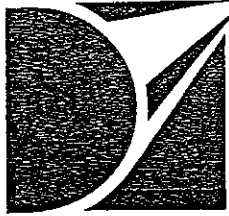


GGT

GOLDFIELDS
G A S
TRANSMISSION

Ref: DAK.ST.NL-0120

13 June 2003

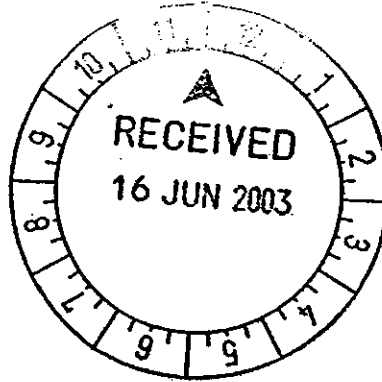
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**CONFIDENTIAL****COPY**

COMMERCIAL IN CONFIDENCE

Dear Dr Michael ^{Ken}

Relative Significance of GGP Transmission Costs

Thank you for the opportunity on 15 April 2003 to present to you the rationale of Goldfields Gas Transmission Pty Ltd (GGT) in making its application for revocation of coverage under the Third Party Access Regime for Natural Gas Pipeline Systems (the Code).

During the presentation, I noted your comment that you were surprised to hear for the first time, that gas transmission tariffs on the Goldfields Gas Pipeline (GGP) represented only a very small fraction of the operating cost of the type of customers mainly serviced by the pipeline.

Obviously this is a critical issue in regard to the outcomes that might be achieved by the ultimate out-working of your decisions in regard to the proposed GGP Access Arrangement. At a higher level, given that the Code affords no greater physical access to the pipeline for third parties than existed prior to its introduction, it goes to the heart of pursuing the economic objectives of National Access Regime, and specifically the Code, in promoting competition and development.

Consequently, GGT wishes to bring to your attention a number of matters relating to the relative operating cost contribution and potential for gas transmission tariffs on the GGP to achieve the objectives of the Code in the specific context of the regional downstream market which the GGP serves.

This subject is discussed in detail in GGT's current application for revocation of coverage before the National Competition Council, publicly available at www.ncc.gov.au. Your attention is drawn specifically to the discussion of the downstream market on pages 23 to 26, as well as the description of GGT's basis for seeking revocation under criterion (a) of section 1.9 of the Code, on pages 29 to 58, which deals with this issue extensively.

I would also like to bring to your attention the fact, as indicated in the attachment to this letter, that this is a matter that has previously been raised in submissions before you. While of course it remains open to your advisers to perform their own calculations in order to verify GGT's position, it might be of assistance to you in the first instance if I supply an example of the basis for our assertions, based on publicly available information.

In its July 2001 submission to the Regulator in response to the GGP Draft Decision, Anaconda Nickel Limited (Anaconda) stated that:

*"For example, we estimate that OffGAR's required tariff reduction will lead to monthly savings to Murrin Murrin of approximately \$250,000."*¹

This statement translates to an estimated annual saving of approximately A\$3 million. The tariff mooted in the Draft Decision represents a reduction of approximately 30%² from the discounted tariff that Anaconda would otherwise be paying. On the basis that a A\$3 million saving results from a 30% tariff cut, the annual gas transport cost for the Murrin Murrin project must be approximately A\$10 million.

On 29 June 2001, Anaconda issued a prospectus to raise new capital in which was provided the following data for the Murrin Murrin project for the first quarter of 2001:³

Nickel produced:	5,714 tonnes
Nickel unit production cost:	US\$ 2.17 / lb

From this information, it can be seen that Murrin Murrin's operating cost for that quarter was approximately US\$27.3 million or approximately A\$54.5 million (based on an exchange rate at the time of approximately A\$ 1.00 = US\$ 0.51). In turn, this translates to an annual operating cost of approximately A\$218 million.

These preceding insights allow us to therefore calculate that Anaconda's total cost of gas transport (i.e. approximately A\$10 million per annum) for the Murrin Murrin project;

- (1) is less than 5% of annual operating cost (i.e. approximately A\$218 million), and
- (2) equates to a contribution to Nickel unit production cost of approximately US\$0.03/lb.

However, even this figure may overstate the significance of gas transport costs in this case for two reasons;

¹ Submission on Access Arrangement Draft Decision Prepared by Anaconda Nickel Limited, July 2001, page 5.

² *ibid*, page 4.

³ Pro-Rata Renounceable Rights Issue Prospectus, Anaconda Nickel Limited, 29 June 2001, page 15.

- (1) the Murrin Murrin plant operated at approximately 50% of nameplate capacity for the first quarter 2001⁴, which means that fixed costs would have made a disproportionately high contribution to overall unit cost, and
- (2) once the past problems plaguing the Murrin Murrin plant are successfully overcome and production is ramped up to a stable level, improved plant efficiency will mean that per-unit gas consumption will fall.

Further, the A\$250,000 per month saving which Anaconda have considered would flow from Draft Decision tariff levels, represents only approximately 1.4% of total Murrin Murrin operating cost.

