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Dr Malcolm Roberts
Chair
Chief Executive Officer
Queensland Competition Authority
GPO Box 2257
Brisbane Qld 4001

Dear Dr Roberts

Peabody Energy Australia Pty Ltd "Peabody" Submission to the Queensland Competition Authority ("QCA") – Aurizon Network's 2013 Draft Access Undertaking.

In response to the QCA's request for submissions in relation to Aurizon Network's 2013 Draft Access Undertaking, we enclose Peabody's submission.

If you have any questions in relation to this submission please contact (07) 3333 5628.

Regards

1. Introduction

On 30 April 2013, Aurizon Network ("AN") submitted to the Queensland Competition Authority their 2013 Draft Access Undertaking ("UT4") which aims to provide the framework for the operation, maintenance and expansion to the Central Queensland Coal Network.

Peabody Energy Australia Pty Ltd "Peabody" rejects the draft UT4 submission in its present form and provides broad comments on some issues contained within to support this position. These comments will be in response to the UT4 submission, the consultation paper released from the QCA in August 2013 and in relation to the Queensland Resource Council's submission.

2. Peabody

Peabody through its existing operations owns 11 coal mines in Australia with a total export capacity of over 30 Million tonnes per annum. Of these 11 operations, six are located within the Goonyella coal supply chain of the Central Queensland Coal Network, with contracted export capacity via the Dalrymple Bay Coal Terminal ("DBCT") located south of Mackay. These six mines represent a significant investment and volume capacity for Peabody and are the driver of continued development in the region.

3. Support for Queensland Resources Council Submission

Peabody supports the QRC's submission to the QCA on the draft UT4. As the industry body representing central Queensland coal producers Peabody notes the significant contribution made by the QRC and its members in developing an in depth submission in response to UT4.

4. Submission

4.1 Industry Consultation

Peabody submits that the industry consultation by Aurizon in the development of UT4 has been insufficient and the nature of the undertaking unrealistic in approach and functionality. UT4 in its present form is overly complex and a material change from the current undertaking.

This lack of consultation has provided inadequate time for industry to engage in meaningful discussions and has forced industry to counter the submission put forward rather than develop a robust and sustainable undertaking for both Aurizon and Industry. While it is natural that Aurizon and industry will have different positions on some issues, it is critical for all parties to engage in genuine and timely discussions to identify the areas that can be progressed and those that will require third party arbitration. In this regard, this present strategy of development in isolation does not facilitate the negotiate-arbitrate model as proposed from the QCA.

On the basis of the isolation in which UT4 has been developed, Peabody submits that UT4 be rejected as it is not capable of satisfying all elements of Sec 138(2) of the QCA Act. Peabody recommends that based on the present position that the undertaking currently in force remain valid with both Aurizon Network and the QRC (on behalf of industry) delivering an achievable plan of developing a sustainable undertaking that facilitates practical supply chain operation and timely expansion to the central Queensland Coal Network ("Network").

A sustainable and achievable undertaking is one that is efficient, transparent and supports the *legitimate* business interests of both Aurizon Network and supply chain participants in respect to risk and delivery of service. Furthermore, it provides a workable pathway to expansion and fosters either direct or indirect network investment. A sustainable undertaking does not support a monopolistic position of providing both a risk averse and price opportunistic outcome.

4.2 Specific Undertaking Issues

4.2.1 Maintenance and Operational Costs

The increase in both maintenance and operational costs from the current undertaking to the proposed UT4 period is to be considered unreasonable in the view that along with the coal industry, Aurizon should be reviewing all opportunities for cost reductions and reviewing the maintenance and operational costs of the business to extract maximum savings while providing service and reliability.

Peabody submits that without full transparency of the cost and scope of works required in conjunction with oversight from the QCA to review proposals annually and on a reasonable basis that these cost increases should be rejected. Of note, is that the increases in costs may suggest that in previous undertaking periods the network has not been maintained to an acceptable standard or that costs are being inflated to provide for inefficient work practices.

Another area that requires consideration is to ensure that Network maintenance is aligned with other areas of the relevant coal supply chains to minimise disruptions to operations and maximise supply chain throughput. Additionally, where maintenance can be deferred (E.g. In periods low coal pricing) without a detriment to Network reliability then these should also be considered. Furthermore, a whole of life asset plan requires consideration to ensure that maintenance and operational cost forecasts extend beyond a single undertaking period to provide long term planning on maintenance requirements and Network availability.

