

Could Regulatory Headwinds in Israel Shutdown Offshore Energy Development?



On the cusp of the New Year, we published a chronicle of self inflicted woes that have befallen Israel's grasp of its energy prize, ["Could Israel Lose the Energy Prize in the Eastern Mediterranean?"](#) The Noble Energy, Inc. (NBL-NYSE) and Israeli Delek Group, LTD, (DELEK-TELV) (the Consortium) has developed the most significant gas fields in the Eastern Mediterranean with over 32 trillion cubic feet (TCF) which at current market prices might produce a value of nearly \$100 Billion. The consortium found itself thwarted by a Consent Decree issued by the independent Israel Antitrust Authority (IAA). The Decree essentially reneged on a deal that would have left the Consortium in control of the Tamar field with 7.9 tcf . That field went on stream in April 2013 and potentially the even more significant Leviathan field was scheduled to begin production in 2017 with reserves of more than 21.9 tcf.

Dr. David Gilo of the IAA effectively ruled that the Noble Energy – Delek Consortium constituted a monopoly and would be forced to sell the Leviathan or Tamar fields in Israel's offshore Exclusive Economic Zone. Gilo was [cited](#) by the *New York Times* saying, "The entry of Delek and Noble into Leviathan has created a situation in which these groups control all the gas reserves on the coast of the State of Israel." Gilo's [rationale](#) for his ruling was the prior agreed to sale of smaller gas fields Tanin and Karish owned by the Consortium "did not create a real competitive solution to

solve the problem of a monopoly in the market." *Globes, Israel Business* reported in an article, [Cukierman & Co. Investment House Ltd.](#), and joint manager of the Catalyst funds.

Edouard Cukierman, French- Israeli financier was [harshly critical](#) of Gilo's ruling:

The bureaucrats and politicians who come along with populist ideas need to understand that it takes two to tango. No international investor will put a cent into oil and gas as long there is uncertainty in the industry. We are freezing the growth of the State of Israel's economy for many years ahead because of this wretched decision. Noble Energy has announced a freeze on investment that could have contributed 2% to the economy's growth rate and yielded huge amounts in tax it's all frozen.

Noble ... was fortunate enough to obtain one of the biggest discoveries in the world, and what does he get? Restrictions on exporting in an economy with very limited demand; he gets a change in the taxation method, and now the straw that breaks the camel's back. It's exactly the same story, because here too you have bureaucrats who want to be popular. Who will pay the price of Israel making a mockery of itself before the international investment community? The public will pay it.

US Secretary of State Kerry had [spoken](#) with Israeli PM Netanyahu about resolving this impasse. Netanyahu indicated that he would have his National Economic Council head, Dr. Kandel prepare an assessment, but indicated that Gilo's decision was out of his control. Amos Hochstein, Special Envoy for International Energy Affairs at the US Department of State, who had settled the maritime boundary dispute between the Israel and Lebanon Exclusive Economic Zones, [remarked](#):

"We'll support any agreement that will satisfy both parties, the Israeli regulators and the companies, and

facilitates developing the gas fields as rapidly as possible. I believe this is also in Israel's interest."



Dr. David Gilo Director General , Israel Antitrust
Authority

Dr. Gilo [defended](#) the abrupt change basically warning the Consortium that if it objected to the Consent Decree declaring the Consortium a cartel owning a duopoly, the Tamar and Leviathan fields, that any delay in development would be the fault of Noble and Delek. The reason for the three year delay in arriving at the change was allegedly due to a "long and complex" public hearing process. Further, the prior settlement the IAA indicated did not evince any effective competition and the cost of not achieving that was greater than the cost in the delay of completing the Leviathan field. Gilo artlessly dismissed the comments that foreign investors would not take risk in the gas development, because of the uncertainty the Consent Decree created, and that the law had to be enforced. He believes that the duopoly, the ownership of both the Tamar and Leviathan fields would not result in lower gas prices to consumers.



Professor Eytan Sheshinski

Professor Eytan Sheshinski of Hebrew University, who devised the original taxation scheme for the offshore gas program for the Israeli government that had issued the permits to the Consortium ,[said:](#)

I'm worried about this euphoria surrounding a split. Forcing Noble Energy and Delek Group to sell Tamar or Leviathan through a legal battle could take 10 years, and the Antitrust commissioner said so himself. I believe that it's worthwhile embarking on such struggles only when you

know that there is a definite advantage at the end of the road. Both experience around the world and economic theory explicitly state that anyone who thinks that a duopoly will lead to perfect competition is wrong. On this question, you can rely on our experience here in Israel.

