

***Case No COMP/M.2745 -
SHELL / ENTERPRISE
OIL***

Only the English text is available and authentic.

**REGULATION (EEC) No 4064/89
MERGER PROCEDURE**

Article 6(1)(b) NON-OPPOSITION
Date: 07/05/2002

*Also available in the CELEX database
Document No 302M2745*



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 07/05/2002

SG (2002) D/229711/229712

In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EEC) No 4064/89 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

PUBLIC VERSION

MERGER PROCEDURE
ARTICLE 6(1)(b) DECISION

To the notifying parties

Dear Sir/Madam,

**Subject: Case No COMP/M.2745 – SHELL / ENTERPRISE OIL
Notification of 04.04.02 pursuant to Article 4 of Council Regulation
No 4064/89¹**

1. On the 04.04.2002, the Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EEC) No. 4064/89, whereby the undertaking Shell Resources Plc., belonging to the Royal Dutch/Shell Group (“Shell”) acquires control of the whole of Enterprise Oil Plc. (“Enterprise”).
2. After examining the notification, the Commission has concluded that the notified operation falls within the scope of Council Regulation No. 4064/89 and that it does not raise serious doubts as to its compatibility with the common market and with the EEA agreement.

I. THE PARTIES

3. Shell is active in the world-wide exploration, production and sale of oil and natural gas, production and sale of chemicals, power generation and production of energy from renewable resources.
4. Enterprise is active in crude oil and natural gas exploration and production, mainly in the North Sea, Italy, the US Gulf of Mexico, Mexico and Russia. The company was formed as a result of the privatisation of British Gas in the 1980ies.

¹ OJ L 395, 30.12.1989 p. 1; corrigendum OJ L 257 of 21.9.1990, p. 13; Regulation as last amended by Regulation (EC) No 1310/97 (OJ L 180, 9. 7. 1997, p. 1, corrigendum OJ L 40, 13.2.1998, p. 17).

II. THE OPERATION

5. The subject concentration arises as a result of a public bid by Shell for all of the issued and outstanding shares in the capital of Enterprise, which was launched on 2nd April 2002.

III. CONCENTRATION

6. As a result of the operation, Shell will acquire control of the whole of Enterprise. The operation thus constitutes a concentration within the meaning of Article 3(1)(b) of the Council Regulation.

IV. COMMUNITY DIMENSION

7. The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5 billion² (Shell: 161 400 million €; Enterprise 2 235 million €). Each of the undertakings has a Community-wide turnover in excess of EUR 250 million (Shell: [...]; Enterprise [...]), but they do not achieve more than two-thirds of their aggregate Community-wide turnover within one and the same Member State. The notified operation therefore has a Community dimension.
8. [...]

VI. COMPETITIVE ASSESSMENT

A) THE RELEVANT MARKETS

9. The proposed concentration only concerns the upstream sector, i.e. the exploration for reserves, reserve development and production, transportation and processing. In line with the Commission's previous decisions in the sector³, the parties have identified the following relevant product and geographic markets where the transaction will give rise to overlaps:
 - (1) Exploration for crude oil and gas (geographic scope: world-wide)
 - (2) Development and production of crude oil (world-wide)
 - (3) Development and production of natural gas (In previous decisions⁴ the geographic markets considered comprised the EEA and possibly Russia and Algeria, however, the final market definition was left open)
 - (4) Crude oil infrastructure, i.e. pipeline transportation and processing (UK North Sea)
 - (5) Gas transportation by pipeline (UK North Sea and Norway respectively)
 - (6) Gas processing (UK North Sea)

² Turnover calculated in accordance with Article 5(1) of the Merger Regulation and the Commission Notice on the calculation of turnover (OJ C66, 2.3.1998, p25). To the extent that figures include turnover for the period before 1.1.1999, they are calculated on the basis of average ECU exchange rates and translated into EUR on a one-for-one basis.

³ E.g., BP Amoco/ Arco (M.1532), Norsk Hydro / Saga (M.1573), and most recently Conoco/Philipps (M.2681).

⁴ COMP/M.1383 – Exxon /Mobil of 29.9.1999.

The transaction leads to affected markets only as regards gas infrastructure in the UK North Sea and crude oil infrastructure in the North Sea.

