3. Pro Rata Allocation – Process

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Proposed Approach:

- Administrator calculates and advises each Producer of their equivalent pro rata allocation based on their contribution to total nominated demand & declared system capacity.
- Each Producer has two options:
    1. Accept the pro rata allocation and exclude themselves from the auction process, or
    2. Participate in the demand reduction auction

Suggestions/Ideas for Discussion

- Only apply an adjustment process (pro rata and/or auction) where aggregate Demand exceeds Capacity by XMt or more. Where excess demand is less than XMt, all producers will be given allocation equal to their nominations
- What should X be set at? (e.g. 2Mt)
- How is the opening queue treated (i.e. tonnes in the queue as at midnight on 31 Dec 04)?
- What should be the target working queue?
- How can the working queue be achieved? (e.g. by issuing more allocation than the available capacity)
- Do you need to know who will participate in the auction before making a decisions to accept pro rata or go to auction?

Rationale:

- An initial pro-rata allocation with opt out provides an explicit opportunity for Producers that are satisfied with a pro rata allocation to exclude themselves from the auction process

4. Demand Reduction Auction (Allocation Mechanism) – Process

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Proposed Approach: As per Auction Simulation Workshops

- Producers who have not accepted Pro-Rata will bid to reduce their Nomination for given levels of compensation.
- Participating Producers who successfully bid to reduce their Nomination by:
  - greater than their Pro Rata Equivalent will **receive** compensation for each tonne reduced in excess of that amount
  - less than their Pro Rata Equivalent will **pay** compensation on each tonne reduced less than that amount
  - the same amount as their Pro Rata Equivalent will **neither pay nor receive** compensation (effective opt-out)
- The auction will be conducted once, following the calculation of Pro-Rata allocations
- The auction will consist of a blind, one-shot bid
- The auction will be conducted by an independent party

Suggestions/Ideas for Discussion

- ??

Rationale:

- A Demand Reduction Auction provides a market based mechanism to efficiently allocate the required reduction in demand between producers, based on the producer's valuation of the loading allocations.
- The auction is designed to provide the lowest cost solution to reducing the excess demand without the creation of monopoly profits (zero sum game between producers only)

4. Demand Reduction Auction (Price Paid and Collection) – Process

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Proposed Approach:

- Producers bid the volume of tonnes they are willing to reduce at different prices per tonne. Maximum bid price is limited to the Newcastle Thermal Coal Spot Price
- Auction Clearing Price is determined by the marginal bid at which the auction clears. All tonnes bid at a price in excess of the Auction Clearing Price are not sold
- All tonnes bid at the auction clearing price are shared in proportion to the total tonnes sold at that price
- Compensation is based on the auction clearing price and the total compensation payment is calculated as a levy on the total nominated tonnes.
- Settlement of the auction is on a net basis such that producers "sell" or "buy" incremental tonnes above/below their Pro-Rata Equivalent at the Auction Clearing Price

Suggestions/Ideas for Discussion

- ??

Rationale:

- Clearing price ensures symmetry of compensation paid/received
- Net Settlement mechanism easier to understand and reduces financing issues for producers and PWCS

4. Demand Reduction Auction – Controls

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Proposed Controls:

- **Auction Price Cap -** The maximum auction price per tonne will be capped at the spot price.
- **Default Pro-Rata -** In the event the auction does not clear before the price cap is reached (which is unlikely), each Producer who has not reduced to their Pro-Rata Allocation will be required to reduce their nomination until the system is in balance. This means that a Producer cannot acquire more tonnes than their Pro-Rata Equivalent unless another Producer is willing to accept less than their Pro-Rata Equivalent.

Suggestions/Ideas for Discussion

- Rules-based limits on incremental bids
- What is an appropriate spot price index to reference?

Rationale:

- "Spot price" cap ensures auction clears whilst constraining total compensation paid/received.
- Producers should rationally bid tonnes at a price less than the spot price, as this would be more than the per tonne profit margin. A cap minimises risk of irrational behaviour and limits the potential liability for producers "buying" additional tonnes.

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Allocation Management

5. Distribution of Increases / Decreases in Capacity

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Proposed Process:

- If PWCS advises there is an increase in capacity then the additional capacity will be distributed pro-rata. The pro-rata capacity increase will only be distributed to those willing to accept tonnes.
- If there is a decrease in available capacity then all producers' allocation will be reduced pro-rata.
- All producers may trade allocation after the pro-rata adjustment, as per the current CDS.

Suggestions / Ideas for Discussion:

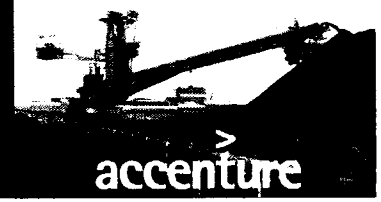
- When is the pro rata applied – based upon initial nomination or following adjustment (auction)?

