PORT WARATAH COAL SERVICES LIMITED

Authorisation Application Nos A90906, A90907, A90908

Capacity Distribution System to address the problem of extensive vessel queues off the Port of Newcastle

Further submission on authorisation application and response to matters raised at the Commission’s pre-determination conference on 27 April 2004

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1 Section One - Executive Summary

Purpose of submission

1.1 This further submission in relation to the applications for authorisation A90906, A90907 and A90908 is made by Port Waratah Coal Services Limited (“PWCS”) in response to the following matters:

• the Commission’s draft determination issued on 8 April 2004;
• submissions by interested parties at the pre-determination conference held in Newcastle on 27 April 2004;
• issues raised in recent submissions to the Commission by interested parties; and
• the Commission’s press release issued on 13 May 2004, concerning the scope of the existing interim authorisation.

Executive summary

(a) Context of applications

1.2 The applications for authorisation in this matter were lodged with the Commission on 5 February 2004 in the context of a substantial vessel queue off the Port of Newcastle, leading to an estimated cost of demurrage of at least A$200 million in 2004 (using conservative estimates of demurrage costs). This vessel queue arose from an unprecedented level of demand for coal in Asia and coal supply chain capacity limitations in the Hunter Valley. In particular, as the Commission has noted, coal supply chain infrastructure involved in moving coal from mines in the Hunter Valley is not able to meet the amount of coal which producers wish to export. Latest information from the relevant government authorities suggests improvements in rail infrastructure will now not occur until Q1 2006 at the earliest.

(b) Positive Public Benefit from the Capacity Distribution System

1.3 The Capacity Distribution System (“CDS”) has now been operating at the Port of Newcastle under the interim authorisation granted on 5 March 2004 for over 2 months and PWCS believes that the positive results achieved during that time speak for themselves. The vessel queue has reduced from a peak of 56 vessels on 14 March to the current level of 10 vessels. This, in turn, has resulted in a significant reduction in vessel waiting times and, therefore, in the amount of demurrage being incurred. PWCS estimates (cross checked against actual data provided by the major coal producers in the Hunter Valley to PWCS) are that at least $14 million (USD$10 million) has been saved by producers in the short period to date under the CDS and estimated demurrage savings would be in excess of $200 million (USD$150 million) by 31 December 2004 (without the CDS, the forecast
demurrage for 2004, assuming vessels arrived in accordance with producer forecasts, is estimated to be higher than $300 million)\(^1\)

1.4 Throughout the period that the CDS has been in operation, PWCS has been able to achieve record levels of throughput at its coal terminals and, together with other participants in the coal chain, achieve significant operational improvements and efficiencies. Given that the CDS has not reduced coal throughput through the Port of Newcastle, it is difficult for anyone to show any quantifiable public detriment. Calculations by the independent CDS Administrator, Accenture, show that the operation of the CDS would have marginal, if any, impact on the actual amount that producers would have been able to export in the absence of the CDS given capacity constraints. This applies irrespective of the claim by some small producers that they would have been able to better manage their exposure to a queue than others - even if they could avoid demurrage costs by short term vessel charters, the loading of their vessel in a queue passes on demurrage costs to others in the line.

1.5 In addition, rather than decreasing the amount of coal that is exported through the Port of Newcastle, PWCS' initiatives (which have been implemented in the context of the CDS) have actually increased the volume of coal exported. The operation of the CDS, through the distribution of capacity and attendant certainty of loading times, has reduced the vessel queue and improved vessel turnaround, with a resulting improvement in the reputation of the Port of Newcastle and coal export reliability from the Hunter Valley - all factors improving Australia's international competitiveness. These are significant public benefits which arise in addition to the demurrage cost savings.

1.6 The issuing of loading rights and the nomination of vessels against those loading rights under the CDS enables PWCS to draw the following factual conclusions as to the impact of the CDS on participants and others involved in the coal chain:

- the four larger producers (defined in the CDS Protocols as those producing over 3.5Mtpa) have borne the brunt of reductions in shipping in percentage terms to bring the queue back into balance, with an average reduction of 20% in Q2 against their forecasts submitted to PWCS via Barlow Jonker. In volume terms, those larger producers have contributed an even greater share of the reduction required, with a reduction in shipping tonnage nominations against forecast of 3Mt in Q2 alone. **Nevertheless, three out of the four “larger” producers support the CDS;**

- of the nine active smaller producers which submitted forecasts to PWCS via Barlow Jonker, the maximum reduction in shipping against forecasts is 6% over the year, and the average is much lower. The reason for these more modest overall reductions is that PWCS allows a flexibility provision of 90,000t, which offsets the common percentage reduction, and because for these smaller players the reductions are spread across the year. PWCS remains confident that with the return of loading allocations by some producers and the release of additional loading allocation through improved performance, even these modest effects will be significantly mitigated by the end of the year. **Of this group, five of the nine have (publicly or privately) indicated to PWCS their support of the CDS;**

- concerns over new entrants and allocation “hoarding” have proved unfounded. PWCS has provided loading allocations to Newpac, a new producer which raised

\(^1\) PWCS believes that the reduction in demurrage and transport costs is a substantial public benefit. That benefit is passed on to the Hunter Valley and Australia through Australian and international coal companies operating in the Hunter Valley in terms of shareholder returns, investment and employment, with particular multiplier effects in the Hunter Valley community.
concerns about entry, and has done so in a fair and reasonable manner. Production changes, such as the delayed start of Ashton and the impact of an underground fire at Southland, have been smoothly incorporated into the CDS and allocations have been re-distributed in a timely manner by the CDS Administrator. In this regard, there are already examples of unused allocation being returned by the CDS Administrator to other producers via the Administrator or directly between Producers and the CDS has been designed to provide such flexibility; and

• concerns about the effect of the CDS on indirect sales channels (such as traders or online marketplaces) have not manifested in the volume of business conducted through those sales channels, based on actual data, not supposition. Sales through traders have continued to increase following the introduction of the CDS. In fact, sales in the last quarter recorded through “non asset-backed traders”, the category that has proved most vocal, have been higher than any quarter on record. Similarly, Newcastle trade on globalCoal has been substantial in May, with 160Kt of physical deals and well over 200Kt of swaps. In fact, Newcastle instruments have dominated trade in May compared to Richards Bay and European instruments, where no CDS exists. Accordingly, PWCS believes that if traders are willing to pay the market price for coal, coal is available under the CDS.

1.7 Accordingly, PWCS believes that the CDS:

• is working in terms of reducing the vessel queue and matching coal chain logistics with incoming vessels;

• is delivering (and will continue to deliver) significant public benefits; and

• has limited (if any) public detriment and in particular appears to have no detrimental impact on the level of competition between producers, traders and in the coal industry generally.

(c) Strong Demand and the coal chain bottleneck

1.8 PWCS believes that there is no substance to the argument that the vessel queue is reducing because of decreased demand, rather than due to the CDS. All industry forecasts and expectations are that the current levels of global demand for coal will continue. In fact, far from abating naturally as some submissions have suggested, demand for coal has continued at unprecedented levels. This is evidenced by continually increasing prices, despite increases in physical supply from Newcastle. For example, the monthly Newcastle price indices as published by globalCoal have increased in every month so far this year as follows:

• Dec 03 US$36;
• Jan 04 US$41;
• Feb 04 US$43;
• Mar 04 US$54;
• Apr 04 US$56; and
• May 04 US$58 (MTD as at May 28).

Price is the best indicator of demand for coal and price is not decreasing.
Accordingly, market forces have not acted to moderate queuing or even correct the steady upward trend in the last eighteen months. However, in contrast, within weeks of the implementation of the CDS, substantial benefits in terms of reduced queuing are clearly evident. PWCS believes that this clear evidence supports its contention that the primary issue is the limited capacity of the coal supply chain in the Hunter Valley, which is creating a bottleneck. Market forces will not prevail in a bottleneck situation, particularly while there is such a high level of demand.

1.10 In relation to the level of demand from China, even if China is now seeking to ensure it has a sustainable level of economic growth over the next few years, the level of demand for coal in China and elsewhere in Asia is still forecast to increase over the next few years (see, for example, the attached article from the Washington Post included in Attachment A). There has been a groundshift in the state of economic development of China and the expectations of Chinese consumers and that will not change through a tightening of credit.

1.11 On this basis, PWCS believes that the current levels of strong demand (and, therefore, if the CDS is not implemented, vessel queues) are likely to continue for the foreseeable future and certainly it is expected to persist until at least the end of 2004. PWCS also notes that any planned expansion of rail infrastructure is now also being pushed back into Q1 2006, such that infrastructure limitations will continue.

(d) The CDS is a short term solution

1.12 The CDS is intended as a short term solution. It provides an opportunity to address the vessel queue and work on longer term arrangements (e.g. a take or pay arrangement), which provide better commercial signals and incentives to match supply and demand.

(e) The fairness of the CDS

1.13 PWCS is currently working with Accenture to design and implement a longer term solution to the current imbalance between demand and capacity in the Hunter Valley coal chain. However, PWCS believes that until a longer term solution can be implemented, the CDS represents the fairest, most equitable and most practical way of addressing that imbalance. In this regard, the CDS:

- is based on forecasts provided by producers themselves to an independent third party;
- is based on, and is operating under, a set of clearly defined and transparent rules; and
- is administered by a reputable, independent and accountable external organisation in Accenture.

1.14 It is inevitable that any system of distributing limited capacity will lead to some criticisms of inequality or unfairness. This is because it is neither practicable nor possible for PWCS to

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2 In response to the submission from BHP Billiton dated 3 June 2004, PWCS notes that no producer has since suggested that it intends to export at lower rates than those nominated in its forecast provided to Barlow Jonker. As previously advised, PWCS is not at liberty to make the individual Barlow Jonker producer figures publicly available because certain producers have declined to consent to their forecast being made publicly available – see paragraph 5.2 of this submission. PWCS also believes that, leaving aside the additional coal anticipated from BHP Billiton's mines in the Hunter Valley (see BHP Billiton's submission dated 23 February 2004 which states that it has "recently spent approximately US$400 million to expand the Mt Arthur Coal mine from a 4 mtpa operation to a 12 mtpa operation over a three year period"), there is ample evidence of strong production in the Hunter Valley from other producers seeking to sell larger quantities of coal in this market environment.
take into account the individual circumstances of each industry participant. In addition, PWCS has an obligation to operate the Port of Newcastle as a common-user terminal and, therefore, consistent with that obligation, any distribution of capacity has to be effectively on a pro rata basis.

