

**IN THE HIGH COURT OF NEW ZEALAND
WELLINGTON REGISTRY**

CIV-2006-485-1600

BETWEEN TODD POHOKURA LIMITED
 Plaintiff

AND SHELL EXPLORATION NZ LIMITED
 First Defendant

AND OMV NEW ZEALAND LIMITED
 Second Defendant

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Judgment: 13 July 2010 (reissued after confidential release on 5 July 2010 and
 consideration of request for amendment of references to confidential
 material)

**RESERVED JUDGMENT OF
DOBSON J AND PROFESSOR RICHARDSON**

*In accordance with r 11.5 I direct the Registrar to endorse this
judgment with the delivery time of 4pm on the 13th day of July 2010.*

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Introduction

[1] The plaintiff in this proceeding is a member of the Todd Energy Limited group and holds Todd’s interest in the Pohokura joint venture (JV), which is exploiting a substantial oil and gas resource in Taranaki. The first defendant is the Shell entity which holds Shell’s interest in the JV. That company also acts as operator of the field, being contracted to do so by the JV partners. The second defendant is the New Zealand subsidiary of an Austrian-based mining and petroleum company. The parties are conveniently referred to as “Todd”, “Shell” and “OMV”.

[2] The essence of this dispute is an allegedly unlawful constraint on the level of production from the Pohokura field. If it is such, the constraint has operated since the field commenced production in late 2006, with the level of production being supported by Shell and OMV, and opposed by Todd. Of more immediate concern when the proceedings were issued was the refusal by the others to allow Todd to connect its own pipes to the Pohokura Production Station (PPS) in order to transport its share of gas and condensate away from the point of production, except on terms that were objectionable to Todd. In August 2006, a mandatory interim injunction issued in favour of Todd, requiring the others to facilitate Todd’s access, and to connect its separate pipelines.

[3] In essence, by way of 11 causes of action, Todd:

- a) claims that the manner in which the production constraint has been imposed is in breach of the contractual arrangements between the parties;
- b) pleads that in enforcing the production constraint Shell and OMV have breached obligations of good faith owed by them to Todd as a

fellow joint venturer, and, discretely, that Shell has breached fiduciary duties owed by it in its capacity as operator of the Pohokura field;

- c) alleges that the arrangements procured by Shell and OMV as to the level of Pohokura's production are in breach of ss 27 and 30 of the Commerce Act 1986 (the Act);
- d) alleges that the contractual arrangements it objects to are in breach of s 41 of the Crown Minerals Act 1991 (CMA) so that they are illegal and unenforceable;
- e) seeks substantive confirmation of its entitlement to connect separate pipelines for the export of gas and condensate from the PPS;
- f) claims that certain agreements, resolutions and the course of conduct estop Shell and OMV from denying Todd's entitlement to connect those pipelines;
- g) seeks declarations as to the unenforceability or illegality of the sources of the constraints under challenge and orders for the removal of Shell as operator; and
- h) seeks damages quantified variously up to approximately \$320,000,000 for alleged breaches of contract and the Act. In addition, exemplary damages are sought, with a suggested formula of three times the commercial gain made by Shell and OMV from their alleged breaches suggesting a sum in excess of \$600 million.¹

[4] Shell and OMV both counterclaim in respect of the inter-connection rights asserted in e) and f) above, seeking declarations that Todd is not entitled to connect its pipes until it has completed an inter-connection deed on terms approved by them within the JV decision-making forum, but objected to by Todd. In addition, if there

¹ Todd closing submissions, para 30.28.

has been a breach of the CMA, then Shell and OMV seek relief under the Illegal Contracts Act 1970.

[5] Professor Richardson, a Lay Member of the Court, was appointed to sit in respect of the Commerce Act causes of action. Those parts of the judgment considering and determining those causes of action ([297] to [504] below) are our joint work, so that our views in that part of the judgment are appropriately expressed in the plural. Because the evidence on Todd's damages claims was linked closely to the economic evidence on the Commerce Act issues, the Professor has also contributed to the analysis of the damages claims ([505] to [518]). The remainder of the judgment is my sole responsibility. To the extent that our joint reasoning relies upon factual findings in the earlier part of this judgment, Professor Richardson agrees with those findings.

[6] Technical terms and abbreviations used in the judgment are explained as they are first referred to but, for ease of reference, a glossary of those terms is appended at the end of the judgment. Similarly, a review of all the material evidence is not warranted. The first reference to any witness is made in terms identifying the position of that witness and a full list of the witnesses and their positions appears after the glossary of terms. In the preliminary factual review that follows, not all references to the specific evidence in issue have been included. However, where they are relevant to more detailed analyses later in the judgment, such references are provided.

Factual background

History of the field development

[7] In 1995, an exploration permit for the relevant Pohokura area was issued by the Minister of Energy to a member of the Fletcher Challenge Energy group of companies plus Preussag Energie GmbH (a European mining entity) and two other entities. By 1999, the respective interests in the exploration permit had been rationalised so that Fletchers had 66.6 per cent and Preussag had 33.3 per cent. In

July 1999, those two companies completed a JV operating agreement (JVOA) to set the rules for their joint exploration, appraisal, development and production work within the area of the Pohokura permit.

[8] The present parties have succeeded to the interests under the JVOA in proportions that, subsequent to OMV's acquisition in May 2003, can be rounded to Shell's at 48 per cent, and each of Todd and OMV at 26 per cent.

[9] In September 2002, the JVOA was amended to provide for the prospect of joint marketing of gas as a purpose of the JVOA. In December 2002, the joint venturers lodged an application with the Commerce Commission (the Commission) for authorisation of joint gas sales.

[10] At the time the application was made to the Commission, a redetermination of the extent of reserves in New Zealand's then major gas field, Maui, was underway. The view arising out of the redetermination was that reserves in Maui were substantially less than had previously been estimated. In April 2003, the Government issued a policy statement under s 26 of the Act. The implicit effect of this was to encourage the Commission to grant the authorisation sought in circumstances that would facilitate early development of Pohokura as another significant field.²

[11] The policy statement began with an acknowledgement that the Maui redetermination had put economically recoverable reserves at considerably less than earlier industry expectations, raising medium term security of supply issues. The introduction continued:

Gas from Pohokura needs to be available in a time frame and manner that ensures that national energy security and economic growth interests are met.

[12] Under a heading "Energy Security Risks" the statement acknowledged the importance of gas for electricity generation, the extent of additional electricity generation capacity required to meet growth in the economy and that notwithstanding energy conservation and improvement in energy efficiency goals:

² Expert witness material, Volume 3, p18631.

...gas will continue to be an important fuel for electricity generation. It is a premium fuel for large-scale generation plant. Direct use of gas will also continue to be an important component of New Zealand's energy future.

[13] The statement concluded with the following:

Pohokura and the National Interest

Pohokura is the only sizeable commercial field available to meet the requirement for significant quantities of new gas.

The Government recognises that it is not certain that gas from Pohokura will be secured for electricity generation. However, investment decisions on a number of generation projects are currently on hold until there is greater certainty on the future of gas supply. The timely supply of gas from Pohokura is, therefore, important to provide greater certainty over where the gas is used, enabling new generation investment decisions (whether gas or alternative fuels) to be made.

Accordingly, gas from Pohokura needs to be successfully marketed and in production in a timeframe and manner that ensures that national energy security and economic growth interests are met. This is particularly important to ensure that new electricity generation projects can be built in a timely manner to meet growing electricity demand.

[14] In September 2003, the Commission granted an authorisation for the joint marketing of gas, subject to certain conditions, including that commercial production had to commence by 30 June 2006.³

[15] By late 2003, the present parties had also become all of the joint venturers in the Maui field, being commonly referred to in that context as the Maui Mining Companies, or "MMCs". They held interests in different proportions, with Shell having 83.75 per cent, OMV 10 per cent and Todd 6.25 per cent. The original terms of sale for Maui gas involved the MMCs selling all the gas to the Crown, which had negotiated on-sale contracts to various buyers. Those contracts were revisited in the context of the Maui redetermination, in a process that became known as the Strawman negotiations. An issue that was to impact on the parties' respective attitudes to marketing of Pohokura gas was a negotiating point that the MMCs should guarantee delivery of certain quantities of Maui gas.

³ CB3882.

[16] Ultimately, the revised contractual arrangements resulting from the Strawman negotiations involved Shell and OMV providing such guarantees, but Todd not doing so. Once Pohokura gas was available, it could substitute for Maui gas, so Shell and OMV had an interest in reserving some part of Pohokura production to cover for any shortfall on their guaranteed Maui commitments. That was not an interest shared by Todd.

[17] Other relatively fundamental differences arose on the preferred strategies for joint marketing of Pohokura gas. Todd was confident of selling gas on a “take it or lose it” basis. This meant that the seller passed to the buyer the risk that the buyer would not be able, or did not want, to take delivery within defined time frames of the relatively constant quantities it had committed to buy. In contrast, Shell and OMV preferred to offer buyers flexibility as to how much gas they took in any particular period, so that the buyer paid a rate for the capacity to call for the gas, and was incentivised by that payment to take gas, but was not compelled to. Buyers then made an additional payment for the amount actually delivered. Such terms are described as selling with “swing”. I return to the subject of swing in the context of the parties’ opposing views on contractual processes in [82] to [96] below.

[18] The parties were proceeding on the basis that they needed commitments from buyers for a substantial initial tranche of gas from the Pohokura field before they could commit to the very substantial capital required to construct the facilities needed to produce the gas and condensate. Condensate is produced from the same flow of molecules out of the wells, at a rate necessarily dictated by the rate of flow of the gas.

Shell and OMV align

[19] In the earlier period of debate on joint selling, OMV and Todd’s interests appeared to be more aligned. However, in February and March 2004, Shell and OMV developed a view that agreement with Todd on mutually acceptable terms for joint selling of gas seemed unlikely within the time-frame that would be necessary to enable the parties to make a decision on development of the Pohokura field. By late

March 2004, Shell was preparing to market quantities of Pohokura gas on a separate basis, and took marketing advice as to how this might best be done.⁴

[20] On 2 April 2004, Shell and OMV concluded an “Alignment Agreement” pursuant to which they agreed to act together on matters in relation to rules and procedures for the Pohokura JV. A schedule to the agreement specified matters on which Shell and OMV would, in good faith, pursue confidential agreement. These matters included the commissioning of facilities, definition of the rights and obligations to take gas, gas balancing and nomination procedures.⁵ The alignment agreement was to expire on commencement of commercial production from Pohokura. Todd only became aware of that agreement in the course of discovery in these proceedings.

[21] Also on 2 April 2004, each of Shell and OMV wrote to Todd advising that they would no longer pursue negotiations on the terms for joint marketing of gas and, in Shell’s case, stating that it would separately market its share of Pohokura gas.⁶ Until that point, at least the bulk of gas produced was to be disposed of jointly. Accordingly, there had been no pressing need for the parties to address the arrangements that would facilitate a balancing of their separate entitlements to gas, to the extent that production from the field was not apportioned on an hour-by-hour basis in the same percentages as the parties’ respective interests in the venture. However, once the prospect of joint marketing was abandoned, the prospect of arrangements that would allow for various circumstances of “unders and overs” in the parties’ respective levels of off-take of gas became a more relevant issue.

Field Development Plan and Final Investment Decision

[22] In April 2004, a field development plan (FDP) was presented by the then operator to the joint venturers. It was a thorough review of the business case for developing Pohokura, which ran to 187 pages plus appendices. It included

⁴ CB6599-6604.

⁵ CB6908.

⁶ CB6919, 6921.

projections about the level of production of gas.⁷ During April and May 2004, each of the parties concluded conditional contracts for sale of sufficient quantities of their respective gas entitlements to enable them to commit to a final investment decision (FID).

[23] At a meeting on 30 April 2004, representatives of the parties recognised that a gas balancing agreement (GBA), which would provide for inconsistencies in the respective level of gas off-take and procedures for addressing imbalances, was not necessary before the field went into production. However, they acknowledged that such arrangements would desirably be worked on constructively between them.

[24] The FID was unanimously agreed on 30 June 2004. It was made in respect of production facilities that would have a “nameplate” capacity to produce approximately 86 petajoules of gas per annum (PJ/a). In much of the work assessing the feasibility of the development, a working assumption had been made, doing various calculations on the basis of production at a plateau level of 70 PJ/a. There is disagreement between the parties as to the standing of that working assumption.

[25] In October 2004, the Minister of Economic Development issued a permit to authorise exploitation of the field. It appears the parties were aiming to commence commercial production from the field around the middle of 2006. Subsequently, in June 2006, the Commission formally withdrew its authorisation for joint marketing of Pohokura gas.

Gas balancing arrangements/off-take rules

[26] During 2004 and 2005, technical personnel within Todd were keen for a GBA to be concluded, because of the difficulties they foresaw in production occurring without an agreed set of rules for the off-take of production from the field. Those responsible for marketing gas within Todd did not treat a GBA as a necessity, and wanted to resist any proposals that could constrain Todd from taking its maximum proportionate entitlement at all times.

⁷ CB6617-6811.

[27] Similarly within Shell, internal communications from those nearer the technical production areas were urging the need for clear, practical instructions as to how division and off-take of gas was to be managed on a daily basis. Those responsible for managing the relationship with Todd were determined not to compromise on the terms for balancing gas entitlements, for instance resisting any terms that might allow Todd to get ahead of the others in proportionate production in circumstances where there was any risk that the others could not “catch up”.

[28] In November 2005, Shell proposed a form of GBA, intending that the joint venturers agree on arrangements for off-take, allowing for “unders and overs” relative to each party’s proportionate share of production of gas.⁸ Todd pursued initiatives to have a GBA on different terms accepted by the other joint venturers,⁹ but ultimately no gas balancing arrangements were agreed between them.

[29] Throughout the period of the present joint venturers’ work at Pohokura that has been reviewed thus far, the joint venturers had retained Shell Todd Oil Services Limited (STOS) as operator. That company, jointly owned by Shell and Todd, was also acting as operator for other ventures in Taranaki, including Maui and Kapuni. In August 2005, Shell and OMV voted to remove STOS as operator at Pohokura, and appoint the first defendant Shell company as the operator instead of STOS. That change, which was part of a wider campaign by Shell to reduce Todd’s influence over, and involvement in, the operation of Taranaki petroleum fields, was opposed by Todd. Court proceedings challenging the change were unsuccessful in respect of Pohokura, but successful in respect of Maui.¹⁰ The change in operator at Pohokura became effective from 1 April 2006. The joint venturers’ primary point of liaison with the operating company was by way of an operating committee, on which all of the joint venturers were represented.

[30] In late 2005, various committees of representatives of the joint venturers had before them, as an aspect of their commercial readiness plans for the production of gas, certain draft off-take rules providing for the mechanical processes for

⁸ CB9505, 9509.

⁹ CB9843.

¹⁰ *Todd Petroleum Mining Co Ltd v Shell (Petroleum Mining) Co Ltd* HC Wellington CIV-2005-485-819, 14 December 2005.

nomination of quantities of gas per hour and per day, and the procedures by which the operator would respond (nomination protocols). I find that Shell and OMV reached a common view about the content of such rules, in the course of dialogue that did not include Todd. In January 2006, Mr Murray Jackson, a contract support manager for Shell’s upstream companies, proposed separately to OMV a version of “off-take rules” that would allow underlift and overlift, “(albeit minimalist)”.¹¹

[31] Then in February 2006, Shell circulated draft off-take rules and nomination protocols to the joint venturers with a proposal that they be debated and agreed by the operating committee.¹² Todd’s immediate internal reaction was that the form of balancing would “...result in significant loss of value and liquids for Todd”.¹³

[32] At a meeting of the operating committee on 3 March 2006, the off-take rules were approved. Shell and OMV voted for the resolution to implement them. Todd voted against the resolution.¹⁴ Todd’s opposition was based on legal advice to the effect that the proposed rules conflicted with the rights and obligations of the parties under Article 10.1 of the JVOA, and as such the rules would need unanimous agreement. In addition, Todd saw the proposed rules as being in breach of the terms of the mining licence.¹⁵

[33] At a meeting of the operating committee on 26 April 2006, the majority of Shell and OMV resolved to adopt and be bound by, and to direct the operator to implement, a set of nomination protocols.¹⁶

Export pipelines

[34] The FDP had contemplated joint pipelines to export the processed gas and condensate from the PPS. STOS originally had a contract for construction of such a

¹¹ CB10305.

¹² CB10497.

¹³ CB10519.

¹⁴ CB10835-10837.

¹⁵ CB10828-10833.

¹⁶ CB11393.

new pipeline on behalf of the Pohokura JV. These proposals contemplated the acquisition of certain redundant pipelines from Methanex. Methanex is an international business that has been active in Taranaki in extracting methanol from natural gas, and exporting it. In April 2005, Methanex withdrew from negotiations to sell those pipelines to the Pohokura JV, and in July or August 2005 Shell and OMV separately formed another JV (EPJV) to provide pipeline services for those two parties. The EPJV was able to purchase the redundant pipelines from Methanex. The FDP was amended by an operating committee resolution in August 2005, to accommodate separate arrangements for the export of products.¹⁷

[35] Those August 2005 resolutions reflected the prospect, then confronting Todd, of the requirement for it to construct its own pipelines (assuming it would not be able to negotiate satisfactory terms for use of the EPJV's pipelines). One of the August 2005 resolutions allowed the operator to make all consequential changes to the FDP in order "to accommodate the export of gas and liquids through the export pipelines proposed by the EPJV and/or Todd Pohokura Limited or any other lines that may be used for this purpose".

[36] Physical works on both sets of pipelines proceeded. In May 2006, Shell and OMV passed by a majority vote a further resolution requiring any party wishing to connect a pipeline to the PPS to enter into a particular form of inter-connection deed. Todd's objection to the form of deed was in part because it incorporated the nomination protocols and, by reference, the off-take rules. Todd's refusal to complete the inter-connection deed led to a stand-off in which the operator declined physical access to Todd contractors, for the purpose of connecting their pipelines to the PPS. This stand-off resulted in the interim injunction hearing in August 2006.

[37] The JVOA provided for the operator to propose a work programme and budget (WP&B) in respect of each year, for debate and approval by the operating committee comprised of representatives of the joint venturers. The first WP&B for the 2006 year was initially drafted in November 2005, with versions subsequently issued to the operating committee in May and June 2006. It was unanimously

¹⁷ CB8731-8739.

approved on 28 June 2006, although subject to reservations recorded by both OMV and Todd.¹⁸

[38] The pattern established in the first WP&B has been maintained since then. Each subsequent WP&B has proposed a level of production consistent with the projections in the FDP and FID documentation. Each WP&B has been objected to on behalf of Todd, as wrongly constraining the extent of production that Todd is entitled to call for.

Todd's contract causes of action

[39] The initial imperative when the proceedings were commenced was Todd's wish to gain inter-connection. Accordingly, the first four of the 11 causes of action alleged a variety of grounds for Todd's entitlement in that regard. However, the primary focus throughout the substantive hearing was on Todd's claimed entitlement to greater volumes of gas than has been produced, and it is appropriate to deal first with the issues arising under that broad heading.

[40] Todd's fifth cause of action pleads an extensive list of criticisms of the off-take rules and nomination protocols. Todd pleads that their purpose or effect was to limit production to less than was available. Todd contends that the rules and protocols are outside the power of the operating committee on a variety of grounds, including that they are beyond the powers it has under Article 5.2 or, if within Article 5.2, were not valid because they were not necessary or were inconsistent with New Zealand law or the permit. Discretely, the rules are alleged to be in breach of the Commerce Act, but that challenge depends on the second part of the case. In addition, implementation of the off-take rules and nomination protocols is alleged to breach particular provisions of the JVOA and voting for them was in breach of obligations of good faith pleaded to be owed by each of the JV partners to the others.

[41] The sixth cause of action pleads that the terms of the JVOA limit the scope of what the operator can undertake to matters that constitute joint operations within the

¹⁸ CB12331.

scope of the JV. Such work must all be done in accordance with the terms of the JVOA, the permit, the CMA and any instructions of the operating committee given to the operator, so long as they do not conflict with the JVOA. For these and other reasons, the 2006 to 2009 WP&Bs are claimed to be invalid and not binding on the joint venturers.

[42] In both the fifth and sixth causes of action, Todd pleads that the operator is obliged to conduct joint operations in a diligent, safe and efficient manner in accordance with good and prudent oil and gas field practice. The limits on production (relative to the larger capacity of the field to produce) reflected in the 2006-2009 WP&Bs allegedly breach such obligations owed by the operator. The approval by the operating committee of those WP&Bs is alleged to have been invalid and voting in favour of them by Shell and OMV was in breach of implied obligations of good faith. Both causes of action also allege that Shell and OMV's failure to take their full equity share of total production available breaches an obligation imposed on each of them under Article 10.1 of the JVOA to do so.

[43] The seventh cause of action claims that, in its capacity as operator, Shell owes Todd fiduciary obligations. Such obligations are said to have been relevantly breached in the conduct leading to a "constrained level" of production being made available to Todd.

[44] To assess the detail of these three contractual causes of action, it is appropriate to describe the genesis and structure of the JVOA and the off-take rules, and some relevant features of how production has occurred at Pohokura, before assessing the meaning of the specific terms relied upon by Todd.

The JVOA

[45] The terms of the JVOA are based substantially on a 1995 model produced by the Association of International Petroleum Negotiators (AIPN). That model form of joint operating agreement appears to be widely used as the starting point for such contracts, having been drafted by a United States-based international non-profit organisation. It is intended for use outside the United States, Canada and the United

Kingdom. A clause-by-clause comparison between the model form of contract and the present JVOA reveals that there have been relatively modest changes from the model form.

[46] Both Todd and Shell sought to adduce evidence from United States academics and/or practitioners specialising in oil and gas contracts. However, I upheld an objection on behalf of OMV to the admissibility of evidence from these experts, given that the essential purpose of the proposed evidence was to address contractual interpretation as a matter of New Zealand law. I did acknowledge that the respective parties might use the opinions from the experts they had retained as supplements to their legal submissions, and I revert to points relevantly made as part of the arguments on interpretation of the terms of the JVOA at [139].

[47] None of the present parties was involved in the JV at the time the JVOA was originally concluded. In that sense, the JVOA is inherited and there is accordingly no relevant factual matrix affecting the circumstances in which its terms were originally drafted for these parties.

[48] There have been two amendments to the terms of the JVOA, the first in 2002 and the second in December 2004. Again, there is no compelling factual matrix relevant to the current contractual dispute by way of context in which those changes were agreed.

[49] The scope of the JVOA, as originally entered into in July 1999, was reflected in recital E which originally specified as follows:

The Parties now wish to enter into this Agreement for the purpose of forming a joint venture, appointing an Operator, carrying out exploration, appraisal, development and production work and defining their respective rights, interests and obligations in respect of the exploration for Petroleum and the appraisal, development and production of any Discoveries in the Permit Area.

[50] On that original scope, the joint venturers were agreeing to pursue together steps up to the production of “petroleum” which is given the meaning ascribed to it by the CMA, and in practice extends to all natural gas and liquid hydrocarbons (respectively “gas”, and “condensate” or “oil”). The 2002 amendment to the JVOA

expanded the scope of the venture by adding to the last words of the recital as follows:

...development, production, marketing and sales of any discoveries in the Permit Area.

That, and other changes made at the time, were intended to facilitate use of the JVOA to regulate joint marketing of gas.

[51] Article 1 contains some six pages of definitions of words and terms used in the JVOA. Reference is made to some of those later, as they become relevant in interpreting the JVOA.

[52] The JVOA was to continue in effect “for so long as the Permit remains in force and until all joint property has been removed and disposed of, and final settlement has been made amongst the Parties”.¹⁹

[53] The scope of the agreement was defined in Article 3.1, which began:

(A) The purpose of this Agreement is to establish the respective rights and obligations of the Parties with regard to operations under the Permit, including without limitation the joint exploration, appraisal, development and production of Petroleum from the Permit Area.

[54] Article 3.1 then specified a list of activities that were outside the scope of the agreement. The list included the construction and operation of any facilities downstream from the point of delivery of the parties’ shares of oil, and transportation of oil, in both cases, beyond the point of delivery, which was to be provided for in an off-take agreement for oil that was to be resolved in terms of Article 10.2 of the JVOA.

[55] Article 3.3 is headed “Ownership, Obligations and Liabilities” and begins:

(A) Unless otherwise provided in this Agreement, all the rights and interests in and under the Permit, all Joint Property and any Petroleum produced from the Permit Area shall, subject to the terms of the Permit and the Act, be owned by the Parties in accordance with their respective Participating Interests.

¹⁹ Article 2.

[56] Articles 4.2 and 4.3 dealt respectively with the rights and duties of the operator. Article 4.3(A) provides that in the conduct of joint operations, the duties of the operator are to include 18 specific duties that are then described. These include:

- (1) Perform Joint Operations in accordance with the provisions of local laws, rules and regulations, the Permit, the Act, this Agreement and the instructions of the Operating Committee not in conflict with this Agreement;
- (2) Conduct all Joint Operations in a diligent, safe and efficient manner in accordance with good and prudent oil and gas field practice and environmental and conservation principles generally followed by the international petroleum industry under similar circumstances;
- ...
- (5) Perform the duties for the Operating Committee set out in Article 5, and prepare and submit to the Operating Committee the proposed work programs and budgets and AFEs* as provided in Article 6;
- (6) Implement such work programmes and budgets as shall, together with the relevant AFEs*, have been approved by the Operating Committee;

...

(* The role of AFEs, authorisations for expenditure, is described in [63] below.)

[57] Article 5 of the JVOA makes provision for the operating committee, beginning in Article 5.1 with provision for its establishment:

To provide for the overall supervision and direction of Joint Operations, there is established an Operating Committee composed of representatives of each Party holding a Participating Interest of 15% or more...

[58] Article 5.2 then addresses the powers and duties of the operating committee:

The Operating Committee shall have power and duty to authorize and supervise Joint Operations that are necessary or desirable to fulfil in a timely manner the terms of the Permit and properly explore and exploit the Permit Area in accordance with this Agreement and in a manner appropriate in the circumstances. Without limiting the generality of the foregoing, but subject to the other provisions of this Agreement, the powers and duties of the Operating Committee shall include:

- (1) the consideration and the determination of all matters relating to general policies, procedures and methods of operation under this Agreement including the Safety, Health and Environmental Policy;

- (2) the consideration, modification and approval or rejection of all proposed Exploration, Appraisal, Development and Production Work Programmes and Budgets, Development Plans and AFEs (including the amount of detail provided therein) prepared and submitted to it pursuant to the provisions of this Agreement;
- (3) the determination of the timing, location objection and depth of all wells drilled as part of the Joint Operations and any change in the use or status of a well; and
- ...
- (5) the determination of whether or not to proceed with Development Operations in respect of any Discovery and the manner in which such development shall be carried out.

[59] Article 5.3 provides that the representative of any party is authorised to represent and bind that party, and that representatives for all parties who have a participating interest of 15 per cent or more are entitled to vote and have a vote equal to the participating interest of the party that that person represents. Article 5.9 provides for a voting procedure in which decisions may be made by a majority vote of two or more parties having individually or in aggregate a participating interest of not less than 65 per cent (in the circumstances of the shares that have pertained at all relevant times), subject to defined exceptions. Article 5.9 also specifies those exceptions, in that the vote of all parties shall be required in respect of any proposal to approve a development plan, voluntary release or surrender of the permit, and any extension or renewal or unitisation of the permit.

[60] Subject to defined exceptions that are irrelevant for present purposes, Article 5.14 specifies that decisions taken by the operating committee "...shall be conclusive and binding on all parties". The operating committee is the only forum provided for in the JVOA in which decisions about the operations of the JV can be made. Therefore, except on the few fundamental decisions on which Article 5.9 requires unanimity, the venturers all have to comply with majority decisions on matters within the scope of the JVOA.

[61] Article 6 deals with WP&Bs. First, in Article 6.1 with regard to the exploration and appraisal phase, and second in Article 6.2 with regard to development. Article 6.2(A) requires the operator to deliver a development plan to the parties with a first annual development work programme as soon as practicable

after an operating committee determination that a discovery should be developed. The operating committee is then required to approve or not approve the development plan. That is one of few decisions required by Article 5.9 to be made unanimously. Once a plan is approved, subject to the parties obtaining a mining permit in respect of the discovery, “each party shall be committed and obliged to proceed with it”.²⁰

[62] The next phase, production, is provided for in Article 6.3, paragraph (A) of which provides:

- (A) At least two months before the commencement of production and thereafter before the end of each Permit Year, Operator shall deliver to the Parties a proposed Production Work Programme and Budget detailing the Joint Operations in respect of production to be performed for the following Permit Year and the projected production schedule for the following Permit Year, and which is intended to be firm for the following Permit Year, together with a contingent Production Work Programme and Budget for the succeeding Permit Year and tentative Production Work Programmes and Budgets for the following 2 Permit Years, to enable estimation of annual revenues and budgets by the Parties and the intended staffing plan, (for information purposes). Within 30 Days of such delivery, the Operating Committee shall meet to consider, modify and then either approve or reject that proposed firm Production Work Programme and Budget. Approval by the Operating Committee of that proposed Production Work Programme and Budget will commit and oblige all Parties to proceed in accordance with it.

[63] Within an approved budget, Article 6.6 of the JVOA also provides for the operator to notify all non-operator parties of proposed commitments or expenditure in excess of \$50,000, excluding general and administrative costs that may be listed as separate line items in an approved WP&B. These “AFEs” afford the operating committee an on-going opportunity to oversee the expenditure of the parties’ money by the operator and again, once the operating committee has approved an AFE, each party is committed to the expenditure involved.

[64] By Article 9, any party that fails to pay a funding requirement for the operator in full is deemed a defaulting party, and such a party is not entitled to attend operating committee meetings or to vote on any matter until the default has been remedied.

²⁰ Article 6.2(D).

[65] Article 10 then deals with what the heading describes as “DISPOSITION OF PRODUCTION”. First, it provides in Article 10.1 as follows:

Article 10.1 Right and Obligation to Take in Kind

Except as otherwise provided in this Article 10 or in Article 9, each Party shall have the right and obligation to own, take in kind and separately dispose of the share of total production available to it under this Agreement in such quantities and in accordance with such procedures as may be set forth in the offtake agreement referred to in Article 10.2 or in the special arrangements for Natural Gas referred to in Article 10.3 provided that Operator shall have the right and authority in conducting the Joint Operations to use or flare as much Petroleum as may be reasonably required by it, and the quantities so used or flared shall be excluded from production estimates to be provided by Operator.

[66] The 2002 amendments to the JVOA included inconsequential changes to the terms of Article 10.1, removing the article before “Operator” in the seventh and last lines as the clause is reproduced above, and capitalising the reference to “natural gas” in the sixth line.

[67] Article 10.2 is headed “Offtake Agreement for Crude Oil” and its opening paragraph provides as follows:

If Oil is to be produced from the Permit Area, the Parties shall in good faith, and not less than three (3) months prior to the first delivery of Oil, negotiate and conclude the terms of an agreement to cover the offtake of Oil produced from the Permit Area. This offtake agreement shall, to the extent consistent with the Act and the Permit, make provision, interalia, for:

That is followed by eight matters that are to be addressed in any such off-take agreement in relation to oil, such as delivery point, the process for the operator to provide periodic advice of estimates of total available production, inventory and overlifts and underlifts, nominations by the parties to the operator, elimination of overlifts and underlifts, and a process by which other parties might sell an entitlement to which one party fails to nominate.

[68] The first of the matters provided for was in the following terms:

- (A) The delivery point, at which title and risk of loss of Participating Interest shares of Oil shall pass to the Parties interested (or as the Parties may otherwise agree);

[69] “Participating Interest” is a defined term in Article 1, meaning:

...in respect of each Party the undivided interest expressed as a percentage held from time to time by that Party under this Agreement in the Joint Operations, Joint Property and all or any rights, property, obligations or liabilities in connection with the same.

[70] Article 10.2 concludes with the provision:

If an offtake agreement has not been entered into by the date of first delivery of Oil, the Parties shall be bound by the principles set forth in this Article 10.2 until an offtake agreement has been entered into.

[71] The heading of Article 10.3 is simply “Natural Gas”. Its current wording is as follows:

The Parties may enter into special arrangements for the disposal of Natural Gas which are consistent with the Development Plan and subject to the terms of the Permit. These arrangements may provide for joint marketing and sales of Natural Gas as may be agreed between the Parties from time to time.

[72] As originally completed, this provision of the JVOA was as follows:

The Parties recognise that if Natural Gas is discovered it may be necessary for the Parties to enter into special arrangements for the disposal of the Natural Gas which are consistent with the Development Plan and subject to the terms of the Permit.

[73] Other relevant provisions include Article 15.1 which declares all the rights, duties, obligations and liabilities of the parties to be several, not joint or collective, states that each party is to be responsible only for its individual obligations, and records the parties’ “express purpose and intention that the ownership of their respective interests shall be as tenants in common in undivided shares”. That article also negatives the agreement being construed as creating a partnership, and stipulates that in their relations with each other under the agreement the parties are not to be considered fiduciaries except as expressly provided.

[74] Article 19 provides that the applicable law of the agreement is the law of New Zealand.

The Off-take Rules and Nomination Protocols

[75] The 3 March 2006 resolution of the operating committee was on terms that the parties “...adopt, be bound by and implement, and to direct the operator to implement, offtake rules in accordance with and on the basis set out in the following paragraphs”.²¹ The rules first provided that the WP&B required to be delivered by the operator was to include the operator’s assessment of the total production available for the relevant year, the share of that available to each venturer, and the operator’s assessment of the minimum daily gas off-take required to maintain continuous gas deliveries for each day of the year.

[76] The operator was also to advise the parties four working days prior to the commencement of each calendar month of the expected maximum daily availability (MDA) for each day in the immediately succeeding month, and estimated MDA for each day in the two further months thereafter. That notification was also to advise any amendment to the operator’s assessment of the minimum daily gas off-take required to maintain continuous gas deliveries.

[77] The resolution next contemplated that the operator would propose nomination protocols. These were to set out how the parties were to convey nominations for the amount of gas to be delivered to them each day, and within individual days. The off-take rules contemplated that each daily nomination provided by a joint venturer had to be for a quantity equal to or greater than that party’s share of the minimum daily gas off-take and for equal to or less than that joint venturer’s share of the MDA, as currently advised by the operator. If any nomination was not within those parameters then, where it was for less than that party’s share of the minimum off-take, the quantity nominated would be delivered if the combined quantity of nominations of all parties was in excess of the minimum daily gas off-take. If the aggregate of the nominations was less, then the nomination by the party whose nomination was below its share of the minimum would be treated as a nomination for the minimum amount required to get total delivery up to the minimum daily gas off-take. Where the nomination was for greater than a party’s share of MDA for that

²¹ CB10835-10837.

day, then the operator would deem the nomination to be for the amount equal to that party's share of MDA for the day.

[78] However, in a separate paragraph the operator was to reject any nomination if it sought delivery of an amount of gas which, when added to that party's share of the estimated minimum daily off-take for each day in the remainder of the year, would result in that party exceeding its share of the total production available for the whole year. (In other words, the operator would monitor the level of production going to each party, and prevent any deliveries that would result in "overlifting".) That constraint was subject to a further separate paragraph providing that in the event of an underlift in any year by a party, that party would be permitted to nominate for a quantity of gas greater than its share of the total production available in the following year, but only to the extent that such nominations enable the party to recover its underlift in the sense of getting back into balance. The right to recover underlift was limited so that it could not occur where it would prevent another party from accessing that party's share of total production available in any year.

[79] The rules then separately provided:

Liquids are to be lifted by each PJVer in accordance with its percentage Participating Interest (regardless of gas nominations) and the principles of Article 10.2 of the JVOA.

[80] As contemplated in the 3 March off-take rules' resolution, nomination protocols in relation to the implementation of the gas off-take rules were circulated and resolved by a Shell/OMV majority at a further operating committee meeting on 26 April 2006.²² These protocols set detailed rules for the timing and content of nominations that each party was to send to the operator, first for a rolling 12 month basis as to forecasts of off-take demand monthly, then for a rolling 28 day period on a weekly basis. In addition, there are separate nominations for the daily gas delivery requirements for the following week, with an additional requirement to give notice of any changes in gas delivery requirements for any given day, before 1pm the day preceding the day of delivery. To the extent intra-day nominations were allowable under the Maui pipeline operating code, if a joint venturer sought to change its

²² CB11395.

nomination within a day, it was to advise the operator 60 minutes before any intra-day nomination cycle under the Maui pipeline operating code.

[81] As to obligations after deliveries had occurred, the nomination protocols required the operator to determine and advise each party of the allocated gas quantity, the total metered gas quantity through the export points and any calculated imbalance. There was a similar obligation on the operator to forward to each party a summary of that party's "current gas balancing position".

