



EUROPEAN COMPETITION LAW LNG SUPPLY DESTINATION FLEXIBILITY

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Background

- European Commission's objective is the liberalization of the EU gas market and the creation of a single European gas market – remove commercial practices that entrench market segmentation
- Began to investigate direct/indirect destination restriction clauses in gas/LNG contracts between non-EU suppliers/producers and European companies in the early 2000s
- Historically, LNG SPAs included provisions which directly prevented an LNG Buyer from diverting a cargo, or on-selling regasified LNG, to any destination other than the originally contracted destination (usually an EU Member State)
- Indirect restraints include LNG Seller consent and profit-sharing mechanisms (PSMs)
- EU competition law prohibits agreements and concerted practices between companies which may affect trade between EU member states and which have as their object or effect the prevention, restriction or distortion of competition within the EU internal market



Key European Competition Law Provisions

ANTICOMPETITIVE AGREEMENTS

Article 101

Treaty on the Functioning of the European Union

Prohibits agreements and concerted practices which have as their object or effect the **prevention, restriction or distortion of competition in the internal market** and which **may affect trade between Member States**, unless certain exemptions apply

ABUSE OF DOMINANT POSITION

Article 102

Treaty on the Functioning of the European Union

Prohibits the **abuse of a dominant market position** in the EU or a substantial part thereof **in so far as it may affect trade between Member States**



Commission Antitrust Enforcement

- Jurisdiction of EU competition law is limited to matters affecting trade within the European Economic Area (EEA) - no application if the relevant LNG trade does not affect the EEA
- Commission considers destination restrictions, diversion clauses and PSMs as potential disincentives for an LNG Buyer to divert a cargo from one EU Member State to another EU Member State, which may cause a distortion of competition within the internal market
- Commission's approach has evolved over time through several investigations
- To date, the Commission has:
 - determined that direct territorial/use restrictions in gas/LNG supply contracts can be treated as hardcore restrictions of competition – incompatible with single European gas market
 - developed a framework for analyzing indirect destination restrictions, such as PSMs
- Enforcement has been primarily through settlements (summarised in press releases), rather than infringement decisions, which has led to some market uncertainty



European Antitrust Gas/LNG Investigations

1. Nigeria LNG settlement (2002)
2. ENI and Gazprom settlement (2003)
3. Sonatrach agreement (2007)
4. Gazprom investigation (2015) and decision (2017)
5. Qatar Petroleum investigation (2018)



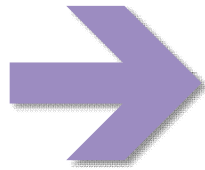
(1) Nigeria LNG Ltd. Settlement: December 2002

“This ground-breaking settlement shows that producers of gas in Nigeria and elsewhere can preserve the essential revenues they derive from the sale of gas in the EU while respecting our competition rules”

(Competition Commissioner, Mario Monti)

Settlement was agreed on the following basis:

TERRITORIAL RESTRICTIONS



- Deletion from an existing contract
- No insertion in future contracts

PSM CLAUSES



- No PSMs in existing contracts
- No PSMs in future contracts

USE RESTRICTIONS



- No use restriction clauses in future contracts

(2) ENI and Gazprom Settlement: October 2003



TRIPARTITE SETTLEMENT

- Between Gazprom and ENI dealing with restrictions in gas supply contracts
- Between ENI and the Commission, setting out market liberalization measures



ENI AND EUROPEAN COMMISSION

- Commitment by ENI to offer significant gas volumes to customers outside Italy over a 5 year period
- ENI undertaking to expand capacity in its majority-controlled Trans Austria Gasleitung (TAG) pipeline
- ENI promotion of an improved third party access regime, facilitating the use of the TAG pipeline as a transit pipeline

