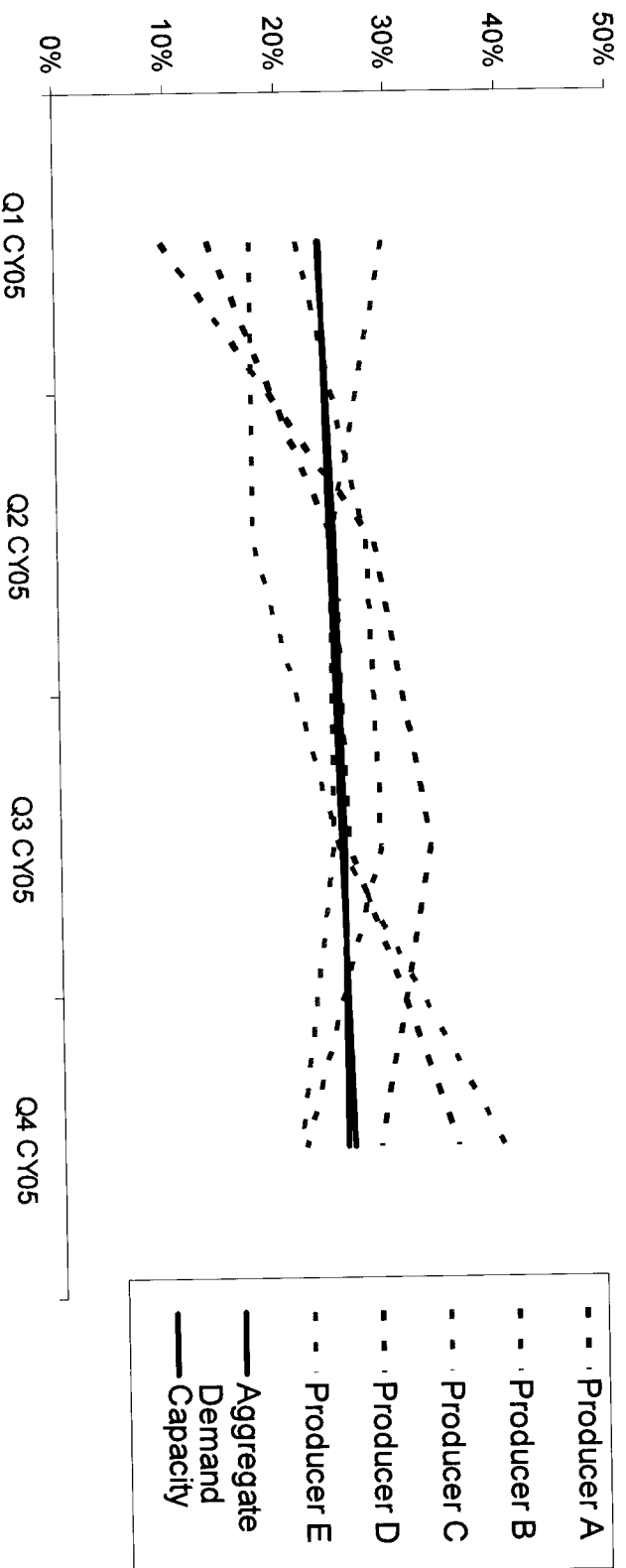


## Quarterly Allocations



- To maximise throughput the available coal chain capacity in every quarter must be fully utilised.
- It is unlikely that the aggregate Demand Profile will match the Capacity Profile exactly

### Demand & Capacity Profiles 2005



Illustrative Only. Based on Indicative Forecasts & Preliminary Coal Chain Analysis

## Quarterly Allocations



A quarterly allocation mechanism is required to distribute the annual allocation across quarters such that the Aggregate Allocation Profile matches the available Capacity Profile AND:

- Each producers' annual allocation is unchanged
- Each producers' demand profile is matched as closely as possible