1.15 However, PWCS has also appointed Accenture as an independent party to administer and oversee the operation of the CDS and to address as many of these concerns as to the “fairness” of the CDS as is practicable. PWCS accepts that the short term CDS is not a perfect solution. However, as the Commission is well aware, it has never been intended to be anything other than a short term solution while a longer term solution is considered and progressed.

1.16 In addition, despite the myriad of arguments that have been raised by certain parties as to why the CDS is unfair in how it applies, no party that opposes the CDS has proposed any solution other than to “do nothing”. Importantly, no producer or trader which has complained in relation to the CDS authorisation has been able to show that they would have been able to export more coal if the CDS was not operating.

1.17 In this regard, the CDS merely crystallises the restriction which already exists because of the supply chain bottleneck. The CDS does not itself restrict throughput and so any arguments of detriment based on revenue loss can hold no water in aggregate. Opponents of the CDS have apparently interpreted the CDS as the cause of the restriction. However, the facts clearly support the existence of the supply chain bottleneck. While some opponents would prefer that they could send any number of ships to ensure that their tonnes gain preference, this would necessarily remove tonnage from other PWCS customers. The end result would be higher total cost and the same throughput – with no guarantee of a significantly different tonnage distribution, let alone a fairer outcome.

1.18 In many respects, as set out in the Coal and Allied submission dated 19 May 2004, the CDS provides increased certainty that coal will be exported. Again, this is a clear public benefit.

(f) The ability to swap capacity allocations

1.19 The ability for producers to exchange, swap or otherwise acquire loading entitlements will further ensure that the CDS delivers economically efficient outcomes, both in terms of:

• ensuring that participants who need to obtain additional loading allocations are able to do so; and

• providing producers with an additional incentive to ensure that the port facilities will not be under-utilised if there is a change to the timing (or any other aspect) of individual producers’ requirements.

1.20 This ability is consistent with the more “market-based” solutions that the industry is striving for in the longer term and should produce mechanisms to address practical and operational issues that arise day-to-day as well as some of the criticisms of “unfairness” in the pro-rata distribution of capacity.

(g) The role of PWCS and the impact of a vessel queue on the reputation of PWCS

1.21 While PWCS is working with industry participants at all levels of the coal supply chain in the Hunter Valley, the CDS is solely a solution for the Port of Newcastle and it is being put forward by PWCS as the operator of the port to address the impact of the vessel queue on its customers, its operations and its reputation as an efficient port operator. It is not, as some submissions have suggested, PWCS seeking to implement an “industry solution”.

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1.22 PWCS is also continuing to work with other coal chain logistics providers to maximise the capacity of the coal chain. It is also continuing to work with Accenture and other key stakeholders in developing a longer term solution to the vessel queues caused by current capacity constraints. Even parties objecting to the role of PWCS in the short term CDS solution have put forward PWCS to resolve the long term position.

1.23 The Washington Post and other articles also clearly demonstrate that there is local and international recognition of the vessel queue problem at Newcastle and, therefore, PWCS submits, a clear reputational issue for PWCS. On this basis, PWCS firmly believes that there is a need to solve the current vessel queue problem to prevent further damage to the international reputation of the Hunter Valley and its coal chain export capability.

(h) Conclusion - The CDS is delivering significant public benefits with little, if any, public detriment

1.24 Since the Commission granted interim authorisation on 5 March 2004, the legal and economic arguments opposing the authorisation have changed from opposition that the CDS operated unfairly and would not work, to now being focused on the reduction in the vessel queue not being the result of the CDS, so that it should be removed in any event. However, irrespective of the range of issues that have been raised (most of which are highly technical and theoretical in nature from an economic and legal perspective), PWCS believes that the operation of the CDS under the interim authorisation provides the best evidence to the Commission of whether the CDS should be granted authorisation.

1.25 The factual evidence that has been provided previously and with this submission, clearly shows that:

• the vessel queue has been reduced from a peak of 56 vessels on 14 March 2004 (following a continual increase over the previous 18 months) to 10 vessels as of 10 June 2004 and a forecast of 5-10 vessels at the end of June 2004. The reduction in vessel queues and waiting times has had a clear impact in reducing wasteful demurrage payments by producers. As acknowledged by the Commission, this is a significant public benefit. Contrary to some arguments in submissions concerning public benefits in the context of mergers, in this authorisation application, the reduction in demurrage is quantifiable based on actual data provided by the coal producers;

• the throughput of the port not only reached but exceeded the “stretch” targets developed as part of the CDS. This increase in exports is a clear public benefit and the fact that there has been no reduction in exports suggests that there is no public detriment; and

• PWCS can deliver against its commitments and act in the interests of its reputation and long term position as a dependable and timely performer as a loading port. Again, the increased certainty as to loading and delivery times is a clear public benefit as it improves Australia’s international competitiveness in relation to coal exports.

1.26 In summary, PWCS believes that the CDS delivers (and is already delivering) significant public benefits both in terms of the reduction of wasteful demurrage and in terms of the benefits to the international competitiveness of the Australian coal industry. Those benefits outweigh any short term or transitory impact on competition (e.g. in the global market for coal trading or in any market in which coal producers operate).
1.27 In this regard, PWCS submits that those producers (large or small) who oppose the CDS have not been able to demonstrate that they would have been able to export their coal production given the capacity constraints in the coal chain and therefore no public detriment has been shown, nor any negative impact on competition as a result of the CDS on a with or without basis. As part of the CDS, PWCS has established clear throughput goals and any failure to achieve these goals reports directly to increased queuing. In aggregate, the capacity of the coal chain is not reduced by the CDS, but may in fact be increased by the specific commitment of PWCS and the coal chain to ‘stretch’ throughput targets.

1.28 Accordingly, PWCS believes that the careful balancing process that the Commission has conducted to date is appropriate and that the material before the Commission (and in particular the incontrovertible factual evidence of the benefits from the operation of the CDS gained from the experience of the interim authorisation) supports the grant of the authorisations requested from the Commission.

Structure of submission

1.29 This submission is structured as follows:

- **Section 2** - sets out further information in relation to the operation of the CDS;
- **Section 3** - sets out further information in relation to the continued need for the operation of the CDS;
- **Section 4** - sets out further information in relation to the substantial public benefits which result from the operation of the CDS;
- **Section 5** - sets out further information in relation to the alleged impact of the CDS on various market participants;
- **Section 6** - provides information in relation to the importance of swaps and other exchanges of loading allocations to the efficient operation of the CDS;
- **Section 7** - sets out PWCS’s response to the various conditions which have been proposed by certain interested parties and further information in relation to the impact that those conditions would have on the effective operation of the CDS; and
- **Section 8** - sets out a brief conclusion.
2 Section Two - The Operation of the CDS

Introduction

2.1 In this matter, where the Commission has granted an interim authorisation and the CDS has been operating for just over 2 months, PWCS submits that, in preference to theoretical economic and legal arguments, the best evidence of the public benefits arising from the CDS is the actual reduction in the vessel queue and therefore the reduction in demurrage, as well as benefits to the international competitiveness of coal exports from Newcastle. In terms of the public detriment anticipated by the Commission in the draft determination, there is no evidence of a loss in throughput at the Port of Newcastle. Accordingly, the only argument as to detriment is whether some “small” producers have unilaterally chosen to reduce production or whether there is some other claimed form of adverse impact on them. The data provided in this submission indicates that:

- the larger producers have had a higher proportionate reduction in capacity and that many smaller producers also benefit from the reduction in demurrage and have not opposed the CDS;
- there is no certainty that those “smaller” producers would in fact have been able to export their coal production absent the CDS because of capacity constraints; and
- many of the “smaller” producers opposing the CDS are in fact part of larger listed organisations or are subsidiaries of international businesses, such that the “impact” on them is arguably much less than has been claimed.

2.2 PWCS believes this, rather than technical arguments, is the key issue. As PWCS does not wish to be argumentative with issues raised by some industry parties which are also its customers, the focus of this submission is the practical operation of the CDS under the interim authorisations and actual benefits to the Australian public.

2.3 Since the commencement of the CDS:

- the increased congestion trend (see Graph 1 below) has been reversed and queues are now reducing in line with expectations. In fact, at time of writing, the queue is 10 vessels and is forecast to stabilise at a working level by the end of the June (see Graph 2 below) – barring failure of producers to meet their own objectives and commitments, the queue will not reduce to a point that affects the ability to rail coal to the port;
Graph 1

Vessel Queue (vessels off port) – Pre CDS

Source: Administrator

Note: The vessel queue increased to > 20 vessels in early 2003, then ~30 in September 2003 and continued to grow.

Graph 2

Vessel Queue (vessels off port) – Post CDS

Source: Administrator

Note: From a peak of 56 vessels in March 2004, the CDS has managed the queue down to approx. 10 vessels, a level which is predicted to be maintained until the end of June.
waiting times for vessels, expressed as average days in queue, have also steadily decreased (see Graph 3 below), with further significant falls forecast as the recent halving of the queue takes effect (current forecast waiting times are less than 5 days);

**Graph 3**

![Average Days in Queue](image)

Source: Administrator

the administrative implementation has been smooth, with changed nomination procedures working and daily tonnage reports available. The quarterly “control” periods have also been shown to work: in fact, allocation usage has overall tracked the linear expectation very closely (see Graph 4 below);

**Graph 4**

![Comparison of Tonnes "Used" against Loading Allocation](image)

Source: Administrator
the CDS has been compatible with continued efforts to improve coal chain throughput. In this regard, PWCS and the Administrator have distributed an additional 1Mt of loading allocation for the second half of 2004 (to be used by September 2004) as a result of improved coal chain throughput. This deals with many arguments that the CDS will not re-allocate increased or excess capacity.

