31 August 2011

Mr John Hall
Chief Executive Officer
Queensland Competition Authority
GPO Box 2257
BRISBANE 4001

By Email: rail@qca.org.au

Dear John,

QR Network's Goonyella Coal Chain System Rules

I refer to the Queensland Competition Authority's ("QCA") invitation to provide submissions regarding QR Network's proposed System Rules for the Goonyella Coal Chain ("System Rules").

Vale Australia Pty Ltd ("Vale") has significant expansion plans for its coal mining activities in Queensland that potentially require substantial capacity on the Goonyella rail system to existing ports. Vale therefore has a strong interest in the efficient and equitable operation of this coal rail system.

Context for this submission

Vale provides this submission in the context of the Goonyella System Rules being a key element in the process by which miners acquire the logistics capacity to ship coal to port.

Vale is planning to substantially expand its coal production in the Bowen Basin and will therefore require additional capacity across the Queensland coal rail network. Vale is therefore focused upon ensuring that the process to achieve an enhancement or extension to the network is efficient and one which delivers the required capacity outcome on reasonable terms and in accordance with the requirements of the Access Undertaking.

Our understanding of the QCA's role

Vale understands that the QCA's responsibilities in relation to the Rail industry are to:

- Assess and approve third-party access undertakings to Queensland's intrastate rail network;
- Arbitrate access disputes;
- Enforce breaches of access obligations; and
- Assess competitive neutrality

In this context Vale understands that the QCA's role with respect to the System Rules is ensuring that the System Rules are consistent with the requirements placed on QR Network under Clause 7.1 (c) of the 2010 Access Undertaking and with the principles QR Network has sought to apply in developing the Goonyella System Rules.

Our understanding of QR Network's principles in developing this agreement

In the System Rules QR noted that the following was the key aim:

"QR Network's System Rules have been prepared in accordance with Schedule G of the Access Undertaking. The purpose of the System Rules is to provide a transparent planning and scheduling process which is clearly understood by all stakeholders. The System Rules provide flexibility within the scheduling environment, whilst ensuring sufficient certainty for Access Holders in respect to their access entitlements. Ensuring trains are loaded to appropriately manage risk on our network."

Vale considers the proposed System Rules are inconsistent with these principles and the requirement under the Access Undertaking that QR Network have "regard to the equitable operation of the System Rules across Access Holders and Access Seekers (should they become Access Holders) and their customers and the terms of Access Agreements".

Comments on the System Rules

Vale is of the view that the likely impact of the System Rules is to comparatively disadvantage all miners that currently use DBCT as their primary coal point and that QR Network have therefore not had proper regard to the equitable operation of the System Rules as required by the Access Undertaking. Vale believes that the disadvantage arises as a direct result of the QR Network decision to base the train path allocation process on a 7 day committed Port projection. Cargo Assembly ports such as DBCT typically work off a 48 hour schedule and as a result Vale believes QR Network would have latitude to treat the Train Service Entitlements ("TSE") requirements of DBCT users as not "contracted" beyond the 48 hour planning horizon and thus allocate train paths to Abbot Point or Hay Point users in preference.

This means DBCT users will be the first to have their Train Paths reduced under Clause 3.2.4 where capacity is not available to service all TSE requests. Vale believes that given the likely increase in Train Path requests across the Goonyella system that will result from the Northern Missing Link traffic capacity restrictions are likely and thus DBCT users face continual reductions in their Train Path allocations. Vale strongly believes that this impact is in conflict with the requirement under the Access Undertaking that QR Network have "regard to the equitable operation of the System Rules across Access Holders and Access Seekers (should they become Access Holders) and their customers and the terms of Access Agreements".

QR Network has acknowledged in the Goonyella System Rules Explanatory Notes that the Proposed System Rules are considered by others to be inconsistent with Cargo Assembly. Vale believes the System Rules have to reflect the current operating mode of operation of the coal chains to ensure any Planning completed on the coal chain is achievable. Vale believes the current underperformance of the Goonyella Coal Chain is a direct result of the inconsistent rules that have been used in the past to model and determine capacity expansion requirements. Whilst Vale recognises the need for and is participating in the further efficient operational development of the coal chain it believes there would be further uncertainty and confusion to the coal chain to proceed with a System Rule that is inconsistent with the current operating mode.

