

GUIDELINES FOR PROPER GAS TRADE

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Fair Trade Commission

and

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Table of Contents

- Part 1 Necessity and Structure of The Guidelines for Proper Gas Trade
 - 1. Necessity of the Guidelines
 - 2. Structure of the Guidelines
- Part 2 Guidelines for Proper Gas Trade
 - I. Proper Gas Trade in the Deregulated Retail Sector (Large-Scale Supply and Specific Large-Scale Gas Supply)
 - 1. Large-Scale Supply by General Gas Companies, etc.
 - (1) Viewpoint
 - (2) Desirable Trade Practices and Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition
 - A. Desirable Trade Practices from the Standpoint of Fair and Effective Competition
 - B. Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition
 - (a) Unjustifiably Low Pricing
 - (b) Setting of an Unreasonably High Gas Price, etc. for Bridging Supply
 - (c) Imposing of Unreasonably High Cancellation Penalties
 - (d) Combined Acts for Impeding New Entries
 - (e) Provision of Equipment, etc. without Charge
 - (f) Suspension of Commodity Purchase and Service Trade
 - (g) Provision of False Information to Users
 - (h) Exploitation of Dominant Bargaining Position in Other Business Fields
 - 2. Specific Large-scale Supply by Community Gas Suppliers
 - (1) Viewpoint

- (2) Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition
- II. Proper Gas Trade in the Consignment Supply Sector
 - 1. Viewpoint
 - 2. Desirable Trade Practices and Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition
 - (1) Prohibition on Uses of Information for Other Purposes
 - A. Desirable Trade Practices from the Standpoint of Fair and Effective Competition
 - B. Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition
 - (2) Prohibition on Discriminatory Treatment
 - A. Desirable Trade Practices from the Standpoint of Fair and Effective Competition
 - B. Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition
 - (3) Handing of Services Incidental to Consignment Supply
 - A. Desirable Trade Practice from the Standpoint of Fair and Effective Competition
 - B. Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition
- III. Proper Gas Trade in the Wholesale Sector
 - 1. Viewpoint
 - 2. Desirable Trade Practices and Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition
 - (1) Desirable Trade Practices from the Standpoint of Fair and Effective Competition
 - (2) Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition
 - (a) Unjustifiably High Pricing ,etc.by Means of Refusal to Deal or Suggest to Do So
 - (b) Dealing on Unreasonable Restrictive Terms, etc.
- IV. Proper Gas Trade in the Regulated Retail Sector (Optional rule)
 - 1. Viewpoint
 - 2. Desirable Trade Practices and Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition

- (1) Desirable Trade Practices from the Standpoint of Fair and Effective Competition
 - (2) Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition
 - (a) Pricing that Does Not Lead to Appropriate Cost Recovery
 - (b) Unjustifiable Discriminatory Treatment Among Users
 - (c) Other Case
- V. Proper Gas Trade Concerning Use of LNG Stations by Third Parties
1. Viewpoint
 2. Desirable Trade Practices from the Standpoint of Fair and Effective Competition
 3. Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition

Part 1 Necessity and Structure of the Guidelines for Proper Gas Trade

1. Necessity of the Guidelines

(1) In the general gas business, the business regulations such as fee control, compulsory supply and accounting regulations, under the Gas Utility Industry Law have been managed to address the harmful effect of the regionally monopolized supply through conduits.

Recently, two amendments to the Gas Utility Industry Law in 1994 and 1999 deregulated gas supply services to large scale users with annual contracted volume of one million cubic meters or more. In addition, they obliged certain general gas companies, namely the Tokyo Gas Co., Ltd., the Osaka Gas Co., Ltd., the Toho Gas Co., Ltd. and the Saibu Gas Co., Ltd., to submit and publish their terms and conditions concerning the consignment supply of gas using existing conduits for large-scale supply by new market entrants. This was designed to encourage competition in the large-scale supply market. In the regulated retail sector, the optional rule which allowed users to choose other terms and conditions was introduced and the approval regulation on supply conditions including wholesale supply prices was deregulated to the notification system. These new measures were designed to bolster competition in the gas market.

(2) The community gas business was also subject to regulations similar to those for the general gas business, to address the harmful effect of monopolized supply. The revised Gas Utility Industry Law in 1999 abolished regulations on supply conditions in the community gas business, including the price of specific large-scale gas supply (to users with an annual contracted volume of 1,000 cubic meters or more) and introduced the optional rule which allowed users to choose other terms and conditions in the regulated retail sector. These measures were designed to bolster competition in the gas market.

(3) As the amended Gas Utility Industry Law came into effect in April 2004, the scope of the consignment supply operators was expanded to the general gas companies and the other gas companies which operate gas supply through specific conduits maintained and controlled on their own (hereinafter referred to as “gas conduit companies”) as well as all general gas suppliers. As measures for ensuring neutral

and transparent consignment supply, it stipulated a new regulation on accounting adjustments and prohibitions on uses of information for other purpose obtained by the consignment supply and discriminatory treatment on the services.