Rationale:

- Any adjustment resulting in an increase in allocation will only be applied to those who are willing to accept tonnes since Take-or-Pay will apply to new allocation.

[redacted]

6. Incorporation of New Entrants/Mine



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Proposed Approach:

- New entrants allowed for as per CDS (i.e.. Nomination of required tonnes subject to independent audit; audited nomination reduced pro-rata; all other Producers' allocations pro-rata reduced if additional allocation not available for release);
- Technical Audit – Audit of nominations from new entrants by suitably qualified technical expert

Suggestions / Ideas for Discussion:

- Notice period – New Entrants will be required to give at least 6 weeks notice prior the end of the preceding quarter, prior to commencement of their use of the port facilities.

Rationale:

- As per CDS – provides no barrier to entry but it may be inefficient to take capacity from existing Producers pro-rata. This can become efficient if one-way trading is allowed.
- Consistent with common-user provisions of PWCS.

7. System Management – Allocation Tracking

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Proposed Approach:

- Allocation will be tracked on a fixed calendar quarterly basis.
- Allocation will be tracked at producer level.
- All participants will have the same fixed periods.
- Usage of allocation will be tracked using transport provider weights.

Rationale:

- Rolling periods reduce the control that participants have over the distribution of their allocations. They add complexity to the tracking of usage and present potential barriers to the transfer of loading allocation.
- Staggering periods dilutes control over the usage of allocation and complicates transfer of allocation between producers.
- Quarterly tracking is a workable compromise between overall system control and individual producer flexibility.

8. System Management – Allocation Transfer and Exchange

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Proposed Approach:

- As per the current CDS:
  - Allocation can be transferred or exchanged (i.e. one or two-way transfers).
  - Transfer or exchange of allocation can happen at any time.
  - Any transfer or exchange must keep the system 'in balance' (transfer within quarters, exchange across quarters).

Suggestions / Ideas for Discussion:

- The Administrator will facilitate transfers and exchanges, including on an anonymous basis to promote liquidity in allocation trading. (e.g. via an on-line market place to enable anonymous posting of bids and offers for allocation.) This facility will operate in addition to bi-lateral trades between producers as per the CDS.
- Take-or-Pay obligations will transfer with allocation.

Rationale:

- Transfers and exchanges enable the redistribution of allocation to match demand and reduce the likelihood of unused allocation. They ensure an efficient market outcome, even with a pro-rata allocation
- Bi-lateral exchanges are critical to facilitating existing trading between producers, but should also remain commercially confidential
- Take-or-Pay charges provide an incentive for the usage or transfer of allocation and thus should attach to the allocation when it is transferred

9. System Management – Unused allocation

Proposed Approach:

- Eliminate unused allocation.
- Provide incentives to transfer allocation to those who can use it.

Suggestions / Ideas for Discussion:

- There will be no adjustments to future allocations (e.g. Existing CDS rules that deduct unused allocation from future periods will no longer apply.)
- Prior to 6 weeks before the start of a quarter, a producer may advise the administrator of their inability to use their allocation for that quarter.
  - The administrator will seek to redistribute those tonnes on a pro-rata basis to producers who indicate they are willing to use those tonnes.
  - In the event that all tonnes cannot be redistributed, the producer will retain those tonnes in their allocation and will be subject to take-or-pay compensation, but exempt from the Compensation Charge
- Allocation cannot be returned to the Administrator at any other time. The Administrator will facilitate the redistribution of allocation on behalf of a producer if requested to do so. Should the administrator not be able to redistribute allocation it shall remain with the producer and all ToP and Compensation Charge obligations shall be enforced.

Rationale:

- Financial costs provide increased incentive to utilise or transfer allocation as compared to physical incentives
- Proposed solution provides greater responsibility to Producers to manage their allocations efficiently

[redacted]

10. System Management – Period End

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Proposed Approach:
- Flexibility provisions between periods as per existing CDS (+/-90kt for producers with total allocation exceeding 800kt)

Suggestions / Ideas for Discussion:
- Allocation for any given period can be used up to 5 days prior to the start of the period and up to 5 days after the period end. This provides an effective ten day overlap when allocation from either quarter may be used

Rationale:
- Incentives already exist to encourage full use of allocation and thus the flexibility does not need to be used as a mechanism for discouraging underuse.
- Overlapping allocation provides a reasonable window of flexibility to cater for vessels with laycans spanning the quarter end.
- Accommodates within reasonable limits the possibility of vessels at the end of a quarter being delayed beyond a producer's control.
- Remove any disincentives for vessels arriving close to the end of the quarter.