	<i>Flat Allocation</i>	<i>Allocation Based on Capacity Profile</i>	<i>Allocation Based on Algorithm or Administrators Best Endeavours</i>
<b>Pros</b>	<ul style="list-style-type: none"> <li>• All producers treated equally</li> <li>• Allocation profile can be adjusted through use of flexibility provisions and secondary market</li> </ul>	<ul style="list-style-type: none"> <li>• Aggregate Allocation profile matches capacity profile</li> <li>• Each producers annual allocation is unchanged</li> <li>• Allocation profile can be adjusted through use of flexibility provisions and secondary market</li> </ul>	<ul style="list-style-type: none"> <li>• Aggregate Allocation profile matches capacity profile</li> <li>• Each producers annual allocation is unchanged</li> <li>• Producers' demand profiles are matched as closely as possible</li> <li>• Allocation profile can be adjusted through use of flexibility provisions and secondary market</li> </ul>
<b>Cons</b>	<ul style="list-style-type: none"> <li>• Will not match capacity profile if capacity is not uniform across the year.</li> <li>• Does not reflect producers' quarterly demand for allocation. Particularly applicable to ramping up mines.</li> </ul>	<ul style="list-style-type: none"> <li>• A producer could be issued with more allocation than they nominated for any given quarter.</li> </ul>	<ul style="list-style-type: none"> <li>• A producer could be issued with more allocation than they nominated for any given quarter.</li> </ul>

## Flexibility Provisions



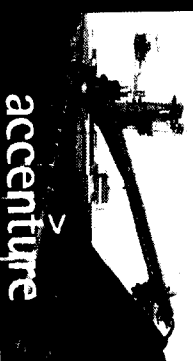
Significant flexibility provisions are included in the solution framework including:

1. Potential for quarterly sculpting of allocation to help match known variation in demand
2. Secondary trading to enable producers to swap and trade allocations
3. -30/+150kt flexibility provisions for closing allocation balance at end of quarter
4. 10 day overlap at the boundary of each quarter for using either quarter's loading allocation

A suggestion from one producer has been that producers cooperate with each other to provide additional flexibility to producers:

- Producer groups may by agreement swap allocation between themselves so as to provide increased flexibility
- There is nothing within the current CDS or the Medium Term Draft Solution that inhibits or prevents producers acting in this manner

## Audit Trigger, Arbitration & Options



### **Audit:**

- Auditor(s) to be appointed by a Producer Reference group
  - The Administrator of the solution will formulate guidelines for the application of audit of demand nominations with input from the industry
  - An audit will determine the capability and intent of the producer to export coal through the coal chain
  - A producer can choose to either accept the auditor's determination, or their original demand nomination (subject to further controls)
  - A producer who is audited and elects to retain their nominated demand will be excluded from bidding beyond pro-rata in a demand-reduction auction and may only act as a buyer of allocation in any one-way transfers of loading allocation
  - The audit should take into account (but not be limited to):
    - appropriate authorisations (mining lease, development consent)
    - capacity of plant/equipment (e.g. wash plant, stockpile capacity etc)
    - mine plans and budgets
    - # employees & shifts in budget plans
    - train contracts and loading point capacity (aggregate forecasts for each specific load point to determine feasibility)
    - plans for domestic vs export production
    - historical exports
  - A producer may elect to not be audited, but will then commit to physical delivery and compensation
- Reference Group:**
- PWCS will develop a mechanism with producers to reach a recommendation for the appointment of an auditor

### **Rationale:**

- To validate accuracy of demand nominations.
- Provide complete transparency to an independent body.

## Compensation for Under-use of Allocation



### Proposed Approach:

- The ability to “hand tonnes back to the Administrator” has been removed. Each Producer is responsible for either utilising their allocation or trading it with another party
- Producers who have unused allocation beyond their flexibility limits at the end of a quarter will be required to pay the coal handling services fee (the TOP charge) on the unused tonnes. Producers who have unused tonnes will also be required to further compensate other producers as follows:
  1. Producers who have either not been audited or have accepted an audited starting demand – will have an equivalent volume of unused tonnes beyond the flexibility limits deducted from their loading allocation in the subsequent quarter. Such allocation will be distributed pro-rata with all other producers willing to accept it.
  2. Producers who have elected to use their original demand nomination as a starting point, rather than an audited reduction, will be required to pay a compensation charge on the unused tonnes beyond their flexibility limit at the end of the quarter. Such financial compensation will be shared pro-rata with all other producers
- 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 find counter parties to accept the allocation and the corresponding TOP obligation it shall remain with the producer and all TOP obligations shall remain on that allocation.
- If a producer seeks to redistribute allocation via the Administrator prior to the start of the quarter, then they will be exempt from the physical or financial compensation, whichever applies (however the TOP obligation of the coal handling services fee still applies)

