Third Party Access to China’s Gas Market

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Overview

- First cargo of LNG delivered from Australia’s Northwest Shelf to China’s first LNG receiving terminal in Dapeng in 2006
- Chinese LNG market dominated by its national oil companies
- 18 LNG land-based regasification terminals in operation in China; only three are owned and operated by private companies.
- TPA Measures in China first issued by NDRC / NEA in 2014
  - CNPC, CNOOC and Sinopec adopted TPA programs in 2016
  - Measures expired in February 2019
  - 2018 Draft Measures pending adoption to replace 2014 Measures
Concept of TPA

• “Idea that in certain circumstances economically independent undertakings … should have a legally enforceable right to access and use various energy network facilities owned by other companies.”
• TPA can be either regulated or voluntary (or combination)
• Terms and conditions of TPA generally set by way of tariff published by operator
• Commercially, TPA occurs generally through terminal use or service agreements (TUA, TSA).
Designing a Successful TPA

• Key characteristics
  – Existence and calculability of spare capacity
  – Non-discriminatory access
  – Transparency of terms
  – Anti-hoarding by users
  – Promotion of competition
  – Security of supply
  – Adequacy of storage and pipeline networks

• China caution: Must ensure that dilution of incumbents’ rights does not erode the core services that support a growing economy
TPA Around the World

- Percent of regas capacity offering TPA via regulation or negotiation
  - Global average: 54%
  - EU: 92%
  - Asia: 51%
  - US: 46%

- EU had first TPA regulation (1998), and today has most comprehensive regime via Third Gas Directive and Regulation 715/2009/EC

- In Asia, TPA via regulation in Japan, Malaysia, Thailand and Singapore.
  - India on case-by-case basis
  - No TPA in Korea (3rd largest market in world)
China’s Energy Picture

• Growing demand, coupled with shrinking supply
• Gas consumption grew by 16% in 2018, production increased 7.5%
• Gas comprises 7.5% of energy mix; Government targets 10% in 2020 and 15% in 2030
• Gas imports to grow from 70 bcm in 2015 to 280 bcm in 2040
  – Will make China second largest importer globally after EU
  – 80% of growth will come from LNG
Dominance of the NOCs – the Incumbents

• NOCs supplied 95% of gas used in China in 2018
• NOCs also dominate the infrastructure that handles gas
  – CNPC owns 91% of trunk lines that supply gas; Sinopec owns the rest
• NOCs dominate LNG receiving and regasification terminals
  – CNOOC -- 8
  – CNPC -- 4
  – Sinopec – 3
• Utilization rates improving – below 70% in 2017; averages 85+% in 2018
National Energy Administration Measures on TPA

- NEA published first *Measures for the Supervision and Administration of Fair Opening of Oil and Gas Pipelines Network Facilities (for Trial Implementation)* on February 13, 2014
- Targeted spare capacity in transportation, storage, gasification, liquefaction, compression and other services
- “Fair and non-discriminatory manner” on first-come, first-served basis
- Detailed application process, timeframe for approval, dispute resolution
- Required contract, and identified key areas for inclusion
- Broad oversight to enforce by NEA
2016 NDRC Notice on Information Disclosure

• NEA issued *Notice on Completing Information Disclosure Related to the Opening of Oil and Gas Pipeline Network Facilities* in September 2016

• Required disclosure by CNPC, Sinopec and CNOOC
  • Details of the project -- location, configuration, length, design capacity, etc.
  • Quality / safety standards of facilities, gas quality, pressure, and measurement
  • Pricing for services
  • Conditions for access to the network facilities
  • Method, process and specific processing time limit for access
  • Spare capacity announced by December 5 for ensuing year

• Must post by October 15, 2016, and guarantee accuracy of information disclosed
NOC Response to NDRC Measures

- NOCs each published with TPA programs on their websites
- Varying degrees of comprehensiveness and compliance with 2016 Notice on Information Disclosure.
- Application requirements
- Conditions that must be in place before TPA is offered
- Process and internal deadline for consideration of application
- CNOOC posted most comprehensive (and restrictive) program
CNOOC TPA Requirements

