ARTC

AUSTRALIAN RAIL TRACK CORPORATION LTD

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Australian Competition and Consumer Commission
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PORT WARATAH COAL SERVICES LIMITED AND NEWCASTLE COAL INFRASTRUCTURE GROUP APPLICATIONS FOR AUTHORISATION A91110 – A91112
ARTC SUBMISSION

Please find attached a submission prepared by the Australian Rail Track Corporation (ARTC) in response to your request for comments in relation to the authorisation of applications made by Port Waratah Coal Services Limited and Newcastle Coal Infrastructure Group to the ACCC on 19 December 2008. At this time, this submission should be taken as ARTC response in relation to both the interim and substantive authorisations.

The submission contains no information considered 'commercial-in-confidence'.

For further information regarding the preparation of this submission, could you please contact myself (08)82174314, sormsby@artc.com.au or Mr. Glenn Edwards, (08)82174292, gedwards@artc.com.au (Email).

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PORT WARATAH COAL SERVICES AND NEWCASTLE COAL INFRASTRUCTURE GROUP: APPLICATIONS FOR AUTHORISATION A91110 – A91112

ARTC SUBMISSION

Port of Waratah Coal Services Limited (PWCS) and Newcastle Coal Infrastructure Group (NCIG) have applied to the Australian Competition and Consumer Commission (ACCC) for authorization of a process for rationing Newcastle port capacity to coal producers for the first 6 months of 2009 (Tonnage Allocation Stage 1), and a process and timing for development and application of industry based Long Term Protocols to apply from 1 July 2009. These processes will supersede the Capacity Balancing System currently in place at Newcastle port due to expire on 31 December 2008.

The authorisation is sought with respect to the above arrangements made between PWCS and export coal producers using the Port of Newcastle which may represent exclusionary provisions within the meaning of s45 of the Trade Practices Act (1974) (TPA), have or may have the effect of substantially lessening competition within the meaning of s45 of the TPA, or may prevent or substantially hinder a third person from engaging in trade or commerce involving the movement of goods between Australia and places outside Australia.

With respect to interim authorization, ARTC notes that the ACCC intends to consider a range of factors, including:

- harm to the applicant and other parties if interim authorisation is, or is not granted;
- possible benefit and detriment to the public;
- the urgency of the matter; and
- whether the market would be able to return to substantially its pre-interim state if the ACCC should later deny authorisation.

In any event, both the interim and substantive authorization decisions would consider the likely public benefits and effect on competition, or any other public detriment, from the proposed arrangements.

It should be noted that, at this time, this submission should be taken as ARTC response in relation to both the interim and substantive authorisations.

BACKGROUND

ARTC is a company, under the Corporations Act, whose shares are owned by the Australian Government and is overseen by the Minister for Infrastructure, Transport, Regional Development and Local Government, and Minister for Finance and Deregulation.

ARTC currently has responsibility for the management of over 10,000 route kilometres of standard gauge track through ownership, lease or under management contract, in South Australia, Victoria and Western Australia and New South Wales. In particular, ARTC manages the interstate rail network from the Queensland border to Kalgoorlie and the Hunter Valley coal network in New South Wales.

On its network, ARTC is responsible for:

i. Selling access to train operators
ii. Pricing access to train operators
iii. Development of new business
iv. Capital investment
v. Operational management
vi. Management of infrastructure maintenance

ARTC has voluntarily submitted, and the ACCC has accepted, an access undertaking, in accordance with Part IIIA of the Trade Practices Act, covering those parts of the interstate rail network managed by ARTC. The undertaking sets out the framework under which access to that network can be negotiated with ARTC in a fair and balanced way. The broad approach adopted by ARTC in the undertaking, consistent with the company's own objectives, is to ensure long term sustainability of the interstate rail network through increased utilization and rail market share growth. ARTC seeks to promote competition in interstate rail transport by providing access to the network in an open, equitable and efficient manner.

In endorsing ARTC's access undertaking, the ACCC recognized that a large part of ARTC's revenue is derived from rail operations that compete in markets subject to strong intermodal competition, particularly road.