The relevance of swing to the level of production

[82] Many potential purchasers of gas have fluctuating levels of demand, by hour, day, week or season. On the other hand, most large purchasers will have a constant base-load demand (a "flat profile") and varying levels of demand above that base-load, depending on their business circumstances. Mr David Hunt, called by OMV as an independent expert in relation to gas usage and demand in New Zealand, produced a graph illustrating observed daily demand for gas in the period between September 2006 and September 2009. That graph is reproduced as Appendix 3 at the end of this judgment. Mr Hunt accepted in cross-examination that the graph demonstrates that there was a constant base-load demand for approximately 250,000 gigajoules per day,²³ with fluctuations going as high on some winter days as more than twice that, and an average calculated at somewhat more than 400,000 gigajoules per day. Todd's approach implicitly seeks to fulfil that base-load demand, whereas Shell and OMV seek to sell on terms that will attract buyers whose usage includes the substantial fluctuations above the "base-load" level.

[83] Within the New Zealand gas market, there has thus far been no material capacity to store gas. Terms of sale that permit fluctuating levels of gas to be delivered, commonly referred to as "swing", would therefore be important to such purchasers in a market where there has not been any material capacity to store gas.

²³ T3313/16.

[84] Shell and OMV were in favour of offering swing, but Todd opposed doing so. Projections as to the level of production during the period in which the parties proposed joint marketing of the Pohokura gas contemplated 70 PJ/a with the difference between that level and the plant's capacity being treated as available to provide for swing, and for short term spot sales of gas. For instance, a technical analysis undertaken by Mr Rogers of Todd, and circulated to the other parties by Mr Chris Hall, Todd's in-house counsel, dated 5 January 2004 noted:²⁴

At present, the contract discussions have focused on Tranche 1 and JV uplift being sold for a 4 year period. Based on 70 PJ/a throughput with 15% swing means that a minimum 80.5 PJ/a deliverability needs to be maintained for the 4 year sales period.

[85] After joint marketing had been abandoned, separate contracts were entered into by each party in April and May 2004. Todd sold more or less on a flat profile, "take it or lose it" basis, involving full payment for all volumes sold. This was for its share of 70 PJ/a. Both Shell and OMV sold gas on terms that incentivised buyers to take the majority, or all, of their gas, but did not require the buyers to pay the full price for the higher volumes of the gas if it was not taken in any particular period. OMV sold marginally more than its share of 70 PJ/a, and acknowledges that it has infrequently had to buy other gas to top up the quantities it is committed to supply. This presumably occurs when its buyers demand all of the "swing" capacity contracted for. In Shell's case, if the buyers exercised their "swing" rights to take all the gas contracted for, Shell would have to deliver equivalent to its share of the plant's capacity (ie 86 PJ/a). In a 24 May 2004 internal email, Mr Bansal described the terms of sale as highly flexible, enabling Shell to sell up to its share of plant design capacity at its discretion.²⁵ Accordingly, Shell's terms of sale could also require it to deliver more than its proportionate share of production from Pohokura at 70 PJ/a.

[86] At the time of those contracts, Shell and OMV were concerned to reserve some capacity from Pohokura to cover any shortfall in the guaranteed commitments they had assumed under the re-negotiated contracts for sale of Maui gas. However, there is no evidence that increases from the planned levels of production have

²⁴ CB5171.

²⁵ CB7423.

occurred at Pohokura either to facilitate delivery at the top end of “swing” allowances in Shell or OMV contracts, or to supplement Shell or OMV Maui obligations. Nor is there any evidence of any party concluding short term or spot sales of Pohokura gas.

[87] A review of overall annual quantities actually delivered compared to projected levels of production is not sufficient to address shorter-term fluctuations in demand. It is not possible to get a clear sense of the extent to which fluctuations in the level of demand require a margin between the notional or average rate of production, and the peak rates needed to accommodate demands for the maxima permitted within the swing tolerances, if, for instance, all Shell and OMV customers required the maximum entitlement at the same time. An earlier report in July 2003 proposed a swing factor of 25 per cent.²⁶

[88] A further graph (Figure 19) produced by Mr Hunt is also reproduced in Appendix 4 at the end of this judgment. It represents the swing ratios for major New Zealand gas fields, and Mr Hunt’s key points regarding the observed swing ratios are endorsed under the graph. It shows that on all of daily, weekly and four weekly measurements, Todd’s Pohokura production involves somewhat higher levels of swing than those of Shell and OMV. It further shows that the shorter the period measured, the higher the ratio of swing. Therefore, levels of swing at Pohokura measured on a daily basis appear to exceed 30 per cent whereas weekly and four weekly fluctuations range a little above and below 20 per cent.

[89] In terms of ability to manage fluctuating demand, it is also relevant that Todd enjoys sole control of its McKee and Mangahewa fields (M&M), which provides Todd with its own alternative source of swing. The May 2004 Todd Energy Board Paper recommending support for FID acknowledged running its gas interests on a portfolio basis, with substantial capacity to substitute Pohokura gas for M&M.²⁷

²⁶ CB2541.

²⁷ CB7454-7455.

[90] Todd's thinking is also reflected in an email sent by Hamish Tweedie on 28 June 2006 to 12 others within Todd, on the subject of "Gas Portfolio Dispatch".²⁸ Mr Tweedie's proposals set out in merit order the fields from which gas should be drawn. The first was Pohokura that was addressed in the following terms:

Pohokura: This is the first field to be dispatched. Obviously this depends upon balancing arrangements (which are very limited at the moment and we contest are simple .. use it or lose it until later) and consequently may be moderated if balancing occurs. Given that this is probably going to be the most expensive field to operate, the tightest obligation to uplift (as we interpret it) and the richest in liquids over the next few years then maximum uplift from this field optimises the value and reduces current (as we can backup from other fields) and future (we have trouble accessing our gas at the tail of the field) risk.

[91] Mr Tweedie then addressed Kapuni which he identified as the second field in the merit order to be dispatched, before commenting on M&M in the following terms:

M&M: This is obviously our swing field where we have maximum flexibility and control (both from the point of control and reinjection). We would prefer to bank gas here as it is more flexible, we have control and it should be the lowest cost operator (as we operate and control) and thus less financial pain if we close it in. Furthermore if we want to bring other projects online such as Karewa then we may need flexibility, and thus I presume the more reservoir energy we bank in this field the more flexibility we will have for the future (when it will be at its more valuable).

[92] Mr Tweedie acknowledged the different perspective Todd's portfolio gave it, when compared with OMV, in the observation:

OMV would like swing at Pohokura as they do not have adequate diversity of off-take contracts or any back-up from elsewhere...

[93] Mr Tweedie's concluding paragraph acknowledged that:

...it may be rare that we fully utilise M&M...

[94] When I questioned Mr Tweedie about the views conveyed in the email, he suggested that it reflected worst case scenarios in a period of uncertainty.²⁹

²⁸ CB12323.

²⁹ T1524/9-11.

However, I was not persuaded that the situation being addressed in June 2006 was atypical, and am satisfied that it is a representative example of Todd's internal view on the respective rates of extraction of gas from its various interests, in the period relevant to these proceedings.

[95] Mr Richard Tweedie saw Todd as having a competitive advantage over Shell and OMV by being able to offer increased flexibility and security across a portfolio of fields.³⁰ I find that Todd's firm stance against swing being offered in Pohokura contracts was influenced by its own capacity to provide swing by fluctuations in the level of production at M&M.

[96] Shell and OMV's preference for swing is supported by economists' analysis that the assets of the Pohokura field include its capacity to provide storage of gas, so that full utilisation of those assets is not achieved unless the gas is sold on terms where additional value is extracted from purchasers for storing gas by means of permitting fluctuating levels of delivery. It follows that sales on terms providing swing to an extent that requires a limit on the average production level at less than the full capacity of the plant could not be struck down as inherently unreasonable use of the contractual powers. On the basis of the evidence, if flexibility of output is permitted, then allowing, say, 15 per cent of plant capacity to cater for an appropriate level of swing could not be condemned as unreasonable.

Origin and status of 70 PJ/a as the plateau level of production

[97] In early studies assessing the scope for development of Pohokura, it was assumed that there would be a market for between 60 and 90 PJ/a of gas, and a working assumption was made of a plateau level of production at 70 PJ/a.³¹ The FDP analysed the proposal by reference to plateau production at that level, contemplating production facilities with a nameplate capacity of 86 PJ/a. It follows that a period of plateau production at 70 PJ/a would amount to 85 per cent of that

³⁰ Mr Richard Tweedie, 22 September 2009 brief, paragraph 8.4(c).

³¹ See, for example, CB10619.

nameplate capacity. That followed a significant number of pieces of work, all of which worked on the same basis.³²

[98] FID was taken in reliance on the same basis, ie the joint venturers committed to the capital required to construct production facilities with a nameplate capacity of 86 PJ/a, with it being contemplated that they would be used to produce gas at around an average level of 70 PJ/a throughout the initial plateau period before the field's ability to produce gas dropped off. Internal reviews by each party leading to their own decisions to support FID were on the basis of plateau production at 70 PJ/a.³³ STOS's very detailed 187 page April 2004 report on the Pohokura field development commented in respect of plant capacity:³⁴

The opportunity for Pohokura in the current gas market is around an annual plateau production of 70 PJ/a. This rate has been selected in conjunction with the gas marketing committee of the JV parties and recognises the balance between gas supply, demand and price.

[99] The status of an expected level of production at a plateau of 70 PJ/a was thoroughly tested in the evidence. Shell and OMV eschewed any reliance on the status of 70 PJ/a in the FDP and FID decision-making as estopping Todd from contending thereafter for a different level of annual production. Rather, they treated that level as the long-standing and repeatedly justified working assumption from which the operator would be expected to begin. At most, some rationale might be expected for the operator to propose, or the joint venturers to approve, average production for the plateau period at a level other than 70 PJ/a.

[100] The unanimous approval given to the FDP and FID does establish a mutual contemplation, at least at that stage, that the parties would commit to production facilities having a nameplate capacity greater than the projected average level of production in the field's plateau period. Todd's own analysis in the May 2004 Board Paper, recommending that it commit to the FID, made an assumption as to production volumes consistent with what has occurred.³⁵ I am satisfied that the

³² CB6010, 6405, 6411, 6499, 6510.

³³ See, for example, OMV CB7278, Todd CB7442.

³⁴ CB6744.

³⁵ CB7458.

production volume of 70 PJ/a in the plateau period had the status summarised in the preceding paragraph.

[101] The parties agreed on 30 April 2004 that a GBA was not needed before commercial production began. However, by late 2005 Shell was proposing a GBA that would have permitted flexibility of levels of off-take. It is reasonable to infer that Shell contemplated that if a GBA could be settled between the parties, it would facilitate production at levels up to the commitments that had been made in the second quarter of 2004.³⁶

[102] Todd argued that Shell and OMV reached a common position on the level of production, inferentially extending to the approach they would subsequently take to later annual consideration on levels of production, during the period the alignment agreement formally committed them to such agreements. Todd argues that having become so “aligned”, Shell and OMV carried on that side agreement in their consideration of subsequent WP&Bs after production began in September 2006.

[103] I am not satisfied that that inference naturally arises. Once a pattern of production at the plateau level projected in the FDP and FID was achieved, there was an obvious commercial rationale for continuing at that level, in the absence of a change in circumstances. All the parties had concluded gas sales for a number of years, relative to production at that rate. OMV had sold its gas subject to a warranty that it would not sell gas to other buyers unless there was an upwards revision of the level of Pohokura reserves. One rationale for that was to provide additional assurance to that buyer of OMV’s ability to deliver the gas it had contracted to sell. However, Todd was inclined to criticise OMV for this, suggesting the constraint gave it a motive to oppose higher levels of production that would otherwise have been appropriate. I do not accept that OMV breached any material obligations in contracting on the terms it did.

[104] I am also satisfied that the attitude that Shell and OMV brought to subsequent considerations of the annual production levels for the purposes of the WP&Bs was influenced by the form of Todd’s allegations in these proceedings. Shell has

³⁶ Draft GBA (CB9541-9559) and Shell commentary CB9561.

acknowledged that in recent years it would have preferred to propose production at a higher level, but has felt constrained from doing so because of Todd's stance on the present claims. Todd insisted that compensation for what it treated as the damages caused by improper constraint had to be included on the agenda for any discussions about agreeing different arrangements for off-take.³⁷

[105] Although production during the 2007 to 2009 years consistent with the working assumptions in the FDP and FID has not met Todd's aspirations, it cannot be claimed to be inconsistent with the level of production contemplated when FID was unanimously agreed. The May 2004 paper to the Todd Energy Board recommending investment in Pohokura described the position under the JVOA as giving it "the right and obligation to take equity shares of all hydrocarbon production from the development".³⁸ That paper used production forecasts of 70 PJ/a whilst acknowledging that off-take could be higher given the planned nameplate capacity of 82.5 PJ/a. That paper also acknowledged that, with separate marketing, the joint venturers:

...will require to agree (sic) gas uplift and balancing arrangements to ensure the prudent management of the field and protect their gas interests.

[106] Before the FID in June 2004, the operating committee had resolved on 1 April 2004, pursuant to Article 6.2(A) of the JVOA, that Pohokura was a discovery that should be developed. That resolution was passed unanimously but a second resolution determining the key project development parameters was objected to in part on behalf of Todd. Todd did not object to plant capacity being nameplate sales gas capacity of 80 PJ/a, nor did it object to the proposed dates for production. However, Todd did oppose the rate of production being based on a conservative "unfracted"³⁹ profile until the partners agreed otherwise because that resolution would bind the operator to what Todd considered to be a conservative production profile. The second resolution was carried by a Shell and OMV majority. The proposals as to production levels remained consistent from the earliest papers produced, to the detailed proposals underlying FID taken in June 2004. The

³⁷ Mr Hall, first brief, paragraphs 11.17, 11.20; XXN, T807/23-808/3.

³⁸ CB7439-7442.

³⁹ Meaning that the facilities would operate to their standard capacity, rather than being "fracted" to enhance their performance, that being a technical option available at a price.

documents from the time FID was taken hardly support Todd's submission that it would not have committed to FID if production could be limited to 70 PJ/a.⁴⁰ The protracted history of 70 PJ/a as the projected plateau level of production clearly put Todd on notice that until a GBA afforded scope for flexibility on terms enabling imbalances to be redressed, the only level relied on would have a presumptive status as the appropriate one.

[107] From the tenor of the documents thereafter, I infer that Todd's campaign for higher production became more insistent as the commercial advantages it would have over the others in pressing for higher production became more apparent.⁴¹ I am also inclined to accept Shell's analysis of Todd internal documents that suggest Todd had a change of heart about the need for a GBA from early in 2005 when it reflected on its ability to use M&M for its own balancing purposes.⁴² These exchanges included another Todd executive acknowledging Hamish Tweedie's proposal with the following response:

Your view on gas balancing is useful (ie we will self balance) and makes sense.

[108] Hamish Tweedie's comments had included:⁴³

If anybody is best placed to self balance then it is probably ourselves.

Interpretation of the JVOA

[109] Todd's claims of breach of the JVOA may be distilled under two heads. First, Todd alleges that the off-take rules breach Article 10.1. Second, Todd alleges that the off-take rules do not adhere to the requirements of Article 10.3 and therefore Article 10.1 operates on its own to create rights to, and is dispositive of, JV gas.

[110] The legal principles applying to interpretation of a commercial contract are well settled. Current authoritative guidance is available from the recent Supreme

⁴⁰ Todd's closing submissions, paragraph 5.16(c)(ii).

⁴¹ See, for example, Hamish Tweedie's 28 June 2006 email, CB12323.

⁴² Shell closing submissions, section 2, paragraphs 2.119, 2.120.

⁴³ CB8107, 8103.

Court decision in relation to a gas supply contract in *Vector Gas Ltd v Bay of Plenty Energy Ltd*, where Tipping J observed:⁴⁴

The necessary inquiry therefore concerns what a reasonable and properly informed third party would consider the parties intended the words of their contract to mean. The court embodies that person. To be properly informed the court must be aware of the commercial or other context in which the contract was made and of all the facts and circumstances known to and likely to be operating on the parties' minds.

[111] In testing the impact of contrasting interpretations, it is still useful to bear in mind the re-statement by Lord Diplock in *Antaios Compania SA v Salen AB* that:⁴⁵

...if detailed semantic and syntactical analysis of words in a commercial contract is going to lead to a conclusion that flouts business commonsense, it must be made to yield to business commonsense.

[112] The approach adopted by the Court in *Vector Gas Ltd* was that material extrinsic to the contract may be used to determine the proper interpretation of a contract.⁴⁶ As Tipping J stated:⁴⁷

The key point is that extrinsic evidence is admissible if it tends to establish a fact or circumstance capable of demonstrating objectively what meaning both or all parties intended their words to bear.

Article 10.1

[113] Todd's contractual claims rely on Article 10.1 of the JVOA (set out in [65] above) as having fundamental importance in setting the limits of two things. First, the rights and obligations of each joint venturer to take production from the field. Second, the extent of what that entitlement is, namely each party's proportionate share of total production available. On Todd's view, in the absence of any other agreement under Article 10.3, Article 10.1 creates an inflexible and constant right and obligation for each party to take at all times its share of all the gas that the Pohokura field is reasonably capable of producing.

⁴⁴ *Vector Gas Ltd v Bay of Plenty Energy Ltd* [2010] NZSC 5 at [19].

⁴⁵ *Antaios Compania SA v Salen AB* [1985] 1 AC 191 at 201.

⁴⁶ Per Blanchard J at [4], Tipping J at [22], McGrath J at [62] and Gault J at [150]-[151].

⁴⁷ At [31].

[114] Todd argues that the parties embarked on commercial production from Pohokura without any GBA which would constitute an agreement under Article 10.3 varying the primary position. Therefore, the venture is stuck with that inflexible position until the parties unanimously agree otherwise.

[115] It follows from the primacy given to this interpretation that it would not be competent for a majority of the joint venturers to deviate from the right and obligation stipulated in Article 10.1. Todd argues that this occurred when Shell and OMV purported to use their majority votes on the operating committee to approve the off-take rules and the nomination protocols, and used the procedures set out in those documents to approve and apply WP&Bs that fixed annual production at approximately 70 PJ/a. Todd's interpretation means that the inflexible right and obligation requires the operator to produce full-out at all times, so that the budgeting process would be confined to how much it will cost to do that (rather than on Shell and OMV's view, extending to a debate as to how much will be produced, and how much various production options would cost).

[116] Shell and OMV's rejoinder is that each venturer's entitlement to its share of total production that might be available in terms of the capacity of the field is not absolute. Rather, each party is to take its share of total production, as "...available to it under this agreement..." (ie the JVOA). Shell and OMV relate the right and obligation expressed in Article 10.1 to the actual level of production from the field as provided for elsewhere, in particular under the WP&Bs approved under Article 6.3.

[117] Article 10.1 does not reflect the most sympathetic drafting style, in that it comprises a single sentence addressing a number of associated notions. It begins with a qualification that its provisions are to apply except to the extent that certain specified provisions provide otherwise. The prospect of qualifying what would otherwise be the effect of Article 10.1 by other provisions in Article 10 is relevant, but the reference to qualifications in Article 9 which deals with financial default by any venturer is irrelevant for present purposes.

[118] So far as crude oil is concerned, the taking of proportionate shares of production is to occur in accordance with such procedures as referred to in

Article 10.2. That provides interpretative guidance as an analogy, but it is not directly relevant in applying Article 10.1 to Todd's claim in respect of gas. Therefore, for immediate purposes, references to any off-take agreement referred to in Article 10.2 can be omitted.

[119] The last notion addressed in the article commencing with "provided that" (in the fifth to last line as reproduced in [65] above) introduces a proviso enabling the operator to use or flare as much of the production as is reasonably required in conducting the joint operations. The operation of the proviso is not contentious, so it can be omitted for present purposes. Accordingly, paring the long sentence down to the words immediately relevant to Todd's claim in relation to gas:

Except as otherwise provided in this Article 10..., each Party shall have the right and obligation to own, take in kind and separately dispose of the share of total production available to it under this Agreement in such quantities and in accordance with such procedures as may be set forth in...the special arrangements for Natural Gas referred to in Article 10.3...

[120] The terminology of "right and obligation" reflects the JV structure in which it is the JV, as permit holder, that is responsible for production. The molecules in the wells are Crown property (ie whilst the minerals are "...in the land" in terms of s 10 of the CMA) subject to the joint venturers acquiring property rights in the molecules upon extraction, in their undivided proportionate shares. "Joint Property" is defined in Article 1 of the JVOA to include:

...Petroleum prior to custody, ownership, possession and control of Petroleum passing as provided in Article 10.

[121] Article 10 deals with the disposition of production so that from the point at which the joint production is made available to each of the venturers, they are both entitled and obliged to assert ownership over it, take it in kind, and then separately dispose of their share of production.

[122] That share of production is in relation to "total production available to it under this Agreement". Neither "production" nor "total production available" are defined terms. From Todd's perspective, a literal approach is sufficient and appropriate: the phrase must contemplate all the production that is available from the field when it is being operated in accordance with good and prudent oil and gas field

practice, as required of the operator under Article 4.3(A)(2). Todd's proposition is that the production that is "available" is reflected in the capacity of the facilities the joint venturers have committed to constructing. FID was taken in respect of production facilities with a nameplate capacity of 86 PJ/a so Todd claims an entitlement to its 26 per cent share of production at as near to 86 PJ/a as can be achieved, after allowing for planned and unplanned stoppages.

[123] Two linguistic considerations arise from Todd's focus on the phrase "total production available". The first, pressed particularly by Mr Goddard, is that "available" is not a part of the concept addressed by the previous two words "total production". Rather, "available" appears where it does to provide the connection between the production of the venture being referred to, and each party in the sense that it is (the share of) total production that is available to each party under the terms of the JVOA. In other words, "total production" is a comprehensible concept on its own, but it only makes sense as used in the wording of Article 10.1 if what occurs to it is that it becomes available to a party.

[124] Throughout the hearing, the parties tended to focus on the phrase "total production available". However, I am inclined to accept Mr Goddard's analysis. Thus, the concept dealt with in this part of Article 10.1 is the total production to which a party becomes entitled at the point of separating all the production of the JV into the parties' separate entitlements, ie it is the "total production available *to it*" that matters.⁴⁸ This supports the concept being confined to what has actually been produced, rather than a theoretical projection of what the plant was capable of producing.

[125] The second linguistic consideration focuses on the purpose served by the phrase "...in such quantities". The phrase serves to qualify "total production" in the sense of what has physically been produced. If a party's entitlement was to its share of "total production available", in the sense of a theoretical volume reflecting the capacity of the plant, then such a concept is complete in itself. It would not require,

⁴⁸ Emphasis added.

and indeed is inconsistent with, any additional reference to quantity. This point also tends to confirm that what Article 10.1 refers to is the actual extent of physical production that reaches the point at which joint ownership ends and each party is entitled to take, and treat as its own property, that party's share of what has been delivered to that point.

[126] The phrase "total production available" may be contrasted with "total available production" as used in Article 10.2(B) where the JVOA addresses the matters to be provided for in an agreement for off-take of oil. Such an off-take agreement is to make provision, inter alia, for:

- (B) Operator's regular periodic advice to the Parties of estimates of *total available production* for succeeding periods, quantities of each grade of Oil produced and each Party's share for as far ahead as is necessary for Operator and the Parties to plan offtake arrangements...⁴⁹

[127] Todd suggested that there was no significance in the different sequence of these three words when used respectively in Articles 10.1 and 10.2. However, Mr Taylor argued for Shell that in their respective contexts there is an intended temporal difference. "Total production available" reflects what has been produced and is available, ie each party's entitlement is to their share of whatever gets to the delivery point. In contrast, "total available production" is a prospective concept, describing the operator's estimate of quantities of oil to be produced in later periods.

[128] I am inclined to agree with Shell's argument that this is a valid point in favour of "total production available" in Article 10.1, reflecting the respective shares of whatever has been produced and is available, rather than addressing disposition of property by reference to the conceptual notion of what could be produced. This is so notwithstanding that on Todd's approach the projection of capacity is a relatively confined exercise because the operator simply has to run the plant full-out whenever it can. It is also relevant that there will always be a measure of uncertainty as to quantities until the product gets to the delivery point.

⁴⁹ Emphasis added.

[129] An approach focusing on quantities actually produced and available for delivery is also supported by the content and location of the proviso in the last five lines of Article 10.1 as quoted in [65] above. The extent of gas that might be appropriated by the operator for operations and to flare is likely to be unpredictable and fluctuating (even if flaring is prohibited or tightly controlled). Because there is a prospect that some part of the production will be diverted for the operator's purposes before the balance reaches the point of delivery to the parties, the entitlement of each party can only be the requisite proportion remaining after any such appropriation. Thus, "total production" or "total production available" must reflect what actually gets to the delivery point. Todd's interpretation could take into account the prospect of fluctuating appropriations by the operator by suggesting that such amounts are added to the amounts necessarily deducted from the plant's projected capacity for periods of plant stoppage. However, that approach introduces uncertainty when it begins with notional plant capacity, subject to deductions for planned and unplanned stoppages, and then any amounts used by the operator. Todd's approach compares unfavourably to the simplicity and certainty of "total production" reflecting what actually becomes available at the delivery point.

[130] A caution is required in placing any significant reliance on headings of parts of commercial documents such as the JVOA. As with headings when interpreting statutes, they are prudently treated as mere "indications".⁵⁰ Even so, headings may assist in determining what a reasonably and properly informed third party would consider the parties intended the words of their contract to mean.⁵¹ A further pointer in favour of "total production available" reflecting entitlements to what is actually produced to the delivery point, is the scope of what is contemplated by the heading to Article 10, "DISPOSITION OF PRODUCTION". That foreshadows provisions about how the parties are going to (separately) dispose of what is (jointly) produced. It does not suggest that Article 10 will contain provisions stipulating the level or manner in which production is to occur, or that it establishes rights to demand particular volumes of production.

⁵⁰ See Interpretation Act 1999, s 5(2).

⁵¹ *Vector Gas Ltd v Bay of Plenty Energy Ltd* [2010] NZSC 5 at [19]; *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896 at 912.

[131] In the same vein, the heading to Article 10.1, “Right and obligation to take in kind”, is inappropriate to foreshadow how the extent of production will be resolved. The heading more naturally signals that each party attains a right to take what was henceforth undivided joint property at a certain point, and further that each party is obliged to take it at that point.

[132] As Shell argued, neither the headings nor the content of Article 10.1 suggest that it is creating a right such as a chose in action for one or more parties to demand that production occur. I find sensible Shell’s suggestion that the stipulation was included in the AIPN model in terms creating a “right and obligation” for tax reasons, and in light of competition law concerns in some jurisdictions.⁵²

[133] Todd contended that Shell’s internal analysis had in fact agreed with Todd’s view of the phrase “total production available” in the period after joint selling had been abandoned, when the parties were reflecting on arrangements needed for separate selling. Todd relied on a number of internal Shell documents to establish this point. As stated above at [112], material extrinsic to the actual words of a contract may be admissible in order to assist in the proper interpretation of the objective intention of the parties. Such extrinsic material may include post-contractual conduct. The issue of admissibility of such evidence was considered by the Supreme Court in *Gibbons Holdings Ltd v Wholesale Distributors Ltd*.⁵³ In *Gibbons*, the majority of the Court departed from the traditional approach precluding the consideration of post-contractual conduct, holding that post-contractual conduct may be admissible in certain situations. The Court was divided on whether admissible post-contractual conduct needs to be mutual.⁵⁴

[134] I would be inclined to agree with subsequent High Court authority in favour of Tipping J’s approach, namely that the conduct must be mutual.⁵⁵ However,

⁵² Shell closing submissions, Part 1, paragraph 2.34(c).

⁵³ *Gibbons Holdings Ltd v Wholesale Distributors Ltd* [2007] NZSC 37, [2008] 1 NZLR 277.

⁵⁴ Tipping J at [53] stated mutuality is required, whereas Thomas J at [135] considered that non-shared or mutual conduct may nevertheless point to contractual meaning.

⁵⁵ *Open Country Cheese Company Ltd v Fonterra Co-operative Group Ltd* HC Auckland CIV-2008-404-727, 11 December 2009 at [8]; *Welsh v Gatchell* [2009] 1 NZLR 241; (2007) 5 NZ ConvC 194,549; (2007) 8 NZCPR 708 at [34].

Tipping J sought to revisit his conclusion in the more recent decision of the Supreme Court in *Vector Gas Ltd* where his Honour stated:⁵⁶

In *Gibbons Holdings Ltd v Wholesale Distributors Ltd* I expressed the view that evidence of subsequent conduct should be admissible, if capable of providing objective guidance as to intended meaning. I suggested that, in order to be admissible, post-contract conduct should be shared or mutual. I saw that as a way of emphasising the need to exclude evidence which demonstrated only a party's subjective intention or understanding as to meaning. I now consider that the approach I am taking in these present reasons is a simpler and clearer articulation of the appropriate principle, but one which still preserves the essential line between subjectivity and objectivity of approach.

There is no logical reason why the same approach should not be taken to both post-contract and pre-contract evidence. The key point is that extrinsic evidence is admissible if it tends to establish a fact or circumstance capable of demonstrating objectively what meaning both or all parties intended their words to bear. Extrinsic evidence is also admissible if it tends to establish an estoppel or an agreement as to meaning. Such an agreement can demonstrate a special (private dictionary) meaning or an accepted meaning of words which would otherwise be ambiguous.

[135] On that approach, absence of mutuality is not sufficient to render evidence of post-contractual conduct inadmissible. If objective in character, the conduct may be an aid to interpretation. The internal Shell comments are in the nature of strategic analysis, weighing up options. In that sense, it is subjective. However, against the prospect that it falls on the other side of the line, and is better characterised as sufficiently objective to be helpful, I will review it and deal with its relevance as a matter of weight, not admissibility.

[136] Todd relied on an internal Shell note prepared to review its objectives and strategy for a meeting that was to occur on 30 April 2004. Under the heading "Shell's assessment of its baseline position", after stating that production parameters had been agreed at 80 PJ/a plant capacity, 235 TJ per day and total P85 reserves of 482 PJ, the note continued:⁵⁷

- The expected "total production available" (use exactly these words which are in Article 10 of the JVOA) is therefore based on these agreed numbers.

⁵⁶ *Vector Gas Ltd v Bay of Plenty Energy Ltd* [2010] NZSC 5 at [30]-[31].
⁵⁷ CB7217.

- Under Article 10 each party has both a right and an obligation to take its share of total production available to it. Shell will be ready to meet its obligations and is expecting the other joint venturers to do likewise. In other words, emphasise the obligation aspect of Article 10 – not just the entitlement.
- Shell is planning to be in a position where it will be able to take all its share of the total production available.
- However, Shell thinks that some flexibility to allow for different approaches would be a good idea, should add value and that it is keen to hear the ideas of others.

[137] A little earlier on 18 April 2004, Mr Frens, a Shell employee working at STOS, commented in an internal Shell email:⁵⁸

Victor,

maybe I am mistaken, but I believed that through the resolution at OCM we have agreed an [sic] Pohokura offtake profile and without a balancing agreement all JV partners need to sell there [sic] share every day. If one party doesn't, they leave their gas in the ground and it becomes part of the remaining volumes and is split in equity proportions (in other words if you don't lift your share you lose significant part of it. Obviously this can be mitigated (optimised) by having a balancing agreement which allows different partners to over and underlift in time as long as in the end everyone gets their entitlement. Not having a balancing agreement in this case has therefore very little risk as long as we sell our gas;

Thanks
Ante

[138] These documents suggest that Shell was conscious of both the right and obligation to take gas, but it does not convey that total production available was to be derived by having the plant run at capacity at all times. Certainly, the note for the 30 April 2004 meeting suggested that “total production available” equated with the plant's capacity. The earlier email is equally consistent with total production available meaning the actual production to the point of delivery to the parties for their separate interests. Even if the inference Todd invites does arise on the terms of the note for the 30 April meeting, it is an inadequate basis on which to contradict the numerous strong indications supporting the contrary interpretation.

⁵⁸ CB7058.

[139] Todd also sought to support its interpretation of Article 10.1 by reference to the opinions of United States experts in the drafting of joint venture agreements, Professor Anderson and Mr Barnes. They both opined that the AIPN model JVOA is intended to encourage and facilitate exploitation of the petroleum resource. Mr Barnes cited several mechanisms within the terms of the AIPN model for a party wishing to aggressively explore and/or exploit the resource not to be unduly hindered by a party that is not as aggressive. These included the opportunity for sole risk operations, and the right and obligation of each party to take in kind and separately dispose of its share of the total production available. I accept that these provisions can be characterised as facilitating exploitation. However, without more, they do not justify an interpretation of Article 10.1 enabling a minority venturer to force joint operations up to full capacity at all times, when a majority of the venturers seeks to exploit the resource at a somewhat lower average rate, subject to such decisions by a majority being challenged as irrational or perverse.⁵⁹

Article 10.1 create an inflexible obligation?

[140] The logic of Todd's case required it to acknowledge that one party not taking its proportionate share at any time (an "underlifter") was vulnerable to the rest of its share being taken by another party or parties able to dispose of it at that time.⁶⁰

[141] Further, Todd's case was that this inflexible regime rendered an underlifter liable for damages for not taking all of its share.⁶¹ Todd's own proposals for a GBA included the notion that a party underlifting by more than eight to 11 per cent on any day would lose its entitlement to claim any larger amounts from later reserves.⁶² OMV and Shell argued that Todd's interpretation could not be upheld because of these prospects that were characterised as uncommercial. Given the wide range of

⁵⁹ See [213] to [221] below, as to constraint on exercise of discretionary contractual powers.

⁶⁰ Richard Tweedie XXN, T321/13-18.

⁶¹ CB12599-12604, Todd letter 13 December 2006 asserting liability of Shell and OMV for not uplifting their equity shares, and T723/1-21, XXN of Mr Hall, that parties liable in damages for underlift.

⁶² CB10819, Burt 20 November 2009 brief, paragraph 176.

circumstances in which a party may not be able to take delivery of its full share without any fault on its part, such outcomes would be inconsistent with the best exploitation of the resource, and are inherently unlikely to have been the intended application of Article 10.1.

[142] A persistent theme for Shell and OMV was that these consequences of Todd's interpretation of Article 10.1 involved appropriation of part of joint property without compensation, rendering the approach unrealistic and unsupportable. It was submitted for Shell that a review of decisions in the United States resolving disputes between parties who had underlifted or overlifted relative to their share in a JV reveals a common theme that the underlifting party is entitled to be compensated by the overlifting party. This analysis did not purport to be exhaustive, and each claim will depend on its own circumstances, particularly the relevant contractual terms. However, it is hardly surprising, and in assessing the range of commercial consequences of Todd's inflexible interpretation of Article 10.1, I am satisfied that more would have been required to support an interpretation under which parties could be deprived of their share of returns on their investment as a result of underlifting. This would be particularly unlikely where the contract did not limit the circumstances in which a party would lose property rights such as where it occurred for reasons beyond the underlifting party's control or in circumstances considered to be reasonable at the time.

[143] There are two indications elsewhere in the JVOA that are inconsistent with an inflexible obligation for each party to take all of its entitlement at all times. First, in Article 10.2(D), the arrangements contemplated for the disposition of oil explicitly recognise the prospect of underlifting and overlifting. There is nothing in the terms of the JVOA to suggest that arrangements for transformation of joint into separate property should be different as between one form of production of the venture (oil), and the other (gas). In addition, the definition of "Entitlement" in Article 1 refers to the quantities that a party has the right and obligation to take, "...after adjustments for overlifts and underlifts". That must contemplate some process under which parties can vary the rate at which they take possession of their proportionate entitlements. In this sense, these other provisions in the JVOA support the

proposition that “total production” available to the parties under Article 10.1 refers to each party’s share of what is actually produced to the delivery point, and that it may be subject to fluctuations in certain circumstances.

[144] Second, the heading to Article 6 of the JVOA is limited to “Work Programmes and Budgets” (see commentary on the content in [61]-[63] above). However, Article 6 provides for the operator to propose and, in a form subsequently approved by the operating committee, to carry out budgeted works at the expense of the parties. Article 6.3 provides for that process in relation to production from the field.

[145] There was no evidence detailing the marginal cost of additional volumes of gas produced at Pohokura beyond, say, an average level of 70 PJ/a, but it was generally agreed that incremental production between, say, 70 and 75 PJ/a would not incur significant additional expenditure. Nevertheless, the nature and extent of work done by the operator under Article 6.3 in producing gas and the associated condensate must be constrained by the proposal approved by the joint venturers in the WP&B. The operator generates no revenue and is entirely dependent on the parties funding all its expenditure. Once a budget is approved, the parties are committed to fund that, but nothing more. In the negative sense, the operator does not have approval to produce gas for which it has not received prior budgetary approval from the operating committee.

[146] The “total production” referred to in Article 10.1 should therefore reflect the extent of production for which the operator has obtained budgetary approval under Article 6.3. Once this connection between Articles 10.1 and 6.3 is made, it reinforces the analysis that “total production” is the physical volume that gets to the delivery point.