An operating cost reduction of this magnitude is highly unlikely to sway any major investment decision regarding a capital intensive project such as Murrin Murrin, which has incurred capital costs of over A\$1 billion dollars to date. For the purpose of this analysis, there should be no need to also consider the financial events that have ensued for Anaconda since mid-2001. Suffice to say that in the context at hand, the A\$3 million annual saving to Anaconda which might derive from a tariff reduction as mooted in the GGP Draft Decision, pales into insignificance in comparison to other financial factors, including normal operating, borrowing, hedging and other project costs.

This is not to say that GGT is not cognisant of the need for Australian resource companies to remain in the lower percentiles for production costs in order to be internationally competitive – as indeed, according to their own various statements, they already are. What GGT is asserting however is that what is relevant for the Regulator's considerations under the Code, is the potential and extent to which regulatory outcomes under the Code, contribute to the objectives of the Code. It is in this context that the potential for the outworking of regulatory decisions upon GGT under the Code, must be considered in light of the potential for the gas transmission services offered by the GGP to influence the attainment of the objectives of the Code.

I would hope that the preceding discussion has demonstrated the basis for GGT's assertions regarding its inability to make any meaningful contribution to the cost-competitiveness of the industries that the GGP supplies. However in order to appreciate its relative significance to any potential project similar to Murrin Murrin, gas transport cost should also be considered in the context of fluctuations in commodity prices. Although international gold and copper prices are also volatile (as discussed in GGT's application for revocation, on pages 49 and 50), for the purpose of consistency with the example at hand, let us consider the relative impact of gas transportation cost and nickel price variations.

In the two year period ending 31 July 2001, the nickel price quoted by the London Metals Exchange averaged US\$7,756, or approximately A\$15,200. However, over this same period, the price varied between US\$5,640 per tonne and US\$10,660 per tonne.

The rated capacity of the Murrin Murrin plant (as stated on Anaconda's Internet website) is 45,000 tonnes of nickel per annum. From this we can calculate that the cost saving which Anaconda has stated might be realised from the 30% tariff reduction mooted in the GGP Draft Decision (i.e. approximately A\$3 million per annum) corresponds, in terms of financial impact, to a change in the nickel price of approximately A\$67 per tonne.

⁴ *ibid*, page 14.

In turn, this means that on the basis that the Murrin Murrin plant performed to specification, savings which might be realised from the tariff levels suggested in the GGP Draft Decision would be canceled out by only a 0.44% decline in the price of nickel. This must be compared to an observed 89% fluctuation in the quoted nickel price over only a two year period. Obviously, gas transport costs are a tiny fraction of total operating cost and changes in gas transport costs have miniscule impact on Anaconda's cost structure compared to observed fluctuations in the price of nickel.

From the facts presented above, it is apparent that tariff reductions of the magnitude of those postulated in the GGP Draft Decision offer minimal competitive advantage to Anaconda and are extremely unlikely to influence major investment decisions.

However, Anaconda and others have in the past put forward arguments and assertions to the effect that GGP tariffs are comparatively high for similar long length pipelines. Unfortunately, such claims are founded on a lack of appreciation or recognition of the intrinsic economies of scale which are associated with pipeline construction. While such a failure to come to terms with the nature of a business which is not ones' own is excusable (although perhaps regrettable) in the commercial world, a Regulator of such items of vital infrastructure does not of course enjoy the same luxury.

While you may have already fully informed yourself in other ways on this matter, I would also refer you to the discussion relating to this aspect of tariff determination in specific regard to the GGP in GGT's revocation application, on pages 64 to 71. As it is pertinent to the overall issue of the significance and relativity of gas transportation tariffs in particular regard to the GGP, I enclose for your convenience, the following excerpt from the above referenced text.

"As has previously been identified, once an initial market is established, and sufficient demand develops, it becomes viable to invest in more capital intensive but also, because of improved economies of scale, more efficient forms of energy supply. Given that the demand for energy in the relevant market is, in this case, actually a demand for electricity, it follows a more or less natural evolution of the market that the small scale diesel fuelled power stations will gradually give way to larger scale, cheaper to run, gas fired power plant. If this market grows sufficiently, then initial gas transmission pipeline capacity will be exceeded and new investment will be required for additional capacity. Depending upon the extent of this growth in demand, and the optimism (or far-sightedness) with which the future potential for growth is viewed, it is reasonable to think that later infrastructure investments will be in a position to enjoy much greater economies of scale than the initial market entrants.

It is critical to realise that it is on the strength of just this claim to greater economies of scale that the proponents of the GEMM pipeline can claim to offer the competitively priced gas transportation tariffs which have been cited. To understand this, it is necessary to firstly consider the relative sizes and capacities of the pipelines in question. The following table compares the size and cost (in comparable, "current value" terms) of the pipelines relevant to this application.

