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From: [REDACTED] (Oil and Gas Authority)
Sent: 20 July 2015 09:19
To: Samuel Andy (Oil and Gas Authority)
Cc: Toole Simon (Oil and Gas Authority); [REDACTED] (Oil and Gas Authority); [REDACTED]; Ljungerud Hedvig (Oil and Gas Authority)
Subject: RE: Request for approval of proposed variation to the Howe/Nelson third party access notice

Attachments:

Submission for Mr Hancock regarding a notice under section 82 of the Energy Act 2011 to resolve a third party access dispute offshore;
Energy Act 2011 Chapter 3.pdf;
Extracts from TPA guidance.docx;
Howe and Nelson diagram.pptx

Andy

As requested, please find attached the following:

- * The original submission to the Minister for the Howe/Nelson Notice (which includes a near-final version of the Notice itself)
- * The relevant sections of the Energy Act 2011 - section 85 relates to Variations to Notices and section 82 relates to the process of considering and giving the Notice
- * Relevant sections of the DECC guidance are in the attached file. The full guidance can be found at:
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/212482/Guidance_on_Disputes_over_Third_Party_Access_to_Upstream.pdf
- * The attached Howe and Nelson diagram shows the location and ownership of the fields

Regards

[REDACTED]

From: Samuel Andy (Oil and Gas Authority)
Sent: 13 July 2015 11:49
To: [REDACTED] (Oil and Gas Authority)
Cc: Toole Simon (Oil and Gas Authority); [REDACTED] (Oil and Gas Authority); [REDACTED]; Ljungerud Hedvig (Oil and Gas Authority)

Subject: FW: Request for approval of proposed variation to the Howe/Nelson third party access notice

[REDACTED]

Many thanks for this submission which I found good and clear.

As discussed I will ask Sarah to schedule a 1-hr review meeting, for when I am in Kings Buildings, that I suggest you, me, Simon, [REDACTED], [REDACTED] and Hedvig ideally attend.

Ahead of that I would be grateful if you could send me:

- * The original submission and notice
- * Relevant section of the 2011 Energy Act
- * Relevant section from DECC guidance
- * Map showing the fields and equities

We also discussed how appeals (only if required) under this TPA scheme are handled and I queried whether there might be merit to see how this legislation might be 'harmonised' with the new Energy Bill - such that for example, the new Tribunal Process could be used for both.

Kind regards,
Andy

From: [REDACTED] (Oil and Gas Authority)
Sent: 10 July 2015 14:41
To: Samuel Andy (Oil and Gas Authority)
Cc: Toole Simon (Oil and Gas Authority)

Subject: Request for approval of proposed variation to the Howe/Nelson third party access notice

Andy

We served the first ever Notice under the legislation in December last year to impose third party access terms, as a result of a dispute between the Howe and Nelson field owners when the transportation and processing agreement for Howe came to an end. In the last few months, we have been considering two requests for variation of that Notice. The attached paper seeks your approval for issue of a Variation, which is also attached. I understand from [REDACTED] that a standard format for such requests has not yet been developed, so I have used broadly similar headings to submissions that we have used with Ministers previously.

I hope that this is clear, but please let me know if you need to discuss or require any further information.

Regards

[REDACTED]

[REDACTED]
[REDACTED]
T: 0300 068 [REDACTED] M: [REDACTED]
Kings Buildings, 16 Smith Square, London SW1P 3HQ
Please send mail to: 3 Whitehall Place, London SW1A 2AW

Submission to the OGA Chief Executive

Issue: Approval is sought for the issue of a Variation to the Notice served on 10 December 2014 that imposed terms for access by the Howe field owners on the Nelson platform owners.

Timing: Not urgent – the Variation has been under consideration for several months – [Redacted]
[Redacted] *[Redacted under section 43(2) of the Act]*

Decision: We seek your agreement that the Variation can be issued

Context/consideration:

Background

An application was made to DECC on 11 September 2013 by the Howe field owners to impose terms for access to processing and transportation services by the Nelson platform owners, following the inability of the parties to reach a negotiated solution. The Howe field was already tied in to Nelson and had operated under an existing agreement for around 10 years. The agreement had been due to expire but had been extended for a short period whilst further negotiation was undertaken.