Just as I have doubts about a duopoly, I also have objections to price controls. Price controls give a lot of authority to a bureaucratic system, and experience does not justify optimism.

Addressing Gilo's comments about prevailing gas pricing, Sheshinski [observed](#):

In my opinion, the goal is to ensure that gas prices in Israel do not differ from those prevailing in similar countries around the world. A revolution in global energy prices is now taking place. The US is becoming the world's largest oil producer, and prices are sliding – for both oil and gas. In my opinion, this trend will persist, and our goal should be not to pay more than the reasonable price in countries whose situation is similar to ours with respect to gas reservoirs.

The crisis created by the summary change in the Consent Decree proposal of December 23, 2014 is reflective of the peculiarities of Israeli anti-trust law, the role of the IAA and the juridical and regulatory mindset of Dr. Gilo, its Director General.

Dr. David Gilo, holds degrees in Economics and the Law from Tel Aviv University and a Doctorate in Legal Science from Harvard Law School. He was an assistant professor at the [US Federal Trade Commission's](#) accountability. He later having a bi-partisan group of five Commissioners appointed by the President and confirmed by the Senate for a seven year term with one Executive Commissioner. The FTC has Bureaus for Consumer Protection, Investment, and conducts pre-merger

clearance under the Hart Scott Rodino Act.

The European Antitrust Review 2015 [revealed](#) the significant expansion of authorities of the IAA since Gilo's assumption of the Director General position. Noteworthy were the following:

The Restrictive Trade Practices Law, 5748-1988 (the Law) and the regulations under it have been amended frequently, adding novel measures to the toolbox of the general director of IAA, enhancing his power and increasing his influence.

For instance, in 2011, the general director acquired the authority to take broad and far-reaching actions against members of a 'concentration group' to prevent harm to competition or to increase competition. This innovative legislation regulates oligopolies and thus expands the scope of the Law, which previously had dealt principally with the 'classic' restraints of trade – restrictive arrangements, monopolies and mergers.

In 2012, the general director gained the authority to impose administrative monetary sanctions in response to certain violations of the Law. Consequently, violation of the Law is not only a civil wrong (and hence exposes the violator to lawsuits) and a criminal act (and hence exposes the violator to penalties), it also bears the risk of considerable administrative fees.

The Israel economy has been fraught with conflicts of interest, reflected in a dual economy, in which the Labor Federation, Histadrut, had historical ownership of economic enterprises including government monopolies. The most relevant example is the Israel Electric Company, which is partially privatized and the sole national power entity. It is embroiled currently in an [embezzlement and corruption case](#) brought against six executives, including a former leader in the Labor Party and a judge. It is alleged bribes were paid by

Siemens to the accused for the tender purchase of infrastructure management systems in the period 2000 to 2001.

The viewpoint of the current IAA Director General Dr. Gilo is reflected in both interviews and articles in the *Global Competition Review*. The October 2014 (*GCR*) [published](#) an interview with Gilo, noting the consumerist slant of his regime:

Since being named director general of IAA in 2011, David Gilo has had the formidable task of leading the authority's enforcement program. A former academic, Gilo has surprised many in the community by his active and sometimes radical approach to his mandate. Speaking to Katy Oglethorpe, he explains why Israel's unique economic and political situation makes extra antitrust attention a necessity, and how the IAA can provide the answer to the high cost of living that plagues its country's consumers.

Ms. Oglethorpe writing in the October 2014 *GCR* [observed](#) about the IAA's questionable overreach as regards Israel's Food Law:

The cost of living is a hot topic in Israel, where the price of food is far above the OECD average. A new Food Law promises to solve these problems through extensive regulation. But the country's antitrust lawyers worry that the new law is excessive in its prohibitions and that in enforcing it, IAA is acting beyond its jurisdiction.

There have been occasions where the IAA's zeal in pursuit of regulatory matters has overreached its legal authority. As indicated in a *GCR* [article](#) on September 2, 2014 an" Israeli Supreme Court decision overturned the Antitrust Authority's bid to stop a company from appealing against the authority's decision to block its merger."

In conclusion, Israel's unique and formidable antitrust regulatory structure and the execution of the IAA authorities by its current Director General present a formidable barrier

to the development of its valuable offshore energy resources. Changes in the IAA's regulatory practice made under Gilo's leadership of IAA reflect possible abuses of power catering to populist consumerist resentment of the high costs of living in Israel. Without relief via legal appeals to Israel's Supreme Court and/or International Arbitration from IAA's proposed Consent Decree the Noble Energy Delek Consortium, its investors and shareholders, and the people of Israel could lose billions of revenues from the energy prize awaiting development in its offshore Exclusive Economic Zone.