



## ***Public Competition Assessment***

7 March 2007

### ***Santos Limited - proposed acquisition of Queensland Gas Company Limited***

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#### **Introduction**

1. On 20 February 2007, the Australian Competition and Consumer Commission ('ACCC') announced its decision to oppose the proposed acquisition of Queensland Gas Company Limited ('QGC') by Santos Limited ('Santos') ('proposed acquisition'). The ACCC was of the view that the proposed acquisition, in conjunction with the proposed undertakings, would be likely to have the effect of substantially lessening competition in the market for production and supply of wholesale gas in the southern interconnected region of Queensland (including Brisbane, Gladstone and Mt Isa) and in the market for production and supply of wholesale gas in the southern states of Australia in contravention of section 50 of the *Trade Practices Act 1974* ('the Act').
2. The ACCC formed its view on the basis of the information provided by the merger parties and information arising from its market inquiries. This Public Competition Assessment outlines the basis on which the ACCC has reached its decision on the proposed acquisition, subject to confidentiality considerations.

#### **Public Competition Assessment**

3. To provide an enhanced level of transparency and procedural fairness in its decision making process, the ACCC issues a Public Competition Assessment for all transaction proposals where:
  - a merger is rejected;
  - a merger is subject to enforceable undertakings;
  - the merger parties seek such disclosure; or
  - a merger is approved but raises important issues that the ACCC considers should be made public.
4. This Public Competition Assessment has been issued because the ACCC decided to oppose Santos' proposed acquisition of QGC.

5. By issuing Public Competition Assessments, the ACCC aims to provide the market with a better understanding of the ACCC's analysis of various markets and the associated merger and competition issues. It also alerts the market to the circumstances where the ACCC's assessment of the competition conditions in particular markets is changing, or likely to change, because of developments.
6. Each Public Competition Assessment is specific to the particular transaction under review by the ACCC. While some transaction proposals may involve the same or related markets, it should not be assumed that the analysis and decision outlined in one Public Competition Assessment will be conclusive of the ACCC's view in respect of other transaction proposals, as each matter will be considered on its own merits.
7. Many of the ACCC's decisions will involve consideration of both non-confidential and confidential information provided by the merger parties and market participants. In order to maintain the confidentiality of particular information, Public Competition Assessments do not contain any confidential information or its sources. While the ACCC aims to provide an appropriately detailed explanation of the basis for the ACCC decision, where this is not possible, maintaining confidentiality will be the ACCC's paramount concern, and accordingly a Public Competition Assessment may not definitively explain all issues and the ACCC's analysis of such issues.

## **The parties**

### *The acquirer: Santos Limited*

8. Santos is a major Australian oil and gas exploration and production company. Santos is Australia's largest domestic gas producer, supplying natural gas to all mainland Australian states and territories, ethane to Sydney and oil, LNG and liquids to domestic and international customers.
9. Santos has an interest in a number of gas fields in Queensland, including:
  - The Denison trough
  - The Roma shelf
  - The Churchie Gas Field
  - The Cooper-Eromanga Basin.
  - The Scotia CSG field
  - The Fairview CSG field

*The target: Queensland Gas Company Limited*

10. QGC is an explorer, producer and wholesaler of gas in southern Queensland. QGC's principle producing gas fields are located close to Wallumbilla in a region known as the Undulla Nose in Queensland's Surat Basin.
11. QGC currently supplies the equivalent of 8 petajoules ('PJ') of gas per year from its Berwyndale South Gasfield and is working to develop its Argyle and Berwyndale Gasfield to supply its long term gas contracts. Each of these fields are located in the Undulla Nose.
12. QGC has certified 'proven and probable' reserves<sup>1</sup> of at least 695PJ.

**Other industry participants**

13. Origin Energy is a major natural gas producer in Australia. Origin Energy has major production interests in the Cooper Basin and is Australia's largest producer of coal seam gas. Origin has interests in major gas fields in both the Bowen and Surat Basins in Queensland.

