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25 October 2010

Mr Anthony Wing
General Manager
Transport and General Prices Oversight Branch
Australian Competition and Consumer Commission
GPO Box 520
MELBOURNE VIC 3001

Via email: transport@accc.gov.au

Dear Mr Wing

ARTC Hunter Valley Coal Network Access Undertaking

The NSW Minerals Council (NSWMC) welcomes the opportunity to respond to the Australian Competition and Consumer Commission (ACCC) Discussion Paper on the Australian Rail Track Corporation's (ARTC) proposed 2010 Hunter Valley Rail Network Access Undertaking (proposed 2010 HVAU).

NSWMC makes this submission on behalf of the Hunter Rail Access Task Force (HRATF), an associated group comprising all 14 Hunter Valley coal producers using the ARTC Hunter Valley Rail Network.

All 14 coal producers strongly support NSWMC's submission. Some of the coal producers will also be making individual submissions to express that support and focus on issues of particular relevance to them. While there may be some differing views on a small number of detailed provisions in the Undertaking, there is unanimous support for the overall position set out in the NSWMC submission.

NSWMC's submission is intended for publication should the ACCC wish to do so. Further supporting documentation referred to in the submission will be forwarded in due course.

The HRATF would like to meet you and your officers as soon as possible to provide a more detailed explanation of the concerns with the proposed 2010 HVAU and the next steps towards achieving an acceptable undertaking outlined in our submission. A representative of the HRATF will contact you in the near future to arrange a suitable time for this discussion.

For further information on the submission, please contact Mr Geoff Andrews on (02) 9386 9957 or via email at an53696@bigpond.net.au.

Yours sincerely,



Ms Sue-Ern Tan
ACTING CHIEF EXECUTIVE OFFICER

Cc: Mr P O'Grady, Chair, Hunter Rail Access Task Force



**NSW MINERALS COUNCIL
HUNTER RAIL ACCESS TASK FORCE**

**SUBMISSION IN RESPONSE TO
THE AUSTRALIAN COMPETITION AND
CONSUMER COMMISSION'S
CONSULTATION PAPER**

IN RELATION TO

**AUSTRALIAN RAIL TRACK CORPORATION'S
PROPOSED 2010
HUNTER VALLEY RAIL NETWORK
ACCESS UNDERTAKING**

25 October 2010

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1. NSWMC POSITION

1.1 Introduction

The NSW Minerals Council (the “**NSWMC**”) welcomes the opportunity to respond to the Australian Competition and Consumer Commission (the “**ACCC**”) Consultation Paper in relation to the Australian Rail Track Corporation’s (“**ARTC**”) proposed Hunter Valley Rail Network Access Undertaking (the “**proposed 2010 HVAU**”).

NSWMC is making this submission on behalf of the Hunter Rail Access Task Force, an associated group comprising all 14 Hunter coal producers using ARTC’s Hunter Valley Rail Network (the “**HVRN**”).

The Hunter coal producers presently rail around 100Mtpa of coal on the HVRN, worth around \$9 billion pa in export earnings, and the HVCN is a key component of the “**Hunter Coal Chain**”, the world’s largest and most complex coal export operation.

Investment in Hunter Coal Chain mines and infrastructure by the coal producers is estimated to be in excess of \$10 billion to date. Further investment of \$5-10 billion is being contemplated to potentially double mine production capacity and exports over the next 5-10 years. Moreover, the additional infrastructure capacity needed will be underwritten by direct investments and service charges paid by the coal producers under long-term take-or-pay contracts, with a potential total commitment of at least \$10 billion.

Aligned, efficient operation and timely, prudent expansion of the Hunter Coal Chain infrastructure, that meets the operating and commercial needs of the Hunter coal producers and the complex logistical systems of the Hunter Coal Chain, will be critical to realising the potential growth in Hunter coal exports and the consequent boost to Australia’s export earnings. ARTC’s role in providing track access will be an essential part of that process.

1.2 NSWMC Position

NSWMC supports, in principle, ARTC’s development of the proposed 2010 HVAU as a separate access undertaking for the HVCN to address the major operational, commercial and regulatory differences from the Interstate Network (for which the ACCC accepted ARTC’s Interstate Undertaking in 2008).