The recent enactment of the amended Gas Utility Industry Law and related laws and ordinances stipulates the following changes: First, the scope of large-scale supply was expanded by relaxing the annual contract volume requirement from one million cubic meters or more down to that of 0.5 million or more. Second, the regulation over the large-scale supply was shifted from the license system to the notification system where ex post suspend and change order for supply may be introduced upon needed. And third, the access obligation of the consignment supply is now applicable not only to gas business for large-scale supply but also to that for wholesale supply. At the same time, the notification requirement for wholesale supply was abolished. These measures are designed to promote further competition in the large-scale gas supply market as well as in the wholesale gas market.

(4) But although progresses were made in the system reform at the gas market such as the entry of new companies and reduced gas charges to some extent, the gas market still has the characteristics as described below. There remains some concern that the principle of competition may not fully work in the gas market if the implementation of the measures established by the recent system reform at the market is not appropriate:

- (a) In terms of gas supply through conduits, the general gas companies still hold large market shares in their respective service areas,
- (b) In some districts, it is difficult to install new conduit networks in addition to the existing networks, and
- (c) While the general gas companies are shifting their supply to high calorie gas, there are limited sources of liquefied natural gas (LNG) and natural gas which are major raw materials of those gases.

There are other concerns that the general gas companies may differentiate among users in their transaction and have pricing with an adverse effect on general consumers during competition with other energies.

Four years have passed since the amended Gas Utility Industry Law was enacted in 1999. Some business activities of the general gas companies are considered to restrict competition. These include some activities that were not prescribed in the existing Guidelines or envisioned in the past institutional changes.

Meanwhile, the gas market is witnessing the increasing number of new entrants which have monopoly positions in other industries. The possibility can not be denied that these new entrants take advantage of these monopoly positions to interfere fair competition in the gas market.

- (5) These problems may be addressed by ex-ante or ex-post regulations under the Gas Utility Industry Law. To ensure impartiality and transparency of the consignment supply, the amended Gas Utility Industry Law sets out for the first time regulations on the activities of companies engaged in consignment supply. Before everything, effective enforcement of the regulations will be needed for the sound development of the overall gas market and bolstering competition among companies. The expansion of the liberalization in the gas market has raised demand for the appropriate measures in order to ensure greater competition and fair trade in the gas market where the trading systems established by the system reform were put into effect. It is possible that the Gas Utility Industry Law alone will not be enough to live up to the demand.

To address the concern, some may argue that the Antimonopoly Act should play its role. However, the law is basically designed to regulate acts that restrict competition. It may not adequately serve to proactively transform the gas market into more competitive one.

The objectives of the system reform at the gas market was originally aimed at ensuring independence in the gas company management and greater efficiency in the gas industry through market competition which serve for the promotion of users welfare. To achieve these goals, it is essential to clarify the guidelines stipulating the acts that cause problems under the Antimonopoly Act and the criteria of issuing suspend and change order for supply under the Gas Utility Industry Law and further, to provide guidelines for the appropriate trade in gas market that are consistent with the Gas Utility Industry Law and the Antimonopoly Act.

The guidelines will specify the areas in which gas market participants can operate their business independently to the maximum extent. By presenting the Guidelines, it may not be necessary to exercise direct administrative intervention against any act infringing the Gas Utility Industry Law and the Antimonopoly Act but to establish a market environment in which participants can enjoy their business with confidence in economic transactions.

- (6) To achieve these objectives, the Ministry of Economy, Trade and Industry responsible

for implementing the Gas Utility Industry Law and the Fair Trade Commission responsible for implementing the Antimonopoly Act bear responsibility in their jurisdiction and collaborate with each other to prepare guidelines concerning proper gas trade that are consistent with the two laws.

(7) In preparing the Guidelines, the following basic principles were laid:

(a) Provide specific interpretation based on the likely questionable cases and specific concerns actually expressed in the Guidelines so that this Guidelines itself will be regarded as a signal to market participants.

(b) Given that the principle of competition has yet to be introduced to the gas trade, it is difficult to predict all possible acts in advance. Provide possible acts of gas companies envisaged at an early stage of the market reform and actual cases consulted at the authorities after the reform.

Given that the market structure is changing dynamically and related system reforms may be foreseen, the Guidelines will also be subject to be changed accordingly as necessary.

(8) The Fair Trade Commission and the Ministry of Economy, Trade and Industry formulated basic rules concerning the prohibition of information usage for other objectives and discriminatory treatment in connection with consignment supply set out by the amended Gas Utility Industry Law. Based on the past cases consulted at the authorities, they hereby supplemented and enhanced the Guidelines for the Proper Gas Trade in order to present what constitutes appropriate gas trade more specifically and clearly.

2. Structure of the Guidelines

(1) The Guidelines categorizes the whole gas trade into five fields: (a) deregulated retail sector (large-scale supply and specific large-scale gas supply), (b) consignment supply sector, (c) wholesale sector, (d) retail supply sector (optional rule) and (e) use of LNG station by third parties. Each part of the Guidelines consists of the followings:

A. Basic views shall be clearly indicated at the viewpoint parts, and

B. In the following parts, the Guidelines provide for acts that are desirable for companies to voluntarily carry out to ensure competition in each field of the gas market mentioned above. They also introduce some acts of gas companies that

may cause questions under the Gas Utility Industry Law or the Antimonopoly Act, and show examples of acts away from infringement of any of these laws in certain cases.