2.4 As stated at the pre-determination conference, given that the reduction in loading entitlements for small producers was less in Q2, PWCS anticipates that the queue will be around 5-10 vessels by the end of June 2004. PWCS will endeavour to maintain a working queue of around 10 vessels for most of the remainder of 2004.

2.5 PWCS believes that the reduction in vessel waiting times has resulted in a significant reduction in the amount of demurrage being paid by producers for vessels to lie idle off the coast. This applies irrespective of the value/cost of demurrage argued by some parties. The CDS has also resulted in increased certainty in delivery times, which is a significant benefit for coal producers, traders, buyers and ship owners - a benefit for Australia and the Port of Newcastle in terms of an increased ability to compete with overseas ports and coal producers, further enhancing the reputation of PWCS.

2.6 Accordingly, PWCS believes that the CDS is working and that it is already resulting in significant public benefits.

Continued improvements in coal chain capacity

2.7 One of the initial concerns expressed by certain interested parties is that the CDS would reduce the incentives for PWCS and others to achieve improvements in the capacity of the coal chain and greater efficiencies in the delivery of coal chain services. However, PWCS believes that the experience over the past 2 months demonstrates that, in fact, the opposite is true and that PWCS’s initiatives (which it has implemented in the context of the CDS) have led to increased coal exports from the Port of Newcastle. This is a clear public benefit.

2.8 The Coal Chain Weekly Reports previously provided to the Commission clearly demonstrate that there has been no reduction in the amount of coal shipped through the port.

2.9 PWCS has also demonstrated its continued ability to load all coal received onto vessels. In this regard, April 2004 under the CDS was a record month for PWCS, with over 7 million tonnes loaded. **This is a new shiploading record.**

2.10 Therefore, contrary to concerns by certain other industry participants, PWCS believes that the cause of the current vessel queue is not a result of any deficiencies in its performance.

2.11 In addition to taking steps to improve its own performance, PWCS is also continuing to work with other coal chain participants to increase rail delivery throughput. As demonstrated by **Graph 5** below, the performance of the coal chain is continuing to improve. Daily tonnage for rail delivery in April and May averaged almost 240Kt per working day, up significantly from the 220Kt performance that was typical of the preceding period. This level corresponds to an annual rate of between 80Mt (335 working day year basis) and 82Mt (345 working day year basis).
In addition to tonnage measures, a particular focus of PWCS has been on coal chain reliability. PWCS has been working on maintenance improvement for several years, with the introduction of a new planned maintenance system in early 2003 and regular maintenance reviews by senior management. One indicator of this is the number of mentions of disruption in daily coal chain reports. While this indicator is not a throughput measure (most PWCS disruptions do not lead to train cancellations), it does provide a process measure of maintenance improvement. As shown by Graph 6 below, PWCS has substantially reduced the number of events reported.

**Graph 6**

Source: PWCS
Accordingly, PWCS believes that it has successfully pursued short term performance improvement, working with other coal chain participants. PWCS has already provided evidence of this in a variety of reports and submissions. However, the most compelling evidence is the results over the past 2 months. PWCS notes one of the arguments in the submission from Donaldson Coal that the rate of ship arrivals has fallen below the rail receival rate at Port Waratah. PWCS does not propose to deal with that submission in any detail as that criticism is instructive as to an apparent fundamental misconception of the logistics management of the export coal chain. In order to reduce the vessel queue, it is of course necessary to reduce the ship arrival rate below the rail receival.

In parallel, PWCS has also been pursuing a number of medium and long term improvements in coal chain capabilities. In particular:

- PWCS and Pacific National ("PN") jointly commissioned a study in early 2004 to determine how best to expand coal chain capacity to 95Mtpa and ultimately to 120Mtpa. A range of improvement and capital projects have been derived from this work and are being progressed with asset owners;

- PWCS has supported PN in implementing a repowering of the Hunter Valley coal train fleet which, in conjunction with a new timetable developed by Railcorp, has substantially increased the timetable coal paths available and mitigated track constraints. PWCS has agreed to fund the incremental costs of the initiative above PN revenue for 2004, to an amount of $6 million;

- PWCS has been actively engaged in discussions with ARTC and the New South Wales and Federal Governments and their agencies to ensure that track capital is progressed despite the delays in completing the lease of track to ARTC. This effort has included public statements, meetings with senior ministers and meetings with bureaucrats and the agencies concerned;

- PWCS projects have been fast-tracked. PWCS has committed over $6 million to refurbish equipment at Carrington Terminal and has commenced engineering studies for Kooragang expansion. PWCS has submitted expressions of interest to the owner of adjacent land at Kooragang, the Regional Land Management Council, to obtain land necessary for it to progress long term expansion;

- PWCS and PN are jointly progressing further planning initiatives, including the development of a multi-million dollar Integrated Planning System, the first two modules of which (stockpile planning and rail scheduling), are due for delivery in early 2005; and

- PWCS is progressing initiatives with BHP Billiton and Queensland Rail to add further to coal chain capacity.

Unfortunately, notwithstanding this progress, all the indications to date are that major capital upgrades are required across the coal chain in order to add significantly to current capacity after short term improvements. These capital projects include track, loadpoint and rolling stock. None of these projects are expected to deliver gains before 2005 and the first significant track project, the Hanbury Grade Separation, is now not due for completion until Q1 2006 at the earliest.

In the time the CDS has been developed, sustainable coal chain capacity rates have been increased from 76 to some 82 million tonnes per annum. PWCS also maintains that any concerns of a “volume cap” are based on a fundamental misinterpretation of the operation of
the CDS, as one of its basic design principles was that throughput be maximised. The recent record performance to levels above the ‘stretch’ target is incontrovertible evidence.

2.17 Accordingly, PWCS submits that the introduction of the CDS has not had any negative impact on either PWCS’s ability or incentive to improve its performance and the performance of the coal chain as a whole.

2.18 PWCS and the Administrator are monitoring throughput and considering the release of additional loading allocations following the good performance of the coal chain in April and May under the CDS, with a view to maintaining moderate queuing and ensuring that all coal chain participants have a continued incentive to maintain throughput at maximum levels.

2.19 PWCS submits that the continued improvement in the coal chain is direct evidence that efforts to improve throughput have been maintained as part of and as a result of the introduction of the CDS. PWCS submits that its extensive, direct and effective interventions have driven real capacity increases which, in turn, has resulted in a public benefit through increased exports. In contrast, there is no evidence that the diffuse, indirect and expensive “queuing signal” (argued by some) has driven any positive outcomes. Similarly, there is no evidence that queuing has of itself had any impact on, for example, the speed of track upgrades.

The CDS is the fairest method of allocating limited capacity in a short term solution

2.20 As the Commission is aware, both PWCS’s estimates as to the likely demand for its services in 2004 and the loading allocations provided to individual producers are based on the forecasts provided by those producers to Barlow Jonker in accordance with the Coal Handling Services Agreement (“CHSA”). The CHSA specifically contemplates in clause 2.4.1 that producers are required to provide accurate forecasts of their likely demand to enable PWCS to develop and plan forward planning systems.

2.21 As set out above, PWCS believes that the capacity of the coal chain in 2004 is likely to be 80-81 million tonnes (depending on the rate achieved in the second half). However, PWCS believes that, in the absence of the CDS, demand for its coal loading services during that period would be at least the 88 million tonnes which producers provided in their forecasts to Barlow Jonker.

2.22 As stated above, PWCS submits that the overwhelming weight of evidence is in favour of continuing high demand. For example:

- as demonstrated in the table contained in PWCS’ previous submission, actual ship arrivals for Q1 2004 were 1% above producer forecasts for that period;

- exports have continued to increase above the levels achieved in January (e.g. exports in April were 7% higher than January, and a new port record, despite being only a 30 day month);

- a number of submissions and comments by other interested parties support PWCS’s view that strong demand for coal from Newcastle will continue (e.g. Excel Coal, the parent company of Wambo, has stated as at 18 May 2004 that:

  “Strong global demand for metallurgical coal, thermal coal and metallurgical coke continues. Spot prices for NSW export thermal coal are currently in excess of US$55 per tonne FOB” - see Attachment B);
although certain producers have suggested that the estimate of 88 million tonnes overstates the demand for PWCS’s loading services, no producer has since suggested that it intends to export at lower rates than those nominated in its original forecast to Barlow Jonker; and

- prices for coal from Newcastle are at unprecedented levels despite the increase in physical throughput achieved at the port compared to 2003.

2.23 In the view of both PWCS and the Administrator, there is no support for any suggestion that the queue has fallen due to factors other than the CDS. In this regard, PWCS submits that the new, high contract prices commencing April 2004 (as recognised by even the small producers) are a response to high demand, not an indication of weak demand in 2004. This is further evidenced by continuing high spot prices.

2.24 In addition, all the evidence from producer submissions is that producers have been managing ship nominations in accordance with the loading allocations specified in the CDS (hence reducing the vessel queue), not because demand has fallen away. The letter from the Administrator set out in Attachment C confirms the Administrator’s view that it is not aware of any reason for the reduction in the shipping queue since 5 March 2004 other than the operation of the CDS.

2.25 BHP Billiton in its submission to the Commission dated 3 June 2004 stated that it believes that the CDS has not been effective in reducing vessel queues, referring to lower producer stocks. Apart from the obvious inconsistency (vessel queues increased rapidly in Q1 as stocks were falling, but BHP Billiton implies that the same level of destocking in Q2 would have been accompanied by a fall in the queue), PWCS has concerns both with BHP Billiton’s presentation of the data and the ‘beliefs’ that are postulated, for the following reasons:

- BHP Billiton data is incorrectly attributed. The Hunter Valley Coal Report is quoted as the source, but this publication merely reports information collected by Coal Services, a company jointly owned by the CFMEU and the NSW Minerals Council, whose principal activity is provision of workers’ compensation insurance. Reported stocks are not a complete picture as ‘in pit’ stocks are not included, only run of mine ("ROM") or product stocks. Further, neither Coal Services nor the Hunter Valley Coal Report collect “estimated export stocks”, only mine stocks, so PWCS assumes that BHP Billiton has interpreted the information without describing its method.