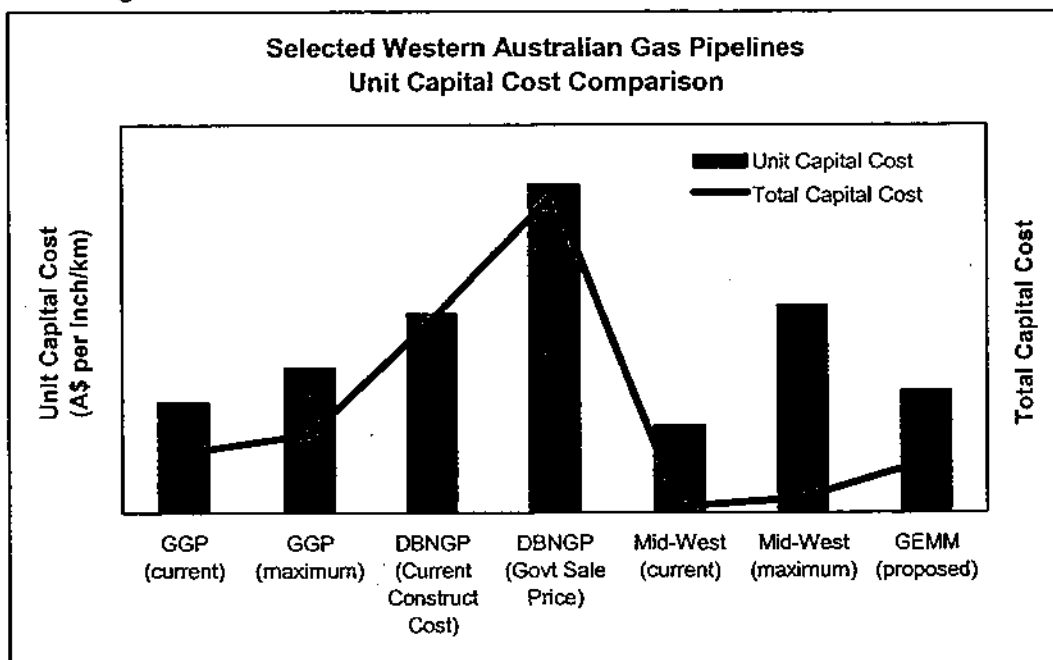
Table 7: Selected W.A. Gas Pipelines Compared

Pipeline	Length	Average Diameter	Capacity	"Current" Build Cost	notes
DBNGP	1399 km	26"	600 TJ/d	A\$1,495m	1
GGT	1378 km	14.8"	100 TJ/d	A\$466m	2
Mid-West	350 km	7.6"	20 TJ/d	A\$48m	3
GEMM	790 km	20"	306 TJ/d	A\$398m	4

- Notes: 1. ref. DBNGP Draft Decision, OffGAR, June 2001.
 2. ref. Updated GGT data (includes Wiluna compressor station)
 3. ref. APT Prospectus, May 2000
 4. ref. "Kick-starting The New Millenium, Developing the Goldfields and Mid-West", Anaconda, December 1999.

Based on publicly available data, the following graph illustrates the relative unit costs of construction associated with these disparate pipelines.

Figure 4.



It can be seen from Figure 4 that the GGP, being a smaller size pipeline than the DBNGP but similar in length, compares favourably on the basis of unit construction cost. This may be largely explained by the fact that the GGP involves physically less steel than the DBNGP and, the pipe diameter being smaller, more linear metres can be transported per load delivered for installation. The Mid-West pipeline, despite being shorter than either the DBNGP or the GGP (and hence enjoying some diminished economy of scale in installation cost), is smaller and had the significant cost advantage of already existing road access, and so enjoyed a lower unit construction cost. The proposed GEMM pipeline, while being shorter than the GGP, has a larger size and hence its unit construction cost is no cheaper than the GGP.

However, this preceding comparison does not provide any insight into the economies of scale inherent in pipeline sizing. This is better illustrated in Figure 5, below, which

shows another view of unit cost, this time taking into account both pipeline capacity as well as length.

Figure 5.

