

3 April 2001

Mr. Robert Pullella
Office of Gas Access Regulation
6th Floor
197 St. George's Terrace
Perth WA 6000

Dear Robert,

HAULAGE CONTRACT – ALINTAGAS SALES / ALINTAGAS NETWORKS

Apache Energy Limited hereby makes a submission to the Office of Gas Access Regulation on the terms and conditions of the proposed AlintaGas Sales Pty Ltd Haulage Contract. This submission may be treated as being in the public domain and we agree to it being placed on the OffGAR website.

In summary, we believe it is open to the Regulator to find that it should refuse to approve the Associate Contract as it would likely have the effect of substantially lessening, preventing or hindering competition in a market.

Indeed, it is our belief that the Gas Distribution System (GDS) charges payable by AlintaGas Sales ("Sales") to date have already served to substantially hinder competition by allowing Sales to price other players out of the market. This is all but admitted in your Issues Paper which states that "the contracted retail price of gas sold by AlintaGas Sales to consumers is too low to accommodate the relevant Reference Tariff". Apache believes there is clear evidence of such pricing practice in recent times. Approval of the proposed Haulage Contract would effectively sanction such arrangements. It is our view that the Haulage Contract could be approved subject to AlintaGas Sales paying Access Arrangement Reference Tariffs, although we are also concerned at the advantages inherent in the non-tariff issues.

On review of the differences between the Haulage Contract and the Access Agreement there are two main areas of difference that give AlintaGas Sales a material competitive advantage over other Users. These are:

1. The formalisation of tariffs at less than the Reference Tariffs; and
2. The provision of terms that provide AlintaGas Sales with improved or more flexible arrangements than are available to third party Users.

Non Tariff Issues

Whilst a number of the changes proposed in the Haulage Contract appear minor, and would be unlikely to constitute substantial competitive advantage to AlintaGas Sales, taken as a whole they provide AlintaGas Sales with more flexibility, longevity and general comfort than those offered to Users under the Access Arrangement. Please see our comments attached.

Tariff Issues

The tariff related issues are critical to the consideration of “a substantial lessening of competition”. There are two main aspects:

1. the ability of Sales to have one contract for all its customers compared to customer by customer contracts required by other Users; and
2. the potential for discounted tariffs.

On the first issue, it is our understanding other Users will be required to enter into an independent Haulage Contract for each and every new sale, rather than provide for a schedule approach as proposed in the Associate Contract. This gives a huge degree of certainty and predictability to Sales compared to another User when negotiating supply. For example, come 2002, another User would be required at face value to enter into 200,000 Haulage Contracts if it were to wish to supply say domestic customers “north of the river”.

With regard to the discounted Reference Tariffs for some services, a number of supply contracts in question were most likely entered into under the Gas Distribution Regulations or in full knowledge of the proposed Access Arrangement, and against competition from other producers. We have previously pointed out to OffGAR the impossibility of competing to supply at the end of the Geraldton and Bunbury Extension “laterals”, given the tariffs for these laterals and the pricing offered by Sales.

With regard to transfer pricing, the neutrality argument may not be correct in that the strict application of the Access Arrangement to every customer in this State would most likely result in significantly increased revenues to AlintaGas Networks. If this transfer pricing does reduce the viability of AlintaGas Sales then it clearly points to the fact that AlintaGas Sales has been receiving a competitive advantage over other Users, confirming it's undue dominance of the market.

The question is not the total profit for AlintaGas Ltd but how the natural monopoly part of the business has supported AlintaGas Sales in continuing to sell at below cost to customers and hence retaining market share where it would not otherwise have done so. AlintaGas Networks is neutral in this in that it continues to receive revenue but AlintaGas Sales is not neutral because the end result may be loss of market share.

These activities (discounted tariffs and cross subsidisation) have substantially lessened competition in the market as other suppliers have not been able to compete as they have not had access to these subsidised tariffs. It is not good enough to say that this practice will cease (in one form or another) at the expiry of these contracts. It must be unwound immediately and AlintaGas Sales be forced to suffer the consequences of it's previous anti-competitive actions.