### Rationale:

- Proposed solution provides greater responsibility to Producers to manage their allocations efficiently
- Provides incentives to release or trade allocation early so that throughput is maximised
- Compensation is to producers (as opposed to PWCS) as it is the producers who have otherwise lost an opportunity



## 1. Trigger In:

- A 3Mt Trigger has been set for the implementation of a balancing mechanism. i.e. pro-rata or auction will only be used to balance demand and supply should aggregate demand exceed supply by 3Mt or more.
- If excess demand is less than 3Mt then all producers will receive their nominated (or audited) demand.
- Under all scenarios there is provision for PWCS to increase or reduce allocation so as to ensure the objectives of the scheme are achieved i.e. to ensure a working is queue available.

## 2. Trigger Out:

- There is no Trigger-out mechanism by which the solution would be stopped. If aggregate demand reduces below the available capacity then all participants have access to all the loading allocation they need, with the ability for any producer to nominate additional vessels beyond their allocation up to the available capacity of the port.
- In a situation where demand and supply fundamentally change during the year, the a mechanism to suspend the compensation charges will be required – to be discussed

# Objectives

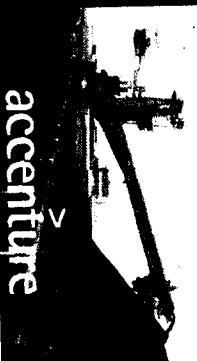


## Breakout Session 2:

### Auction Controls

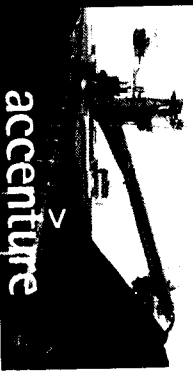
- Conduct of auction: sealed-bid; open outcry (i.e. real-estate auction); online English auction
- Price controls i.e. maximum allowable bid price; clearing price safety net
- Volume controls i.e. minimum bid volumes (e.g. all producers must submit at least up to a pro rata reduction to cap exposure to auction price)

# Conduct of the Auction



Sealed Bid Auction	English Auction	Dutch Auction
<p>Bidders submit a schedule of bids indicating their willingness to reduce tonnes at different price points. All bids are submitted at once.</p> <p><b>Pro's</b></p> <ul style="list-style-type: none"> <li>• Administratively simple</li> <li>• Likelihood of collusion reduced</li> <li>• Encourages rational bidding behaviour                             <ul style="list-style-type: none"> <li>– Removes potential for 'frenzied' bidding</li> <li>– Potential for intimidation removed</li> </ul> </li> <li>• Demand / Supply nature of bids precludes use of 2<sup>nd</sup> price sealed bid auction type</li> <li>• Confidentiality of bids maintained</li> </ul> <p><b>Con's</b></p> <ul style="list-style-type: none"> <li>• Optimum strategy is to shade bid</li> </ul>	<p>Bidders nominate their willingness to reduce tonne as the compensation price increases. As price increases, more bids are expected.</p> <p><b>Pro's</b></p> <ul style="list-style-type: none"> <li>• Optimal to bid up to perceived value of item</li> </ul> <p><b>Con's</b></p> <ul style="list-style-type: none"> <li>• Higher likelihood of collusion</li> <li>• Bids are not confidential (forced to disclose commercially sensitive information, unless anonymous online auction format used)</li> <li>• Administratively more complex e.g. online auction infrastructure</li> <li>• Weaker bidders may be intimidated</li> <li>• Potential for irrational bidding behaviour</li> </ul>	<p>Bidders nominate their willingness to reduce tonnes as the compensation price decreases. As price decreases, fewer bids are expected.</p> <p><b>Pro's</b></p> <ul style="list-style-type: none"> <li>• Privacy maintained</li> <li>• Theoretically produces equivalent bid strategies to sealed bid auction</li> </ul> <p><b>Con's</b></p> <ul style="list-style-type: none"> <li>• Potentially time consuming</li> <li>• Potential for irrational 'frenzied' bidding</li> </ul>