[147] Todd argued against each step in this reasoning.⁶³ First, Todd argued that it was no part of the operator’s responsibilities in proposing a WP&B to include any projected level of production. Article 6.3(A) does not explicitly require the operator to do so, and Todd instead submitted that the operator should focus on the level of

⁶³ Todd closing submissions, paragraphs 9.11 to 9.33.

production projected at the time as being deliverable by the plant, acknowledging that as circumstances change, so might the finite extent of gas actually able to be produced. For the operator to go beyond this and propose a level of production on grounds other than deliverability is, on Todd's analysis, stepping outside the role of the operator and beyond the scope of joint operations. That is because projected levels of production are a reflection of separate marketing decisions, with which the JV is not concerned.

[148] However, I am satisfied that the level of production is a matter within the JVOA. Gas and the associated condensate are produced by the JV, and numerous important considerations that are clearly within the scope of the JVOA could influence the rate at which production occurs. For instance, there could well be genuine differences of technical opinion about the preferable rate of production intended to maximise the ultimate volumes able to be extracted from the wells. That has not been raised as an issue at Pohokura, but competing expert opinions about the relative merits of re-injecting gas at Todd's McKee field illustrate the real prospect for technical debate on the rate and sequence of extraction. That inarguable part of the operator's task, and the operating committee's jurisdiction, means that the level of production is not a matter inflexibly and arbitrarily dictated by the terms of the JVOA at the outset, but rather will be the subject of on-going consideration through the life of the field.

[149] Todd could argue that its reliance on total production available as used in Article 10.1 does accommodate various technical considerations that alter the extent of production available to the parties. If the oil field geology dictated a change, then levels beyond those prudently produced have to be treated as not "available". However, once such matters are within the scope of the JV, it would be inconsistent to exclude on-going decisions about the level of production that reflect, for instance, varying views on extracting value from another of the field's assets, namely its natural storage capacity.

[150] Todd's approach would require the level of production to be dictated by factors beyond the control of the parties, namely what the facilities are technically able to deliver. It treats the original parties as having signed on to a commitment to

fund and deal with production at levels over which they have no control for a period of production that could extend to 25 or 30 years. This had occurred when the JVOA was completed in 1999 before the discovery had been assessed in even a preliminary way. On Todd's approach, flexibility to vary this could only be achieved if parties subsequently agreed unanimously to a GBA. The inflexible commitment would occur with the real prospect of numerous changes in the parties to the venture throughout its life. I consider that more would be required to impose such a regime on the parties, than the terms of Article 10.1, which I have found can more naturally be interpreted to accommodate an annual budget review, with the prospect of a measure of flexibility.

[151] Unless Article 10.1 is interpreted to impose the inflexible right and obligation Todd contends for, the balance of its arguments against the approach I have suggested lose their force. The role of the operator is to manage the operations that accord with good oil field practice in the manner for which the operator anticipates it will get budgetary approval. I am satisfied that proposals by the operator incorporating a suggested level of production are within the appropriate content of the operator's role under Article 6.3(A). Accordingly, such a WP&B setting the following year's level of production can properly be approved by a majority of the parties.

[152] A further challenge Todd argued to the capacity of the operating committee to resolve the off-take rules was that paragraph A1 of them was inconsistent with, and therefore amounted to an amendment to, Article 6.3(A) of the JVOA. Article 6.3(A) provides for the operator to deliver to the parties a proposed WP&B that was to detail the production to be performed for the following permit year.

[153] Paragraph A1 of the off-take rules stipulates that the WP&B delivered in accordance with Article 6.3(A) was to include "the operator's assessment of the total production available for the relevant year...".

[154] There is nothing in Todd's argument that this purports to give the operator a different or inconsistent task from that contemplated by Article 6.3(A). The terms of

off-take rule A1 are consistent with, and simply provide more detail as to how the operator is to go about the task directed of it in, Article 6.3.

[155] Todd further argued that, in the absence of an agreement between the parties, the only objective reference point by which to estimate available production is deliverability. However, that overlooks the production arrangements contemplated at the time of FID, including the rationale for settling on an average level of production that would allow for fluctuations to accommodate sales made with “swing”. Recognising that as the preferred position for a majority of the parties does not take the operator outside the scope of joint operations. Rather, on the facts here, it contemplates joint production arrangements that conform both with the originally contemplated arrangements and current wishes of the majority where they are consistent with that.

[156] In preparing for commercial production from Pohokura, Todd’s internal analysis recommended the same view as that held within Shell and OMV, namely that the venture would require gas uplift and balancing arrangements to ensure the prudent management of the field.⁶⁴ Todd has subsequently relied on an interpretation that the failure to agree such balancing arrangements forces all parties into an inflexible commitment that I am satisfied would put at risk the return on the investments made by the parties. For all the reasons I have traversed, I do not consider that interpretation can be sustained.

Article 10.3

[157] Can Article 10.1 operate on its own to create rights to, and be dispositive of, JV gas, as Todd’s arguments necessarily require? Shell and OMV argued that the terms of Article 10.1 are inadequate to regulate the disposition of property because the share of each venturer has to be ascertained and mechanical arrangements made for the transfer of ownership including the point of physical delivery from undivided interests in the whole, to separate interests in the identified shares. On this view, what amounts to “total production available to [a party] under this Agreement” is

⁶⁴ Todd investment recommendation, 24 May 2004, CB7440-7441.

incomplete until fleshed out by material matters such as delivery point and arrangements for accommodating fluctuations in a party's capacity to take gas (even if confined only to force majeure type contingencies).

[158] The use of “the” in referring to special arrangements, instead of “any” such arrangements, suggests the drafters of Article 10 contemplated that in cases where the agreement governed the production of gas, special arrangements would indeed be concluded in terms of Article 10.3. However, particularly in light of the original wording of Article 10.3 (see [72] above), it would be artificial to interpret the use of “may” in the current wording of Article 10.3 as if it were “must”, introducing the notion that completion of special arrangements by the parties is mandatory. On the terms of the article, “may” is to be read as permissive. Accordingly, an interpretation solely on the words in Articles 10.1 and 10.3 cannot sustain a meaning that it was mandatory for the parties to conclude special arrangements under Article 10.3, before the provisions in Article 10.1 as to disposition of gas production could apply.

[159] For OMV, Mr Goddard analysed the nature of common law rights of owners as tenants in common, when applied to minerals extracted pursuant to a permit issued by the Crown. He suggested that, in the absence of an order for partition by the Court, or specific agreement about division as applying to specific property (such as “special arrangements” made under Article 10.3), then no one tenant in common can assert a separate entitlement to any part of the jointly owned property. Confirmation that this usual feature of ownership as tenants in common applies is provided in the Article 1 definition of “Joint Property” (see [120] above). In addition, Article 15.2 commits each party to not seeking partition, by any Court order or otherwise, of any Joint Property unless that course is unanimously agreed. These provisions suggest that the parties can only attain separate ownership of their parts of what is produced by the means provided for in Article 10.1 and the arrangements it contemplates will be made under Article 10.3.

[160] Accordingly, as a somewhat extreme alternative to OMV's principal argument that the off-take rules have standing as special arrangements for the purposes of Article 10.3, it was argued for OMV that if that is wrong then absence of

arrangements under Article 10.3 would mean that there is no sufficient agreement between the joint venturers for disposition of particular parts of the gas. Consequently, none of them could deal with any of it by virtue of the constraints applying at common law on dealings in property jointly owned as tenants in common.⁶⁵ Further, OMV argued that Todd could not complain of a breach of Article 10.1 because Article 10.1 does not, on its own, confer rights to any specific quantities of petroleum.⁶⁶ That leads to the extreme notion that the JV has been operating without any lawful basis for the allocation of gas to each of the parties. That is obviously an unhelpful conclusion, and one that the Court should strive to avoid.

Off-take rules “special arrangements” under Article 10.3?

[161] OMV’s principal argument, focusing on the terms of Article 10.3, was that the off-take rules do constitute “special arrangements for the disposal of natural gas”. Having come to the view that total production available reflects actual production reaching the delivery point, it is appropriate to test how Article 10 would apply, in light of that interpretation, to OMV’s arguments as to the status of the off-take rules and nomination protocols. OMV argued that unanimity was not required for special arrangements under Article 10.3 because of the use of the word “arrangements” and the absence of any reference to “agreement”. Further, there was no obligation at all to negotiate, in contrast to the Article 10.2 obligation in respect of an off-take agreement for oil, which was to negotiate in good faith within three months prior to the first delivery of oil. The 2002 addition of the last sentence of Article 10.3 contemplates that such arrangements might provide for joint marketing and sales of natural gas “...as may be agreed between the parties from time to time”. This suggests that at least those parts of any such arrangements would be capable of review by the parties so that they did not necessarily require the permanence of provisions in the JVOA itself. Finally, the requirement that any such special arrangements had to be consistent with the FDP would not be necessary or

⁶⁵ See, for example, *Coleman v Harvey* [1989] 1 NZLR 723 where it is acknowledged that if one co-owner manages to sell, and the joint property is not retrievable, then liability to the co-owners for conversion will arise.

⁶⁶ OMV closing submissions, paragraph 9.5.

appropriate if such arrangements could only be entered into unanimously. That is because it would be competent for the parties to make any arrangements unanimously, whether consistent with the FDP or not. OMV argued that these indications as to the status of “special arrangements” mean that they could be introduced by operating committee resolution using the voting mechanism under Article 5.9.

[162] Todd has consistently insisted that any special arrangements under Article 10.3 must be agreed unanimously. On the words used in the first sentence, each party has to “enter into” them, which is inconsistent with the coercion involved in being deemed to have “entered into” arrangements to which a party was opposed. Further, the sentence added in 2002 refers separately to arrangements “as may be agreed between the Parties”, so that unanimity is the natural condition, at least for the arrangements that are addressed under that additional sentence. The case for unanimity on joint marketing may be stronger than in respect of the balance of Article 10.3 because it would involve a significant extension on what the JVOA otherwise undertook, in that such arrangements would regulate marketing and sales, a function otherwise outside the JVOA and recognised as requiring Commission approval.

[163] There is no forum for decisions by the joint venturers other than in the operating committee. That is clear from Articles 5.1 and 5.2 (see [57] and [58] above). It follows that the reference to “the parties” in Article 10.3, to the extent that the subject matter of such arrangements is within the scope of the JV, most naturally refers to arrangements made by the operating committee. I am satisfied that special arrangements for disposal of natural gas are clearly within the scope of the JV. After all, the heading of Article 10 is “DISPOSITION OF PRODUCTION” and the process of disposing of the venture’s joint property by its allocation and delivery to the parties, even if near to the final step (in the absence of joint marketing), is certainly within the scope of the JV.

[164] As against this approach, if “special arrangements” could be settled by the operating committee, would Article 10.3 not refer explicitly to a process involving resolution by the operating committee? Article 10.3 follows on from Article 10.2

and may contemplate a simpler version of the same process in that under Article 10.2 the parties are obliged to negotiate and conclude an agreement. In that context, the subject matter is beyond the operating committee because the agreement contemplated extends to disposal of oil that one party ought to have taken, and has not (Article 10.2(H)). The forum in which any off-take agreement for oil is concluded therefore extends to matters outside what the joint venturers do in resolving matters in relation to the JV, all of which are done within the operating committee.

[165] In contrast, for arrangements under Article 10.3 that are within the JV, any forum other than the operating committee would be an exception to what appears to be the exclusive jurisdiction bestowed on it to provide for the overall supervision and direction of joint operations. There is no provision as to whom other parties might treat as representative of corporate entities other than in the context of the operating committee. The operating committee's jurisdiction is exhaustive, within the scope of the JV. For example, the operating committee:

- settles all general policies, procedures and methods of operation under the JVOA;
- reviews, and either approves or rejects, proposed WP&Bs and AFEs;
- determines the timing, location, objective and depth of all wells drilled; and
- determines any other matters relating to the joint operations that might be referred to it by the operator or a party.

It is the forum in which unanimity is required for the most serious level of decisions, being those so identified by Article 5.9. Because Article 10.1 is inadequate to sufficiently provide for disposition of property on its own, and more generally because of the need for the JVOA to be interpreted so as to provide for a commercially workable set of procedures, I conclude that the reference to “the parties” in Article 10.3 contemplates, or at least includes the prospect of, such arrangements being made by the operating committee.

[166] Such arrangements are not one of the types of decision on which unanimity is required under Article 5.9, and therefore I find the operating committee is competent to resolve, if necessary by majority, special arrangements for the purposes of Article 10.3.

[167] The notion that the off-take rules would constitute special arrangements for the purposes of Article 10.3 was not addressed at the time. Todd was critical of the “window dressing” undertaken by Shell to allegedly downplay the impact of the off-take rules as merely “operationalising” the JVOA. Further, Todd rejected the reason suggested by Shell’s Mr Jackson for distinguishing the impact of the off-take rules from what he treated as the more permanent and potentially wide-ranging impact of the GBA that could not be agreed between the parties.⁶⁷

[168] Todd pointed to numerous Shell internal documents which raised doubts about the lawfulness of regulating gas off-take by a majority vote, rather than in the form of unanimous agreement between the parties. I have recorded my approach to the admissibility of one party’s post-contractual communications bearing on interpretation of the contract at [133] to [135] above, and apply that same approach, with the same reservation, here.

[169] In the period shortly after abandonment of the prospects of joint selling, internal Shell documents acknowledged doubts as to the situation that would pertain in the absence of balancing arrangements.⁶⁸ Such documents suggested that it was a matter requiring unanimity because it was a “property rights” issue.⁶⁹ Others recognised the prospect that all parties could be obliged to take their full share of amounts of gas actually produced, leading to an obligation to “use it or share it”.⁷⁰

[170] In August 2005, Mr Jackson’s internal analysis for Shell emphasised that the JVOA required a gas off-take agreement, that a basic off-take agreement would not necessarily provide for any flexibility, and that his view was that a basic (inflexible) gas off-take agreement should be concluded with Todd first and then an attempt be

⁶⁷ See [185] to [187] below.

⁶⁸ CB7129, 23 April 2004, “...legal advice...seems to change depending which lawyer you ask”.

⁶⁹ CB7059, 16 April 2004.

⁷⁰ CB7217, 7520 and 7659 in the period April to August 2004.

made to negotiate a GBA permitting flexibility. He emphasised “flexibility is a negotiated right, not an extant right under the JVOA”.⁷¹ In December 2005, Shell personnel were considering a GBA as a form of amendment to the JVOA and Mr Tim Trafford, a legal officer with Shell in Singapore, suggested that introducing entitlements to underlift or overlift were, he guessed, “...powerful principles to append to the JVOA”.⁷²

[171] In addition, on the last business day before Christmas in 2005, there were numerous internal Shell communications on workable off-take/balancing arrangements for Pohokura. They were suggested to be a first step towards off-take and gas balancing arrangements that might be palatable, and once in place Shell could try to get the additional flexibility it needed “through a full GBA”.⁷³ In the course of those proposals, Mr Jackson raised the prospect that an operating committee resolution might be sufficient to achieve off-take arrangements until a GBA was concluded. That suggestion was rejected by Mr Trafford, who observed that off-take rules required the unanimous approval of all parties, and that a resolution of the operating committee would not be sufficient. His comment was endorsed with the observation:⁷⁴

(Between us kids these are significant amendments to the JVOA – which, as we know, is not actually strictly workable for lifting of gas out of common stream.)

[172] On 3 March 2006, the date of the operating committee meeting at which voting on the off-take rules was proposed, Mr Richard Tweedie advised the other parties by letter of Todd’s intention to vote against the proposed off-take rules. His letter, despatched by facsimile, attached to it advice from Russell McVeagh, Todd’s solicitors, dated 27 February 2006. That advice opined that Article 10.1 obliged each party to take its share of production, that being interpreted by Russell McVeagh as being a party’s equity share of maximum daily availability of the plant. The letter reasoned that any arrangements affecting the rights and obligations under Article 10.1 were not matters that could be determined by the operating committee,

⁷¹ CB8689-8698.

⁷² CB10059.

⁷³ CB10133.

⁷⁴ CB10137.

and that rather the arrangements proposed required all parties' agreement.⁷⁵ In the weeks after the majority had passed the off-take rules, Shell contemplated internally and in liaison between Mr Jackson and Mr Burt of OMV, the prospect of declaratory judgment proceedings to confirm the capacity of the operating committee to have concluded its resolution on off-take rules.⁷⁶

[173] These doubts about the form in which off-take rules could be promulgated for the JV recognise that the point is not entirely straight-forward. A construction of the JVOA permitting this course was only pursued by a majority of the parties after earlier attempts to resolve a GBA by unanimous agreement were perceived by the majority to be impossible or impracticable on account of the entrenched differences of view. However, such doubts are not a basis for arriving at a different interpretation of the procedures enabling the JVOA to apply in a workable way. As Thomas J observed in *Gibbons Holdings*:⁷⁷

Evidence of subsequent conduct is admitted, not for the purpose of importing an intention which was not expressed in the contract, but with a view to elucidating the meaning which the parties intended their contract to have when they entered into it.

[174] These doubts held by Shell do not assist in determining what the then parties are to be taken to have objectively intended at the time the JVOA was entered into. None of the parties to the present dispute were original parties to the contract. Rather, this evidence merely illustrates subsequent concerns in ascertaining the proper interpretation.⁷⁸ Therefore, it is not probative in establishing the objective intention of the parties. Further, I would be reluctant to deprive the off-take rules of status as “special arrangements” under Article 10.3 simply because of these doubts which essentially relate to a question of law. Nor do I consider that it materially detracts from their status as “special arrangements” merely because the off-take rules were not labelled as such at the time they were entered into.

[175] Todd also argued that the powers of the operating committee are circumscribed because they are expressly subject to the other provisions of the

⁷⁵ CB10828-10831.

⁷⁶ CB10960, 10963-4.

⁷⁷ At [114].

⁷⁸ *McIntyre v Nemesis DBK Ltd* [2009] NZCA 329 at [112].

JVOA. On Todd's analysis, Article 10.1 created an inflexible right that could not be derogated by an operating committee majority vote. Any such constraint does not arise if Article 10.1 is characterised not as creating an inflexible right, but rather being declaratory of the process by which the joint production of the venture is to be disposed of into the separate interests of each party. Accordingly, there is nothing in the terms of Article 10.1 itself that creates an exception to the breadth of the powers otherwise provided for in Article 5.2.

[176] OMV argued that Todd's challenge to the operating committee's approval of the off-take rules ran together two quite distinct issues that it was important to address separately. The first is whether the operating committee is competent to determine the amount of gas to be produced in any year, the alternative being that the field would have to be run at its maximum technical capacity in the absence of unanimous agreements to the contrary. The second is whether the operating committee can adopt a regime for managing unders and overs in the shares of production taken by the parties, to ensure that the parties' gas take is not materially out of step with their equity interest, in the absence of a GBA concluded unanimously by the parties.

[177] Once the inadequacy of the terms of Article 10.1 to force the default position urged for Todd on the first of these propositions is acknowledged, then the common sense of including annual levels of production in the budgetary approval process is compelling.

[178] On the second issue, having found that the terms of the JVOA contemplate a measure of flexibility, then rules ensuring that imbalances can be redressed are also a matter of commercial common sense.

[179] Shell raised an alternative argument in support of the off-take rules, in the event that Todd was correct in arguing they required unanimity to constitute special arrangements under Article 10.3.⁷⁹ Shell's point was that if the venture could not get the benefit of special arrangements because of a lack of unanimity, then in their stead, the operating committee could promulgate rules or mechanisms sufficient to

⁷⁹ Shell's closing submissions, Part 1, paragraph 2.33; opening submissions 5.104 to 5.110.

enable Article 10.1 to work. Mr Taylor's argument implicitly likened the extent of the operating committee's jurisdiction in such circumstances to Mr Jackson's approach in "operationalising" the JVOA until a full GBA could be agreed unanimously. I took Mr Goddard's lack of enthusiasm for this alternative to mean that OMV did not support Shell on this point.

[180] I accept that Article 10.1 is insufficient on its own terms to provide for all aspects of division of joint property, and enforceable rights and obligations in relation to it. A party's share of "total production" has to be made available to it in such quantities, and in accordance with such procedures, as are provided in that regard. It would deprive the JVOA of significant utility if it was merely an agreement to agree in respect of gas, pending completion of special arrangements under Article 10.3. On Shell's alternative approach, in the absence of special arrangements under Article 10.3 (potentially having similar scope to the various matters provided for in respect of oil in Article 10.2), more limited procedures consistent with Article 10.1 would be needed to effect the disposition of joint property, by vesting it and handing over possession to each of the parties.

[181] Accordingly, if I am wrong in interpreting Article 10.3 to permit special arrangements to be made by means of majority operating committee resolution, then at least those parts of the off-take rules and nomination protocols that do no more than provide for the ascertainment of quantities and procedures required to make Article 10.1 work would be within the jurisdiction of the operating committee. This would be because of the breadth of its powers under Article 5, and the imperative that it be able to fill gaps in more formal arrangements between the parties, sufficient to enable the JVOA to work.

[182] On this approach, there is one aspect of the off-take rules that goes beyond any default power the operating committee may have to promulgate sufficient rules to enable Article 10.1 to work. That is paragraph H of the 3 March 2006 off-take rules, which provides:

Liquids are to be lifted by each PJVer in accordance with its percentage participating interest (regardless of gas nominations) and the principles of Article 10.2 of the JVOA.

[183] In fact, Article 10.2 already has its own default position in the absence of an agreement concluded by the parties under its terms, namely that the principles set forth in Article 10.2 are to bind the parties. The interpretation of Article 10.1 in relation to oil/condensate could not recognise the same imperative for an operating committee initiative in the event of default. As the Court comments below,⁸⁰ Article 10.2(A) in any event provides its own direction as to the allocation of shares of oil. Although paragraph H of the off-take rules is consistent with it, it is otiose and the operating committee could not assume the same default jurisdiction as Shell's alternative argument attributes to it on the standing of the rest of the off-take rules.

[184] Accordingly, with the exception of paragraph H, if necessary I would uphold the validity of the remainder of the off-take rules, and as a consequence the nomination protocols that rely upon them, as competently resolved by the operating committee, pending a unanimously agreed GBA.

Off-take rules "a GBA in drag"?

[185] A significant part of Todd's arguments against the operating committee having the capacity to promulgate off-take rules is that they constituted "a GBA in drag".⁸¹ Todd identified the relevant elements of the proposed GBA, and argued that they were substantially the same as the constraints imposed by the off-take rules. From Todd's perspective, both enabled the majority to constrain the rate at which Todd can access gas from Pohokura, below Todd's 26 per cent share of the full capacity of the facilities. However, I consider that there are material differences between the two. The off-take rules afford any party that has underlifted relative to its share of production a qualified opportunity to get back to parity in subsequent periods. It cannot do so in any way that interferes with other parties' entitlements to take their own shares of production. That is a very limited form of flexibility of off-take. It does not provide any mechanism for redressing an imbalance between the parties, other than in the limited way I have described. Nor do the off-take rules

⁸⁰ See below, [440] to [446].

⁸¹ In March 2006 Mr Hamish Tweedie commented on the proposed off-take rules "all of this looks to be gas balancing in drag" – CB12342.

recognise a prospective right to take at a higher rate than the party's proportionate share. In contrast, a GBA would enable a party in Todd's position to achieve the flexibility it desires by taking more than its share of gas in the early stages of the field's life, subject to being committed to some commercially appropriate mode of redressing that imbalance. Redress could be achieved in two ways:

- by permitting those who have taken less than their share of gas to "catch up" in the later parts of the field life, or
- to agree on, or if necessary provide a mechanism for resolving, an appropriate formula for financial redress, if it was not possible to restore the balance in the proportionate shares by later delivery of adjusted volumes of production.

[186] It is reasonable for the parties in this JV to expect that there be a GBA on unanimously agreed terms before permitting disproportionate off-take above a party's proportionate share of the current year's production where that could lead to the likelihood of one party taking more than its share of the overall resource. Accordingly, there are material differences between a GBA permitting this level of flexibility (subject to a formula for redressing them) and the substantially more limited off-take rules. Those differences are sufficient to justify the distinction between a GBA needing unanimity, and more limited off-take rules able to be concluded by an operating committee resolution that does not require unanimity.

[187] In support of its arguments to the contrary, Todd protested that such an outcome is unsustainable more generally because it permits the other joint venturers who are its competitors in the gas market to constrain the rate at which it can access its entitlements from the field. Todd complained that the off-take rules prevented it "getting ahead".⁸² In the contractual sense, I am not satisfied that the JVOA affords any such unfettered entitlement. Fluctuating levels of production, including at rates higher than a party's proportionate share, could be accommodated once a GBA was agreed that provided a mechanism for redressing imbalances.

⁸² Todd closing submissions, paragraph 3.26(a).

Majority decisions inconsistent with parties' rights?

[188] In assessing the risk that a minority venturer may not be able to access production at its preferred rate on the terms of this JVOA, some regard can be had to a rational expectation that all venturers would continue to share sufficient common interest and would rationally confine their decisions within parameters that more or less accord with the aspirations motivating their original commitments. A substantial measure of commonality was needed to unanimously agree on the FDP and FID.

[189] Here, there has been an on-going difference of view as to the preferable means by which to exploit the resource for optimum ultimate return. It is possible that both sides are right as to the preferential terms of sale. Certainly, the conduct thus far suggests that Todd was able to sell its first tranche of Pohokura gas without any substantial swing, and without compromising the level of return on the gas sold.

[190] In most such situations investors' shared interests are likely to constrain the boundaries of economically rational decision-making on matters such as annual production levels. That is not to suggest any particular obligation to vote objectively acknowledging the best interests of the JV as a whole, but rather to suggest that entirely aberrational or clearly value-destructive decisions are unlikely to command majority support, and if one ever did, it would be unlikely to survive scrutiny.⁸³

[191] A further possible source of assurance to all venturers is that the operator is required by Article 4.3(A)(2) to conduct the joint operations of the venture in accordance with good and prudent oil and gas field practice. Assuming that obligation is honoured consistently with the FID and annual WP&Bs, it is likely to prevent production decisions driven by unrelated commercial considerations that were inconsistent with identified financial parameters in the FID, and technical parameters required of the operator in the exploitation of the resource.

⁸³ See below, [213] to [220].

[192] If the operating committee is not competent to settle special arrangements under Article 10.3 by a majority decision (or, on Shell's alternative, to promulgate sufficient rules to enable Article 10.1 to work), then the venture could be paralysed for want of unanimity. Todd's interpretation would mean that all venturers would be on notice from the outset that a minority could dictate full production in all circumstances, however perversely, and notwithstanding a rational view by a majority that their return from their joint property would be better protected by production at lower or varied levels. Further, given that the JVOA was concluded in these terms years before the decision to develop the field, it seems inherently unlikely that such a default position would apply when it would unnecessarily restrict options likely to arise once production parameters and other circumstances impacting on maximisation of return can be assessed.

[193] Todd's approach would also mean that in the absence of special arrangements, the parties would lack rules on matters such as how capacity or deliverability was to be defined for any period, what the physical arrangements were for taking delivery, and the point at which that was to occur. The terms of Article 10.1 are inadequate to deal with a range of procedural and mechanical matters, and it is unrealistic to suggest that they would take care of themselves.

[194] In closing submissions, Mr Farmer was inclined to accept that further stipulations on process matters were necessary. In this context, he accepted that the nomination protocols were unobjectionable in terms of the processes they provided for. They remained objectionable because they were derived from the off-take rules in terms of the constraints on a party's ability to call for production from the field. At least one member of Todd's technical team considered gas nominations procedures and gas balancing arrangements were needed to allow the field to be operated. Although in cross-examination Mr Hall denied that the view was shared by management, in an internal email on 22 March 2005 expressing that view, Mr Rogers also commented:⁸⁴

Whilst we do not need gas balancing arrangements in the view of gas marketers, it is next to impossible to manage the field without having some principles agreed on how the field will be managed, how ownership of gas

⁸⁴ CB8103.

will be tracked and how the nominations processes will work for both condensate and gas.

[195] On all the evidence, I find that Mr Rogers' practical concerns accord with common sense. Such technical or mechanical provisions are one form of "special arrangement" under Article 10.3. They are a difference of degree, but not kind, from the off-take rules .

[196] Todd's alternative argument is that even if the JVOA does empower the operating committee to promulgate rules for the matters covered in the off-take regime, then this particular form of rules was beyond what the operating committee could lawfully promulgate. This was argued to be the case because the form of off-take regime was said by Todd not to be necessary or desirable to properly exploit the permit area. Therefore it was not within the powers and duties granted to the operating committee by Article 5.2 of the JVOA, where the powers and duties bestowed on it were those "that are necessary or desirable to fulfil in a timely manner the terms of the permit".

[197] It is clear that some form of off-take rules was necessary in the absence of a GBA. The terms of the off-take rules are capable of providing for exploitation of the permit area in a manner reasonably consistent with FID. Although the prospect of the rules being invoked in a way which was inconsistent with FID cannot be disregarded, the risk of improper application of such rules in particular circumstances cannot constitute any sufficient basis for treating these rules as beyond the power of the operating committee. Accordingly, I find those aspects of Todd's fifth and sixth causes of action that depended upon its preferred interpretation of Article 10.1, and the absence of power for the operating committee to promulgate off-take rules, cannot be made out.

Claimed obligations of good faith

Good faith – the law

[198] Common law courts have been reluctant to recognise that good faith obligations are generally to be implied into contracts.⁸⁵ There are two broad categories in which the courts may uphold an implied term: implication in law based on the nature of the contractual relationship, and implication by fact – namely the factual matrix of the particular contract. As such, a term implied by fact is not a term which the Court adds to the contract; it is already in the contract as a matter of construction.⁸⁶ The Court is simply recognising it.

[199] With regard to implication in law, terms are implied by law as a way of specifying some of the duties which arise out of certain contractual relationships. These relationships may be seen as “predicated upon mutual confidence”.⁸⁷ The enquiry as to an implied term in law goes to the “concern of the courts that, unless such a term be implied, the enjoyment of the rights conferred by the contract would or could be rendered nugatory, worthless, or perhaps, be seriously undermined”.⁸⁸ With regard to the joint venture contractual relationship, there is a trend towards implying a term requiring good faith.⁸⁹

[200] Perhaps the nearest analogy to the present situation is that in *Todd Petroleum Mining Co Ltd v Shell (Petroleum Mining) Co Ltd*,⁹⁰ in which Wild J determined that a consequence of the contractual relationship being that of a JV was that the parties must act toward each other in good faith in relation to their JV, and in particular in carrying out the obligations they have assumed under their JV agreement. That

⁸⁵ See Burrows, Finn and Todd *Law of Contract in New Zealand* (3rd ed, LexisNexis, 2007) at [6.3.3(i)] and specifically *Dymocks Franchise Systems (NSW) Pty Ltd v Todd* [2002] 2 All ER (Comm) 849 per Lord Browne-Wilkinson at [54].

⁸⁶ *Attorney-General of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988 at [27].

⁸⁷ *J L Stanley v Fuji Xerox New Zealand Ltd* HC Auckland, CP479/96, 5 November 1997 at 55.

⁸⁸ *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410 at 450 (HCA).

⁸⁹ *Kiwi Gold No Liability v Prophecy Mining No Liability* CA30/91, 18 July 1991 at 12; *Petroleum Resources Ltd v Greymouth Petroleum Acquisition Co Ltd* HC Auckland CIV-2003-404-6962, 22 December 2003; *Symphony Group Ltd v Pacific Heritage (Auckland) Development Ltd* HC Auckland CP362/98, 17 August 1998.

⁹⁰ *Todd Petroleum Mining Co Ltd v Shell (Petroleum Mining) Co Ltd* HC Wellington CIV-2005-485-819, 19 June 2006, at [177].

litigation related to Todd's challenge to Shell and OMV's initiatives to remove STOS as operator at Maui. Complaints about breach of obligations of good faith arose where Todd was challenging the legitimacy and genuineness of claims about deficiencies on the part of STOS.

[201] With regard to terms implied in fact, the traditional approach is the five point test of the Privy Council in *BP Refinery (Westernport) Pty Ltd v Shire of Hastings*,⁹¹ adopted in New Zealand by the Court of Appeal in *Devonport Borough Council v Robbins*.⁹² The indicia are that the term (1) must be reasonable and equitable; (2) must be necessary to give business efficacy to the contract so that no term will be implied if the contract is effective without it; (3) must be so obvious that "it goes without saying"; (4) must be capable of clear expression; and (5) must not contradict any express term of the contract.

[202] The current approach of the Privy Council has been to move away from this test. Lord Hoffman, delivering the advice of the Board in *Attorney-General of Belize v Belize Telecom Ltd* regarded the *BP Refinery* indicia:⁹³

...not as [a] series of independent tests which must each be surmounted, but rather as a collection of different ways in which judges have tried to express the central idea that the proposed implied term must spell out what the contract actually means, or in which they have explained why they did not think that it did so. The Board has already discussed the significance of 'necessary to give business efficacy' and 'goes without saying'. As for the other formulations, the fact that the proposed implied term would be inequitable or unreasonable, or contradict what the parties have expressly said, or is incapable of clear expression, are all good reasons for saying that a reasonable man would not have understood that to be what the instrument meant.

[203] Delivering the minority judgment in *Dysart Timbers Ltd v Nielsen*, Tipping J adopted the reasoning of Lord Hoffman at [25]:

...the question is what a reasonable person would consider both parties must have meant to happen in circumstances not expressly addressed by the contract.

⁹¹ *BP Refinery (Westernport) Ltd v Shire of Hastings* (1977) 180 CLR 266 at 283.

⁹² *Devonport Borough Council v Robbins* [1979] 1 NZLR 1 at 23.

⁹³ *Attorney-General of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988 at [27].

[204] For present purposes, I am comfortable treating Lord Hoffman's approach in *Attorney-General of Belize* as a gloss on the five point enquiry mandated in *Devonport Borough Council*, rather than as a replacement of it. If a term sought to be implied does not satisfy one or more of the five points from *BP Refinery*, then that raises a question as to whether a reasonable person would indeed recognise that suggested term as what the parties to the contract would have meant to apply.

Todd's claim

[205] Todd pleaded that the conduct of Shell and OMV in voting for the resolutions that introduced the off-take rules and approving the WP&Bs was in breach of implied obligations of good faith owed by the joint venturers to each other. The obligations of good faith were pleaded to include the venturers:

- a) not acting so as to prevent another venturer enjoying the full benefit of the JV and its investment therein;
- b) acting in compliance with standards of conduct which are honest and reasonable having regard to the interests of the joint venturers; and
- c) not exercising any power or discretion for a purpose extraneous to the JV.⁹⁴

[206] Such obligations have allegedly been breached by Shell and OMV in that they:

- a) voted in accordance with the alignment agreement between them which had been kept secret from Todd and then acted in accordance with it by implementing the off-take rules and nomination protocols;
- b) withheld from Todd the full benefit of the JV and Todd's investments therein, namely access to its full share of the plant's capacity; and

⁹⁴ Third Amended Statement of Claim (3rd ASC), paragraph 17.

- c) exercised their voting power for an extraneous purpose, namely to further their respective commercial interests outside the scope of the Pohokura JV.⁹⁵

[207] Given my interpretation of Articles 10.1, 10.3 and 6.3, Todd's claimed necessity to imply obligations of good faith is to be tested in circumstances where Shell and OMV have acted in accordance with the contract in introducing the off-take rules, and subsequently in approving WP&Bs that projected gas production at an average rate of 70 PJ/a. The context is therefore that whilst the JVOA authorised the conduct that is now challenged, Shell and OMV's ability to act as they did was constrained by the pleaded forms of good faith obligations, and that the actions they took breached those obligations.

Shell and OMV's response

[208] Shell and OMV argued that obligations of good faith cannot be implied as a term of the JVOA on the tests from *BP Refinery*, in that such obligations are not necessary to give the contract business efficacy and because the extent of good faith obligations alleged by Todd are certainly not so obvious that they go without saying. Further, the contract can operate without them, and in certain respects would be inconsistent with express provisions.

[209] Shell and OMV deny that an obligation of good faith can be implied into the JVOA. They cite Article 15.1 (see [73] above) which negatives any fiduciary relationship between the joint venturers as well as stipulating that the agreement is not to be deemed to construe any party as acting, or authorise any party to act, as an agent, servant or employee of any other party, and that the agreement is not to be construed as creating a partnership or trust.

[210] Here, the relatively exhaustive provisions in the JVOA suggest that all contingencies have been considered so that arguably the test for additional obligations by way of implied term cannot be met. That was also the point relevant

⁹⁵ 3rd ASC, paragraph 67(a), 69(c).

to the Privy Council decision cited by Shell in *Attorney-General of Belize* where Lord Hoffman observed:⁹⁶

The question of implication arises when the instrument does not expressly provide for what is to happen when some event occurs. The most usual inference in such a case is that nothing is to happen. If the parties had intended something to happen, the instrument would have said so. Otherwise, the express provisions of the instrument are to continue to operate undisturbed. If the event has caused loss to one or other of the parties, the loss lies where it falls.