With regard to the questions raised by OffGAR on this matter in page 6, we make the following comments:

- There are advantages to AlintaGas Sales in revenue transfer from Networks to Sales as this has enabled Sales to maintain market share which it may not otherwise have retained had it been forced to pay full price for access to the network.

- Yes, this has hindered competition in the market and examples can be provided to OffGAR on a confidential basis..
- Making discounted tariffs available to other Users is irrelevant given that AlintaGas Sales already has the contracts. The discounts should not be perpetuated. We have previously raised this issue with respect to the pricing of “transmission pipelines” such as the Geraldton lateral and the extension of the Dampier to Bunbury pipeline south. These are transmission laterals and should be priced accordingly. They are not distribution laterals and the application of distribution pricing to them has distorted the cost of access.

If customers at the end of these laterals were to pay delivered gas prices based upon the Reference Tariffs, they would face substantial price rises despite strong upstream competition in the gas market. This can only have been avoided or will only be avoided by Sales offering pricing to such customers based on discounted tariffs.

- The correct course of action is to correctly price gas transport to the delivery points in question, make that pricing known now and apply that pricing to any renewal of the affected contracts. Until that occurs, AlintaGas Sales should be forced to pay the full tariffs, as per the Access Arrangement. There is a strong argument that this should be retrospective to the time of signing of the contracts in question, taking into account the history of the Access Arrangement and the Gas Distribution Regulations.
- The discounted distribution tariffs should be made public and arguably could form a realistic basis for determining the ongoing tariffs.
- Of course there is a material advantage to AlintaGas Sales by continuing the discounted distribution tariffs. Once again, these tariffs have enabled AlintaGas to acquire and maintain a market share that it may not otherwise have acquired had it been forced to compete on a level playing field.
- Put together as a package, it is clear that the discounted tariffs and the proposal for more flexibility and more comfort under the Associate Contract arrangements will serve to entrench AlintaGas Sales’ position in the market which in turn will substantially lessen competition and prevent or hinder access by other Users to certain of AlintaGas Sales’ customers.

In coming to these conclusions we have considered the differences between the Haulage Contract and the Access Arrangement noted in your Annexure 2 to the Issues Paper. We have summarised our comments on these differences in the attachment to this letter.

Should you wish us to elaborate on any of the points raised in this letter or the attachment, please contact either Rod Lake or myself.

Yours sincerely,

R.G. Stephenson
Marketing Manager – Gas Sales

**APACHE ENERGY LIMITED COMMENTS ON PROPOSED HAULAGE
CONTRACT BETWEEN
ALINTAGAS NETWORKS PTY LTD AND ALINTAGAS SALES PTY LTD**

The clause references shown below refer to the provisions in the Haulage Contract and mirror the comparisons provided in Annexure 2.

Clause 3

The ability of AlintaGas Sales to terminate haulage arrangements at any time gives Sales a distinct advantage in the market compared to its competitors who are obliged to enter into arrangements of at least a year. Further, with no apparent mechanism to adjust the price of non-Reference Tariffs, discounted tariffs would appear to be able to continue indefinitely.

Clause 4

Again the flexibility offered by this clause is not available to competitors under the Access Arrangement. This allows Sales far more flexibility in its arrangements.

Clause 6

While at face value this appears not to have any competitive ramifications it distils the flexibility available to AlintaGas Sales with respect to the previous clauses.

Paragraph 6 (4) (h)

Again this provision arguably gives Sales an advantage over other Users as it can amortise the cost over 20 years rather than a lesser period. Apache's discussions with AlintaGas Networks for new facilities has (correctly) had amortisation over the duration of the proposed haulage contract.

Clause 7

Appears to offer no advantage to Sales.

Clause 8

An Interconnection Contract is a pre-requisite for the granting of a Haulage Contract. Any provisions that provide Sales with certainty compared to a third party User is to the advantage of Sales.