- (2) Furthermore, with regard to the interpretation of individual cases, individual judgment will be sought to conform practices to the actual situation of the market structure or trade practices; it is therefore difficult to exhaustively indicate all of these cases in advance. Accordingly, in the event that problems or disputes occur, they should be dealt with case-by-case according to the basic principles and content stipulated at the Guidelines. The accumulation of such judgments expectedly contributes to further clarification of the Guidelines.

Part 2 Guidelines for Proper Gas Trade

I. Proper Gas Trade in the Deregulated Retail Sector(Large-Scale Supply, Including Specific Large-Scale Gas Supply)

1. Large-Scale Supply by General Gas Companies, etc.

(1) Viewpoint

With respect to the gas users in the deregulated area, in principle the Gas Utility Industry Law does not impose any regulation on supply conditions for general gas companies. This comes from the idea that gas energy will be effectively supplied if the existing general gas companies effectively compete with new entrants that own LNG and other supply sources and with other companies that supply competing energies such as oil and liquefied petroleum gas.

In this competitive market, the general gas companies have basically full discretion in not trading with users with whom they do not agree on the trading conditions such as prices and services, and in setting prices and supply conditions according to the actual situation of gas use.

But as far as gas supply through conduits is concerned, the general gas companies with conduit networks still hold large market shares in their service areas. They should take appropriate measures in accordance with the following principles to ensure fair and effective competition. In the same way, the gas conduit companies and the large-scale gas companies are also expected to take appropriate measures.

(2) Desirable Trade Practices and Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition

A. Desirable Trade Practices from the Standpoint of Fair and Effective Competition

For fair and effective competition, the general gas companies should widely publish their average price based on a reasonable method of calculation and their standard price in terms of a large-scale supply service.

B. Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition

(a) Unjustifiably Low Pricing

Unjustifiably low pricing may constitute a violation of the Antimonopoly Act if a general gas company proposes an excessively low price solely to large-scale users with whom new market entrants are negotiating to hamper their business activities (private monopolization, unjust low price sales).

Nevertheless, it does not in principle constitute an infringement of the Antimonopoly Act to set a price that is not below the cost of supply to users on the basis of in-depth surveys of the actual consumption situation of individual large-scale users.

(Note) If a company reduces its prices in competition with its rivals to attract users, this price reduction is a proper outcome of competition. It is often seen in usual business activities and it does not constitute any problem by itself under the Antimonopoly Act.

However, if a company with a dominant bargaining position in its service area, such as a general gas company, offers a favorable price that is significantly lower than the supply cost to a substantial part of users aiming at maintaining the existing contract with the users from a new entrant with an effective cost performance who is negotiating or expected to do so with them, then this act may hinder the business activities of the new entrant. This may constitute violation of the Antimonopoly Act.

If a general gas company supplies to large-scale users at a lower price that incurs

deficit in its large scale supply business, such act will be regarded to harm the interests of other gas users than the large-scale users. The act will likely to be subject to a corrective action under the Gas Utility Industry Law (the Gas Utility Industry Law Section 25-2(2)).

(b) Setting of an Unreasonably High Gas Price, etc. for Bridging Supply

If a general gas company, in response to a request for bridging supply (Note), refuses to conclude an agreement without due cause, imposes an unreasonable higher price than to the prices for other users in alike supply conditions or imposes unjustifiably disadvantageous conditions, it is assumed to be infringing the Antimonopoly Act given that it obliges the user to have gas supplied from the general gas company in question which activity impedes the business activities of new entrants (refusal to deal, discriminatory pricing, discriminatory treatment, etc.).

(Note) Bridging supply refers to the supply of a general gas company to a user who is switching its supplier to a new entrant until the new entrant is ready to supply gas, in a case in which the new entrant is not able to supply gas immediately after termination of the existing agreement with the general gas company due to the preparations for market entry.

(c) Imposing of Unreasonably High Cancellation Penalties

In principle, it is the management decision of gas companies to determine the agreement period with users and the penalties for cancellation prior to expiration of the agreement.

However, if a general gas company collects unjustifiably high penalties from a user who wishes to cancel the existing agreement to receive gas supply from a new entrant and the user is forced to withdraw an agreement with the new entrant, such act is likely to be in violation of the Antimonopoly Act (dealing on restrictive terms, dealing on exclusive terms, etc.)

(d) Combined Acts for Impeding New Entries

If a general gas company with a monopolistic position in the retail market in its

service area conduct combination of acts, such as termination of an existing agreement with a large-scale user who is negotiating with a new entrant, gas prices slashing to compete with a new entrant and conclusion of a new long-term contract with cancellation penalty provisions resulting in interfering the business activities of the new entrant, it is likely to be in violation of the Antimonopoly Act (private monopolization, interference with a competitor's transaction, etc.).

(e) Provision of Equipment, etc. without Charge

In principle, general gas companies manage their business operation in the large-scale supply service by their own decision. If they offer the users to provide equipment which is assumed to be paid for without charge, it will not cause a problem under the Gas Utility Industry Law as long as the cost of the equipment is appropriately covered in the large-scale supply business.

However, any conducts of enticing any prospective user into a transaction with the gas company by offering an unreasonable benefit in light of normal business practices, such as offering equipment without charge which would normally be paid for, is likely to be in violation of the Antimonopoly Act (customer inducement by unjust benefits).