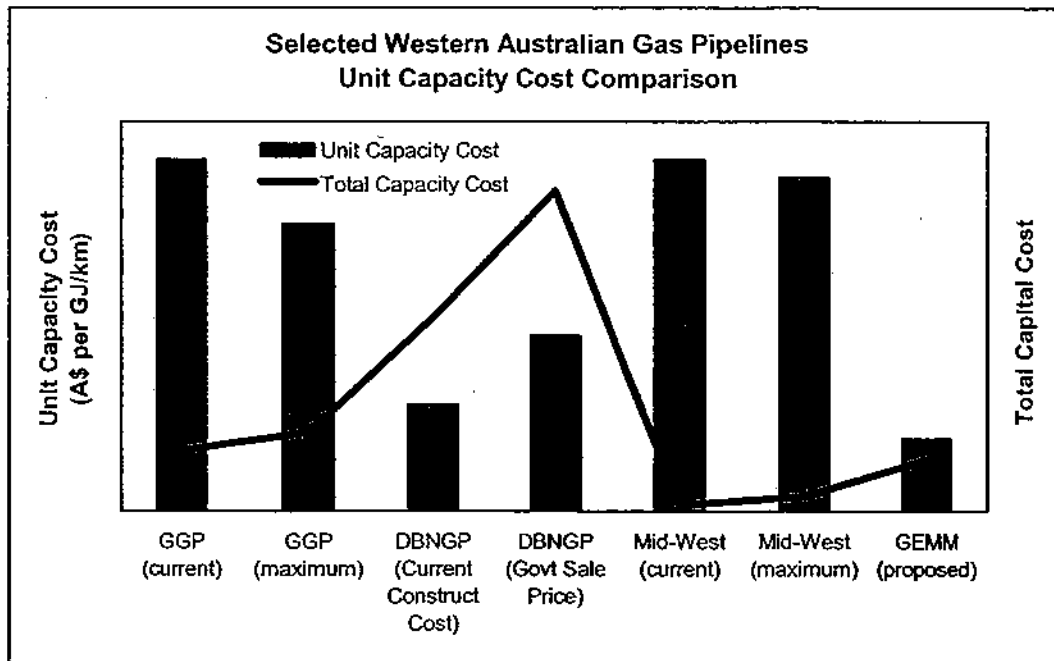


Figure 5 clearly illustrates the basis for claims that it is possible for a new pipeline to provide the gas delivery service to the Goldfields that the GGP currently provides, at a lower tariff. Quite simply, for the same unit capital cost, a bigger capacity pipeline can carry more units of gas and hence, needs to charge less per unit in order to achieve the same return on investment."

It is not GGT's contention that it should have an unconstrained ability to extract monopoly rents from the market which it services. Nor is it GGT's intention to be dismissive of the role and continued potential for the availability of gas to augment industrial growth and regional development. However GGT does maintain that it is critical, particularly for the Regulator given your role in these matters, to understand the scope and nature of the ability and limitations of the GGP in being able to contribute to these objectives and the pro-competitive objectives of the Code.

The GGP is already an open-access pipeline and GGT is engaged in no other business except the transportation of gas belonging to other parties. It is GGT's experience that the gas transmission tariff component of delivered energy cost is unable to significantly influence outcomes in the relevant markets. The viability of regional gas supply is dictated by the economics of lateral capital cost recovery for new projects, and this plus the cost of power plant conversion, for existing projects. (This matter was recently raised and effectively confirmed, in a submission to the NCC on 15 May 2003 by Newmont Australia Limited. As it is relevant to this subject, I enclose as an attachment, GGT's response to the NCC, which contains an analysis of the evidence provided in that submission). The critical issue in both situations (i.e. the decision to use or convert to gas-fired power) is one of preparedness to commit to an investment in capital (either directly or through the transportation contract which must recover the investment underlying it), when faced with all of the uncertainties

which underscore regional resource development. It seems apparent to GGT that the Code is unlikely to produce any outcome, which contributes positively to this situation. One adverse consequence which the Code may have however, is to shift the obligation for funding the investment in gas infrastructure essential to the growth of regional gas supply, from traditional infrastructure investors, onto the potential downstream regional consumers. This would exacerbate an already difficult commercial situation and certainly not serve to further regional development and I would bring to your attention the prospect that a decision of yours under the Code has the potential to have this adverse effect.

If you wish to discuss this matter in greater detail, or any related issue which arises out of this submission, please do not hesitate to contact me.

Yours faithfully



David A King
General Manager

Attachments

- (1) Previous submissions from GGT to Regulator
- (2) GGT Response To NCC on Newmont Submission, 30 May 2003

Attachment 1: Previous Submissions to the Regulator

On the 10 July 2001, in a public submission entitled, "Submission on Supposedly High Tariffs on the Goldfields Gas Pipeline (GGP)", GGT addressed the issue of the relative significance of gas transportation costs in the following terms.

"(2) The relative impact of the transportation component in the delivered cost of gas.

The cost of delivered gas in the Goldfields (as elsewhere in Australia) will vary from customer to customer depending upon the size, duration and nature of the specific contracts into which they enter. Larger corporate businesses will negotiate their own gas supply and transportation contracts, or buy from a Gas Trader whose commission will be included in the delivered cost of the gas.

This variability (as well as commercial confidentiality associated with contracts and the fact that some of these are held by competing companies) makes direct comparison of the tariffs paid by these larger corporate customers within the region and between other regions problematic. However based on publicly available data, GGT has performed its own analysis of the relative contribution of the total cost of gas, and specifically the cost of gas transportation, within the total annual cashflow considerations of a major resource development project serviced by the GGP. For a relatively intensive gas consumer, these figures indicate that the cost of gas transportation represents considerably less than 5% of total operating costs.

At the other end of the customer spectrum, a breakdown of the publicised cost of gas delivered to the average small business or domestic household provides some insight into the relative significance of the cost of gas transportation in the overall price of gas.

According to the new price schedule published by AlintaGas, from 1 July 2001 the price of gas delivered to residential and business customers in Kalgoorlie is 5.86 and 5.22 cents per unit (including GST and the recent 3.5% price rise imposed by AlintaGas). This equates⁵ to a delivered cost of gas of \$16.27/GJ for residential customers and \$14.50/GJ for business customers.

As a rough guide, the price of purchasing gas in the North West Shelf area is around \$2.00/GJ. The current cost (under the published "A4" tariffs) to transport this gas the full length of the GGP to Kalgoorlie is somewhat under \$3.00/GJ, depending upon the specific customer's load factor. The balance of the cost of delivering the gas goes to the local distribution and marketing utility. The following table summarises this breakdown.