Access to those parts of the ARTC network in NSW (including those not forming part of the interstate network and the Hunter Valley coal network) is currently governed by the NSW Rail Access Undertaking which is not certified by the National Competition Council (NCC) for the purposes of Part IIIA of the TPA

In order to recognise the unique commercial and operational arrangements that exist on the Hunter Valley coal network, ARTC has decided to submit a separate access undertaking to apply to this part of ARTC's network. ARTC is currently consulting with stakeholders on the content of this undertaking and is intending to submit an application with respect to this undertaking to the ACCC in late 2008.

ARTC's ROLE IN THE HUNTER VALLEY COAL CHAIN

In order to gain greater control over the management of the key north-south rail corridors ARTC, with the support of the Australian Government, has negotiated a long term lease arrangement with the NSW Government in September 2004, which effectively gave ARTC control over the interstate network, and Hunter Valley coal network in NSW in order to deliver the greater continuity of access management on these networks.

ARTC's key objectives in relation to the Hunter Valley network has been to actively cooperate and support industry arrangements and forums seeking to optimise coal supply chain capacity, and to deliver rail capacity (in the context of the broader coal chain) to meet industry demand. To this end, ARTC recognises the successful outcomes that have been achieved through the activities of the Hunter Valley Coal Chain Logistics Team (HVCCLT), a supply chain coordination group established through voluntary participation of coal chain service providers. ARTC recognises that Hunter Valley coal export volumes through the port of Newcastle are constrained by the supply chain system capacity and activities that have been undertaken by the NSW Government and the industry to seek to develop both short and long term solutions to improve the performance of the export coal supply chain.

Since take up in NSW, ARTC has been delivering a substantial program of infrastructure investment on the interstate north-south corridors, and the Hunter Valley network, that will bring about significant performance benefits designed to improve rail efficiency and infrastructure capacity and to improve rail's competitiveness.

ARTC has, together with relevant industry stakeholders, developed and annually updated an investment strategy for Hunter Valley coal network. The latest development, '2008-18 Hunter Valley Corridor Capacity Strategy' is about to be released for further industry consultation. This strategy recognizes existing capacity constraints in the Hunter Valley coal supply chain, as well as forecasted demand for coal throughput. The strategy contemplates further investment in the order of $1bn in the below rail elements of that supply chain managed by ARTC over the next 5 years. This investment strategy contemplates a range of projects in various parts of the network, and is focused on delivering sufficient capacity to meet demand forecasts for mines. This is intended to increase throughput of the Hunter Valley export coal chain from around 100mT currently to around 260mT in 2018. This assumes commensurate investment is undertaken in other parts of the coal chain including the mines, port and rail rollingstock.

ARTC recognises that the Hunter Valley is different to other parts of the national rail network. In particular:

- The Hunter Valley coal mining industry generates 36% of Australian coal exports;
- That industry directly employs 9,500 persons with more employed indirectly in support activities such as rail and port operations and services;
- Growth and employment potential for the Hunter Valley coal industry is wholly dependent on its competitiveness in an international market that, in turn, is greatly influenced by the efficacy of the transportation system;
- The railway network is dominated by the coal industry and is an integral component of the coal chain;
- The railway network must accommodate passenger, intermodal and general freight services interspersed with the coal service; and
- Coal transport on rail is high volume and short haul.

ARTC appreciates that the railway network is but one component of a coal supply chain. The coal supply chain encompasses mining, processing, stockpiling, train loading, above rail transport resources and track access, coal unloading, blending, stockpiling, ship loading and sea transport. ARTC's basic commercial interest is to assist, in whatever way is most effective, to optimise this supply chain so that the lowest overall cost of coal production can be achieved, and make it more competitive on world markets.

PWCS APPLICATION FOR AUTHORISATION

ARTC has participated in the ACCC's public consultation in relation to previous applications by PWCS regarding the authorization of the Capacity Distribution System in 2004 as well as the application in relation to the Vehicle Queue Management System put forward by PWCS, Pacific National and Queensland Rail in 2007.

In its submissions, ARTC has, in principle, not supported the use of an allocation system that limits coal throughput for the purpose of reducing ship queues at the port of Newcastle. The basis of ARTC's objections has been around the impact that any system that serves to limit a producer's ability to sell coal on some basis would have on smaller producers. The Hunter Valley coal industry is characterized by a few very large players responsible for the majority of coal production and operating a number of mines in the region, and a number of smaller players responsible for the remaining production. The smaller producers would generally operate one or maybe two mines. There are also both established producers and new entrants to the market seeking to develop new mine opportunities in the region.