(f) Suspension of Commodity Purchase and Service Trade

If a general gas company suspends the purchase of commodities or services or the reduction of the trade volume, etc. or suggests to do so with the users (such as business operators engaged in manufacturing, installation or sales of gas conduits or other infrastructure equipment indispensable to gas supply business) with whom it has business relationship with respect to those commodities and services, in a case where the users intend to receive supply from a new entrant, it will cause for the users to withdraw the contract with the new entrant. It is likely to be in violation of the Antimonopoly Act. (dealing on exclusive terms, etc.).

(g) Provision of False Information to Users

If a general gas company provides users with false information, for example by claiming that new entrants do not have enough maintenance capabilities for gas safety, in their business activities, it will cause the impediment of trade between

new entrants and users. It is likely to be in violation of the Antimonopoly Act (interference with a competitor's transaction).

(h) Exploitation of Dominant Bargaining Position in Other Business Fields

If a company which has a monopolistic position in another business area makes use of this position to provide advantages or disadvantages to users or suggest to do so in a bid to make the business in the gas market more favorable to it, it is likely to be in violation of the Antimonopoly Act given that it may cause difficulties for other gas companies to conduct their business activities (customer inducement by unjust benefits, forced trade, etc.).

2. Specific Large-Scale Gas Supply by Community Gas Companies

(1) Viewpoint

Community gas companies are in a competitive relationship with liquefied petroleum gas companies that supply the gas whose standard is same to that of the community gas companies filled in gas cylinders. In consideration of this competitive relationship, the sector of specific large-scale gas suppliers was deregulated by the amendment of the Gas Utility Industry Law in 1999. The reduction of gas charges in competition with rivals in this sector to attract customers should be regarded as the natural outcome of competition and should in principle be left to an autonomy of operators.

(2) Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition

If a community gas company supplies gas to users belonging to the supply point where certain specific large scale users also belongs at a price below cost in the sector of specific large-scale gas supply, then that company concerned is likely to face an order for corrective action under the Gas Utility Industry Law given that this act harms the interest of gas users other than those concerned with specific large-scale users (the Gas Utility Industry Law Section 25-2(2) applied by Section 37-7 of the law).

II. Proper Gas Trade in the Consignment Supply Sector

1. Viewpoint

To encourage new market entries and ensure fair competitive conditions among gas companies, it is essential to ensure social credibility in impartiality and transparency in the use of conduit networks. For this purpose, the items listed in Section 22-4 (1) of the amended Gas Utility Industry Law, including a case in which it is applied by Section 37-8, stipulate prohibition on general gas companies and gas conduit companies (referred to as “general gas companies, etc.” in this chapter) from making any use of information for other purposes and from applying discriminatory treatment in connection with contract supply.

As for conducts that are prohibited in association with consignment supply, the Guidelines are expected to deter prohibited acts effectively by describing desirable conducts and conducts which may cause problems and clarifying the criteria for issuing cease orders from the viewpoint of the transparent implementation of provisions and promotion of fair and effective competition.

(Note) Under the Gas Utility Industry Law, general gas companies are obliged to specify the supply terms and conditions including charges for backup and parking that are considered to be incurred in the consignment supply and submit them to the competent authority. The modification orders may be issued from the authorities if the terms and conditions for the consignment supply are inappropriate, for example when the terms and conditions are too tough for a gas supplier to use consignment supply services.

General gas companies will face an order to open their conduit network for consignment supply services if they refuse to access to them without due cause.

It is desirable for non-general gas companies that own conduit networks to open them voluntarily.

2. Desirable Trade Practices and Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition

(1) Prohibition on Uses of Information for Other Purpose

A. Desirable Trade Practices from the Standpoint of Fair and Effective Competition

General gas companies should take the following measures to ensure that no information arising from consignment supply services is used for any other purpose than that intended:

(a) General gas companies should appoint and announce contact point for information on the consignment supply services not within their section engaging in the gas marketing for large scale supply and gas supply business (hereinafter referred to as “wholesale supply”) against the gas companies which use the consignment supply services (including those who wish to begin to use consignment supply services; hereinafter referred to as a “consignment supply service client”) but within the section dedicated to consignment supply operations and related operations (hereinafter referred to as “consignment supply related operations,” and the section itself is hereinafter referred as a “consignment supply related operation section”), and

(b) Staff engaged in consignment supply operations in the consignment supply related operation section should not undertake any operation in the marketing section. However, in such a case where gas supply shortage needs to be urgently cleared as an accident in supply equipment or a natural disaster, those in the marketing section should be allowed to conduct consignment supply related operations.

(c) Regardless of the provisions in (b) above, general gas companies should pay attention to ensure the flexibility and efficiency in their gas supply operations which they are currently required to collaborate with the marketing section. If necessary, they should specify operations that need collaboration with the marketing section.

(d) To prevent any use of information about consignment supply clients or gas consumers arising from the consignment supply services (hereinafter referred to as “consignment supply-related information”) for other purposes, staff for the consignment supply operations should properly retain documents and data containing consignment supply-related information and control the transfer of the information from the consignment supply related operation section to other

sections and the sharing of the information among those sections. The consignment supply related operation section should be physically separated from other sections.

(e) To prevent any use of consignment supply related information for other purposes, general gas companies shall prepare a code of conduct for personnel exchange between the consignment supply-related operation section and other sections and let it be observed by the staff concerned.