1. Product markets

Gas infrastructure

10. When natural gas emerges in a steam from the well-head of a production facility at a field off-shore in the UK North Sea, the steam contains gaseous hydrocarbons and hydrocarbons liquids. This unprocessed gas requires transportation by sub-sea pipeline to the UK shore, where the gaseous steam is then subject to further processing/purification at an on-shore terminal. Only after this processing, the gas can then be introduced into the national UK gas distribution system for transportation to the end-consumers. In some cases, a pre-processing is conducted at off-shore facilities to provide a first purification, and to achieve for the necessary pressure and temperature for the transport via pipeline to the shore.
11. Although a pipeline is connected to only one on-shore processing terminal, so that the choice of a specific pipeline tends to pre-determine the choice of the terminal, the Commission has in previous cases divided transport and processing of natural gas into separate product markets, and the approach appears to be still valid in the light of the market investigation in the present case. Competitive conditions with regard to pipelines and processing terminals differ, since the shareholders in the pipeline and the terminal do not correspond. It has been confirmed by third parties that the decision of a field owner for a specific evacuation option is determined by an assessment of the different elements of the chain of transportation and their combination, and that competition takes place between the terminals to make a specific pipeline/terminal combination attractive. Furthermore, it appears that it is technically possible to construct extension pipelines on-shore that would allow for a pipeline to connect to another terminal located in proximity. Thus, for the purpose of this decision, the Commission considers pipeline transport and processing as distinct product markets.

Crude oil infrastructure

12. Due to a close similarity in the relevant considerations, like for gas infrastructure the transportation of crude oil by pipeline and crude oil on-shore processing have to be considered as distinct product markets⁵.

2. Geographic markets

Gas infrastructure

13. In geographic terms, the parties follow the Commission's approach in previous cases to divide the UK North Sea into two separate markets, i.e. Northern North Sea ("NNS"), which refers to the area of the North Sea lying to the north of latitude 55°, and Southern North Sea ("SNS"). This approach has been confirmed by the Commission's investigation in the present case. Third parties agreed that the pipelines in each of these areas are broadly interchangeable. Although each pipeline has its individual technical specifications and specific requirements as regards the quality of the transportable gas,

⁵ Norsk Hydro / Saga (M.1573)

it appears that these differences do not hinder substitutability, as only modest investment is necessary to adjust the gas quality to the individual pipeline requirements, and the vast majority of pipelines transport gas which does not need significant off-shore processing. The same applies to processing facilities in the mentioned areas, which in addition are partly linked with each other via pipelines.

14. There are therefore no indications that the geographic market has to be defined more narrowly. Some third parties indicated that the geographic market might consist of the UK North Sea as a whole and possibly includes the Norwegian continental shelf, as at least for large field discoveries, evacuation options over this whole area would be considered by the field owners. However, for the purpose of this decision it can be left open whether the market might be larger since no competition concerns would arise under any of the alternative definitions of the geographic market.

Crude oil infrastructure

15. The parties consider the relevant geographic markets for crude oil infrastructure to be NNS and SNS, following the principles applied for gas infrastructure. Due to a close similarity in the relevant considerations, this appears to be reasonable, and it has also been confirmed in the market investigation. However, it can be left open whether a wider market should be applied, as the only activities of the parties with regard to crude oil infrastructure are located in the NNS, and even on the basis of a NNS market no competition problems are arise. The market investigation did not reveal any indications that a more narrow definition should be applied.

B) ASSESSMENT

16. As indicated above, the transaction only leads to affected markets through horizontal overlaps as regards gas pipeline transportation, gas processing and crude oil transportation and processing in the UK North Sea area. There are no vertically affected markets.

1. Gas transportation (pipelines)

17. Due to the high investment requirements, gas transportation infrastructure is operated through joint ventures, which mainly consist of the owners of the gas fields which were located in proximity to the pipeline at the time of the construction of the pipeline. These pipelines are either operated as “undivided rights” or as “divided rights” pipelines. Operating agreements for pipelines with *undivided rights*, which account for the majority of cases, generally allow the owners to veto decisions relating to the use of any spare capacity, irrespective of the owner’s equity interest in the pipeline. Operating agreements for pipelines with *divided rights*, on the other hand, only allow the owner to control the use of capacity to an extent that corresponds to his equity interest in the pipeline. In previous cases, the Commission analysed the transportation markets in terms of pipeline throughput, total capacity and, in particular, spare capacity.

