

Offshore Energy Law

Running out of places to go?

European waters look increasingly choppy for destination clauses

The Commission is once again putting the review of destination clauses in LNG import arrangements firmly on its antitrust agenda. On 21 June 2018, it announced that it would be investigating Qatar Petroleum companies' contractual arrangements for the import of LNG into the EU, in order to assess whether or not these arrangements anti-competitively hinder the free flow of gas within the European Economic Area.

The action follows on from the Commission's successful negotiation of commitments from Gazprom to modulate its gas contract supply terms, prices and conduct in Europe, in exchange for closing its investigation into Gazprom's gas contracts, and appears to have been initiated of its own accord rather than in response to a customer or competitor complaint. Although the Commission is focusing its current investigation specifically on Qatar Petroleum, the case is likely to serve as a precedent for other LNG suppliers.

The Commission has stated that it will be looking particularly at whether Qatar Petroleum's long-term import agreements (typically 20-25 years in length) contain direct and/or indirect territorial restrictions. It has highlighted certain clauses for review, namely those which (i) prevent any diversion of cargoes to another destination, (ii) restrict the territories to which diversion can take place, and/or (iii) restrict the volumes that can be diverted. In other words: "destination clauses".

As noted above, the Commission has previously indicated that destination clauses are not permissible in long-term FOB contracts where the receiving terminal is in the EU, but they are generally permissible in long-term delivery "ex-ship" DES contracts. The rationale for this is that in FOB contracts the delivery point under the contract is the loading terminal, with the buyer being liable for the transportation of the LNG cargo

from the loading terminal to the unloading port. Therefore, imposing a destination restriction prevents buyers from freely reselling LNG (including exploiting arbitrage opportunities), even though they will already have taken title and risk for the LNG before this point.

In DES contracts meanwhile, the delivery point is the buyer's unloading terminal and the seller is liable for the LNG up to this point.

The Commission's current investigation appears to stem from recent EU activity in the area, including the publication in 2017 by the Commission's Energy department of a study into LNG and storage strategy which criticised the impact of destination clauses in creating barriers to liquidity and competitiveness in the gas sector. Furthermore, in June 2017 the EU signed a memorandum of cooperation with Japan which advocated removing destination clauses from LNG contracts.

The Commission has not given a timeframe for its current investigation into Qatar Petroleum, and notes that opening an investigation does not prejudice its outcome. For its part, Qatar Petroleum has confirmed that the investigation will focus on it and five of its LNG subsidiaries.

The Commission has also not yet indicated whether its investigation will focus on abuse of a dominant market position, the establishment of anti-competitive agreements/practices, or a combination of both, as its theory of harm. Currently, Qatar Petroleum and its subsidiaries account for around 40% of the EU's overall LNG imports and have significantly higher import shares in certain member states.



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