

Energy

Fourth Edition

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Australia

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Overview of the current energy mix, and the place in the market of different energy sources

The volatility in world energy markets during 2014-2015 has been so extreme that one hesitates to rely on the accuracy of trends based on 2012-2013 statistics set out in the Australian Government's *Energy White Paper*, which was released on 8 April 2015. However, the *Energy White Paper* asserts that, in 2012-2013:

- Australia's energy production rose by 9%, underpinned by increases in the production of coal (8%), uranium (18%), natural gas (14%) and renewable energy (12%);
- the breakdown of Australia's energy consumption was: coal 33% (a decrease of 6%); natural gas 24% (an increase of 2%, with 1,232PJ used for industrial and electricity purposes and 155PJ for household purposes); oil 38% (an increase of 1%, with petrol, diesel and aviation fuel accounting for over 90% of transport energy use); and renewable energy 6% (an increase of 12%);
- electricity generation in Australia was fuelled 64% by coal (a decrease of 7%); 21% by natural gas (an increase of 5%); 13% by renewable energy (an increase of 26%); and 2% by other resources. Electricity consumption decreased from approximately 8,700 kWh *per capita* in 2012-2013 to approximately 8,450 kWh *per capita* in 2013-2014, from a high of approximately 9,600 kWh *per capita* in 2003-2004;¹ and
- Australia's energy exports rose by 14% to 15,504PJ (being 80% of total energy production), underpinned by strong growth in coal, uranium and liquefied natural gas (**LNG**) exports, of which Australia is among the world's largest exporters. The *International Energy Agency* has forecast that Australia will overtake Indonesia as the world's biggest exporter by volume by 2030 (although Indonesia will remain the largest thermal coal exporter), with Australia's coal export volume projected to increase by +90Mt, and Indonesia's to decrease by -21Mt, between 2013-2019.² Energy imports also increased strongly by 5% to 2,310PJ, comprised predominantly of crude oil and refined petroleum products.³

A variety of factors is driving the prices of Australian commodities lower, but predominant among them is the uncertainty of China's ability to sustain the growth of GDP above 7% per annum, particularly as the economy has already grown substantially by the transition of large numbers of the population from agrarian to industrial activities and given the significant increases in public and private sector debt to facilitate the transition.

The Australian coal⁴ price has fallen from US\$ 120.09/Mt in June 2011 to US\$ 59.34/Mt on 28 August 2015 and the iron ore price⁵ has fallen from US\$ 187.18/ dry Mt in February 2011 to US\$ 55.65/ dry Mt in July 2015. Australia is the world's second-largest iron producer (after China) and the largest iron ore exporter.

Changes in the energy situation in the last 12 months which are likely to have an impact on future direction or policy

Australia is nearing the end of a boom which has seen 9 of the 11 largest construction projects in the global energy and resources sectors under development concurrently. Six of those are LNG projects,⁶ which are estimated to have involved capital expenditures aggregating close to US\$ 200bn. Given the enormous expenditures involved and that, at least until recently, LNG prices have been linked to the average cost of a ‘basket’ of crude oils landed in Japan (*JCC pricing*), the recent volatility in crude oil prices will mean the current LNG prices will be far less than those assumed at the time final investment decisions were taken on each of the six LNG projects.

The spot price of Brent crude oil reached US\$ 124.93/barrel on 31 March 2012; on 24 August 2015 it was US\$ 41.59 and on 24 August 2015 it ‘jumped’ US\$ 4.42/barrel (the largest one-day increase since December 2008) to close in afternoon trade at \$47.56. Industry expectations are that Saudi Arabia will endeavour to cause crude oil to trade in the range US\$ 40 to US\$ 80/barrel, as much of the US shale oil production currently becomes sub-economic below US\$ 80/barrel.

With the benefit of hindsight, Australia allowed too many large-scale projects to be developed concurrently without taking adequate steps to increase the pools of skilled labour available to those projects. By way of example, welders working on Chevron’s Gorgon LNG project offshore Western Australia were able to work two weeks on, one week off for in excess of AU\$ 400,000 per annum; welders from Sri Lanka and the Philippines working on Exxon’s Port Moresby LNG project were required to work eight months on, one month off for around US\$ 60,000 per annum. The consequence is that future *greenfields* LNG projects in Australia are likely to be developed utilising floating LNG facilities built in Korea, Taiwan or China, with the first being Shell’s giant *Prelude FLNG* facility.

Developments in government policy/strategy/approach

As noted above, the Australian Government’s *Energy White Paper* was, after a lengthy consultation process, finalised and released on 8 April 2015. The Paper has three principal themes:

- increasing competition to keep energy prices down;
- increasing energy productivity to promote growth; and
- investing in Australia’s energy future.