[211] If any good faith obligation can be implied then, at least on OMV's case, it could not be one that prevented a party from voting on an off-take regime in accordance with that party's own genuinely held view as to the optimal off-take profile for the field. Any obligation would be confined to not acting in bad faith, in the sense of acting dishonestly.

[212] The JVOA includes an "entire agreement" clause in Article 20.14 and recital E provides that the parties were entering into the agreement for the purpose of "...defining their respective rights, interests and obligations...". Shell argued that these provisions negative the prospect for implying any additional terms. I do not accept that the terms of those provisions can of themselves absolutely exclude a party successfully arguing for the implication of additional terms. Their inclusion, taken with the relatively exhaustive provisions in the 117 page agreement, do, however, count against the prospects of recognising the need to imply additional provisions.

Implied terms in law

[213] Before assessing whether each of the specific obligations of good faith claimed by Todd should be implied into the JVOA, it is appropriate to acknowledge the extent to which fetters apply on each joint venturer's discretion when voting on matters such as the WP&Bs.

⁹⁶ At [17].

[214] I note that in *Devonport Borough Council v Robbins*,⁹⁷ Cooke J suggested that in that case there was no practical difference between invocation of a principle of law applying to certain kinds of contracts, as distinct from an implied term required in the particular contract (ie an analysis reflecting the factual context). Wild J's recognition of good faith obligations in the earlier *Todd v Shell* litigation is an example of the former, applied to JV contracts as a category.

[215] In *Socimer International Bank Ltd v Standard Bank London Ltd*,⁹⁸ the United Kingdom Court of Appeal reviewed authorities on constraints on the exercise of a contractual power to make decisions. That review included the decision in *Paragon Finance plc v Nash*,⁹⁹ with which Mr Goddard sought to draw an analogy in confining the scope of terms that might reasonably be implied to one that such discretionary powers should not be exercised dishonestly, for an improper purpose, capriciously or arbitrarily. The Court in *Socimer* concluded:¹⁰⁰

It is plain from these authorities that a decision maker's discretion will be limited, as a matter of necessary implication, by concepts of honesty, good faith, and genuineness, and the need for the absence of arbitrariness, capriciousness, perversity and irrationality. The concern is that the discretion should not be abused. Reasonableness and unreasonableness are also concepts deployed in this context, but only in a sense analogous to *Wednesbury* unreasonableness, not in the sense in which that expression is used when speaking of the duty to take reasonable care...

[216] Perhaps predictably, a more recent United Kingdom Court of Appeal decision has dissociated itself from the use of "*Wednesbury* unreasonableness" as an analogy when construing commercial contracts, given the very different overtones of public law challenges that it might be seen to import.¹⁰¹ I do not treat *Paragon Finance* or *Socimer* as importing any of the other trappings of public law challenges. Rather, it is simply that "*Wednesbury* unreasonableness" is useful because it is such a recognisable label for decision-making that defies common sense by virtue of arbitrariness or perversity.

⁹⁷ *Devonport Borough Council v Robbins* [1979] 1 NZLR 1 at 22.

⁹⁸ *Socimer International Bank Ltd v Standard Bank London Ltd* [2008] 1 Lloyds Law Reports 558.

⁹⁹ *Paragon Finance plc v Nash* [2002] 1 WLR 685.

¹⁰⁰ At [66].

¹⁰¹ *Lymington Marina Ltd v MacNamara* [2007] EWCA Civ 151 at [69].

[217] The decisions reviewed in the United Kingdom, and the circumstances in *Socimer* itself, all involved a discretion for one party (classically a creditor of some sort or an insurer) to make a decision with the potential to adversely affect the other party to the contract (debtor/insured). In Australia or more specifically in New South Wales, however, the Courts appear to be more willing to imply a term as a matter of law into normal business contracts. For example, in *Vodafone Pacific Ltd v Mobile Innovations Ltd*,¹⁰² Giles JA referred to *Alcatel Australia Ltd v Scarcella*¹⁰³ and *Burger King Corporation v Hungry Jack's Pty Ltd*¹⁰⁴ as supporting the proposition that:

...an obligation of good faith and reasonableness in the performance of a contractual obligation or the exercise of a contractual power may be implied as a matter of law as a legal incident of a commercial contract.

[218] I consider that is a broader recognition of good faith obligations than has thus far been implied by the law in New Zealand.

[219] However, consistently with the earlier *Todd v Shell* litigation, I am satisfied that the rationale for the law implying a core obligation of good faith extends equally to intra joint venture decisions made by a majority of the venturers pursuant to the terms of the agreement governing their JV.

[220] This constraint against perverse or irrational decision-making is a further answer to Todd's objection that Shell and OMV's approach to Articles 10.1 and 10.3 leaves a minority venturer vulnerable to the whim of the majority. It is also an important aspect of the context, when coming to consider whether additional good faith obligations of the types claimed by Todd are required to give this JVOA efficacy.

[221] I note that Todd did not plead this form of implied constraint on the exercise of voting powers by the majority. Had it done so, I am satisfied that it would have

¹⁰² *Vodafone Pacific Ltd v Mobile Innovations Ltd* [2004] NSWCA 15 at [189].

¹⁰³ *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349.

¹⁰⁴ *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187.

failed to make out a breach of Shell and OMV's obligations not to vote arbitrarily or perversely in their approval of each of the 2006 to 2009 WP&Bs.¹⁰⁵

Implied terms in fact

Obligation not to prevent Todd maximising its financial benefits?

[222] The first instance of good faith obligations alleged by Todd was in effect that Shell and OMV were obligated not to act so as to prevent Todd enjoying the full benefit of the JV and its investment in it. That claim is akin to some form of fiduciary obligation, in that each of the joint venturers was allegedly obliged not to act in a way that might obstruct others from optimising their return. It is similar in concept to the third form of obligation pleaded, namely that the joint venturers were not to exercise any power or discretion for a purpose extraneous to the JV.

[223] I accept arguments for Shell and OMV that their freedom to protect their own commercial interests in decisions relating to the JV cannot be constrained by an obligation of good faith owed in such terms to the other venturers. Commitment to the venture on the terms in the JVOA was by no means risk-free, and the factors I have identified in [213] to [219] above as moderating those risks negate the need to additionally overlay an implied obligation in such terms. Certainly, the terms of such obligations could not be articulated sufficiently simply and exhaustively to be recognised as so obvious as to "go without saying".¹⁰⁶ In addition, such obligations would most likely be inconsistent with Article 15.1 regulating the relationship between venturers in terms negating any dependence of one on others.¹⁰⁷

[224] The contemporaneous documents demonstrate that all three parties approached their Pohokura decision-making having regard to their own commercial interests. Todd has operated its various interests in gas production on a portfolio basis, so that its decisions have not reflected any objective analysis of what is best

¹⁰⁵ See [82] to [108], [188] to [197] above.

¹⁰⁶ These being two of the criteria required for implied terms in *BP Refinery* ([201] above).

¹⁰⁷ See [73] above.

for the venture as distinct from what is best for Todd.¹⁰⁸ Unsurprisingly, Mr Richard Tweedie accepted in cross-examination that parties are able to act in the JV, in their own commercial interests.¹⁰⁹ This supports the conclusion that the parties never intended such a term as part of the JVOA. Accordingly, no such term can be implied.

[225] On each of the articulated forms of good faith obligation, Todd's complaint is that the alleged breach has precluded it getting 26 per cent of Pohokura's capacity at all times when the contract does not give Todd a right to that. I accept Shell's point that good faith obligations could not be invoked to obtain that greater volume by "a sidewind". It is also relevant that the conduct complained of involves Shell and OMV supporting levels of production at Pohokura that are consistent with the projections on which all parties voted to proceed with the development.

Obligation to act honestly, and to have regard to interests of other venturers?

[226] The second form of obligation alleged would require the joint venturers to act in compliance with standards of conduct which are honest and reasonable having regard to the interests of the joint venturers. The first aspect of this is hardly in dispute. In virtually all situations, the parties to contracts with on-going obligations will be required to conduct their dealings with the other parties honestly. In New Zealand commercial circles, that is a basic obligation that certainly does go without saying, and although there may be some debate as to whether it is necessary to invoke obligations of good faith as the means by which it arises, it is appropriately labelled as a limited form of good faith obligation in the present JV context.

[227] The second aspect of this second claimed form of good faith obligation, namely to act in compliance with reasonable standards having regard to the interests of the joint venturers, is a variant of the first and third forms of obligation alleged by Todd. It similarly contemplates a subjugation of a party's own legitimate commercial interests to the interests of others, to the extent the party is aware of

¹⁰⁸ See, for example, Mr Hamish Tweedie's 28 June 2006 email, CB12323, quoted in [90] to [93] above.

¹⁰⁹ T269/13-23.

them. In that respect, it is distinguishable from the good faith required in carrying out the obligations each has assumed under the JV, as articulated by Wild J in the earlier *Todd v Shell* litigation.¹¹⁰ I am similarly satisfied that this aspect of the obligation asserted cannot be made out in the present relationship.

[228] Mr Goddard instanced the predicament confronting a joint venturer considering its stance on a WP&B where options on the level of work that might be approved raise meaningful differences in the extent of financial obligations that would ensue, where the party has very real financial pressures on it. Implied obligations of good faith could not justify requiring such a party to vote in favour of larger expenditure because it appreciates the wish of other joint venturers to pursue that course, when doing so would impose undue financial pressure on its own situation.

[229] So too, where the parties genuinely hold different views on what the preferable course is for the JV to pursue in optimising ultimate recoveries. Thus, this proposed term fails to meet the indicia in *BP Refinery* or the broader test adopted by Tipping J in *Dysart*. After all, it is not the place of any implied obligation of good faith to require one or more parties to act inconsistently with their own genuinely held views of the preferable course to adopt, merely because they are on notice that another party's stance reflects a view that a different course would indeed produce the best ultimate return for that party.

Obligation not to act for purposes extraneous to the JV?

[230] It follows from my analysis of the second form of obligation alleged that the third suggested obligation, constraining venturers not to act for purposes extraneous to the JV, can also not be made out in that form. The essence of such an obligation would oblige all venturers to exclude any considerations that did not focus on the best outcome (presumably financially) for this JV. I am satisfied that each of the present parties would have rejected that notion, had they been invited to confirm that it was so clearly implied as to “go without saying”, when they originally committed

¹¹⁰ See [200] above.

to the JV. In the situation instanced by Mr Goddard, as summarised in [228] above, a financially pressed venturer would have to subjugate its own concerns to preserve cash flow, by voting for a budget requiring it to commit more money, once that larger budget was established in some general sense as being in the best interests of the JV. That would be inconsistent with the structure of the contractual relationship designed by the JVOA.

[231] In addition, Mr Taylor argued that in determining what purposes were “extraneous”, the Court would have to substitute its own view for that of corporate decision-makers. That is something it should not do, under the so-called “business judgement rule”.¹¹¹ I agree that no good faith obligations would be warranted on terms requiring the Court to decide on the relative wisdom of business judgements applied by the parties in their JV decision-making.

[232] Accordingly, I find that the specific forms of good faith obligation pleaded by Todd do not arise within this JVOA contractual relationship. There is no basis for implied obligations beyond the basic one not to act dishonestly or in bad faith.

Good faith – the facts

[233] There was a substantial focus in the evidence on reconstructing how the relationship between the parties had been conducted over the relevant period. Although such matters would often not be relevant in a contractual dispute, it is necessary to traverse that evidence for two main reasons. First, against the prospect that I am wrong in confining the scope of good faith obligations as narrowly as I have, the points Todd worked hard to establish in cross-examination might well be relevant to allegations of breach of good faith obligations owed on wider terms than I have been prepared to imply. Second, the way in which the relationship between the parties was conducted also has relevance for the allegations under the Commerce Act causes of action. That is on the purpose of Shell and OMV’s conduct relative to the

¹¹¹ *Todd Petroleum Mining Company Ltd v Shell (Petroleum Mining) Company Ltd* HC Wellington CIV 2004-485-2809, 3 June 2005 at [180]; *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 821 (HL) at 832 per Lord Wilberforce; *Latimer Holdings Ltd v SEA Holdings New Zealand Ltd* (2004) 9 NZCLC 263,694 (CA) at [71].

arrangements they made, and also as context in ascertaining the effect of such arrangements.

The Shell/Todd relationship

[234] This has been characterised by entrenched bitterness and mutual suspicions of ulterior motives on the part of the other. Illustrative of how divisive it has been in the governance of the JV is the reaction of Mr Wright, who was employed as commercial executive with OMV from July 2003 to May 2004. I found Mr Wright to be a careful and balanced witness. He had extensive experience in the industry and was appropriately qualified for the responsibilities he assumed. He acknowledged in his evidence that he left after only 10 months in the role because of the inability of Shell and Todd to agree on even non-contentious matters.¹¹² The tenor of his evidence was that he considered the animosity between Shell and Todd had impaired rational decision-making. As early as October 2003 he commented internally on a particular difference between Shell and Todd:¹¹³

I also wonder if Shell and Todd have so much bad blood we are just seeing the old emotions stirred up.

[235] Differences in the Shell/Todd relationship have frequently been litigated, most relevantly in the judgment of Wild J dated 19 June 2006, which involved findings about a Shell initiative, variously described as Project Moa and Project Zinfandel.¹¹⁴ Shell accepts the findings recorded in that judgment, which include findings that Shell wanted to change the role that STOS occupied as operator of Taranaki JV fields, to substitute STOS with a standard Shell operating company, and to maximise the value of Shell's upstream assets against the prospect of possible divestment. That project was found to have commenced in or around May/June 2004.¹¹⁵

¹¹² T3122/12-3123/8.

¹¹³ CB19/1319.

¹¹⁴ *Todd Petroleum Mining Company Ltd v Shell (Petroleum Mining) Company Ltd* HC Wellington CIV-2005-485-819, 19 June 2006.

¹¹⁵ At [250].

[236] Given the extent of the dealings between Shell and Todd which have been on-going since 1955, it would be impossible to determine who cast the first stone for the purposes of allocating responsibility for the strained relationship.

[237] In the Pohokura JV context, the tone of Shell's internal communications was set by June 2003 when a draft paper on the Pohokura gas marketing strategy included the following comment about Todd:¹¹⁶

Todd has historically been very good at blocking everything that is out of line with Todd's own wishes. They are a successful, entrepreneurial, small, agile, litigious, tight management group, continuously managing their substantial and diverse asset portfolio. Shell have a guarded respect for Todd, yet they do not respect Shell. They are extremely good at bullying multinationals, extracting value from them, and their general (guerrilla) tactics are:

- Take and take, but never give
- Divide and conquer
- Attack until the "weak multinational" gives in
- ...

[238] Mr Jackson prepared an internal Shell strategy document in September 2003 called "New Zealand JV management. Proposed Strategy". It suggested changing the way that Shell engaged with Todd in order to maximise the delivery of value from Shell's JV interests. The paper stated that maximisation of value from its New Zealand JVs with Todd would only be achieved by changing the way Shell approached the relationship with Todd, and that Todd had gained significant value historically at the expense of Shell in spite of determined efforts by numerous Shell staff at managing the Todd relationship.¹¹⁷

[239] In cross-examination, Mr Jackson acknowledged that he gave the proposed strategy the name "Project Ulysses", that name being a reference to Ulysses S Grant, the United States civil war general noted for his tactics in outflanking his opponent, General Lee.¹¹⁸ The paper acknowledged that Mr Richard Tweedie had been highly successful in delivering significant value to the Todd family, commenting that the

¹¹⁶ CB2359.

¹¹⁷ CB3688-3696.

¹¹⁸ T2215/29, T2216/21.

Todd modus operandi involved intransigence, delays, negativity and threats, and expressed the view that a large part of the Todd value had come from the Shell relationship. The paper noted that OMV's future in New Zealand was inexorably linked with Todd rather than Shell, and the options for improving Shell's position included attempts to align OMV with Shell rather than Todd, to be more assertive in the relationship with Todd, and to be prepared to test the JV voting processes, if necessary calling Todd's bluff on legal action against Shell.

[240] Another point raised in the Project Ulysses paper was to seek absolute alignment between Shell's regional and local (ie New Zealand) staff, and not accept Mr Tweedie's practice of "elevating issues", ie going over the heads of local Shell executives to seek concessions or compromise from more senior executives outside New Zealand. Another perspective on that concern is given in an email from Mr Victor Ojeda to Mr Ajit Bansal on 16 January 2004.¹¹⁹ This was a frank communication from one Shell secondee in New Zealand to another, when Mr Bansal was about to arrive, as a sketch of the commercial environment he would find in New Zealand. Mr Ojeda described the main issue in New Zealand as the entrenched divisive behaviour of industry participants, and particularly one partner, Todd. He observed that it had taken him a while to "...believe the shenanigans that went on". Mr Ojeda referred to a bitter past of work by local personnel being undermined by senior managers, implicitly located outside New Zealand and not sufficiently familiar with the on-going difficulties perceived in dealing with Todd. Mr Ojeda observed:

Ultimately, regardless of where the overseas leadership sits on matters, it's still about ensuring that Shell does not just give up to Todd demands for disproportional value at every twist and turn – there is no goodwill bank, so they just pocket value and rarely even say thankyou, let alone give something back.

[241] It would be naïve to expect internal communications about managing commercial relationships with JV partners not to have some blunt observations about business practices. Unguarded and frank internal communications may not reflect the party's formal position, and attitudes can change over time. Further, it is

¹¹⁹ CB19/1043.

inappropriate to evaluate both sides of the Shell/Todd relationship simply by an analysis of the internal documents. As demonstrated in many respects throughout the trial, Shell business practices involved exhaustive written reporting and communications. In contrast, Todd's small management team has lent itself to oral communications with no equivalent document trails as have been discovered on behalf of Shell.

[242] An earlier Shell paper in September 2003 noted the Shell/Todd relationship as being "at an all time low",¹²⁰ and that at that time OMV was largely siding with Todd. In his cross-examination, Mr Wright volunteered that OMV was more aligned with Todd at that stage, against Shell in the JV, but that that subsequently changed.¹²¹

[243] On 12 December 2003, Mr Ojeda reported internally within Shell on a falling out between OMV and Todd at a meeting discussing rules for each of the parties to uplift some gas separately, in the context of joint marketing of gas.¹²² By 27 February 2004, an internal OMV review of issues then being negotiated recorded OMV as aligned with Shell on entitlements for the parties to uplift separate supplies of gas and on Maui make-up gas. As to a gas sales agreement (GSA) for Pohokura, it recorded Shell and OMV having moved their position substantially to accommodate Todd's views and not being prepared to move further so that OMV and Shell were at a point of telling Todd to "take it or leave it".¹²³ The note observed:¹²⁴

OMV and Shell...have bent over backwards to get Todd aligned within the Joint Venture. Todd have repeatedly stalled, delayed and manoeuvred to their own advantage.

[244] In a little more than a month, Shell and OMV had settled the terms of their alignment agreement which was executed on 2 April 2004.¹²⁵

¹²⁰ CB4060.

¹²¹ T3188/9-16.

¹²² CB5025.

¹²³ CB5873.

¹²⁴ CB5874.

¹²⁵ CB6879-6888.

[245] The evidence for Shell and OMV sought to cast Todd in an unreasonable light in relation to the protracted negotiations that occurred on various aspects arising within the JV. They suggest Todd:

- was inclined to press for urgency on matters of particular concern to Todd whilst delaying or completely ignoring others it did not want to deal with;¹²⁶
- elected not to attend meetings on topics it considered were being progressed inappropriately;¹²⁷ and
- (on terms for easements and pipeline access arrangements) asserted inconsistency in respect of Todd Pohokura Limited and Todd Taranaki Limited's (TTL) respective positions where they were either the beneficiary of, or the party assuming burden under, such arrangements. Mr Burt instanced TTL seeking indemnity from loss suffered by TTL that was caused by its own negligence, seeking \$40 million more in public liability insurance cover than other easement holders, and imposing a constraint on assignment that essentially gave TTL a right of veto on assignment of JV interests (which JV partners did not have in their own right).¹²⁸

[246] Throughout a thorough cross-examination of Mr Jackson, Mr Farmer did not get a straight-forward acceptance of his proposition that Shell executives, or Mr Jackson at least, resented the skills Todd brought to “getting the better end of the bargain”, but in effect the uncompromising tactics Todd adopted appear to have produced those results. That does not suggest that Todd resorted to anything that was illegal, or contrary to its asserted view of its contractual entitlements, but rather that it was tough and uncompromising. Mr Jackson did acknowledge his view that in endeavouring to progress issues in the JV, Todd “was the problem”.¹²⁹ Shell itself was not above simply putting off dealing with Todd, if that suited its own purposes.¹³⁰

¹²⁶ Burt 20 November 2009 brief of evidence, paragraph 180.

¹²⁷ Burt brief, paragraphs 129-133, 144, 167 re 24 November, 6 December 2005 and 16 February 2006 meetings respectively.

¹²⁸ Burt brief, paragraph 32.

¹²⁹ T2367/1.

¹³⁰ CB6975.

[247] There were numerous strands to Todd's allegations of lack of good faith, particularly as alleged against Shell. Mr Farmer's criticisms of Shell's conduct ranged widely during his closing submissions, extending to:

- a conscious plan to minimise Todd's influence in the governance of this and other JVs to which Shell and Todd were parties (drawing on findings in prior litigation about Project Zinfandel);
- a plan to isolate Todd, by forging a secret alliance with OMV and using their majority power to block Todd's wishes for production from Pohokura;
- the Shell/OMV alliance precluding genuine consideration of Todd's views at various meetings, because Shell and OMV representatives had previously agreed a mutual position on the matters to be discussed;
- an animosity on the part of senior Shell executives reflected in a wish to harm Todd's interests;
- a strategy to protect or enhance Shell's interests in other fields, by delaying production from Pohokura.

[248] Criticisms of OMV relative to its alleged breach of obligations of good faith were more limited. Todd relied upon OMV's commitment to the secret alignment agreement and on OMV's part in approving the off-take rules as constituting a lack of good faith. Todd instanced an internal OMV email in which difficulties in dealing with Todd were commented on in a light-hearted vein suggesting that OMV and Shell were the "Anti Todd Squad".¹³¹ In essence, OMV aided and abetted Shell by going along with it.

[249] On the basis that Article 10.1 relates to disposition of what has actually been produced and made available at the point of separate delivery to each party, and that a majority of the parties can decide on levels of production, conformity with the

¹³¹ CB6307.

levels of production contemplated in the FDP and FID may still afford a measure of safeguard to a minority joint venturer. I discussed the prospect of restraining any *Wednesbury*¹³² form of unreasonableness in voting on such matters in the context of good faith expectations, at [213] to [220] above.

[250] In light of the earlier analyses, especially on the status of 70 PJ/a in [97] to [108], and the review of the parties' relationships, I find:

- a) The commercial relationship between Todd and Shell was already exceptionally stressed in 2004 when the FDP and FID decisions were taken unanimously.
- b) The perception of longer-term New Zealand based Shell executives, such as Mr Jackson, was that the lack of understanding or commitment by senior Shell personnel overseas and those seconded to direct its relevant New Zealand operations had contributed to a pattern of accommodating Todd's wishes where they did not fully align with Shell's. Project Ulysses was an initiative driven by New Zealand based Shell personnel determined to stand up to Todd, and not make further concessions.
- c) Shell executives responsible for the detailed negotiations with Todd executives on the terms for production at Pohokura suffered high levels of frustration at the tactics employed by Todd.
- d) The terms of all parties' dealings with the other JV partners were selfishly focused. In Todd's case, they were combatively presented, and lacked a sense of "give and take" that might be expected in a reasonably conducted, significant JV of this type. It seems more likely than not that the built-up antagonism in the relationship left Todd executives believing that such combative tactics were justified. In Mr Richard Tweedie's reply brief of 22 December 2009,

¹³² Analogy with classic administrative law unreasonableness, per *Associated Provincial Picture Houses Ltd v Wednesbury Corporation* [1948] 1 KB 223.

commenting on Mr Bansal's brief that had sought to justify Shell's desire to reduce Todd's level of control over STOS, Mr Tweedie volunteered:¹³³

Frankly, I can only view this behaviour on all these fronts as obsessive, self-serving, and an on-going attempt to beat Todd into the ground. It is truly a David and Goliath struggle, a little New Zealand company trying to act in its and New Zealand's best interests, versus the might of a large multinational, only interested in itself and going to any lengths to get its way.

There is obviously a stark difference between the relative extent of financial and other resources, as between Shell and Todd. However, in the particular context of their dispute over production from Pohokura, I am not persuaded that that disparity of resources has been relevant. Todd has brought skill, determination and continuity of personnel to counter Shell's initiatives.

- e) In a largely oral corporate environment the relatively sparsely-documented approach adopted by Todd executives would have been similar to the aggressive advocacy of Todd's position in extensive embellishments to the answers in cross-examination given by all of Messrs Richard and Hamish Tweedie, and Mr Hall.
- f) There is evidence of personal sentiments on the part of Shell personnel that were clearly anti-Todd.
- g) To the extent that majority decision-making is relevant to JV governance, Shell enjoys negative power because a majority vote cannot be achieved without it. That is an appropriate reflection of Shell having nearly twice as much money at stake and the relative size of its share of the JV cannot influence the extent of good faith obligations owed.

[251] I further find:

¹³³ Paragraph 16.

- a) There was an absence of good faith in Shell and OMV covertly concluding an alignment agreement, thereby committing them to vote together on the operating committee. Whatever prior consultation occurred between Shell and OMV before any particular issue was for determination by the operating committee, the commitment made in the alignment agreement may well have prevented Shell and OMV from considering the different views articulated for Todd with an open mind.

- b) Shell's initiatives to prepare itself for separate marketing of Pohokura gas, before conveying to Todd that joint marketing initiatives were at an end, showed a lack of good faith.

[252] Although the protracted course of difficult dealings with Todd generated expressions of hostility towards Todd among Shell executives, I do not find that Shell's conduct in the governance of the Pohokura JV was motivated by a desire or intention to harm Todd's interests. Certainly, if pursuit of the course intended to best advance Shell's wider interests incidentally harmed Todd's interests at Pohokura, then Shell would not have altered its stance to avoid that harm, but I am not satisfied that any of Shell's relevant conduct in respect of Pohokura occurred for the purpose of harming Todd.

[253] These findings lead to the question whether Shell and/or OMV's participation in the operating committee decisions to approve the off-take rules and nomination protocols, or thereafter in approving WP&Bs, was sufficiently tainted by lack of good faith to require any of those decisions to be struck down, assuming they are otherwise valid.

[254] Here, well-resourced and thoroughly experienced parties have inherited a comprehensively documented JVOA. Where a discretionary power has been found by the Court to fall within those contractual terms, it is not appropriate for the Court to consider whether the power should not be exercised, because the opposing party treats the stance of the majority as lacking good faith. Here, I have found that the majority of the forms of good faith obligation pleaded by Todd cannot be made out.

[255] I am satisfied that the limited failures to act in good faith in dealing with Todd that are identified in [251] above do not fall within any of the forms of good faith obligations pleaded by Todd and nor are they sufficiently related to the harm Todd alleges in the contractual context to give rise to any relevant liability. The course of operating committee meetings between conclusion of the alignment agreement in early April 2004 and the commencement of production in September 2006 was not considered in detail in the evidence. On certain issues, it ought to have been reasonably apparent to Todd that Shell and OMV were debating the issues in Todd's absence. After all, Todd absented itself from meetings it was invited to at various times. In other contexts, Todd would reasonably have been misled into thinking that the stance to be adopted by the parties was still open for debate, when private arrangements between Shell and OMV made pursuant to the alignment agreement meant that that was not the case.

[256] In the end, however, it was more or less inevitable that operating committee resolutions would progress along the lines that they did. Todd's opposition to the form of GBA proposed by Shell relied on the interpretation Todd preferred of Article 10.1, but Shell and OMV would not agree to that. Shell's resort in the alternative to a set of rules that would permit limited flexibility of off-take was predictable. It may be that Shell had enhanced confidence in promoting the off-take rules because of the alignment agreement, but by March 2004 differences between OMV and Todd made OMV support for the off-take rules a logical consequence, irrespective of the alignment agreement.

[257] In the end, I have upheld the lawfulness of the procedure adopted by Shell and OMV. Some variant on it was virtually inevitable given the irreconcilable differences arising from the different views adopted as to interpretation of the relevant provisions of the JVOA.

[258] Further, I find that the terms of the inclusion in WP&Bs of levels of annual production around 70 PJ/a are consistent with a view that was genuinely open to the joint venturers on the optimal off-take from the field. Those decisions are clearly not arbitrary, capricious or perverse. They are consistent with all the earlier projections

and are decisions that would more likely than not have been made by majority Shell/OMV vote, regardless of the undisclosed alignment agreement.

[259] Mr Taylor argued for Shell that none of the steps taken to protect its own interests within the JV could be in breach of any implied obligations. I raised with him the instance of Shell retaining a consultant to advise it on the preferable means for separate marketing of Pohokura gas in the week before advising Todd that Shell and OMV were no longer prepared to work with Todd on terms for joint marketing of the gas.¹³⁴ If there were obligations to act with the utmost good faith, then Shell could gain advantages, theoretically at least, by stealing a march on the other parties in preparations for separate selling. In terms of commercial morality, that would be sneaky, to say the least.

[260] However, in the end I am persuaded that the relatively exhaustive definition of obligations owed by each joint venturer, and the carefully defined limits on the scope of joint operations to which the JV was subject, did entitle all of the parties to protect and advance their own commercial interests. The conduct I have instanced was not a complaint pleaded by Todd against Shell. In the end, Shell's head start did not harm Todd and I am satisfied Todd was able to procure as good, if not better, terms for sale of its first tranche of Pohokura gas than Shell was. It follows that no loss could possibly arise.

Breach of fiduciary duty

[261] Todd's seventh cause of action pleads breach by Shell, in its capacity as the operator for the Pohokura JV, of fiduciary duties owed to Todd. Todd alleges that in its capacity as operator, Shell:

- a) failed to act in the best interests of the Pohokura joint venturers;
- b) preferred the interests of one or more of the joint venturers (being itself and/or OMV) over the interests of another joint venturer (Todd);

¹³⁴ CB6573-6576, 26 March 2004.

- c) exercised a power or discretion conferred on it by the JVOA for an extraneous purpose, namely to suit commercial purposes of itself and OMV outside the scope of the Pohokura JV.

[262] The position of operator as defined in the JVOA is to be undertaken by a party to it. That reflects commercial sense, and what I understand to be industry practice that such ventures are managed by one of those who have researched the prospect and invested in it. Subject to having the requisite range of expertise, there is also some sense in the venturer having the largest interest in the field being the entity directly involved in its operation, by means of assuming the role as operator.

[263] The imputation of fiduciary obligations, in addition to the contractual obligations assumed, does not arise by virtue of the status of the relationship between the joint venturers and the operator delegated to act on their joint behalves. The existence of any fiduciary obligations, and their extent, requires a situation-specific analysis of the nature of the relationship to identify the respects in which, if at all, the joint venturers are obliged to repose trust and confidence in the integrity of the operator.¹³⁵

[264] It is implicit in such an analysis that a finding that one aspect of the relationship has a fiduciary character does not mean that obligations of a fiduciary kind can be overlaid on all that the operator does on behalf of the joint venturers. There are many aspects of the diverse tasks required of the operator that can adequately be carried out by it as agent for the venture solely on the terms of contractual responsibilities assumed as a commercial agent.

[265] Here, the operator does exercise powers on the parties' behalf and in their interests. However, Shell denies the existence of any fiduciary obligations. First, because of the terms of Article 15.1(A) of the JVOA, which stipulates that "the parties" shall not be considered fiduciaries, except to the extent expressly provided in the agreement. The definition of "operator" in Article 1 of the JVOA:

¹³⁵ See, for example, the Supreme Court decisions in *Chirnside v Fay* [2007] 1 NZLR 433 at [75], [85]; and *Amaltal Corporation Ltd v Maruha Corporation* [2007] 3 NZLR 192 at [21].

...means a Party to this Agreement designated as such in accordance with this Agreement, and acting in that capacity and not as the owner of a Participating Interest.

[266] On the basis of this definition, Shell argues that the exclusion of fiduciary relationships as between “the parties” also extends to it qua operator, as the definition includes the operator within the scope of “parties”.

[267] I am not persuaded that the reference to “the parties” in Article 15.1 extends to the status of the party that is the operator, when considering the position of that entity as operator. The terms of the definition of “operator” explicitly recognise the different capacities to be attributed to the operator when acting as such, contrasted with its role as one of the owners of participating interests in the venture. It follows that Shell, in its capacity as operator, does not fall within the provision at the end of Article 15.1(A) that negatives the existence of fiduciary relationships.

[268] Shell is on stronger ground in denying liability as operator, for anything undertaken by STOS until the end of March 2006. To the extent that fiduciary obligations are attributed by Todd to the operator in relation to conduct up until that time, clearly the claim must fail as against Shell.

[269] Shell also invites an analysis of the detailed contractual provisions defining the rights and obligations of the operator, in support of a submission that they adequately protect the joint venturers’ interests and leave no room for the implication of additional obligations. The particular conduct pleaded against the operator as breaching fiduciary obligations is implementing the off-take rules, nomination protocols and work programmes in the 2006 to 2009 years. The criticism is that Shell assessed total production available at a constrained level and thereafter constrained production to that level.¹³⁶

[270] Shell’s specific response to this is that the role of the operator in these matters was to present proposals to the joint venturers, but the joint venturers did not abrogate their decision-making power to the operator. The joint venturers approved the off-take rules, the nomination protocols, and thereafter each of the WP&Bs

¹³⁶ 3rd ASC, paragraph 89.

containing total production figures. Shell argues that that process is not one in which there is any scope for reliance and dependence by the joint venturers on the integrity of the operator to cater for all of their interests. It was open to any of the joint venturers to direct the operator to produce more information and similarly open to any of the joint venturers to argue for the adoption by a majority of them, of amended WP&Bs. OMV puts it more bluntly that Shell cannot have a fiduciary obligation to act inconsistently with operating committee instructions, and that is inarguably correct. If the operating committee had capacity to introduce the off-take rules and vote on the WP&B as proposed, then criticisms of the operator's role in proposing and subsequently carrying out such matters add nothing. Conversely, if the operating committee did not have the requisite capacity, then the operator's contributions to its error also add nothing in legal terms.

[271] During the period in which STOS was the operator at Pohokura up to the end of March 2006, its work appears to have been carried out substantially by Shell employees with appropriate expertise seconded to work for STOS. After Shell became operator, the personnel on the ground appear not to have changed significantly. In settling the arrangements as to how the mechanics of production and delivery of product to the joint venturers were to work, there was on-going and relatively close liaison between STOS/Shell personnel for the operator on the one hand, and personnel representing Shell's interest as a joint venturer, on the other. One important contributor to that for Shell's JV interest was Mr Jackson who described in his evidence how STOS personnel "pleaded" for guidance on how operational matters were to work.¹³⁷

[272] I am satisfied that the form in which Shell as operator proposed nomination protocols, and the form in which each of the WP&Bs were presented to representatives of the JV on the operating committee, were influenced by Shell's perspective as a joint venturer.¹³⁸ However, there is no allegation against Shell as operator that it suppressed relevant information, or misled the joint venturers when seeking approval for either the nomination protocols, or WP&Bs. The nature of the

¹³⁷ T2246/16, T2435/13.

¹³⁸ For example, CB10055, 20 December 2005 internal Shell email suggesting agenda items including "Influencing and coaching STOS, eg WP&B and GMP".

relationship between Shell personnel attending respectively to the operator and JV interests would have been apparent to Todd throughout, even if it was not aware of the minute detail of the communications flowing between them. The influence of Shell's interest as joint venturer on the form and content of the operator's proposals to the joint venturers is likely to have resulted in presentations that were different to the presentations made if Shell's JV interest exerted no influence at all over those communications.

[273] I am satisfied that the operator's obligations to joint venturers in this part of its work were not subject to fiduciary obligations. It was not a function in which the joint venturers were vulnerable to discretionary judgements made on their behalf by the operator, nor did they vest decision-making power in the operator. All joint venturers were keenly aware of the issues. Todd's opposition to the constraint on level of production relied on legal advice to the effect that it contravened Article 10. Todd was entitled to demand additional information, and did not depend on the operator's integrity in making any relevant decisions which indeed were taken by the joint venturers themselves. Even if some limited fiduciary obligation arose in respect of the objectivity with which the operator presented proposals to the operating committee for consideration, then the "slant" resulting from a recognition of, and playing to, the interests of Shell as joint venturer would not constitute a material breach of such fiduciary obligations. The remedy for other parties was in their own hands, and lack of vulnerability in respect of JV decisions clearly takes the relationship outside the circumstances in which fiduciary obligations could be imputed to Shell as operator.