NNS pipelines

18. The parties have shareholdings in five gas pipelines (SEAL, SAGE-Beryl, FLAGS, Fulmar and Miller) out of the ten pipelines in the NNS (the others being CATS, SAGE-Brae, Frigg UK, Frigg Norway/Vesterled and Britannia).
19. As regards throughput volumes, according to the parties their share would be [10-20%] in the NNS, calculated on the basis of field equity multiplied by field production for the fields feeding into the appropriate pipelines. The increment in market share resulting from the transaction amounts to only [<5%]. In those terms, the new entity would be third largest player in the market behind BP ([10-20%]) and Exxon ([10-20%]). As regards total pipeline capacity in the NNS, the parties account for [35-45%]. This calculation does not take into account individual equities, but is based on the assumption that the parties have a veto right in each of the pipelines where they have a shareholding and thus can control the full capacity of such pipeline.
20. The main competition concern, however, relates to the possibility for third parties to be foreclosed in access to pipeline capacity, which would exclude them from developing new competing gas fields. Therefore, based on the Commission's approach in previous cases, the parties also provided shares in terms of pipeline spare capacity which could be vetoed by the parties according to the pipeline joint venture agreements described above. Thus, the parties would account for [50-60%] of the pipeline spare capacity in the NNS (Shell [0-10%], Enterprise [40-50%]). These figures have been broadly confirmed by the Commission's market investigation. It has only revealed one aspect which might require an adjustment of the parties' figures. Due to technical reasons related to the infrastructure of the Frigg field, it appears that today the Frigg Norway pipeline cannot be run at its full nameplate capacity. However, this issue has only minor effects on the competitive situation. Taking into account these constraints, the parties' share of the available spare capacity would increase by only c. 2 percentage points. In addition, these constraints are expected to lapse in the very near future, when the Frigg field will cease its production due to depletion.
21. It appears that no competition concerns arise from the parties' position. Over a period of 10 years, the parties' share will have decreased to [40-50%]. The amount of spare capacity not controlled by the parties largely exceeds projected demand from newly developed fields over the coming 10 years. For example, according to the parties' estimates which have been confirmed in the investigation, in 2005 projected demand amounts to [...] million cubic meters per year (mcm/yr), compared to [...] mcm/yr of spare capacity not controlled by the parties. Between 2005 and 2012, the available independent spare capacity will be 2.1 to 4.4 times higher than projected demand.
22. Furthermore, third parties confirmed that in the NNS it is still likely that fields of a size and specification are discovered that would make the construction of a completely new pipeline economically viable, so that access to the existing pipelines is not essential, and the provision of additional pipeline capacity can be expected. For example, a new pipeline will be built for the evacuation of the Goldeneye field, and the same is considered probable for the Atlantic/Cromarty fields. The owners of the Ormen Lange field in Norway apparently are currently considering several evacuation options, one of them being the construction of a new pipeline to the UK shore.
23. Finally, it has to be taken into account that several pipelines, such as Miller and Frigg Norway, today have a very low capacity utilisation, which increases the interest of the pipeline owners to attract transportation business through competitive offers in order to

cover their fixed costs. Several third parties confirmed a general trend of decreasing transport tariffs in the area and expect this to continue over the coming years.

24. There are indications that a certain amount of the Frigg Norway pipeline, which accounts for a significant proportion of the independent spare capacity, might be occupied by imports of Norwegian gas to the UK. The pipeline has just recently been connected to Norwegian fields (Heimdal) under the Vesterled project. However, the amount and probability of these imports, as well as their evacuation routes, remain highly uncertain. Today, the pipeline is used at very low capacity utilisation and there are no contracts on future utilisation over the next 10 years in place. According to market participants, the possible imports from Norway will largely depend on future demand in the UK, price developments, and production evolution in both the UK and Norwegian continental shelf, which are difficult to predict in exact terms.
25. In addition, there are other possible evacuation routes for Norwegian gas to the UK shore today, and there is also a certain probability that new field developments such as the large Ormen Lange field will result in additional pipeline connections for Norwegian fields to the UK shore, providing another alternative transportation facility for these imports. Furthermore, Marathon, one of the parties' competitors, has announced an initiative to lead the development of a pipeline project to link the Norwegian Heimdal area with the UK, with the pipeline terminating at the Bacton terminal area, which would provide capacity for Norwegian imports, and would leave the Frigg Norway capacity available. Finally, based on estimates of the parties which, subject to the precautions mentioned above, have been considered as reasonable by third parties, the remaining spare capacity not controlled by the parties would still largely exceed the projected demand. Independent spare capacity would even be enough to cover future demand if one would entirely exclude the Frigg Norway pipeline from the available amount of free spare capacity.
26. In the light of the above, it can be concluded that the transaction will not lead to the creation or strengthening of a dominant position on the market for NNS gas pipeline transportation.