However, NSWMC submits that the proposed 2010 HVAU should be rejected (in its current form) by the ACCC for the reasons set out in this submission and in relevant sections of our July 2009 submission on the April 2009 HVAU.

While some of the concerns set out in our July 2009 submission have been addressed, at least partially, in the proposed 2010 HVAU, many of the substantive issues have not. In particular, NSWMC considers that the HVAU, in its current form still:

- Will not promote the economically efficient operation of, use of and investment in the HVRN or in the other coal and port infrastructure that forms part of the Hunter Coal Chain;
- Does not adequately take into account the legitimate interests of Hunter Valley coal producers;
- Will be contrary to the public interest that lies in maximising the throughput of the Hunter Coal Chain and coal export volumes; and

- Does not ensure that the charges payable for services covered by the HVAU will be consistent with the pricing principles set out in Part IIIA of the Trade Practices Act.

Many of these concerns were recognised in the ACCC's Draft Decision on the April 2009 HVAU. NSWMC supported the ACCC's draft decision to not accept the HVAU in its April 2009 form and agreed with the preliminary view expressed in the Draft Decision that there were many provisions in the April 2009 HVAU which made it unacceptable under Part IIIA of the Trade Practices Act.

1.3 NSWMC Concerns with the 2010 HVAU

Although there has been substantial redrafting of the April 2009 HVAU, many significant issues have not been satisfactorily addressed. NSWMC believes that the proposed 2010 HVAU does not adequately respond to many of the issues identified by the ACCC in its Draft Decision. Nor does it address most of the major issues and more detailed changes put forward by NSWMC on behalf of the coal producers. Where ARTC has responded, the changes often fall short of those needed to resolve the problems.

Section 2 of NSWMC submission sets out the Hunter coal producers' concerns in five key areas

1. There is no certainty of contracted volumes on the track.
2. There is insufficient ARTC accountability for delivering contracted capacity.
3. There is no commitment to provide accurate, timely access pricing signals to guide stakeholder investment decisions in rolling stock and infrastructure upstream and downstream of the track.
4. There is no certainty that contractual alignment will be enhanced through the development of effective capacity management protocols.
5. There are almost no incentives to align ARTC and Access Holder interests through performance improvement mechanisms that reward ARTC for improved efficiency.

Further documentation supporting NSWMC submission, which will be submitted shortly, sets out numerous other significant concerns that need to be addressed in relation to access pricing, including the new proposals relating to access charges (rate of return, remaining mine life and the access pricing model) which are unsatisfactory; the ARTC's involvement in system management processes and the determination of System Capacity; ARTC's provision of information to HVCCC, RGC and Access Holders; stakeholder consultation in relation to Additional Capacity; and performance monitoring.

These comments encapsulate many of the areas of concern identified by the ACCC. The supporting documentation also sets out NSWMC comments on other matters on which the ACCC Consultation Paper sought comment.

1.4 Achieving an Acceptable Undertaking

The Hunter coal producers remain committed to implementation of rail access arrangements which align with the long term Capacity Framework Agreement for the coal chain implemented from 1 January 2010. As stated in all NSWMC's submissions and correspondence with the ACCC and ARTC over the last two years, the coal producers are

keen to work with, and support, ARTC and the other infrastructure service providers to ensure this commitment is met.

NSWMC also supports the ACCC's endeavour to issue a statement in relation to the proposed 2010 HVAU prior to the end of 2010. The Hunter coal producers are anxious to secure commitments of track access capacity to match their port terminal access commitments. They are very disappointed at the continuing delays in getting an appropriate undertaking in place.

Nevertheless, the Hunter coal producers believe that it is more important to take the time to adequately address the coal producers' serious concerns with the proposed 2010 HVAU. Under the HVAU, the producers will be required to enter long-term, take-or-pay commitments to ARTC totalling more than \$2 billion. It is essential to achieve an effective undertaking that will allow alignment of the producers' rail access and port terminal contracts and ensure the efficient operation and timely, aligned expansion of the HVRN and the Hunter Coal Chain as a whole.