Breach of the Crown Minerals Act 1991

[274] It is convenient to deal next with the last claim challenging the contractual position. Todd's eleventh cause of action pleaded that the off-take rules were in breach of s 41 of the CMA because Ministerial consent was required and was not obtained. Consequently, Todd claims that they are of no effect.¹³⁹

¹³⁹ 3rd ASC, paragraph 108.

[275] Section 41 of the CMA provides:

41 Transfers and other dealings with permits

(1) In this section—

Agreement includes a contract or deed and an arrangement; but does not include an access arrangement:

Transfer includes assign.

(2) No permit holder or any other person shall enter into an agreement (except by way of mortgage or other charge only) which—

- (a) Transfers a permit; or
- (b) Creates any interest in or affecting any existing or future permit; or
- (c) Transfers or otherwise deals, either directly or indirectly, with any interest in or affecting any existing or future permit; or
- (d) Imposes any obligation on the permit holder which relates to or affects the production of minerals from the land to which the permit relates or the proceeds of such production—

unless the agreement is entered into subject to the consent of the Minister and an application for such consent is made within 3 months after the date of the agreement.

(3) The Minister shall consent to an agreement of the kind referred to in subsection (2), on such conditions as he or she thinks fit, unless in his or her opinion special circumstances exist. Before making a decision in respect of any such agreement, the Minister may require the production of such information relating to the agreement as the Minister considers necessary or desirable.

(4) An agreement which is subject to the consent of the Minister under this section shall not have any effect unless application for the Minister's consent is made in accordance with subsection (2) and the Minister consents to the agreement.

(5) All conditions of the Minister's consent under this section shall, for the purposes of this Part, be deemed to be conditions of the permit concerned.

...

[276] I accept the essence of a number of arguments advanced on behalf of Shell or OMV as to why the off-take rules fall outside the “agreements” to which s 41 relates. First, assuming the off-take rules constitute “an arrangement” for the purposes of the

definition of “agreement” in s 41(1), then it has not been entered into by someone other than the permit holder, which is a necessary pre-requisite. The definition of “permit holder” in s 2 of the CMA includes all those who have a share in holding the permit. Accordingly, all the parties here constitute a single entity as the permit holder, and it is only their joint status, when entering into an arrangement with a third party, that is the subject of the provisions in s 41. If the off-take rules were internal operational arrangements to facilitate the disposition of production between, say, two wholly owned Todd subsidiaries that between them owned all of the permit, then such rules would not be the source of obligation on Todd as the permit holder. Nor would they create any effect on the production of minerals that did not already arise under the terms of the permit granted to those Todd companies. The position can be no different merely because different commercial interests comprise the holders of the permit.

[277] Second, I am satisfied that the purpose or effect of the off-take rules is not caught by the types of content contemplated in s 41(2). Clearly, the off-take rules do not address any of the matters in subs (2)(a) to (c) (ie they neither transfer the permit, create any interest in or affecting any existing or future permit, and nor do they otherwise deal directly or indirectly with any interest in or affecting the permit). Accordingly, the off-take rules could only constitute a relevant agreement because they imposed some obligation on the permit holder relating to or affecting the production of minerals, or the proceeds of such production under subs (2)(d). I consider that those concepts ought to be interpreted in light of the purpose of s 41 generally and, more particularly, in light of the mischief intended to be addressed by the requirement to obtain the consent of the Minister in respect of agreements reflecting the more specific forms of activity described in sub-paragraphs (a) to (c).

[278] In the decision in *Greymouth Petroleum Holdings Ltd v Attorney-General*, Miller J observed:¹⁴⁰

...section 41(2)(d) serves a clear legislative purpose, which can be deduced from s 41 itself, of ensuring that the Crown knows the identity of all those with a degree of control over permits. Section 41(2)(d) itself points to a

¹⁴⁰ *Greymouth Petroleum Holdings Ltd v Attorney-General* HC Wellington CIV-2004-485-1115, 3 October 2005 at [39].

concern with control, because it attaches to agreements that impose “any obligation on the permit holder” relating to production or to its proceeds.

[279] The Minister has a legitimate interest in knowing the identity of all of those who can influence the manner in which the work required to comply with the terms of the permit is carried out, with an exception for those who are merely financiers. Therefore, s 41 is concerned with the identity of those other than a permit holder who might be involved in such arrangements where the arrangements create the ability for parties other than the permit holder to exert any influence over the production of minerals in accordance with the permit. That ability could arise because of some obligation assumed by the permit holder in favour of the third party.

[280] In contrast, the off-take rules are an intra-permit holder arrangement of a type provided for by the JVOA. They do not create any prospect for someone other than the permit holder to affect how the permit is operated.

[281] Third, s 41 is not concerned with compliance by a permit holder with the terms of the permit. Section 33 of the CMA separately provides that every permit holder is to comply with the conditions of the permit and with the Act, and that where the permit is held by two or more persons they are jointly and severally liable for those obligations. In addition, ss 100 to 103 make it a strict liability offence to fail to comply with the terms of a permit. An applicant for an exploration permit (needing standing as the holder of a prior prospecting permit) is required by s 43 of the CMA to submit a work programme which is to be approved by the Minister, and compliance with the work programme can be expected to be a condition of the permit issued. The provisions enabling the Ministry to check on compliance have led to regulations obliging a permit holder to supply to the Secretary, not later than 40 working days after the end of each half year, a report on the mining activities and any production operations that have taken place under the permit during that half year. Such reports must also include projections in relation to the following half year that enable compliance, and levels of performance, to be monitored.¹⁴¹

¹⁴¹ Crown Minerals (Petroleum) Regulations 2007, reg 39 and Schedule 6, Part 2, clause 17.

[282] These other provisions reinforce the point that the focus of s 41 is on those able to exert influence over the conduct of the permit, rather than how work pursuant to the permit is undertaken.

[283] Fourth, the legislative history of the section further reinforces this conclusion. Section 41 is, by and large, a re-enactment of s 23 of the Petroleum Act 1937. The marginal note to s 23 states “Approval of instruments creating interests in licences”. When analysed alongside s 33, the inference arising from that marginal note is that the section is concerned with the creation of new interests in a licence or imposing of obligations on a licensee thus giving a third party some new control over the production of (in the case of the Petroleum Act) petroleum. To accept the interpretation offered by Todd would limit both Shell and OMV’s right to utilise their property interest. In circumstances where there are other means, namely s 33, by which the Crown can enforce the abovementioned purposes of s 41, such an interpretation should not be adopted.

[284] Submissions for Shell and OMV also raised an inconsistency in Todd’s claim that the off-take rules are in breach of s 41, when the same argument was not made in respect of the JVOA, in reliance on which Todd sues Shell and OMV. The JVOA was not the subject of a s 41 approval, and Mr Hall was inclined to accept that such joint venture agreements do not require s 41 approval.¹⁴² On the above analysis of s 41, that view is correct, but the inevitable corollary is that the off-take rules are similarly outside the scope of s 41.

[285] Given the clear exclusion of the off-take rules from the scope of s 41, it is not necessary to consider Shell and Todd’s counterclaim for relief under the Illegal Contracts Act.

Inter-connection dispute

[286] It is sufficient to deal with Todd’s first four causes of action, and the counterclaims on behalf of Shell and OMV, somewhat cursorily relative to the

¹⁴² T927/11-13.

detailed arguments that have been presented on these causes of action, largely because matters have moved on in certain material respects since the issues arose.

[287] Todd's causes of action pleaded an entitlement to connect its pipelines variously in reliance on:

- rights to connect claimed to arise directly out of Article 10.1 of the JVOA;
- the access agreement concluded when the parties recognised that two sets of pipes would be used to export product from the PPS;
- the August and September 2005 and January 2006 resolutions about progressing terms for that access agreement, or because that course of conduct gave rise to an estoppel precluding Shell and OMV from resisting Todd's inter-connection;
- reasonable reliance on matters that had occurred previously;
- the resolution requiring completion of the inter-connection deed as a pre-condition to Todd connecting its pipes to the PPS being an invalid resolution and therefore an unenforceable requirement inconsistent with Todd's rights; and
- the terms of the inter-connection deed itself being invalid by virtue of its purporting to adopt the off-take rules and nomination protocols.

[288] For their parts, Shell and OMV sought declarations confirming the lawfulness of insisting on completion of the inter-connection deed where its terms cross-referenced the off-take rules and nomination protocols, as a pre-condition of permitting Todd to connect its export pipelines in the vicinity of the PPS.

[289] At the time of the interim injunction argument before Harrison J in early August 2006, the parties were at a stand-off that does not reflect rationally on the stakes that were at issue. Todd had been invited to complete the inter-connection

deed without prejudice to its entitlement to challenge the enforceability of the off-take rules and nomination protocols. Todd countered that it ought not to be required to complete an inter-connection deed that made any reference to those documents at all, and maintained that it was adequate for it (as it had done) to complete an inter-connection deed addressing matters other than the references or incorporation by implication of the off-take rules and nomination protocols. In retrospect, the difference between those two positions appears more theoretical or tactical, than real.

[290] Since a decision in mid 2005 that Todd would not share export pipelines with the other joint venturers, Todd had proceeded with plans for its own export pipelines and spent some \$10 million in constructing pipelines and obtaining appropriate consents for their use. In these circumstances, and with the benefit of hindsight demonstrating that the physical aspects of inter-connection have worked satisfactorily without incident for nearly four years, there is a certain inevitability about Todd having been granted an interim injunction, as it was on mandatory terms, to facilitate the inter-connection of its export pipelines.

[291] I have now found that the operating committee could resolve to adopt off-take rules by majority decision, and further that the nomination protocols, dealing with relatively mechanical matters, were promulgated lawfully within the terms of the JVOA. However, that does not necessarily lead to the conclusion that Shell and OMV were entitled to insist on Todd executing an inter-connection deed that novated or in any way required Todd to acknowledge the obligations arising from the off-take rules and nomination protocols. Mr MacDonald, the corporate counsel at Shell who was supervising the documentation for pipeline access, was cross-examined on the need for cross-referencing and rather graphically observed that he did not think "...you need to kill someone twice".¹⁴³ I took that observation to reflect that if the off-take rules were valid and binding on all parties on their own terms, then there was no point in requiring any separate acknowledgement of those

¹⁴³ T4308/12.

obligations as a condition of inter-connection. Conversely, if the off-take rules had not been validly introduced, then any purported independent acknowledgement of the obligations they address would not give them validity.

[292] Relations were strained between the parties in the months leading up to the production of first gas in September 2006. I can appreciate the reluctance Todd would have to yield to pressure to sign an inter-connection deed making reference to the off-take rules and nomination protocols or incorporating those documents by implication, even on terms acknowledging that completion of the deed in that form was without prejudice to Todd's rights to challenge those provisions. Subsequent vindication of Shell and OMV's contractual analysis does not warrant recasting the situation that confronted Todd at the time. On this aspect of the case, I am not prepared to hold against Todd's entitlement to inter-connection, where it had committed to all the relevant provisions except those referring to or relying on the off-take rules and nomination protocols.

[293] I understood from counsel that all other operational matters that need to be addressed as between the operator on behalf of the JV, and a party controlling the export of production from the PPS, are adequately dealt with in the inter-connection deed. For OMV, Mr Stephens identified one situation in which cross-reference to the off-take rules and nomination protocols is required. That is to deal with the contingency that the entity owning the pipes and entitled to the benefit under the inter-connection deed is not a member of the JV, and is therefore not bound by the off-take rules and nomination protocols. Mr Stephens instanced the fact that the EPJV, a JV formed by Shell and OMV, is the owner of the other set of export pipelines from the PPS, and in contractual terms it is not bound to the off-take rules and nomination protocols because that JV is not a party to the Pohokura JV. Mr Stephens' concern only becomes material if the benefit of the inter-connection deed is able to be assigned by Todd to a non-party to the JV. That could occur without the operator or the Pohokura JV being entitled, as a condition of consenting to any such assignment, to require any such assignee of Todd's interest to commit to being bound by the terms of the off-take rules and nomination protocols, so far as

they relate to exports through those pipes. Addressing that concern should be a simple drafting matter.

[294] It follows from this analysis that it would be inappropriate to make any of the declarations that were sought in competing terms by the parties, and I am not persuaded of the need for formal declarations in any terms. The present position, which is sufficient to reflect the rights and obligations of all parties, is that inter-connection of export pipelines is sufficiently regulated by terms such as those in the inter-connection deed, but excluding any explicit or implied novation of obligations under the off-take rules and nomination protocols. Unless my findings on the interpretation of the JVOA are overturned, those provisions, or hopefully some unanimously agreed substitute for them, will regulate processes for off-take. Inter-connection of all export pipes can continue with all parties' interests adequately protected, independently of the terms applying to off-take. Whilst the subject matters of off-take and inter-connection abut, they do not overlap.

[295] In the event that the benefit of such an inter-connection deed is assignable, one condition on which consent to such assignment may be granted becomes relevant. Consent to assignment should reasonably include an obligation, in the case of a non-Pohokura JV assignee, to acknowledge the need for inter-connection rights to be exercised only on terms that conform to any off-take rules and nomination protocols, or other sources of substantially similar obligations.

[296] Accordingly, whilst all of Todd's claims for breach of contract have failed, the practical imperative for it to secure connection to the PPS on terms not prejudicing the interests of the JV or the other parties, is confirmed. I will return to a summary of the outcome of the contract claims at the conclusion of the judgment.

The Commerce Act claims

[297] Independently of Todd's claims that the constraint on the extent of production breached its contractual entitlements, Todd pleaded three additional causes of action that the production constraint breaches ss 27, 30 and 29 of the Commerce Act (the Act).

[298] In its eighth cause of action, Todd pleads that the off-take rules, the nomination protocols and the 2006-2009 work programmes (jointly referred to as “the off-take documents”) constitute contracts, arrangements or understandings between Shell and OMV within the meaning of ss 27, 29 and 30 of the Act. Shell and OMV are alleged to have given effect to an arrangement or understanding between them in the off-take documents that has the purpose, effect or likely effect of substantially lessening competition for the purposes of s 27 of the Act, by limiting production below the total production available, or artificially limiting production from Pohokura. This has occurred in what is pleaded as the national natural gas production (and first point of sale) market.

[299] In its ninth cause of action, Todd relies on the same conduct to plead a breach of s 27 “(via s 30)”, alleging that the off-take documents have the purpose, effect or likely effect of controlling, maintaining or providing for the controlling or maintaining of the price of gas. This has occurred where the parties are alleged to be in competition with each other for the supply of gas from Pohokura and elsewhere.

[300] Todd’s tenth cause of action under s 29 of the Act pleads that the off-take documents constitute exclusionary provisions for the purposes of that section, in that they were entered into by Shell and OMV over Todd’s opposition for the purpose of limiting production at Pohokura and thereby limiting supply of Pohokura gas to potential purchasers. This is alleged to arise in circumstances where potential purchasers, as well as Todd’s affiliate Nova Energy Limited, are in competition with Shell, OMV and Todd for the supply of Pohokura gas.

[301] On all the Commerce Act causes of action, Todd claims declarations of contravention of the respective sections, injunctions prohibiting Shell and OMV from giving effect to the off-take documents, damages pursuant to s 82 of the Act, and exemplary damages pursuant to s 82A of the Act.

Cause of the claimed constraint

[302] Todd’s claims under the Act were brought irrespective of the outcome of its contract claims, so that the conduct of Shell and OMV complained of is argued to be

contrary to the Act, even if it is permitted on the interpretation of the JVOA preferred by the Court. Approaching the matter from that perspective, Todd's arguments face an important preliminary hurdle. In his reply submissions, Mr Farmer clarified that on this part of the case, Todd did not argue that Shell and OMV had also to take production full-out, which is the consequence of Todd's interpretation of Article 10.1 on its contract claims. Rather, they just could not prevent Todd from doing so. However, Shell and OMV's conduct did not unconditionally prevent that occurring. Rather, they had made a higher rate of extraction of gas by any party conditional on completion of a commitment to a set of rules by which the unequal levels of off-take would later be redressed. This was to be the subject of a GBA, proposed by Shell in November 2005 after discussions at a much earlier time about the basis for a GBA failed because of fundamental differences about the rate of extraction.

[303] Todd's opposition to the proposed terms of a GBA was because Todd treated the terms proposed as inconsistent with its contractual rights. Todd asserted a right to have access to at least its share of the maximum capacity at which the plant could produce on a daily basis, rather than accessing its proportionate share of a lower level of production settled by the annual budgetary process.

[304] Todd's own proposals went further than this expectation, for instance asserting an entitlement to its share of any extent of underlift by another party, on any day.¹⁴⁴ A potential consequence of Todd's proposal was that an underlifter was exposed to the risk that it would not retrieve its overall share of production from the field later in the life of the field before the resource was exhausted. In addition, on Todd's approach, an underlifter would have no mechanism (and arguably no right) to be reimbursed for the value of property forgone.

[305] We consider it more likely than not that if Todd accepted the limits on its contractual position consistent with the interpretation determined in the contract aspect of this judgment, then the parties would have concluded a GBA before

¹⁴⁴ CB9845.

commencement of commercial production at Pohokura. It may not have been in the form proposed by Shell, but would have permitted flexibility for over and underlifting, subject to a mechanism for redressing the imbalances at a subsequent time. We accept the evidence of economists to the effect that concluding a GBA was the entirely rational response once the parties were not distracted by differences over the interpretation of the contract, and Todd's asserted right to require Pohokura to produce full-out all the time had been rejected.¹⁴⁵

[306] The structure of the JV is that each party contributed to all the costs of production of gas and condensate, proportionate to their equity interest. Therefore, the parties would reasonably expect to earn returns commensurate with that level of investment. In addition, flexibility in the levels of off-take has value. A set of rules permitting flexibility and providing predictable and fair mechanisms for redressing imbalances is then, objectively, no more than a matter of commercial common sense. Todd's own analysis of how it would manage its various production interests on a portfolio basis implicitly recognises value in flexibility.¹⁴⁶ There is no basis for suggesting that the principles underlying Shell's proposed GBA were at odds with the contractual interpretation. Nor did Todd argue that if it lost the contractual arguments, it was nonetheless reasonable for it to refuse to negotiate mutually agreeable terms.

[307] Certainly, we are not prepared to find, as Todd's competition case would require, that Shell and OMV would still have blocked Todd's access to larger volumes of gas, had Todd accepted the contractual position as analysed in this judgment. In the absence of perversity and irrationality, such acceptance would have led to a process for resolving ultimate discrepancies in the level of off-take.

[308] We are unable to accept, in light of all the history of dealings between the parties and the critical importance of their opposing views on the application of the JVOA, that any scenario would have developed in which, in the absence of the off-take rules (or a GBA), Shell and OMV would have permitted a pattern of

¹⁴⁵ For example, Hausman brief, paragraphs 57, 59.

¹⁴⁶ See, for example, Hamish Tweedie's June 2006 analysis quoted in [90] to [93] above.

conduct in which Todd procured production of more than its share of agreed volumes of gas. Any circumstances in which the off-take rules were banned would not realistically lead to a capitulation by the majority to the minority, without resolution of the conflicting claims on the interpretation of the JVOA. A ban would therefore lead to a stalemate. In light of the meaning of the contract, all likely roads seem to us to lead to agreement on some terms that would permit inconsistent levels of off-take of production, but only on terms protecting all parties' entitlements to a fair process for redressing imbalances.

[309] In short, Todd has had the remedy for accessing larger volumes of gas in its own hands. Shell and OMV concerns to have a GBA in place before allowing material discrepancies in the level of off-take were not unreasonably required to protect their interests in production from Pohokura, and we are satisfied that had Todd agreed to terms consistent with the contractual interpretation it has thus far rejected, then it could have obtained access to larger volumes of gas.

[310] Notwithstanding that Todd's case was closed on the basis that the Commerce Act claims were pursued irrespective of the outcome on the contract claims, certain parts of the Commerce Act analysis on Todd's behalf require its view of the contract to be upheld. For instance, it was important to Todd's analysis of the consequences of it producing its portion of Pohokura at full capacity, that this initiative would lead to an inevitable response by Shell and OMV to match Todd's level of production. We are satisfied that such an imperative would only exist if Shell and OMV were concerned not to fall significantly behind Todd in terms of the shares of production taken, in circumstances where there were no binding arrangements that would commit Todd to redress the imbalance later. Attributing that predicament to Shell and OMV requires either acceptance of Todd's interpretation of the contract (ie requiring the plant to produce at capacity at all times in the absence of unanimous agreement to the contrary), or that Todd could prevent the majority using the off-take rules as they have, and force production full-out, without any commitment to redress imbalances. Todd's analysis in identifying a substantial lessening of competition

(SLC)¹⁴⁷ depended primarily on an extent of difference in the level of production between the factual and counterfactual that involved all three parties increasing the level of their off-take from Pohokura to the plant's capacity, rather than just Todd in respect of its 26 per cent share. However, in light of the Court's interpretation of the contract, such an outcome is not among those reasonably entertained as likely.

[311] Because Todd has based all its dealings with Shell and OMV in relation to Pohokura on an untenable interpretation of the contract regulating their relationship, it is hardly appropriate to treat the circumstances of production as they have occurred as "the factual" for purposes of contrast with the "counterfactual" (ie how matters would have played out in the absence of the conduct Todd complains of). In the factual, Todd complains of a constraint on the amount of production it has been able to call for from Pohokura, but that constraint has been materially contributed to by Todd's insistence on a view of the contract which has not been upheld. Absent that error on Todd's part, the factual situation would more likely than not have been different in that the constraint on the level of production Todd complains of would not have been present. In these circumstances, the factual situation reflecting the position that was correct in law, and the counterfactual situation in which the constraint did not exist, become the same.

[312] We consider this to be a fundamental impediment to Todd's complaints of conduct by Shell and OMV that is in breach of the Act.

Market definition

[313] There is a second preliminary difficulty with Todd's Commerce Act claims. That is its failure to make out the functional dimension of the market in which it pleaded the anti-competitive conduct occurred.

[314] Section 3(1A) of the Act specifies that the term "market":

¹⁴⁷ Our analysis adopts a rule of thumb that a lessening in competition would be "substantial" if the challenged conduct has caused between, say, a 5 and 10 per cent difference in prices relative to prices in the absence of that challenged conduct.

...is a reference to a market in New Zealand for goods or services as well as other goods or services that, as a matter of fact and commercial common sense, are substitutable for them.

[315] In the evidence from five economists that we will review below, there were diverse strands of analysis on the relevant dimensions of the market in which the production and sale of Pohokura gas occurs. However, we are satisfied that the market in which Pohokura gas is sold is wider than the market for natural gas production and first point of sale¹⁴⁸ because producers of gas compete in its sale with wholesale traders in gas, such as Contact Energy and Vector. Wholesale traders are not producers, but can compete with producers in re-selling gas they acquire at a “first point of sale”.

[316] Closing submissions for OMV and Shell argued that Todd was obliged to make out the existence of the market it had pleaded, that Todd had failed to do so and that, in the absence of this essential element of the causes of action under the Act, they must all fail. Analogy was invited with the decisions in *Commerce Commission v Bay of Plenty Electricity Ltd*¹⁴⁹ and *Ophthalmological Society of New Zealand Inc v Commerce Commission*.¹⁵⁰

[317] In the first of those decisions, the Commission sought remedies against Bay of Plenty Electricity Limited (BOPE) alleging anti-competitive behaviour in BOPE’s refusal to allow competitors in the business of electricity supply to access meters measuring the extent of electricity supplied to consumers. The Commission alleged that BOPE had taken advantage of substantial market power in one market, namely the Eastern Bay of Plenty electricity metering services market, for the purpose of affecting competition in another market, namely the market for supply of electricity in that geographical area. The Court found that the Commission had failed to make out a separate market within the geographical area for electricity metering services. After considering guidance from earlier cases on the approach to, and purpose for, defining markets,¹⁵¹ the Court assessed the evidence in relation to provision of

¹⁴⁸ As pleaded, paragraph 95, 3rd ASC.

¹⁴⁹ *Commerce Commission v Bay of Plenty Electricity Ltd* (BOPE) HC Wellington CIV-2001-485-917, 13 December 2007, Clifford J and Professor Richardson.

¹⁵⁰ *Ophthalmological Society of New Zealand Inc v Commerce Commission* CA168/01, 26 September 2001.

¹⁵¹ At [281], [282].

electricity metering services in the relevant geographical area.¹⁵² The Court concluded that the Commission had not made out the market it pleaded. It followed that the Commission could not make out its case under either s 27 or s 36 of the Act. The Court noted that no other market formulation was put to it, with the rider that BOPE did not expect to, and did not, respond to any other formulation of the applicable market.¹⁵³

[318] In *Ophthalmological Society*, the relevance of the plaintiff pleading the correct market accurately arose in an interlocutory context. In that case, the Commission sought to amend the market in respect of which it alleged anti-competitive behaviour by ophthalmologists and the Society. The Commission originally pleaded a market for the supply of routine cataract surgery in Southland, and sought to re-plead this as a market for supply by ophthalmologists of routine ophthalmic procedures in New Zealand. There is a three-year limitation period on such causes of action under the Act, and by the time the Commission sought to amend the scope of the market in which it alleged the anti-competitive behaviour had occurred, more than three years had elapsed since the behaviour complained of. Accordingly, if the amendment had the effect of introducing a new cause of action, it would be time-barred.

[319] The Court of Appeal held, by a majority, that the proposed amendment was sufficiently different to introduce a new cause of action. The Court acknowledged that whether a new pleading was something essentially different from that which had been pleaded earlier must be a question of degree.¹⁵⁴ In so doing, the Court adopted reliance placed in earlier New Zealand decisions on the Australian decision in *Harris v Raggatt*,¹⁵⁵ where the analysis was described as follows:

...to set up a new cause of action, we use the term in a special sense as meaning a 'new case' varying so substantially from what has previously been set up that it would involve investigation of matters of fact or questions of law, or both, different from what have already been raised and of which no fair warning has been given, so that it would be unfair and unjust to the defendant to put him in peril of a judgment founded on the new matter.

¹⁵² At [477]-[482].

¹⁵³ At [492].

¹⁵⁴ At [23].

¹⁵⁵ *Harris v Raggatt* [1965] VR 779 at 785.

[320] The situation in *Ophthalmological Society* was somewhat different in that there the alteration in pleading occurred pre-trial. Therefore, the defendants would have had an opportunity to regroup and recast the terms of their defence, and gather evidence in support of it. Todd sought to apply the reasoning from *Ophthalmological Society*, but distinguished the outcome. Todd argued that not every change in the detail of the market is significant. Further, any difference between the market as pleaded and as found here does not constitute a “new case”, and Todd had not sought to re-plead.

[321] However, those points are not determinative on the issue here. An important element of the cause of action in any case under the Commerce Act is for the plaintiff to plead with appropriate particularity the market in which the conduct complained of is alleged to have occurred. If the Court then finds that the relevant market has different features from the one pleaded, there is an important question of degree as to whether the differences between the market as pleaded and as established mean that the plaintiff has failed to make out a material part of the cause of action.

[322] In the present situation, the issue is whether the whole of Todd’s competition law case ought to fail because of its misdescription of the relevant market. Alternatively, because of the commonality of the substance of its allegations, whether measured against the market as alleged or the different market as made out, should Shell and OMV be expected to have covered sufficient ground in responding to the allegations for their responses to meet the case brought against them in respect of a different market from the one alleged against them?

[323] Instinctively, we are reluctant to hold against Todd on this primary definitional issue. Wholesalers of gas are not in a position to increase the total capacity of the market by generating gas in the way that producers could. In respect of any particular volumes of gas, wholesalers such as Contact or Vector might be seen as simply standing in the shoes of the producer from whom they acquire the gas. Further, intuitively, we incline to the view that the response by such wholesalers in the relevant context, ie where there was a material increase in production from Pohokura, may not be significant and may be relatively predictable.

[324] Their behaviour in respect of quantities they are committed to pay for, whether they take it or not, will depend on their marginal costs in electing to use or on-sell those parts of their gas entitlements. Regarding gas for which they have to pay regardless of whether they take it, it seems likely that they will have developed their own internal bypass prices at which they will, depending on other factors, either on-sell gas, or use internally the gas they do take. Consequently, it might be considered likely that increases and decreases in the consumer price of gas will have asymmetric effects on their behaviour in respect of such gas; a fall leaving them as net consumers and a rise triggering on-sales. So one might anticipate that a fall in prices due to increased Pohokura supply would not induce any change in on-selling activity from these market players.

[325] Assuming that some or all of these Maui contracts have old style “take or pay” provisions under which the buyer has to pay for certain minimum quantities of gas irrespective of whether they are taken or not in each relevant contractual period, then for the quantities governed by that obligation to pay in full irrespective of whether they take the gas, the buyers have a marginal cost of taking delivery that is nil. Unless there is no market for it at all, the buyers would rationally continue to take such quantities of gas rather than lose the entire price paid for it. After dealing with that level of commitment, the marginal cost will essentially be the difference between the capacity fee to which the wholesaler is committed in any event, and the second component of the purchase price payable to the MMCs, namely the delivery fee for actually taking the gas. It might be assumed that such wholesalers would continue to be motivated to market gas, provided the return was greater than that marginal cost. However, we infer that in some Maui contracts, the point of paying the capacity fee is to enable wholesalers to defer for a period the option of acquiring that Maui gas. Accordingly, the theoretical decision being evaluated would in such cases also depend on the wholesaler’s view of the relative margin able to be earned on that same gas if it were to defer taking delivery of it until a later period, coupled with the components feeding into any internal bypass pricing calculations.

[326] There was no evidence as to how wholesalers of gas, as distinct from producers of gas, might respond to any material increase in the volume of gas available in the market. Although it is tempting to infer what seems the

economically rational reaction, quite different economic drivers are likely to influence the conduct by wholesalers in reacting to any increase in output from Pohokura. One aspect of the flexibility available to Contact and Vector, as substantial buyers of Maui gas, is that they need not have regard to the on-going operating costs of Maui. That high level of operating expenses was generally recognised by the economists who gave evidence as likely to have some influence over decisions for the MMCs on their response to an increase in production from Pohokura.

[327] The volumes available to these wholesalers are substantial. In addition to their right of first refusal (ROFR) status at Maui, Vector has a long-term position as buyer of 50 per cent of the production from Kapuni (ie 6.4 per cent of total national gas production in 2008).¹⁵⁶

[328] The problem is that relegating the potential impact of behaviour by wholesalers would be speculative. There was no detailed analysis of the terms on which substantial volumes of gas are available to wholesalers such as Contact or Vector. Various asides were made about the point. For example, Mr Goddard in closing noted that Vector has very flexible entitlements to Maui gas under “the old 367 contract”, throughout at least part of the period being considered, and additional, relatively flexible, entitlements under more recent ROFR contracts. Clearly, such wholesalers have had significant volumes of Maui gas available to them over a period of years on payment of a capacity fee that appears to be less than the wholesale market price for resale of the gas. Those volumes appear to be larger than those wholesalers need for their own generation and retail or industrial resale purposes.

[329] There are meaningful differences in the economic analysis required, when one compares the market as pleaded with the market as established on the evidence. We accept that there is material prejudice to Shell and OMV in having to adjust their analysis, evidence and arguments to rebut the allegations made against them in

¹⁵⁶ Hunt brief, Figure 7: Total Kapuni production 12.8 per cent.

relation to a wider market that includes wholesalers of gas. That prejudice is not as significant as it might be, given that the market is larger than pleaded, and therefore the prospect of the defendants' conduct amounting to an SLC ought to be less. Even so, the change creates prejudice which could not be eliminated when it arose in the circumstances it did. The difference does not have to constitute a "new case" in the pleading sense used in *Harris and Ophthalmological Society*. Rather, the issue is an evidentiary one as to whether Todd has made out a material part of these causes of action. For the reasons analysed above, we are bound to acknowledge that the difference between the market as pleaded and that as established is material.

[330] We are therefore satisfied that Todd has failed to make out a material element of these causes of action, namely the pleaded market in which the activity is alleged to have occurred. It follows that, as in *BOPE*, the allegations of breach of the provisions of the Act must fail.

[331] We treat each of these fundamental obstacles as sufficient to dismiss Todd's Commerce Act claims. In case we are wrong on that, it is appropriate to record our views about the evidence and arguments on the remainder of the elements of the Commerce Act causes of action.

The economic evidence

[332] Todd's principal economic expert was Mr Kieran Murray. Mr Murray is a director of the New Zealand subsidiary of LECG LLC, an international expert services firm employing some 800 experts and professional staff. He is an economist with a particular focus on the energy sector and is based in Wellington.

[333] Todd also called Dr Cento Veljanovski, the managing partner of a London-based competition and regulatory economics consulting practice. Dr Veljanovski concurrently holds adjunct academic positions in the United Kingdom and Australia, and in his private practice has specialised in the economics of competition, regulation and law.

[334] Shell called evidence from Professor Jerry Hausman, a senior Professor of Economics from the Massachusetts Institute of Technology in the United States, where he has held academic positions since the early 1970s. Professor Hausman's academic specialties include econometrics, the application of statistical methods to economic data, and applied microeconomics, involving the study of behaviour by firms and consumers.

[335] OMV called evidence from Dr Gustavo Bamberger, an economist in private practice based in Chicago, USA. Dr Bamberger also has extensive experience in the analysis of competition and antitrust topics.

[336] After service of the briefs from the economists being called by the defendants, Todd served a brief in reply from Professor James Sweeney of Stanford University in California. Because a confidentiality undertaking had been tendered by Professor Sweeney at the inspection stage of preparation of the proceedings, but no brief had originally been served from him, Shell had pursued an interlocutory application to constrain Todd from serving any subsequent brief from him in reply without leave. That application was unsuccessful. The brief subsequently served focused on a response to Professor Hausman's econometric analysis, including the elasticity of demand for natural gas in New Zealand.

[337] All of the economists were eminently qualified to express the opinions they did. Whilst other economists and commentators on their discipline might rank the relative level of pre-eminence some of them undoubtedly enjoy in their respective fields, the views we have come to do not depend on attributing weight to the opinion any of them offered, by reference to reputation. Rather, we have formed views on the various economic issues debated, as best we can, solely on their merits.

[338] Todd's final submissions raised criticisms that the economists called by Shell and OMV had advocated for the case of the parties calling them, and failed to adhere to their obligations as independent experts. We did discern some respects in which some of those called on all sides appeared to identify with the theory of the case propounded by the party calling them. However, we are satisfied that this did not

occur to an objectionable extent and has not impeded the analysis we have undertaken.

[339] All the economists gave evidence in a “hot tub” forum, which involved their respective briefs of evidence being read by the Court before all of the economists were called. Mr Murray and Dr Veljanovski both produced reply briefs and, in Mr Murray’s case, a (third) supplemental brief. Once called, each economist was permitted a relatively short period for an opening statement, and were then cross-examined on the content of their evidence. The course of cross-examinations extended to comments on the answers provided, where appropriate, from others of the economists, and usually a rejoinder from the cross-examinee. However inaptly named, we found the hot tub a convenient form in which to understand the competing opinions, and test the relative strengths and weaknesses of them.

[340] We have analysed the detail of all the competing arguments. We intend no disrespect to the refined level of analysis provided in four and a half days of hot tub evidence and counsel’s subsequent detailed legal arguments on the Commerce Act issues in recording our findings in a somewhat cursory manner. Having done all our own analysis, we are satisfied that additional layers of detail in our reasoning are neither necessary nor desirable.

[341] Putting to one side the two primary objections we have upheld, a summary of the issues arising on the claims under the Act can be appropriately addressed in the following sequence:

- the elements of the relevant market;
- the conduct in likely counterfactuals;
- the market response: what likelihood of a substantial lessening of competition?

[342] In light of those relevant aspects of background, we then analyse the issues arising under:

- section 27, purpose and effect
- section 27 (“via” s 30)
- section 29.

[343] In reviewing the conclusions we draw on each of these causes of action, it is then appropriate to comment on the policy considerations relative to the outcomes. An aspect of that is to acknowledge the competing arguments about the statutory “joint venture defence” that was raised on behalf of Shell and OMV in relation to the cause of action under s 30.

The relevant market

[344] The reason why such causes of action begin with a determination of what constitutes the relevant market is reflected in classic statements as to what the concept is intended to convey:¹⁵⁷

We take the concept of a market to be basically a very simple idea. A market is the area of close competition between firms, or putting it a little differently, the field of rivalry between them – within the bounds of the market there is substitution – substitution between one product and another, and between one source of supply and another – in response to changing prices. So a market is a field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive.

[345] And in the New Zealand context:¹⁵⁸

Generally a market will be identified by reference to the activities of those engaged in commerce, the structures underlying their activities and the perceived susceptibility to change in the medium-term future. In other words what competitors are doing or might reasonably be expected to do indicates the market in which they are participants.

[346] “The market is a multi-dimensional concept – with dimensions of product, space, functional level and time”.¹⁵⁹ Thus there are four dimensions to the concept

¹⁵⁷ *Re Queensland Co-op Milling Assoc Ltd – Proposed Merger* (1976) 8 ALR 481 at 517.