**The proposed transaction**

14. Santos made two proposals to acquire QGC. The first proposal, announced on 5 October 2006, was a 100% takeover offer ('the 5 October offer'). The second proposal, announced on 30 January 2007 (and subsequently amended on 7 February 2007), involved two steps. QGC would first create a new company 'NewCo' as a wholly-owned subsidiary of QGC and would transfer the assets, liabilities and obligations not related to the 'Undulla Nose' to NewCo. NewCo would then be de-merged from QGC and Santos would acquire QGC. Santos would own 30% of NewCo.
15. On 31 January 2007, the ACCC announced that in light of the proposal by Santos to acquire QGC announced on 30 January 2007, the ACCC would not make a decision on its consideration of the 5 October 2006 offer, and its consideration of that offer ceased.

*The 5 October 2006 proposal*

16. On 5 October 2006, Santos announced an offer to acquire all the shares in QGC.

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<sup>1</sup> Gas reserves are often referred to as 1P, 2P or 3P reserves. The ACCC understands these terms to mean:

- 1P Reserves – Proven reserves – with a 90% probability that the actual amount of reserves able to be recovered will be greater than or equal to the reserve estimate
- 2P Reserves – Proven + Probable reserves – with a 50% probability that the actual amount of reserves able to be recovered will be greater than or equal to the reserve estimate
- 3P Reserves – Proven + Probable + Possible reserves – with a 10% probability that the actual amount of reserves able to be recovered will be greater than or equal to the reserve estimate.

17. On 30 January 2007, Santos announced that it would be letting the 5 October 2006 offer lapse and on 8 February 2007, Santos announced that the 5 October 2006 offer lapsed on 7 February 2007.

*The 30 January 2007 proposal (amended on 7 February 2007)*

18. On 30 January 2007, Santos announced a new proposal to acquire QGC. This new proposal involved the creation of a new ASX-listed entity, 'NewCo'. On 7 February 2007, Santos advised of amendments to the 30 January 2007 proposal.
19. The ACCC commenced market inquiries on the new proposal on 31 January 2007. It is this proposal that will be referred to as 'the proposed acquisition'.
20. Below is a summary of the proposal as announced on 30 January 2007 and subsequently amended on 7 February 2007.

Santos (post acquisition)

21. Under the proposed acquisition, Santos would acquire the assets, liabilities and obligations of QGC that relate to the Undulla Nose acreage. This included nearly all the current production reserves of QGC and the existing gas supply agreements and commitments.