- BHP Billiton has selectively presented information. It has chosen to present only half of a coal market cycle, from the ‘trough’ price lows of late 2002 to the current price highs. In fact, coal stocks were also at low levels in April-May 2001, a comparable point in the price cycle, and also low in 1998/99. Graph 7 below demonstrates that there is nothing unusual in the current level of producer stocks.
BHP Billiton draws a flawed and inconsistent conclusion. To state beliefs about flows (i.e. production) based on data about stocks without evidence of a causal link is respectfully flawed. In its own case, BHP Billiton has low stocks, but maintains its own forecast provided to Barlow Jonker were understated and asserts it can increase production in the absence of the CDS. BHP Billiton has provided an explanation: it has ‘reduced production to try and fit CDS allocations’. However, PWCS is at a loss to explain why BHP Billiton, without evidence, draws the opposite conclusions about other producers from the same evidence: it ‘believes’ that their low stocks mean that the other producers forecasts are overstated and that they cannot increase production as their production levels are unsustainable. PWCS notes the statements made by Wambo and Camberwell at the pre-determination conference at Newcastle and in their written submissions to the Commission which confirm that they will build stockpiles of coal – see paragraph 5.5 of this submission.

PWCS submits that to the extent that any producer is decreasing stock levels, this is their own commercial response to the current circumstances. However they could also elect to increase stockpiles, as stated by Wambo and Camberwell. In any event, producers such as BHP Billiton now have defined allocations and the ability to plan with certainty, so one approach is to match production to the allocation instead of carrying high stocks. Current ROM and product stocks represent about three weeks of production, an ample amount to support cargo assembly in the current environment. This does not mean that the CDS has reduced production or that more coal could in fact be exported, as the same physical capacity constraint continue to exist in the export coal supply chain.

PWCS strongly believes that, with the broader knowledge available to PWCS, BHP Billiton’s concerns on the following two issues are unfounded:

- Zero queue: PWCS respectfully submits that it and the Administrator have access to more information concerning vessel queues than BHP Billiton. The
Administrator’s estimate of queuing to the end of June is shown in Graph 8 below.

Graph 8

Tonnes in Queue

Source: Administrator

- **Other producers’ forecasts overstated:** PWCS has distributed extensive information on producer forecasts provided to Barlow Jonker and maintains it is evident that producers can produce to the level of their loading allocations.

As previously explained in this submission, PWCS does not believe that the Barlow Jonker producer forecasts have been overstated, based on the actual data provided by the Administrator. In any event, even if individual producers are unable for one reason or another to produce coal to the levels forecast by them in their Barlow Jonker forecast, as explained in previous submissions by PWCS, the Protocol governing the CDS requires the Administrator to release additional Loading Allocations to producers in the event that the system is forecast to have spare capacity. In fact due to record throughput of coal during the months of April and May 2004, on 8 June 2004 the Administrator advised all producers of the release of an additional 1 million tonnes of loading allocation. This is further evidence that the CDS is working effectively to accommodate any material fluctuations between the capacity of the coal chain and the demand for coal handling and loading services. PWCS accepts that coal supply chain logistics are complex, but PWCS is happy to meet with Commission staff and the Administrator to more fully explain from an operational perspective why PWCS believes that BHP Billiton's assessment of the operation of the CDS is not factually correct, based on a complete picture of all producer data.

2.26 **Graph 9** below shows the actual vessel arrival pattern at Newcastle. The ship arrival rates since the commencement of the CDS are at levels not seen since May-June last year when prices were at historical lows. Since then, mines including Mt Arthur, Newpac and Ashton have been commissioned and prices are at record highs. It appears inconceivable to PWCS that this outcome is a result of any other factor than the CDS loading allocations.
2.27 PWCS submits that all markets involve a balance between supply and demand and that producer estimates are the most likely to be accurate in tight markets. In weak markets, producer estimates naturally overestimate outcomes as not all coal can be sold. By contrast, in tight markets, when all coal can be sold, producer estimates closely track demand. The fact that in the past, in weaker coal markets, producers estimates have on occasion overestimated eventual throughput does not mean that producers forecasts will be overstated at times of unprecedented high demand as is now the case. PWCS rejects the suggestion that producer forecasts for 2004 are necessarily overstated.

2.28 Some producers have also suggested that both:

- the willingness of producers to engage in one-way swaps; and
- the fact that they were able to put through the port 100% of their budgeted coal production during Q1,

raises a question as to the accuracy of the Barlow Jonker figures. However, PWCS disagrees with each of those contentions.

2.29 First, a producer’s desire to enter into a one-way swap may indicate nothing more than its desire to re-schedule its exports in response to changed customer requirements or that it has been offered something more valuable than the use of that loading allocation at that particular time. Second, if a producer was able to export 100% of its budgeted exports during Q1 (which PWCS certainly cannot guarantee to any producer at this time), that ability clearly came at the expense of other producers who were not able to forecast their export tonnes.

2.30 PWCS has always said that, although producers may in certain circumstances be able to move all of their budgeted coal through the port during a particular period (generally by being over represented in the queue), the simple fact is that not all producers will be able to
do so. It is this “tragedy of the commons” which, in the absence of the CDS, would result in producers arranging more and more ship arrivals, even in the face of clear evidence that the coal chain cannot meet all of those orders.

2.31 In summary, PWCS believes that the producer forecast figures provided to Barlow Jonker provide the most **accurate, fair and equitable** basis for the pro-rata allocation of loading entitlements in accordance with the CDS Protocols. Those producer estimates were provided before there was any indication that the CDS might be implemented. To invite new or revised estimates from producers at this stage would involve significant risks of overstating and gaming.

**The CDS is administered by an independent Administrator**

2.32 As mentioned above, the CDS is based on, and is operating under, a set of clearly defined and transparent rules. It is also administered by a reputable, independent and accountable external organisation.

2.33 PWCS believes that this “independence” and transparency further reinforces the integrity of the CDS and demonstrates PWCS’s commitment to implementing a system which is both effective in reducing the vessel queue and is fair to different industry stakeholders. In this regard, PWCS notes the comments contained in the submission to the Commission by a small producer, Gloucester Coal (dated 6 May 2004) that:

> “GCL is pleased with the overall management of the scheme, and there has been a high level of professionalism and impartiality by Accenture. GCL’s initial concerns about management of the scheme by Accenture were unfounded…

> GCL continue to strongly support the scheme and the principles behind the CDS”.

**PWCS remains committed to implementing a longer term solution**

2.34 For completeness, PWCS again notes that it is continuing to work with Accenture and other key stakeholders in the supply chain to design and implement a longer term solution (such as “take or pay” demand nominations) to address the imbalance between demand and physical coal chain capacity.

2.35 In the meantime, PWCS believes that the CDS is the most effective, fair and equitable way of addressing that imbalance. PWCS also believes that:

- the demonstrated success of the CDS in reducing the vessel queue and vessel waiting times, with the resulting reduction in demurrage; and

- the increased exports which have resulted from PWCS’s initiatives (in the context of the operation of the CDS),

are strong evidence of the public benefits which arise as a result of the CDS - in particular, the more efficient allocation of resources in anticipation of a long-term solution being progressed and enhancing the international competitiveness of the Australian coal industry.
Section Three - The continued need for the CDS

High global demand for coal

3.1 All industry forecasts and expectations are that the current levels of global demand for coal will continue. This has not been contested in any of the submissions provided to the Commission or by any of the parties who attended the pre-determination conference in Newcastle. It is further supported by the article “Booming China devouring raw materials” which appeared on the front page of The Washington Post on 21 May 2004 (see Attachment A).

3.2 PWCS therefore believes that the level of global demand will continue to exceed the capacity of the Hunter Valley coal chain for the foreseeable future. PWCS also refers the Commission to the relevant websites of all of the large coal mining operations in Australia such as BHP Billiton and Rio Tinto, which contain presentations expressly dealing with this continued demand from China and other countries.

The queue will not be reduced if left to “market forces”

3.3 A number of submissions by interested parties have suggested that this capacity and demand imbalance should be left to be resolved by market forces. In this regard, the Commission stated in its draft determination that:

“it is inevitable that market forces will eventually dissipate the queue...if authorisation is denied. The issue is whether this will occur in 2004”.

3.4 However, PWCS believes that in order for market forces to reduce the vessel queue in the foreseeable future, there needs to be some evidence that either demand (customers) or supply (producers) will respond to queuing signals. PWCS submits that there is no evidence that any participant in the coal chain is responding to those congestion signals. To the contrary, a number of parties who oppose the CDS are seeking the unfettered right to send more ships to Newcastle on the basis that one way or another their coal will be exported, rather than responding to the queuing signal.

3.5 The evidence is that vessel queuing at Newcastle has been both persistent and unusual. While most queues at other ports dissipate in a matter of months, the queue at Newcastle has persisted since late 2001. Accordingly, the queue is demonstrably not simply a response to tight market conditions. To the contrary, it formed at times of low global coal prices. Graph 10 below sets out the amount of coal exported through the Port of Newcastle in the period from 31 January 2001 to 30 April 2004, as well as the international spot price for Newcastle coal for the same period.

Graph 10
3.6 A “supply side” solution to capacity shortfalls depends on the correct market signals being available, sent and received by the asset owners concerned. In the case of the Hunter Valley coal chain, only PWCS has invested major capital in the last few years. Track capital has been delayed for a range of reasons and the first of many projects acknowledged as necessary will not be delivered until 2006. New rolling stock is not expected in operation before 2005. Part of the longer term solution, through take or pay contracts, is to deal with these capacity signals to ensure orderly provision of future capital based on confirmed demand to meet coal industry needs.

3.7 **Graph 11** below also demonstrates that the level of queuing at Newcastle also exceeds all international standards for bulk loading ports.