¹⁵⁸ *Port Nelson Ltd v Commerce Commission* [1996] 3 NZLR 554 (CA) at 560.

¹⁵⁹ *Tru Tone Ltd v Festival Records Retail Marketing Ltd* [1988] 2 NZLR 352 (CA).

of “market”: the geographic context, the functional dimension, the product market and the temporal dimension. Each is dealt with in turn below.

[347] As a snapshot of how gas is consumed in New Zealand, we are appending at the end of this judgment, as Appendix 5, Figures 1 and 2 from Mr Hunt’s brief. The first of those is a pie graph depicting the sectors in which gas is consumed, built up from Ministry of Economic Development (MED) data. It shows that electricity generation accounted for some 60.8 PJ of gas consumed in 2008, with industrial uses and petrochemicals accounting respectively for 31 and 28.7 PJ. The second of the graphs charts gas consumption in the various sectors of the economy over the period from 2000 to 2008, and endorsed at the bottom of it is the content of paragraph 15 of Mr Hunt’s original brief providing his comments on the features of gas demand. Notwithstanding other evidence that the MED data is unreliable, these graphs are useful to help sketch the general picture as to gas usage.

[348] Todd’s case was that there is a market for producing natural gas and selling it at a “first point of sale”, whether that be to large-scale consumers using it for electricity generation or co-generation, or for petrochemical manufacture, or to wholesalers who on-sell the gas to industrial, commercial or residential consumers of it (some buyers fit within both categories). The Commission determination authorising joint selling concurred in Todd’s view of the market, although it did recognise some overlap with wholesalers.¹⁶⁰ Mr Hunt’s analysis of MED data on the proportions of production attributable to various field owners in 2008 suggests that Shell accounted in that year for some 50.6 per cent, Todd some 25.4 per cent and OMV some 13.5 per cent of New Zealand gas production. A further six, much smaller, producers accounted for all but 0.9 per cent of the remaining 10.5 per cent of gas produced.

Geographical extent

[349] Natural gas is delivered to consumers by pipeline. It is common ground that the geographical extent of the market is defined by the extent of the pipeline

¹⁶⁰ CB3930, paragraphs 247-249.

network. That is confined to a majority of the major centres in the North Island. Hence, although it is commonly referred to as the “New Zealand” natural gas market, a more accurate description would be the North Island market.

Functional dimension

[350] Todd pleaded its functional dimension as the national natural gas production (and first point of sale) market which encompasses transactions between producers of gas and first point of sale customers. Notwithstanding that pleaded scope, the view expressed in Mr Murray’s first brief was that there were discrete markets for “committed” gas, ie a market for relatively long-term, large sales, and for “uncommitted” gas, namely shorter-term or “spot” sales, generally involving smaller volumes. That distinction was abandoned in Mr Murray’s reply brief.

[351] Both Shell and OMV denied the pleaded market. A criticism advanced for Todd was that neither in their Statements of Defence, nor in the evidence tendered on their behalves, did Shell or OMV offer a definitive alternative as to the scope of the market in which sales of Pohokura gas occurred. Whilst the credibility of a denial may be enhanced by identifying an alternative, there is no obligation for defendants to do so.

Product market

The SSNIP test

[352] A method commonly used by economists to test the definition of a market is the so-called SSNIP test, referring to a “small but significant non-transitory increase in price”.¹⁶¹ This relies on a theoretical test, attributing to a notional monopolist in the purported market, a decision to make a small but significant and non-transitory increase in price, being confident that it will increase the profitability of the monopolist’s business and not lead to an offsetting decrease in demand sufficient to

¹⁶¹ This test was first proposed in the US Department of Justice *Merger Guidelines* of 1982: see p 6 of <http://www.usdoj.gov/atr/hmerger/11248.pdf>.

render it unprofitable. If the outcome of the theoretical test is that the notional monopolist would find such a SSNIP profitable, then the sphere of commercial activity against which it is tested must at least encompass the appropriate market. If, on the other hand, such an initiative by the notional monopolist would be unprofitable, then the scope of the purported market has been drawn too widely because acquirers of the notional monopolist's good or service will find a substitute. There was substantial debate during the hot tub about how the SSNIP test might confirm the proposed extent of the market, or suggest it was of a different extent, or indeed whether the idiosyncratic influences on the New Zealand gas market rendered it less reliable here than in other contexts.

[353] There are certainly important, idiosyncratic factors influencing behaviour in the New Zealand market for gas. It appears that, by international standards, the proportion used for electricity generation is unusually high. In that, and in other uses that have been significant at various times, including Methanex and other petrochemical uses, there is a derived demand, ie the demand is not strictly for gas, but for what it can produce. Hydrological factors are an important influence on the electricity market, and hence also on the gas market. In relatively wet winters, there will be materially less demand for gas than in dry winters.

[354] The utility of a SSNIP test as a step towards both defining the market and going from there to the heart of the issue, namely the extent of competitive constraints on the parties in question, is lessened by these idiosyncrasies, whether they are accepted as "non price events" as Professor Sweeney urged, or as matters that are not readily reconciled with the usual approach to a SSNIP test. We are satisfied that the debate on the SSNIP test did not justify varying the view we came to on the relevant dimensions of the market in question.

Elasticity of demand

[355] A tool conventionally used by economists to assess the scope of a market is the elasticity or inelasticity of demand within a defined sphere of commercial activity. The price elasticity of demand for a good measures the responsiveness of the quantity demanded of that good to a change in its price and is defined as the

percentage change in quantity demanded for a one per cent increase in its price, all other factors affecting demand being held constant. Given the usual expectation that an increase in price will lead to a reduction in quantity demanded, the value of a measured elasticity will be negative: economists nevertheless discuss it in absolute value terms so that a “greater” or “higher” elasticity typically refers to a number that is more negative than another. If a price increase of one per cent leads to a decrease in demand of less than one per cent, then the demand for that good is said to be “inelastic”. If an increase in price of one per cent produces a reduction in demand by more than one per cent, then demand for that good is said to be “elastic”. The role of price elasticity in determining the scope of a market is that it indicates the extent to which supra-competitive pricing might be constrained by consequent decreased sales.

[356] Analysis of the elasticity of demand is also relevant when we analyse the impact on the market of the conduct complained of (ie whether it causes an SLC) and potentially also in assessing the extent of damages.

[357] Adopting calculations from earlier studies in New Zealand and elsewhere, including those done by the Commission, Mr Murray suggested a relatively inelastic response to a notional price increase within the production and first point of sale market for gas in New Zealand. He assessed a range between -0.15 to -0.3. His analysis relied on this to confirm the functional dimension of the market he identified. He also relied on it to project the extent of price response that would occur in the hypothetical circumstance of increased production from Pohokura.

[358] Professor Hausman undertook two projections of price elasticity of demand for gas in New Zealand, one a conventional algebraic calculation, and a second drawing on his expertise in econometrics. The outcomes of both of these were projections of elasticity much higher than Mr Murray. For the period 2001 to 2008, Professor Hausman’s direct calculation was -1.81. For his algebraic calculations, Professor Hausman assumed that increases in national income would be reflected in proportionate increases in demand for gas. At the outset in 2001, annual demand for gas was 247 PJ whereas in 2008 it was only 160 PJ. In that period, national income had risen by 24.06 per cent. Assuming an increase of 24.06 per cent on 247 PJ

would project a level of demand in 2008 of a little over 306 PJ, but instead demand had dropped to 160 PJ, some 47.7 per cent lower than the “expected” quantity of 306 PJ. On Professor Hausman’s data, the gas price had increased from \$4.72 to \$6.87 per PJ over that period – an increase of 45.6 per cent. Allowing for errors we consider arise in the use of the wrong basis for the percentage calculations, and a mistake in calculating the percentage price change, the implicit price elasticity of demand correcting for those errors would have Professor Hausman’s approach suggesting an elasticity of -1.04.¹⁶²

[359] Professor Hausman’s alternative econometric approach adopts a statistical technique called two stage least squares regression to find the “best fit” statistical relationship between observed price quantity pairs. He uses aggregate New Zealand data over a number of years for total gas consumption and average prices for gas and allows also for the effects on demand of changes in national income. His original exercise over the 2001 to 2008 period projected estimates of the price elasticity of demand that ranged between -1.96 to -3.47. After criticism of this as too long a period, Professor Hausman recalculated for the period 2004 to 2008 and arrived at an elasticity of approximately -1.0.¹⁶³ All of his elasticity projections remained at a sufficiently high level to incline Professor Hausman to the view that the market must be broader than that as defined by Mr Murray. We accept criticisms of the statistical validity of the econometric analysis. On annual data, Professor Hausman’s case used only nine observations and his quarterly data in the supplementary brief provided only 20 observations. That number is lower than would be treated in academic work as adequate for reliable projections.

[360] On examination of what has occurred in the production and sale of gas in New Zealand, Professor Hausman identified two occurrences that led him to suggest that coal might be a substitutable product, and that the geographical boundaries might extend beyond New Zealand. The first of these suggestions arose because of a marked decline in use of gas at the Huntly Power Station, where the operator elected to substitute coal for gas during the relevant period. The second arises from

¹⁶² Compare the calculation of 1.81 per cent, paragraph 37, Hausman brief; and supplementary brief, paragraphs 5, 7.

¹⁶³ Hausman, supplementary brief, paragraph 34.

Methanex's election to substantially reduce its New Zealand business in the production of methanol from gas, and instead relocate that business to Trinidad.

[361] Neither of these occurrences appears to us to alter a reasoned analysis of the scope of the market, given the purpose for which the exercise is undertaken here. Without necessarily accepting Professor Sweeney's reason for rejecting them as "non price events", we are certainly wary that they are sufficiently atypical, and explicable within their own particular circumstances in a way that they ought not to bear on a re-definition of the scope of the relevant market.

[362] A further dynamic influencing the market was the Maui redetermination. In February 2003, the gas market was informed that the estimated reserves at Maui had been dramatically downgraded from some 830 PJ to approximately 409 PJ. The inevitable consequence of that would be the anticipation of less gas being available with a consequent upward pressure on prices. By March 2006, the market was aware that the reduction in reserves had been substantially overstated, so that the prospects of greater supply would, other things being equal, lead to downwards pressure on prices.

[363] We also accept that there are sufficient idiosyncratic features of the New Zealand gas market to question the relevance of economic analyses undertaken in gas markets elsewhere. Professor Hausman was wary of studies undertaken in the United States where well head prices had increased by over 65 per cent in the period 2001 to 2008 and demand had increased by 4 per cent over the same period, whereas New Zealand's wholesale price has risen some 33 per cent over the same period whilst the quantity demanded fell by 43 per cent. In the United States, the retail gas sector makes up 21 per cent of total consumption whereas in New Zealand it is 4 per cent. Here, electricity generation accounts for almost 44 per cent of gas use, whereas in the United States it is 29 per cent. One peculiarity of the New Zealand market is that for parts of the period being compared, a single company, Methanex, has accounted for approximately the same percentage of use as the total industrial gas usage in the United States. Accordingly, we are inclined to regard sceptically any analyses that depend on the application of studies undertaken outside New Zealand.

[364] We also acknowledge the unreliability of price data used by the economists that were derived from MED. A witness statement was adduced, on behalf of Todd and without opposition from Shell or OMV, from Mr Paul Hunt at MED. That uncontested evidence acknowledged certain relatively fundamental inadequacies in the accuracy of the data MED was able to produce in respect of the period in question. Indeed, Professor Sweeney suggested that the inadequacy of the MED data was the most significant criticism he had of Professor Hausman's econometric approach.¹⁶⁴

[365] Professor Hausman also took the view that a decision by a notional monopolist operating a field such as Pohokura to reduce gas output for the purposes of increasing prices would be constrained by the need to take into account the drop in condensate revenue. The rate of condensate production is dictated by the rate of gas production. We do accept that, for fields where the value of condensate production is significant relative to the value of gas production, any decisions to defer gas production have adverse consequences for the timing of revenue from condensate. This suggests that, relative to any projected response to an increase in prices by way of reduction in demand, the extent of that reduction for any given increase in price would need to be less than if the field were just producing gas, to take account of the consequential drop in condensate revenues.

[366] It is unnecessary for our analysis to make a specific finding on the numerical value of the elasticity of demand for gas in New Zealand. We do accept the validity in a number of the criticisms advanced on behalf of Todd of Professor Hausman's projections of a relatively high elasticity. On the other hand, Mr Murray's approach depends upon the application to New Zealand of studies in markets that are quite different, as noted above, and which may be of limited applicability. As a tool in aiding the analysis of the market definition, we are satisfied that the market demand is relatively price inelastic when assessed over a one or two year period. We are certainly not persuaded that the market needs to be defined in any broader functional terms than we have contemplated, as a result of evaluating the competing views on elasticity that were put by the economists.

¹⁶⁴ T4194/8ff.

[367] In argument over the functional dimension of the market, Todd's fall-back position was that to the extent producers compete in the wholesale gas market, it did not necessarily follow that the wholesale market provided a competitive constraint on the producer/first point of sale market. In the context of assessing the effect of the off-take rules and the annual limits on production from Pohokura, Todd argued that the market definition should still be confined to exclude wholesalers because the wholesalers could not increase the amount of gas in the market and in that sense could not provide a competitive constraint on producers.

[368] We do not accept that the overlap is "one way" as this argument suggests. In cross-examination, Dr Veljanovski accepted that Vector and Contact selling to mid-sized industrial consumers were competing in the same market as Todd.¹⁶⁵ Moreover, Dr Veljanovski accepted that the wholesale and first point of sale gas markets were inter-related to some degree.¹⁶⁶ Further, the perception of Todd's own personnel who gave evidence suggested that it treats Vector and Contact as "competitors", being among those monitored as such by Hamish Tweedie.¹⁶⁷ Contact and Genesis could compete with Todd when it tries to sell Pohokura and M&M gas.¹⁶⁸ Mr Richard Tweedie referred to Todd having gained a contract to supply gas to the Whareroa joint venture where it was competing with Contact for that sale.¹⁶⁹ That competition is illustrated by the fact that half of the gas produced at Kapuni is contracted to Vector so that it stands in the shoes of the producer at that field, in terms of on-sale.

[369] Under cross-examination, Mr Murray and Dr Veljanovski were inclined to accept that a broader market than that pleaded, including wholesalers/re-sellers, was appropriate.¹⁷⁰ We agree with that.

[370] Accordingly, we are satisfied that the market in which field owners produce and then sell gas extends to the activities of major wholesalers of gas, including at

¹⁶⁵ T3731/21-3732/5.

¹⁶⁶ T3776/7-12.

¹⁶⁷ First brief, paragraph 1.10(f)(iii), T1087/4-7.

¹⁶⁸ T1087/17-1088/2.

¹⁶⁹ T277/13-22.

¹⁷⁰ Veljanovski XXN T3731-3734, T3775-3776 and Murray T4072-4074.

least Contact and Vector, given their access to substantial volumes of gas, and ability to compete with producers for sales to others.

[371] Although the Court is able to observe the wholesalers' participation in the same market, there has been no discovery from those participants in the market, and nor is there any sufficient information about the dynamics of their involvement in it to reconstruct their influence on how the market would operate in the theoretical counterfactual, absent the off-take documents that are under challenge.

Temporal dimension

[372] Todd's case was that there was an annual market for gas. In closing submissions, that was given a pragmatic justification because the effect of the conduct complained of had to be measured within some time period. The budget decisions are made annually and Todd's case is that its level of production is constrained annually. In terms of effect, Todd argues that the price effect crystallises each year. However, Shell and OMV dispute that these are sufficient criteria to constitute discrete annual markets for gas. The market is in essence a continuous one, with significant contractual commitments extending for a period of years. That was certainly the case for the first tranche of sales of Pohokura gas by all parties, and their length appears to be typical for sales of substantial quantities. There is possibly a trend towards shorter periods in contracts for smaller quantities. Mr Murray and Dr Veljanovski accepted that there were no discrete markets for each or any calendar year, and that that approach was neither orthodox nor appropriate.¹⁷¹

[373] We are satisfied that there are no discrete annual markets for gas. Because buyers do not have any significant storage capacity, they are unable to arbitrage price differences from year to year, so the market is both continuous, and measured by the terms of contracts that reflect the market. Here, the impact of the conduct complained of can be measured in a market that is in a sense continuous. It is most relevantly characterised as between Shell, Todd and OMV by relatively large-scale contracts for periods typically of, or in excess of, four years, but nonetheless with

¹⁷¹ Veljanovski T3716/3723, Murray T4086.

annual impact. However, the boundaries of the market are to be drawn by reference to the conduct at issue (as well as the terms of the relevant sections and the policy of the Act).¹⁷²

[374] The point Shell advances in challenging a discrete annual temporal dimension to the market is that conduct that is likely to register as an SLC when measured over one year, would never suffice for that purpose if its effect was assessed, for instance, over the lifetime of a field. Mr Richard Tweedie was confident that the market could absorb another 16 PJ/a without materially impacting on price.¹⁷³ Implicitly, that reflects a longer-term view of the market than one year.

[375] To assess the anti-competitive effects alleged to arise, one reasonable approach is to consider the impact of practices complained of within, say, a one to two year span, relative to a market that operates continuously. The more significant transactions are likely to recur on a rolling annual basis, but less frequently than within the period during which specific instances of conduct would be considered. The temporal dimension does not assume the significance that the functional one does. Annual markets for gas were not pleaded and the issues were joined as between the experts on a basis adequately protecting Shell and OMV by reference to a continuous market with annual effects.

Conduct in the counterfactual

[376] The conventional device for testing the alleged impact of anti-competitive conduct is to contrast the outcomes that have occurred in light of the conduct complained of, with the different outcomes that would have pertained in a market operating without the conduct complained of. That construct is described as “the counterfactual”.

[377] The approach adopted to the counterfactual analysis in earlier cases suggests an evaluation of what is likely to have occurred. Given the hypothetical nature of this analysis, there can be no expectation of proof as to what indeed would have

¹⁷² *Telecom Corporation v Commerce Commission* (1991) 4 TCLR 473 at 500.
¹⁷³ T488/27-490/2.

occurred. A plaintiff must establish a real and substantial prospect, recently treated as something less than a balance of probabilities “more likely than not” standard.¹⁷⁴

[378] This evaluation is necessarily situation-specific. We accept Todd’s proposition that the prospect of some other conduct occurring, inconsistent with Todd’s hypothesis, does not necessarily exclude the real chance of Todd’s scenario constituting a valid counterfactual.

[379] Todd’s counterfactual involves it having been able to call for the production of 26 per cent of Pohokura’s capacity since the commencement of commercial production in September 2006. Todd’s rationale for this expectation throughout the period has relied on its view of Article 10.1 of the JVOA as entitling it to call for that level of production. On its competition law case, putting the contractual expectation to one side, it is that the constraint imposed via the off-take documents has unlawfully prevented that occurring. We have made the fundamental point that the majority owners would not have permitted substantially unequal production relative to each party’s share in the venture without an enforceable commitment for redressing imbalances.¹⁷⁵ Consistently with that, we are not persuaded that there is any real and substantial prospect, either in the JVOA or otherwise for Todd to start from the premise that 26 per cent of the plant’s capacity is the entitlement it would have received. It seems much more likely that any demands to receive gas on those terms would have led to stalemate. Todd would be most unlikely to have obtained any injunctive relief without having to reveal the numerous weaknesses in its contractual arguments in support of such an entitlement, and having to deal with the inconsistency between that and the unanimous agreement to FID. All prospects of Todd getting access to more gas than it has lead directly or indirectly back to the proposition that this would only occur on terms such as a GBA that protected the position of all parties by some process for redressing imbalances.

[380] However, in order to review the other elements of likely counterfactuals, it is appropriate to test whether Todd’s reconstruction may have occurred, namely where it can insist on full production of its share, but no arrangements are in place to

¹⁷⁴ See *Woolworth Ltd v Commerce Commission* (2008) 8 NZBLC 102,108 at [110]-[114].

¹⁷⁵ See [305] to [308] above.

protect all parties by an enforceable process for redressing imbalances later in the life of the field.

[381] It would only be in those circumstances that Shell and OMV would have the incentive to match Todd's level of off-take. Whilst Todd's closing submissions accepted that it was not a necessary part of its case that the other parties would confront a situation in which they were obliged to produce full-out as well, that is the counterfactual scenario on which Mr Murray's analysis primarily depends. However, we consider that scenario is inherently unlikely.

[382] We consider the clearly more likely scenario to be that full production would have been permitted for Todd once commitments were concluded between the parties to redress imbalances. In those circumstances, Shell and OMV would not have the same imperative to match Todd's level of production, and the likely scenario is that they would not have done so, at least until relatively recently. The evidence included acknowledgements on behalf of Shell that more recently it would have been keen to increase the level of its own production, subject to resolving satisfactory arrangements to redress imbalances, and to resolving the issues in these present proceedings.

[383] It follows that we are not satisfied to the requisite standard of a real and substantial prospect that a counterfactual situation would have developed in which all three joint venturers called for production from Pohokura at capacity. Rather, with all the qualifications reviewed in [305] to [308] above, the likely counterfactual is one in which Todd procured an entitlement to produce full-out, subject to agreeing on appropriate commitments to redress imbalances, but the others did not follow suit.

Market response: what likelihood of a substantial lessening of competition?

Would Todd have sold more gas?

[384] Todd's counterfactual contemplated that production from Pohokura would have been increased to 86 PJ/a until 2016,¹⁷⁶ on the basis that its forcing production at capacity would have obliged the others to follow suit. Mr Murray subsequently revised this downwards to acknowledge that production at 86 PJ/a would not have occurred until an upwards revision of the extent of Pohokura reserves in 2007. Accordingly, the increase would have been less until the revision, and then a plateau rate of 82.5 PJ/a from 2009 to 2013.¹⁷⁷ Todd's reconstruction treats this as additional gas that would be available to buyers, and be sufficient to have a material impact on price. It would follow that the curtailment of that activity in the factual has led to an SLC. Timing was also important in this reconstruction. Mr Murray assumed that Todd would have sold its share of additional Pohokura gas prior to ROFR sales of Maui gas being negotiated, and also before Shell and OMV could market their shares.¹⁷⁸

[385] There were numerous challenges to this hypothesis:

- OMV disputed that Todd's additional gas would be any more than between 1.9 and 3 PJ/a.
- Shell and OMV disputed that Todd would in fact have promoted the sale of its own additional Pohokura gas, and found buyers for it on terms acceptable to Todd.
- Todd's internal arrangements provided for Nova to acquire Pohokura gas, and Nova did not participate in the first point of sale market, so increased gas supply to Nova would not have any impact in the alleged market. Alternatively, that Todd would have directed additional gas to its own

¹⁷⁶ Murray, first brief, paragraph 250.

¹⁷⁷ Murray, supplementary brief, paragraphs 3, 6.

¹⁷⁸ Murray reply brief, paragraphs 197-198.

electricity generation businesses, which would similarly not have an impact on the alleged market.

- Shell and OMV dispute that they would have followed suit by marketing additional Pohokura gas so that, if at all, the additional gas from Pohokura would only be Todd's share.
- Shell and OMV argued that the market was relatively well in balance in the 2006 to 2009 years, so that any increase in production from Pohokura would most likely have been met by supply side response, most likely with a reduction in the volume of Maui gas coming to the market, and that Todd itself would have held back production from M&M, to balance any increased volumes from Pohokura.

[386] There are sufficient grounds for all of these responses for us to be satisfied that there is no real and substantial prospect that the additional volumes postulated in Todd's counterfactual would have been sold. We deal with each of them in turn.

[387] OMV's first point was simply a reflection of the arithmetic. Todd's 26 per cent of 70 PJ/a amounts to 18.2 PJ/a. Its claim to access up to a further 4 PJ/a was dependent on Pohokura producing at the nameplate capacity Todd relied on of 86 PJ/a. However, that gross capacity was not available because of the extent of downtime for planned and unplanned outages. Numerous reductions from that gross capacity were proposed. For instance, if the plateau rate of 82.5 PJ/a accepted by Mr Murray in his supplementary brief was treated as capacity, then the additional gas represented by Todd's 26 per cent of that capacity would be some 3.25 PJ/a.

[388] Evidence on further potential sales by Todd was adduced for two purposes. First, to support the counterfactual analysis in its claims under the Act, and second to support the quantum claimed in damages. The analysis of it overlaps for those two purposes. As to the factual scenario in which such sales were assumed to have occurred, Mr Hamish Tweedie expressed confidence that had Todd known of greater volumes being available on a long-term basis, then that gas would have been sold to best advantage. Mr Richard Tweedie was also confident that additional amounts,

certainly more than volumes up to 4 PJ/a that Todd claimed it could expect, could easily have been absorbed by the market in long-term contracts at or around the prices that Todd had originally secured for sales of its share of 70 PJ/a.¹⁷⁹

[389] Todd's claims about its own conduct were challenged in two principal respects. First, that Todd did not sell all the gas it had available to it in any event, and that its contemporaneous documents do not support its present claim that it was seeking larger volumes of gas, and was confident that it could sell them. Those contemporaneous documents rather suggest that Todd would have pursued the same strategies it did, namely deferring commitment to sell any additional volumes of gas for longer terms, for some years.

[390] The second objection related to Mr Hamish Tweedie's claim that Todd would have taken advantage of selling into a less than fully informed market in a window at the beginning of 2006 when Todd was aware of the prospect of greater Maui reserves, but the market was not. In contrast, Mr Richard Tweedie denied that Todd would pursue sales on any morally dubious or potentially illegal basis that took advantage of a less than fully informed market.¹⁸⁰ On the basis of this constraint from the managing director in respect of Mr Hamish Tweedie's freedom to act, Shell and OMV argued that Todd could not establish that it would have sold in the window of opportunity that took advantage of higher prices, before the market was informed of the relatively larger Maui reserves.

[391] The period in which Todd was informed of the probable extent of increase in Maui reserves, and before the market was informed, was no more than seven weeks. A Todd internal email dated 31 January 2006 warned of a STOS re-appraisal of reserves to be delivered the following day. Hamish Tweedie and others were provided with details on 7 February 2006.¹⁸¹ It appears these increases were disclosed to the market, certainly before Contact made an announcement on 31 March 2006¹⁸² and, on Shell's analysis, the ROFR buyers were advised on or

¹⁷⁹ T489/10-490/2.

¹⁸⁰ T275/20-277/2.

¹⁸¹ CB10407, CB10485.

¹⁸² CB11035.

about the day of a ROFR subcommittee meeting on 14 March 2006.¹⁸³ We are not satisfied that Mr Richard Tweedie's concerns for Todd not to transact with buyers who were less informed than Todd, would have entirely precluded Mr Hamish Tweedie pursuing such sales. However, to use Todd's own phrase, Mr Richard Tweedie's reservations about that situation would have had a chilling effect on the pace and enthusiasm with which Mr Hamish Tweedie sought sales. We are not satisfied that the fact of the market being less informed than Todd was, in the relevant window, of itself a complete answer to Todd's claim that it would have made substantial sales in that period.

[392] Reverting to the first ground for challenging Todd's reconstruction of the counterfactual, we find that it is valid. Certainly within a contractual analysis, Todd could not make out on the balance of probabilities that further sales would have occurred within the window available prior to the market for gas being influenced downwards by the availability of greater levels of Maui reserves. It also cannot meet the lower onus of there being a real and substantial prospect that it would occur.

[393] At the time of the original sale of Pohokura gas, an internal technical risk review implied that further commitments should not be made before Todd was better informed as to how the field produced. That, and Mr Hamish Tweedie's evidence, support an inference that Todd intended to wait until commercial production was underway, before addressing sales for the post-2010 period.¹⁸⁴

[394] The most relevant document in reconstructing Todd's aspirations in relation to further gas sales in early 2006 is the Todd Energy Group 2006 Corporate Plan. Its managing director, Mr Richard Tweedie, confirmed that such documents constituted thorough reviews for the Board.¹⁸⁵ Their content was presumably intended to fully inform the Board to enable it to carry out its governance responsibilities and to guide executive performance.

¹⁸³ Shell closing submissions, paragraph 3.82, relevant minutes not identified.

¹⁸⁴ CB7162, Hamish Tweedie brief 11 September 2009, paragraph 3.19, XXN T1072/5-8.

¹⁸⁵ T434.

[395] The details retain a measure of commercial sensitivity so that, consistently with our comments on other such documents, the analysis is necessarily abstracted to a level of generality to minimise the prospect for harm to the discovering party's present commercial position. It is sufficient to observe that Todd Energy's projections of its forecast daily gas portfolio reveal:

- volumes of gas able to be “deferred”;
- commentary acknowledging excess deliverability of gas in the fourth quarter of 2006; and
- an analysis demonstrating that Todd had materially more gas available to it for new projects from 2008 than the additional gas it claimed on Mr Murray's reconstruction would be sold.

[396] The commentary about strategies into the future, as seen at that time, focused on projects that would generate the prospect of more sales, without expressing any concern at inadequate supply.¹⁸⁶ A different part of the Corporate Plan addressing the re-sale of gas by Nova commented on how competitive the downstream gas market was.¹⁸⁷

[397] Shortly before this period, in December 2005 internal Todd analyses forecasting gas sales for 2006 showed volumes that were “uncommitted” being substantially greater than the additional volumes Mr Murray postulates would be sold. Slightly more than Mr Murray's additional volumes were prospectively earmarked for re-injection, with somewhat more than that being “closed in” at M&M, and a further, more modest, volume being “backed out” from Kapuni.¹⁸⁸

[398] In an internal exchange on 24 January 2006,¹⁸⁹ a Todd executive commented that the structure of a valuation of gas assets:

¹⁸⁶ CB18/197-200.

¹⁸⁷ CB18/171.

¹⁸⁸ CB10124.

¹⁸⁹ CB10386.

...virtually conceded that we can't sell the excess gas from Pohokura which is something we don't necessarily want to do. We have until September to sell this uncommitted gas.

Mr Hamish Tweedie's response was:

Sorry Anton I don't understand this statement? We are taking the prudent approach as far as I can see. At this stage it looks remote that we will move this gas even if we discount it significantly. Maui now appears to have extra reserves and will be discounting significantly in a market when everybody is fairly contracted over that period due to Pohokura first gas. I'm all ears as to how we can move this gas, but can't see how it can be budgeted that we will roll the dice and sell it now.

[399] The expression "fairly contracted" appears to relate to the level of demand being more or less met in existing contracts, rather than a reflection on the fairness of terms in those contracts.

[400] The reaction of another Todd executive, Mr Brett Rogers, to the increase in reserves at Maui, and therefore more Maui gas, conveyed internally within Todd at the end of January 2006 was:¹⁹⁰

...the market must both expand to accept it, and some sales will be deferred across all gas sources.

[401] In a February 2006 email forwarding the detail on updated Maui gas reserves to 10 others within Todd, Mr Rogers commented:¹⁹¹

Whereas previously, we had held back sales due to a perception that we would pick up a price increase until the demand excess increased in ca 2010, this will likely be delayed until ~2012 (ignoring extra Pohokura volumes that may occur). The key thing we need to focus on going forward is how we maximise the liquids offtake while maximising the gas value into those markets. We would likely have a strong preference to build new high value gas markets (cogen/other/electricity) with upside value on electricity pricing in order to ensure we shift our gas and therefore gain the liquids upside from our portfolio.

[402] This reflects an attitude that Todd would defer making new contractual

¹⁹⁰ CB10407.

¹⁹¹ CB10486.

commitments, because of a perception that the supply/demand dynamic would lead to an increase in prices. However, the words in the first set of parentheses suggest that additional gas from Pohokura could be dealt with, perhaps by way of addition to the existing contractual commitments, on the same terms.

[403] Further insight into Todd's thinking at the time is gained from a series of slides prepared for a March 2006 Corporate Plan presentation. It dealt with the Todd Energy Group's interests at all levels, including the Auckland Gas Company and Nova Gas Limited. In an overview on the wholesale situation for 2006, it acknowledged "Excess uncontracted deliverability in Q4 with Pohokura startup" and relevant to that "Q4 volume needs to be managed". The paper aspired to wholesale strategies for 2006 that suggested the challenges were in finding expanded opportunities to dispose of additional gas arriving on the market, rather than in acquiring gas.

[404] In respect of the whole of the Todd gas group, issues acknowledged in the slides included that Todd was facing an increasingly competitive environment across all segments and the strategy for the group included:¹⁹²

- **Locking in contracts** to cover over supply for next few years.

[405] The Todd Energy 2006 Corporate Plan recorded among the goals for its gas group for 2006 that of developing one category of customer "...to deal with oversupply of gas post commissioning of Pohokura production":¹⁹³ The same document referred to an initial oversupply when Pohokura comes on-stream, and recorded Todd's intention to "...manage this by using swing within the portfolio (ie M&M), using a Pohokura gas balancing agreement where applicable and/or seeking to contract to parties (example cited)".¹⁹⁴ After a graph reviewing the Todd Energy Group's gas sources and contract position from 2006 to 2016, the paper included a comment that showed that Todd had substantially more unsold gas in each year from

¹⁹² CB10686; see also CB10676, 10678, 10679.

¹⁹³ CB18/193.

¹⁹⁴ CB18/197.

2008 than the amounts of extra gas Mr Murray's projections claimed Todd would have sold from Pohokura, if not constrained.¹⁹⁵

[406] The consistent theme in Todd's documents from this period is that demand for gas was relatively well-satisfied, and that Todd saw itself facing increasingly competitive conditions in marketing gas. On a subtly different topic, a confidential Todd analysis of recent events at Pohokura dated 23 December 2005 expressed concerns that control of the Pohokura facilities was being used "...as a means to control Todd's ability to compete in the market for gas and liquids".¹⁹⁶ However, that does not relate to quantities, and rather foreshadowed the later interconnection dispute.

[407] An analysis of Todd's confidential documents in respect of production in 2007 and the following years similarly fails to reveal any concerns that it should be procuring more production from Pohokura. A detailed, portfolio-wide spreadsheet for the 2007 year detailing sources of supply and the extent of demand concluded with an extent of gas available after provision for re-injection as "deferred gas" of somewhat more than 1 PJ.¹⁹⁷ The availability of surplus gas in 2007 tends to be confirmed by the comment in Todd's 2008 Corporate Plan explaining slightly below budget gas sales from M&M as resulting from the "commercial/strategic decision to use McKee/Mangahewa to balance the portfolio".¹⁹⁸

[408] A similar pattern is reflected in respect of gas availability from 2008 onwards.

[409] There is an isolated comment in part of Todd's 2008 Corporate Plan, noting in respect of a graph showing levels of production by field for Pohokura and M&M for the years 2006 to 2008 as follows:¹⁹⁹

The Pohokura production decrease reflects offtake restrictions by Shell remaining in place through 2008.

¹⁹⁵ CB18/198.

¹⁹⁶ CB10127.

¹⁹⁷ CB18/433, Hamish Tweedie XXN, T1215.

¹⁹⁸ CB18/464.

¹⁹⁹ CB18/460.

[410] The reduction graphed is extremely small and appears in the context of substantial information suggesting that Todd had no shortage of gas, relative to the perceived demand for internal use and sale of gas. A credible inference is that Todd was keen to get as much gas as it could from Pohokura, on the basis that it was the resource best utilised first, within Todd's portfolio. However, that is distinct from a wish to sell more gas, when the comments suggest that the consequence would have been that Todd could defer production elsewhere, in particular at M&M, for longer.

[411] Mr Farmer urged that the gloss put on the Corporate Plan and these other contemporaneous statements by Mr Hamish Tweedie when they were put to him in cross-examination should be preferred, as the documents were not entirely representative of the willingness and ability of Todd to sell additional gas at the time. However, to the extent that Mr Tweedie's responses in evidence were inconsistent with the contemporaneous documents, we reject his evidence and find that the meanings reasonably attributed to these contemporaneous documents are justified. We note that numerous interlocutory arguments were necessary for Shell and OMV to get access to progressively less redacted versions of some of the documents Mr Tweedie was relevantly cross-examined on.

[412] A commentary by a Vector executive contributing to a national power conference on 2 March 2006 included the following comments on the New Zealand gas supply outlook:²⁰⁰

At the same time the short term supply position looks strong with Pohokura being commissioned later this year, a high likelihood of additional Maui reserves being recovered, and Kupe due by 2008.

This, in fact, creates a potential short term over-supply, which, if this gas is delayed coming to market to match this particular demand scenario (...), puts back the supply gap to 2015.

This could potentially be even longer if new indigenous sources of gas are discovered and brought on stream in the next 5-10 years.

Those observations are consistent with Todd's own internal comments from the time, to the effect that the commissioning of Pohokura created the risk of there being a state of over-supply in the New Zealand gas market.

²⁰⁰ CB19/1330.

[413] As to projecting fluctuations in demand for gas, one international norm is that demand increases in step with increases in gross domestic product (GDP), all other things being equal.²⁰¹ The statistics show significant reductions in gas usage in New Zealand between 2001 and 2005 despite increases in GDP.²⁰² Without analysis of changes in gas prices, wet winters and the position of Methanex, it is difficult to tell whether that norm applies to the New Zealand gas market. Certainly, the drop in usage reflected fluctuations in the quantities used in electricity generation, and the drop in use by Methanex.