Such code should be observed by the staff in the position of administration over both sections and the company managers.

(f) General gas companies should ensure that no information provided for any other section than the contract supply related operation section is used for other purposes even if it needs to be disclosed to the other section for unavoidable reasons in order to carry out third party access related operations (e.g. for technical assessment) . Such control measure includes encrypting the individual names of the consignment supply clients or the user concerned.

(g) General gas companies should prepare and publish internal standard handling consignment supply-related information, including prohibition on the use of such information for other purposes. In addition, they should appoint and announce an administrator responsible for compliance with the internal standard.

(h) If it is difficult to strictly implement the measures described in to above because of its company size and business situation, general gas companies should perform appropriate information management in accordance with its situation taking account of the objective of the amended Gas Utility Industry Law, which is to ensure fairness and transparency in the use of conduit networks.

B. Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition

If a general gas company is deemed to use or provide any information on the consignment supply client and the gas users concerned arising from the consignment supply operations for any purpose other than the operations themselves, that an order to discontinue or change such acts will be issued

pursuant to Section 22-4 of the Gas Utility Industry Law, including cases in which Section 37-8 applies.

The abovementioned “information on the consignment supply clients and the gas user concerned arising from the third party access operations” refers to any information that may have an impact on the company management when it is known to other companies as the followings:

(a) Conditions on the sources of gas supply (including those procured by agreements, hereinafter the same shall apply) to the contract supply customers

- 1) Position where gas supply sources are connected, scheduled time of operation (or commencement of supply)
- 2) Plan on gas production method, specifications of production facilities, material procurement or gas procurement
- 3) Characteristics and pressure of gas,

(b) Gas supply conditions, etc. of the consignment supply clients

- 1) State of the contract gas supply (volume of gas covered by contract supply, imbalance amount, accidents, etc.)
- 2) Backup supply capacity
- 3) Safety system and organization, and

(c) Demand trend and past demand situation of the gas users regarding consignment supply

- 1) Demand trend (Maximum flow ratio, projected demand from individual customer, distribution of customers and their scales, etc.)
- 2) Past demand situation (Maximum gas volume, track record of gas flow fluctuations)
- 3) Conditions on contract supply (gas volume in contract supply).

The abovementioned “use or provide any information on the consignment supply client and the gas users concerned for any purpose other than the operations themselves” refers to the use or provision of the information for the purposes as

the followings:

- (a) Grasping the business conditions of the consignment supply client,
- (b) Proposal of a gas supply plan in rivalry with the consignment supply client,
- (c) Sales activities targeted at specific users who receives gas supply from the consignment supply client, and
- (d) Enticing any user to switch its gas supply contract from the consignment supply client to itself or its related operators or to refrain from changing its existing agreement.

(2) Prohibition on Discriminatory Treatment

A. Desirable Trade Practices from the Standpoint of Fair and Effective Competition

To ensure fair disclosure and notification of the conditions for use of conduits and the consignment supply capacity of the conduit networks to all consignment supply clients, it is desirable for fair and effective competition for general gas companies to organize relevant materials and information to publish them.

When it is difficult to implement any of these measures in consideration of the scale of the gas business of a general gas company, etc. or the installation situation of conduit networks, the information disclosure should be done in an appropriate manner to follow the principle of the Gas Utility Industry Law for fair and transparent use of conduit networks.

To ensure the transparency and fairness of the consignment supply charges and the respective part of their own charges equivalent to consignment supply to large-scale or wholesale supply, it is desirable for the general gas companies to immediately produce fees equivalent to consignment and past demand records for individual large-scale and wholesale supply accounts at the request of the consignment supply and the gas users concerned.

B. Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition

If a general gas company, for example, conducts any act that constitutes unreasonably preferential treatment or benefits, an unreasonably disadvantageous treatment or damage against specific supplier to the third party access in its

consignment supply operations, an order to stop or change the act will be issued pursuant to Section 22-4 of the Gas Utility Industry Law, including a case in which Section 37-8 applies.

(a)Discriminatory Application of Individual Rules by the Third Party Access Related Operation Section

Unreasonably discriminated treatment of general gas companies, etc. described as the followings, between their marketing sections and consignment supply clients at the stage of planning in the access to the conduit networks, utilization and maintenance of the conduit networks, (including a case where unreasonably discriminating treatment between specific consignment supply clients and other suppliers when multiple suppliers request to access the conduit networks; hereinafter the same applies in to):

- 1)When unreasonable discrimination lies in the time period required for consideration, the content of the consideration, the response to a modification to the conditions of consignment supply, the content of the response, the judgment criteria or technical standard applied, cost bearing, and the treatment after the plan is withdrawn, between the marketing sections of general gas companies, etc. and consignment supply clients,
- 2)When unreasonable discrimination lies in the operation of conduit networks between the marketing sections of general gas companies, etc. and consignment supply clients, for example in conditions for limiting or stopping gas supply,
- 3)When unreasonable discrimination lies between the marketing sections of general gas companies, etc. and consignment supply clients in provision of information necessary to such clients in making use of consignment supply services, for instance in timing of notification of conduit maintenance or replacement of gas gauges, or failure to make prior notification to specific operators, and
- 4)When there exist unreasonably discriminating treatment in construction of conduit networks between the marketing sections of general gas companies, etc. and consignment supply clients, for instance making a detour installation of conduits on an indirect route even though consignment supply clients express explicitly their intention to bear a fair cost.

