
[22] ACG Report, p.26.

67. If, on the other hand, Shell, Chevron and ExxonMobil were compelled to sell separately and compete, this would reduce their bargaining power with the likelihood of lower prices.[23]

68. Higher gas and electricity prices impact every West Australian business and household. This public detriment will far outweigh any public "benefit" that might be gained from any reduced costs on the part of Shell, Chevron and ExxonMobil.

69. The ACCC should not endorse an outcome which will give authorisation for the world's biggest oil and gas companies to impose higher gas and electricity bills on Australian industry, small business and households.

5.2 Consumers are being asked to pay around three times or more for the price for new gas compared to in Victoria

70. As the result of cartel selling arrangements, Western Australia is one of the most uncompetitive gas markets in Australia.

71. Just two supply groups control close to 100 per cent of the market, with the North West Shelf Joint Venture cartel producers controlling 70 per cent of the market.

72. As a result, WA consumers are therefore being asked to pay around three times or more for the price for new gas compared to consumers in Victoria.

73. The absence of competition is impacting businesses and households through higher energy bills.

74. In June 2009, the WA Office of Energy approved significant increases in business and residential gas tariffs. The new tariffs came into force on 1 July 2009.

75. As a result, the annual gas bill of the average Mid West and South West household has increased by $78 or almost 23 per cent.[24]

---

[23] ACG Report, p.28.

[24] WA Office of Energy, *Gas Tariffs Review: Interim Report to the Minister for Energy*, June 2009, p.3.

Impact of Tariff Cap Increases on Median Customers (based on Annual Bills) [25]

	Cost increase	Gas Disruption Costs	Total
Mid-West / South-West Residential	$78 (20%)	$11 (2.4%)	$89 (22.9%)
Mid-West / South-West Non-Residential	$78 (4.9%)	$47 (2.8%)	$126 (7.9%)
Kalgoorlie – Boulder Residential	$86 (20%)	$11 (2.2%)	$98 (22.6%)
Kalgoorlie-Boulder Non-Residential	$109 (20%)	$17 (2.6%)	$127 (23.2%)
Albany Residential and Non-Residential	$78 (20%)	-	$78 (20%)

76. A key driver for the gas tariff increases was significantly higher wholesale gas prices. The Office of Energy Report assesses:

> "Natural gas commodity costs in the Western Australian domestic market have increased dramatically in recent periods, moving sharply away from historical prices in the $2.50 per GJ range earlier this decade."
>
> "In its analysis provided to the Office of Energy, ACIL Tasman has indicated the view that gas prices have continued to increase beyond the above levels based on consideration of publicly available information relating to the signing of gas commodity contracts between Santos and Moly Metals Australia (for supply of gas from the John Brookes field to the Spinifex Ridge molybdenum and copper mine in the Pilbara region) and also between Santos and CITIC Pacific's Sino Iron project (for supply of gas from the Reindeer gas project to a world scale magnetite mining project). ACIL Tasman has indicated that analysis of the public information on the Moly Metals Australia contract suggests an implied gas commodity price of $6.70/GJ (in 2009/10 dollars), and for the CITIC Pacific contract, a price of $7.80/GJ (in 2009/10 dollars)."[26]

[25] WA Office of Energy, *Gas Tariffs Review: Interim Report to the Minister for Energy*, June 2009, p.3.
[26] WA Office of Energy, *Gas Tariffs Review: Interim Report to the Minister for Energy*, June 2009, pp.14-15.

77. It should be added that the Moly contract was based on a formula linked to international oil prices. The ACG Report therefore assesses the Moly contract to be at $16.20 / GJ (basis US $90 a barrel).[27]

78. The CITIC Pacific contract is also fixed for only three years, with the price thereafter indexed to international oil prices.[28] The $7.80 / GJ price referred to above appears to be based on the contract's assumed oil price of $US 50 a barrel.

79. Major gas producers continue to push for gas prices upwards of $8.50 per GJ, before pipeline transport costs. In contrast, gas prices in Victoria are around $3 - $4 per gigajoule on a delivered basis.

80. Any extension of cartel selling to the Gorgon Project will further entrench the market power of major suppliers. This will lead to higher gas and electricity prices for Australian businesses and households.