[414] As to demand for new electricity generation, there was some evidence of OMV's dialogue with a major generator of electricity. That suggested that generators are keen to get long-term commitments for significant volumes of gas, as the first step in assessing the economics of constructing new generating capacity. The parameters of such demand appear to be approximately 20 PJ/a for five, and ideally up to 10, years' committed supply.²⁰³ It is understandable that generators would encourage producers to offer commitments within these parameters. It also seems likely that electricity generators would evaluate the prospect on assumptions that further gas would be available at similar prices to existing market conditions. Increase in supply to meet a generator's articulated demand of this type therefore seems unlikely to have an impact on prices in the market, commensurate with the proportionate increase it would represent in annual production.

[415] Irrespective of the debate between economists on the elasticity of demand, we were struck by the confidence Mr Richard Tweedie expressed in being able to sell substantial additional volumes of gas if Todd could secure them on a longer term basis from Pohokura, on the same terms as its existing contracts.²⁰⁴ Mr Farmer confirmed in closing that Todd's case was that it could sell an additional 4 PJ at the same price it had achieved.²⁰⁵ There would likely be two aspects to the saleability of

²⁰¹ Sweeney brief, paragraph 92; Hausman supplementary brief, paragraphs 2-3.

²⁰² David Hunt brief, paragraph 15 and figure 2.

²⁰³ For example, a new Combined Cycle gas turbine generator requires between 18-20 PJ/a – CB3384-3385.

²⁰⁴ T489/9-490/2.

²⁰⁵ T4914, 4915.

more gas. First, certainty of deliverability, and second, a relatively long-term commitment. Less likely, but still possible, would be the prospect of Todd increasing the quantity sold under its initial Pohokura contract by, say, 2 PJ, some time through the term of that contract. Again, if a sale of an increased quantity occurred, the preponderance of evidence suggests that would occur on the same terms as the original contract. Neither scenario introduces the prospect of an SLC.

MMCs' response to increased Pohokura production

[416] Another issue that was extensively debated in the hot tub was whether the MMCs would respond to increased production by Todd from Pohokura, by reducing the level of production from Maui. Mr Murray's analysis for Todd was that the high level of operating expenses at Maui would count against the MMCs reducing output. Certainly in June 2004, Shell's internal thinking acknowledged that with Maui's "massive opex" the key was "to get the gas out as quickly as possible".²⁰⁶ On Mr Murray's analysis, additional production from Pohokura would therefore be entirely additional to the gas that was otherwise in the market, and the extent of price reductions he predicted from that increased supply was on that basis.

[417] Shell and OMV contested this theory, pointing out that Maui was not in any event producing at capacity, and that the rational response for the MMCs would be to decrease production from Maui so as not to weaken the market for gas.²⁰⁷ Generally, economic theory supports the views of the economists called for Shell and OMV to the effect that increased output from one producer will typically induce reduced output by others.

[418] In the course of the hot tub, Dr Bamberger identified significant abandonment costs at the end of the life of the Maui field as a material consideration offsetting the concerns the MMCs might otherwise have, if they have to extend the period in which they were meeting its relatively high levels of operating expenses.

²⁰⁶ Mr Fairweather's email, 22 June 2004, CB7509.

²⁰⁷ David Hunt brief, figure 23 and paragraph 112 calculates that Maui produced at 63 per cent and 58 per cent of its capacity in 2007 and 2008 respectively.

On his analysis, Dr Bamberger suggested that deferral of significant abandonment costs, which might be up to \$750 million, was a sufficient influence on rational decision-making, to incentivise the MMCs to respond to an increase in production from Pohokura in the 2007 to 2009 years; that is, rather than being committed to continuation of gas production at Maui on the previously projected volumes, so as to get to the end of Maui's field life sooner.

[419] Todd's experts disputed the validity of \$750 million abandonment costs as unsupported and, in any event, unrealistically high. They focused upon an alternative number of possibly \$250 million. After the hot tub, Mr Burt of OMV produced more recent STOS workings that cast doubt on the \$250 million estimate as substantially too low.²⁰⁸ We are not persuaded that any particular level of abandonment costs had been identified by MMCs, in a way that would dictate their response to any increase in production from Pohokura, decisively one way or the other in the period between 2006 and the present.

[420] In a February 2006 draft of Todd's preferred form of gas balancing arrangements for Pohokura, one of the observations arguing for production full-out at 85 PJ rather than "artificially low" 70 PJ, was a bullet point in the following terms:²⁰⁹

If Pohokura produces 25 PJ pa (125.6 PJ over five years) then Maui produces 125.6 PJ less.

[421] In a confidential 2008 "10 Year forecasts" that appears to have been part of its Corporate Plan for that year, Todd commented on gas sales from Maui in the following terms:²¹⁰

Maui gas sales during 2007 were below budget due to decreased demand as Pohokura came fully onstream and ROFR buyers taking only their minimum contract amounts.

[422] These comments clearly suggest a practical view at the time that the major

²⁰⁸ CB19/1865-1873.

²⁰⁹ CB10630.

²¹⁰ CB18/462.

producers understood the level of demand, that it was being adequately met, and that an increase by one of the major fields would be met by a corresponding decrease in production from another. We find that the pattern of production from Maui, being less than its capacity, suggests that they would make at least a partial response to increased production from Pohokura, so as not to allow any excessive fall in the market price to occur.

Spare capacity at M&M?

[423] The prospect of Todd having more gas available for sale from its M&M fields throughout the same period as it postulated it would have sold more Pohokura gas, took on something of a life of its own in the proceedings. In his brief, Mr David Hunt undertook an analysis reconstructing the nature of the gas market in the years since first production at Pohokura in 2006. Mr Hunt's analysis suggested that there were volumes of unsold gas from Todd's M&M fields at around, and possibly more than, the additional gas Todd claimed it ought to have been able to access at Pohokura.

[424] In Mr Murray's initial brief, this point rated only a mention in a footnote, which suggested that Todd had made decisions to re-inject gas at McKee, as an economic means of boosting the level of ultimate returns from the field.

[425] Reference was then made to work undertaken for Todd calculating the comparative benefits of re-injection of gas at M&M, relative to producing the gas. This led to the production of a later brief of evidence from a Todd executive, Mr Boeren, who described his responsibilities for a programme monitoring the relative benefits of extraction and re-injection at M&M. His explanation of the basis for such decisions and the extent of re-injection that has occurred led in turn to a brief, available only after commencement of the trial, served on behalf of OMV from Mr Geoffrey Barker. Mr Barker is an independent consultant from Perth, Western Australia, with expertise in the upstream hydrocarbon industry as a petroleum engineer. Mr Barker's conclusions were that from March 2006 to September 2009 the M&M fields had material capacity over and above the gas actually produced for

sale or re-injected. Further, that Mr Boeren's projection of gains from re-injecting or conserving gas appeared to be overstated.

[426] Todd's rejoinder to this evidence was to produce a brief from Dr Rosalind Archer, a senior lecturer in the Department of Engineering Science at the University of Auckland. That was available on 24 March 2010 and Dr Archer's evidence was admitted after I disallowed an objection on behalf of Shell and OMV, to the effect that it was too late and otherwise inadmissible.²¹¹ The effect of her evidence was that the re-injection and conservation practices recommended by Mr Boeren have had sufficient beneficial effects for their pursuit to be an economically rational influence on the rate of extraction from M&M.

[427] We intend no disrespect to the careful evidence given by all of Messrs Boeren and Barker and Dr Archer, in not reviewing it in detail. The critical points are that gas was not produced from M&M at the maximum rates possible, after providing for prudent levels of re-injection. So if it had wished to, Todd could have sourced more gas for sale from M&M in the 2006-2009 years.

[428] Further, we find that Todd has not managed its programme of re-injecting gas at McKee by any precise application of a price indifference graph that reflected the competing benefits of production of gas for sale on the one hand, as against increased value of the ultimate level of production from the field by re-injection, on the other. Rather, Mr Boeren's views on that from time to time have been but one input into decisions ultimately made, having regard to a range of commercial and technical considerations. We accept the point made for Shell and OMV that had the level of re-injection been dictated solely by such a price indifference graph, then a reasonable operator in Todd's position would have undertaken substantially more technical work on an on-going basis, to maintain the current integrity of such a price indifference graph.

[429] We find that Todd has made decisions on the extent of re-injection of gas at M&M, at least in part to optimise the ultimate level of gas and condensate able to be

²¹¹ *Todd Pohokura Ltd v Shell Exploration New Zealand Ltd* HC Wellington CIV-2006-485-1600, 1 April 2010 (Ruling 8).

extracted. There have been varying levels of additional gas that could have been extracted from M&M. However, the evidence does not allow a precise finding as to the extent of such excess gas, over and above the amounts reasonably re-injected to optimise ultimate returns. We note that in June 2006 Mr Hamish Tweedie commented in an internal email on the Pohokura start-up that "...we have a strong chance of closing in M&M over 4Q 2006". After reviewing Todd's gas resources, the email summarised the situation as M&M re-injecting 1.7 PJ with a worst case that it would also defer 2.44 PJ, and a best case that it would defer 1.64PJ.²¹²

[430] It follows that from 2006 to 2009 Todd was not motivated to find all possible gas available for sale, in that decisions about the level of production from M&M have not been made in light of pressure for those fields to produce as much as possible, at all times. We are satisfied that Todd's conduct at M&M is inconsistent with a wish in 2006 and from that time, to source and sell more gas than was otherwise available to it. However, we are not in a position to compare the unquantifiable "excess M&M gas" with the additional volumes Mr Murray's damages calculation contends would have been sold by Todd, if available from Pohokura.

Todd's internal use of gas

[431] From around the end of 2006, Todd had an informal arrangement within its energy group that Todd would sell Pohokura gas to Nova.²¹³ That arrangement was not formalised by way of a contract until 2009. This arrangement raised both economic and legal issues. There were suggestions made on behalf of Shell and OMV in the hot tub that if Todd was committed to transferring any additional Pohokura gas it got to its affiliate Nova, then that transaction would have no impact on the market, leading to the argument that the alleged constraint could not possibly have caused any SLC.

²¹² CB12315.

²¹³ Hamish Tweedie, T1091/30.

[432] We are inclined to accept Dr Veljanovski's analysis that all additional gas produced and delivered to any entity in the gas market has the same potential to effect a change in that market.

[433] However, the impact on pricing in the market is likely to be different. The tenor of comments in Todd's Corporate Plans suggest that considerable focus was given to expanding internal demand, by means of constructing new electricity generating capacity.

[434] The economically rational approach to adopt in analysing whether production of more gas was likely to be profitable for Todd would involve its identifying a bypass price reflecting what Todd could itself afford to pay for more gas. This would reflect a projection of its return on the gas by internal use (principally electricity generation) and that would be a preferable use for the gas so long as it matched or exceeded the external market price Todd/Nova could achieve in selling to third parties.

[435] There was no evidence that Todd had identified and was applying any such bypass price for internal uses of gas. A partial exception was the periodic review undertaken in respect of re-injection versus production from M&M, guided in part by Mr Boeren's "value indifference curve", and involving decisions as to whether re-injection was more valuable than any internal use or external sale of more gas. For the sake of the theoretical construct of what would have occurred in the counterfactual, we can only observe that had Todd adopted this economically rational decision-making process, the opportunities for additional Todd sourced gas getting to the external market would be constrained by the extent to which it identified its own internal market, up to its own perception of that bypass price. Certainly more recently, Todd's confidential analyses and planning appear to attribute a relatively high internal price as the opportunity cost of selling externally. There is an emphasis on internal projects.²¹⁴

²¹⁴ See, for example, the comments on the Todd Wholesale group's longer terms plans, last paragraph, CB18/503, from the 2009 Corporate Plan.

[436] That strategy does tend to count further against any SLC occurring, if Todd had more gas to market.

[437] Having reviewed the various prospects for counterfactuals canvassed on behalf of Todd, we consider that there are numerous substantial obstacles to its ability to establish a counterfactual in which an SLC was a real and substantial prospect, relative to the state of competition in the factual circumstances that have pertained. We are not satisfied that Todd would have changed its behaviour by pursuing sales for any material volumes of additional gas. We are satisfied that for the major part of the relevant period, at least, Shell and OMV would not have sought to sell material volumes of additional gas. To the extent that additional gas was marketed from Pohokura, we are satisfied that it would generate a response from other sellers in the market that would, at the least, substantially offset the increased Pohokura production.

[438] Accordingly, Todd has failed to make out the necessary proposition on its counterfactual, namely that had it been permitted to increase production at Pohokura to its share of capacity, that would have led to a sufficiently material increase in the supply of gas to produce a material lessening in price. The same finding holds, in the event that the increase from Pohokura was a further 15 PJ/a, which could ensue if, contrary to our analysis, increased production from Pohokura by Todd was followed by similar proportionate increases by Shell and OMV.

[439] In all these circumstances, we are satisfied that Todd could not make out an SLC.

Claim that condensate should be shared relative to uplift, not in proportion to equity shares

[440] Before considering each of the causes of action under the Act in light of the above findings, it is appropriate to comment on an aspect of Todd's case that we found curious.

[441] No separate point was taken in Todd's pleading that inclusion in the off-take rules of a stipulation that the parties would take condensate in accordance with their percentage participating interests breached Todd's rights under the JVOA. This point appears not to have been the subject of any separate attention prior to trial. In Todd's opening, there was also implicit acceptance that entitlement to condensate was by reference to equity shares, rather than reflecting a party's level of off-take of gas. In summarising the relief sought in the proceedings, Todd's opening stated:²¹⁵

Secondly, as a consequence of deferring gas production that, but for the offtake regime, would have occurred in 2007-2009, the production of associated condensate was also deferred.

[442] Approaching a head of damages in this way could only be consistent with Todd's entitlement to its equity share of condensate being deferred, because the off-take rules deferred gas production. Relief in that form is inconsistent with a discrete challenge to the arrangements for sharing condensate. A claim to the benefits of a larger portion of condensate that would follow from Todd lifting more gas and being entitled to the proportionate part of condensate produced with that gas, would have been expressed quite differently.

[443] During his cross-examination, Mr Richard Tweedie appeared to accept without objection that condensate is being sold on an equity basis. When re-examined on the answer involving this point, Mr Tweedie appeared to acknowledge that the sharing of condensate relative to participating interests was explicit in the JV, before acknowledging that this point might be arguable. Those comments, and his answers to questions from the Court, were consistent with Mr Tweedie accepting the effect of the provisions in Article 10.2 in respect of condensate, at the same time as protesting that that outcome is unfair.²¹⁶

[444] Mr Hall confirmed that there has been no negotiation between the parties on any alteration to the provision that liquids are to be taken in equity shares.²¹⁷

²¹⁵ Todd opening submissions, paragraph 7.21.

²¹⁶ XXN, T321/19, RXN, T485/6-9, Questioned T492.

²¹⁷ T947/5-948/2.

[445] The last witness to be heard was Mr Burt of OMV. Somewhat unsatisfactorily, a technical reason for providing that condensate is to be divided on “equity shares” (ie in accordance with levels of participating interests) emerged only in questions asked of him within minutes of the evidence in the case closing. Mr Burt explained that the ratio of condensate to gas produced will reduce over time as the pressure of the gas in a field reduces.²¹⁸ Because field operators do not know what the level of liquid production will be in the future, irrespective of gas off-take, it is appropriate to allocate condensates in accordance with equity shares to avoid complications later in the life of the field. In all the fields of which Mr Burt was aware, liquids are taken in proportion to parties’ equity shares, for this reason. Although Todd had a very limited opportunity to contest this point, it does accord with common sense and would certainly justify the drafters of the AIPN model stipulating as the standard provision that condensate is to be taken in accordance with equity shares, as provided for in Article 10.2(A).

[446] The effect of the relevant part of Article 10.2 did not arise in the contract part of the case.²¹⁹ However, we are satisfied that it provides for division of condensate in accordance with each party’s proportionate share of the venture. The relevant provision in the off-take rules accords with that provision.²²⁰

[447] The point does not bear directly on any of Todd’s claims. However, Mr Murray’s projections as to the conduct of each of the parties in his counterfactual (and indeed damages calculations) were predicated on the contrary assumption that, had Todd been entitled to uplift the larger amounts of gas it claims it wished to sell, it would also have procured proportionately larger volumes of condensate relative to its own higher level of production, rather than its equity share of condensates produced.²²¹

[448] Mr Murray’s assumption was also relevant to the position of OMV. Part of his analysis was that OMV’s own financial interests were advanced by supporting Shell in the constraints imposed. His analysis assumed that OMV would only get a

²¹⁸ T4672/6-20.

²¹⁹ Quoted in [68] above.

²²⁰ Quoted in [79] above.

²²¹ T4090.

proportion of condensates, relative to its own uplift of gas. Dr Bamberger's analysis challenged this on two grounds. First, that if the calculation of returns was done on the basis that OMV was allocated 26 per cent of all the condensates produced, then it was actually in its financial interests to allow Todd to uplift its full entitlement, because of the benefit accruing to OMV from increased condensate production. Second, that any OMV concern to hold back on Pohokura to optimise the prospects for Maui ROFR sales could no longer arise once the ROFR sales were concluded. It would follow that OMV was actually harming its own financial interests from 2007, if these errors were addressed. We accept Dr Bamberger's criticisms.²²²

Section 27

[449] As noted above at [298], under s 27 no person may enter into an arrangement or understanding containing a provision that has the **purpose**, or has or is likely to have the **effect**, of substantially lessening competition in a market. The Court considers that neither of these elements is satisfied. For completeness, we give our reasons.

Section 27 – Effect

[450] Our conclusions on the evidentiary matters reviewed in [376] to [439] above mean that Todd would fail to make out any anti-competitive effect, sufficient to sustain a claim under s 27. Whilst most of the economists acknowledged that any material constraint would have some impact on competition, our own analysis confirms the view of those called for Shell and OMV, namely that the effect was never likely to be substantial.

Section 27 - Purpose

[451] The strands of analysis in the Court of Appeal judgments in *ANZCO Foods*

²²² See Murray XXN, T4114-4118.

*Waitara Ltd v AFFCO New Zealand Ltd*²²³ on “purpose” as used in s 27 were summarised conveniently in *BOPE* as follows:²²⁴

- [a] Purpose is primarily (and perhaps preferably) to be assessed objectively, but subjective evidence of an anti-competitive purpose will be relevant to the inquiry.
- [b] As a result, purpose cannot be equated with actual or likely effect – there may be a prohibited purpose notwithstanding no actual or likely effect of substantially lessening competition.
- [c] However, where the provision in question is incapable of having the effect or likely effect of substantially lessening competition, that will be relevant, and may be determinative, of the purpose inquiry.

[452] The wording of s 27 makes it clear that the purpose is to be attributed to the agreement, arrangement, etc, not to the parties themselves.

[453] It is unnecessary in the present circumstances to be diverted by the debate as to whether the requisite anti-competitive purpose under s 27 can be established in the absence of an actual or likely effect of the off-take rules in lessening competition. Todd’s submission in support of the proposition relied upon William Young J’s judgment in *ANZCO* in which he dissented on this point. *ANZCO* involved alleged breaches of the Act in AFFCO’s attempts to enforce a restrictive covenant intended to run with the land on sale of a former meat works, prohibiting its subsequent use as such. William Young J’s reasoning was to the effect that proscribed conduct was intended to include conduct where the purpose was to substantially lessen competition in a market, irrespective of proof that a substantial anti-competitive effect ensued or was likely.²²⁵ However, the majority of the Court took the view that if the inability of the restrictive covenant to ever achieve a substantial effect in lessening competition was absolutely clear, then it would be unreal to attribute to AFFCO, in enforcing the covenant, the purpose of substantially lessening competition. The approach of the majority reflects prominence being given to an objective analysis of purpose, as reflected in the conduct complained of. It would suggest, for example, that a requisite anti-competitive purpose attributable to a

²²³ *ANZCO Foods Waitara Ltd v AFFCO New Zealand Ltd* [2006] 3 NZLR 351 (CA).

²²⁴ *BOPE* at [339].

²²⁵ At [150] to [157]. See especially [152].

defendant's conduct but not being objectively sustainable on an analysis of the anti-competitive effect of the conduct would not be sufficient to make out a claim of breach of s 27.

[454] The present situation, unlike *ANZCO*, is not one in which an anti-competitive purpose is reflected in the terms of the off-take documents themselves. There, the covenant forbade use of the site for a meat works and that was the alleged anti-competitive constraint. Here, the terms of the off-take rules do not constrain production levels at Pohokura. Todd's further claims seek to establish anti-competitive purposes from contemporaneous exchanges reflecting the concerns behind the documents, and their potential to be used for anti-competitive purposes. If a majority supported a WP&B at, say, 40 or 50 per cent of the expected production of 70 PJ/a in the plateau period, then such a use of the off-take documents would need to be viewed in a different light from their use thus far. However, that is not to say that the terms are inherently anti-competitive merely because an extreme use of them may give rise to that prospect.

[455] Other commercial reasons for allegedly anti-competitive conduct will not save it from breaching s 27, if a requisite anti-competitive purpose is made out.²²⁶ That does not prevent the Court assessing the nature and extent of other purposes, to the extent that they may become relevant in denying an anti-competitive purpose. It simply means that if a requisite anti-competitive purpose is made out, it remains such, notwithstanding other non-proscribed justifications for the conduct.

[456] If we apply an objective analysis of purpose as preferred by the majority of the Court of Appeal in *ANZCO*, then the substantial margin by which Todd fails to make out any requisite effect or likely effect in the nature of an SLC tends to negative the existence of any relevant anti-competitive purpose. Where, on a fully informed analysis, it appears highly unlikely that an anti-competitive effect could be achieved, then an objective assessment of purpose would tend to lead to a consistent result, that an anti-competitive purpose could not be made out.

²²⁶ *Auckland Regional Authority v Mutual Rental Cars (Auckland Airport) Ltd* [1987] 2 NZLR 647.

[457] The provisions of the off-take documents were pleaded as having the purpose of lessening competition in that they limited production, allowed an artificial limit on production, and prevented the parties from selling their respective shares of the total capacity of Pohokura. No greater level of particularity was pleaded, and during the hearing Todd focused on three motives related to the introduction and use of the off-take documents which Todd argued as further manifestation of the anti-competitive purpose in limiting production from Pohokura. These were first, to enable the MMCs to prioritise production from Maui, second to protect reserves at Pohokura, and third as part of an “anti-Todd” campaign, intended to harm Todd.

[458] The third of these anti-competitive purposes was not addressed in Todd’s closing. In [234] to [252] above, the Court addressed the factual scope for such concerns. That review concluded that harming Todd was not among the purposes motivating Shell. As a matter of law, any attributed purpose of harming a particular competitor is not in any event relevant where the section requires more than trivial and transitory harm to the competitive process.²²⁷

[459] Reverting then to the nature of the anti-competitive purpose pleaded, namely limiting Pohokura production, submissions for Shell protested at the pervasive way in which the whole of Todd’s case was presented as if the off-take documents have produced “constraints” and “limits” on production. From Shell’s perspective, the off-take documents should be characterised as enabling provisions, ensuring that joint production of gas and condensates can occur subject to a workable regime in which the products jointly produced can be separated out for each of the parties to take possession and deal with.

[460] A further factual rejoinder is that it is wrong to characterise production as “limited and constrained” when it has occurred at the levels that had uniformly been proposed from the earliest work by these joint venturers. Further, once swing capacity is acknowledged as an asset of the Pohokura field, then rules facilitating fluctuations in the level of production that will enable the swing capacity to be exploited are not limiting production. Rather, the rules facilitating fluctuations are

²²⁷ See, eg, *ANZCO* at [242].

managing production in a manner enabling a return on the asset represented by that swing capacity.

[461] We accept that the WP&B resolutions providing for production at the rate of 70 PJ/a have limited production to less than the overall capacity that the PPS is capable of. However, our use of the terms “limited” or “constrained” when referring to the level of production is not to be taken as inferring that such limits have necessarily been procured improperly.

Prioritising Maui

[462] Todd focused on a number of Shell internal documents to invite the inference that Shell was sufficiently concerned about harm to the level of ultimate returns to be earned from Maui, that Shell pursued deferral of production from Pohokura so as to facilitate earlier sales of more gas from Maui. Todd invited that inference to be drawn, in particular, from three internal Shell emails. The first, dated 28 June 2004, contained confidential material. The context was a preliminary suggestion that Shell should consider promoting agreements that would permit substitution of production as between Maui and Pohokura. Such a proposal was seen as premature, in part because the author suggested Shell needed to understand “where we would get to on Pohokura gas balancing”. In reviewing considerations that could influence Shell’s own thinking as to which field it might press gas sales from first, the Shell executive commented:²²⁸

We observe that if we want to bias buyers to lift Maui over Pohokura, we need to shoot for a low lifting cost for Maui – this, however, is the antithesis of what Strawman is all about.

[463] That communication suggests that Shell had yet to form any view on whether it wished to pursue initiatives to prioritise one field over the other.

[464] The second internal comment was in a Shell email dated 12 April 2005.²²⁹ It included the comment:

²²⁸ CB7520.

²²⁹ CB8331.

We have only assumed 70 PJ/a offtake so far in supply/demand study – 83 PJ/a will take even more production/sales off Maui.

[465] In the context at the time, that suggests that production from Pohokura would generate an excess of supply over the then perceived level of demand so that at a point (presumably somewhere below 70 PJ/a) the introduction of gas produced from Pohokura would displace sales that would otherwise be made of Maui gas. That does not of itself suggest a view by Shell as to its priorities between the two fields.

[466] The third internal communication is dated 5 October 2005 and is from a STOS executive based in New Plymouth, to a Shell international employee based in The Hague. The recipient's views were sought on the potential content of GBAs, implicitly because of her experience in such agreements in other jurisdictions. In seeking guidance on the possible content of a GBA, the request was introduced in the following way:²³⁰

The background is that NZ only has 3-4 reasonable sized gas fields (Maui – Shell share 84%, Kapuni SS 50%, Pohokura 48%, Kupe 0%). Pohokura would be the first one with a balancing agreement. Shell's aspiration would be to have a large flexibility to underlift and overlift to play its portfolio of gas (particularly Maui has a large capacity in the short term that is somewhat stranded when Pohokura comes on stream. Having the ability to produce Maui gas preferentially (not lifting Pohokura) could be desirable because of the high operating cost structure of the Maui field (even if the Maui partners which jointly sells, also get extra sales because of it).

[467] Todd also relied on a comment in minutes of an MMC ROFR sub-committee meeting on 18 May 2006 at which all of Shell, OMV and Todd were represented. In the context of reviewing the prospects for an offer of ROFR gas to Methanex, the minutes record an observation that:²³¹

...significant competitive tension may be lost from the long term ROFR discussions, and Maui offtake rates post Pohokura may require implementing a single gas train operation at Oaonui, with all the associated costs that this would incur.

[468] As part of Mr Murray's reply brief, he undertook an analysis and determined that deferral of Pohokura production for the sake of prioritising sales of Maui ROFR gas thereby enabling higher prices to be maintained was a profitable strategy for

²³⁰ CB9189.

²³¹ CB11896.

Shell and OMV.²³² Mr Murray's hypothesis assumed that Todd would profitably market its additional Pohokura gas on comparable terms to the sale of the quantities that it did achieve, but that Shell and OMV would not be able to market their additional Pohokura gas. In those circumstances, and because of the impact he attributed to reduction at Pohokura maintaining prices for Maui gas, he suggested ranges of financial advantage to Shell and OMV up to some \$252 million. There is no suggestion in any of the Shell internal documents that any analysis on anything like these terms was undertaken by anyone at Shell in the relevant period.

[469] The documents summarised above were put to Dr Bansal who had been the head of Shell at the relevant time. He disagreed that the proposition for prioritising Maui over Pohokura had at any stage got to a point where it was Shell's firm policy. We are inclined to accept that. All projections of the level of production suggested for Pohokura were consistent from the period around 2003, when the Maui redetermination process was suggesting less reserves at Maui than the MMCs would have been expecting, to fulfil their existing Maui contractual obligations. Whilst that was the position in respect of Maui, Pohokura could be seen as a source of back-up for inadequate supply from Maui. The same projections for the level of production from Pohokura continued to be adopted by Shell and OMV once the level of Maui resources was re-estimated upwards again.

[470] The MMCs faced the prospect of a consistent level of competition from Pohokura, namely 70 PJ/a, throughout the varying circumstances of potential undersupply from Maui, and later concerns that oversupply from Pohokura would dent the demand for gas from Maui. If, indeed, every PJ of Pohokura gas over a certain level (which would inevitably be below 70 PJ/a) was more or less a PJ that would not be sold from Maui, and Shell and OMV, as the majority at Pohokura, wished to protect their Maui interests, then the rational response would be to have authorised production from Pohokura at a level substantially less than 70 PJ/a. There is no suggestion at any stage that Shell or OMV considered doing so. All three parties sold their shares of the first tranche of Pohokura gas in early 2004. Those sales appear to have anticipated production at or possibly above an average of 70 PJ/a.

²³² Murray reply brief, paragraphs 237-250.

[471] Todd's perception that production at 70 PJ/a was a constraint to protect Maui assumes that Pohokura would otherwise produce at higher levels. We are satisfied that this is not the reason why WP&B decisions were not made for higher levels of production.

[472] In any event, any such strategy is not one that Shell and OMV could be sure would succeed. They were not unconditionally preventing Todd from taking more gas at Pohokura. Rather, they required enforceable arrangements to be in place to redress imbalances in the level of off-take from Pohokura, before permitting Todd to take more than its 26 per cent share of the level of production that had been agreed by the majority. Had Todd concluded arrangements that protected the position of Shell and OMV when they took at lower levels, even on terms that were without prejudice to Todd's entitlement to challenge the interpretation of the JVOA on which it rested, then Shell and OMV would not have constrained a higher level of production from Pohokura by Todd.

[473] Nor can Shell and OMV's positions be treated as the same. Shell had a significant majority interest in Maui. OMV, like Todd, had a substantially larger interest in Pohokura than it did in Maui. Mr Murray's analysis of financial benefits for Shell to prioritise Maui over Pohokura could not similarly apply to OMV. This is particularly so when his assumptions are corrected to allow for OMV taking condensate relative to its equity share, rather than the level of its own gas uplift.²³³

[474] For these reasons, we are not satisfied that Todd could make out an anti-competitive purpose on the part of Shell or Shell and OMV, by virtue of the suggested wish to prioritise production from Maui.

“Protecting reserves” at Pohokura

[475] Todd contended that the off-take documents had been introduced and were implemented to protect the level of reserves available to Shell and OMV at Pohokura. This protection is argued to be an anti-competitive purpose because it

²³³ See [448] above.

prevented Todd accessing production from Pohokura at the rate the PPS was capable of producing. In particular, Todd's final submissions attributed to Shell a wish to protect the level of reserves arising where Shell had sold on flexible terms and the buyers had not demanded delivery of all of the gas to which their contracts entitled them. When compared with Todd that had sold on a flat basis, this would result in Shell falling behind Todd.

[476] As to OMV, the terms of sale of its first tranche of gas included a warranty given to the buyer that it would not sell more Pohokura gas than it had contracted to under that contract, unless and until additional amounts were available to OMV within revised P85²³⁴ reserves. Todd argued that having assumed that self-imposed constraint, OMV was, like Shell, motivated to protect its on-going reserves at Pohokura by preventing Todd taking gas at any higher level.

[477] Todd's characterisation of Shell and OMV's concerns to prevent substantial imbalances in the level of off-take of production from Pohokura depends on there being no contractual authority or other justification for Shell and OMV to wish to keep the respective levels of off-take of gas from Pohokura more or less in balance with each party's respective percentage interests in the venture. The fundamental premise on which it was claimed to be anti-competitive for the majority to use rules intended to keep the parties in this form of balance was that Todd had a right to call for production from Pohokura at higher volumes. Whilst conduct complying with a contract may nonetheless be found to be anti-competitive, the context of a plaintiff's position in its postulated counterfactual must reflect the reality of the situation, absent the challenged conduct. Here, that is the application of rules such as those in the off-take documents. We are not satisfied that Todd can postulate any realistic possibility of a scenario in which it would have an entitlement to production at higher rates, merely by removing the off-take documents. The whole basis of such a joint venture is commitment in proportionate shares, and a return reflecting those shares.

²³⁴ Defined term, see Appendix 1.

[478] We are satisfied that Shell and OMV had valid grounds for concern that if Todd got materially ahead of them in proportionate levels of gas taken, without enforceable arrangements for redressing the balance, then they might ultimately lose a part of the return on the amounts they had invested, and their proportionate contributions to on-going operating expenses. At the least, Shell and OMV foresaw difficulties in resolving such issues with Todd, if the rules were not settled in enforceable form before disproportionate off-take occurred. In the context of their difficult relationship, it would be unrealistic to expect that Shell and OMV should ignore such concerns and permit unequal lifting without such arrangements in place. Their stance was not about limiting sales, but rather about protecting entitlements.²³⁵

[479] Shell cited some colourful language used by Mr Richard Tweedie during a conference held by the Commission on its draft authorisation for joint selling in July 2003. In that context, in support of the authorisation sought, Mr Tweedie made dire predictions of the value-destructive consequences of requiring separate selling. He speculated in terms where other parties would be “thieving our gas...they haven’t paid for it and we’ve got an internal scrap...”.²³⁶ Both Mr Richard Tweedie and Mr Hall were tested on cross-examination about the consequences of their theory that an underlifting party was vulnerable to having its share taken by others who were able to take the gas in a timely way.²³⁷

[480] The outcome of this point does not depend on the reasonableness of Shell and OMV’s apprehensions that enforceable arrangements should be in place before one party was allowed to uplift materially disproportionate volumes of gas. On the view the Court has come to on the contract, and in the factual context as it developed, it is simply not tenable to assert that the wish of Shell and OMV to “protect reserves” by promulgating and then implementing the off-take rules and the respective WP&Bs is an anti-competitive purpose in terms of s 27.

²³⁵ See, for example, Bansal XXN, T2965/15-29.

²³⁶ CB2946.

²³⁷ T330/29-331/19 (Richard Tweedie) and T749/23-750/2 (Hall).

Section 27, “via” s 30

[481] The subheading within Part 2 of the Act immediately prior to s 30 is “Price Fixing” and the relevant part of the section for present purposes is as follows:

30 Certain provisions of contracts, etc, with respect to prices deemed to substantially lessen competition

(1) Without limiting the generality of section 27 of this Act, a provision of a contract, arrangement, or understanding shall be deemed for the purposes of that section to have the purpose, or to have or to be likely to have the effect, of substantially lessening competition in a market if the provision has the purpose, or has or is likely to have the effect of fixing, controlling, or maintaining, or providing for the fixing, controlling, or maintaining, of the price for goods or services, or any discount, allowance, rebate, or credit in relation to goods or services, that are—

(a) Supplied...by the parties to the...arrangement...

[482] The classic mischief addressed by this provision is arrangements between competitors to agree on the price for their goods or services when all others affected by their conduct would expect those prices to be influenced by competitive tensions between them. Other forms of anti-competitive arrangements potentially caught by s 27 require a case-specific analysis as to whether they have a purpose, effect or likely effect of substantially lessening competition. However s 30 creates “per se” liability for a breach of s 27 without the requirement for that analysis, if the nature of the arrangement being challenged provides for the fixing of prices because such arrangements are deemed by the Act to have the purpose or to have, or be likely to have, the effect of an SLC.

[483] In the present case, Todd does not allege that Shell and OMV had any agreement or arrangement to fix prices. Rather, Todd characterises the off-take documents as fixing levels of output and relies on economic analysis from Mr Murray and Dr Veljanovski to the effect that arrangements between competitors to fix the level of production is the other side of the same coin as competitors arranging to fix prices.²³⁸

²³⁸ Mr Murray, first brief, paragraph 184; Dr Veljanovski, first brief, paragraphs 145, 148 and 149, T3529/5-13.

[484] OMV argued that s 30 could not apply to arrangements to limit the quantities supplied in a market, because the impact on price will be indirect, and will vary depending on the extent to which the parties to such an arrangement have market power. In contrast, an agreement to fix prices inarguably does fix those prices. This submission questioned Mr Murray and Dr Veljanovski's proposition that limitation on price and on output are the two sides of the same coin. This is because, for the purposes of regulating anti-competitive behaviour, per se liability is obviously intended by Parliament where competitors agree on price, but the anti-competitive impact of agreements on level of output is not so clearly likely to have, or be intended to have, such anti-competitive effect.

[485] Shell submitted that Todd's pleading does not conform with s 30 in alleging any arrangements that "fixed" price. Rather, Shell argues that the pleaded allegation is of arrangements that had the effect, or likely effect, of "controlling or maintaining", or providing for the controlling or maintaining of the price of gas. Shell denied that any of the consequences of the off-take documents could be characterised as controlling or maintaining prices. Each of the parties separately sold their first tranches of Pohokura gas. There was no analysis undertaken that the price terms achieved in those sales were influenced by the prospect that annual WP&Bs would conform with the plateau level of production reflected in the FID, at or around 70 PJ/a.

