

Record of meeting with Xstrata Coal - coal chain reform in NSW and Queensland

2 December 2008

ACCC:	David Hatfield, Jaime Martin and Clare McGinness (Adjudication Branch) David Salisbury, Anthony Wing, Michael Gauci, Mark Roberts, Patrick Wu and Grant Kari (Transport and Transport Access Branches)
Xstrata:	Steve Bridger, Anthony Pitt and Danielle de Kock Dave Poddar and Kim de Kock (Mallesons Stephen Jaques)
Location:	ACCC (Sydney and Melbourne)
Time:	2.30 - 4pm
Attachment:	Discussion document prepared by Xstrata, <i>Coal Chain Reform</i> , December 2008.

Xstrata requested the meeting with the ACCC to discuss the Queensland coal applications for authorisation and the long term issues facing the coal export industry, including track access and port access regimes in Queensland. The meeting could also cover some issues on NSW. To the extent it covered NSW, D Poddar noted he would not be involved and if appropriate excuse himself.

During the meeting Xstrata talked to a discussion document, which is provided at [Attachment A](#). An overview of the issues raised by Xstrata at the meeting follows:

- Xstrata submits that the fundamental issue confronting coal chains is 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.
- Xstrata noted that every million tonnes per annum of contracted capacity that the system cannot deliver equates to approximately 10 ships in the queue.
- Xstrata considers there are three critical components that must be addressed to remove the current misalignment:
 - defining system capacity based on an agreed operating mode of the system so that 'interface losses' can be taken into account
 - this definition of system capacity must be incorporated into the Access Undertakings and Access Agreements governing access to the port and track infrastructure to ensure that capacity sold by infrastructure owners is actually deliverable through the system as a whole and
 - establish Access Protocols that provide certainty to all coal exporters (both existing and future) of: ongoing access to contracted system capacity; a defined process to trigger and gain access to new capacity (but not at the expense of existing contracted users); and service providers investing to fulfil contracted obligations.
- Xstrata believes that defining system capacity does not have to and should not disadvantage anyone compared to their current situation. It would, however, enable parties that subsequently invest in means to increase system capacity (for example

upgrading a load point), to 'capture' that benefit and thus provides appropriate incentives for efficient investment that do not currently exist.

- Xstrata recognises there is a lot of history in terms of previous applications for authorisation of queue management systems, but all the producers in the Hunter Valley are at a point of commitment, following the Greiner process, and there is a real opportunity for the industry to reach a long term solution - particularly with the imminent assessment of Australian Rail Track Corporation's (ARTC) proposed Access Undertaking.
- For the long term solution to be effective, Xstrata submits that ARTC's Access Undertaking must also adopt a common definition of system capacity to ensure that ARTC does not over contract and that there can be full contractual alignment within the coal chain.
- Xstrata believes that if a long term solution is not developed and implemented shortly, there will be an imbalance between demand and the capacity of the Hunter Valley coal chain for the next five to ten years. As a result, there would be a need for some form of ongoing capacity rationing system.
- Xstrata considers there is a role for regulators to ensure that monopoly service providers within a supply chain are only contracting for what they can deliver.
- Xstrata noted that the Hunter Valley Coal Chain Logistics Team has prepared a first draft of the ten year Master Plan for investment in the Hunter Valley coal chain.
- In the absence of interim authorisation, Xstrata is of the view that a proportion of the industry will look for government to introduce an alternative 'band aid' solution to address potential ship queues, which will prevent the agreement and implementation of a long term solution.
- Xstrata supports the request for interim authorisation. Further, it also recommends that the ACCC grant conditional interim authorisation, setting out firm timeframes as to when the long term solution must be developed, as well as setting out the ACCC's expectations of the principles that any long term solution should include. Xstrata believes this will help maintain the momentum and will facilitate agreement of the remaining details of a long term solution by the industry, including approval by the NSW Government.
- Xstrata noted that it intended to provide a written submission by Friday, 5 December 2007 in relation to the applications for authorisation (A91110 – A91112) lodged by Port Waratah Coal Services and the Newcastle Coal Infrastructure Group.