NewCo

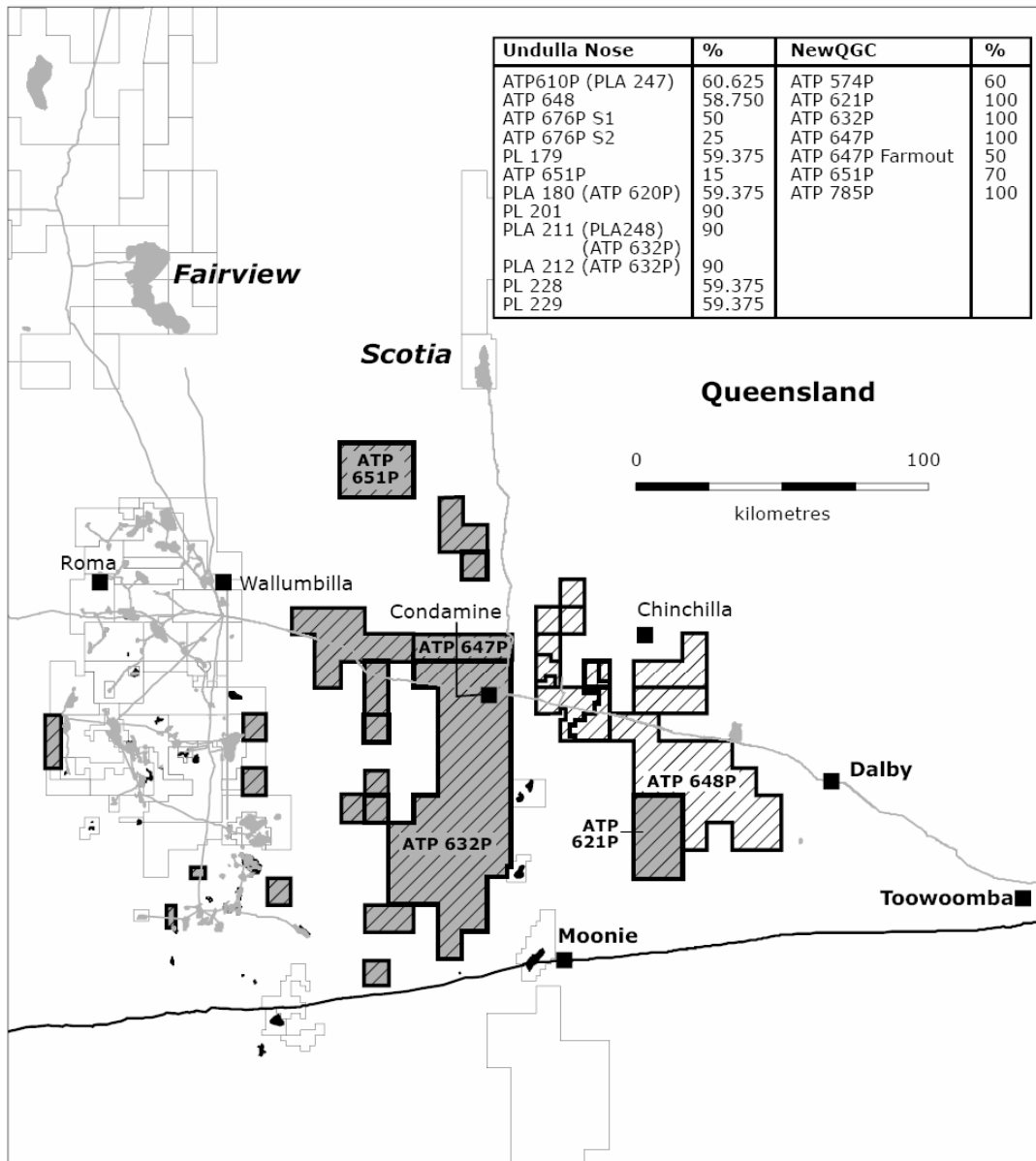
22. NewCo would have the assets, liabilities and obligations of QGC that relate to the non-Undulla Nose acreage. The assets of NewCo would also include a contractual right to develop gas reserves in the Undulla Nose in the ATP648P of up to 100PJ and to sell and receive the proceeds of sale of those reserves to gas buyers. NewCo will also have the right, but not the obligation to sell those reserves to Santos.
23. NewCo would be established with the same Board and Management team of the existing QGC. Santos would have a total shareholding in NewCo to 30% of its issued capital.

Further implementation details

24. The new proposal included a number of arrangements between Santos and NewCo, including:
  - Transitional services, assistance, records and information agreement for the purpose of establishing NewCo's operations independently from Santos as soon as possible;
  - Pipeline consent agreement to enable NewCo to construct and operate a pipeline connecting ATP621P to the Roma to Brisbane pipeline (refer to the map below for the location of ATP621P);

- Drilling Rig access agreement for the purpose of enabling NewCo to use such drilling rigs that QGC owns or has a contractual right to use, including associated personnel and services;
- Pipeline and plant infrastructure access agreement for the purpose of enabling NewCo to use spare capacity in upstream pipeline and plant infrastructure owned by QGC;
- Arrangements in relation to ATP648P (refer to the map below for the location of ATP648P) which will enable NewCo to conduct operations there to meet a reserves target of 100PJ of gas for sale to consumers, or at NewCo's election for possible sale to Santos at an agreed price.
- Transportation and gas swap agreement providing for access to the Roma to Brisbane pipeline and a gas swap agreement for north-west Queensland.
- Interim funding agreement that will provide for Santos to make available \$million to QGC to assist it in meeting its financial commitments and continuing with its capital expenditure program. Santos is also prepared to make additional finance of up to \$million available to QGC if it is deemed appropriate to restructure certain of QGC's existing debt finance arrangements.