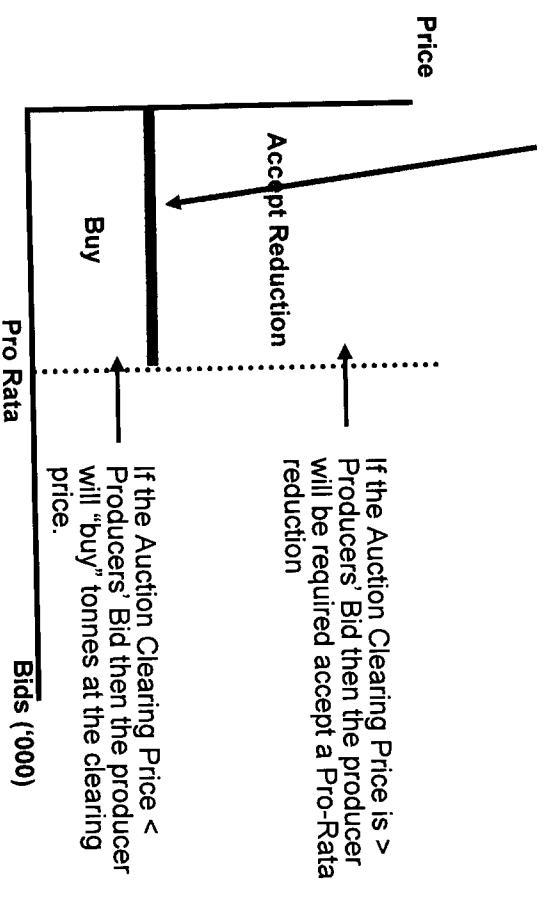




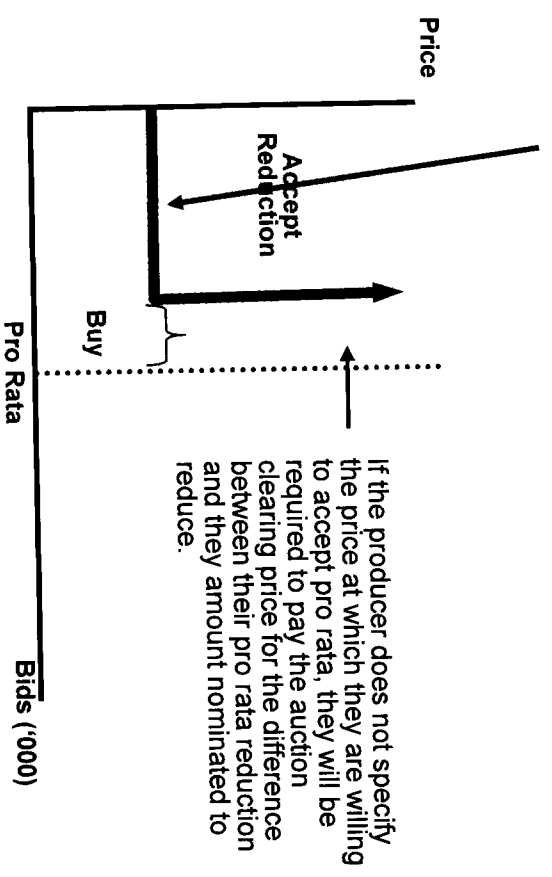
## Auction Price & Volume Controls

A minimum bid rule (requiring each Producer to bid a minimum of their pro rata reduction) is being proposed to ensure each Producer sets the maximum price at which they will "buy" tonnes .