Increasing competition to keep energy prices down

The White Paper suggests that this should occur by:

- introducing competitive and voluntary smart metering services to allow consumers to monitor their energy use and respond to pricing signals, such as higher prices during periods of peak demand;
- privatisation of energy assets owned by State and Territory Governments so as to limit their involvement in the energy markets. The Federal Government has agreed to make available to the States and Territories, on a ‘first-come, first-served’ basis over five years, AU\$ 5bn by way of 15% of the purchase price of each asset privatised, if all of the sales proceeds are allocated to new infrastructure investment in that State or Territory. A collateral benefit for the Federal Government is that, by privatisation, the relevant assets may change from being owned by a State-owned enterprise which

does not pay income tax to an entity which does. This so-called ‘Asset Recycling Initiative’ has the stated policy objectives of discouraging the States and Territories from using the proceeds of privatisations merely to pay down pre-existing debts and encouraging them to invest in new infrastructure so as to improve economic efficiency. The expectation is that the Government’s AU\$ 5bn will leverage AU\$ 40bn of new infrastructure expenditure;

- increasing gas-on-gas competition by reversing the flow of the Alice Springs-to-Darwin Pipeline and linking it with a new gas transmission pipeline either to existing pipelines at either Moomba or Mt Isa. This would allow gas reserves currently stranded offshore Western Australia and the Northern Territory to enter the East Coast gas markets; and
- responsible development of coal seam gas and unconventional gas resources. Policies to this end will be developed in light of the findings and recommendations of the Australian Consumer and Competition Commission into transparency and pricing in the East Coast gas markets.

Increasing energy productivity to promote growth

This initiative involves development of a National Energy Productivity Plan to improve the ways in which energy is used, by providing consumers with the choice, information and tools to source and use energy and by promoting energy efficiencies in buildings, transport, equipment and appliances.

Investing in Australia’s energy future

The White Paper suggests that this should occur by:

- promoting Australia as a destination for foreign capital and technology to develop reliable energy supplies;
- supporting a technology-neutral approach to the future supply of electricity and transport fuel;
- continuing to support research and development of new energy technologies by removing unnecessary regulatory and other non-market barriers; and
- improving the capacity of the Government to identify future opportunities for, and to respond quickly to, major changes in the production, transportation and use of energy.

Developments in legislation or regulation

On 18 May 2015, the Federal Government and the Australian Labor Party-dominated Opposition announced that they had agreed to reduce the Renewable Energy Target (**RET**) from 41,000 GWh to 33,000 GWh by 2020. The RET was established in 2010 with the aim of increasing the proportion of electricity generated in Australia from renewable sources. Under the scheme, electricity retailers are required to surrender certificates evidencing that electricity has been generated utilising renewable sources in order to meet prescribed annual targets, failing which the delinquent retailers incur a ‘shortfall financial penalty’. The RET scheme was subject to biennial reviews.

Under the amended scheme, biennial reviews have been eliminated, leaving the Clean Energy Regulator to report annually to Parliament on progress towards achieving the stipulated targets. Further, electricity users in emissions-intensive, trade-exposed industries (such as aluminium smelters which are unable to pass on costs associated with the RET due to international competition for their output) have been exempted from the requirement to surrender certificates.

In anticipation of the United Nations Climate Change Conference in Paris in December 2015, on 11 August 2015 the Prime Minister announced that Australia will reduce its greenhouse gas emissions so that they are 26%-28% below 2005 levels by 2030. If achieved, this will mean Australia's *per capita* emissions will decline by 50% between 2005 and 2030, while emissions per unit of GDP will fall by 64% in that same period. The Federal Government proposes to achieve the reduction by a so-called 'direct action plan', rather than by the introduction of a carbon tax or an emissions trading scheme. The 'direct action plan' includes a National Energy Productivity Plan, improving the efficiency of vehicles, phasing down hydrofluorocarbons used in refrigerators and air conditioners, improving the utilisation of solar power, Minimum Performance Standards for appliances and buildings, planting 20 million trees and developing a low emissions technology 'roadmap'.

Judicial decisions, court judgments, results of public enquiries

In 2010, India's Adani Group acquired thermal coal reserves in the Galilee Basin in Central Queensland and a 99-year lease of coal-loading facilities at the Port of Abbott Point, and announced its intention to develop Australia's (and one of the world's) largest coal mines and a vertically integrated 'pit to plug' coal export business servicing international customers. The project, known as the Carmichael Coal Mine and Rail Project, would require a new 388 km standard gauge railway line from the mine site to Abbott Point.

The project would comprise five open cut and three underground mines producing in excess of 60Mt per annum and would involve capital expenditures in excess of AU\$ 16bn. Mine-life would be 60 years and it is estimated that some 10,000 direct and indirect jobs would be created and that, in the first 30 years, the project would generate around AU\$ 20bn in mining taxes and royalties.

There has been considerable opposition to the project, both in Australia and internationally, not only because the mines would be located in prime agricultural land, but also because of general opposition to new fossil fuel developments, particularly of this scale.