## Surat/Bowen Basins



### Legend

- Santos acreage
- Oil Field
- Gas Field
- Oil Pipeline
- Gas Pipeline
- Undulla Nose
- NewQGC



Source: Santos Limited, 'Santos proposes new superior transaction with QGC', 30 January 2007, accessed at [www.santos.com.au](http://www.santos.com.au)

## Timing

25. The following table outlines the timeline of key events in this matter.

Date	Event
05-Oct-2006	ACCC commenced public review under the Merger Review Process Guidelines.
16-Oct-2006	Market inquiries commenced.
26-Oct-2006	ACCC published a Statement of Issues outlining preliminary competition concerns.
09-Nov-2006	Closing date for submissions from interested parties.
23-Nov-2006	ACCC requested further information from Santos. ACCC timeline suspended.
29-Nov-2006	Proposed date for announcement of ACCC's findings delayed to allow consultation on Statement of Issues.
7-Dec-2006	Proposed date for announcement of ACCC's findings delayed pending further information from Santos.
4-Jan-2007	ACCC received further information from Santos. ACCC timeline recommenced.
30-Jan-2007	Santos announced a new takeover proposal for QGC and that it will let the previous takeover proposal lapse.
31-Jan-2007	Proposed date for announcement of ACCC's findings. In light of Santos' new proposal the ACCC announced that it would not be making a formal decision on the previous takeover proposal. ACCC establishes a timeline for market inquiries in relation to Santos' new proposal.
07-Feb-2007	Santos provided amendments to the 30 January 2007 takeover proposal.
13-Feb-2007	Closing date for submissions from interested parties in relation to the new proposal.
20-Feb-2007	ACCC announced its decision to oppose the proposed acquisition.

## Market inquiries

26. The ACCC conducted market inquiries with a range of industry participants, including competitors, potential competitors, customers, industry bodies, and other interested parties. Submissions were sought in relation to the substantive competition issues and proposed undertakings.

## Statement of Issues

27. The ACCC published a Statement of Issues on 26 October 2006 identifying a number of competition issues with the 5 October offer. In the Statement of Issues the ACCC raised issues relating to market definition and identified issues of concern.
28. The Statement of Issues sought further information on the geographic scope of the market definition. Further information was sought on the likelihood of greater interconnectivity of Queensland gas fields with south-eastern Australia through the construction of gas transmission pipelines or through the use of gas swap transactions.

29. The Statement of Issues identified competition issues including that the proposed acquisition would increase ownership concentration for the supply of wholesale gas in Queensland (that is, sales of gas by gas producers). The Statement of Issues also raised the possibility that the proposed PNG gas pipeline would pose a competitive constraint on the wholesale supply of gas in Queensland.

## **Market Definition**

### *Market definition*

30. The ACCC considered the following markets relevant to its decision:
- the market for the production and supply of wholesale gas in the south Queensland region connected by pipeline infrastructure (including Brisbane, Gladstone and Mt Isa); and
  - the market for the production and supply of wholesale gas in the southern states of Australia.

### Product dimension

31. The ACCC considered the product dimension of the markets to be natural gas. The ACCC found that conventional gas and coal seam gas are close substitutes and hence part of the same market.
32. The ACCC considered whether the product dimension should be expanded to include coal and/or electricity. The ACCC noted that a number of gas customers used gas for electricity generation. This suggests that gas, at least indirectly, competes with other fuels used for electricity generation, such as coal. Generally, market inquiries indicated that only a limited number of large gas customers had the potential to switch to coal and/or electricity. Furthermore, market inquiries revealed there are a large number of customers that have limited viable substitution possibilities to gas.

### Functional dimension

33. The ACCC considered whether there existed functional separation in the markets between the exploration of gas and the large-scale production and supply of wholesale gas to customers.
34. In market inquiries industry participants indicated there are important differences between exploration or 'junior' gas producers and gas producers with sufficient proven and probable gas reserves to directly market and supply gas to customers requiring a high degree of certainty in delivery.