NSWMC therefore submits that, instead of accepting the proposed 2010 HVAU in its current form, the ACCC should ask ARTC to work with the coal producers and other stakeholders to rapidly resolve the alignment issues in a manner that is consistent with the Capacity Framework Agreement, and amend other provisions of the proposed 2010 HVAU to meet the reasonable needs of the coal producers, as set out in this and our previous submissions. The objective should be to lodge, as soon as possible, an amended undertaking, supported by the coal producers, that can be quickly accepted by the ACCC.

Moreover, NSWMC emphasises the need not to ensure a more effective consultation process than was conducted by ARTC before lodging with the ACCC both the April 2009 HVAU and the proposed 2010 HVAU. NSWMC therefore submits that the ACCC should:

- Clearly set out the legitimate issues raised by the coal producers and other stakeholders that need to be resolved and emphasise to ARTC that it must effectively address them; and
- Strongly request that ARTC work with the coal producers and other infrastructure service providers in a close and cooperative, workshop process, coordinated by the ACCC if necessary, to develop suitable amendments to the proposed 2010 HVAU as rapidly as possible.

NSWMC believes that, with a more cooperative and engaged approach, many of the issues could be resolved relatively quickly and, if ARTC incorporated suitable amendments in a revised undertaking, such a revised undertaking could be acceptable.

NSWMC submits that, considering the scope of the amendments to the proposed 2010 HVAU that are necessary, a revised undertaking would then need to be subject to further review by the ACCC and stakeholders. However, that review could be completed relatively quickly if the ACCC and stakeholders have been involved in a cooperative process of developing suitable amendments.

NSWMC also requests that the ACCC support the further extension of the access contracts for coal haulage on the Hunter Rail Network that Pacific National and QR National currently hold with ARTC until a suitable undertaking is accepted by the ACCC.

2. FIVE KEY ISSUES

2.1 Certainty of Contracted Volumes on the Track

Certainty of capacity for Access Holders and Access Seekers is essential to allow coal producers to align their track access capacity with their investments in coal production operations and their capacity commitments at the port terminals.

2.1.1 Transition Arrangements

The proposed 2010 HVAU does not provide for the transition from the current track access arrangements, under which existing coal producers have access to track capacity, to the initial allocation of Available Capacity under the HVAU. Nor does it provide a process for the allocation of Additional Capacity in future to align with the process for allocating capacity increases at the port terminals.

Hunter coal producers have now committed, under long-term take-or-pay contracts, to port terminal capacity allocations expanding to well in excess of current track capacity but have no certainty that they will be able to contract for track access capacity to match their already contracted current and future port terminal access capacity.

NSWMC submits that a transparent initial and subsequent annual process for coal producers to nominate for, and ARTC to allocate, track access capacity must be included in the proposed 2010 HVAU. The process should be aligned with the capacity nomination and allocation processes for the port terminals.

2.1.2 Delivery of Additional Capacity

Major expansion of the Hunter Valley coal production is forecast in the coming years and major new investments in coal production and port terminal facilities are planned. Consequently, major expansion of track access capacity will be necessary to align with the other elements of the Coal Chain.

However the provisions of the proposed 2010 HVAU dealing with new capacity are inadequate and uncertain.

Firstly, the process of determining whether Additional Capacity is required for an Access Seeker is not clear. The requirement for the Initial review in s3.6 is an unnecessary duplication of the process of assessing Available Capacity in s3.9(c); the priorities for allocation of Additional Capacity among coal Access Seekers are not defined (as highlighted above) except under s3.13 which allows ARTC wide discretion to allocate Access Rights which would not align with the access priorities for port terminal access.

Secondly, under s6.2 and 6.3, there is no certainty that Additional Capacity will be committed to meet Applications for Access and thus track capacity may not be expanded to align with port terminal capacity.

Under s6.2 (a) to (f), which deals with Capacity expansions to provide access sought by Applicants, ARTC will commit to provide Additional Capacity only if TOP commitments cover the economic life of the Additional Capacity and the Additional Capacity is “commercially viable” (i.e. can be financed by ARTC) and does not compromise ARTC’s “legitimate business interests” (which are not defined). If ARTC does not consider the Additional Capacity commercially viable, the Applicant can agree to meet the total cost by up-front Capital Contribution, access charges, periodic payments reimbursing ARTC’s capital outlay, or some other agreed way.

