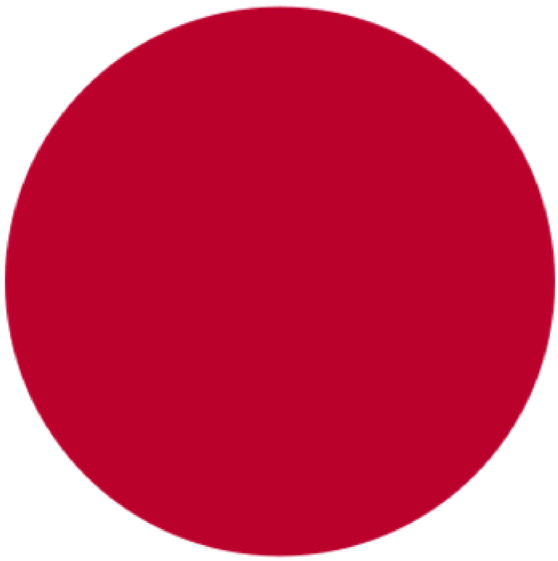
Japan takes aim at destination clauses

INTERNATIONAL law firm Baker Botts has urged LNG sellers to review their contracts amid reports that Japan's Fair Trade Commission is investigating whether destination clauses in long-term LNG supply contracts with Japanese buyers violate the country's competition law.

Haydn Black (/author/profile/888c32d3-3646-4857-be37-825277f70940/haydn-black) 08 March 2017 08:53 News



The firm said overnight that it understood the JFTC had confirmed rumours that it launched the investigation last year.

It said LNG sellers need to be prepared to navigate the hurdles created by the JFTC investigation.

If the JFTC formally objects to destination clauses, which are typically contained in LNG contracts with some of the world's largest LNG sellers, it may result in the forced renegotiation of LNG sale and purchase agreements.

That would be a complicated process, and could trigger price review procedures in Japan, and could trigger a series of antitrust enforcement agencies in the Asia region and subject LNG supply agreements involving buyers in their jurisdiction to the same level of antitrust scrutiny as well.

Buyers in Japan, and South Korea, are increasingly frustrated that they are over-contracted and restricted by their contacts about how they can sell surplus volumes.

The standard destination clauses in most long-term LNG contracts restrict where shipments of gas can be unloaded and prevent buyers from selling on excess cargoes.

JERA, a Gorgon partner and JV between Tokyo Gas and Chubu Electric, said last year it would no longer sign fixed destination contracts.

Earlier last year, Japan's Ministry of Economy, Trade and Industry recommended the supply contracts to be reworked.

The investigation, which is understood to have begun late last year, could be complete by year's end, but it presents a myriad potential implications for LNG sellers against a backdrop of a global glut and a current energy over-supply of the Japanese market.

Analysts estimate that Japanese buyers will face a surplus of 12.2 billion cubic metres of LNG in 2017 and 8.6 billion cu.m in 2019.

It could mark the end of destination clauses in the region, if not globally, the International Gas Union has warned.

Buyers have been pushing for destination clauses to be removed so they can trade their contractual purchases when it would make more economic sense to sell into other markets.

Japan buys about a third of global LNG shipments, and is still a major customer of Australian LNG, although it is increasingly taking US gas as well.

According to the latest Energy Quest review, however, Japanese buyers were paying an average price of $US12.63/MMBtu for gas from the Sabine Pass facility, well above Australian prices closer to $US7.36/MMBtu.

Sabine Pass shipped a record 15 cargoes in January, including eight into Asia, with Japan buying three.

Japanese LNG imports fell by 2% year-om-year, but stabilised towards the end of the year.

Although the Japanese gas market is shrinking overall, Australia is increasing its volumes and imports from Australia were 33% higher quarter-on-quarter, EnergyQuest reported.

Australia was Japan's largest supplier providing 30% of total imports, with around 90% in the December quarter from the North West Shelf, Pluto LNG and Darwin LNG.

The east coast LNG plants shipped a total of 10 cargoes, with half coming from Shell's Queensland Curtis LNG.

Eleven of Gorgon's 19 cargoes delivered were delivered to Japan in the December quarter, and Papua New Guinea LNG has contracts 2.3MMtpa.

LNG producers have warned that scrapping the contracts could lead to fewer new LNG projects being developed, if developers cannot pre-contract a significant proportion of the cargoes before reaching a final investment decision, although the entry of more US gas in the market could change that.

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