35. The ACCC found that gas producers need to be of a minimum size and scale to be considered viable gas supply options for customers, particularly large industrial customers. Market inquiries showed that besides Santos and Origin, QGC was considered the next most viable competitor in supplying wholesale gas directly to large customers. Market inquiries suggested that the other gas producers were not considered to be of a size and scale to be a viable competitor, or a competitive constraint.

Time dimension

36. The ACCC considered the relevant period of time over which to consider the proposed acquisition was a period of less than five years. The ACCC considered that to take a time period beyond five years was too speculative to determine whether any new entrant or substitution possibilities would emerge to constrain any exercise of market power by Santos.

Geographic dimension

37. The ACCC considered markets in two geographic regions:
- The southern Queensland region interconnected by gas transmission pipelines (including Brisbane, Gladstone and Mt Isa); and
  - The southern states of Australia.

Southern Queensland region for the production and supply of wholesale gas market

38. The southern Queensland region covers the area QGC can ‘reach’ using existing gas transmission pipelines. This market did not extend to include the Australian Eastern seaboard due to the lack of or limited pipeline infrastructure interconnection between southern Queensland and the southern states (including South Australia, New South Wales and Victoria). Further, the ACCC was of the view that the existence of gas swaps did not overcome this lack of pipeline infrastructure interconnection as market inquiries indicated that the ability to engage in gas swaps did not provide competitive constraints on gas producers in the southern Queensland region. Gas swaps require two willing parties and typically involve an arrangement whereby one party supplies the other party’s required volume of gas to a particular destination, and vice versa. These arrangements are mutually beneficial and may be used where, due to either the lack of pipeline infrastructure or the direction of gas flow along existing pipeline infrastructure, the parties would not otherwise be able to send its gas to the required destination. The ACCC considered that, particularly due to the limited number of significant players in southern Queensland, the number of willing parties is likely to be limited.
39. The ACCC also considered that the generally higher ex-field prices for gas in the southern states (compared to southern Queensland), combined with the costs of transmission, makes it unlikely that the potential for gas to be supplied from areas outside of southern Queensland would act as a significant price constraint on gas producers in southern Queensland.

40. The ACCC took into consideration the possibility that pipeline infrastructure may be built in the future. The ACCC considered that, if the proposed acquisition occurred, the likelihood of the pipelines being built was not sufficient to affect the market definition. The issue of possible changes in the likelihood of the pipelines being built arising due to the proposed acquisition is discussed further below.
41. The ACCC also considered that the geographic dimension of the market did not extend to include the northern Queensland gas fields (the Moranbah gas fields) due the lack of pipeline infrastructure connecting the Moranbah gas fields to southern Queensland. The ACCC took into consideration the possibility that a pipeline may be built, but considered that the potential for gas from the Moranbah gas fields was not a strong competitive constraint on gas producers in southern Queensland.
42. The ACCC considered that the most relevant geographic dimension to consider the proposed acquisition was the southern Queensland region interconnected by existing gas transmission pipeline infrastructure.

#### Production and supply of wholesale gas markets in southern states of Australia

43. The ACCC also considered whether the proposed acquisition would have competition effects in other geographic regions in Australia. For this, the ACCC noted that there are two proposed pipeline projects that will enable southern Queensland gas to be supplied to the southern states:
  - the Ballera to Moomba Interconnect; and
  - the Queensland Hunter Gas Pipeline.
44. Market inquiries suggested that one driver for these proposed interconnecting pipeline projects was the existence of lower ex-field prices for gas in southern Queensland and the potential for this gas to be a competitive constraint on gas producers in the southern states (even including gas pipeline tariffs). Competition from an independent QGC was seen as an important driver of these price differentials. Therefore, the ACCC considered the southern states of Australia to be a second relevant geographic region in which to consider the likely competition effects of the proposed merger, since the building of the pipelines would affect competition in the southern states and QGC's independence was seen as relevant to the likelihood of the pipelines being built.

#### *Competition analysis*

##### Market Concentration

45. The ACCC considered the most relevant measurement of gas for the purposes of analysing concentration in the market was proven and probable gas reserves, but noted that there are a number of other relevant measures that provide insight into the level of competitive tension in the market.