81. It will also set back competition in the WA gas market for decades. The ACG Report notes other projects expected to enter the domestic market between 2013-2016 and considers:

"As these projects attempt to enter the domestic market, it may lead to significant change as companies and projects develop marketing tactics. *Gorgon cannot contribute to this 'competitive tension' if joint marketing arrangements have enabled its volume obligation to be locked away.*" (emphasis added)[29]

5.3 The Gorgon applicants' claims of $3 / GJ gas are misleading

82. In its submission of 31 July 2009, the Gorgon applicants assert that price rises in WA are not due to cartel selling and the absence of competition.

83. In justifying their claims, the applicants seek to rely on WA government published data that represents the average of historic contract prices, including those under existing long term contracts. They assert that "the current weighted average price of gas in WA is around US$3/GJ".[30]

84. This is misleading. As the applicants are well aware, the price of gas today is that which is on offer in the current market. It is not the price contained in a contract negotiated 15 years ago.

---

[27] ACG Report, p.5.
[28] Santos, 'Santos signs US$585 million Sino Iron gas supply contract', media statement, 7 January 2009, available at: http://www.santos.com/Archive/NewsDetail.aspx?p=121&id=1122
[29] ACG Report, p.30.
[30] Applicants' submission, 31 Julyh 2009, para.4.16.

85. The applicants have also failed to disclose that many of the major long term contracts which make up those historic contract prices are approaching expiry.

86. In fact, Western Australia will require around 270 terrajoules per day of gas by 2013 to replace existing contracts as they expire.[31] This equates to *a quarter of the State's existing demand*.

87. The applicants have also failed to disclose that Shell and Chevron are, as part of the North West Shelf Joint Venture, actively seeking to significantly increase gas prices under its existing 1998 long term contract with Alinta.

88. In October 2008, it was publicly reported that the North West Shelf participants are seeking to increase the price of gas sold under the long term contract with Alinta. The dispute has proceeded to arbitration.[32]

89. The ASX announcement by Babcock & Brown Power states:

"The contract provides a mechanism for the market value of gas sold under the contract to be periodically reviewed and agreed between the parties or determined by an arbitrator if required by either party following a change in circumstances in the market in which Alinta sells gas."[33]

90. The fact remains that WA gas producers continue to press for wholesale prices above $8.50 per gigajoule (before pipeline transport costs). This compares to $3-$4 *delivered* gas prices in Victoria.

91. It is revealing that strikingly similar claims about WA gas prices were made by Woodside, the North West Shelf Joint Venture operator, in a letter to the *Australian Financial Review* dated 11 August 2009. That letter claimed:

"The vast majority of gas supplied to WA consumers is under long term contracts with price escalation terms that were agreed to at the beginning of those contracts.

As a result, average natural gas prices in WA historically have been much lower than eastern states prices. This continues to be the case. According to information published by the WA Department of Mines and Petroleum, average natural gas prices in WA at the end of 2008

[31] Economics Consulting Services, *Natural Gas Demand Outlook for Western Australia and Economic Impact*, October 2008.
[32] *The Australian*, 'Alinta's North West Shelf dispute in arbitration', 23 October 2008.
[33] Babcock & Brown Power, 'Arbitration subpoena process has commenced in relation to Alinta', ASX Release, 22 October 2008, available at: www.asx.com.au

were around $3.70 per gigajoule compared with $4.10/GJ in the east coast." [34]

92. This highlights the level of information sharing on pricing that is occurring between the supposedly separate and independent North West Shelf and Gorgon Joint Ventures.

93. WA gas consumers would welcome Shell, Chevron and ExxonMobil marketing Gorgon gas at $US 3 per gigajoule gas prices, which they claim to be the "current weighted average price of gas in WA".

6. NEW ZEALAND POHOKURA GAS PROJECT

6.1 Shell's "lack of direct knowledge" of its experience in New Zealand

94. It is noteworthy that in their application, the applicants failed to alert the ACCC to Shell's own practices in New Zealand. The applicants now claim that these practices concerned a separate entity within the Shell Group operating outside Australia and "not within the direct knowledge of Shell" as a participant in the Gorgon Project.[35]

95. It is curious however that in the New Zealand case, separate entity arrangements did not appear to prevent Shell and its Pohokura partners from drawing extensively on experience in the Australian gas market and the North West Shelf Joint Venture case which Shell was a participant in.