SNS pipelines

27. In the SNS, the parties have shareholdings in five pipelines (West Leman, East Leman, Inde, SPOTS-Sole Pit, Sean) out of the 16 gas pipelines in the SNS (the others being Hewitt, EAGLES, Cleeton, West Sole, Amethyst, LOGGS, Pickerill, Viking, CMS, LAPS and Thames).
28. In terms of throughput, the parties will account for [10-20%], with only a minor increment of [<5%] resulting from the transaction. The most important competitors are ExxonMobil ([20-30%]) and BP ([20-30%]). The parties have shareholdings in pipelines representing [20-30%] of total pipeline capacity in the SNS. As regards spare capacity, the parties will account for [20-30%] (Shell [10-20%], Enterprise [0-10%]) in 2002, and this figure will remain stable over the coming ten years. Thus there is ample spare capacity available which is not influenced by the parties. In addition, the SNS appears to be a mature area, with a low and further decreasing production and overall capacity utilisation. Demand projections provided by the parties, and confirmed by third parties in the investigation, show a 2005 demand of [...] mcm/yr meeting [...] mcm/yr of spare capacity not controlled by the parties. Independent spare capacity will exceed projected demand by 7 to 25 times throughout the years 2005 to 2012.

29. Against this background, it can be excluded that the transaction will lead to the creation or strengthening of a dominant position on the market for gas pipeline transportation in the SNS.

2. Gas processing (terminals)

Processing facilities NNS

30. The processing facilities in the NNS consist of the four terminals in St. Fergus and the two terminals in Teeside. Out of the 4 terminals in St. Fergus the parties will have interest in three of these. Shell is the operator of the St. Fergus (Shell) terminal and has a 50% interest in it. Enterprise has a 7.5% interest in the St. Fergus (Miller) terminal operated by Totalfinaelf and an 11.4% interest in the St. Fergus terminal operated by Exxon Mobil. The parties do not have any interest in three terminals, which are the two Teeside terminals and the St. Fergus (Frigg) terminal operated by Totalfinaelf.
31. Based on throughput the parties will be the third largest processor with [10-20%]. The largest processor is BP with a [10-20%] followed by Exxon Mobil with [10-20%].
32. Like pipelines, processing terminals are mainly operated as joint ventures, organised under a Terminal Operating Agreement. Ownership of an interest in a terminal gives a right to a proportion of terminal capacity corresponding to the owner's equity interest. Furthermore, the agreement often gives the owners veto rights over commercial decisions. It includes the veto over decisions concerning further development of the terminal facilities for newly constructed offshore pipelines infrastructure and third party access to the terminal.
33. As explained for pipelines, the main competition concern arising from an interest in such infrastructure is the possibility for the infrastructure owners to constrain the development of new, competing gas fields. The position of an individual company will depend not so much on its capacity share which corresponds to its equity, but rather on the total capacity, and especially spare capacity, of the infrastructure in which it has an interest.
34. The spare capacity in 2002 where the parties have an interest accounts for [20-30%] of the total NNS processing spare capacity, leaving [70-80%] free of any veto rights from the parties. This share of the spare capacity remains stable over the period 2002–2012 accounting for [30-40%] in 2012. In the same period the demand for processing capacity is expected to be [...] mcm/yr in 2005 rising to [...] mcm/yr in 2012. The estimated future demand from new discoveries is considerably smaller than the available spare capacity without any equity interest of the parties which is [...] mcm/yr in 2002 and [...] mcm/yr in 2012 [several times higher than demand]. The estimated future demand for processing was confirmed by third parties during the market investigation. Some third parties argue that the spare capacity allocated to the St. Fergus Frigg terminal connected to the Frigg Norway pipeline is overestimated, in case the Frigg Norway pipeline is used for gas imports from Norway. The issue of a potential use of the Frigg Norway pipeline by Norwegian imports has been dealt with already in the section on pipelines above. The same considerations apply with regard to the connected processing facility. Moreover, available independent spare capacity for processing would still exceed projected demand, even assuming that the entire capacity of the Frigg terminal was utilised.

35. Based on the above, the Commission considers that the transaction does not create or strengthen a dominant position on the market for processing of natural gas in the NNS.