46. The ACCC considered the proposed acquisition would result in a large existing gas supplier effectively acquiring nearly all the current production reserves of a smaller, but still significant wholesale gas supplier. Post-acquisition Santos would account for a substantial proportion of the wholesale supply of gas in southern Queensland. Together with Origin, Santos would account for a very significant percentage of the wholesale supply of gas to the southern Queensland market.
47. The ACCC noted that the newly created NewCo would have a right to develop 100PJ of 2P reserves in the Undulla Nose in ATP648P. Even with this, however, NewCo would have a very small market percentage of the wholesale supply of gas in the southern Queensland market.

#### Actual and potential level of import competition

48. The ACCC considered whether the actual and potential level of imports would be sufficient to constrain Santos post acquisition.
49. The ACCC has previously considered the potential importation of gas from Papua New Guinea ('PNG') to Queensland by the proposed PNG Gas Pipeline Project provided a competitive constraint and has previously stated that PNG gas was considered to be a 'shadow competitor' by some market participants.
50. Market inquiries indicated that the proposed PNG Gas Pipeline Project was becoming increasingly speculative and the potential for PNG gas to be imported was no longer considered to be a competitive constraint. The ACCC noted that during the course of its inquiries, it was announced that the PNG Gas Pipeline Project had been shelved.

#### Height of barriers to entry

51. The ACCC considered that gas explorers and junior gas producers face significant impediments to achieve the scale necessary to enter the market for the production and supply of wholesale gas in southern Queensland and to become an effective competitive constraint on Santos.
52. The ACCC found that there did not appear to be significant barriers for acquiring land tenements or licenses for initial exploration and test wells. The ACCC noted that while there appeared to be large acreage available for exploration, geographic considerations were a significant factor for determining the successfulness of the exploration.
53. However, the ACCC found that there appeared to be high barriers to entry for companies to become a credible alternative in the market for the production and supply of wholesale gas directly to customers. Market inquiries indicated that for an explorer or junior gas producer to become a credible alternative, it must, at a minimum, prove up significant proven and probable gas reserves.

54. Market inquiries indicated that for a gas producer to develop its gas fields and prove up the gas reserves to 'proven and probable' gas reserves considerable capital expenditure is required; this capital expenditure is largely sunk investment. Moreover, the gas producer needs to undertake capital investment to construct gas processing facilities and pipelines to connect to the main gas pipeline infrastructure. Market inquiries suggested that often a gas producer is unwilling to invest significant capital without some degree of certainty that it will have a customer to take its gas.
55. Market inquiries indicated that customers, particularly large gas customers, need to source their gas from a reliable supplier that has sufficient proven gas reserves, an ability to supply large volumes of gas and a track record of an ability to provide continuity of gas supply. Market inquiries revealed that from a customer perspective, there is a distinction drawn between smaller gas explorers and producers and those larger gas companies capable of entering into significant gas sales agreements.
56. Many market participants referred to this as the "chicken and egg" barrier faced by gas producers wanting to expand its operations to market wholesale gas.
57. The ACCC considered whether large customers have the ability to sponsor new entry, or foster the development of smaller gas producers. The ACCC noted instances where large customers have entered into agreements or joint ventures with smaller producers to provide a capital injection to undertake investment in infrastructure and to prove up certified gas reserves. However, market inquiries revealed that there are still large risks involved and significant time lags before the gas producer might be able to supply customers.
58. The ACCC noted that the proposed acquisition included Newco entering into a number of arrangements with Santos aimed at assisting NewCo in overcoming many of the barriers faced by new entrants. However, the ACCC still considered NewCo would face significant barriers to entry and expansion.
59. The ACCC considered a key issue in this matter was the time it would take a new entrant or NewCo to develop sufficient reserves and become an effective competitive constraint in the market for the production and supply of wholesale gas in southern Queensland.
60. The ACCC had regard to the nature of the gas industry and found that while the gas industry, particularly the coal seam gas industry, has experienced considerable growth recently, much of the infrastructure used in the industry and owned and operated, or used by industry participants are large investments and long term assets. The period required to enter the market was considered to be significant, particularly since the ACCC considered the relevant functional dimension of the market to be the ability to enter into gas sales agreements with customers, not simply the exploration of gas reserves.