These provisions could prevent Applicants obtaining access unless they contribute the total capital cost of the Additional Capacity. As well as any spur line used only by the Applicant, the requirement could include an expansion of the multi-user track section that the Applicant has to use, whereas the current capital costs of Additional Capacity on multi-user track segments are best recovered from all the users of the section (as provided for in the access pricing provisions). Moreover, although ARTC's "legitimate business interests" provide some limit on its discretion to decide whether it will agree to build Additional Capacity that an Applicant is willing to fund, the application of this provision is uncertain and needs to be more clearly defined.

S6.2(g) is a further inhibitor of the provision of Additional Capacity. It provides, where Additional Capacity is provided by a Capital Contributions by an Applicant, for an "equitable form of reconciliation between the Contributor, ARTC and another user sharing the Additional Capacity" according to a complex set of principles. NSWMC submits that this section remains too uncertain. Furthermore it is overly complex and needs to be simplified to make the equitable form of reconciliation clearer.

Under s6.3, which deals with Capacity expansions recommended by HVCCC, ARTC will commit to the Additional Capacity only if TOP commitments cover the capital costs over its economic life and the Additional Capacity is "commercially viable" (i.e. can be financed by ARTC) and does not compromise ARTC's "legitimate business interests" (not defined).

These provisions could prevent HVCCC and producers, through the RCG, ensuring track capacity and capacity increases are aligned with port capacity and capacity increases. NSWMC submits that, if the Additional Capacity is endorsed by the RCG and sufficient TOP commitments are contracted to cover the annual capital costs for 10 years through the access pricing provisions, ARTC should agree to the Capacity being built, subject to financing. Again, ARTC's "legitimate business interests" need to be defined to clarify the extent of ARTC's discretion to not construct Additional Capacity for which it has financing and TOP commitments.

Furthermore, there appears to be no provision for financing HVCCC recommended Additional Capacity by any other party if ARTC chooses not to finance that Additional Capacity. NSWMC submits that, if ARTC chooses not to finance the Additional Capacity, then Access Holders and Applicants should have the right, individually or in a group, to finance it and to equitable recovery of their capital cost contributions from other users of the Additional Capacity.

Thirdly, the Project Completion Conditions Precedent in the Train Path Schedule of the proposed IAHA appear to give ARTC the opportunity to decline to fund a specific expansion required to deliver Base Path Usages, even after an Access Holder Agreement is signed, removing the certainty that ARTC will provide capacity even if it has entered into an Access Holder Agreement.

NSWMC submits that, at the time of signing an Access Holder Agreement, ARTC should commit to provide the Additional Capacity need to fulfil the Agreement.

2.2 Greater ARTC Accountability for Delivering Contracted Capacity

Access Holders are required to pay TOP charges whether or not they use their contracted rail access capacity. Conversely, coal producers face serious economic losses if ARTC does not provide the capacity needed to deliver contracted volumes.

The True-Up Test is currently the only means of recompense for Access Holders in the event that ARTC fails to deliver the required Train Path Usages, given the liability exclusions in the proposed IAHA. It is therefore critical that the True-Up Test ensures that ARTC is held accountable for any Capacity Shortfalls that it causes.

NSWMC therefore submits that, to be effective as an incentive for ARTC to run the Network efficiently, the True-Up Test must be transparent with independent verification by HVCCC, particularly of the Network Path Capability (NPC) since no rebates will be paid if NPC is overestimated. Moreover,

- The determination of NPC should align to the modelling done by the HVCCC, which is a more rigorous approach than that currently proposed by ARTC.
- ARTC should use the transparency contained in HVCCC publications as a guide for the level of transparency needed in its True-Up Test publications.

NSWMC therefore submits that the True-Up Test should also be comprehensive, including Tolerance. Tolerance is a key system-wide right which allows Access Holders to adjust the use of their allocated BPUs between Periods in order to accommodate the variability of the Hunter Valley Coal Chain. As Access Holders will pay for Tolerance as part of the Access Charges ARTC should be required to compensate Access Holders if it does not make Tolerance train path usages available.