![Graph 11](source: Rio Tinto Shipping)

3.8 PWCS understands that it has been suggested by certain parties that the following market forces will operate to reduce the current vessel queue:

- **Coal market forces** - The Commission has suggested that the most likely “market forces solution” is China re-entering the export market. The Commission has also suggested that it is possible that general demand for coal might fall. While each of these factors is possible, the current high coal prices and China’s decision in early May to remove subsidies for export coal (which it is accepted occurred after the Commission’s draft determination was released) both strongly suggest that coal market forces are unlikely to reduce demand for coal from Newcastle in 2004. Irrespective of this, no producer would be disadvantaged under the CDS in the event of a fall in market demand. By definition, this would result in at least some producers seeking to ship less than their allocation, freeing up capacity which would be made available on the secondary market (if the Commission approves one-way exchanges of loading allocations) or redistributed via the CDS Administrator;
• **Shipowner concerns and freight rates** - Freight rates did indeed rise in late 2003 largely in response to conditions in China (and, as has been evidenced in a number of submissions, have started falling again to reduced, but still high levels). However, PWCS believes that there is no evidence that high freight rates have had any impact on vessel arrival rates and queuing. In particular, the increase in freight rates has clearly not acted to reduce the queue;

• **Buyer concerns and Newcastle coal prices** - It has been suggested that coal buyers’ concerns about queuing and discount coal prices at Newcastle are likely to result in a reduction in demand and, therefore, a reduction in the vessel queue. However, although PWCS believes that the current situation is causing significant long term harm to the reputation of the Hunter Valley coal industry with international buyers, there is no evidence that buyers’ concerns are likely to result in a reduction in the current vessel queue;

• **Expansion by infrastructure providers** - PWCS agrees that the most effective long term solution to reduce vessel queues is for the coal chain capacity to be expanded and increased. Unfortunately, to date PWCS is the only participant in the Hunter Valley coal chain to make major investments towards this goal. Track capital has been delayed by the handover of the track from the NSW Government to ARTC and the current estimated completion date for the Hanbury Grade Separation, the first major capacity upgrade project, is now Q1 2006. Further delays are also possible depending on the completion of the handover from RIC to ARTC. It is also far from clear that market forces are driving track investment behaviour. More trains are on the way, but they are not due until 2005; and

• **Coal supplier behaviour** - It appears to PWCS that the most likely and effective “market force” that would act to limit queuing would be independent decisions by coal producers to avoid demurrage by planning throughput to match capacity. However, not only is there no evidence that this has occurred in the absence of a CDS, a number of submissions to the Commission have suggested that producers will ignore the demurrage signal in an effort to maximise their own throughput at the expense of others.

**Conclusion on the continued need for the CDS**

3.9 PWCS submits that the available evidence simply does not support the view that market forces will operate to reduce the queue in any meaningful timeframe. Having regard to the continuing vessel queues, the substantial amounts of demurrage being incurred by producers and the continuing harm to the reputation of PWCS and the Hunter Valley coal industry, PWCS believes that there is a strong need for the Commission to grant an authorisation which enables it to continue with the CDS.

3.10 PWCS believes that:

- until PWCS is able to implement a longer term solution which effectively matches demand with available capacity (and provides an efficient funding mechanism for necessary coal chain upgrades); and

- government funding of necessary upgrading to the government owned rail track infrastructure in the Hunter Valley is guaranteed and the upgrades actually occur, the CDS remains the fairest and most effective solution to that imbalance.
4 Section Four - Public benefits

Introduction

4.1 As set out above, PWCS believes that the CDS, and the demonstrable reduction in the vessel queue, as well as the increase in exports, is already delivering substantial public benefits. The immediate success of the CDS in reducing the vessel queue has resulted (and will continue to result) in a reduction in the amount of wasteful demurrage costs incurred by producers. Demurrage costs are a part of, or at least associated with, coal transport costs and a reduction in transport costs has in the past been recognised by the Commission as a public benefit. At the same time, the CDS has not resulted in any reduction in the amount of throughput at the port and has in fact resulted in, or at the very least contributed to, an increase in coal exports.

4.2 In addition, the CDS has delivered (and is continuing to deliver) both:

- reduced waiting times for ships; and
- increased certainty and transparency in relation to loading and delivery times,

factors which enhance the export competitiveness of the Port of Newcastle and Australia in general as a source of coal.

4.3 PWCS believes that the CDS is an important step in improving the reputation of both PWCS and the Hunter Valley coal industry as a reliable and secure source of supply.

4.4 Each of those public benefits is addressed below.

Substantial reduction in wasteful demurrage payments

4.5 A number of submissions provided to the Commission have sought to raise questions in relation to the accuracy of PWCS’s estimates of demurrage payments and PWCS’s calculations as to the savings that would arise as a result of the operation of the CDS. For example, Donaldson states that “PWCS’ claimed savings in demurrage are uncertain and lacking in substantiation and are not shared across the industry”. The Donaldson submission may have been prepared prior to the provision of actual demurrage costs by Coal & Allied and Xstrata in their recent submissions to the Commission and may not have considered all of the data on demurrage provided to the Commission by PWCS. In any event, this submission will again set out material on demurrage (to the extent that producers have not claimed confidentiality) and how it has been calculated for the public record, so as to confirm the conservative nature of the demurrage calculations and their reliability, so that there is no doubt that the Commission is fully entitled to accept and be satisfied on those calculations.

4.6 PWCS maintains that the evidence supports its contention that the combination of high demand, restricted supply and no mechanism to match the two would lead to persistent queuing in 2004 in the absence of the CDS. High demand has been clearly referred to in almost all submissions. No established producer has indicated to PWCS or in its submissions that it proposes to reduce production.

4.7 In the real world, the queuing at Newcastle is obvious to all observers. Not only that, it is an impost that is avoidable. All other bulk loading ports have lower queuing levels. The level of queuing at Newcastle in 2004 has been extraordinary and has attracted international comment. Further, shipowners do not place their ships at Newcastle unpaid: vessels chartered to load at Newcastle incur a demurrage charge for waiting time.
4.8 The actual queuing experienced in the first quarter before the CDS came into effect is actually higher than PWCS estimated. PWCS had estimated a simple linear increase in the queue from 30 vessels at the start of the year to an assumed 42 ships at the end of the first quarter. In fact, queuing peaked at 56 vessels and averaged some 45 ships in the quarter, above the peak that PWCS has estimated.

4.9 PWCS submits that it is not necessary to know the precise quantum of demurrage costs and the distribution among all participants to show that reduction in queuing is a clear benefit. The actual cost depends on the specific commercial terms for both coal supply and ship chartering arrangements that may have been recently entered into or may in fact relate to contracts entered into some time ago. The simple fact is that shipowners require financial compensation for time spent waiting to load and hence a substantial reduction in days of queuing - a fact which is now clearly visible as a tangible fact - will necessarily result in substantial public benefits.

4.10 **Graphs 12** shows the actual and forecast (with and without CDS) average days spent waiting in the queue. **Graph 13** shows cumulative days in the queue, both actual and forecast, with and without the CDS. Both graphs point to a steady reduction in the days of vessel queuing.
4.11 PWCS’ estimates of the financial benefits of queuing reduction are deliberately conservative, based on JSM terms. Some submissions have made much of recent reductions in spot freight rates, but even current/spot rates put forward in those submissions are far higher than the assumptions used by PWCS. Similarly, the actual demurrage costs of the large producers, as raised at the pre-determination conference in Newcastle, are in line with those of some of the small producers who claim to enjoy “favourable” demurrage terms. Hence there is not the discrepancy as between large and small producers that has been claimed by some.

4.12 In a very small minority of cases, coal sellers are able to pass-on demurrage cost (selling under Customary Quick Despatch or CQD terms), but it is axiomatic under shipping contracts that some party in the coal chain always bears the responsibility for compensating the shipowner for delay costs. Unfortunately, PWCS is not aware of any cases where shipowners have chosen to forgo demurrage.

4.13 Table 1 and Graph 14 provide an estimate of the accumulated demurrage incurred YTD, and the forecast demurrage savings under the CDS.

### Table 1

**Forecast Vessel Queue and Demurrage Savings**

<table>
<thead>
<tr>
<th>Quarter</th>
<th>Cum./(Avg) Queue Days – with CDS</th>
<th>Cum./(Avg) Queue Days – w/out CDS</th>
<th>Demurrage – with CDS USDm</th>
<th>Demurrage – w/out CDS USDm</th>
<th>Demurrage Savings USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q1 (Actual)</td>
<td>3,866 (42)</td>
<td>8,678 (53)</td>
<td>37.4</td>
<td>48.8</td>
<td>29.8</td>
</tr>
<tr>
<td>Q2</td>
<td>6,194 (26)</td>
<td>14,984 (69)</td>
<td>19.0</td>
<td>66.6</td>
<td>46.6</td>
</tr>
<tr>
<td>Q3</td>
<td>7,114 (10)</td>
<td>22,739 (84)</td>
<td>2.0</td>
<td>84.0</td>
<td>82.0</td>
</tr>
<tr>
<td>Q4</td>
<td>8,034 (10)</td>
<td>22,739 (62)</td>
<td>60.3</td>
<td>236.8</td>
<td>176.4</td>
</tr>
<tr>
<td>Total/Avg</td>
<td><strong>8,034 (22)</strong></td>
<td><strong>22,739 (62)</strong></td>
<td><strong>60.3</strong></td>
<td><strong>236.8</strong></td>
<td><strong>176.4</strong></td>
</tr>
</tbody>
</table>

**Demurrage Calculation:**

Vessels in Queue x (Demurrage Days / Average Queue Days) x Demurrage Rate, where:

- *Demurrage Days = Average Queue Days – Days Demurrage Free, and*
- *Average Queue Days = Vessels in Queue / Vessels Loaded per Day*
4.14 When compared against actual demurrage incurred by a limited sample of producers in Q1, PWCS estimates seem realistic. Table 2 shows an extrapolation of the actual demurrage incurred on a sample of tonnes across total tonnes shipped in Q1.

