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17 March 2010

Mr Mike Buckley
General Manager
Network Regulation North Branch
Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601

Dear Mike

PUBLIC VERSION OF 2 FEBRUARY LETTER TO AER

Jemena Gas Networks (NSW) - Revised Access Arrangement - August 2009

Following representations made by Phil Randall of EnergyAdvice on behalf of O-I at the round table forum held in December (and in separate discussions with Gwenda Gleeson) and subsequent review of the notes from that round table as published on the AER website, O-I would like to provide specific responses/feedback to AER in relation to certain aspects of the revised Jemena Gas Networks Access Arrangement (AA) on a commercial-in-confidence basis.

O-I (formerly ACI Glass Packaging) is one of the largest gas users in NSW, operating a glass bottle manufacturing facility at Penrith, in the outer western suburbs of Sydney. The facility consumes in excess of 2 PJ of gas per annum via a continuous 24x7 operation across 4 glass furnaces at the site.

O-I is severely and unfairly impacted by the proposed increase in gas network charges which it would face under the tabled Jemena proposal, which is thus considered unreasonable. For commercial-in-confidence reasons, O-I is not is a position to identify exact cost impact in this public document. However for indicative purposes only, O-I's can advise that its current network charges are in the vicinity of $500,000 pa. Under the Jemena proposal, O-I's charges would increase by almost 70%.

O-I wants to ensure that AER understands both the context and absolute need for AER in its decision on this revised Access Arrangement to address issues related to bypass pricing and separation of trunk and local network assets – and to ensure regulated tariffs are cost reflective.

Cost Reflectivity of Proposed Network Tariffs – O-I's experience

In January 1999, AGL Gas Networks (AGLGN) (then owner of the Jemena NSW gas network) submitted a proposed Access Arrangement to IPART for their approval. The 1999 proposal followed on from the 1997 Access Undertaking and over the following 18 months established the initial capital base and forward tariff structure for the NSW gas network under the September 2000 Access Arrangement.

ACI Glass Packaging engaged the services of EnergyAdvice (then known as GasAdvice) to review the appropriateness or otherwise of the AGLGN's proposed tariffs. In conjunction with a group of other large gas users, a feasibility study was undertaken for the construction of a series of pipelines to be connected to the AGLGN network as bypass pipelines.

In the case of ACI's site at Penrith, AGLGN had proposed a Local Network Unit Charge of \$297.2/GJ.MDQ.pa.

The bypass feasibility study incorporated the design and costing of a pipeline which connected to the trunk pipeline at Schofields (north of Horsley Park). This particular pipeline proposed to connect to only three sites – CSR at Schofields, ACI at Penrith and Crane Enfield at Penrith. The analysis concluded that an appropriate bypass rate (under this standalone pipeline) would be \$86/GJ.MDQ.pa. Following representations to AGLGN (who were led in those negotiations by Alf Rapisarda), AGLGN and ACI concluded the signing of a ten year transportation agreement under which the negotiated local network rate was reflective of appropriate distribution costs to the facility.

Full details of the bypass studies were provided in submissions to IPART to verify the basis of the pipeline cost structures and the resultant charge rates – which were set to reflect the cost of a standalone pipeline for those sites only.

The approved regulated charges for the site under both the September 2000 Access Arrangement and the June 2005 Access Arrangement were actually lower than the standalone bypass rate. One would expect that to be the case given recognition that the appropriate cost reflective tariffs for AGLGN under the Access Arrangements would be based on supply to all users in the region, not just to three sites only.

Jemena's Proposed Tariffs

As noted above, under the Jemena proposal, O-I's charges would increase by almost 70%. Over the period of the Access Arrangement, the increased cost impact on O-I is between \$1.5 and \$2.0 million. Particularly based on the background, studies undertaken and negotiations conducted with AGLGN and via the IPART processes over the past ten years, this proposed increase is totally unreasonable and unjustified.

Comments at Round Table on December 11

O-I wishes to make the following observations in relation to the AER notes from the Round Table held on 11 December published on your website:

Quote from AER Notes	**Response**
"MB [Mike Buckley] noted that we are mapping the existing access arrangement and what is proposed against the rules and the cost of providing services. The tariff classes need to be economic and reflect cost." (page 2 last paragraph)	The proposed tariff structure is in no way cost reflective – refer our comments above in relation to O-I's own experience re bypass costs.
"Jemena has had preliminary discussions with customers regarding the first response tariff." (page 3, section 5.2)	O-I consumes in excess of 2 PJ of gas per annum, making it one of the ten largest users in the State. Jemena has not made any such contact with O-I in relation to first response. In any event, O-I – as a continuous furnace operation – would not be in a position to curtail at short notice without significant damage to our furnaces.

"AR [Alf Rapisarda] noted that partial bypass of the network was not a logical option from a technical or commercial perspective (i.e. any bypass to a customer site would be a complete bypass of the network) and hence the issue of a single price or separate prices was not related to the issue of potential bypass." (page 4, last sentence)	It is difficult to understand how Alf Rapisarda could argue that partial bypass was not logical from a commercial perspective. It was Alf Rapisarda who led the commercial negotiations with O-I/ACI in 1999 for a negotiated local network tariff which reflected partial bypass of the network.
"AR also noted that even if a separate price was retained for the trunk and local network, the total price will be the same and the current access arrangement only provides this as a bundled reference service." (page 5, first sentence)	This is incorrect. O-I would refer AER to section 2.9 Negotiated Services of the current Access Arrangement, which makes it quite clear that separation of these services will be provided via a standalone trunk negotiated services offered on comparable terms and conditions as the equivalent trunk reference service.
"PR [Phil Randall] noted that the huge decrease in network pricing over time was about IPART requiring AGL to be cost reflective. AR [Alf Rapisarda] stated this was not correct because overall it is cost reflective." (page 5, 3rd paragraph)	Not sure how to interpret this note. Overall it is cost reflective because IPART required network pricing to be cost reflective, as per the outcome in O-I's experience re charges to the Penrith site.

O-I intends to closely evaluate the AER Draft Decision to ensure the outcome is fair and cost reflective, and we give notice of our intention to participate at the proposed Public Forum after the Draft Decision.
We trust that the AER recognises the importance of this matter to our business. We have been active throughout the period of IPART's regulatory processes to date – including challenging unreasonable positions tabled by the incumbent service provider – and will maintain a strong and active participation to ensure the interest of gas users are being appropriately represented and protected through these regulatory processes.

O-I would welcome the opportunity to further discuss this submission directly with AER.

Yours faithfully

Neil Cooper
Chief Financial Officer
O-I

cc: Phil Randall
Managing Director
EnergyAdvice Pty Ltd