(b)Discriminatory Disclosure or publish of information owned by the consignment supply related operation section

The differential treatment described as the followings between the marketing section of general gas companies, etc. and consignment supply clients in the disclosure or publish of information owned by the consignment supply related operation section in connection with revisions of consignment supply charges and consideration of access plans to conduit networks.

- 1)Unreasonably discriminating treatment between the marketing section of general gas companies, etc. and consignment supply clients in information disclosure prior to consideration of access plans to conduit networks, such as the conduit installation situation, inertia pressure of conduits, maximum flow, capacity volume of consignment supply, etc.
- 2)Unreasonably differentiated treatment between the marketing section of general gas companies, etc. and consignment supply clients prior to the notification of price revisions and modification of the terms and conditions, for instance, in a case where the marketing section of a general gas company conducts sales activities with a revised fee in accordance with new contract supply charges immediately after they are published.
- 3)Unreasonably discriminating treatment between the marketing section of general gas companies, etc. and consignment supply clients in disclosure of information on gas users, such as annual or monthly consumption, owned by the consignment supply related operation sections of the gas companies.

(c)Discriminatory Response in the Provision of Consignment Supply Fee Menus and Services

Unreasonably discriminating treatment between the marketing sections of general gas companies, etc. and consignment supply clients, as listed below, in the application of the consignment supply fee menu and the provision of consignment supply services against the demand with universal supply conditions:

- 1)Where a consignment supply client has provided consignment supply service using low pressure conduits, which service was not included in the terms and conditions of consignment supply service it becomes difficult for the client to provide gas supply service comparable to that provided by the marketing

section of general gas companies, etc. for customers due to delayed presentation of the consignment supply charge applicable to low pressure conduits or a difference in consignment supply charges,

- 2)The discriminating treatment lies between the marketing section of general gas companies, etc. and consignment supply clients in the application of the consignment supply fee menu (base rate, contracted maximum consumption, etc.) caused by the difference between them in contractual unit of the consignment supply agreement,
- 3)The discriminating treatment lies between the marketing section of general gas companies, etc. and consignment supply clients in the application of the compensation fee in changing the contracted maximum consumption volume during the period of the consignment supply agreement,
- 4)Where a consignment supply client has provided gas supply service comparable (for example in the contracted period) to that provided by the marketing section of general gas companies, etc. it become difficult for the client to continue its service due to the discriminating treatment concerning the contracted period, for example, in cases in which a consignment supply client is not allowed to conclude any consignment supply agreement for a period of less than one year or to cancel and settle up the agreement in prior to the expiration, and
- 5)When a consignment supply client has provided it service, it became difficult for the client to continue its notification service of the users' gas consumption comparable to that provided by the marketing section of general gas companies, etc. due to the unreasonable difference between them in terms of the timing and method of notification of the consignment supply volume from the general gas companies, etc..

(d)Other Discriminatory Handling of Customers in Connection with Consignment Supply

Unreasonable differential treatment of gas users whether they are customers of general gas companies, etc., or those of consignment supply clients in the way the companies respond to the accidents in conduit networks (inquiries about accident conditions and instructions for recovering, etc.) and replacement of gauges, etc.(It does not cause a problem about unintended alteration in the order of accident recovery works.)

(3) Handling of Services Incidental to Consignment Supply

A. Desirable Trade Practice from the Standpoint of Fair and Effective Competition

The services incidental to consignment supply are defined as optional operations of general gas companies and therefore are not subject to orders for alteration and orders for consignment supply pursuant to the Gas Utility Industry Law.

(Note) Major elements of the services incidental to consignment supply service include the followings provided in response to an excess or shortfall of gas supply, such as backup and parking and the followings provided using equipment other than conduits, such as control, supervision, calorie control, storage and vaporization of raw gas material:

(i) Backup

Bridging supply of gas to compensate for a shortage of gas supply that goes below the statutory range for consignment supply service (Disparity of 10% or lower between the gas intake volume and gas output volume per hour),

(ii) Parking

Temporary storage of gas in response to excessive gas supply that exceeds the statutory range for consignment supply service,

(iii) Operations or Use of Equipment for Control and Supervision

Equipment needed to stabilize the property and pressure of gas (Odorizers, filters, thermometers and pressure gauges, control valves, etc.),

(iv) Operations or Use of Equipment for Calorie Control

Operations and equipment necessary when there is gap in calories between intake gas and gas in the conduit networks (for example, LP gas (with approximate 24,000 kcal/m³) is added to natural gas (approximately 9,500 to 10,800 kcal/m³) to raise the calories up to 11,000 kcal/m³, and

(v) Use of Equipment for Storage and Vaporization of LNG and Other Materials.

A very heavy burden will be put on consignment supply clients in operating their services unless those incidental services are provided by general gas companies. To encourage new entries into the market for large-scale supply and other services, it is desirable for general gas companies, etc. to voluntarily provide these incidental

services to the extent that does not disrupt the steady implementation of the business.

B. Acts which May Cause Problems from the Standpoint of Fair and Effective Competition

General gas companies, etc. regularly provide services incidental to consignment supply service. It is a violation of the Antimonopoly Act (refusal of trade, etc.) if they refuse to provide such services for specific consignment supply clients.

