

**Submission to the Office of Gas Access Regulation
Parmelia Pipeline Ring Fencing Arrangements**

**AlintaGas Trading Division
8 May 2000**

Background

This submission addresses an application by CMS Gas Transmission of Australia ("CMS") that the Office of Gas Access Regulation ("OffGAR") waive ring fencing obligations for the Parmelia pipeline. It is made on behalf of AlintaGas's Trading Division ("AlintaGas"). AlintaGas opposes the waiving of ring fencing obligations for the Parmelia pipeline.

The discussion has been presented in a form that will enable OffGAR to make the submission public. AlintaGas's arguments would be strengthened by providing specific examples that demonstrate CMS's significance as a player in the State's gas industry. AlintaGas will provide such information to OffGAR on a confidential basis if OffGAR considers it necessary to support AlintaGas's case.

General

Ring fencing arrangements help prevent the abuse of a privileged position by the marketing business of an organisation that also owns and operates a pipeline. AlintaGas submits that CMS is a significant gas market participant and as such its gas transportation and marketing businesses should be ring fenced, as required by the National Access Code. If CMS is not ring fenced it will put CMS's marketing business in a privileged position that is not available to its competitors, such as AlintaGas, which compete in the same market but are required to meet the ring fencing requirements of the National Access Code.

Whilst the Parmelia pipeline does not have a large delivery capability in absolute terms relative to the Dampier to Bunbury natural gas pipeline ("DBNGP"), the Parmelia pipeline was not intended to compete in some of the markets that the DBNGP competes. However, the Parmelia pipeline has sufficient capacity that it could, for example, supply all gas demand in the existing metropolitan distribution system (whilst continuing to supply gas to its existing customers).

CMS is currently working with AlintaGas's Distribution Division and Epic Energy to connect the Parmelia pipeline into the metropolitan distribution system. Once this connection is available, CMS or any other user of the Parmelia pipeline, will have the opportunity to utilise the Parmelia pipeline as the transmission pipeline that delivers gas to the approximately 395,000 metropolitan distribution system customers. These are customers that have traditionally been supplied with gas via the DBNGP. Users on the Parmelia pipeline will be direct competitors to users of the DBNGP in supplying metropolitan area demand.

Gas producers in the Perth Basin are at a competitive advantage when compared to producers in the North-West because of the geographic proximity of Perth Basin gas fields to the South-West gas market. Users that are able to negotiate appropriate access to the Parmelia pipeline will be in a strong position to benefit from this geographic proximity. If CMS is not ring fenced there will be no realistic opportunity for marketers such as AlintaGas, which compete with CMS's marketing business, to utilise the Parmelia pipeline. The potential for marketers other than CMS and CMS's associates to access gas supplies from the Perth Basin will, effectively, be unavailable. This reduces the level of competition that would be available through application of the National Access Code.

Whilst connection of the Parmelia pipeline to the metropolitan distribution system will increase CMS's competitiveness, AlintaGas submits that CMS is already a significant player in the State's gas industry. When the Parmelia pipeline was constructed in 1971 it was designed to pass through the major industrial areas in Perth's southern suburbs. Thus, the Parmelia pipeline passes through Canning Vale, Kewdale, Kwinana, O'Connor and Welshpool. These are significant areas of gas demand. CMS is in the unique position of being able to choose not to use the metropolitan distribution system in delivering gas to these areas, allowing CMS to circumvent the government's gas deregulation timetable. This has enabled CMS to compete directly with AlintaGas for the business of both large and small gas customers that are close to the Parmelia pipeline.

AlintaGas contends that to say CMS and the Parmelia pipeline are not significant players in the State's gas industry is incorrect. As far as AlintaGas is aware, CMS has gas transportation arrangements with two of the largest shippers on the DBNGP, in Western Power and Alcoa. In its role as a gas marketer, CMS already supplies gas via the Parmelia pipeline to end users such as Alcoa, Jandakot Wool Scourers, Midland Brick and Western Mining. CMS has also recently won the business, in competition with AlintaGas and possibly others, to supply gas to existing gas customers, being customers that used to be supplied with gas under contract by AlintaGas. The average demand of these existing gas customers is about 8 TJ/day. AlintaGas considers this to be a significant quantity of gas demand relative to the size of the competitive market.

AlintaGas has successfully retained the business of over a dozen other contract customers in the face of strong competition from CMS.