Environmental approvals for the project were granted by the Federal Minister for the Environment, the Hon. Greg Hunt MP, in July 2014, but their validity was challenged in the Federal Court of Australia by anti-coal activists, the Mackay Conservation Group. The Federal Court ordered that the approvals be set aside on the basis that the Minister and his Department had not given due consideration to the impact of the project on two vulnerable species, the yakka skink and the ornamental snake, which inhabit areas in the vicinity. The Minister must now consider the materials and re-make his decision.

Environmental groups have claimed a major victory, but the response of the Federal Government has been to introduce into Parliament the *Environmental Protection and Biodiversity Conservation Amendment (Standing) Bill, 2015*. The purpose of the Bill is to repeal s.487 of the *Environment Protection and Biodiversity Conservation Act, 1999* (the **EPBC Act**), which extends the meaning of *person aggrieved* for the purposes of the *Administrative Decisions (Judicial Review) Act, 1977* (the **ADJR Act**) to include Australian citizens, residents, organisations and associations who, at any time within two years of the making of a relevant decision (or the failure to do so), have been engaged in a series of environmental conservation or research activities in Australia.

If the Bill is enacted in its present form (as to which there is some doubt, given the extent of the likely opposition from Green and Australian Labor Party Senators), environmentalists and conservation groups will need to establish that they are *persons aggrieved* within the

meaning of the ADJR Act before they have standing to institute proceedings. To do so, they will need to demonstrate that their own interests, as opposed to those of third parties, are adversely affected by any decision they are seeking to challenge.

Major events or developments

It has been estimated⁷ that, since 2008, Australia's four major trading banks have lent over AU\$ 36bn to fossil fuel projects in Australia. In the wake of the Federal Court challenge to the environmental approvals for Carmichael Coal Mine and Rail Project, the Commonwealth Bank of Australia has withdrawn from its role as financial adviser for the project and Standard Chartered Bank has announced that it will not provide financial advice to, or participate in funding of, the project.

It seems inevitable that new coal projects will become more difficult to finance in Australia. To put this issue in perspective, the Bureau of Resources and Energy Economics estimates that there are 93 projects in the coal investment pipeline in Australia involving capital expenditures of approximately AU\$ 118bn and, in the case of 64 of the projects, creating 75,000 new jobs.⁸

The renewables industry suffered another setback when, in July 2015, the Federal Government directed the Clean Energy Finance Corporation (**CEFC**), a statutory authority constituted with AU\$ 10bn to fund clean energy initiatives, to cease funding new wind power projects. The Prime Minister's objection to wind farms seems to be that they are 'visually awful', but the official position is that wind power is mature technology and that the CEFC was set up to fund innovative proposals and technologies. The CEFC is currently invested by 33% in solar power, 30% in energy efficiency, 21% in wind power and 16% in other technologies.

The Minister for the Environment has also undertaken to appoint a wind farm commissioner to handle complaints about turbine noise.

Proposals for changes in laws or regulations

Coal presents a significant conundrum for policy makers in Australia. It continues to be a significant contributor to the Australian economy⁹ and the Internal Energy Agency expects world coal consumption to grow by one-third by 2035, given that 18% of the population have no access to electricity at all and 38% are dependent on wood, crop residues and animal waste for their main cooking and heating fuels.¹⁰ However, increasingly coal is viewed as a 'sunset business' in many developed economies, with the fuel generation 'mix' moving dramatically away from coal. The longer Australia continues to shun the international community by developing more of its substantial coal resources, the more difficult it is going to be for the country eventually to 'kick the habit'. Of course, technological advances, such as in carbon capture and storage, may ultimately provide a solution, but progress to date has been slow.

* * *

Endnotes

1. The electricity consumption statistics are drawn from *Electricity Gas Australia (EGA) 2015* published by the Energy Supply Association of Australia.
2. *Coal Hard Facts*, Minerals Council of Australia, www.minerals.org.au, 7.

3. *Energy White Paper – at a glance*, Department of Industry and Science, Australian Government, www.ewp.industry.gov.au, 5-7.
4. FOB Ports of Newcastle and Port Kembla; 6,300 kcalper Kilogram; less than 0.8% sulphur and 13% ash.
5. China Import Ore Fines 62% spot (CFR Tianjin Port).
6. Gorgon LNG, Ichthys LNG and Wheatstone LNG in Western Australia and Queensland Curtis LNG, Australia Pacific LNG and Gladstone LNG in Queensland.
7. By the environmental group, Market Forces.
8. *Resources and Energy Major Projects, October 2013 Report*, 27 November 2013.
9. The ‘broader coal economy’, being coal mining, related industries and services and spending of wages earned in the coal economy, was estimated to represent 4.2% of GDP or almost AU\$ 60bn in 2011-2012 – see *Coal Hard Facts*, n.2, 10.
10. *Ibid*, 18 and 19.

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The views expressed above are those of the author.

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