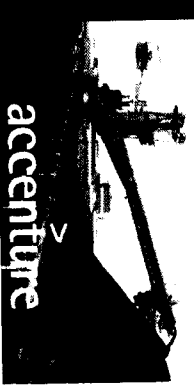
By bidding up to their pro-rata reduction a producer sets the maximum price that they are prepared to pay for allocation.



If a producer failed to bid in a pro rata reduction at any price, they would have an uncapped "buy" exposure to the auction clearing price.



## Auction Price & Volume Controls

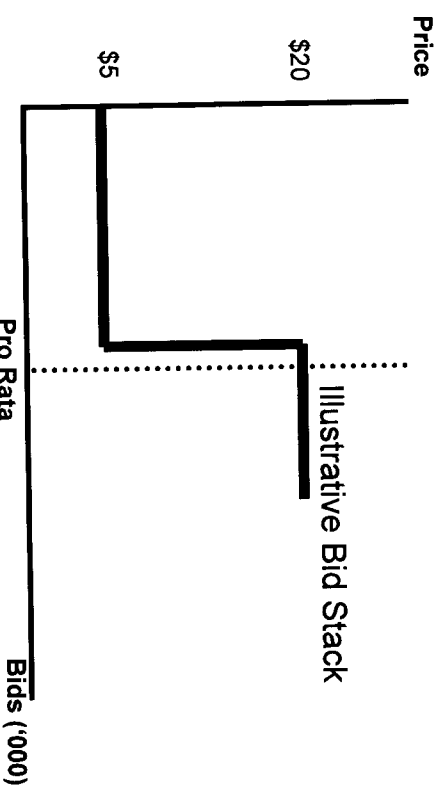


What additional price controls does the industry desire to minimise the total cost of demand and supply balancing?

### Scenario:

- 10Mt of demand reduction required in auction
- 9.9Mt bid at \$5/t
- 0.1Mt bid at \$20/t

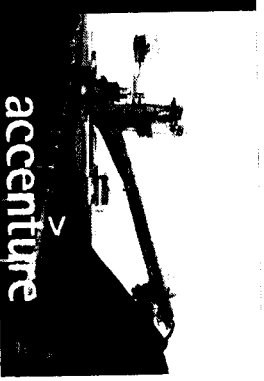
Cash flows increased by \$150M as a result of small volume bid at high price



### Options for discussion

- Accept bid structure as bid as true indication of value of loading allocation: sellers benefit from higher price, buyers pay no more than they are prepared to pay
- Give Administrator discretion to clear the auction at 9.9Mt and impose an addition 0.1Mt pro-rata adjustment on auction participants
- Publish the bid stack and let the auction participants determine the clearing level

## Objectives



### Next Steps:

- Demand Forecasts
- ACCC Authorisation
- Legal Framework
- Timetable
- Action Items


## Demand Forecasts



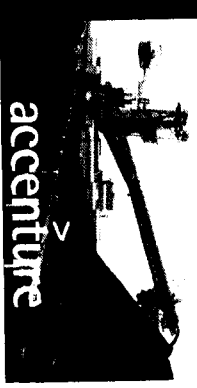
PWCS will be requesting nominations from Producers for 2005 to 2007. These forecasts will form the starting point for determining each producer's loading allocations in 2005.

### PROPOSED CONDITIONS TO APPLY TO 2005 FORECASTS:

- A **Take or Pay obligation** on each Producer's final loading allocation equal to the coal handling services fee will apply
- The potential **audit of mine forecasts** to confirm the productive capacity of the mine to produce and deliver to the port the volume of coal indicated by the forecast
- Publication of the forecast at the Producer level to all other Producers to ensure **transparency** and confidence in the forecasts
- Requirement to provide physical or financial compensation to other producers in the event loading allocation goes unused (beyond flexibility provisions) in a quarter

- 
- **Request issued** – Next Week
  - **Demand nominations due** – Third Week of September

### TIMETABLE:



## Application

- Implementation of the full solution is dependent upon approval from the ACCC
- An application to the ACCC reflecting the industries preferred approach is being drafted with the intent of seeking interim authorisation to enable an auction to be conducted and allocation to be calculated for all producers.
- The objective is to provide all producers with certainty of allocation volumes and system rules for 2005 as soon as possible, but still to provide the usual process for interested parties to make submissions to the ACCC before the solution can be implemented