96. In fact, Shell and its partners relied almost exclusively on the ACCC's 1998 North West Shelf Determination as the "precedent" to persuade the New Zealand Commerce Commission into granting authorisation for joint marketing.

97. Shell and its partners made extensive reference to the market features identified in the ACCC's 1998 Determination to support their claims that separate selling was not possible, practical or feasible in the New Zealand market.[36]

98. Shell Australia also appears to have had detailed knowledge of matters in New Zealand. According to Shell and its New Zealand partners, Allens Arthur Robinson had "detailed discussions" on behalf of Shell Australia with the applicants in the New Zealand Pohokura case.[37]

---

[34] *The Australian Financial Review*, 'WA gas always low', Letters, Rob Cole, Executive vice-president Woodside Energy, 11 August 2009.
[35] Applicants' submission, para.5.2.
[36] See Shell and its partners' application to the New Zealand Commerce Commission for authorisation for the Pohokura gas project, 20 December 2002; see also the CRA Report commissioned and submitted by Shell and its partners to the New Zealand Commerce Commission.
[37] Applicants' submission to the New Zealand Commerce Commission's Draft Determination in the Pohokura case, 10 June 2003, para.31.

99. It is remarkable that the Gorgon applicants / Shell Australia should claim a lack of “direct knowledge” when Allens Arthur Robinson had “detailed discussions” on behalf of Shell Australia on the New Zealand case.

100. Shell and its partners in the New Zealand case also advised they were inviting Allens Arthur Robinson to comment on Shell’s behalf on any particular issues relating to the Australian experience.[38] Presumably, such comment would have been made with the knowledge of Shell Australia.

101. The Gorgon applicants’ statement of apparent fact to the ACCC that “there is no precedent for a major greenfields gas project such as the Project being separately marketed”[39] should be examined by the ACCC.

102. It is curious that a lack of direct knowledge did not prevent Shell and its Gorgon partners from making extensive reference to the United States and United Kingdom (presumably where separate Shell entities also operate), while ignoring Shell’s experiences in New Zealand - Australia’s close neighbour, with comparable gas market, investment environment and Trade Practices laws.

103. Shell and Chevron have also been compelled by the European Commission to sell separately from a major joint venture in Denmark. Shell and ExxonMobil were compelled to sell separately from a major joint venture in Norway.

6.2 Shell’s *ex post facto* justification of separate selling in New Zealand is unconvincing

104. In seeking to distinguish Shell’s experience in the New Zealand Pohokura case, the Gorgon applicants proffered a number of arguments as to why the Gorgon Project is “not comparable” with the Pohokura Project.

105. These arguments range from technical complexities, environmental differences, to the outrageous claim that there are “no comparable security of supply concerns in WA”.[40]

106. It is axiomatic that every project could ultimately be distinguished from another – whether on the size of the investment, the nature of gas resource, the technical and engineering aspects of the project, the prevailing regulatory environment, the current market conditions, etc.

---

[38] Applicants’ submission to the New Zealand Commerce Commission’s Draft Determination in the Pohokura case, 10 June 2003, para.32.
[39] Applicants’ submission, 20 May 2009, para.7.106.
[40] Applicants’ submission, 31 July 2009, para.5.10.

107. The claims made by Shell and its partners in the New Zealand case, and Shell and its partners in relation to Gorgon are however strikingly similar.

108. The applicants have failed to demonstrate *why* Shell:

- having strenuously argued that separate selling was impossible, unfeasible and not practical in New Zealand because of the supposed market features outlined in the ACCC's 1998 Determination,

- *was subsequently able to sell separately within a short period of time with no delay to project development or domestic gas supply*.

109. They have also failed to demonstrate *how* the supposed market features that it claimed made impossible separate selling, *suddenly changed within a short period of time so as to make separate selling possible*.