Table 2

<table>
<thead>
<tr>
<th>Actual Demurrage Incurred</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sample</td>
</tr>
<tr>
<td>Sample Throughput (mt)</td>
</tr>
<tr>
<td>Sample Total Demurrage (USDm)</td>
</tr>
<tr>
<td>Average Demurrage (USD/t)</td>
</tr>
</tbody>
</table>

Projection

| Total Throughput (mt)     | 19.3   |
| Projected Total Demurrage (USDm) estimate only | 33.43 |

Note: Demurrage costs are a function of average queue days and consequently there is a lag between the Queue length and demurrage costs incurred (i.e. demurrage incurred in April is in part due to the size of the queue in March)

Notes

The assumptions underlying these demurrage calculations are:

Port Throughput: 80mtpa  
Vessel Size: 80,000t  
Vessels loaded per day: 2.74 (throughput/vessel size)/days  
Queue days before demurrage is charged: 3  
Demurrage Rate (estimate): US$12,000/day

Under these assumptions, an average queue (# Vessels / Daily Loading Rate) of 8 vessels can be sustained before demurrage charges are incurred (as all vessels will be loaded within 3 days). For each additional vessel in the annual average queue, the demurrage cost to the industry increases by approximately USD 4.38m.
### Table 3
Relationship between vessel queue and estimated demurrage

<table>
<thead>
<tr>
<th>Vessel Queue</th>
<th>Daily Demurrage USD</th>
<th>Annual Demurrage USD</th>
<th>Annual Demurrage AUD</th>
</tr>
</thead>
<tbody>
<tr>
<td>10</td>
<td>21,360</td>
<td>7.80m</td>
<td>11.14m</td>
</tr>
<tr>
<td>20</td>
<td>141,360</td>
<td>51.60m</td>
<td>73.71m</td>
</tr>
<tr>
<td>30</td>
<td>261,360</td>
<td>95.40m</td>
<td>136.30m</td>
</tr>
<tr>
<td>40</td>
<td>381,360</td>
<td>139.20m</td>
<td>198.85m</td>
</tr>
<tr>
<td>50</td>
<td>501,360</td>
<td>182.30m</td>
<td>261.40m</td>
</tr>
<tr>
<td>60</td>
<td>621,360</td>
<td>226.80m</td>
<td>323.99m</td>
</tr>
<tr>
<td>70</td>
<td>741,360</td>
<td>270.60m</td>
<td>386.57m</td>
</tr>
<tr>
<td>80</td>
<td>861,360</td>
<td>314.40m</td>
<td>449.14m</td>
</tr>
</tbody>
</table>

Exchange Rate: 0.70 USD = 1 AUD

Source: Administrator

As stated in previous submissions, PWCS has forecast that, without the CDS, the vessel queue could reach 80 vessels or more.

4.15 PWCS maintains that its estimates are conservative as they were based on JSM terms for demurrage, rather than the much higher freight rates seen recently. Secondly, they exclude the substantial cost to end user customers for the difference between contract and actual shipping rates for the times vessels are waiting. Actual queues have been higher than estimated, with the queue rising to over 55 vessels in March, a level that PWCS did not expect until mid-year.

4.16 In addition, while visiting Japan in March, PWCS enquired about the additional cost of demurrage paid by end users as a result of high freight rates. The estimate provided by the leading Japanese shipping companies at that time indicated a total cost at some US$150M annualised rate. None of these benefits have been included in PWCS estimates of demurrage savings, but their avoidance will assist in the competitive positioning of Newcastle as a supply source and in a competitive coal market will ultimately enhance returns to Australian producers. Finally, in response to the submission from Donaldson that Japanese coal buyers under term contracts scaled back purchases because they previously exercised provisions known as “10 per cent plus clauses”, PWCS notes that this must be reflective of Donaldson’s disclosed position as an exporter of coal on a 100% spot basis (which implies that Donaldson has no term contracts and hence is not in possession of the knowledge to make such a statement). PWCS enquiries of a number of coal producers indicate that, with the significant shift in contract arrangements since the collapse of the ‘reference’ price system for Japanese purchases of coal in the last two years, most ‘optionality’ from shipping tolerance or buyers’ option clauses has been removed or limited (this is an expected and rational response to changing contract structures and a more liquid spot market).

4.17 Accordingly, PWCS maintains that, in the absence of the CDS producers in the Hunter Valley would continue to incur demurrage costs in excess of A$200 million in 2004.

Cost of demurrage

4.18 A number of submissions have argued that demurrage is merely a cost of doing business and can be passed on to end users.
4.19 PWCS submits that while demurrage itself is not unusual, the level of queuing and consequently of demurrage at Newcastle in the last 18 months is most unusual. The fact that this cost is avoidable is demonstrated by the evidence that other coal ports have avoided it. Avoiding this cost through reduced waiting time and decreased port congestion is an efficiency gain enjoyed by all port users.

4.20 Demurrage is not generally a cost that can be passed on to end users. This is supported by two arguments:

- most coal sold through Newcastle to North Asian consumers is sold at contract prices that do not reflect the cost of short term queuing variations. There is no reason why consumers would deviate from the usual practice that it is the coal supplier that pays demurrage, not the end user. Secondly, most of the ports with which Newcastle is in direct competition, notably the Queensland ports, have experienced minimal queuing; and

- the practical mechanism that end users would use to pay demurrage would be to buy coal on Customary Quick Despatch terms (CQD). PWCS enquiries have revealed that minimal volumes of coal are sold on CQD terms through Newcastle and, in any case, CQD simply shifts responsibility for demurrage to another party in the coal chain, rather than removing the cost required to compensate a shipowner for delays.

4.21 All ships with coal from all producers have to pass through the queue to be loaded and hence queuing is a delay that affects all ships to a broadly similar extent. While the financial costs to an individual shipper may vary depending on their contractual positions, in much the same way that coal sales prices will vary, there is no reason to expect that the fact that a producer is larger or smaller will necessarily affect demurrage costs in any systematic way. Some small producers such as Donaldson claim to sell 100% spot, others sell 100% contract, but all admit to paying demurrage.

4.22 It follows that a system that reduces queuing for all players will result in benefits to all - whether large or small producers.

**Improvement to the international reputation of PWCS and the Hunter Valley coal industry**

4.23 PWCS believes that, notwithstanding the Commission’s preliminary views as set out in its draft determination, the current level of vessel queuing at Newcastle is having a significant long term detrimental impact on the reputation of the Port of Newcastle and the Hunter Valley Coal industry. The newspaper articles at Attachment D evidences some of the adverse publicity generated from the vessel queue and demonstrate the potential detriments that could arise if the problem is not addressed. The CDS is an important step in addressing this issue.

4.24 PWCS attended the recent Japan Australia High Level Energy Group meeting, an open exchange of views at a senior government to government level. Stability of supply and the state of NSW infrastructure were issues raised by the Japanese delegation as being important.

4.25 PWCS submits that this is prima facie evidence that a failure to address queuing at Newcastle will impair producers’ ability to meet buyer needs and hence compete with other coal sources as:

- other ports do not suffer from demurrage to the extent incurred at Newcastle; and
• if Newcastle continues to operate without a mechanism to manage demand to meet available capacity, persistent queuing is likely to recur and this is inconsistent with stable, predictable supply.

4.26 At the pre-determination conference, it is noted that the representative of the Department of Industry, Tourism & Resources, Mr John Karas, noted that while no opinion was expressed as to the appropriate mechanism, something needed to be done to address the vessel queue. Similarly, it is understood that evidence has been submitted by individual producers on a confidential basis of exports being lost from the Port of Newcastle because of the vessel queue. It is hoped that this further evidence will be persuasive to the Commission. Equally, the reduction in vessel queues and the certainty of loading and delivery times are factors increasing the international competitiveness of Australia’s coal exports and are therefore a public benefit that the Commission is required to take into account.

**Impact of the vessel queue on freight rates**

4.27 There is some evidence that the extensive vessel queues at Newcastle may be contributing to higher world freight rates. To the extent that fixing the queue at Newcastle releases vessels, this is likely to assist in relieving rates. As Newcastle is the port most distant from North Asian discharge ports (versus China, Indonesia and Queensland), this factor will also enhance coal chain outcomes and add to consumer surplus.

4.28 This is an additional benefit which is likely to flow on to Newcastle coal prices and ultimately, in part, to the Australian community.

**Limited impact on competition**

4.29 The Commission has raised concerns that the CDS may “freeze” the market share of Hunter Valley producers and that this could distort competition.

4.30 PWCS contends that at a time of unprecedented high coal prices and strong demand, combined with unfettered queuing that would pertain in the absence of a CDS, all producers would share a similar incentive to accept ships. Market shares would be based on the relative ability of each producer to flood the port with ships waiting to load, rather than any rational economic system. There is no evidence that the resulting market share outcomes would be significantly different than apply under the CDS.

4.31 PWCS has already submitted its estimates of the tonnage that would be exported by producer in the absence of the CDS and demonstrated that these tonnages are not materially different than those that would apply under the CDS.

4.32 Finally, a temporary intervention such as the CDS will have a minimal impact on long term competitive decisions relating to supply and competition.

**Community Benefits**

4.33 As mentioned above, PWCS believes that a reduction in demurrage will have the effect of directly reducing aggregate operating costs for Hunter Valley coal producers in 2004 by reducing payments to overseas shipping companies for demurrage. Achieving this gain, whilst at the same time maintaining revenues earned by coal producers at levels that existed prior to the introduction of the CDS, will directly improve aggregate profits for Hunter Valley coal producers. This in turn will directly impact on the amount of dividends paid to shareholders of producers and will increase the amount of Australian income tax paid by producers and shareholders, significantly benefiting the Australian community. For example,
Coal and Allied, in its 2003 "Social and Environmental Report", states that 74% of the tax and royalty paid by it are levied at a Federal level in Australia.

4.34 Reduced operating costs for each tonne of coal exported from the Hunter Valley will also directly improve the international competitiveness of Hunter Valley coal producers. This over time will create further opportunities for sales of Hunter Valley coal.