Breakdown	Residential Customer		Business Customer	
Gas Purchase	\$ 2.00/GJ	12%	\$ 2.00/GJ	14%
Transportation	\$ 3.00/GJ	18%	\$ 3.00/GJ	21%
AlintaGas	\$11.27/GJ	70%	\$ 9.50/GJ	65%
Total	\$16.27/GJ	100%	\$14.50/GJ	100%

[Note: this table has since been updated to reflect a more conservative estimate of cost of purchasing gas as well as inclusion of the AlintaGas Standing Charge and subsequent annual price indexing. In the updated table, the transportation component of delivered gas price reduces to 15% for residential customers and 17% for business customers – refer page 26 of

⁵ On the basis that one "unit" equates to 1 kilowatt hour, or 3.6 MJ.

GGT's Revocation Application currently before the National Competition Council and available from www.ncc.gov.au].

- (3) That reducing the cost of transporting gas will have any significant effect on the development of new business.

Market evidence, reinforced by the poor response elicited by the recent EDT offered by GGT, indicates that there are no new projects on any scale for which the cost of gas transportation is a critical determinant of viability.

To put the argument in the extreme, even if GGT were able to offer a gas transportation service for free, the evidence available to GGT indicates that this in itself would not precipitate one single new business venture proceeding. The only economic effects that would result would be to increase the profits of existing businesses and a possible loss of business for diesel fuel supply companies and diesel delivery drivers.

Obviously offering to transport gas at no cost is not a commercially viable option, however GGT would be most grateful to hear from the proponent of any new business who considers that the viewpoints offered in this section are erroneous. GGT would welcome the opportunity to explore how it might be able to work cooperatively to contribute to the viability of any new undertaking.

It should be noted that GGT is an open access pipeline and as such, actively seeks to promote and attract new business through offering gas transportation services at prices which are commercially defensible and fair and reasonable."

In its submission of 13 July 2001 to the Regulator, "GGT Public Submission No. 1: Draft Decision for Goldfields Gas Pipeline Access Arrangement", GGT raised the following matters for the Regulator's consideration.

- (1) On page 27:

"Utilisation of Gas Resources

The Regulator states in the Draft Decision (page B189):

the Regulator considers that the conclusion reached by GGT that gas transport markets in the East Pilbara and Goldfields are comparatively price inelastic has not been adequately demonstrated.

During the first and second quarters of 2001, the owner of a major mining project serviced by the GGP has made a series of widely reported public announcements regarding the magnitude of operating costs for that project.

It is apparent from this data that gas transport cost constitutes a small fraction (i.e. a few percent) of the total operating expenditure for that project. Further, the project in question is representative of the mining operations which obtain natural gas supplies via the GGP.

The Regulator has not considered these matters in his Draft Decision and accordingly the Draft Decision does not address the requirements of Section 8.10(h) of the Code."

- (2) On page 50:

"Furthermore, recent commercial initiatives via the offering of an Economic Development Tariff (EDT), representing a marginally priced, incremental-load-dependent, tariff discount on the part of GGT, confirm the assumptions for short term prospects for gas transportation growth on the GGP.

Under this scheme, the more new load committed to by Users, the greater the resulting base to spread the recovery of the largely fixed increment of necessary investment in capacity, and hence the lower the marginal price of transportation that could be offered.

Such an initiative is sanctioned under Tariff Setting Principle 13 of the existing State regulatory regime, although there is no equivalent concept defined under the national Code. (The closest concept being one of "Prudent Discounts" which involve cross-subsidisation between different classes of User).

It should be emphasised that as the EDT was based on marginal pricing, it was entirely dependent upon the volume and duration of additional load evidenced, and as such, cannot be considered to have any wider or more sustainable application than in the context it was offered. In the event, GGT was disappointed that a credible load increase of only a matter of a few percent of the previously contracted base load was committed to.

Information regarding the progress and success of the EDT was made available to the Regulator during the time since the proposed Access Arrangement was submitted. Despite this, the Regulator in the Draft Decision reaches the conclusion that the outcome of the EDT did not demonstrate the inelasticity of resource projects in the East Pilbara and Goldfields to gas transportation costs (page B 189).

GGT finds that the analysis in the Draft Decision is entirely superficial and misleading. The fact is that Goldfields projects have indeed proceeded, they have merely done so without using gas transported via the GGP (ie. they have used diesel instead). Examples are provided in the following list of recently committed developments.

Project	Resource	Approx. Distance from GGP	Approx. Load	When
Bulong	Nickel	30 km	1.5 TJ/day	1999
Tarnoola	Gold	20 km	2.0 TJ/day	99/00
Carusoe Dam	Gold	90 km	2.0 TJ/day	2001
Sons of Gwalia	Gold	20 km	2.5 TJ/day	2000
Granny Smith	Gold	150 km	4.5 TJ/day	01/02
Sunrise Dam	Gold	150 km	3.5 TJ/day	01/02

This effectively demonstrates the nature of the competition which GGT faces. That is, GGT is competing directly with an alternative and non-capital intensive fuel and that delivered gas pricing is not the critical determinant in whether a project proceeds or not, but simply which fuel it will utilise.

