



Australian Paper

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29 June 2007

Steve Edwell
Chairman
Australian Energy Regulator
GPO Box 520
Melbourne VIC 3001

Dear Steve,

Re: GasNet Australia Access Arrangement Review

I am writing to you in respect of the above review to highlight a number of matters that are of crucial importance to our business, Australian Paper.

Background

Australian Paper is member of the PaperlinX group, a leading international marketer and a leading Australian manufacturer of fine communication papers and high performance packaging papers.

Maryvale Paper Mill

The Maryvale Mill was built in 1937, but has been upgraded periodically over the years to improve efficiency and environmental. This mill can produce more than 500,000 tonnes of paper every year.

Maryvale Mill was converted from coal firing to gas in 1981 as part of a long-term investment to the Australian paper industry. The Mill now uses three main energy sources:

- natural gas;
- electricity from the Victorian grid; and
- wood waste from the pulp mills.

The mill meets almost half of its steam requirements and one-third of its electrical requirements by burning pulping residues.

However, and most importantly for the above review, the Maryvale Paper Mill is connected directly to the GasNet gas transmission pipeline and is the largest single industrial consumer of gas in Victoria.

GasNet Australia Access Arrangement Review

Australian Paper became aware of this review on Monday 18 June on receipt of preliminary advice from our energy retailer that the total annual cost of gas would increase from 1 January 2008. This increase was attributed by our retailer to changes in gas transmission tariffs proposed by GasNet in a recent submission to the AER.

We have subsequently established that the increase in total gas transmission charges proposed would be some 160%, from approximately \$0.4 million currently to over \$1.0m in 2008.

We have also obtained copies of the GasNet Australia proposals and the AER's related Issues Paper dated 28 May 2007. However, we have had insufficient time to review these documents, understand their content, analyse the impact of GasNet's proposals on our business and formulate a credible response.

We also note that you have nominated a deadline for comments on the Issues Paper of 29 June 2007. Australian Paper has no capacity to respond in a sensible and constructive manner to such important matters is so short a timeframe. We are currently investigating options to respond to the GasNet submission and your Issues Paper, but we are not likely to be in a position to respond in detail until the end of July.

Australian Paper's initial response

While we are unable to formulate a detailed response to matters of substance, it is clear that the following issues must be considered by the AER as a high priority for this review.

GasNet's breach of process

On receipt of advice from our energy retailer, Australian Paper contacted GasNet Australia in an effort to establish why no attempt was made to communicate the proposed changes to its largest industrial customer. Such a courtesy was offered by GasNet's previous owners in the lead up to the 2002 transmission revenue review. In short, GasNet's regulatory manager advised that the information had been communicated to retailers; and GasNet had no obligation to deal with gas users.

We believe it would have been useful if GasNet had communicated its proposals directly to Australian Paper. A similar opportunity should also have been offered to other large customers. GasNet's failure to do so is a classic display of indifference and monopoly behaviour that should be of concern to the AER.

Lack of justification for price increase

Our preliminary examination of the GasNet documents has led us to conclude that the proposals contain no rationale for the proposed increases to Australian Paper's transmission changes that could be considered fair and reasonable.

In 2006-07, the Maryvale Mill consumed some 7.52 PJ of gas at an average Load Factor of 99%. Similar load profiles have occurred throughout the last 5 years, and were being anticipated for the next 5 years.

That is, Australian Paper has not significantly changed its gas consumption profile over the last 5 years; and had no plans for any significant change over the next 5 years. On that basis alone, it is not possible to understand how Australian Paper could have contributed to any increase in GasNet's costs that would justify increases of the magnitude proposed.

Confused economic signals

Our preliminary understanding of material in the GasNet proposals is that major cost drivers for GasNet's business are linked to increasing demand from gas-fired thermal power stations. If that is the case, it would seem both prudent and rational for GasNet to allocate those costs to the parties that cause the cost drivers. This would send better pricing signals to generators and produce a more equitable outcome for other users.

Detrimental impact on Australian Paper

There is no doubt that the GasNet proposal represent a substantial impost against Australian Paper's business.

Australian Paper operates in a competitive market against imports from lower cost businesses in Asia and elsewhere. The business has limited capacity to pass on increased costs, much less increases of the magnitude proposed. Australian Paper's long term survival depends on finding continuous productive improvements and cost reductions in all aspects of its business.

As Victoria's largest single industrial gas user, Australian Paper expects its energy retailer and GasNet to find better and more efficient ways to operate their businesses – to our mutual benefit.

Preliminary advice of intention to appeal an adverse decision by the AER

Australian Paper understands that the gas Code provides opportunities for aggrieved parties to appeal decisions of the AER. We also understand that such appeals can be complex, costly and time consuming – and require significant commitment of time and resources. However, the potential impact of GasNet's proposals is so severe that, if accepted by the AER, we would have no option but to lodge an appeal.

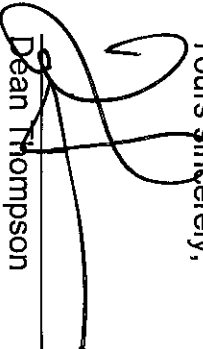
Next steps

It will take several weeks for Australian Paper to engage resources to assist our understanding of the GasNet Australia proposals and develop a considered response.

In the meantime, I would appreciate an opportunity to discuss our concerns with you and your senior staff. The objectives for this meeting would be to ensure that our position is understood by your office, that we can develop an understanding of your processes and timeline and explore what we can do to provide information that would assist your deliberations.

I would appreciate it if you could arrange a convenient time for me to meet with you within the next week or so.

Yours sincerely,



Dean Thompson
Procurement Manager
Australian Paper