It may be unlawful under the Antimonopoly Act (Refusal of trade, etc.) for any general gas company, etc. to terminate services incidental to consignment supply services that it has provided to the consignment supply clients before.

III. Proper Gas Trade in the Wholesale Sector

1. Viewpoint

In procuring the raw materials of gas to be supplied by gas operators, the options are as follows:

- (i) Purchase of natural gas through conduits from major general gas companies or natural gas companies producing domestically,
- (ii) Purchase of offgas (low calorie gas) from oil refineries, petrochemical, steel and other businesses through the conduit networks,
- (iii) Purchase of liquefied natural gas (LNG) from major general gas companies or natural gas companies producing domestically, and
- (iv) Purchase of LPG, naphtha and other raw materials from domestic wholesalers.

In particular, the general gas industry has shifting its supply to higher calorie gas in Japan. The number of small and midsize general gas companies wishing to deal natural gas is expected to increase. As a major raw material of high calorie gas, most part of the natural gas is procured by imported LNG from overseas, and only a small portion is produced in Japan. Given that the import of LNG requires the conclusion of a long-term procurement agreement and enormous capital investment, a very limited number of operators actually import LNG from overseas. Many small and

midsize general gas companies are purchasing natural gas from these importers, which are major general gas companies and the like, as well as from the natural gas companies producing domestically by means of conduits or by tank trucks.

It is not easy to switch gas materials to others with different calories because enormous cost and labor are required for replacing the gas supply equipment and adjustment of the consumption equipment of gas users. Moreover, cases where any act in material procurement market causes an anti-competitive effect on the deregulated gas supply market should be avoided.

(Note) Under the Gas Utility Industry Law before amendment (hereinafter referred to as the “former Gas Utility Industry Law”), the above activities (i) and (ii) were statutorily defined as “wholesale supply” and were subject to regulations requiring those operators to submit their wholesale supply conditions including gas charges to prevent any adverse effect on gas charges in the regulated field of general gas companies to which the wholesalers sold their gas. However, the amended Gas Utility Industry Law abolished such requirement for submission of wholesale supply conditions in April 2004. Still, until three years from the date of enactment, with respect to the wholesale supply agreement stipulated in the former Gas Utility Industry Law concluded by the whole sale suppliers stipulated in the former Gas Utility Industry Law, transitional treatments apply which impose notification of alteration, government orders for alteration or the like to wholesale supply conditions. For this reason, orders for alteration under the Gas Utility Industry Law will be issued against any unreasonable wholesale supply condition specified in the agreement that “have harmful effect on appropriate supply conditions including gas charges of general gas companies which are receiving the gas in question,” such as unjustifiably high prices, for a period of three years from the amended Gas Utility Industry Law come into effect.

In this case, to avert ex post facto government intervention and to ensure fair and effective competition, it is preferable for general gas companies engaged in gas wholesale and other operators (referred to as “wholesalers” in this chapter) to take appropriate actions with reference to the followings

2. Desirable Trade Practices and Trade Practices That May Cause Problems from the

Standpoint of Fair and Effective Competition

(1) Desirable Trade Practices from the Standpoint of Fair and Effective Competition

Since general gas companies have an obligation to supply gas to consumers in their respective service zones pursuant to the Gas Utility Industry Law as purchasers of wholesale gas, wholesalers should maintain their gas supply to general gas companies to the extent possible.

(2) Trade Practices that May Cause Problems from the Standpoint of Fair and Effective Competition

(a) Unjustifiably High Pricing by Means of Refusal to deal or Suggest to Do So

When it is actually difficult for general gas companies to procure gas in any other measure than purchasing wholesale gas from specific wholesalers, if the wholesalers oblige the general gas companies concerned to enter into transactions with disadvantageous conditions, such as unjustifiably high prices, by refusing the trade or implying the refusal of trade without reasonable reason, such conduct may constitute a violation of the Antimonopoly Act (refusal to deal, abuse of dominant bargaining position, dealing on restrictive terms, etc.).

(b) Dealing on Unreasonable Restrictive Terms, etc.

If wholesalers carry out transactions with general gas companies on the condition that the general gas companies they are dealing at wholesale should not buy any gas from competitors, they may violate the Antimonopoly Act (dealing on exclusive terms) .

If wholesalers conduct any act that has an unjustifiably disadvantageous effect in light of proper trade practices in conditions or implementation of transactions with general gas companies they are dealing at wholesale, they may violate the Antimonopoly Act (abuse of dominant bargaining position).

If wholesalers oblige general gas companies they are dealing at wholesale to supply their gas to a limited number of customers, they may violate the

Antimonopoly Act (dealing on restrictive terms).

IV. Proper Gas Trade in the Regulated Retail Sector (Optional Rule)

1. Viewpoint

Amended in 1991, the Gas Utility Industry Law introduced the optional rule in the regulated retail sector to enhance flexibility of fee menu settings by general gas companies and community gas companies. It is expected to stimulate competition with other forms of energy while it is possible that these companies may place much emphasis on rivalry to draw up unfavorable terms and conditions that include unreasonable discriminatory treatment or they may produce unfavorable terms and conditions with an adverse effect on general consumers to whom the optional system does not apply.

