



**For Public Register**

28 November 2008

Mr Darrell Channing and Mr Shane Chisholm  
Director, Adjudication  
Australian Competition and Consumer Commission  
23 Marcus Clarke Street  
CANBERRA ACT 2601

Dear Mr Channing and Mr Chisholm

**Support for authorisation application regarding Dalrymple Bay Coal Terminal applications for authorisation A91107 - A91109**

We refer to your market inquiry letter dated 17 November 2008.

Xstrata Coal Pty Limited ("Xstrata") welcomes the opportunity to provide comment to the Australian Competition and Consumer Commission ("Commission") on authorisation applications A91107- A91109, lodged on 14 November 2008 in relation to the Queue Management System ("QMS") at Dalrymple Bay Coal Terminal ("DBCT").

Xstrata is supportive of the authorisation applications, the supporting submission and the proposed timetable, primarily on the basis that progress demonstrated in broadly agreeing a sound set of commercial Coal Chain Principles represents a significant step towards addressing the underlying issues of the coal chain and finally removing the need for any future rationing systems once and for all.

As indicated in the authorisation application, the most critical issue confronting Australia's largest export coal chains over the last five years has been the misalignment between the capacity of the coal chain as a whole, and the volume of contracts entered into across the separate elements of train, track and port. To the extent that coal exporters hold contracts to transport coal that are, in aggregate, in excess of the underlying capacity of the coal chain as a whole, there will be an on-going risk of excessive off-shore vessel queues forming with resultant demurrage costs being incurred, significant lost export earnings, loss of potential earnings for the State in the form of taxes and royalties, and a risk that future investment in coal mine development will be diverted elsewhere. Xstrata is of the view that, in order to resolve the misalignment, incorporation of the following three fundamental concepts should be pursued with a degree of urgency:

1. Define System Capacity: Key coal chain parameters must be agreed for the system so as producers have the ability to align separate port, track and train contracts with the capacity

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of the coal chain. These parameters must be based on an agreed operating mode of the system so as the level of 'interface losses' can be taken into account. Such losses reduce the nominal capacity of any individual element of the system and must be understood to avoid over-contracting and consequent queuing. Similarly, the parameters need to specify the levels of planned and unplanned capacity losses associated with maintenance and day to day operations. Xstrata encourages the service providers in every coal chain develop and implement Interface Agreements which document the agreed operating mode(s) of the system and associated coal chain parameters, together with the resulting definition of system capacity.

Xstrata believes that lack of a defined 'Standard Coal Chain Tonne' is the root cause of many coal chain issues and must be addressed to enable contractual alignment.

2. Introduce the definition of System Capacity into the Access Undertakings and Access Agreements governing access to the port and track infrastructure to ensure that the capacity being sold by the infrastructure owners is realistically deliverable through the system as a whole.
3. Ensure that Access Protocols are established within the Access Undertakings and Access Agreements which provide certainty to all coal exporters (both existing and potential future exporters) such that:
  - (a) Existing users have certainty of ongoing access to contracted system capacity
  - (b) New users have a defined process/path by which to both trigger and gain access to increased, or otherwise available, system capacity
  - (c) No new/expanding producer will gain access to system capacity at the expense of contracted existing users, and service providers invest to fulfil contracted obligations

These three fundamental reforms, together with other important initiatives to ensure efficient consumption of available capacity, are encapsulated in the Coal Chain Principles as outlined in the authorisation and provide the basis for achieving a long-term sustainable solution for the coal chain which eliminates the need for over-riding rationing systems and other regulatory intervention.

Xstrata believes these principles align with previous observations of the Commission that mis-alignment of contracts with system capacity is the underlying cause of vessel queuing, and that a long-term and sustainable solution is required to replace the indefinite operation of the QMS at DBCT. Xstrata also draws the Commission's attention to a paper prepared by Professor Jonathan Pincus and Henry Ergas of Concept Economics<sup>1</sup>, which examines the current problems within Australian coal supply chains. The paper expands on the challenges confronting our coal chains and discusses specific mechanisms for resolution of those problems. Importantly, the solutions proposed in the Concept Economics paper align closely with the Coal Chain Principles.