110. Furthermore, the Gorgon applicants have failed to respond to Shell and its partners' own evidence in the Pohokura case which considered the Australian and New Zealand markets comparable:

- "The Australian gas markets are described in contrast as 'contract' or 'project' markets where gas is only produced to meet specific contractual obligations. *Like Australia, gas in New Zealand is only produced to meet specific contractual obligations*."[41]

- "Our conclusion is implied by the peculiar nature of the industry and the state of the New Zealand gas market. *It is also the position on joint marketing of gas in Australia, where the market characteristics are similar to those in New Zealand*."[42]

111. The New Zealand Commerce Commission noted that the separate marketing and sale approach did not apparently lead to a delay in the FID or a delay in full production of the field. Rather, any delays were attributable to the *seven and a half months spent attempting*, and failing, to reach agreement on joint marketing and sale arrangements.[43]

112. The Gorgon applicants' arguments about the New Zealand experience are therefore unconvincing. They are no more than an attempt to provide *ex post facto* justification of a claim disproven by Shell's own subsequent actions in selling separately.

[41] Applicants' submission in the Pohokura case, para.20.
[42] CRA, *Coordinated Marketing of Pohokura Gas – An Economic Analysis*, December 2002, p.3.
[43] Synergy submission, 9 June 2009, pp.4-5.

6.3 The distinguishing features claimed by the applicants

113. The applicants' arguments as to why the Gorgon Project is "not comparable" with the Pohokura Project are unconvincing at best and misleading at worse.

114. The applicants claim for instance that the cost of the Project is likely to be "around sixty times more than the cost of Pohokura" and that the sensitivity of the applicants to risks and delays make any comparison to Pohokura "almost entirely meaningless".[44]

115. In making this claim the applicants neglect to mention that domestic gas will only account only a very small proportion of the Gorgon Project – around 5 per cent. The applicants should be asked whether this expected cost is "sixty times more than the cost of Pohokura".

116. The applicants also claim that unlike in New Zealand, "there are no comparable security of supply concerns in WA" with WA having "hundreds of years" of gas.[45]

117. The applicants are well aware that such a claim is patently false. The fact is that WA has been experiencing a serious domestic gas supply shortage since at least 2004 and will continue to do so for many years.

118. The Alliance's 2009 WA Domestic Gas Security Report highlights this:

- Current and prospective gas users in WA are unable to secure long term gas supplies in substantial quantity.
- Major producers are limiting domestic gas contracts to a maximum 6 years, while continuing to sign 20-25 year contracts with overseas customers.
- Major producers are focusing on LNG exports and appear to be withholding gas from the Australian market
- Producers appear to be utilising retention leases to warehouse gas resources for LNG projects when those resources might commercially supply the Australian market.
- Potential new gas field developments are unlikely to meet Western Australia's requirement for over 1100 TJ/day in new and replacement gas by 2014-15.
- Gas resources in the Carnarvon Basin could be depleted within 30 years with unrestricted growth of LNG exports coupled with domestic demand.

---

[44] Applicants' submission, 31 July 2009, para. 5.10.
[45] Applicants' submission, para.5.10.

- If LNG export targets are reached, the total existing resources of the Carnarvon Basin will be fully committed by 2015-2020.

- Where gas is locked up in long term LNG contracts, it is no longer available to meet the needs of Australian industry and households.[46]

119. According to the Australian Bureau of Agricultural and Resource Economics, Australia has just 1.4 per cent of the world's conventional natural gas resources.[47]

120. At *current production*, this equates to 57 years of supply.[48] This figure would not appear to take into account projects like Gorgon, nor the extra six LNG processing trains and additional 77 million tonnes of LNG capacity recently flagged by Woodside.

121. Western Australia accounts for around 80 per cent of Australia's natural gas resources. The State is also the most gas-dependent economy in Australia. Natural gas supplies half of the State's primary energy needs and fuels 60 per cent of the State's electricity generation. In contrast, natural gas supplies 19 per cent of the primary energy needs of Australia as a whole.

122. In claiming there are no comparable security of supply concerns in WA, the applicants have failed to mention recent incidents which highlighted these concerns.

123. In January 2008, an electrical fault at the North West Shelf Joint Venture's gas processing plant at Karratha resulted in domestic gas supply being suspended for more than two days. Shell and Chevron are participants in the North West Shelf Joint Venture.

124. In June 2008, an incident at Apache Energy's Varanus Island plant shut off 30 per cent of the State's total gas supply and resulted in significant economic damage to gas users. The loss of supply resulted in severe costs as companies were forced – to the extent they were able – to switch to alternative gas supplies or energy fuels. Gas users that were unable to do so were forced to curtail or shut down operations, leading to significant job losses.

