



AUSTRALIAN RAIL TRACK CORPORATION LTD

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Dear Stakeholder

Revised 7 September 2010 Hunter Valley Access Undertaking (2011 HVAU) – Further amendments following industry consultation

In early April 2011, ARTC provided the 2011 HVAU to the ACCC following further consultation with the ACCC and stakeholders after the release of a Position Paper by the ACCC in December 2010.

The ACCC has commenced a public consultation in relation to the 2011 HVAU. During that consultation period ARTC has continued to review a number of key items with the ACCC and key stakeholders representing existing Hunter Valley export coal producers (Existing Export Coal Stakeholders).

Following these consultations, ARTC has drafted amendments to the 2011 HVAU (and associated Indicative Access Holder Agreement) as set out at Attachment 1. These amendments have been drafted by ARTC in response to several concerns expressed by Existing Export Coal Producers. ARTC understands that Existing Export Coal Producers would support the 2011 HVAU, including ARTC's proposed Rate of Return, following ARTC's engagement in further consultation and a satisfactory outcome arising from that consultation. The amendments described in this letter should be considered as a packaged response following that further consultation, and ARTC understands that the package largely addresses the concerns expressed by Existing Export Coal Producers. A brief description of the rationale for the package of amendments is provided below.

This letter is provided to stakeholders in order to inform the ACCC consultation of these alternative proposals and to enable consideration to be given to the package of amendments in completing any submissions to the ACCC. This letter has also been submitted to the ACCC for consultation. The inclusion of these amendments in a revised 2011 HVAU will be considered with reference to stakeholder comments and the level of industry support.

Consistent System Assumptions and Basis of Contractual Entitlements

Existing Export Coal Producers have raised two critical issues as follows.

- The System Assumptions adopted by ARTC in its assessment of Capacity (network capacity) should be consistent with those used by the HVCCC.
- Access Holders contractual entitlements should be limited to the HVCCC assessment of Coal Chain Capacity.

Consistent System Assumptions

The 2011 HVAU requires ARTC to participate in the development of System Assumptions with the HVCCC. ARTC strongly supports the use of System Assumptions as a common reference set for capacity analysis and planning.

The 2011 HVAU and associated Indicative Access Holder Agreement (**IAHA**) both incorporate System Assumptions and include additional assumptions not included in the list of HVCCC agreed assumptions (Systems Assumptions Document), being section run times, train axle load, train speed and train length.

ARTC cannot, however, be in a position where System Assumptions upon which ARTC plans and manages its business in the Hunter Valley can be unilaterally changed by the HVCCC, where ARTC has only a single vote.

ARTC accepts that the requirement for it to agree to any changes to System Assumptions is not desirable to industry and, as such, ARTC proposes the following adjustments to the 2011 HVAU for consideration:

- a. Specify the list of System assumptions that are relevant to ARTC's assessment of Capacity (network capacity) as agreed with the HVCCC, being:

HVCCC Agreed

- ARTC track including path numbers
- live run management
- ARTC system losses
- maintenance intervention
- train parking capacity (for shut downs)

ARTC Published

- section run times
- train length
- train axle load
- train speed
- other assumptions reasonably determined by ARTC from time to time as necessary for the purposes of determining Capacity

- b. The right to arbitration (proceeded by informal resolution procedures) where the HVCCC and ARTC have different views in relation to relevant System Assumptions, except where ARTC reasonably believes that practical adoption of a proposed System Assumption would negatively impact safe operations, network condition or ARTC's commercial position.
- c. Determination and publication of Capacity as assessed by ARTC in accordance with relevant System Assumption in the annual Hunter Valley corridor capacity strategy prescribed in section 8.1 of the 2011 HVAU.

Basis of contractual entitlements

Existing Export Coal Producers have advised that a key concern around Capacity arises due to the risk that capacity contracted at the ports may exceed Coal Chain Capacity. Industry seeks ARTC, as a service provider, to be responsible for ensuring that capacity contracted across the Hunter Valley coal chain does not exceed Coal Chain Capacity as determined by the HVCCC, based on System Assumptions.

The 2011 HVAU and IAHA align contracted Capacity Entitlements with entitlements contracted through the ports. This has been a fundamental tenant of the access undertaking and a critical consideration of ARTC, the ACCC and industry during the regulatory assessment of the undertaking. The IAHA is based on matching Capacity entitlements with those at the terminals with the assumption that the terminals would not over-contract coal chain capacity as determined by the HVCCC. The HVCCC must determine Coal Chain Capacity, as ARTC does not have the expertise required to model other parts of the coal supply chain. ARTC believes the industry set up the HVCCC with this purpose in mind consistent with the principles underpinning the long term solution for the Hunter Valley coal chain envisaged by industry.