GGT is happy to discuss with the Regulator or any other interested party, an example of how small a fraction of total annual end-user cashflow is represented by gas transportation costs, based on publicly available information regarding a representative resource project."

Attachment 2:

**GOLDFIELDS GAS PIPELINE REVOCATION APPLICATION
GOLDFIELDS GAS TRANSMISSION Pty. Ltd.
RESPONSE TO NEWMONT SUBMISSION
30 MAY 2003**

Goldfields Gas Transmission Pty Ltd ("GGT") wishes to make the following submission in response to the public submission made by Newmont Australia limited ("Newmont") to the National Competition Council ("NCC") on 15 May 2003, concerning the application for revocation of coverage of the Goldfields Gas Pipeline ("GGP").

GGT considers that the Newmont submission contains nothing which in effect opposes the arguments made in the GGP Revocation Application. It appears that essentially the Newmont submission distils down to the following argument:

- (i) There is no significant foreseeable scope for load growth on the GGP (pages 15-16), and,
- (ii) What small load growth potential may exist is not represented by new third party load, but expansion of the operations of incumbent customers (page 16) who already have access to the pipeline and current contractual provisions.
- (iii) The present barriers to competition in the relevant energy markets arises due to;
 - (a) the non-viability of gas supply to small, short-lived remote mine sites (page 18),
 - (b) possible restrictions for upstream suppliers to access the GGP via the DBNGP due to constraints on the DBNGP (pages 25-26)⁶,
 - (c) the competitive pricing response of Western Power to the threat of loss of electricity market share, and the evident decision by Western Power to utilise its own facilities for reasons of strategy that have nothing to do with economic rationale (page 17).

It appears to be Newmont's contention that there will be no third party beneficiaries of the application of the National Third Party Access Code for Natural Gas Pipeline Systems (the "Code") when it eventually has effect over the GGP.⁷ Newmont has

⁶ Newmont observe on page 26 that "*At the moment, Epic Energy is not in a position to expend any more capital on looping and the DBNGP is effectively fully loaded.*" What Newmont omit to mention is the reason why Epic Energy is "not in a position to expend any more capital" at the moment. This is due to the effect that the imposition of the Code has had and, following the release by the Western Australian Independent Gas Pipelines Access Regulator (the "Regulator") of his Final Decision regarding the DBNGP, appears set to continue to have. This hardly seems to lend support for the case for coverage of the GGP.

⁷ Noting that in the continued absence of an approved Access Arrangement governing the terms of third party access to the GGP, the Code, whilst "covering" the GGP, has made as yet no contribution to the terms of access which apply to the pipeline.

made an extensive submission to the NCC which presents arguments about purported shortcomings of the Goldfields Gas Pipeline Agreement (the "State Agreement")⁸ and seeks to contradict GGT's statements in regard to market power. However, given Newmont's view about the lack of third party beneficiaries, its submission ultimately appears to merely represent support for a reduction in GGP tariffs for the apparent benefit of existing customers. While this is not the express intention of competition reform, it is also not precluded. However, in the context of the NCC's considerations in regard to the merits or otherwise of coverage of the GGP under the Code, it should be noted that Newmont provide no evidence that access (which is already provided) will be increased by application of the Code when this occurs, or that competition in any market will be promoted.

Further, the submission notes that even such capacity as is presently unutilised on the GGP does not represent "spare" capacity (page 14) - a reference to Newmont's own terms of preferential access as a former owner of the pipeline which are preserved under the terms of its contract. Any additional third party load could therefore only be accommodated by incremental investment in capacity expansion.⁹

In this regard, Newmont states (on page 38) that under section 6 of the Code, the pipeline owners are required to expand capacity to meet the requirements of access seekers, but that under the GGP State Agreement, GGT would be "*compelled to make such extension at the cost of the third party...*". This statement substantially misrepresents the facts in order to claim a reversal of the actual funding requirements under the two regimes. In fact, under sections 3.16 and 6.22 of the Code, the Service Provider can not be compelled to fund capacity expansion, but must meet the capacity needs of an access seeker if the access seeker agrees to fund the expansion (noting also that under the Code, the access seeker is prohibited from ownership of the facility which it has funded). This situation contrasts with clause 20 of the State Agreement, which provides that the onus is upon the pipeline owners to expand capacity, providing only that GGT can not be compelled to fund the cost of a lateral pipeline or its connection to the GGP without its agreement. Even so, GGT is compelled to undertake the connection of any such lateral. There is a significant distinction between capacity expansion of the main trunkline, and the construction of a single-user, dedicated lateral pipeline.

Thus, contrary to Newmont's assertion, the Code (unlike the GGP State Agreement) shifts the obligation to fund expenditure required for additional capacity away from the Service Provider and on to the access seeker.¹⁰ Therefore it might be concluded

⁸ GGT addresses the specific issues in a separate submission.