## Timing

- Application: Mid September
- Interim Authorisation (Partial for auction): Mid October
- Final Authorisation: Q1 2005

## Support

- A high level of support from the industry for the proposed solution will facilitate ACCC decision making, thereby creating certainty to the industry sooner
- To this end PWCS is seeking to attach written support or comments to its application from willing producers



### CHSA Amendments

- The Medium Term Solution will be effected via amendments to the Coal Handling Services Agreement
- A draft of the amended documents is being prepared
- The revised agreement will be included as part of the application to the ACCC

### Indicative Timing

- Draft Objectives Principles & Protocols: Mid September
- Inclusion in ACCC Application: Mid September
- Final Implementation: Q1 2005 (Subject to ACCC Authorisation)

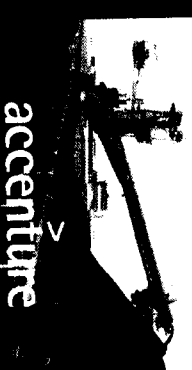
### Implementation

- Implementation of CHSA Amendments is subject to the consultation provisions of the CHSA
- PWCS with formally consult with the industry on the CHSA amendments (as was done for the implementation of the CDS)

# Draft Medium Term Implementation Timetable



	August				September				October				November				December				
	9	16	23	30	6	13	20	27	4	11	18	25	1	8	15	22	29	6	13	20	27
<b>Solution Design:</b>																					
Finalise Solution Design																					
<b>Allocation Determination:</b>																					
Issue Demand Forecast Request Letter																					
Collate Forecasts & Issue Data to Producers																					
Auction Training																					
Conduct Auction																					
Issue Draft Allocations																					
<b>Contractual &amp; Approval Processes:</b>																					
Draft Principles & Protocols Amendments																					
Draft ACCC Application																					
ACCC Approval Process																					
CHSA Amendment Consultation																					
PWCS Board Approval																					
Solution Commencement																					
	<p>Subject to reasonable industry consensus</p>																				
	<p>Objective is to obtain demand forecasts ASAP</p>																				
	<p>Timetable may vary depending on Audit effort – may defer auction by several weeks until audit complete</p>																				
	<p>Protocols &amp; ACCC Draft prepared in parallel with on-going consultation</p>																				
	<p>ACCC Approval sought by end of year</p>																				
	<p>Auction may proceed prior to final approval of scheme to provide a basis for planning for 2005. The allocation and management process will not be binding until ACCC and Board Approval is finalised</p>																				



**Key Action Items to finalise the Medium Term solution are as follows:**

**Producers:**

- Ensure understanding of the proposed solution
- Contact PWCS or Accenture on any outstanding issues, concerns or with desired input
- Prepare Demand Forecasts in accordance with the solution
- If willing, prepare attachments to PWCS application to ACCC
- Make preparations to participate in an auction (e.g. undertake training & simulations offered by Accenture)
- Ensure processes, systems and people are ready for the implementation of the solution in Q1 2005

**PWCS:**

- Continue consultation with industry on both the solution finalisation and next steps
- Finalise the solution design details
- Complete the draft of the amendments to the CHSA
- Submit application to the ACCC seeking authorisation
- Commence preparation for implementation of the solution (processes, systems, people, auction training & simulation etc)



## Next Steps: Long Term Solution



### Physical Initiatives:

- To be discussed at CEO Forum on X<sup>th</sup> of September

### Commercial Initiatives:

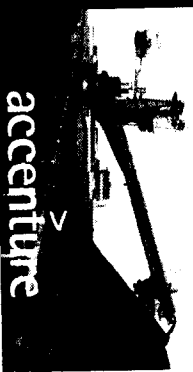
#### Formalisation of HVCCLT & Creation of System Rules:

- To be further developed with the logistics services provider and taken to industry for consultation

#### Introduction of Long-Term Top

- Commercial terms to be further developed and taken to industry for consultation

## Contact Details:



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