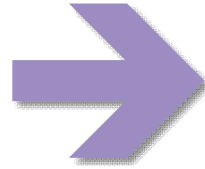


GAZPROM AND ENI

- Deletion of territorial sales restrictions imposed on ENI from all existing supply contracts
- Commitment by Gazprom not to introduce and by ENI not to accept territorial sales restrictions or provisions with similar effect, including use restrictions and PSMs, in future contracts
- Deletion of provision in existing contracts obliging Gazprom to obtain ENI's consent when selling gas to other customers in Italy

(3) Sonatrach Agreement: July 2007

TERRITORIAL RESTRICTIONS



- Deletion from existing contracts
- No insertion in future contracts

PSM CLAUSES



- Only applied in DES LNG SPAs, treated as a change of contract
- No PSMs in future FOB and CIF LNG SPAs
- No PSMs in existing or future pipeline gas supply contracts

Commission determined that the transfer of title and risk in LNG is the key factor in distinguishing between PSMs in LNG SPAs. Once LNG Buyer takes title and risk to LNG, the subsequent application of a PSM would likely amount to a restriction of competition in violation of Article 101 TFEU.

(4) Gazprom Investigation: April 2015

- No restrictions on cross-border gas flows
- ↔ Upon request must deliver gas to/from markets lacking interconnections with EU neighbours
- €€€ Upon request must adjust gas price in line with competitive Western European benchmarks

In April 2015, the Commission sent a Statement of Objections to Gazprom setting out its preliminary view that Gazprom breached EU antitrust rules by pursuing an overall strategy to partition gas markets along national borders in 8 Member States (Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland and Slovakia) which may have enabled Gazprom to charge higher prices in 5 of those Member States

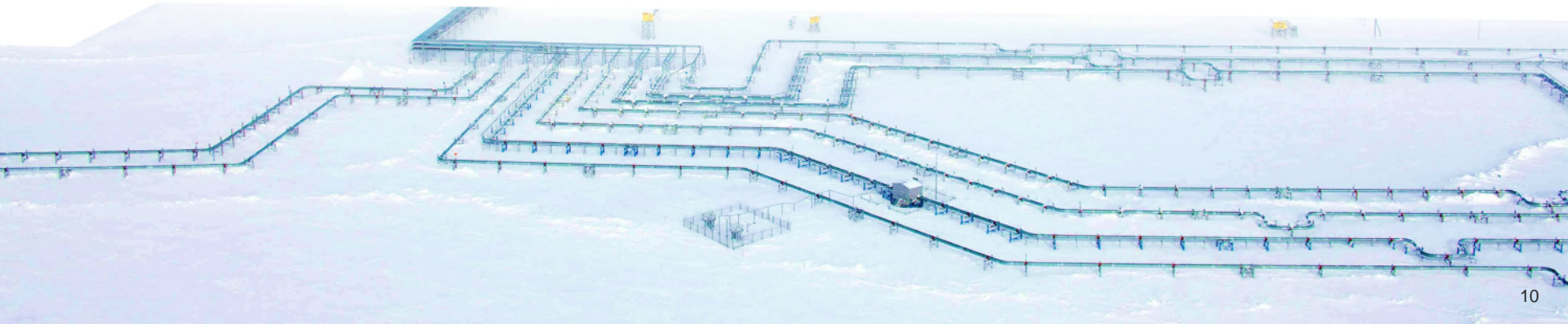


Source (Photos): European Commission

(4) Gazprom Decision: May 2018

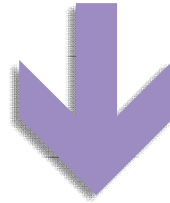
The Commission imposed four legally binding obligations on Gazprom which will be in place for eight years – if any are broken a fine of up to 10% of Gazprom's worldwide turnover can be imposed, without the Commission having to prove an infringement of EU antitrust rules:

1. **Remove Contractual Barriers to the free flow of gas**
2. **Facilitate Gas Flows to and from isolated markets**
3. **Implement Structured Process to ensure competitive gas prices**
4. **No leveraging of Dominant Market Position**



(5) Qatar Petroleum Investigation: June 2018

Qatar Petroleum is the largest supplier of LNG to Europe, accounting for more than 40% of the EU's overall LNG imports



The Commission opened an investigation to determine whether Qatar Petroleum's long-term LNG supply contracts to the EEA contain direct and/ or indirect destination restrictions, including clauses which:

- prevent the diversion of cargoes
- restrict the jurisdictions into which LNG may be sold
- limit the volumes of LNG that may be diverted



The Commission's investigation is ongoing...