QR Network also notes in its Explanatory Notes that the DBCT coal chain does not include a reference to the efficiency of the shipping stem as in the Hunter Valley Coal Chain. A critical factor in the development and acceptance of this requirement was the development of an independent body to administer the scheduling and planning processes in the Hunter Valley to ensure that these are completed in a transparent and independent manner. The coal chain co-ordinator (HVCCC) is independent of all service providers and coal producers with the goal of

ensuring efficient operation of the coal chain. Decisions made by the HVCCC are therefore made for efficiency reasons rather than commercial reasons. Therefore, this reference to shipping stem efficiency should only be considered in light of an independent scheduling and planning body. The Goonyella coal chain does not currently have this independent body to ensure that decisions are based on efficiency reasons rather than commercial reasons. In the Goonyella System QR Network is the commercial beneficiary of any decisions. QR Network have already indicated, via communication at industry forums, that its preference is for a 7 day planning cycle which will unfairly disadvantage DBCT users as the mode of operation at DBCT makes it difficult to plan on a 7 day cycle.

QR Network also state in the Explanatory Notes that, "the establishment of railing plans by the terminal operator under a strict order of arrival is not commensurate with the efficiency of the DBCT Coal Chain. This is consistent with the capacity modelling undertaken by the Integrated Logistics Company"(ILC). This has been identified as an area to improve efficiency of the coal chain and the ILC are currently conducting studies to understand this matter further to provide a more efficiency solution. Therefore, it is inappropriate for QR Network to assume a solution within these System Rules where a final solution has not be established or understood. Vale reiterates that the current System Rules should reflect the current operating environment until other alternatives have been clearly developed and understood. It is important to note that this work is being developed by an independent coal chain co-ordinator similar to the HVCCC in the Hunter Valley, but it is restricted in producing the most efficient result as the co mingled Hay Point Coal Chain, and future Abbot Point Coal Chain, are not participating in the study to provide the most efficient Goonyella System solution.

The Explanatory notes only refer to the DBCT coal chain. This is only one of three coal chains that currently run on the Goonyella System. There is no transparency as to the consistency or inconsistency of the Hay Point Coal Chain or the Blackwater Coal Chain has on the Goonyella System Rules. In early 2012 this will be complicated further with the inclusion of the Abbot Point Coal Chain which will be linked to the Goonyella System via the Northern Missing Link. This lack of transparency does not enable all users to understand the interface of the System Rules with these other coal chains that use the Goonyella System. Vale is concerned that all other coal chains are consistent with these rules and therefore highlights Vale's concern that other coal chains will be serviced to a level greater than the DBCT coal chain and that the System Rules do not operate equitably. Vale believes it is important that any system rules must consider all coal chains using the Goonyella System and must treat all of these coal chains in transparent and equitable manner.

Submission Topics

Cargo Assembly Requirements

The DBCT regulations and operating methodology provides for DBCT to only operate on first in-first out principle (or vessel turn of arrival). This method requires cargo be built just in time and this is referred to as cargo assembly.

QR Network refers to vessel flexibility in the DBCT cargo assembly operation to achieve the required level of even railings. Berthing out of order (vessel flexibility) does provide limited benefits to the coal chain in the form of providing a higher number of mine load-outs available for train services to draw from. Some level of berthing out of order is already performed by DBCT for operational benefits with close liaison with affected producers. QR Network, however, seems to be wrongly equating cargo assembly to even railings by assuming that berthing vessels out of order at DBCT will enable the required form of even railings.

Employing vessel flexibility to achieve required level of even railings as QR Network suggests would require a ship queue far greater than what the DBCT terminal has experienced in the past and would result in many ships being delayed for extensive periods of time. Reordering of vessels cannot achieve even railing as the terminal does not have sufficient stock holding capability to suit the conditions explained below:

- DBCT services at least 19 mine load outs. Assuming each mine produces only one type of product; to service 19 mine load outs on an even railings basis, a total of 38 stockpiles would need to be constantly being built and 38 stockpiles constantly completed, ready to be reclaimed for loading onto ships. This would require a terminal with approximately twice the stockpiling capacity of the current DBCT terminal.
- Additionally, approximately 83% of the vessels that DBCT services are multi-parcel vessels i.e. these are vessels with more than one producer providing cargo for shipment. This extends the ship cargo build time and therefore sterilisation of the yard becomes evident.