⁹ Note that Newmont calculates an average tariff and an incremental expansion tariff (pages 11-14) for comparative purposes. However the results are based on certain assumptions derived from the Draft Decision handed down by the Regulator in April 2001 but which has subsequently been effectively withdrawn by the Regulator in November 2002 in admission of errors of law which it contained in common with the Epic Decision in the Supreme Court. The nature of these errors affect the assumptions used by Newmont in their calculations, which also fail to give recognition to the step-wise nature of incremental pipeline capacity expansion. Hence, the average tariffs shown can be misleading and, in any event, do the potential access seeker little good if the capital is unlikely to be available to invest under the regulatory uncertainties and low returns afforded by coverage under the Code.

¹⁰ It might be argued that this difference in the two regulatory philosophies is consistent with the different underlying philosophies regarding permissible rates of return on investment, however this of itself would mean very little to the remotely situated, new access seeker, who must confront the additional

that the outcome sought by Newmont would have as its outworking, a raising of the barriers of entry to potential new market entrants, effectively increasing the market power of the existing users of the GGP within their own field of competition. This stands in direct opposition to the objectives of coverage and GGT requests the NCC to give consideration of these matters in regard to criteria (a) and (d).

On the issue of the extent of GGT's market power and its ability to influence the dependent markets, Newmont describes various aspects of the relevant markets which largely corroborate GGT's own descriptions. However, Newmont interprets the implications of these descriptions to arrive at conclusions that are sometimes contradictory.

For example, in regard to evidence of the incentives which GGT has to exercise market power, Newmont states (on page 28):

"Finally, if transmission charges were insignificant, as GGT claims, in production costs and in decision-making in relation to development of new projects upstream and downstream, then whether or not the pipeline operator was able and willing to exercise its market power might be inconsequential. But this is not the case.

As discussed previously, factors such as mine consumption, cost of conversion of power plants, lateral pipeline costs and remaining mine life affect the decision whether to switch to gas firing."

GGT notes that the discussion in regard to the economic determinants of choice of energy source, Newmont largely reinforces the observations that are included on these issues in the Revocation Application. Despite this, Newmont goes on to state (same page):

"In sites where the distance from the GGP is great or the mine life is short, a small change in the transmitted cost of gas can determine whether it is economic to switch to gas or not."

However, the Newmont submission also includes a particularly informative graph on page 52, with a short analysis on the following page. Of particular interest to the preceding statements is the example provided of a small mine having a life of 5 years, consuming less than 3TJ/d of gas and located 40km from the GGP. This is not a bad example of a reasonably typical situation, however it should be noted (as illustrated in Table 3 on page 25 of the GGP Revocation Application) that mines can have even smaller gas demands and be located considerably further away from the GGP.

It is not uncommon for GGT to be asked to quote on situations where mine life might be only three years, or where the mine proponent cannot be sure that the mine will still be economic in even one year's time, as a consequence of macro effects like reserves depletion or international commodity price volatility. Nonetheless, the example shown provides some insight into the relative magnitude of the impact on

hurdle of having to provide substantial up front capital, the benefits of which will be shared by others, and which were not a cost faced by its competing predecessors.

gas supply economics as a result of the need for even a moderate length lateral pipeline.

Whilst there are a number of assumptions which remain un-stated¹¹ in regard to such potentially significant factors as asset residual values etc, obviously under the correct set of circumstances, a small change in the delivered cost of gas (whether this derives from any or all links in the delivery chain) could marginally affect the total price differential between energy options. However, this is hardly indicative of an abuse of market power by GGT, which in any event, is responsible for only one part of the electricity production process.

For many other examples which might be cited, gas sourced via the GGP could be either more or less economical than the diesel alternative by a considerable margin. In cases where for example the mine is located further away from the GGP, gas will be unable to compete due, as Newmont points out¹², to the prohibitive expense of a lateral. In cases where a prospective customer is closer to the GGP, gas will represent a considerably better economic choice for the user as there will be a significant price advantage. Clearly, this significant advantage in gas fuelled power generation would not exist if GGT were merely pricing just under the cost of alternative sources of power in order to seek to extract monopoly rents.

Curiously, and despite the indications in the preceding graph which shows that for mines of like sized requirements situated close to the GGP, the difference in power costs deriving from gas compared with diesel is in the order of \$90/MWh, Newmont concludes (on page 53) that:

"Because of the dominance of fuel costs in the power cost, quite small changes in the delivered gas cost can change an uneconomic investment into an economic one."

This conflicts somewhat with the evidence put forward by Newmont itself. The fact is that the magnitude of the cost differential for the final delivered cost of electricity, which exists between gas and diesel in this regional electricity market north of Kalgoorlie, is not something over which GGT has discretion. Besides the powerful constraints of GGT's obligations under the State Agreement – including recognition of the checks and balances under the tariff setting principles established by the original owners (including, in a corporate sense, Newmont) – GGT is subject to competitive constraints. This is not restricted to merely being obliged to work within the scope of its intrinsic economic limitations in competition with diesel fuelled power generation, but also due to the electricity market which exists in and around Kalgoorlie. This is discussed throughout the Revocation Application, however Newmont have also

¹¹ The NCC may wish to take up Newmont's offer to supply the details of its calculations in order to verify its own interpretation of the information supplied.