AlintaGas Sales has in the past complicated the granting of an Interconnection Contract by insisting that AlintaGas Networks keeps Sales whole with respect to linepack (supposedly in conformance with AlintaGas Sales' agreements with Epic Energy). There should be a provision in the Access Arrangement that removes the necessity for AlintaGas Sales to influence these matters.

Following on from that, AlintaGas Sales has insisted that if a customer is supplied via the Parmelia pipeline, then the operator of the Parmelia pipeline must provide back-up arrangements to its supply in the case of the failure of the Parmelia pipeline or its facilities. This is patently ridiculous and designed only to exclude third party Users.

Sub Clause 13 (4)

This clause potentially gives AlintaGas Sales an advantage over other Users in that if a third party user requests a pressure higher than 7 kPa, AlintaGas Networks may insist on a new lateral and it's associated costs. If this provision is designed to give flexibility to AlintaGas Sales not open to others then it is to the advantage of AlintaGas Sales.

Sub Clause 14 (1)

In a multi-user environment AlintaGas Sales should be due no more data than other Users. In other words, if AlintaGas Sales can insist on this information then so should a third party User be able to access that information. Information should be transparent to all Users.

Sub Clause (14) (2)

See comments above.

Sub Clause 14 (3)

See comments above.

Clause 15

This is by far the most controversial provision in the Haulage Contract. Despite the assurances that third party Users can in the future access the same (discounted) tariffs as AlintaGas Sales, should supply to the particular customers be renewed, this provision perpetuates the market power given to AlintaGas Sales to sell to a customer below cost.

AlintaGas Sales must, and retrospectively since the release of the Access Arrangement, pay tariffs for services to these customers at the rates and on the conditions under the Access Arrangement. In a number of cases Sales won this business on the basis that third parties could not approach the delivered gas prices offered by Sales because of the terms of the Access Arrangement. This must be unwound immediately and not perpetuated. It is not good enough to now provide for matching terms for contracts that expire sometime in the future.

We believe this is abuse of market power.

Clause 19

Refer to the comments above with regard to supply of sales data.

Clause 20

Whilst these provisions may reflect common practice in the industry the same provisions are not available to other Users under the Access Arrangement. We have no objection in principal to this but once again any such provisions should be available to third party Users or not to AlintaGas Sales.

Sub Clauses 21 (2) to 21 (4)

The question of determination of the higher heating value in particular parts of the network has been under review for a number of years. It is our understanding that technical solutions exist for AlintaGas Networks to determine the heating value in particular sub-networks and apply that to the customers supplied from that sub-network.

AlintaGas Sales should be subject to the same provisions as all other Users. If AlintaGas Networks can use gas quality data to determine higher heating value then it should do so and advise all Users. AlintaGas Sales should not have any particular rights in excess of those available to other Users.

Clause 23

Invoicing at 30 days is at face value no concern.

Clause 27

There are two issues embodied in this requirement. The continuation of a Reference Tariff past the Access Arrangement Period is an advantage to AlintaGas Sales compared to third party Users which will not have such certainty. Secondly, it enables lower Non-Reference Tariffs to be continued past the current Access Arrangement. Please see the comments above with respect to AlintaGas Sales' access to discounted Reference Tariffs.

Clause 28

At face value of no particular concern.

Clauses 59 and 60

This clause appears to give no advantage to AlintaGas Sales but one would question the changes AlintaGas Sales has proposed allowing AlintaGas Networks to assign all or part of its rights or obligations. This appears to override the provisions of the Access Arrangement in that Sales can approve assignment by Networks. It is unclear as to the extent of such assignment. Is it only to the parts of the network supplying AlintaGas Sales or to all parts of the network? If so, this puts third party Users at a distinct disadvantage as the network may be "sold from underneath them". This appears to be a 'Trojan Horse' tactic, as it seems to circumvent the Access Arrangement limitation on assignment.

Clauses 61 and 62

At face value these clauses are standard and as such should also be applied if applicable to other Users under the Access Arrangement. If not, AlintaGas Sales has a degree of comfort by their inclusion not available to third party Users.

Clause 64

No disagreement.

Clause 66

See comments for clause 61 and 62.

Clause 67

Seems to be acceptable.