2.3 Provision of Accurate, Timely Access Pricing Signals

ARTC's Hunter Corridor Capacity Strategy Studies have foreshadowed the need for up to \$2 billion of additional below rail investment to expand capacity over the next 10 years. Investments of perhaps \$1 billion in new rolling stock with operating lives of 15-20 years are also being contemplated by rail operators and coal producers to increase capacity over the period and operate more efficiently.

To ensure efficient investment by ARTC in below rail assets and allow coal producers and rail operators to optimise their selection of rolling stock, accurate and timely provision of access pricing signals will be required. However, the provisions of the proposed 2010 HVAU dealing with access pricing will not provide accurate and timely price signals.

Firstly, the process and timing for determining the Indicative Service and Indicative Access Charges is quite uncertain. In s4.16 of the proposed 2010 HVAU, ARTC is now required to submit to the ACCC, within 12 months of the determination the efficient train configuration, the characteristics, developed in consultation with HVCCC, and charges for Indicative Services.

However, this submission could be up to 4 years after the undertaking comes into effect and, if accepted by the ACCC, in which case the new indicative service and charges are unlikely to apply until the sixth year of the undertaking.

Moreover, in a letter to NSWMC dated 6 May 2009, ARTC made a commitment to "pricing parity" on a GTK basis between 91 wagon and 74 wagon trains in Pricing Zones 1 and 2, for a period of not less than 5 years from the commencement of the undertaking, to apply to Interim Indicative Services which may become non Indicative Services when the Indicative Service is eventually determined. The status and applicability of this commitment in the context of the proposed 2010 HVAU is unclear and the commitment suffers from not being incorporated in the proposed 2010 HVAU itself.

The delay in determining the characteristics and charges for the Indicative service will prevent coal producers and rail operators investing in the most efficient rolling stock during this period. Conversely, determining an Indicative Service which has different characteristics to the Interim Indicative Services will disadvantage those who have invested in rolling stock (with a working life of 15-20 years) in good faith in recent years.

To address these issues, NSWMC submits that the proposed 2010 HVAU should clearly provide for:

- Conditional on grandfathering of existing rights as set out below, ARTC to promptly propose to the ACCC within a fixed period (e.g. in 1 year) the characteristics of, and charges for, the Indicative Service to facilitate rolling stock investment;
- Interim Indicative Services for existing and currently committed capacity to be grandfathered for a period of five years, consistent with ARTC's commitments to industry and the Commission's previous Draft Decision; and
- ACCC to consult with Access Holders & Seekers in considering ARTC proposals.

Secondly, the principles & criteria for charge differentiation set out in s4.14 of the proposed 2010 HVAU and for limits on charge differentiation set out in s4.15 are poorly defined. While there have been some minor improvements from the April 2009 HVAU, the range of factors remains too broad and their application in determining the differentials from the Indicative charges is completely unspecified. In this form, they provide no certainty that the price differentials will be determined on an equitable and efficient basis and no price signals to Access Holders and to future Access Seekers.

This is particularly critical because, after the Indicative Service defined, a substantial proportion of existing coal services will become non-Indicative Services and subject to charge differentiation. Furthermore, all coal services seeking and granted Access Rights in the period before the Indicative Service is determined by ARTC and accepted by the ACCC will not know what service characteristics they should be using to purchase rolling stock and otherwise structure their operations.

NSWMC submits that differential pricing should be based on the effects of service characteristics on the efficient use of Capacity and Coal Chain Capacity rather than the broad range of potentially subjective criteria which ARTC can use under the provisions the proposed 2010 HVAU.

NSWMC acknowledges that, if ARTC is unable to determine the Indicative Service at this point it will also be unable to determine, at this point, appropriate price differentials reflecting variations in service characteristics. NSWMC therefore submits that the proposed 2010 HVAU should require ARTC to:

- Apply the same process as it applies to develop, in consultation with the HVCCC, the proposed characteristics of the Indicative Service under s 4.16 in order to develop the proposed service characteristic variations and price differentials for non-Indicative Services; and
- Submit to the ACCC, at the same time that it proposes the Indicative Service under s4.16, the proposed service characteristic variations and price differentials for non-Indicative Services and seek the approval of the ACCC to vary s 4.14 & 4.15 of the undertaking accordingly.