We followed the process described in section 82 of the Energy Act 2011, supplemented by our published guidance where appropriate. This involves giving the parties the opportunity to be heard, the issue of a 'minded to' letter which described the terms that we were considering setting, and the issue of two draft notices, with comment being welcomed at all stages. The main point at issue was the timing of a switch to cost-share; the Nelson owners thought that this should be immediate, whereas the Howe owners felt that it should be deferred for around 5 years. Our view, based on our guidance and in terms of maximising economic recovery from the fields, was that the Howe field should not switch to cost-share until the point at which

[Redacted]
[Redacted] *[Redacted under section 43(2) of the Act]*

Making a third party (Howe) pay more now is likely to lead to an earlier cessation of production for that field, so that it may be unable to provide a larger contribution when the host (Nelson) really needs it in order to continue operating. [Redacted]

[Redacted] *[Redacted under section 43(2) of the Act]* A Notice was issued on 10 December 2014 which imposed these terms, although did not make explicit provision for assigning these terms to a new field owner.

Shell operates both the Nelson and Howe fields and is an owner in each with roughly equal percentages, hence took a neutral line in the dispute. The [Redacted]

██████████ [Redacted under section 43(2) of the Act] were not happy with the proposed terms, although their main argument was that anything other than an equal cost per barrel for processing and transportation from both fields was unfair. As soon as the Notice was accepted by the Howe field owners, ExxonMobil submitted a request for variation under the legislation to amend the imposed terms to require immediate cost-share as well as impose associated restrictions on assignment. It is this request, and a counter-request by OMV as a Howe field owner to allow assignment of the terms, that has prompted the proposed Variation of the Notice.

Relevant factors/decisions

The Notice of 10 December 2014 was the first ever issued under the upstream third party access legislation; the three other formal applications made to DECC had been resolved through further negotiation by the relevant parties following the issue of a 'minded to' letter. Approval for the Notice was given by the Energy Minister at the time, Matthew Hancock. There is no specific appeal mechanism under the third party access legislation, but Judicial Review can be sought by any party to challenge a decision. The JR process has not been invoked by any party in connection with the Notice and the time limit for action on that has now passed. However, ██████████ appear to be using the variation process as an unofficial appeal mechanism, and might argue that they did not seek JR on the Notice regarding the switch to cost-share as they were trying to reverse the decision by another route.

The parties were sent a draft Variation on 23 February 2015 and were told that approval of any final version would probably be given by Simon Toole – this assumed that the Variation would have been issued before the formal establishment of the OGA. ██████████ have engaged with Simon as a result of this advice, including attending a meeting on 27 April. There did not appear to be any significant new issues raised in that meeting (over and above those considered when drafting the Notice) and Simon responded with a letter on 30 June which supported the position taken in the Notice.

In their latest communications, ██████████ have suggested that the decision to issue the Variation should now be made with the knowledge of the Chief Executive of the OGA and possibly the Minister also.

Options:

The following options are suggested:

1. That you recommend issue of the Variation
2. That you review the process that we have undertaken in considering the requests for variation and the concerns raised by ██████████

We suggest that you recommend issue of the Variation without the need for Ministerial approval, but are happy to take part in any review if you wish to carry this out.

Internal reviews:

The Variation has been reviewed by [REDACTED] from an economic perspective and by [REDACTED]. It has been approved by Simon Toole.

Financial implications:

No direct implications – although a request for Judicial Review of the Variation could have a significant impact.

Variation of the Notice served under section 82(11) of the Energy Act 2011 in respect of the Howe field seeking access to the Nelson Platform, dated 10 December 2014 ("the Notice")

Amendments to the Notice

In the exercise of powers under section 85(2) of the Energy Act 2011, the Secretary of State, having received an application from persons to whom the notice was served to vary that notice, has decided to vary the Notice.

With effect from 08 July 2015, the Notice is varied to include the following additional term:

1. The Nelson owners and the Howe owners are free to assign the rights secured and the duties imposed by this Notice to any Person, subject to the execution of an agreement between the Nelson Operator, the Howe Operator, the assigning party and the new party. The agreement will record the assignment of the rights and duties from the assigning party to the new party and should be of a similar form to that contained in Schedule 7 to the [REDACTED]
[REDACTED]
[REDACTED]. 'Person' in this term has the same meaning as in the [REDACTED].

In Annex 1 of the Notice, in sub-section 1 following the requirement to delete Clause 17.1.3, the following sentence should be inserted:

Clause 20 should be deleted.

08 July 2015

Explanatory Note to the Variation

The Notice came into force on 1 January 2015, following acceptance of it by the Howe owners on 19 December 2014.

A number of responsibilities for oil & gas regulation, including application of sections 82-91 of the Energy Act 2011, were transferred to the Oil & Gas Authority on 1 April 2015. This variation has been issued by the Oil & Gas Authority, which is currently an Executive Agency of the Department of Energy and Climate Change (DECC).

Requests for variation of the Notice

Two requests were made to vary the Notice, by Esso on 22 December 2014 and by OMV on 23 December 2014. Esso requested that the Notice be varied to cover:

- An immediate switch to a cost share arrangement in line with previous communications
- No reconciliation of costs in favour of Howe for interim period services during 2013 and 2014
- No assignment of Notice terms without cost share provisions in place

Esso subsequently clarified the third bullet point in a meeting on 15 January 2015 that the Nelson owners should be able to assign but the Howe owners should not.