¹² *"Note also that diesel engines and gas turbines can be moved to other locations, but a buried gas pipeline cannot be moved and re-used. Installing a gas pipeline with a useful life of perhaps 70 years for just a few years of operation does not make much common sense [...] The sample case is typical of many sites in WA. In this case, if the mine is new and can buy gas engines or gas turbines, the case for use of gas is marginal and not persuasive. If an existing diesel plant exists (as is most often the case), then the combined capital, operating and fuel costs of a gas fired plant exceed the operating and fuel costs of the diesel plant and no economic case exists."* Newmont, page 53 (with emphasis added).

provided some statements in regard to this market and the competition which exists there (pages 24-25 and 54-55).

Newmont confirms the historic benefits derived from the introduction of cleaner, cheaper competing energy in the market (see in particular page 48). And while it obviously tries to play down the extent of the spare capacity currently available to deliver electricity into the Kalgoorlie region, it nonetheless concedes that there is in the vicinity of 20-40MW of spare competing capacity available (pages 17 and 25). It also estimates that some 8-10TJ/d of spare capacity might be available on the GGP (page 19), although – quite rightfully given its own control over at least part of that capacity – it heavily qualifies the terms upon which this might be made available (pages 11-12 and 19).¹³

Given Newmont's view of the prospects for future demand growth then, it would appear that the electricity transmission system has at least sufficient capacity to meet likely future electricity needs in Kalgoorlie, and that this capacity might be more accessible than that available to GGT in order for it to compete. (Noting that GGT's constraint arises in part from the terms of preferential access to pipeline capacity, which the original owners enjoy as a result of the contracts they devised at the time of the sale of their interests in the pipeline). Despite this, Newmont (on page 24) makes the assertion that:

"The lack of close economic substitutability between gas and other fuels for producing electricity (and heat) suggests that absent coverage by the Code, the extent of any constraint on the pipeline operator from alternative fuels would be limited."

Similarly, on page 51, Newmont state:

"There is not 100-140MW of spare transmission capacity as GGT maintains. Accordingly electricity generated in the South West of Western Australia does not act as a significant constraint on GGT exercising market power."

One might assume then that, in the absence of any competitive constraints, GGT would be free to extract a monopoly rent in the Kalgoorlie electricity market. However, Newmont also notes (page 25) that:

"Even with additional [electrical transmission] capacity, it is questionable whether this alternative would be much of a constraint on GGT as differences in the supply costs based on supply from Western Power would leave GGT with a significant 'gap' over which to exercise its market power."

However, Newmont states elsewhere (page 23), and WMC also confirms,¹⁴ that Western Power has in fact engaged in aggressive competitive price reductions since

¹³ It should be noted that the restrictive terms for the availability of this "spare" capacity described by Newmont, bear no relationship to GGT's own terms of third party access – they reflect the view of a holder of unutilised capacity who has reserved it for possible later use. The discussion also ignores any consideration of the need for prudent operation and capacity management in order to be able to satisfy firm service obligations.

¹⁴ WMC Submission, Appendix by Frontier Economics, 15 May 2003, page 14.

the GGP introduced gas into the market. Newmont also observes (on page 25) that Western Power load growth in Kalgoorlie has continued, despite the supposed price advantage from which GGT is claimed to derive its market power.

The preceding discussions appear to have a central tenet: because it is difficult under certain circumstances for gas to compete with the alternatives, the conclusion is drawn that gas does not compete, from which is derived the assertion that gas faces no competition. Besides the critical flaw in the logic of this argument, within the present context of consideration of the tests for coverage, there have been no arguments made in regard to either the means or scope for enhancing competition or providing any other benefits, which might be in the public interest. If anything, the outcomes sought by Newmont are clearly intended to see it receive a marginal operating cost reduction with no benefits for any party that is not already a gas user, at the expense of future infrastructure investment and genuine third party access.

Conclusion

In summary, the Newmont submission represents an attempt to realise a windfall benefit by a vested incumbent interest, which is quite at odds with the intended outcome of competition reform.

Furthermore, the submission contains no evidence or substantiation of the claims made by Newmont which oppose any of the arguments made in the GGP Revocation Application. While the conclusions that are drawn within the submission are consistently opposed to the grounds cited in the Revocation Application, these conclusions appear often to be at odds with the preceding logic and evidence cited within the submission.

GGT requests the NCC give consideration to the role played by Newmont in the history of the GGP, the nature of the benefits received by it and its corporate predecessors, and its motivation for making a submission to the NCC.

In addition, the NCC is requested to give consideration to the likely consequences for the objectives of the Code and competition reform in general, if the outcomes sought by Newmont (i.e. reduced tariffs for current market incumbents at the expense of past investors and future access seekers) are realised.

Finally, GGT requests the NCC give consideration to the likely effects of the provisions of the State Access Regime and the State Agreement, which exclude the application of the Code to at least a substantial portion of the capacity of the GGP, and the consequential impact upon any cost-benefit analysis of the merits of coverage under the Code.