125. WA's domestic gas security challenges have been extensively examined as part of the 2007 Commonwealth – State Joint Working

---

[46] DomGas Alliance, *Western Australia's Domestic Gas Security Report*, 2009.
[47] ABARE, *Energy in Australia 2009*, available at:
http://www.abareconomics.com/interactive/09_auEnergy/index.html

[48] ABARE, *Energy in Australia 2009*, available at:
http://www.abareconomics.com/interactive/09_auEnergy/index.html

Group process into natural gas supply, as well as a 2007 report by the WA Chamber of Commerce and Industry.[49]

126. They have also been the subject of a 2008 Senate inquiry by the Senate Economics Committee.

127. That the State is experiencing serious security of supply challenges also prompted the WA Government to implement a 15 per cent gas reservation strategy. The WA Government's 2006 Reservation Policy Consultation Paper highlighted these security of supply challenges:

"In order to satisfy Western Australia's domestic gas requirements of around 6.2 Tcf to 2020 (under a 4% annual growth scenario), up to 2 Tcf of gas may need to be sourced from existing and proposed export gas projects.

The Gorgon domestic gas reservation of 1.85 Tcf, in combination with the development of one or two new small domestic only gas projects, should be sufficient to meet this demand.

If Gorgon gas is not available, then the shortfall will need to be sourced from the NWS and/or proposed new LNG projects (e.g. Scarborough).

Beyond 2020 additional gas will almost certainly be required from potential LNG project reserves in order to satisfy domestic gas demand.

On the basis of the above analysis it is clear that WA's forecast gas demand in the medium to longer term can only be satisfied if the State has access to a share of the reserves that have been identified as underpinning existing or potential LNG export projects."[50]

128. The WA Government paper also emphasises the importance of the Gorgon Project in meeting the critical supply shortage – by supplying 1.85 of the 2 Tcf needed by 2020.

129. The applicants' claims that "gas supplied by the Project will augment existing supplies, rather than being the only development capable of countervailing a known supply shortfall" are therefore misleading.

130. The Alliance is not aware of the above or other studies predicting an *oversupply* of gas by 2015 as claimed by the applicants.

131. Such claims nevertheless confirm what appears to have been the practice of major gas producers over many years. Major producers

---

[49] Chamber of Commerce and Industry of Western Australia, *Meeting the Future Gas Needs of Western Australia*, May 2007.
[50] WA Department of Industry and Resources, *WA Government Policy on Securing Domestic Gas Supplies: Consultation Paper*, February 2006, pp.7-8.

have been using, and continue to use, cartel selling arrangements to withhold supply and increase prices for Australian consumers.

132. These concerns were raised with the ACCC as early as 2007 in relation to the North West Shelf Joint Venture cartel. WA gas consumers continue to register these concerns with the ACCC.

6.4 The New Zealand market is a third the size of the WA domestic gas market

133. In their attempts to distinguish the New Zealand experience, the applicants have failed to draw the ACCC's attention to an important fact – that the New Zealand gas market is around *one third the size of the WA gas market*.

134. According to the New Zealand Ministry of Economic Development, New Zealand's gas consumption in 2007 was 153 petajoules PJ.[51] This equates to around 153,000 TJ/year or 420 TJ/d.

135. In contrast, Western Australia's gas consumption averaged around 1,194 TJ/d in 2006-07.[52]

136. This makes the WA market alone almost three times the size of the New Zealand market.

137. Despite claiming the New Zealand market to be too small and too immature, Shell and its partners sold separately with no delay to the Pohokura project or to domestic gas supply.

138. They have failed to demonstrate why they are unable to sell separately for Gorgon when they sell separately in New Zealand:

- a market around *one third the size of the WA market*; and
- which according to their own evidence, is "even less mature than the Australian equivalent".[53]

[51] New Zealand Ministry of Economic Development, New Zealand domestic gas consumption, available at: http://www.med.govt.nz/templates/ContentTopicSummary____21218.aspx
[52] ABARE, *Natural gas consumption by State*, 2008.
[53] 'A Critique of the Commerce Commission's Draft Determination', report by M.D. Agostini, 9 June 2003, p.17, submitted by Shell and its partners in the Pohokura case.