Processing facilities SNS

36. When looking at the SNS area, it must be mentioned that it is not expected that new large fields will be discovered in the SNS. The area is characterised by an overall capacity under-utilisation on both pipelines and processing facilities. Future discoveries are only likely to be satellite fields of previously developed larger fields only requiring limited spare capacity.
37. Overall, processing in the SNS can take place in the four Bacton terminals, the two Easington terminals and in Theddlethorpe. Shell is the operator and has an interest in two of the Bacton terminals, with a 50% interest in the Bacton Shell terminal and a 12.4% interest in the Bacton terminal connected to the SEAL pipeline. Enterprise has a 14.8% interest in the Bacton BP terminal operated by BP.
38. Based on throughput in 2001 the parties will account for [10-20%] of the SNS natural gas processing throughput. ExxonMobil is the largest processor with a [20-30%] share of throughput followed by BPA with [20-30%]. If the parties were to use their veto rights in the processing facilities where they have an equity interest, this would in 2002 amount to [50-60%] or [...] mcm/yr of the total available spare capacity of [...] mcm/yr.
39. In the period 2002-2012 the spare capacity controlled by the parties will decrease from [50-60%] in 2002 to [40-50%] in 2012. In addition, the demand for future capacity was estimated by the parties and verified by the market investigation. The future demand is expected to be [...] mcm/yr in 2005 and gradually rising to an estimated [...] mcm/yr in 2012. In the same period the estimated spare capacity without any Shell/Enterprise veto rights is estimated to be [...] mcm/yr in 2005 and [...] mcm/yr in 2012 [several times higher than demand]. Thus, independent spare capacity largely exceeds projected demand.
40. It can therefore be concluded that the transaction will not create or strengthen a dominant position on the market for processing of natural gas in the SNS.

3. Crude oil infrastructure

Crude oil pipelines

41. Out of the six oil pipelines in the NNS (Beatrice, Forties, Flotta, Norpipe, Brent and Ninian) the parties have equity interests in two pipelines, Brent and Ninian. Pre-merger, Shell holds an equity interest in Brent of 33.257%; Enterprise Oil has an equity interest of 2.209% in Brent and 0.375% in Ninian respectively. The Brent system is run on an undivided rights basis giving each party the right to block third party access. Ninian is run on an divided rights basis, which means that either party may exercise a veto right only over the use of spare capacity to the extent of its equity interest in the pipeline.
42. The information provided by the parties shows that the combined entity's throughput through the Brent and Ninian pipelines is approximately [...] barrels/day which represents approximately 5% of UK North Sea crude oil production. Compared to

Shell's pre-merger throughput of [...] barrels per day the increment resulting from the transaction would be minimal.

43. The Commission's main competition concern, however, lies in the possible foreclosure of third parties to spare capacity in the pipeline infrastructure due to pipeline owners exercising their veto rights.
44. There will not be an addition of veto rights compared to the pre-merger situation, as Shell already has an interest in the Brent pipeline, and Enterprise's shareholding in the Ninian pipeline does not confer a veto right. Based on information provided by the parties, which was confirmed by the results of the market investigation, the combined entity would be able to control [30-40%] of the spare capacity in 2002 decreasing to [20-30%] over the period up to 2012. The increment resulting from the merger is negligible, consisting in the control of an additional [<1%] of spare capacity (2002) as a result of the increase of equity in the Ninian pipeline by 0.375%. The figures presented by the parties, show that in 2005 the total capacity required will be [...] kilobarrels per day (kb/d), whereas the independent spare capacity available (without a blocking vote by the combined entity) will be [...] kb/d. For 2012, these figures will be [...] kb/d (demand) and [...] kb/d (independent spare capacity) respectively. Total spare capacity of the NNS oil pipelines is thus several times greater than forecast demand; the spare capacity/demand ratio varying from 22.2 to 8.9 in the period from 2005 to 2012. Market investigation has shown that, in general, these are considered to be reasonable estimates. Moreover, although not being a full substitute in all circumstances, evacuation of crude oil from a field by tanker has been considered by third parties as an alternative means of transport, which can be taken into account as a factor which additionally constraints the position of the parties.
45. On the basis of the above, it can be concluded that the transaction will not lead to the creation or strengthening of a dominant position in the market for crude oil pipeline transportation in the UK North Sea.

Crude oil processing

46. The parties have interests only in the processing terminal Sullom Voe, other NNS oil processing terminals are Flotta, Cruden Bay, Nigg and Teesside. Shell's equity interest is 19.8%, whereas Enterprise Oil holds a 1.6% stake in the terminal. Under the Sullom Voe Terminal Operating Agreement [description of the voting arrangements under the Sullom Voe Terminal Operating Agreement]. The transaction therefore has no effect on the parties' influence in the terminal's policy. [Description of the voting arrangements under the Sullom Voe Terminal Operating Agreement]. In addition, market information provided by the parties and confirmed by third parties has shown that there is ample independent spare capacity available, which largely exceeds forecast demand. It can therefore be concluded that the concentration would not create or strengthen a dominant position in the market for crude oil processing in the UK North Sea.
47. [...]

VII. CONCLUSION

48. For the above reasons, the Commission has decided not to oppose the notified operation and to declare it compatible with the common market and with the EEA Agreement. This decision is adopted in application of Article 6(1)(b) of Council Regulation (EEC) No 4064/89.

For the Commission

Signed by Mario MONTI
Member of the Commission