The recent public forum that OffGAR held to consider its draft decision on the proposed AlintaGas metropolitan distribution system Access Arrangement raised a number of concerns. One concern, which prompted a number of questions predominantly from CMS personnel and Perth Basin producers, is the potential for cross-subsidisation of costs between a company's related businesses. The potential for cross-subsidisation increases significantly if a company does not ring fence its related businesses. Cross-subsidisation is inappropriate. AlintaGas submits that this is a further reason to ring fence CMS's marketing and transportation businesses.

CMS is clearly a strong competitor in the gas industry. It should not be afforded a privileged position that is unavailable to its competitors. Specifically, AlintaGas

submits that CMS should be required to ring fence its businesses in accordance with National Access Code expectations.

Issues for Consideration

OffGAR's Issues Paper, released by OffGAR on 26 April 2000, to assist interested parties in making submissions on CMS's application to waive ring fencing obligations, suggests interested parties might like to comment on a number of items. The items are summarised below, together with AlintaGas's comments.

1. The measure used by CMS in asserting it is not a significant player in the State's gas industry.

AlintaGas contends that, rather than using CMS's measure of market significance, a more appropriate measure is the potential for the Parmelia pipeline to supply gas to customers in the South-West. Consideration should be given to likely future outcomes that will increase the competitive position of the Parmelia pipeline. Two such outcomes are the complete deregulation of the gas market by mid 2002 and connection of the Parmelia pipeline to the metropolitan distribution system. These changes will give users of the Parmelia pipeline access to about 395,000 tariff and 250 contract customers. AlintaGas submits that this puts the Parmelia pipeline in a significant market position.

Despite this, AlintaGas contends, as discussed earlier and despite CMS's claims, that CMS is already a significant participant in the State's gas industry.

2. How the gas market has been defined by CMS.

The State's gas industry is an existing industry that is being opened up to competition. A more appropriate measure of market size in such a context than the measure used by CMS might be to define the market as the volume of gas delivered to tariff customers and to contract customers whose contracts are due for renewal during the Access Arrangement period.

3. Whether the measure of significance should be based on actual throughput or capacity.

AlintaGas submits that the Regulator should measure the significance of the Parmelia pipeline by considering the potential market that can be supplied by the Parmelia pipeline. The Parmelia pipeline has the capacity to supply all demand in the metropolitan distribution system together with some major customers in the South-West. This will provide users of the Parmelia pipeline with access to at least 80% of the South-West gas market by volume and 95% of the market by customer numbers that is not committed to long term supply contracts. This is clearly a significant portion of the market

4. Whether CMS is able to influence competition in the market, including upstream and downstream.

As discussed earlier, CMS already has a significant influence on market competition. This will increase once the Parmelia pipeline is connected to the metropolitan distribution system.

5. The potential public benefits in relation to the ring fencing obligations.

AlintaGas submits that the public benefit will be served if the Regulator requires CMS to comply with the ring fencing requirements of the National Access Code. This will engender public confidence that market participants are being treated equally and that the potential for misuse of a privileged position is reduced.

6. Whether a 4.5 year timeframe is appropriate in assessing CMS's costs of compliance.

AlintaGas anticipates that the cost of compliance with ring fencing obligations is predominantly variable. As such, a 4.5 year timeframe is probably reasonable.

7. Whether CMS's proposed confidentiality arrangements are suitable.

AlintaGas considers CMS's proposed confidentiality arrangements to be unsuitable. AlintaGas submits that, for the reasons presented in this submission, CMS should be required to comply with the ring fencing requirements of the National Access Code.

8. Whether CMS's proposals to deal with associated contracts are sufficiently detailed.

AlintaGas considers CMS's proposals to deal with associated contracts are not sufficiently detailed. Once CMS is ring fenced the Regulator must satisfy himself that CMS's associated contracts are acceptable.

Conclusion

AlintaGas submits that CMS is already a significant participant in the State's gas industry. Future developments will result in almost every customer in the South-West having the option to have gas transported on the Parmelia pipeline and have CMS as its gas marketer. As such, CMS's market position will become more significant during the existing Access Arrangement period of the Parmelia pipeline.

AlintaGas submits that the Regulator should require CMS to ring fence its businesses, in compliance with the requirements of the National Access Code. AlintaGas is of the opinion that there is an urgent need for this ring fencing. Until

CMS's businesses are ring fenced, potential users of the Parmelia pipeline, such as AlintaGas, will not have the confidence to contract with CMS for pipeline capacity. This is placing CMS in a privileged position that restricts the competitive benefits and intent of national competition policy in Western Australia.