ARTC is however willing to amend the 2011 HVAU in order to address the concerns of Existing Export Coal Producers by providing for the following:

- A right for ARTC to reduce access entitlements of an Access Holder where that Access Holder is unable to provide evidence of Network Exit Capability **and**

written evidence from the HVCCC that there is sufficient Coal Chain Capacity to enable the access entitlements to be delivered across the coal chain.

- ARTC can rely on (and cannot be held accountable for) the accuracy of the evidence provided.

True Up Test Audit

Existing Export Coal Producers have advised that there should be a firm commitment to conduct an annual audit of the system wide true up test upon request.

ARTC has previously incorporated in the IAHA a commitment to identify and engage an independent auditor to audit ARTC's obligations under Schedule 2 of the IAHA in relation to the performance of the system true up test in each Pricing Zone.

At Schedule G of the HVAU, ARTC has committed to provide a copy of the final audit report to the ACCC as part of the annual ACCC compliance assessment, which is intended to result in ARTC making any necessary financial reconciliation to Access Holders as determined by the ACCC where ARTC has not complied.

As such, it is ARTC's view that the 2011 HVAU provides for the audit sought by Existing Export Coal Producers to be conducted annually, irrespective of whether it is requested.

In order to clarify this, ARTC is willing to amend the 2011 HVAU in order to meet the needs of Existing Export Coal Producers by providing for the following:

- Clarify that ARTC will conduct the Audit as soon as practicable in accordance with terms approved by the ACCC.
- Clarify that the audit report is provided to the ACCC to review as part of the annual compliance assessment process under the access undertaking.
- Where the ACCC determines as a result of the audit that TOP Rebates have not been calculated correctly, the ARTC will pay any underpayment, and is entitled to recover any overpayment as determined by the ACCC as part of the annual compliance assessment.
- Where the ACCC considers that this reconciliation will not materially affect the determination of the compliance assessment, the ACCC can advise ARTC of the details of the necessary amounts ahead of a determination in relation to the annual compliance assessment.

- Within 15 Business Days of this advice ARTC will inform Access Holders of amounts owed by ARTC and to be remitted by Access Holders.
- Within 15 further Business Days, ARTC will make payments to Access Holders and be entitled to recover amounts from Access Holders.

Efficient Train Configuration

Existing Export Coal Producers have advised that the coal industry needs early advice of what constitutes the efficient train configuration leading to the prescription of the Indicative Service and Indicative Access Charge. Existing Export Coal Producers indicated that they recognised that:

- Early advice may not deliver an outcome that provides for optimal utilisation of Coal Chain Capacity, but a practicably achievable outcome based on existing HVCCC modelling and coal chain constraints only.
- The prescription of the Indicative Service and Indicative Access Charge may be revised, when informed by more thorough and comprehensive optimisation modelling to be undertaken.

ARTC is willing to amend the 2011 HVAU in order to meet the needs of Existing Export Coal Producers by providing for the following:

- ARTC will consult with the HVCCC, Access Holders and Operators in order to determine and propose the Indicative Service and Indicative Access Charge to the ACCC within 5 months of the Commencement Date. It should be noted that ARTC has not yet been able to confirm participation to the necessary extent by the HVCCC and that this may impact on the proposed project timeframe.
- The Indicative Service will be determined having regard to existing coal chain infrastructure constraints (as used by existing HVCCC modelling) and by testing existing coal service configurations plus a reasonable number of alternative configurations agreed between ARTC and the HVCCC.
- ARTC will seek the approval of the ACCC to vary the undertaking to provide for the adoption of the Indicative Service and Indicative Access Charge.
- Within 30 Business Days of approval to vary the undertaking, ARTC will publish the details of:

- the Indicative Service;
 - Indicative Access Charge; and
 - Charges for non-Indicative Services (specifically those Services that are Interim Indicative Services)
- Pricing parity obligations for certain Services will be maintained as currently contemplated.
- The more comprehensive assessment as currently proposed in the 2011 HVAU will be retained and result in submission of the Indicative Service and Indicative Charge within two years of the above approval. This is expected to be around 2.5 years from the Commencement Date.
- In formulating Charges for Coal Access Rights, ARTC will reflect in any differentiation between Services the commercial impacts arising from the impact on consumption of Capacity and Coal Chain Capacity, and logistical impacts on ARTC's business arising from reduced Capacity and reduced Coal Chain Capacity as determined by ARTC. ARTC will have regard to all other factors as currently contemplated.

RCG Voting Rights

Existing Export Coal Producers have raised a concern that ARTC's discretion to allow a party that reasonably expects will contract for future volumes, but has not done so, to have RCG voting rights in relation to Additional Capacity for that future volume may enable such a party to trigger investment which the other existing parties with contracted volumes may have to pay for, should an expected contract not ultimately eventuate.