A pro-rata limit on each producer's level of production is likely to have a greater impact on the small producers in the region than on the major players. Mines represent high fixed cost facilities are one would expect the larger producers to have a greater propensity for flexibility in fixed cost areas to accommodate varying levels of production and absorb profitability downturns in broader corporate structures than might smaller players. Where margins in the industry are low, even a short term limit on production may seriously impact the profitability of smaller players making them vulnerable to some form of industry rationalization and corresponding reduction in the level of competition in the industry. ARTC would also expect a limit on production to have a detrimental impact on mine investment for small producers.

ARTC accepts that in the current environment, this risk would be mitigated by higher coal pricing. This however may not be sustainable. Also it could be argued that the presence of smaller and larger players is inherent in this type of industry. Whilst this is true, any regulation of the industry should not create an uneven playing field.

Further, to the extent that limiting throughput may impact on the new mining developments in the upper Hunter Valley region, where transport costs are higher and operations are more marginal, ARTC sees greater risk to those new developments. As such, any capacity allocation system that constrains throughput will also constrain investment in infrastructure. A substantial component of ARTC's planned investment program is to create capacity for new developments in the upper Hunter Valley region.

As such, ARTC continues to have reservations in relation to the use of a capacity allocation system that limits production, and the impacts on competition and investment in the Hunter Valley.

PWCS Tonnage Allocation Stage 1

The approach proposed by PWCS and NCIG in their submission at Part B to Attachment 1 is difficult to assess. ARTC understands that confidentiality obligations may prevent disclosure of actual calculations, and it is not clear whether the actual calculations have been provided to the ACCC. In any event, a worked example may have been helpful.

The outcome described in Section 4.5 of the submission suggests that the approach results in restoration of capacity to those Producers where terminal capacity was diluted under a previous capacity balancing system, with volume to 5 producers being uplifted by 1.7mT. Presumably, the approach has directed the additional 1.7mT in capacity between 2008 and 2009 to 5 particular producers. ARTC understands that 5 producers include both small and large producers.

There may be an argument that where certain producers have been disproportionately impacted by previous systems that limit capacity, then such users should be given some priority to new capacity that comes on line, but only to the extent that an original competitive framework may be restored.

ARTC recognizes that there is a need for some framework to be in place from 1 January 2009 that has the effect of reducing ship queues; something that the industry generally considers is to its detriment, and to that of the public.

Notwithstanding the concerns held by ARTC in relation to this type of solution to the problem, ARTC does not object to the adoption of the PWCS Tonnage Allocation Stage 1 as proposed from 1 January 2009 until replacement with a long term solution, as long as the approach was generally supported by both large and small producers in the Hunter Valley.

The Long Term Solution

Over the last twelve months, ARTC has actively participated in industry development, as part of the Greiner review, of a long term solution to capacity allocation and investment in the Hunter Valley coal supply chain. ARTC's continues to take a key interest in the ongoing development of a long term solution by the industry. Any solution will have some impact on the nature of ARTC's access undertaking in the Hunter Valley, and as such, ARTC would welcome any commitment by industry participants to a firm timetable for finalization of a solution as proposed in the application.

The present lack of agreed long term industry solution creates some uncertainty for ARTC as it endeavours to develop its access undertaking intended to cover the next ten years.

It is ARTC's view that any long term solution should incorporate undertakings made by the coal terminals at the port of Newcastle to the ACCC incorporating enforceable commitments as to how terminals will manage access and capacity expansion. This will increase certainty in relation to investment in the Hunter Valley coal chain, as well as confidence for new market entrants and expanding operations.

ARTC's position

Despite ARTC's previous stated concerns in relation to the impact on competition and investment of the application of capacity rationing systems, and in the absence of any alternative business solution to the problem, ARTC accepts that a keeping ship queues to efficient levels results in benefits to the Hunter Valley coal industry and the wider community.

Subject to the ACCC satisfying itself that the proposal has the general support of small and large producers in the Hunter Valley, ARTC does not object to the introduction of the proposed PWCS Tonnage Allocation Stage 1 from 1 January 2009 until replacement with a long term commitment. ARTC supports the complimentary and contingent commitment by the ports to the development of a long term solution by 1 July 2009, and believes that any long term solution should incorporate enforceable commitments by the ports in relation to access and capacity expansion, incorporated in Part IIIA Access Undertakings approved by the ACCC.