4.35 There is also the potential for the CDS to provide many indirect gains for the Australian community. Reduced operating costs will enhance prospects for further investment and development in Hunter Valley coal production. Also, the benefits that the CDS provides in improving planning and certainty of coal exports and in improving the reputation of the Hunter Valley coal industry will support the future development of the coal industry in NSW.

4.36 The coal industry in the Hunter Valley is a major employer and contributor to both the Australian economy and local communities, in the following manner:

- **Employment** - the 2003 NSW Government publication "Coal Industry Profile" estimates that in Singleton North West and Newcastle districts there are 7,384 people employed directly in the coal industry. The NSW Department of Mineral Resources quotes an employment multiplier of three, so the coal industry in these districts is estimated to have an overall employment impact of over 20,000 jobs, a major part of the regional economy.

- **Local services** - the mining industry is a major purchaser of goods and services, especially regionally. For example, Coal and Allied in its 2003 "Social and Environmental Report" indicates that 89% of payments to its suppliers are within N.S.W. and 99% within Australia.

- **Economy** – the value of coal exports from N.S.W. were approximately $5 billion in 2001-02, most of which was generated from the Hunter Valley (source: NSW Department of Mineral Resources).

- **Taxation** – as stated above, any efficiency gain will translate directly to increased profits and hence increased income tax paid to the Australian community.

- **Shareholders** - wealth from economic efficiency will flow to the Australian community, both directly where shareholders are Australian, or indirectly where efficiency gains will encourage further investment or facilitate purchasing of local services.

4.37 Coal companies exporting from Newcastle with substantial Australian shareholding include:

- Coal and Allied (listed on ASX in its own right and held 75% by Rio Tinto, which is a dual listed company listed in Australia and UK. Rio Tinto Limited, the Australian company, is one of the largest companies in Australia)

- Hunter Valley Energy Coal (owned 100% by BHP Billiton, also a dual listed entity; BHP Billiton Limited, the Australian company, has 94% of its shareholders based in Australia)

- Excel, recently listed in Australia.

- Gloucester Coal, an Australian listed company
• Centennial, an Australian listed company.

4.38 Table 4 below provides further information on the contributions that Coal and Allied makes to the Australian economy.

<table>
<thead>
<tr>
<th></th>
<th>Hunter Valley</th>
<th>Rest of NSW</th>
<th>National</th>
<th>International</th>
<th>Total</th>
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</thead>
<tbody>
<tr>
<td>Payments to suppliers</td>
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<td>151</td>
<td>52</td>
<td>3</td>
<td>495</td>
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<td></td>
<td>58%</td>
<td>31%</td>
<td>11%</td>
<td>1%</td>
<td></td>
</tr>
<tr>
<td>Wages, salaries and benefits</td>
<td>213</td>
<td>213</td>
<td>213</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>100%</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Taxes and Royalties</td>
<td>4</td>
<td>41</td>
<td>74</td>
<td>119</td>
<td></td>
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<tr>
<td></td>
<td>3%</td>
<td>34%</td>
<td>62%</td>
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</tbody>
</table>

Source: Coal and Allied: Social and Environmental Report 2003

Further information about the economic impact of the Hunter Valley coal industry may be obtained from the N.S.W. Department of Mineral Resources website at http://www.minerals.nsw.gov.au/mine/focus-00-01.htm.

**Conclusion on Public Benefit**

4.39 In this submission and in the various additional material provided to the Commission by PWCS, specific data on demurrage costs and actual and projected savings have been provided. Accenture has confirmed those figures, based on discussions with actual producers.

4.40 In relation to the benefits claimed on vessel turnaround and the impact on the reputation of PWCS, the Port of Newcastle and the international competitiveness of Australian coal exports, PWCS notes as follows:

• material has been provided on the reduced length of vessel queues and the associated increased turnaround of vessels;

• material has been provided on the view of international coal buyers on buying coal from Newcastle in the face of long vessel queues, and high demurrage (some of which demurrage costs are borne by customers, as acknowledged by the parties opposing the authorisation);

• data has been provided on the work of PWCS to improve coal chain capacity (part of which would have occurred irrespective of the CDS, but also part of which has occurred as part and parcel of the CDS); and

• data has been provided on the increased level of exports from the Port of Newcastle during the operation of the CDS - part of this increased exports would have occurred anyway as a result of coal chain improvements and part of which has occurred as part of the CDS process.

4.41 In terms of whether the benefits of the CDS are “public”, data has been provided to the Commission that participants in the CDS include Australian and overseas companies, with Australian shareholders and Australian employees, which operate out of the Hunter Valley.
Apart from the benefits of investment and employment by those companies to the local and
the Australian communities involved, evidence has been presented as to how large
international companies make global investment decisions as to where they will invest and
build and/or reduce investment based on the efficiencies associated with relevant mines and
the coal chain. However, if the Commission requires more information on this, it can be
provided.

4.42 In any event, it is submitted that there are clear benefits associated with the CDS in terms of
PWCS’s reputation, the reputation of the Port of Newcastle and the enhancement of
Australia’s export competitiveness in terms of coal. However, if the Commission requires
further information on this, PWCS will provide it.

4.43 In these circumstances, PWCS believes that clear evidence has been provided to demonstrate
the public benefits arising from the CDS.
Section Five - Impact of the CDS on market participants

Impact of the CDS on smaller producers

5.1 Some of the submissions to the Commission have made statements about other coal chain users, suggesting various proportions of spot or term business, surmising impacts on large or small operations or raising concerns about differential information or treatment.

5.2 In response, PWCS can only point to the large number of contradictions and complexities that result from these assertions without the provision of actual factual foundation and in particular that PWCS believes that these assertions are unfounded based on factual material provided to PWCS, which material is confidential as between competitors. PWCS notes, in particular, that some of the parties making those assertions also insist on confidentiality of their data which prevents these assertions being publicly responded to by PWCS based on actual data.

5.3 The reality is that the shortage of available capacity imposes direct and opportunity costs on all producers. In the situation where PWCS was aware that a pro-rata distribution of limited capacity pursuant to the common user principle would cause issues, PWCS has sought to design the CDS with a number of concessions to minimise the impact on smaller players:

- first, only larger players are required to reduce tonnage preferentially in Q2 and hence bear the brunt of clearing the queue - this fact is not acknowledged by the smaller producers who have opposed the CDS; and
- the flexibility provision of 90,000 tonnes significantly reduces the tonnage reduction required by the smaller players. As an example, for a 1Mt producer, the flexibility provision almost entirely offsets any reduction in forecast throughput. The average reduction required of the smaller players is, as a consequence, much smaller than that by the larger players.

5.4 In terms of claims of a negative impact on employment, efficiency or marginal cost operation of the smaller producers, PWCS believes that these claims have been overstated. Although producers may reduce the amount of coal exported in a given time period as a result of the CDS, it is never clear that this coal would have been exported in any event because of capacity limitations and the vessel queue. In any event, PWCS believes that production will most likely remain unchanged and there will be minimal effect on employment.

5.5 The evidence from Wambo and Camberwell at the conference was that they will build stockpiles of coal to be exported and will forward sell that coal so that they bear the stockpiling fee, but enjoy the higher prices created by the current high market demand (see for example Attachment B which contains the Excel Coal Limited Quarterly Report for the three months ended 31 March 2004). Excel Coal owns the majority stake in Wambo. The Report confirms the higher prices for NSW export thermal coal in excess of US$55 per tonne and that "production and sales at Wambo are running above planned levels for the three months year to date and are on track to achieve FY2004 targets".

5.6 Claims of revenue loss as a result of the CDS cannot in aggregate be sustained as the coal chain is operating at higher throughput levels with higher prices than were achieved before the CDS. Overall, Newcastle coal revenue is incontrovertibly increased. To suggest that the opportunity cost of increased revenue offsets any demurrage saving cannot, when viewing the totality of coal exports, be true.
5.7 However, again, the key answer in relation to these smaller producers is that there is no substantiation of their claim that they would have been able to export all of their coal production in any event without the CDS and the fact that the Port of Newcastle is operating at record levels under the CDS. In addition, the Commission considers the public detriment, not the detriment to individual companies, as part of the weighing process.

**Impact of the CDS on traders**

5.8 Various producer submissions have focused on the effect of the CDS on traders, with references to the “elimination” or “exit” of coal traders. However, Coaltrade notes, in more moderate terms, that “world market circumstances combined with the allocation system have curtailed the spot market… the allocation system is not the sole factor for the reduction in tonnes”.

5.9 PWCS also notes some of the recent submissions to the Commission which have pointed out the actual international scale of some of the traders in the context of the claims made about the “elimination of coal traders”. PWCS does not consider that such elimination is very likely at all.

5.10 In conclusion, overall, PWCS has not seen tangible evidence that the viability of traders or the volume of traded coal is threatened or that producers will not sell to traders as a matter of principle.

**Alleged impact on new entrants**

5.11 In its draft determination, the Commission raised the concern that the CDS procedure for new entrants may be “an additional and uncertain barrier”.

5.12 PWCS is pleased to report that a new entrant, Newpac, has been granted a loading allocation under the CDS following the procedure laid down. Accordingly, PWCS believes that the CDS has not proved a barrier to this customer.
6 Section Six - Swaps and trading of loading allocations

6.1 PWCS has not sought to become involved in commercial arrangements between parties in relation to swapping/trading of loading allocations as part of the CDS. However, the Protocol as originally provided to the Commission does permit swaps and ‘one-way trades’ (please refer to Schedules 6 and 9 of the Protocol) as this was, and still is, considered appropriate by the Administrator, Accenture. See for example the comments of the Administrator in paragraph 4 of its memorandum to PWCS dated 1 June 2004 (Attachment C).