To accommodate even railings will require the ability to store the cargoes at the port, which as illustrated above is not possible given the amount of available stockyard space and the amount of mines that need to be serviced.

Therefore, suggesting that vessel flexibility at DBCT is essentially a feasible mechanism to align two different operating methodologies within the Goonyella coal chain is incorrect and such a statement is open for misinterpretation. Vessel flexibility is being considered in a process of consultation with stakeholders in the DBCT chain. At this time a clear understanding of how this will operate has not been established and therefore the System Rules being developed by QR Network should only reflect the actual current mode of operation until a viable alternative has been developed. To proceed with a System Rule that is inconsistent with the current mode of operation will not assist the coal chain as decisions made using these System Rules may be inconsistent with the mode of operation.

Vale is of the view that a System Rule should not be created where the likely impact of the System Rule is to comparatively disadvantage all miners that currently use DBCT as their primary coal point. Vale believes that is a direct result of the QR Network decision to base the train path allocation process on a 7 day committed Port projection. Cargo Assembly ports such as DBCT typically work off a 48 hour schedule and as a result Vale believes QR Network would have latitude to treat the Train Service Entitlements ("TSE") requirements of DBCT users as not "contracted" beyond the 48 hour planning horizon and thus allocate train paths to Abbot Point or Hay Point users in preference.
This means DBCT users will be the first to have their Train Paths reduced under Clause 3.2.4 where capacity is not available to service all TSE requests. Vale believes that given the likely increase in Train Path requests across the Goonyella system that will result from the Northern Missing Link traffic capacity restrictions are likely and thus DBCT users face continual reductions in their Train Path allocations. Vale strongly believes that this impact is in conflict with the requirement under the Access Undertaking that QR Network have "regard to the equitable operation of the System Rules across Access Holders and Access Seekers (should they become Access Holders) and their customers and the terms of Access Agreements".

Timeframes

The NML will be operational in first quarter 2012. The Newlands System will be then be intrinsically linked to the Goonyella system. It has been identified by the ILC that substantial cross system traffic issues will impact the Goonyella coal chain throughput. The proposed draft System Rules for Goonyella Coal Chain does not address these issues and hence, once in operation would be applicable for no more than 3 months. The System Rules should consider this system to ensure the co-joined Northern Bowen Basin System functions as one efficient system.

From an overall coal chain perspective, the importance of the Northern Bowen Basin scheduling methodology cannot be underestimated. The ILC conducted two (2) workshops to identify and establish the methodology that may be used to coordinate scheduling issues between the Newlands and the Goonyella Coal Chains and this issue still has not been resolved. This methodology is important for planning services to coal load points that service two or more ports. The concern that Vale has is that any Port with even railings and therefore greater planning period will be given priority of planning and service over of cargo assembly ports such as DBCT with a shorter planning period due to the mode of operation at DBCT.

Consumption of Train Service Entitlements (TSEs)

The Goonyella system has a high level of daily operational variability to plan. This variation will increase once the Newlands system is connected to the Goonyella coal chain.

We understand that the TSEs will continue to be allocated as per current Access Agreements i.e. monthly entitlements in accordance with the Access Agreements where monthly paths are based on a 30 day month. For scheduling purposes the monthly entitlements will be divided into weekly entitlements with adjustments for planned maintenance. We understand that this division of entitlements is for scheduling purposes only and is not rigidly applicable in the context of contractual entitlements. The concern Vale has with this rule is that cargo assembly mode of operations required high volumes in short periods which could delay the operations at DBCT. Cargo Assembly mode may require a producer to transport coal above the notional weekly allocation for a week. This additional tonnage would rank lower in the hierarchy which could delay the loading at DBCT. This will have a flow on effect as a large portion of shipments at DBCT are multi cargo so this user will affect other producers on this shipment and any delay in vessel loading will reduce stockpile space at DBCT which will ultimately reduce port throughput. Vale believes this rule needs to be reviewed to reflect that cargo assembly moves closer to even railings over a month but is incompatible with even railings over a weekly planning cycle. It will also be important to establish the rule that equitably treats the reallocation of paths that differ from the weekly plan. Any deviation from the plan should be reallocated in an equitable manner between the competing coal chains on the Goonyella System.