OMV requested that the Notice be varied to enable the assignment of the rights and duties contained within it.

Given that assignment is a common element in the requests from Esso and OMV, it was decided that they should be considered together.

First variation requested by Esso

Esso explained that they did not consider the Notice to be fair or appropriate in the circumstances. They consider that the tariff imposed by the Notice to represent a subsidy in favour of the Howe Owners.

[REDACTED]

It is not clear that there is a dispute on this point between the parties to whom the Notice was given; it appears that the dispute is between Esso and DECC/OGA. Although it is therefore questionable whether the first variation requested by Esso meets the requirements of section 85(3) of the Energy Act 2011, the benefit of the doubt has been given and the request has been considered.

This first variation request, if granted, would alter the fundamental conclusion of the assessment carried out by DECC that was used to prepare the Notice. In the time since that assessment was carried out, the oil price declined significantly during the second half of 2014 and has fluctuated around the \$60 per barrel level since. Production from Nelson during 2014 averaged 6,824 barrels per day according to data reported to DECC, [REDACTED]. Production Efficiency

reported to DECC/OGA for the Nelson/Howe/Bardolino facilities for 2014 was █%, with most losses being attributed to █. Nelson production reported to DECC/OGA for the first five months of 2015 was 8,942 barrels per day.

It was expected when carrying out the assessment that there would be fluctuations both in the performance of Nelson and Howe and in market conditions. The arrangements that were specified in the Notice were intended to allow for changes in the fortunes of the two fields, specifically that there are measures in place to ensure that Howe makes a larger contribution to the running costs of Nelson when the latter is close to becoming permanently uneconomic. In the event that oil prices do not recover substantially and the operating costs of Nelson cannot be reduced, these measures will be triggered by the actions of the Nelson Owners in moving towards cessation of production. As this possibility was envisaged in the assessment by DECC (and the measures were put in place in the Notice to enable a switch to a cost sharing arrangement in that event), there does not appear to be any significant new or changed information that could undermine the basis of that assessment.

The matter of the conflict of interest of some of the Nelson Owners was considered as part of the assessment carried out by DECC. The measures in the █ were believed to present some protection for the non-conflicted owners (by requiring their agreement to the decommissioning schedule that is prepared each year), as discussed in the Explanatory Note to the Notice. It is feasible that Nelson could be uneconomic for an extended period while Howe is very profitable, but the relative sizes of the fields suggests that the overall benefit to the conflicted Nelson Owners would be small (even if positive) in most cases. From a perspective of risk, the conflicted Nelson Owners would be offsetting the substantial costs of operating the Nelson infrastructure with the modest income from production from the single Howe well which is exposed to single points of failure with associated risk of disruption. It is therefore hard to envisage a situation in which the conflicted Nelson Owners would delay planning for cessation of production of Nelson due to the profitability of Howe.

Esso have observed that, although the non-conflicted Nelson Owners can refuse to agree the annual decommissioning schedule and so force a referral to expert determination, this does not allow them to trigger the cessation of production process itself (for which they would require █% of votes). For the reasons given in the paragraph above, it appears that the conflicted and non-conflicted Nelson Owners should not be seriously misaligned when considering cessation of production, and are likely to be in agreement if Nelson becomes genuinely and permanently uneconomic.

As a result of the foregoing, no reason has been found to substantially revisit the assessment made by DECC prior to issue of the Notice. The request to change the terms of the Notice to require an immediate change to a cost share arrangement is therefore declined.

Second variation requested raised by Esso

Temporary agreements were in place between the Nelson owners and the Howe owners during 2013 and 2014, and these contained provision for reconciliation of

costs in the event that a new [REDACTED] was agreed between the parties. These agreements terminated on 31 December 2014. The Notice was an imposed (not negotiated) solution with terms that took effect from 1 January 2015, was forward-looking in nature and did not seek to reconcile costs for the period when the temporary agreements were in force. It is therefore clear that the Notice does not require reconciliation of past costs, and it is understood that this point is not in dispute amongst the persons to whom the Notice was given. On the understanding that there is no dispute, which has not been contradicted by Esso, the conditions specified in section 85(3) of the Energy Act 2011 are not met and so a variation is not appropriate.

Assignment of the rights and duties in the Notice

Section 82(13)(b) of the Energy Act 2011 allows a notice to contain a provision permitting a right secured or a duty imposed by the notice to be assigned. The omission of a specific provision in the Notice to allow assignment was not deliberate, with the assumption being made that the assignment clause (20) in the existing [REDACTED] would be adequate. However, further consideration has indicated that clause 20 is not sufficient to allow assignment of the Notice. The requests for variation give an opportunity to consider the matter of assignment in more depth.