Removal of a vigorous and effective competitor

61. The ACCC noted that market participants in Queensland considered QGC to be the third major producer and supplier of wholesale gas behind Santos and Origin. Market inquiries also revealed QGC is widely and strongly considered as a vigorous and effective competitor.
62. Market inquiries pointed to QGC's growth since moving from an exploration vehicle to a producer and supplier of wholesale gas and QGC's role in actively underpinning a number of infrastructure projects. Market inquiries suggested that QGC has been an aggressive competitor in the supply of wholesale gas and that QGC's existence as a large independent supplier of gas has led to some customers experiencing competitive tendering processes for their gas requirements.
63. The ACCC noted that NewCo would have assets in the 'non-Undulla Nose' acreage in which it could prove up gas reserves and develop and a right to develop up to 100PJ of gas in the Undulla Nose in ATP648P. However, market inquiries revealed that customers were mindful of the uncertain prospects of the newly established NewCo, to the extent that they largely dismissed its ability to act as an effective constraint on Santos or Origin in the foreseeable future.
64. Market inquiries also raised concerns about the ability and potential for NewCo to be an independent and vigorous competitor when Santos would hold a 30% shareholders interest in NewCo. Further market participants raised concerns about the potential for Santos to influence future development and expansion of NewCo through the commercial relations that were a part of the proposed acquisition.

Ability to increase prices and profit margins

65. The ACCC considered the merged entity would have the ability to increase prices and/or increase profit margins.
66. When considering the incentive and ability of Santos to increase prices post-acquisition the ACCC had regard to current pricing behaviours of the industry participants and how incentives may change. The ACCC noted that gas sales agreements vary in duration, and that some gas sales agreements last for up to 20 years. As well, the ACCC noted that some gas sales agreements provide for the parties being able to renegotiate the price of gas being supplied under a contract periodically for the duration of the contract.
67. Market inquiries indicated that ex-field gas prices in southern Queensland, particularly in the south eastern region (the Surat Basin), were lower than the ex-field gas prices elsewhere in eastern Australia. Market inquiries also suggested that QGC has been very competitive with its gas price when submitting tenders for gas sales agreements.

68. Market inquiries raised concerns regarding Santos' incentives to increase gas prices post acquisition. Santos operates a portfolio of gas assets. It is likely that Santos will be mindful of the negative effect lower gas prices in southern Queensland may have on the value of its other gas reserves. Market inquiries further raised concerns on Santos' incentives due to the existence of price renegotiating clauses present in some gas sales agreements. Market inquiries noted that often these price renegotiating clauses allow parties (including Santos) to renegotiate the price of gas in the gas sales agreement periodically for the duration of the contract and a reference point may be the 'market' price for gas.
69. The ACCC noted that a number of existing gas sales agreements, as well as new gas sales agreements, will be negotiated (or renegotiated) over the next few years. The ACCC considered the proposed acquisition will likely lessen competition for these agreements and, given the long term nature of gas sales agreements, this lessening of competition will have long lasting effects in the market.
70. The ACCC also considered whether the proposed acquisition will affect the likely timing of construction of new gas transmission pipelines. The ACCC considered that QGC was an important player in several pipeline projects. If Santos acquired most of QGC's proven and probable gas reserves, the likelihood of the proposed pipeline projects occurring would be lessened. The ACCC considered that Santos had less incentive for pipeline projects linking southern Queensland to other areas to be built. Any delays in the pipeline projects would lead to a less competitive environment in those areas that the pipelines would potentially supply, particularly given the lower price of southern Queensland gas compared to other areas.
71. The ACCC considered whether NewCo, with the 100PJ of 2P reserves would be in a position to constrain the pricing behaviour of Santos.
72. Market inquiries raised concerns regarding the potential for a 'floor price' for gas to be created due to the proposed arrangements whereby NewCo could sell the gas to Santos if it was unable to sell to a third party customer. Specifically, customers considered that NewCo would not be willing to sell its gas to a customer at a price below any price agreed to between Santos and NewCo if NewCo exercises an option to put the gas to Santos for payment.
73. The ACCC considered that the Santos entity would have the incentive and the ability to increase gas prices in southern Queensland. The ACCC considered that NewCo would not be in a position to constrain the pricing behaviour of the Santos entity with only 100PJ of 2P reserves. The ACCC noted that NewCo may be able to develop and prove up further 2P gas reserves in the non-Undulla Nose; however the ACCC considered that NewCo may not be able to expand in the foreseeable future to a minimum size and scale necessary to constrain the pricing behaviour of the Santos entity.
74. The ACCC considered that the proposed acquisition would be likely to lead to higher current and future gas prices in the southern Queensland market and reduce the likelihood of significantly lower gas prices in other regions, particularly in the southern states.