To avert ex post facto government intervention and to ensure fair and effective competition, the general gas companies and community gas companies are required to take appropriate measures with reference to the followings.

2. Desirable Trade Practices and Trade Practices That May Cause Problems from the Standpoint of Fair and Effective Competition

(1) Desirable Trade Practices from the Standpoint of Fair and Effective Competition

It is effective for ensuring fair and effective competition for general gas companies and community gas companies to produce optional rule suited to individual user groups with the same demand properties and announce them to the public. This enables for all consumers to be treated impartially irrespective of their attributes (whether they are individual consumers, they are in a certain area, they are new users with plants or residential houses and whether they converted from other energy sources) other than their consumption situation.

In setting the charges for gas supply under the optional rule, the net revenue test method (Note) is adopted in addition to accumulated cost pricing. The idea behind is that if the choice of the optional rule serves to increase profit it will ultimately serve to maintain or expand the interests of other small-scale users that are not subject to

the optional rule. If the optional rule prepared by a gas company passes the net revenue test, there is little possibility for the company to face any alteration order under the Gas Utility Industry Law.

(Note)The Gas Utility Industry Law requires any new or revised optional rule to be designed to encourage the efficient use of equipment and other business operation and to have little harm on the interests of users who enjoy gas supply according to the standard offer. It required the net revenue test, which checks the method of calculation and if pricing increases the profit (whose cost recovery period is defined by general gas companies and community gas companies at their discretion with the range from one to five years) as well as accumulated cost pricing.

To maintain transparency, general gas companies and community gas companies should provide comprehensive and precise explanations on pricing in their optional rule from the standpoint of fair and effective competition.

(2)Trade Practices that May Be Problems from the Standpoint of Fair and Effective Competition

(a)Pricing that Does Not Lead to Appropriate Cost Recovery

Provided that the optional rule prepared by the gas companies fails to pass the net revenue test or that cost has not been properly covered after passing the cost recovery period stipulated at the submission of the optional rule even if the optional rule passed the net revenue test at the time of submission, it is regarded as detrimental to the interests of the users who enjoy gas supply under the supply rule and therefore an alteration order will be issued under the Gas Utility Industry Law (the Gas Utility Industry Law Section 17(8), including cases in which Section 37-7 applies).

(b)Unjustifiable Discriminatory Treatment among Users

If general gas companies and community gas companies formulate an optional rule that applies a lower price only to certain users in their service area, such as those who enjoy gas supply from a rival supplier of other energies or are

negotiating the supply, it will constitute discriminatory treatment for specific users and an alteration order will be issued under the Gas Utility Industry Law (the Gas Utility Industry Law Section 17(8) , including cases in which Section 37-7 applies).

(c)Other Case

It constitutes discriminatory treatment for specific consumers to set any optional rule by a general gas companies and community gas companies designed exclusively for the users of gas consumption equipment which they are dealing and therefore an alteration order will be issued under the Gas Utility Industry Law (the Gas Utility Industry Law Section 17(8), including cases in which Section 37-7 applies).

If general gas companies and community gas companies require their users to purchase their gas consumption equipment by exploiting its dominant position at which they solely conduct gas piping work, it may constitute a violation of the Antimonopoly Act (tie-in sales, etc.).

V. Proper Gas Trade Concerning Use of LNG Stations by Third Parties

1. Viewpoint

Since Japan depends on a large portion of its domestic gas supply to the LNG import, the LNG stations are the starting points of conduit networks. Encouraging third parties to use the LNG station is desirable to promote new entries in the market and diversify gas procurement sources from the viewpoint of invigorating the gas market and developing conditions for fair competition.

Specifically, LNG stations differ from conduit networks in that the stations are easier to construct but more difficult to inform their surplus supply power to outsiders. To facilitate the use of LNG stations by third parties, it is necessary to stipulate that any party wishing to use them should directly negotiate with the operator owning or controlling the LNG stations (hereinafter referred to as the “LNG station operator”) in order to ensure transparency and impartiality of utilization.

2. Desirable Trade Practices from the Standpoint of Fair and Effective Competition

It is desirable for LNG station operators to take the following actions with respect to the use of their LNG stations by third parties from the standpoint of fair and effective competition:

- The LNG station operators should prepare Guidelines to clearly define the preconditions for negotiations on the third-party use of LNG stations and negotiation rules,
- The LNG station operators should disclose sufficient information to estimate surplus supply capacity, such as the facility capacity of the stations, current operational status, a future (or expected) operation schedule,
- When refusing an application for utilization, the LNG station operators should make written notification of the reasons of refusal to the applicant, and
- When an LNG station operator finally concludes an agreement on use with an applicant, it should disclose the contractual conditions, such as the trade volume concerned and the period of use, after passing a certain length of time from the conclusion of the agreement with the reference to corporate information treatment such as paying attention to the position in competition and getting approval of the user.

3. Trade Practices That May Cause Problems from the Standpoint of Fair and Effective Competition

If a LNG station operator unreasonably rejects an application for use from a gas company whose station is indispensable for its business activities but that is in a competitive relationship with the operator itself or its related business or impose unreasonable delay the negotiations where the operator can open its station to other gas companies, it causes difficulty for the applicant to conduct its business activities, it may constitute a violation of the Antimonopoly Act (refusal to deal, private monopolization, etc.)