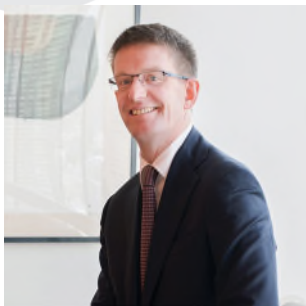
Conclusions

- Commission's approach developed over time to address its key objective of a liberalized and single European gas market
- EU competition law is limited to matters affecting trade within the internal market
- Prohibits agreements and concerted practices which may affect trade between EU Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market
- Direct territorial/use restrictions in gas/LNG supply contracts can be treated as hardcore restrictions of competition – incompatible with single European gas market
- PSMs in FOB and CIF LNG SPAs are considered to disincentivize an LNG Buyer from diverting a cargo from one EU Member State to another EU Member State which leads to a presumption of a distortion of competition within the internal market
- PSMs in DES LNG SPAs constitute a new contractual arrangement, but must be structured not to disincentive LNG Buyer from diverting (raw PSMs v. net PSMs)
- PSMs require the sharing of confidential information which may raise competition concerns in its own right



Any Questions?

Contact



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Honors

- *Chambers Asia-Pacific, Projects & Energy: International (Japan), 2010–2019; Energy & Natural Resources (Asia Pacific Region), 2012–2015 and 2017*
- *Legal 500 Asia Pacific: Japan, Projects and Energy: International Firms and Joint Ventures (Leading Individual) 2016, 2017 and 2019*

Education

- Bachelor of Laws, University of Bristol, 1996, *First Class Honours*

Practice Areas

- Energy
- Infrastructure
- Oil & Gas
- M&A and Private Equity

James Atkin is the global head of Orrick's Oil & Gas practice.

Widely recognized as a leading energy lawyer in Tokyo and Band 1 ranked by Chambers Global, James focuses his practice on helping companies with their international energy investments. He advises clients in the oil and gas sector on transactions in Asia, Australia, the Middle East, Africa and North America, and has extensive experience advising on large-scale oil and gas projects, LNG sales arrangements, and energy-related mergers and acquisitions.

Representative Engagements

Liquefied Natural Gas

- Assisted a Japanese trading company on the negotiation of a liquefaction and regasification tolling agreement for capacity in a planned LNG export facility in the United States, together with all related LNG sale arrangements
- Assisted a Japanese trading company in connection with the off-take and on-sale of LNG from a proposed liquefaction project in West Africa
- Assisted an independent energy company on the negotiation of LNG sales arrangements from the Wheatstone LNG Project in Australia
- Assisted a National Energy Company on the development of a floating storage and onboard regasification project for the import of LNG into a Middle Eastern country

- Assisted an Asian utility company in connection with the negotiation and documentation of various LNG master spot purchase and sales arrangements
- Assisted a project company with respect to the conduct of its marketing and LNG sales arrangements for the development of an LNG project in Gladstone, Queensland, Australia

Upstream – Oil & Gas

- Assisted a Japanese trading company in relation to the acquisition of an interest in the West Qurna 1 oil project in Iraq
- Assisted a Japanese trading company on the negotiation of the license and joint operating arrangements for the development of a gas field in Southern Africa

Regulatory & Infrastructure

- Assisted an Indian energy company on the proposed Ras Issa refinery project in Yemen
- Assisted an oil trader on the acquisition of an interest in a petroleum products storage facility in Aqaba, Jordan

Admissions

- England and Wales
- Registered Foreign Lawyer in Japan

