Peabody ENERGY

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Mr Mathew Schroder
General Manager
Fuel, Transport &Prices Oversight Branch
Australian Competition and Consumer Commission

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Dear Mr Schroder

Submissions of Peabody Energy Australia Pty Ltd in response to the Australian Rail Track Corporation Limited's ("ARTC") application to vary the June 2011 Hunter Valley Coal Network Access Undertaking (HVAU) in relation to non-TUT-related performance incentive mechanism

1 About Peabody

Peabody Australia Mining Pty Ltd, a subsidiary of Peabody Energy Australia Pty Ltd (**Peabody**) holds a long term contract with the Australian Rail Track Corporation for the provision of Access Rights in the Hunter Valley.

Peabody is responsible for large-scale mining operations across Australia. It operates seven coal mines in Queensland and three coal mines in New South Wales. These mines produce a broad range of metallurgical and thermal coals which are exported through Queensland-based ports located in Mackay and Brisbane and New South Wales-based ports in Newcastle and Wollongong.

2 Introduction

Peabody believes that the approach taken by ARTC in the formulation of the non-TUT related performance incentive mechanisms do not appropriately align with the provision of capacity to meet the contractual and operating requirements of the Hunter Valley coal chain prior to the recognition of performance incentives.

Peabody submits that the incentives as proposed should not be accepted in their present form; however Peabody does support the ability for ARTC to be rewarded for performance and as an active industry participant Peabody is open to working with ARTC in the formulation of appropriate incentive mechanisms.

The following submissions will outline the broad issue for the incentives to align to capacity and briefly review the two primary incentive measures as identified.

3 Submissions

Peabody sets out below its submissions in relation to the ARTC's proposed variation to the June 2011 HVAU (**"Proposed Variation"**).

3.1 Coal Chain Capacity

Peabody submits that the primary consideration for ARTC to consider (aside from safety) is the provision of capacity to support the contracted volumes of the coal chain factoring the operating characteristics of the various ports and above rail operations.

As the performance metrics as submitted by the ARTC do not seek to provide capacity as a primary basis of service delivery prior to achieving incentives that may be outside of or seek to guarantee relevant ceiling revenue limits, Peabody cannot presently support the introduction of any proposed incentive measure.

3.2 Additional Capacity Investment Innovation Incentive (ACIII)

Peabody supports mechanisms that seek to support innovation in the provision of capacity where there is a corresponding cost offset from traditional capital programs but only to the extent that the capacity increases are realisable, will not result in a future capacity deficit and have not been as a result of previous capital programs.

Where there are realisable decreases in cost and/or the ability to contract additional capacity, Peabody believes that appropriate offsets be in place reduce the risk of 'double counting' by ensuring, as an example that an increase in the in the regulated asset base is offset by a decrease in unit rates where there is an increase in contracted capacity.

As the mechanism of the ACIII relates to a potential increase in the value of the Regulated Asset Base, this metric should be viewed only as an alternative method of capacity delivery which recognises innovation in a similar view to capital but which is not an annual performance incentive.

3.3 Positive Performance Incentive Metrics

Peabody submits that the performance incentive scheme metrics as outlined in the proposed variation should not be accepted in their present form as there are a variety of inconsistencies such as;

a) The metrics as identified do not consider the delivery of capacity prior to the implementation of the incentive

b) The metrics while important for measuring the availability of the network to support the capacity are within the scope of the general operation of the network which is captured within the scope of the relevant return on investment.

c) The reporting framework to which the incentives apply is not clear.

d) The potential cost of the incentives is not clear and the extent of revenue that can be raised from the incentives is not clear.

e) The timeframe for the incentives should be an annual true up (despite reporting period) to ensure capacity is available consistently throughout a year.

4 Summary

Peabody submits that while it is supportive of the ability for ARTC to be rewarded for performance and innovation and is agreeable to work with the ARTC in the development of appropriate incentives, the incentives as proposed should not at present be accepted as:

- The Incentives as proposed do not align to the provision of contracted coal chain capacity.
- The Additional Capacity Investment Innovation Incentive is not necessarily a performance mechanism but an alternative form of capacity delivery.
- The Positive Performance Incentive Metrics are incomplete, do not align to capacity and are presently within the scope of the provision of the network and relevant return on investment.