[redacted]

Objectives

Implementation Planning, Timetable & Next Steps

[redacted]

2005 Implementation Timetable

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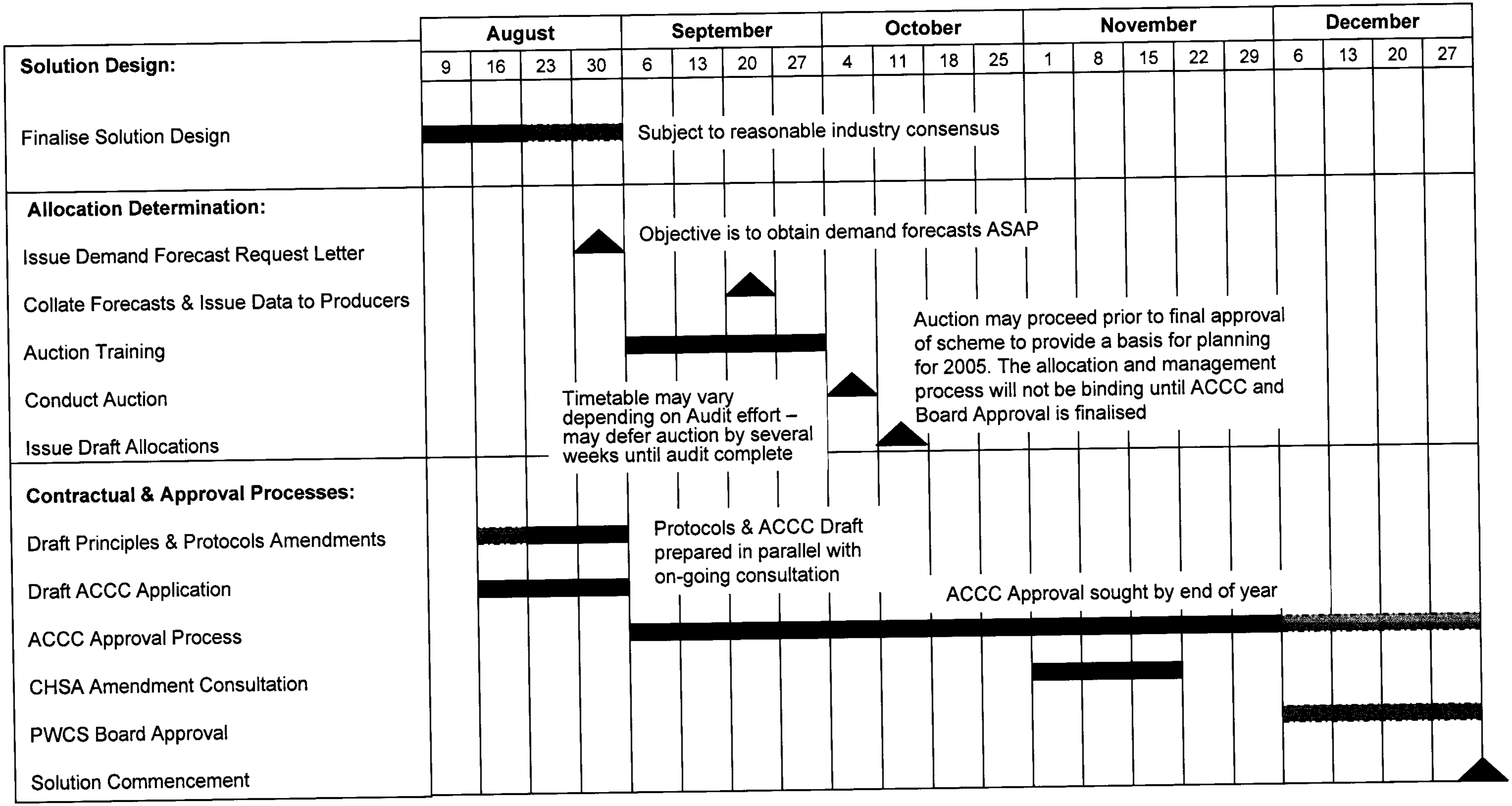

Next Steps – Medium Term

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To ensure a solution can be implemented for 2005, a recommended approach and application to the ACCC is required by late August.

PWCS are seeking a commitment to the following timetable from the industry:
Items in BOLD are actions for all participants to diarise:

• PWCS to collate feedback and draft a solution	On-going
• Solution Design Meetings with all Stakeholders	On-going
• Auction Simulation Sessions	On-going
• **2005 Solution Presentation & Workshop 1**	**Today**
• **2005 Solution Presentation & Workshop 2**	**Wednesday 18th August (NOTE NEW DATE)**
• **Final Position Sought from all Stakeholders**	**Late August**
• Application to ACCC as required	Late August

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