4.2.2 Aurizon Risk and WACC

Peabody submits that the WACC rate being sought for UT4 is excessive and not aligned to the risk nature of Aurizon Network's business operations. The WACC expressed in the UT4 submission outlines a number of risk parameters to which there is minimal foundation. Firstly, there is minimal funding risk to existing operations that are backed up by long term contracts across a multitude of companies with many of those companies being of significant size to further reduce any risk around default or creditworthiness. Subsequently there is minimal evidence that the apparent volatility of the global markets would place any negative impact on the ability of Aurizon to raise funds to support any existing obligations. Finally, While Peabody will rely on the QRC submission to outline the specific issues with the proposed WACC rate, Peabody notes that the overall risk of Aurizon to provide existing assets is less than in an open and competitive market.

4.2.3 Supply Chain Participation

Peabody acknowledges that Aurizon forms an integral part of the central Queensland supply chains and their services are vital to facilitate export trade. For this reason, Peabody believes that section 8.8.1 of the undertaking, which notes that participation in a Supply Chain Group is only on a reasonable basis, is inconsistent with the proposed UT4 on the basis that it seeks to implement prescriptive Network Management Principles and operational guidelines for Network users but without open and transparent accountability to the supply chain participants where there is the ability to impact on the operation of a supply chain.

Peabody submits that it is mandatory for Aurizon and any supply chain participant to contribute to the efficient operation and development of the supply chain. This must be achieved through open, effective and transparent supply of information that seeks to maximise the equitable throughput for a coal supply chain. Where AN is only obligated on a reasonable basis to participate there is the risk of non-performance through misalignment of planning objectives, reduced oversight in the delivery and availability of contract and subsequent inability to fully utilise the supply chain.

The various System Rules processes for example underpin the Network operation to provide the framework for each dynamic supply chain and form the appropriate link with the connecting infrastructure operators and provide the agreed supply chain operating parameters required for Access Holders and end users of the Network.

Peabody recognises that supply chain operation has potential consequential impacts to Take or Pay and other financial performance measures. These matters are outside of the scope of these comments which are limited to the operation of the Network.

4.2.4 Network Management Principles

Schedule H of UT4 outlines the Network Management Principles that cover areas such as the provision of a Master Train Plan and provision of services through Intermediate and Daily Train Plans. These principles operate in isolation and are not reflective of the interaction required to coordinate an efficient supply chain. Peabody submits that the Network Management Principles must facilitate supply chain efficiency by enabling flexibility in application.

As outlined, Aurizon Network must have a mandatory obligation to participate in the operation of the supply chain. Furthermore, System Rules must be mandatory in development and review by the QCA to align the operation of the Network with the dynamic nature of the coal supply chain to which they are developed. These System Rules must be able to incorporate flexible use of the Network Management Principles to facilitate supply chain operation.

Areas of flexibility under the Network Management Principles that may allow the current framework to be maintained but provide the ability to facilitate the operation of each coal supply chain are;

- Master Train Planning
The Master Train plan must provide transparency around contractual obligations (Annual and Monthly) as well as peaking capacity available in Monthly period where another period has insufficient capacity. The Master Train Plan must also provide transparency that the whole supply chain has sufficient capacity to coordinate all contractual obligations throughout the annual and Monthly period. I.e. A supply chain will not operate effectively where components of the Network are severely misaligned in the capacity availability
- Intermediate Train Planning.
A static intermediate train plan does not align with all supply chain operations and may simply provide unnecessary rigidity in scheduling. While there may be merit for purposes of reporting and to improve efficiency and equitable throughput, this is an area that must be able to change to support each supply chain operation.
- Daily Train Planning
The critical area of service delivery is important to ensure that Sectional Run Times are able to be achieved to ensure the validity of the Master Train Plan and the Intermediate Train plan (whether dynamic or fixed).
- System Rules
As commented, System Rules for a supply chain underpin the operation of the Network. These must be mandatory and must be capable of review by Access Holders and End Users with oversight from the QCA. As System Rules facilitate supply chain operation they must facilitate end-to-end operations. Furthermore, these System Rules should be separated from Take or Pay implications except to the extent that contracted capacity is demonstrated and deemed available.

Further consideration of the proposed Network Management Principles is that there is a lack of oversight by the QCA which contributes to the unwillingness of Aurizon Network to participate in supply chain operations. This lack of oversight and participation may reduce transparency in constrained operating environments, allow misalignment of operating activities and reduce the ability to ensure contractual capacity can be achieved.

5. Summary

Peabody does not support Aurizon Network's 2013 Draft Access Undertaking due to a;

- A lack of meaningful discussion and engagement with industry in the development of UT4.
- Unreasonable expectation around the level of return on assets that have minimal risk and the arguments to support the claim for return on assets.
- The lack of transparency and oversight of the maintenance, operation and delivery of the Network's that support the coal industry
- An unwillingness to be bound by mandatory participation in the supply chains to which they are an integral part of.
- The Structure and flexibility of the Network Management Principles

Peabody supports the QRC response to UT4 and looks forward to working with all participants in the supply chain to work toward an appropriate outcome that provides acceptable return to Aurizon and transparency and oversight to Industry.