7. FINAL AUTHORISATION

7.1 There is no justification for continuing authorisation after a Final Investment Decision

139. A key element of the applicants' claims is that authorisation for joint selling is necessary to enable them to engage customers prior to a Final Investment Decision. This imperative would no longer apply after a Final Investment Decision is made.

140. It has been clearly established on the evidence that separate selling is commercially practical and feasible.

141. Given there is nothing preventing the applicants – once a Final Investment Decision is made – from selling separately to WA consumers, any authorisation for joint selling should cease with a Final Investment Decision.

142. The ACG Report considers for instance:

> "There appears to be a conflict between the request to jointly conclude agreements for 2000 PJ and "to obtain a firm understanding of the likely level and timing of demand." Given that Interim Authorisation has been granted, it could be argued that when the FID is made, the Applicants should then be required to substantiate why joint marketing should occur. This may be particularly relevant because sales contracts may not be negotiated for some time."[54]

143. This clearly demonstrates that the Gorgon applicants' claims are not based upon any logical reasoning or practical necessity. Cartel selling should be dismissed for what it is – an arrangement to suppress competition and drive up prices for Australian consumers.

144. Interim authorisation should therefore be withdrawn following a Final Investment Decision on the Gorgon Project and final authorisation refused by the ACCC.

7.2 Form of any final authorisation

145. The ACG Report suggests possible options for the form a final authorisation might take should the ACCC decide to grant final authorisation.

146. These include a shorter duration for authorisation, limiting it to a smaller total resource or delivered quantity, or granting authorisation on a case-by-case basis for specific customers (such as buyers seeking more than 50 TJ/day or 10 years).

---

[54] ACG Report, p.30.

147. The Alliance does not consider these options practical or workable. For instance, if the Gorgon applicants were to combine together in marketing for specific contracts or specific resource quantity, it would be impossible to prevent them colluding on this information on pricing, demand and contract terms for other contracts.

148. Given the extremely tight domestic gas market, the applicants are likely to receive significant demand from customers for available gas. It is unclear how they would then apportion joint selling versus separate selling arrangements so that they do not exceed any resource limit for cartel selling set out in the authorisation.

149. Limiting authorisation to "larger" buyers will not protect the tens of thousands of businesses and households that purchase gas and electricity from "larger" buyers like Alinta, Synergy and Horizon Power. These consumers are completely dependent on aggregators like Alinta, Synergy and Horizon Power being able to negotiate on a level playing field with Shell, Chevron and ExxonMobil.

150. Restricting authorisation to a shorter duration will not avoid the significant anti-competitive detriment from cartel selling. As the ACG Report points out, if cartel selling arrangements enable the Gorgon supply commitment to be locked away, the Project cannot contribute to "competitive tension" in the market place in relation to other gas developments.[55]

151. Any contracts negotiated as the result of cartel selling arrangements will establish price expectations for the rest of the WA gas market. The anti-competitive effect will not be limited to an individual contract or volume supply commitment.

152. As the North West Shelf Joint Venture cartel continues to demonstrate, once authorisation is granted and cartel selling arrangements put in place, major producers are extremely reluctant to abandon these arrangements.

153. The NWSJV participants continue to sell as a cartel notwithstanding authorisation for the Incremental Joint Venture lapsed in 2005. WA gas consumers continue to raise concerns with the ACCC about the anti-competitive impact of the NWSJV cartel arrangements.

154. The ACG Report assesses that cartel selling by the Gorgon applicants is not necessary to manage risk or to underpin Gorgon Project investment.

[55] ACG Report, p.30.

155. Separate selling is practical and feasible and should be pursued by the Gorgon applicants. There is no justification for permitting the world's biggest oil and gas companies to sell as a cartel to fix prices for Australian consumers.

List of Attachments

1. Santos, "Santos secures $100 million Newmont gas supply extension in Western Australia", ASX / Media Release, 27 July 2009

2. ExxonMobil, 'ExxonMobil and Petronet sign Gorgon LNG supply agreement', media release, 10 August 2009

3. ExxonMobil, 'ExxonMobil and PetroChina sign Gorgon LNG supply agreement', media release, 17 August 2009

4. WA Office of Energy, *Gas Tariffs Review: Interim Report to the Minister for Energy*, June 2009