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Concept Economics - *Improving the Efficiency of Australian Coal Chains: Economic Principles and Perspectives*. This paper is accessible at [www.concepteconomics.com.au](http://www.concepteconomics.com.au), as well as on the Queensland Competition Authority's website at [http://www.qca.org.au/ra\\_2009-DAL/index.php](http://www.qca.org.au/ra_2009-DAL/index.php)



Work has already begun to progress implementation of the Coal Chain Principles with the owner of the Dalrymple Bay Coal Terminal (DBCT), Babcock and Brown Infrastructure Pty Limited ("BBI") and consultation with QRNetwork and the Queensland Competition Authority (QCA) continues in respect of the QRNetwork Access Undertaking.

To support this work proceeding over the next year, and until alignment of coal chain capacity with existing contracts can be achieved, Xstrata agrees that an interim form of capacity rationing is required to mitigate against the risk of excess vessel queuing. It is Xstrata's view that any interim system must be as consistent with the Coal Chain Principles as possible and should establish sound commercial drivers to encourage alignment of contracts for train, track and port capacity with the underlying capacity of the system as a whole. This requires that the interim system of rationing must be done by reference to all existing contracts, not just port contracts as is the case under the QMS. The allocation mechanism must also ensure that each producers allocation closely resembles (taking into account the capacity constraint), the share of capacity that the producer would otherwise have been entitled to had there been no allocation system introduced. Such an approach is commercially sound, provides a measure of equity in the treatment of all producers and minimises the potential for distortion as a result of the operation of the allocation system.

For this reason Xstrata supports the continued operation of the QMS for only a very short time to enable the industry to finalise the details of the Transitional Allocation Mechanism (TAM). If the details of the TAM and the longer term mechanism are not defined in detail and submitted to the ACCC by 31 March 2008, then the QMS will self-terminate. Xstrata supports this approach which provides incentive for the coal producers to continue their cooperative approach towards addressing the issue of capacity rationing within a short period of time. Xstrata also notes that addressing the TAM and the longer term solution can only be done with the support and cooperation of the logistics service providers. It is fundamental that if the Coal Chain Principles are to be adopted into the commercial framework that governs the operation of the coal chain that the track and port providers in particular participate constructively in the reform process. We also note the critical role that the QCA will continue to play in facilitating a long-term outcome, particularly in light of the review of the DBCT and QRNetwork Access Undertakings that are scheduled in 2009 and which hold the key to addressing the underlying problem permanently.

In respect of the Commission's statutory test for the authorisation, Xstrata believes this should be satisfied on the following basis:

- The limited operation of the QMS means that the risk of vessel queuing in the early part of 2009 is mitigated, thereby providing a public benefit
- The defined period of time with a clear end-date and trigger for self termination means that the current QMS cannot continue to be relied upon as a substitute for a more commercially sound and permanent solution, addressing the Commission's concerns that the QMS may act to inhibit a long-term solution. Xstrata Coal notes that it would vigorously oppose any extension of the QMS beyond the periods within the application as the QMS is inconsistent with the Coal Chain Principles and any extension beyond the period applied for would provide distorted signals for investment and contracting that would worsen the problems which currently exist.



- There will be no public detriments arising as a result of retaining the QMS for the defined period, particularly when balanced with the prospects of a long term solution being developed within the defined timeframe. In the event that the current economic downturn reduces the requirement for capacity rationing at DBCT, the operation of the QMS should not inhibit coal exports, and in any event there is an established mechanism by which the QMS will not operate if capacity is not constrained.
- The demonstrated progress on fundamental coal chain reform and the commitment of the coal exporters in the application to table a more commercially acceptable proposal by 31 March 2008 based on the stated Coal Chain Principles is a substantial step towards addressing this coal chain challenge permanently.

In conclusion Xstrata supports the application for authorisation in relation to DBCT, as submitted by the Applicant Producers, on the above basis. Xstrata respectfully requests the Commission to enforce strict adherence to the timetable as stipulated in the application and to reinforce the Coal Chain Principles reiterated above and the need for contractual reform to ensure that coal exporters can quickly move to a position whereby they can rely on their commercial contracts as a bankable means to provide certainty of export volumes in future years.

If the Commission has any further questions, Xstrata would be pleased to assist.

Yours sincerely

A handwritten signature in black ink, appearing to read 'S. Bridger', written over a light grey rectangular background.

Stephen Bridger  
General Manager, Commercial