Coal Chain Reform

Discussion Document

December 2008



The mismatch between contracts and capacity

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 either do not specify a tonnage obligation, or 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.

Dalrymple Bay Coal Chain

As at 1/4/2009:

System Capacity: 69Mtpa

Vs

Port Contracts: 85Mtpa

Track Contracts: 74Mtpa

Train Contracts: 74Mtpa

Hunter Valley Coal Chain

As at 1/1/2009:

System Capacity: 94.5Mtpa

Vs

Port Contracts: ?117 Mtpa

Track Contracts: ? X Mtpa

Train Contracts: ? 112 Mtpa



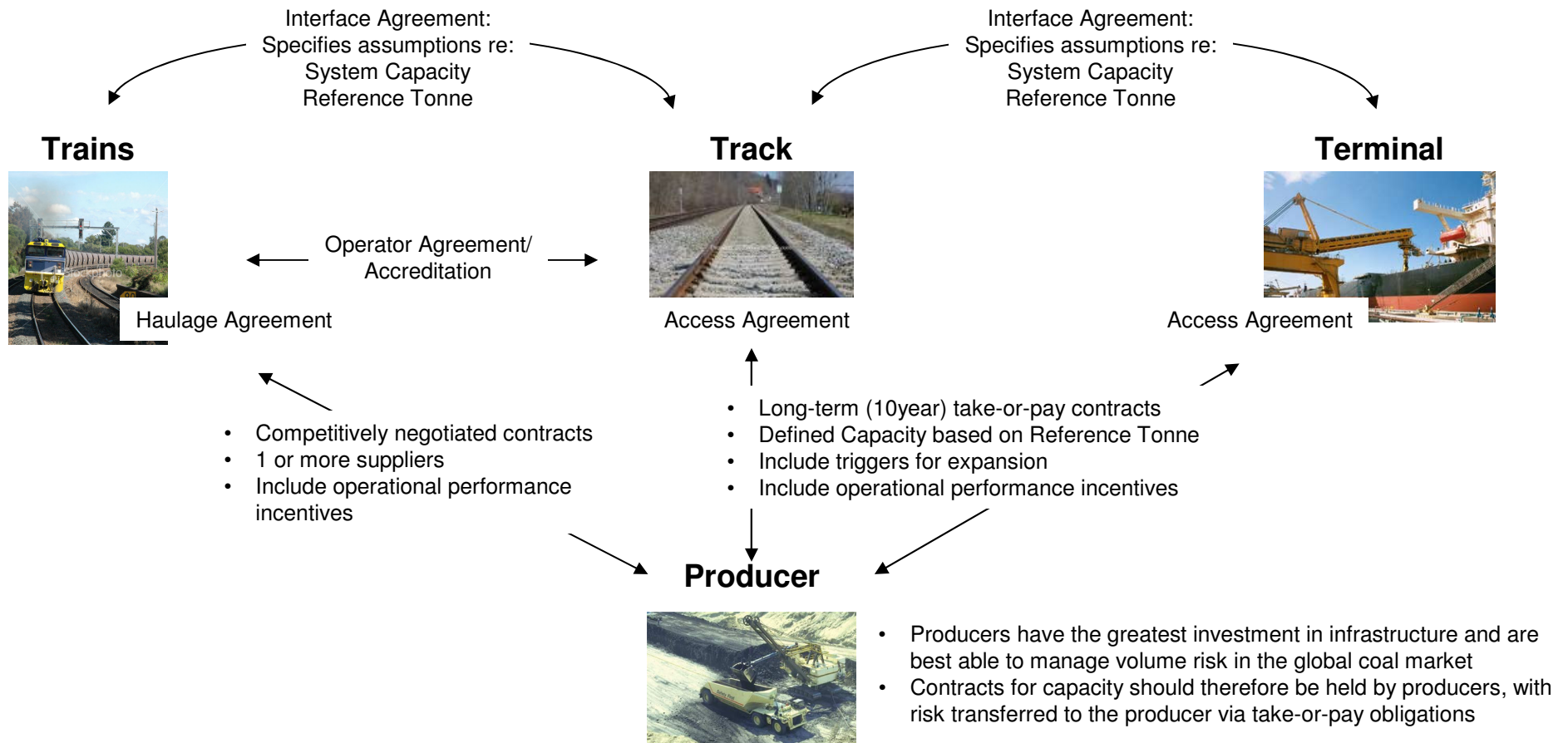
Reform is required to address the misalignment