[486] No authority was cited for the proposition that arrangements to fix output are to be treated as if they are arrangements for the fixing of price, for the purposes of s 30. We do not need to decide the point, but conceptually recognise the prospect that a carefully crafted arrangement between competitors to restrict output, such as in circumstances where the competitors recognise the impact it would have on price and sought to avoid the literal wording of s 30, might arguably be caught by the section. However, that is not the situation here.

[487] Shell also sought to distinguish the competition that occurs between Shell, Todd and OMV in their capacity as sellers of gas, from their joint conduct in directing the level of production from Pohokura. On Shell's analysis, the arrangements as to the level of production from Pohokura are a reflection of their

decisions as joint venture producers of gas from jointly owned production facilities where the gas is initially produced for them as tenants in common. We are not persuaded that this would be sufficient to take the off-take arrangements outside the scope of s 30, if it otherwise did apply. A material input into the WP&B decisions by each venturer as to the level of production will be their separate perceptions of the level of demand. Accordingly, it would be artificial to exclude such decisions on the ground that they are notionally made whilst the parties wear their hats as joint producers, rather than when wearing separate hats as competing sellers of gas.

[488] Any agreement on price will obviously have an impact in the market and would rationally only be undertaken if the parties to it perceived their position in the market as sufficiently strong for them to be advantaged by it. In contrast, arrangements as to the level of output between joint owners of production facilities may have a legitimate rationale other than an intention to influence prices. The justification for attributing per se liability does not arise, and the consequences of arrangements such as the present should be measured by reference to the tests under s 27 itself. Accordingly, to the extent, if at all, that the off-take documents reflect an arrangement to limit supply, then it is not one that is to be treated as an arrangement to limit prices for the purposes of s 30. Todd's ninth cause of action must fail.

Section 29

[489] Todd's tenth cause of action pleaded that the off-take documents contain exclusionary provisions within the meaning of s 29(1) of the Act. The operative provisions of s 29 are:

29 Contracts, arrangements, or understandings containing exclusionary provisions prohibited

- (1) Subject to subsection (1A), for the purposes of this Act, a provision of a contract, arrangement, or understanding is an exclusionary provision if—
 - (a) It is a provision of a contract or arrangement entered into, or understanding arrived at, between persons of whom any 2 or more are in competition with each other; and
 - (b) It has the purpose of preventing, restricting, or limiting the supply of goods or services to, or the acquisition of goods or

services from, any particular person, or class of persons, either generally or in particular circumstances or on particular conditions, by all or any of the parties to the contract, arrangement, or understanding, or if a party is a body corporate, by a body corporate that is interconnected with that party; and

- (c) The particular person or the class of persons to which the provision relates is in competition with one or more of the parties to the contract, arrangement or understanding in relation to the supply or acquisition of those goods or services.
- (1A) A provision of a contract, an arrangement, or an understanding that would, but for this subsection, be an exclusionary provision under subsection (1) is not an exclusionary provision if it is proved that the provision does not have the purpose, or does not have or is not likely to have the effect, of substantially lessening competition in a market.
- (2) For the purposes of subsection (1)(a) and (c), a person is in competition with another person if that person or any interconnected body corporate is, or is likely to be, or, but for the relevant provision, would be or would be likely to be, in competition with the other person, or with an interconnected body corporate, in relation to the supply or acquisition of all or any of the goods or services to which that relevant provision relates.

[490] Todd alleges that the purpose of the off-take documents is to limit production and supply of Pohokura gas, thereby preventing, restricting or limiting the supply of Pohokura gas by one or more of the parties to actual and potential wholesale purchasers of Pohokura gas and/or to Todd's affiliate, Nova.²³⁹ Further, that the actual and potential wholesale purchasers of Pohokura gas and/or Nova are in competition with one or more of the parties for the supply of Pohokura gas.

[491] The section targets collusive behaviour in the nature of boycotts. As cited in *Gault on Commercial Law*:²⁴⁰

A classic boycott is an effort by a group of traders to exclude or inhibit a competitor trying to enter or compete in their market either by themselves not dealing with the competitor or by coercing or inducing one or more suppliers or customers not to deal with him.

²³⁹ 3rd ASC, paragraph 100.

²⁴⁰ Thomas Gault (ed) *Gault on Commercial Law* (looseleaf ed, Brookers) at [CA29.05(2)], citing L A Sullivan *Handbook of the Law of Antitrust* (West, St Paul, 1977) at 255.

[492] Shell argued that s 29(1)(b) of the Act requires something in the nature of a targeted boycott, whereas, if at all, the off-take documents limit the supply of Pohokura gas to the entire market. It is not as if, say, the off-take documents reflected an agreement to not sell to the ROFR buyers, so that they would be pressured to deal with the MMCs. Todd has complained that Nova is constrained, but there is nothing in the off-take documents that identifies any potential purchasers of Pohokura gas and Shell is right to say that any limitation on supply is indiscriminate. That counts against the provision applying. Any limitation in the potential supply to, for example, Nova that results from WP&B decisions is also indiscriminate because it limits supplies to the whole market, when the mischief addressed by the section is inherently discriminatory to keep one or more persons out of a market.

[493] OMV argued that s 29 does not apply for an additional reason, namely that Shell and OMV do not compete to supply Pohokura gas to Todd. The challenged arrangements in the off-take documents relate to the rate at which the jointly owned facilities will produce gas, with each of the parties taking delivery of their proportionate shares. They then compete in the downstream supply to various purchasers. However, we do not accept that the absence of competition between the parties allegedly enforcing a constraint to supply the complainant (Todd) should take the conduct outside the purview of s 29.

[494] Nonetheless, we accept that the absence of any targeted element in the off-take documents takes the conduct complained of outside of what is rendered unlawful by s 29. If we were wrong in that conclusion, we would nonetheless be satisfied that Shell and OMV could discharge the onus required of them to make out the defence under subs (1A). That is because, for the reasons previously outlined,²⁴¹ the relevant parts of the off-take documents do not have the purpose and are not likely to have the effect, and nor do they have the effect, of substantially lessening competition in the relevant market.

²⁴¹ See [450] to [480] above.

The joint venture defence

[495] When dealing with Todd's ninth cause of action alleging breach of s 30, it was unnecessary to consider whether, had that cause of action otherwise been made out, Shell and OMV could nonetheless have availed themselves of the so-called "joint venture defence" in s 31 of the Act. That section acknowledges, as one relevant form of joint venture, an activity in trade carried on by two or more persons, whether or not in partnership. The business structures contemplated include the joint venture arrangements of parties to these proceedings, in their Pohokura JV. Section 31(2) provides that nothing in s 30 applies, inter alia, to arrangements entered into for the purposes of a joint venture, where such provisions relate to the supply of goods jointly produced by the parties to the joint venture in proportion to their respective interests in the joint venture. We note that the Commission, in its September 2003 determination authorising joint selling of gas, opined that the s 31 defence would have applied to the then proposed joint selling arrangements.²⁴²

[496] The evident purpose of s 31 is to recognise that where activities in trade are undertaken by parties to a joint venture instead of by a single entity, then the joint venture process for decision-making within their JV does not constitute such decisions "contracts, arrangements or understandings" for the purposes of s 30. One rationale for this is that the joint venturers are contributing to the equivalent of a single decision such as might be taken by a single business entity.

[497] Had we been persuaded that arrangements as to the level of output had status as arrangements limiting price, then we would have accepted that s 31 applied. Had the Pohokura JV been a sole venture, such as by Shell, then its singular decisions about the level of annual production would be the equivalent of the JV decisions made. Accordingly, the conduct challenged by Todd as contrary to s 30 would fall both within the letter and spirit of the joint venture defence in s 31.

²⁴² CB3933, paragraph 267.

Wider policy considerations

[498] Although s 31 is relatively confined in its scope, it is illustrative of the policy behind Part 2 of the Act dealing with restrictive trade practices, and subject to the overall purpose of the Act in s 1A to promote competition in markets for the long-term benefit of consumers within New Zealand. For the reasons we have reviewed, we are satisfied that none of the Commerce Act causes of action could succeed. We are reinforced in these views by standing back and reflecting on the policy considerations influencing the application of ss 27, 29 and 30 to conduct of the type Todd complains of here.

[499] Shell urged that it was inconsistent with the policy of the Act to render decisions made by the joint venturers vulnerable under the Act, when they would not have been vulnerable in the same way if reached by a single business. A recurring theme in the evidence from Professor Hausman was that joint ventures are pro-competitive because they permit sharing of risk and therefore enhanced investment in risky ventures such as oil and gas exploration. It would follow that, to the extent that it was only the JV structure that brought the conduct of business at Pohokura potentially within the Act, the pro-competitive consequences of resort to that form of business organisation ought to be taken into account in arriving at any view on the net extent of anti-competitive consequences.

[500] In this regard, where the JVOA was seen as not having an adequate mechanism for division of the joint property produced by the venture, then Shell urged that the off-take documents ought themselves to be seen as pro-competitive because they facilitated production by addressing the manner in which it would thereafter be divided into proportionate shares for the parties. Where relief under the Act was pursued by Todd in circumstances in which it had failed on its contractual claims, granting such relief would mean that a minority in a joint venture could force the majority to pay for and produce more gas than the majority considered to be the optimum level of production. Further, such relief under the Act could require delivery to Todd of more than its proportionate share of production. All that would be without Shell and OMV having any enforceable commitment to later redress the imbalances that that would involve. Mr Taylor for Shell argued that such an

outcome would generally undermine the use of joint ventures because, where the Act intervened to advantage Todd in this way, it was unlikely that any different contractual provisions could prevent a similar outcome recurring.

[501] Mr Taylor also urged that such an outcome would be entirely inconsistent with the policy underlying the Act, in that it is naïve to suggest that the consumers whose interests are to guide the application of the Act would ever be materially advantaged, if the Court was prepared to intervene. Shell invited the inference from the evidence that gaining the advantage over Shell and OMV that it seeks at Pohokura would be used by Todd in forcing higher levels of output at Pohokura, but then “backing off” production at M&M which it viewed as “insurance”.²⁴³ Shell suggests that the outcome overall would not see more gas offered to consumers, which is the most basic justification for intervening under the Act.

[502] These concerns of Shell invite analogy with decision-making within a closely held company, by means of shareholder voting. Generally in such situations majority rule will not be upset unless an opposing minority could make out a case of oppression for relief under the Companies Act. Shell would be on strong ground in submitting that no such case of oppression could be made out, where the off-take documents, and particularly their application in the annual WP&Bs, were of a type generally recognised by all parties as necessary, or at least desirable, at the time they committed to the investment, and the levels of annual production are consistent with FID.

[503] OMV raised a somewhat similar range of concerns that the claims by Todd are inconsistent with the policy underlying the Act. Whilst the relevant provisions are intended to protect the process of competition, and not particular competitors, granting any of the relief sought would involve a re-assignment of property rights under s 27. Such relief would also potentially compel disposal of property disproportionately, without Shell and OMV having the comfort of an enforceable arrangement for later redressing imbalances. All this, in circumstances where Shell

²⁴³ Mr Corlett, in cross-examining Mr David Hunt (T3311), suggested that production at less than capacity from M&M was a valid form of “insurance policy” for Todd because the additional capacity would afford security to buyers that Todd would deliver. In that light, it would also afford flexibility for Todd to take advantage of short-term opportunities.

and OMV would be paying 74 per cent of the costs of excess production and where Todd could have gained access to that additional property without Court intervention once it had concluded arrangements to address the imbalances. OMV argued that any relief granted to Todd would force a situation on Shell and OMV inconsistent with their original decision to invest, when the Act should not intervene to override the basis on which their investment was made.

[504] Cumulatively, these points provide substantial support for the view we have arrived at, namely that it is inappropriate to invoke the provisions in Part 2 of the Act which are intended to prevent the effect of anti-competitive practices, in relation to the conduct complained of within this JV.

Damages

[505] Against the prospect that this judgment may subsequently be found to be wrong on either or both the contract or Commerce Act causes of action, it is appropriate to provide an overview of the issues going to damages.

[506] Todd sought damages on all its contract causes of action on the conventional basis, namely that it was entitled to the measure of damages reflecting the amounts required to put it in the position it would have been in, had the contract been performed. This involved reconstructing what, on Todd's view, would have been the relatively more profitable sales of greater volumes of gas than it will achieve later in the life of the Pohokura field. That is, if its level of production had not been constrained below the volumes of gas it would have acquired for on-sale if Pohokura had delivered to Todd 26 per cent of its full capacity since first production. The last summary of variables provided to the Court with Todd's closing submissions quantified these losses as between approximately \$239 million and \$320 million.

[507] The measure of damages Todd sought for alleged breaches of the Commerce Act were the amounts allegedly required to compensate it for losses suffered as a result of Shell and OMV's conduct in breach of the relevant sections of the Commerce Act. Those causes of action also sought exemplary damages, proposed in Todd's final submissions to be calculated at up to three times the gains claimed to

have been made by Shell and OMV from the alleged breaches, and quantified on that basis at somewhat more than \$600 million.²⁴⁴

[508] Todd relied solely on Mr Murray to carry out the calculations on various assumptions as to what the net present value of such losses might be. Mr Murray acknowledged that he had undertaken the exercise only to reflect the extent of loss he analysed as flowing from the breaches of the Commerce Act as alleged by Todd, and had not separately undertaken any exercise to quantify damages for breach of contract.²⁴⁵

[509] Mr Farmer submitted that as a matter of law, the measure of loss in the present circumstances was the same. The fundamental approach in contract is captured in the following proposition:²⁴⁶

If the plaintiff has suffered damage that is not too remote, he or she must, so far as money can do it, be restored to the position he or she would have been in had the breach of contract not occurred.

[510] Mr Murray's assessment depended on the premise that, had Todd known in early 2006 that it could obtain its share of full deliverability from Pohokura, then it would have committed at that time to long-term sales out to 2016 for all the additional gas. Further, Mr Murray's analysis was on the basis that Todd would have taken advantage of higher prices potentially available at that time, before the market became aware of substantially more gas being available from Maui, than the market considered was the case in light of a substantial downward redetermination of the extent of Maui reserves in 2003.

[511] Mr Murray's analysis accepted that if sales were not made in that window, then the price differential would drop substantially, and any loss would have to be valued on a substantially more modest basis. No alternative calculations were proposed. In addition, Mr Murray acknowledged that not all of the volume of additional sales he originally attributed to Todd in this favourable window would

²⁴⁴ Todd closing submissions, paragraph 30.28.

²⁴⁵ T4223/21-28.

²⁴⁶ Burrows, Finn and Todd *Law of Contract in New Zealand* (3rd ed, LexisNexis, Wellington, 2007) at [21.2.1].

have been made because it depended on an upwards re-estimation of the extent of reserves at Pohokura not known to the parties until 2007.

[512] The basis on which damages were argued for at trial is in stark contrast to the quantification of losses when Mr Hall spelt out Todd's claims in a letter to Shell and OMV in July 2007. Todd quantified its damages at that time at \$4-4.5 million for gas, plus \$3.5-4 million for deferral of condensate.²⁴⁷ The projections of gas losses assumed Todd would get "at least 3.2 PJ/a of gas until at least the end of the plateau period...". The letter treated Pohokura's maximum capacity as 82.5 PJ/a.

[513] The Court analysed the prospect of further sales by Todd in the course of analysing its counterfactual hypotheses under the Commerce Act causes of action.²⁴⁸ In challenging both the suggested conduct in the counterfactual, and the construction of Todd's claim for damages, Mr Goddard focused particularly on the need for Todd to have made what Mr Goddard labelled as a "mega sale" in the short timeframe at the beginning of 2006, when Todd was aware of a further revision of Maui reserves, this time upwards, but the market was not. Todd's analysis also treats Shell and OMV as being unable to act as promptly as Todd would have, in negotiating long-term commitments for large volumes of gas. For all the reasons analysed in [384] to [439] above, I am satisfied that Todd cannot make out that such sale was more likely than not to have occurred.

[514] Todd did not invite analysis of the losses on any alternative loss of a chance basis.²⁴⁹ Given the substantial doubts established about a number of the impediments to Todd achieving favourable sales, the Court has simply not been provided with the evidentiary basis on which to test the proportionate prospects of such improved sales. Nor was any hypothesis along those lines tested in the course of evidence or argument.

²⁴⁷ CB12895-12899.

²⁴⁸ [384] to [439] above.

²⁴⁹ See generally, Burrows, Finn and Todd *Law of Contract in New Zealand* (3rd ed, LexisNexis, Wellington, 2007); *Benton v Miller & Poulgrain* [2005] 1 NZLR 66 (CA).

[515] Accordingly, I am satisfied that had there been a breach of contract, Todd would not have been able to make out losses of the type postulated in Mr Murray's reconstruction.

[516] Two further issues that would arise in evaluating Todd's entitlement to damages should be noted. First, Shell and OMV identified numerous strands under the heading of failure to mitigate that they argued would very substantially limit any award to which Todd was entitled. A first point is that access to greater volumes of Pohokura gas has been in Todd's own hands. It could have concluded a GBA recognising the arrangements to apply to rebalancing the shares taken, without prejudice to its claim that the regime imposed by the present off-take rules was not within the powers of the operating committee. Such an arrangement could also have been concluded without prejudice to the outcome of these proceedings. Todd could then have contracted to sell, and taken at higher rates than Shell and OMV, subject to Shell and OMV having appropriate contractual commitments to redress the imbalance later, either by taking gas at higher levels, or by resolving a formula for financial adjustment in the event that the imbalances could not be redressed in terms of delivery of production.

[517] Second, Todd's case was that the presence of the off-take rules and the pattern of majority decisions taken by Shell and OMV reasonably caused Todd to fear for the level of production that Shell and OMV would authorise in subsequent years. This "chilling effect" was claimed to operate to an extent that precluded Todd undertaking any further sales, at any level. The obvious rejoinder was that any such "chilling effect" could not rationally operate in that absolute way. Shell and OMV would, in all probability, want to continue production at the same levels, and Shell has indicated a preference for increasing levels of production. The chilling effect claimed could therefore not operate to rationally deter Todd from pursuing a base level of sales for subsequent years, within reasonable parameters around the levels of production already approved by the majority.

[518] A further concern raised was the period of delay since Todd commenced the proceedings, in circumstances where it was claiming on-going losses. Todd opposed an earlier initiative on behalf of Shell and OMV to separately determine Todd's

challenge to the lawfulness of the off-take rules. Instead, Todd has insisted on protracted interlocutories and the building of what has been a very extensive case, where on the terms of its own claims, every month has added very significantly to the damages it seeks from Shell and OMV. If the point became material, Shell and OMV could well be entitled to argue that damages ought not to run through at least some part of the protracted period of preparation for the substantive hearing.

Summary

Contract claims

[519] I have found that Todd cannot make out any of its claims for breach of contract. The right and entitlement addressed in the provisions on disposition of property in Article 10.1 relates to Todd's proportionate share of the gas actually produced at the PPS. That volume is appropriately settled on an annual basis by the budgetary process, proposed by the operator and eventually approved by the operating committee.

[520] The off-take rules constitute special arrangements relating to disposition of gas for the purposes of Article 10.3, and were promulgated in accordance with provisions of the JVOA by majority vote of the operating committee. Alternatively, if they cannot have status as special arrangements in the absence of unanimity, then the parts of the off-take rules dealing with disposition of gas were competently concluded by a majority resolution of the operating committee.

[521] Todd has made out certain of the aspects of conduct, particularly by Shell, of which it complained. However, those criticisms do not constitute a breach of any relevant obligation of good faith. Nor is Shell in its capacity as the operator of the Pohokura JV in breach of any fiduciary obligations owed to Todd.

[522] Notwithstanding that Todd was incorrect in asserting the interpretation it did of Article 10.1, it was entitled to connect its export pipelines in August 2006, and that entitlement continues.

[523] In the event that I am wrong on all these conclusions, I have analysed the claims brought by Todd for damages, for breach of contract. I am satisfied that it could not make out the losses claimed.

Commerce Act claims

[524] All of Todd's claims under the Commerce Act have been unsuccessful. Todd's claims failed two preliminary hurdles. First, an answer to the complaints they made of anti-competitive behaviour lay in their own hands. Second, they failed to make out a material element of the market they pleaded as the one in which the alleged anti-competitive behaviour occurred. In addition, we are satisfied that Todd could not make out a substantial lessening of competition, and the challenged arrangements do not constitute price fixing so as to attract per se liability under s 30. Nor do they constitute trade boycotting so as to be caught by s 29.

Costs

[525] Shell and OMV are entitled to costs. In light of the final observation I am about to make, I urge discussion between the parties on costs, having regard to the desirability of a positive on-going business relationship, rather than a sole focus on the history of the litigation. If needed, the parties may have a period of six months before reverting to the Court, should resolution of the costs issues not be possible between them.

A last word

[526] Any reader with the fortitude to have reached this point of an already overly long judgment will inevitably come to the view that it would be naïve in the extreme to urge that this judgment not be appealed, in light of the amounts at stake and the tensions in the relationship between the parties. Nonetheless, I take the unusual step of recording my view that the issues this judgment leaves the parties to grapple with ought to be resolved by negotiation between them, and not by further litigation. I venture that view not as a Judge apprehensive that the Court of Appeal might arrive

at a different view on any of the material issues. Rather, I do so as a New Zealander concerned that the resource vested in these parties by virtue of the permit they have from the Crown deserves to be managed without the significant inefficiency caused by the distraction of this dispute.

[527] There was general consensus among the expert economists that a GBA is, in all rational evaluations, inevitable. Professor Richardson agrees with that. Even on Todd's view of the dispute, flexibility of off-take has substantial value and after the very thorough airing all Todd's arguments have had, the prospects of securing any basis for disproportionate off-take without enforceable arrangements to redress the physical and/or financial consequences of doing so are surely negligible.

[528] This is a significant business relationship that needs a thorough breath of fresh air. That is possible in the context of renewed attempts to agree a GBA but seemingly impossible whilst the competing positions advanced in the litigation continue to be pursued.

Dobson J for the Court

Solicitors:

Russell McVeagh, Wellington for the plaintiff

Minter Ellison Rudd Watts, Wellington for the first defendant

Simpson Grierson, Wellington for the second defendant

Appendix 1

Glossary of Abbreviations and Terms

3 rd ASC	Third Amended Statement of Claim
AFEs	Authorisations for expenditure
AIPN	Association of International Petroleum Negotiators
CB	Common Bundle
CMA	Crown Minerals Act 1991
EPJV	Separate joint venture between Shell and OMV for ownership and operation of one set of export pipes from the PPS
FDP	Field Development Plan
FID	Final Investment Decision
GBA	Gas Balancing Agreement
GSA	Gas Sales Agreement
JV	Joint Venture
JVOA	Joint Venture Operating Agreement
M&M	McKee and Mangahewa fields
MDA	Maximum daily availability
MED	Ministry of Economic Development
MMCs	Maui Mining Companies
Overlifter	Joint venture party taking more gas than its proportionate share of production in any given period.
P85/P50 etc	A measure of reserves, referencing the probability of that outcome. A “P85” measure of reserves is one that has an 85 per cent chance of being exceeded, and P50 where there is a 50 per cent chance of that level being exceeded.
PJ	Petajoule - a unit of measurement of gas
PJ/a	Petajoules of gas per annum
PPS	Pohokura Production Station
ROFR	Right of First Refusal – category of sales contracts for Maui gas.
SLC	Substantial lessening of competition
SSNIP test	Small but significant non-transitory increase in price – see [352].
STOS	Shell Todd Oil Services Limited
Swing	Facility for buyer of gas to take fluctuating volumes of gas in different time periods.
T	Transcript
TJ	Tetajoule – unit of measurement of gas. 1,000 tetajoules = 1 PJ
the Act	Commerce Act 1986
the Commission	Commerce Commission
Underlifter	Joint venture party taking less gas than its proportionate share of production in any given period.
WP&B	Work Programme and Budget

Appendix 2

List of Witnesses

Todd Factual Witnesses

Richard Tweedie, Managing Director of Todd

Chris Hall, Todd In-House Counsel and director of numerous Todd Energy Group companies

Hamish Tweedie, Group Manager–Gas for the parent of the Todd plaintiff company, responsible for managing Todd’s upstream and wholesale gas sales as well as downstream sales by Nova Gas Limited and the Auckland Gas Company Ltd.

Winfred Boeren, Technical and Onshore Assets Manager for the plaintiff company’s parent with relevant responsibilities for M&M, also at Kapuni.

Paul Hunt (brief of evidence admitted by consent, no cross-examination), energy analyst at MED.

Todd expert witnesses

Kieran Murray, Economist, Wellington. Credentials described at [332] of the judgment.

Cento Veljanovski, Economist, London, UK. Credentials described at [333].

James Sweeney, Economist, California, USA. Credentials described at [336].

Rosalind Archer, Senior Lecturer, Department of Engineering Science, University of Auckland. Credentials described at [426].

Shell factual witnesses

Andrew Beaumont, Engineer, until February 2004 employed by STOS with responsibility for development of the Pohokura project.

Murray Jackson, Contract Support Manager for Shell’s upstream companies in New Zealand.

Ajit Bansal, Chairman of Shell in New Zealand, January 2004 to June 2007.

Robert MacDonald, Shell In-House Lawyer.

Shell expert witnesses

Jerry Hausman, Economist, Massachusetts, USA. Credentials described at [334].

OMV factual witnesses

George Goodsir, Commercial and Legal Manager at OMV in New Zealand, April 2004 to August 2009.

Michael Wright, Commercial Executive at OMV, July 2003 to May 2004.

John Burt, Commercial Executive at OMV, August 2004 to August 2006, and since January 2009.

OMV expert witnesses

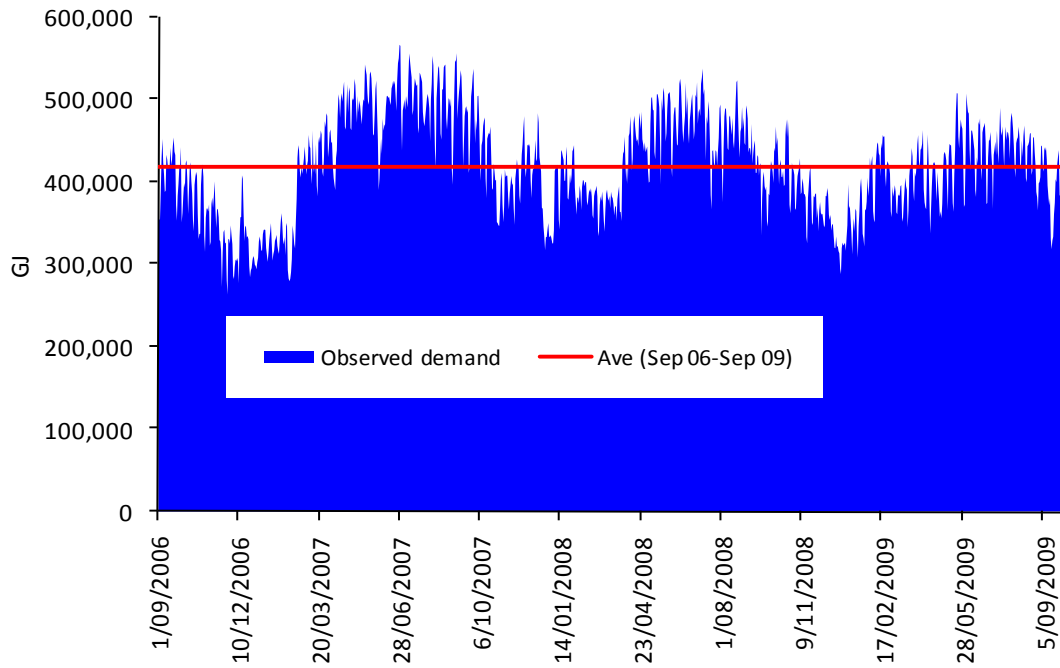
Gustavo Bamberger, Economist, Chicago, USA. Credentials described at [335].

Geoffrey Barker, Petroleum Engineer, Perth, Western Australia. Credentials described at [425].

David Hunt, Wellington based consultant on energy sector issues, former senior executive of Contact Energy.

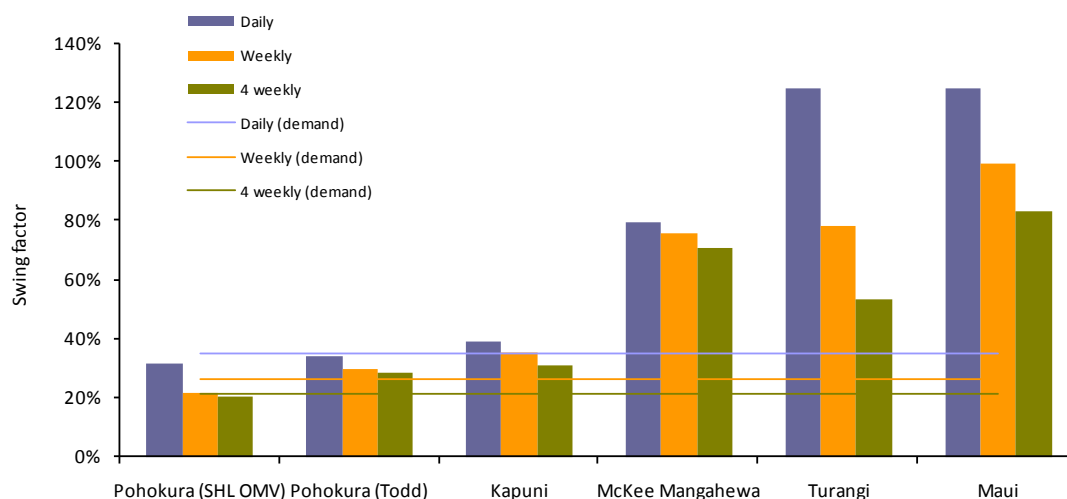
Appendix 3
(Extract from evidence of David Hunt, referred to at [82] above)

Figure 14 – Observed daily gas demand (GJ/day)



Appendix 4
(Extract from evidence of David Hunt, including footnotes,
referred to at [88] above)

Figure 19 – Swing ratios for major producing gas fields



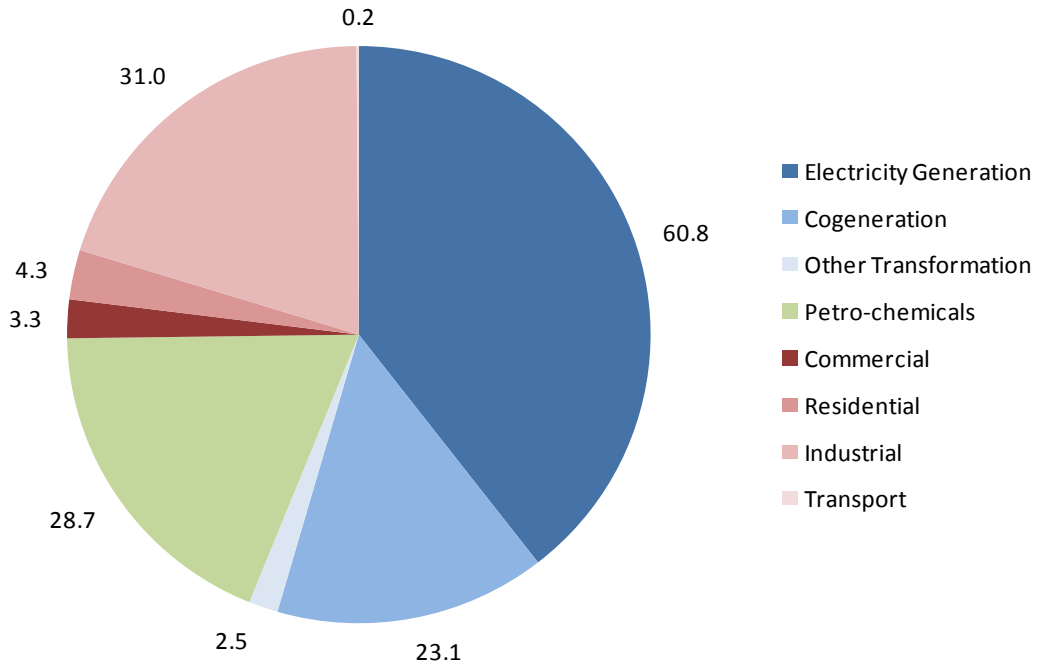
66. The key points regarding the observed swing ratios are:

- (a) Pohokura gas production attributable to Shell and OMV has the lowest swing ratio of all sources shown – ie the ‘flattest’ production profile. It is also the only gas source with lower swing ratios than overall gas demand (shown as lines).
- (b) Production from the Todd share of Pohokura and from the Kapuni field²⁵⁰ exhibits intermediate swing, approximating the swing in overall gas demand.
- (c) Gas production from the McKee Mangahewa,²⁵¹ Turangi²⁵² and Maui fields have much higher swing ratios than the other sources, with ratios well above the levels observed for overall gas demand.

²⁵⁰ As noted later, swing at Kapuni is understood to be entirely related to variations in production capability.
²⁵¹ The McKee Mangahewa figures are not directly comparable with other estimates due to gas reinjection activities at McKee. This issue is discussed later in my evidence.
²⁵² The observed ratio for the Turangi field should be treated with caution. There is evidence that gas flows occurred from the field to Methanex plant in 2008 that are not captured in the data used for this analysis. The inclusion of the additional data would be likely to reduce the swing ratio for Turangi (assuming the sales to Methanex have a relative flat profile).

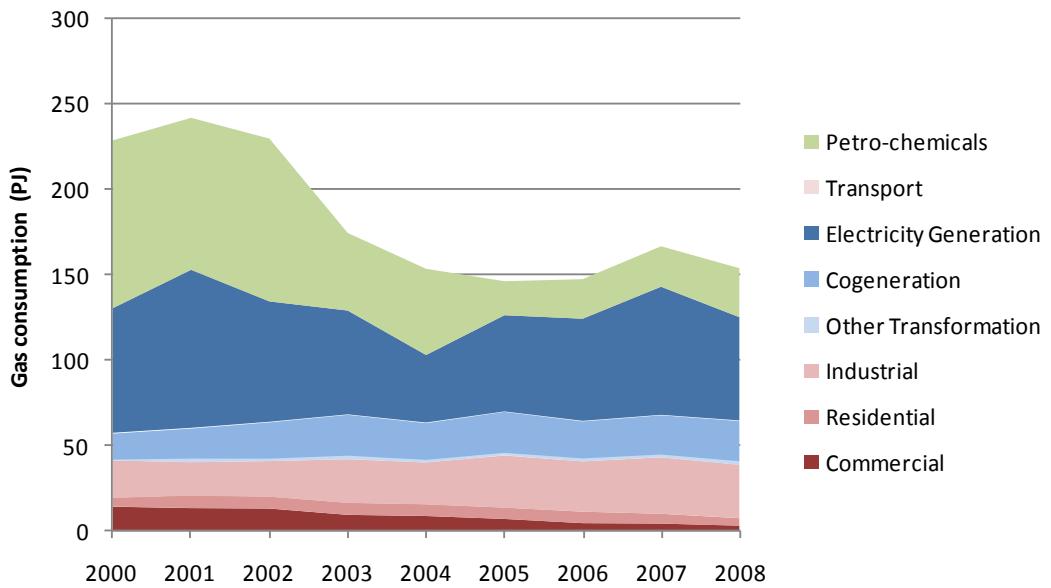
Appendix 5
(Extract from evidence of David Hunt, including footnotes,
referred to at [347] above)

Figure 1 - Gas consumption in 2008 (PJ)



Source: MED 'Energy Data File'. July 2009.

Figure 2 - Gas consumption over time



Source: MED 'Energy Data File'. July 2009.

15. Figure 1 and Figure 2 illustrate a number of important features of gas demand:
- (a) Overall gas demand fell steeply between 2001 and 2005, but has recovered somewhat since then.
 - (b) Gas usage within the electricity generation and cogeneration sectors has been a significant component of overall demand and has accounted for over 50% of demand in recent years. It has fluctuated through time, in part due to changing hydrology conditions and partly due to increasing use of coal at the Huntly power station instead of gas.
 - (c) The 'direct use' category has grown slowly through time, and is dominated by industrial customer usage.²⁵³
 - (d) Gas usage as a chemical feedstock has fluctuated through time. In 2000, it accounted for approximately 43% of total demand, but since then has declined sharply. In 2008, for example, this usage accounted for approximately 19% of all gas consumed in New Zealand.
16. The steep fall in gas demand over the 2001-2005 period occurred mainly because of declining usage by two parties... (Huntly Power Station and Methanex).

²⁵³ Note that some of the fall in commercial sector consumption over time may be attributed to classification changes in the MED data and/or returns not being filled out on a consistent basis over time. In particular, some of this consumption may have been attributed to the industrial sector in later years.