2.4 Contractual Alignment Through Capacity Management Protocols

An essential objective of the coal producers and the infrastructure service providers in the Hunter Coal Chain must be improved contractual and operational alignment of all elements of the Coal Chain to facilitate optimal use of the assets on a whole-of-Coal-Chain basis. The importance of this objective is highlighted by consideration of the massive sunk and future investment expenditure of the stakeholders in the Coal Chain and the critical importance of meeting throughput objectives in a timely manner.

The identification and management of capacity gains and losses under the HVAU is a critical element of this capacity management process and NSWMC has previously identified the need for mechanisms to identify the causes of Capacity losses and allocate responsibility to parties causing them, so that the impact of these losses on other Access Holders is diminished as far as is reasonably possible and there are drivers to improve the utilisation of Capacity.

NSWMC acknowledges that the proposed 2010 HVAU incorporates new provisions for the review of a mechanism to identify and assign Capacity losses in s5.9. They provide that, within 12 months, ARTC, in consultation with HVCCC and with input from Access Holders and service providers, will commence a review of policy and processes for allocating losses of capacity caused by Access Holders and their Operators and may submit to the ACCC a proposal to vary the HVAU aimed at increasing Capacity and allocating the impact of a shortfall to the Access Holder causing it.

NSWMC submits that a more definite and certain requirement is needed and therefore that ARTC should be obliged to submit a proposal, based on the HVCCC recommendations, to ACCC within 18 months. Furthermore, the process should not be restricted to losses caused by Access Holders and their Operators but should reflect a whole-of-Coal-Chain approach and encompass losses caused by other service providers including ARTC and the port terminal operators. It will be important to ensure that gains in one area are not at the expense of losses in another part of the coal chain.

To achieve this objective, NSWMC submits that the review should be co-ordinated by the Hunter Valley Coal Chain Coordinator (HVCCC), not ARTC, in view of the HVCCC's existing role of planning and co-ordinating the co-operative daily operation and long term capacity alignment of the Hunter Valley Coal Chain. However, it will be necessary for ARTC to constructively participate in this process and be willing to adopt the HVCCC's recommendations in the proposal that it submits to the ACCC for an appropriate variation of the undertaking.

Consistent with this approach, NSWMC submits that the proposed 2010 HVAU should provide for the review to specifically address, and propose solutions for the following related concerns

- The five day period for Capacity Shortfall events currently proposed in s 5.5 & 5.6 of the Proposed 2010 HVAU and clause 6 of the proposed IAHA will, in practical terms, have the effect of providing ARTC with total discretion to allocate all likely shortfalls in track capacity, with no regard to either "at fault" or "affected producers", potentially leading to inequitable outcomes; and
- The approach to addressing Network Capacity losses due to Train cancellations in clause 11.6 of the proposed IAHA is inadequate and will not facilitate contractual alignment.

2.5 Incentives to Align ARTC and Access Holder Interests

Coal producers believe that the interests of ARTC and Access Holders will be more strongly aligned if there are appropriately structured incentives for ARTC to pursue efficiency in capacity utilisation and other key operating performance indicators as well as in capital and operating cost management.

The only significant performance incentive in the proposed 2010 HVAU is the rebate of TOP charges under the True-Up Test although a new s8.3 now requires ARTC to comply with performance incentive schemes which it will propose before acceptance of the undertaking.

In principle, coal producers are prepared to support the inclusion of well designed performance improvement incentive mechanisms that will lead to gains in the throughput of the Hunter Coal Chain as a whole and reduce the capital expenditure otherwise required for Additional Capacity. In particular, coal producers would support incentives which:

- Allow ARTC to earn additional revenue subject to maintaining Access Holders' access to their Base Path Usages and Tolerance
- Encourage ARTC to achieve improved safety and operating performance
- Drive operational improvements that reduce operating costs and reduce capital investment requirements.

However, NSWMC submits that there must be adequate opportunity for coal producers and other stakeholders to carefully consider the details of such mechanisms before the ACCC issues a Draft Decision on the proposed 2010 HVAU.