There is a level of ambiguity regarding when the consumption of the allocated TSEs occur. The draft Goonyella system rules specify that the TSE consumption is at the 48 hour scheduling process whilst it has been communicated at coal chain forums that consumption of TSEs will be calculated against a fixed weekly plan. The System Rules now appear to be in conflict with the verbal communication that has been received from QR Network.

We understand that a fixed weekly plan is being proposed by QR Network where planning for a weekly period will be done every Tuesday and locked in on every Thursday of the week prior to the applicable weekly period starting next Monday of each applicable week. So, in effect the weekly plan will already be locked in at least 3 days in advance of the start of the plan period and 10 days in advance of the end of the weekly plan period

While this might be suitable for even railing scenarios in a non-congested system; this will not work for cargo assembly operations in an increasingly congested system with a high level of operational variability. There has been no evidence to suggest that the Hay Point Coal Chain based on even railing operation experience any less variation. In fact, due to the shared rollingstock and network infrastructure applied across both DBCT and HPCT, logistically it would be fair to accept that variation exists. With increased tonnages leading to a more dense coal supply chain, the likelihood of variation increasing in an uncoordinated environment is highly probable.

Transparency

QR Network states that the draft Goonyella System Rules are aimed to provide a transparent scheduling environment. The current status quo does not provide for this to happen and the draft System Rules for Goonyella Coal Chain provide no remedy to this ongoing problem. The scheduling environment for the Goonyella Coal Chain should be completed by an independent body to ensure decisions are made for the efficient use of the Coal Chain and not for commercial reasons. There needs to be a paradigm shift in planning and consumption transparency across the entire coal chain, and these rules do not offer any increased transparency to the planning function from a coal chain perspective.

Vale believes the System Rules can only be developed with the transparency and co-operations of all coal chains that use the Goonyella System. The DBCT coal chain, via the ILC, has currently established a model with system assumptions and rules to develop capacity

expansions and improve efficiency of the coal chain. However, one of the main obstacles in the development of this model has been the lack of information on the Hay Point and Newlands Coal Chains, who declined to participate in this process. Any efficiency gains identified cannot be accurately assessed as it is difficult to understand the impact the other coal chains will have on these gains.

Concluding Remarks

Vale is very concerned that the System Rules have been submitted with the knowledge that they currently do not represent the current cargo assembly mode that currently operates in the DBCT coal chain. The System Rules appear to provide more certainty to even railings operations at the detriment of users that work on a cargo assembly basis. DBCT has limited stock pile area and is servicing a large number of producers and have limited opportunity to modify operations to enable them to work to these System Rules. As a result, Vale's view is the System Rules do not operate equitably across Access Seekers and Holders and considers that the System Rules should be amended to reflect that DBCT operates on a cargo assembly basis, with turn of arrival vessel order until any other operating modes are developed.

It is very important that these System Rules are correct as they should be used as the underlying assumptions in any system model that is developed by QR Network. The assumption and rules need to be accurate and equitable to ensure that future expansions that are based on these assumptions and rules achieve the capacity desired. The Goonyella Coal Chain has historically struggled to achieve the capacity expansion levels that service providers have suggested would be achieved via their modelling. It is critical that any System Rules that are now being developed and approved must reflect the current operational performance to minimise shortfalls in capacity expansions in the future. This is very important to ensure the future certainty of coal to market for new and existing coal producers. It is also important that these System Rules are established in a transparent manner which includes all coal chains that may operated on the Goonyella System to ensure the most efficient outcomes are achieved.

The DBCT coal chain has developed a model in conjunction with service providers and coal producers and the system assumptions and rules that have been established in this process should be considered as a very good reference point to compare and validate any assumptions or rules proposed by QR Network. This model is unable to include the Hay Point Coal Chain, as they declined to participate, but has been developed and administered by an independent body that is widely accepted by DBCT stakeholders. Any System Rules should be validated by an independent model similar to this to ensure that as per 7.1(c)(i) of the Access Undertaking, it has regard to the equitable operation of the System Rules across Access Holders and Access Seekers and their Customers and the terms of the Access Agreements.

Vale would welcome the opportunity to discuss these comments with the QCA in greater detail.

Yours sincerely,

Bob Skuza
General Manager Logistics
Vale Australia Pty Ltd