6.2 While PWCS is not directly affected by the interim condition imposed by the Commission, PWCS and Accenture are of the view that swaps and ‘one way trades’ provide an important additional flexibility to the CDS and to remove this ability may have some unintended consequences. For example:

- PWCS has no evidence of money changing hands for loading allocations or that parties are acting inappropriately with respect to exchanges - the exchange or trading of the “right” does not occur because of the authorisation as claimed by some parties - an authorisation does not “create” a right;

- the opportunity to participate in swaps and ‘one way trades’ provides additional flexibility for producers as well as providing an incentive for producers that may be unable to use their allocation to release it in a timely manner to those who can use it (rather than waiting until the last moment);

- it provides an opportunity for producers, large or small, to deal in an efficient operational manner with production mishaps and to place allocations (whether from those mishaps or from a pro-rata increase in Loading Allocations by the Administrator, as occurred on 8 June 2004) in sufficient quantity to make the swap or "one way trade" commercially practicable – the Commission has been provided with this information so that it should be aware of the legitimate commercial nature of these transactions; and

- it leaves it to the market to determine the distribution of surplus loading allocation. This is a market-based solution and all industry participants have been encouraging PWCS to adopt such solutions as soon as practicable.

6.3 PWCS also notes that if ‘one way trades’ are not allowed, the relevance of the Barlow Jonker producer forecasts is increased, because producers are unable to obtain allocation from others to exceed their initial allocations. The CDS as drafted provides greater flexibility and, in doing so, addresses one of the assertions made by some parties that the Barlow Jonker figures were inflexible and not the most accurate. PWCS emphasises to the Commission that the evidence of producer volumes to date shows that the Barlow Jonker producer forecasts were not "optimistic" and have in fact proved to be conservative.

6.4 Finally, the criticism of one-way trades is mixed among the parties opposing the authorisation. PWCS believes that the criticism of the one way trades is based more on an attempt to oppose the authorisation application overall, rather than on their particular merits in allowing increased flexibility for all producers.
7 Section Seven - Discussion of conditions

Introduction

7.1 First and foremost, the temporal condition already imposed by the Commission on the CDS limits the operation and impact of the CDS. This is important in terms of weighing the public benefit and the consideration of the request by some parties for conditions. PWCS notes that it has concerns that the continuing high level of demand for coal will mean that the queue will re-form in 2005, particularly as the benefit of the first elements of government investment in rail infrastructure is unlikely to occur before Q1 in 2006.

7.2 PWCS has set out its response to each of the conditions proposed to date.

CDS to lapse once queue falls

7.3 PWCS has reviewed the length of queue required to ensure that stockouts are avoided and hence capacity lost. At a queue of 8, the statistical probability of empty berths is minimal (estimated to be lower than one in 10,000). However, PWCS aims to ensure a working queue of a nominal 10 vessels is maintained and will release additional loading allocation to achieve this result in conjunction with the Administrator.

7.4 To introduce a condition that the CDS should lapse if the queue reaches a certain level is not appropriate as the queue length is not an independent variable. In practice, it is not realistic simply to remove the CDS and allow the queue to re-form. It is PWCS’s view that a condition based on queue length is neither practical nor necessary. The arguments presented at the pre-determination conference did not provide any compelling reasons as to the merits of the CDS falling away once the length of the queue recedes to a certain limit.

7.5 Paragraph 1 of the memorandum dated 1 June 2004 from the Administrator to PWCS (Attachment C) provides views from the Administrator in relation to this proposed condition.

Revised producer forecasts

7.6 In relation to the suggestion of producers providing revised forecasts, PWCS believes that there is a real risk of gaming figures now that the CDS has been introduced. It is understood that in any event the majority view put forward at the pre-determination conference that any benefit from this would be marginal at best.

Unused allocation

7.7 BHP Billiton proposed that not less than 10 weeks notice before the end of the quarter must be provided to the Administrator if a producer cannot use its loading allocation for the quarter.

7.8 PWCS believes that the current system of releasing individual capacity through swaps and collective capacity through additional capacity declaration is adequate. Current experience is that most producers are able to advise firm nominations no more than 5 weeks ahead. Often production issues, such as those recently experienced by some producers, are only apparent at short notice. Paragraph 3 of the memorandum dated 1 June 2004 from the Administrator to PWCS (Attachment C) provides views from the Administrator in relation to this issue.

7.9 BHP Billiton is also seeking to terminate the CDS if any allocation is unused at the end of quarter. In practice this is not a realistic condition as there are a variety of reasons, including
production or shipping difficulties or a deliberate strategy by one party, that this situation could occur quite unrelated to the CDS itself.

7.10 PWCS believes that a condition on allocation under-use is unnecessary as, if supply and demand move more into balance, the CDS will naturally allow loading allocations to be progressively made available. PWCS and the Administrator will continually monitor the queue and, where possible, release more allocations to ensure a working queue. Producers who find their shipping needs are met can either swap allocation or return it to the Administrator, who will progressively redistribute it. Any persistent under-use of allocation will be quickly apparent and can be acted on. In other words, the natural operation of the CDS as required will allow the system to respond progressively to increased capacity or reduced demand in a controlled manner, thereby avoiding queuing.

7.11 Paragraph 2 of the memorandum dated 1 June 2004 from the Administrator to PWCS (Attachment C) provides views from the Administrator in relation to this proposed condition.

Transparency of loading allocation usage

7.12 PWCS supports transparency in use of loading allocations, but for confidentiality reasons imposed by producers, is unable to disclose this data without consent. PWCS has requested consent from all producers and will provide these details if all producers consent. The Commission should be aware that some parties putting this condition forward have yet to provide their consent. Paragraph 5 of the memorandum dated 1 June 2004 from the Administrator to PWCS (Attachment C) provides views from the Administrator on this issue.

Sale of loading allocations

7.13 BHP and Wambo have stated that they seek conditions to prevent sale of loading allocations between producers. However, BHP has then stated that unused allocations should be auctioned-off and that proceeds from auction process be used to fund infrastructure upgrades.

7.14 As mentioned above, there are benefits in making loading allocation available for those who need it. However, the auction approach requires careful design to avoid gaming and other adverse effects of a poorly designed market solution. It is PWCS’ view that this is difficult to achieve in the short time remaining to December 2004.

PWCS transparency/governance

7.15 There have been a range of assertions about lack of transparency, the motivation of PWCS Directors and even the employment of PWCS directors.

7.16 PWCS is already supporting transparency within the constraints imposed by its customers as demonstrated by its wide ranging consultation with customers and its efforts to seek permission to reveal the maximum amount of information about the CDS. Accenture provides independence in the formulation and administration of the CDS. However, this increased disclosure requires co-operation. PWCS notes that several players have withheld permission for Barlow Jonker forecasts to be released on the basis that it is commercially sensitive. PWCS appreciates that position. However, it demonstrates the issues faced by PWCS in relation to transparency.

7.17 PWCS also confirms that the Commission correctly identified the employment of 3 out of 10 PWCS directors as full time employees of Coal and Allied or Xstrata. For the record, of the ten PWCS directors, three are full time employees of coal importer organisations, one is a
full time employee of Rio Tinto, two are part time employees of Coal and Allied (one of whom is the Chairman without a casting vote), two are full time employees of Xstrata, one is a full time employee of Anglo and one is a full time employee of Bloomfield.

7.18 PWCS has consistently supported transparency in its implementation of the CDS. Many players have alleged that other producers’ forecasts are overstated or inaccurate. PWCS has requested that all producers release PWCS from confidentiality arrangements to allow the distribution of these figures.

Reporting of medium and long term capacity improvements

7.19 PWCS provides a range of mechanisms to disseminate capacity information, both via the HVCC LT and directly through the regular monthly CDS meetings. PWCS is willing to work with any coal chain player so that it can better meet their specific information requirements.

Redistribution of excess or unused loading allocations

7.20 Proposed conditions are that excess or unused capacity is returned to public domain for redistribution or sale by auction.

7.21 The Protocols already deal with the concept of redistribution of excess capacity. Even in the short time of operation so far, PWCS can demonstrate that these elements of the CDS are working in practice and believes additional steps are unnecessary.

Ceiling on loading allocation transfers each month between producers

7.22 Peabody CoalTrade has proposed a limit on swaps between 2 producers to 90kt per month. However, it is unclear why larger swaps would have any adverse impact and PWCS believes that the objectives of the CDS are best served by maximising flexibility to swap tonnage in response to individual circumstances.

Independent supervisory body

7.23 PWCS believes that this is unnecessary in view of the extensive attention granted to this matter by the Commission itself and the important and independent role of Accenture.
8 Section Eight - Conclusion

PWCS believes that the CDS has significant industry support

8.1 There are some fundamental misconceptions about the level of support for the CDS. PWCS has already noted that the majority of active producers, by number and tonnage, support the CDS. In fact, 8 of 13 active producers have (publicly or privately) indicated support for the authorisation.

8.2 The reality is that a vocal minority have raised issues in relation to the CDS. However, PWCS believes that the majority of producers have considered the overall, aggregate outcomes and consider that acting to remove queuing, while fundamentally unpalatable, is preferable to the same tonnage being achieved with the demurrage costs and other disadvantages associated with a vessel queue.

8.3 In summary, PWCS believes that the results of the past 2 months speak for themselves. The vessel queue has reduced from a peak of 56 vessels to the current level of 10 vessels with a forecast of 5-10 vessels in late June. This, in turn, has resulted in a significant reduction in vessel waiting times and, therefore, in the amount of demurrage being incurred by producers.

8.4 At the same time, PWCS has been able to achieve record levels of throughput at its coal terminals and, together with other participants in the coal chain, has been able to achieve significant operational improvements and efficiencies. In addition, rather than decreasing the amount of coal that is exported through the Port of Newcastle, PWCS’ initiatives (which have been implemented in the context of the CDS) have actually increased the volume of coal exported.

8.5 Accordingly, PWCS believes that the CDS:

- is working;
- is delivering (and will continue to deliver) significant public benefits; and
- has limited (if any) detrimental impact on competition between producers, traders and in the coal industry generally.

8.6 PWCS provides further material in support of this submission in Attachments E and F, which are confidential.

Further assistance

8.7 If the Commission has any questions, or would like any further information, PWCS would be pleased to assist.

Port Waratah Coal Services Limited
10 June 2004