Under the 2011 HVAU, in order for an investment to be deemed approved by the RCG (and so included in the RAB), 50% of volume in the relevant Pricing Zone must support the investment, and 70% if the investment will increase access pricing by more than 10%. It is difficult to foresee that a new entrant could trigger approval of an investment where the additional volume needed to achieve this would amount to around 200mTpa in Pricing Zone 1, 50mTpa in Pricing Zone 2, and 25mTpa in Pricing Zone 3.

ARTC is also mindful that requiring contractual commitment too early in the project development process, where information in relation to the nature, timing and cost of a project is unlikely to be known, may act as a deterrent to new entry or additional volumes.

To balance this, ARTC is willing to amend the 2011 HVAU in order to address the concerns of Existing Export Coal Producers by providing for the following:

- ARTC discretion as currently contemplated is retained in relation to RCG voting rights for Concept Assessment and Project Feasibility
- For Project Assessment and subsequent stages, ARTC's discretion is removed. That is, an Access Holder must have an executed TOP contract to be able to vote in relation to endorsement of Project Assessment and subsequent stages.

HVAU Review

Existing Export Coal Producers have advised that ARTC is not the appropriate party to conduct a review of its own voluntary access undertaking. The Existing Export Coal Producers' position is that an independent review should be undertaken (presumably by the ACCC) and if ARTC does not adopt all findings (by varying the undertaking) then the undertaking could be immediately terminated.

ARTC notes that the NSW Minerals Council submission, representing most of the coal industry, in September 2010 did not raise concerns with a 10 year term, nor the 5 year review mechanism proposed in the 7 September 2010 Hunter Valley Access Undertaking.

Nevertheless, ARTC has expanded on this previous version of the 5 year review to prescribe a consultative process, objectives and reporting designed on the basis of an approach proposed by a key coal industry stakeholder in its submission in relation to that review.

In addition, ARTC is now obliged to undertake a number of earlier reviews within the first few years after the Commencement Date of key elements of the 2011 HVAU such as:

- Indicative Service (initial and final);
- True up test;
- Tolerance;
- trading period;
- capacity losses; and
- performance incentives

All access undertakings submitted to the ACCC are done so on a voluntary basis under the Competition and Consumer Act (2010). The approach proposed by Existing Export Coal Producers now requires ARTC to vary its voluntary undertaking

in accordance with all positions put forward as a result of an independent review. If ARTC elected not to seek a variation in line with all such positions, the undertaking would effectively be terminated.

ARTC considers that the approach proposed in the 2011 HVAU is reasonable and represents a balance of interests, including providing for some flexibility whilst maintaining some certainty over the Term. The 5 year review is contemplated in addition to a number of earlier reviews of key elements of the 2011 HVAU as described above.

ARTC remains concerned that a 5 year term would be inconsistent with contracting over at least 10 years across the coal chain, and the 15 year term of the ports authorisation.¹

However, in order to increase the transparency and independence of the 5 year review, ARTC is willing to amend the 2011 HVAU in order to provide for the following:

- ARTC will, in addition to providing for publication of a report (subject to confidentiality requirements), and providing a copy of the report to the ACCC, provide a copy of all submissions made by stakeholders to the ACCC.

This will enable the ACCC to independently consider all review documents. In the 2011 HVAU a stakeholder is not prevented from commissioning an independent review of the 2011 HVAU after 5 years and submitting it to ARTC, to be ultimately provided to the ACCC.

Transitional Arrangements

ARTC provided advice to the industry in April 2011 signifying an intention to extend transitional arrangements that had been previously advised to the industry (December 2010). Given that a conclusion to the ACCC's review of the access undertaking is now imminent, ARTC will provide further advice to the industry in the near future in relation to the transitional arrangements that will apply going forward.

A related concern expressed by Existing Export Coal Stakeholders relates to the approach adopted by ARTC to resolving mutually exclusive access applications. ARTC has previously advised that, during transition, it will consider all applications on an equitable basis.

¹ ACCC, *Applications for authorisations lodged by Port Waratah Coal Services Limited, Newcastle Coal Infrastructure Group and the Newcastle Port Corporation in respect of the Capacity Framework Arrangements at the Port of Newcastle (Authorisations - A91147 - A91149 & A91168 & A91169)* - 9 December 2009.

In order to address this concern, ARTC is willing to amend the 2011 HVAU in order to provide for the following:

- Where two or more mutually exclusive access applications provided to ARTC with a comparable present value of future returns after considering all of the risks associated with the resulting agreements, ARTC will allocate access on a pro rata basis. This would normally be the case where the two applications satisfy the following criteria:
 - Mines in the same Pricing Zone.
 - Applicants are willing to agree to the same terms and conditions.
 - Term of resulting agreements is greater than 10 years.

Revised HVAU and IAHA

The amendments outlined in this letter may form a revised version of the HVAU and IAHA to be submitted to the ACCC. Accordingly, ARTC will conduct a more thorough review of both the HVAU and IAHA to identify and make any other consequential changes that may be required as a result of the amendments.

Yours sincerely



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