## Undertakings

75. The ACCC also considered whether the court enforceable undertakings proposed by Santos, pursuant to section 87B of the Act, would address the issues of concerns identified by the ACCC. A brief summary of the undertakings offered by Santos is set out below:

- Santos not to purchase further shares in NewCo or assets of NewCo

The proposed undertakings included provisions that Santos undertakes not to, without the prior written approval of the ACCC, acquire any legal or equitable interest in shares in NewCo if it resulted in Santos' shareholding in NewCo exceeding 30% of the total issued ordinary voting share capital of NewCo and not to, without the prior written approval of the ACCC, acquire any legal or equitable interest in any asset of NewCo.

- Ringfencing concerning the operations of NewCo and the Board of NewCo

The proposed undertakings included provisions for Santos to ringfence itself from the operations and the Board of NewCo.

With regard to the operation of NewCo, the undertakings provided that Santos will not interfere with the management or operation of NewCo; do anything to prevent NewCo from continuing to operate independently, and any dealings between Santos and NewCo will be conducted on arm's length commercial basis; seek any confidential information from NewCo; or attempt to influence, either directly or indirectly, the decision of the NewCo Board of Directors including but not limited to decisions relating to pricing, removal or appointment of management personnel.

With regard to the board of NewCo, the undertakings provided that Santos will use its best endeavours to procure that no person is appointed to the Board of NewCo or continues to act as a director of NewCo unless they are an Independent Person. The undertakings also included provisions that Santos will ensure that no officer or employee of Santos will accept a position of the Board of NewCo and not to appoint to any of Santos' boards any person who is an officer or employee of NewCo. Also Santos will not without the written approval of the ACCC propose, vote on or act in any way to influence a resolution to change the structure of, or otherwise seek to make changes to the corporate structure of NewCo, or to raise capital or undertake another transaction for the funding of the operations of NewCo.

- Reporting breaches and audit requirements.

The proposed undertakings included provisions for Santos, upon becoming aware of a breach of particular clauses of the 87B Undertaking, advising the ACCC of the breach including the full particulars of the breach and the measures Santos will take to rectify the breach and to avoid its repetition.

The proposed undertakings also provided for an Independent Auditor's report being provided to the ACCC reporting on Santos' compliance with particular clauses of the 87B Undertaking, making any recommendations as the auditor consider necessary to ensure that Santos complies with the clauses, any qualifications made by the auditor in forming its view and any recommendations by the auditor to improve the integrity of the audit process.

76. The ACCC did not consider the proposed undertakings proffered by Santos went to resolving the ACCC's competition concerns.
77. While the undertaking may have ensured that Newco remained largely independent from Santos, and had some access to capital, the undertaking did not alter the fact that Newco would return to the status of an exploration company and there was no guarantee that it would re-emerge as a competitor in the wholesale gas market.
78. Even if the undertaking had fully addressed this concern, the Commission may have been reluctant to accept a long term behavioural undertaking aimed at addressing a structural issue.

### **Conclusion**

79. On the basis of the above, including taking into account the proposed undertakings, the ACCC formed the view that the proposed acquisition of Queensland Gas Company Limited by Santos Limited would be likely to result in a substantial lessening of competition in the market for the production and supply of wholesale gas in the southern region of Queensland and in the market for the production and supply of wholesale gas in the southern states of Australia in contravention of section 50 of the Act.