To remove the misalignment between what is sold and what the system is capable of achieving, three urgent reforms are required to the commercial agreements for access to coal chain infrastructure:

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 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.
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:
 - Existing users have certainty of ongoing access to contracted system capacity
 - New users have a defined process/path by which to both trigger and gain access to increased, or otherwise available, system capacity
 - 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

A Sustainable Commercial Framework

The onus is on the producer to secure commercial arrangements to transport coal from the mine to the ship. The contractual framework should ensure the total contracted volumes represent achievable throughput from the chain.



Work is underway, but more is required

Coal producers have made substantial progress in 2008 towards developing solutions. Substantial further work is required with service providers, government and regulators to give effect to the solution.

Queensland	Status	Required
DBCT Port Access Undertaking	<ul style="list-style-type: none"> Producers working with BBI to re-draft Access Undertaking to introduce System Capacity 	<ul style="list-style-type: none"> Detailed negotiation to be completed Subject to QCA review and approval and support
Track Access Undertaking with QRNetwork	<ul style="list-style-type: none"> QCA consulting with producers. System capacity not yet adopted into draft access undertaking submitted by QRNetwork New form of Access Agreement distributed by QRNetwork for consultation 	<ul style="list-style-type: none"> System capacity to be adopted into the undertaking and aligned with drafting of DBCT AU. New access agreement to be distributed Subject to QCA review and approval
Coal Chain System Capacity Definition and Master Plan	<ul style="list-style-type: none"> Limited progress 	
New South Wales	Status	Required
Port Access Arrangements	<ul style="list-style-type: none"> Negotiated agreement by Producers facilitated by Nick Greiner Implementation subject to on-going negotiation by producers and NSW Government 	<ul style="list-style-type: none"> Finalisation of acceptable agreement with government and drafting of suitable access contracts
Track Access Arrangements	<ul style="list-style-type: none"> Draft Access Undertaking circulated – does not adopt definition of system capacity 	<ul style="list-style-type: none"> System capacity to be adopted into the undertaking New form of access agreement to be developed to provide for coal producers to hold capacity contracts



Next steps:

- The momentum established in both NSW and Qld for Coal Chain reform must be maintained in order to finally address the need for rationing systems and bring certainty to coal chain access arrangements
- The authorisation applications in both NSW and Qld provide for an end to the existing port based temporary mechanisms within a defined period, providing sufficient time to follow through with the progress already made on getting a sustainable solution implemented
- The public benefits from containing excessive vessel queues while limiting the extension of existing rationing systems to a short time frame provides a clear public benefit
- In granting interim and final authorisation it is essential that:
 - Strict timeframes for action be outlined and enforced – to maintain the momentum
 - The requirement for service providers (particularly track (ARTC and QRNetwork) and port (PWCS, NCIG and BBI) owners), government and regulators to act to support the process and give effect to the solution be clearly encouraged
- There is a window of opportunity in 2009 with port and track access undertakings and arrangements in Qld and NSW both up for review and providing an opening for new commercial terms to be introduced. Failure to address the reforms now will likely result in the problem of misalignment being perpetuated for years to come.