Esso argued that, due to their view that the terms imposed by the Notice are unfair to the Nelson owners, assignment by the Howe owners should not be permitted. They were concerned that the imposed terms represent a benefit to the Howe owners, [REDACTED]

OMV argued that the Notice did not prevent assignment and the use of the [REDACTED] without any comment on this matter implied that it should be permitted.

The DECC guidance on dispute resolution does not contain any advice on how to deal with assignment. Other published DECC documents give qualified support for assignment; as a way of improving alignment on licences (petroleum licensing guidance) or ensuring that assets are in the hands of those with collective will, behaviours and resources (stewardship guidance). The stewardship guidance indicates that divestment is one option to help bring about improvement. DECC policy in specific cases has been to encourage the departure of parties who do not have a strong interest in remaining involved with an asset.

For the above reasons, it is considered appropriate that assignment should be allowed. Moreover, it would be counter-productive to stop parties from leaving an asset if they have found a buyer who is likely to have more interest in investing in it. Esso requested that assignment should be allowed for the Nelson owners but not for the Howe owners. However, the above rationale would apply equally to both sides of the dispute. [REDACTED]

[REDACTED] it does not appear to be a relevant consideration whether or not one party in a dispute is already engaged in a sale process. Taking account of such a fact in setting terms would undermine a Notice if another party announced a sale shortly after a Notice was issued.

It is therefore concluded that assignment of the rights secured and the duties imposed by the Notice should be permitted. The means by which this is achieved is now considered.

Clause 20 of the [REDACTED] allows an existing party (owner and/or operator) to assign their liabilities and obligations to a new party in the event of agreement for sale and purchase of the production licence and associated interests. This is achieved through a novation agreement that is executed in conjunction with the Nelson Operator and Howe Operator. There is no explicit requirement for any other owner on either side (Nelson or Howe) to agree to the new party. It is assumed that this approach was adopted because the most significant impact of a new party that is considered to be unsuitable (e.g. due to insufficient financial resources) would be on the particular field group (Nelson or Howe). Approval of the new party by the remaining members of the field group would be needed in accordance with the terms of the relevant [REDACTED]. In the event that the remaining members do not approve the new party in their own field group, the assignment of the interest in the field group will not take place, making novation of the [REDACTED] irrelevant.

In addition, DECC/OGA have powers to prevent assignment or change of control of production licences in the event that there is concern about the suitability of a new party.

The means of enabling assignment of the rights secured and the duties imposed by the Notice is therefore to follow the general approach of the [REDACTED] by requiring an agreement to be executed between the Nelson Operator, Howe Operator, assigning party and new party in order to record such assignment. The form of the agreement contained in Schedule 7 to the [REDACTED] should be followed but would need to describe the assignment of the rights secured and duties imposed by the Notice rather than the liabilities and obligations described in the [REDACTED]. The Secretary of State shall not be required to be a party to such an agreement.

Note of meeting of 28 July 2015 with Andy Samuel (Chief Executive of the Oil & Gas Authority) to review the proposed variation of the Howe/Nelson notice dated 10 December 2014

Present:

Andy Samuel, Simon Toole, [REDACTED]

Discussion points

A summary of the background to the case and the process for considering the application was given. A number of points of clarification, including the extent of peer review that was carried out and how limited information provided by the operator was handled, were raised. It was confirmed that peer review has taken place at various levels within DECC/OGA, as well as seeking advice from external consultants. Where limited information was provided and assumptions were made as a result, the 'minded to' letter and the two draft notices were used to test these assumptions with the parties.

A wider discussion was also held regarding the use of the third party access legislation, including the level of expertise needed to consider applications, the total resources (mostly people with a range of skills) that are required, and the publication of summaries of concluded cases.

[REDACTED]

[REDACTED] *[Redacted under section 42(1) of the Act]*

Decision on variation

AS was content with the case made in the documentation provided to him with the subsequent clarifications, and agreed to the issue of the variation.

Action points

[REDACTED] to prepare presentation on third party access cases to interested parties in OGA, once more staff are in post

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From: Samuel Andy (Oil and Gas Authority)
Sent: 18 August 2015 17:36
To: [REDACTED] (Oil and Gas Authority)
Cc: Toole Simon (Oil and Gas Authority)
Subject: Howe/Nelson Notice - Variation request

[REDACTED]

I'm happy to confirm that Simon and I conducted our review on Howe/Nelson on the 28th of July and were fully satisfied it has been a robust, fair and thorough process from our perspective.
Kind regards,
Andy