• Published basic information about its facilities, access standards, measurement requirements for access to pipeline facilities, date of operation, location, berthing capacity, LNG processing capacity, pipeline capacity and pricing basis

• Also published circumstances under which TPA would be offered, e.g.:
  – Terminal company / pipeline facilities have spare processing capacity
  – Performance of long-term agreements can be guaranteed
  – Performance of existing users’ LNG supply and sale plan will not be affected
  – Use in target market will not impact existing users
  – User has secured upstream international LNG resources, and licenses
  – User meets CNOOC’s requirements regarding creditworthiness
  – User possesses substantial experience in the natural gas industry.
Examples of NOC TPA

- **CNPC** – opened Jiangsu, Tangshan, and Dalian LNG terminals to ENN, Beijing Gas, Nanjing Pacific, Shanghai Natural Gas Pipeline for loading and unloading, storage, regasification and/or transportation of imported LNG.

- **Sinopec** – natural gas transportation service to PetroChina Kunlun Gas Co., Ltd. and China Gas Holdings Ltd.

- **CNOOC** – announced in July 2018 that it would open all of its LNG regas terminals to TPA, but limited information on specific users.
PRC Government *Opinions* on TPA

- **CPC Central Committee and State Council** – *Opinions on Deepening the Reform of the Oil & Natural Gas System* (May 2017)
  - Need to “realize that the main oil and gas pipelines, provincial and inter-provincial pipelines are open to third party market entities”
- **NDRC / NEA** -- *Opinions on Accelerating Natural Gas Utilization* (June 2017)
  - Encouraged “all types of capital to enter the field of natural gas infrastructure construction and utilization”
- **NDRC / NEA** -- *Opinions on Accelerating the Construction of Gas Storage Facilities and Improving the Market Mechanism of Gas Storage and Peaking Auxiliary Services* (April 2018)
  - Recognized the importance of storage in the liberalization of natural gas system
2018 Draft Measures on TPA

• *Measures for the Supervision and Administration of Fair Opening of Oil and Gas Pipeline Network Facilities* (August 3, 2018)
• Published for comment ahead of expiration of 2014 Measures
• NDRC / NEA still reviewing measures and taking stock of NOC comments
• One area of reported concern is “grandfathering” existing rights (or applying TPA only to spare capacity) when terminal utilization is nearing 100%
• Generally, 2018 Draft Measures are seen to be an improvement over the 2014 Measures in a number of areas
2018 Draft Measures on TPA (cont.)

- Focus on operators and placement of responsibility to adopt and implement TPA
- Encouragement and support for capital investment in facilities by private parties
- Requirement that national and local development plans include consideration of TPA
- Requirement that “spare capacity” be calculated to assure full facility utilization
- Imposition of strict standards on operators to enter into service contracts with qualified users without unreasonable delay or the of unreasonable conditions
- Requirement to adhere to PRC Government pricing standards
- Encouragement to operators to provide both interruptible and non-interruptible services on a monthly, quarterly or annual basis according to market demand
2018 Draft Measures on TPA (cont.)

- Expansion of information disclosure and requirement to timely update
- Requirement to announce spare capacity on a per-monthly basis
- Shorter time allowed to respond to applications for access
- Imposition of stricter standards of compliance – both for operators and users
- Imposition of onus on operators to demonstrate basis for rejection of applications
- Elevation of right to interpret the 2018 Draft Measures to NDRC
- Expansion of NEA oversight and authority to enforce 2018 Draft Measures against operators and users, including imposition of penalties
- Adoption of dispute resolution through civil litigation or arbitration
Assessment of 2018 Draft Measures

- Reflects continuing commitment to TPA by NDRC / NEA
- Encouraged by *Opinions* of CPC Central Committee and State Council
- Delay in promulgation concerning, but the TPA “cow is out of the barn”
- NOCs did not pull back TPA programs when 2014 Measures expired
- Draft Measures expand and deepen the programs required of the NOCs and strengthen enforcement powers of NEA
- Issuance expected shortly; no reason to believe they will be scuttled