NSW GOVERNMENT | Trade & Investment

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Director-General

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Mr Sam Haddad
Director General
Department of Planning and Infrastructure
GPO Box 39
SYDNEY NSW 2001

Dear ~~Mr Haddad~~ Sam

Planning and Assessment Commission Review of Coalpac Consolidation Project

We are writing to you with respect to the Coalpac Consolidation Project, which is currently under consideration and review by the Department of Planning and Infrastructure.

Both the Department of Trade & Investment and NSW Treasury wishes to note their strong support of this project due to its strategic importance to NSW energy capabilities, as well as its project-specific economic benefits.

This includes no objection to the project from agencies within our cluster such as the Department of Primary Industries (incorporating NOW, Fisheries, Forest and Agriculture). We also understand the EPA has no objection.

BACKGROUND
As you are aware Coalpac Pty Ltd has sought approval to consolidate the operations of its Cullen Valley and Invincible coal mines to expand the project area and to increase production to 3.5 Million tonnes per annum (Mtpa) for 21 years. The approval was sought to enable the company to access additional coal reserves to enable the mines to continue operations past February 2013.

Following a review of key impacts of the proposal by the Planning Assessment Commission (PAC), Coalpac prepared a Preferred Project Report (PPR) which modified the proposal based on the recommendations of the PAC.

There are a number of broader strategic issues of State and regional significance which go beyond the narrow consideration of the Coalpac proposal which need to be carefully considered.

The key issues are:

- Impact on coal supply in the Lithgow region and in particular coal supply to the existing power stations (Mt Piper and Wallerawang)
- Potential impacts on electricity prices
- The introduction by the PAC of a new constraint relating to buffers around rock formations without assessing the broader economic implications
- Serious flaws in the previous PAC assessment of the economic benefits of the project with the PAC attaching "*little weight*" to the economic assessment

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- PAC's implicit assessment of placing a high value on non-quantified environmental impacts.

Additional information on these issues is attached.

In early March 2013 the Cullen Valley and Invincible coal mines were placed on care and maintenance, resulting in the loss of 107 direct jobs and the potential for a total employment impact of 500 direct and indirect jobs.

There are a number of strategic consequences to the State of this project not proceeding. Potentially significant risk exists for future NSW energy security, especially in regards to coal supply to Mt Piper and Wallerawang Power Stations. Very limited options exist for sourcing replacement coal to supply these generators if this project does not proceed. The viability of both generators, but particularly Wallerawang, is dependent on access to local domestic coal at competitive prices. The closure of Wallerawang Power Station would result in the loss of a further 200 jobs as well as likely constraints on power production from Mt Piper.

Mt Piper and Wallerawang Power Stations currently source most of their coal supply from either Centennial Coal or from Coalpac. In 2011-12 Coalpac supplied nearly 25% of all coal used in these power stations. The permanent closure of the Coalpac mines would result in Centennial Coal having a virtual monopoly on coal supply to these generators. This would come at a time when some of the Centennial Coal contracts are starting to wind down and would increase the negotiating power of Centennial Coal in future coal pricing contract negotiations and may result in future supply being priced closer to export parity prices.

This would be expected to lead to further electricity price increases and be out of line with NSW Government policy with respect to lower electricity pricing for consumers.

The estimation of electricity price impacts requires complex modelling and is necessarily imperfect, however coal supply costs, which is the main variable cost for power stations, could potentially increase from the current level of around $50/tonne to a possible $70/tonne.

The precedent of basing a recommendation on curtilage in the assessment process has wide ranging implications for further approvals for other operating mines and for the development of proposed coal projects in the Lithgow region.

Should the Coalpac proposal not proceed there would be significant State and regional economic consequences. The project estimates State economic contributions of $275 million in annual direct and indirect regional output, $133 million in annual direct and indirect regional value added, $48 million in annual household income, 519 direct and indirect jobs; and over the 21 year life of mine, $439 million in royalties and local capital investment in the greater Lithgow area of $122 million.

Lastly, we would ask that the PAC take into consideration the tenets of the current Mining SEPP amendments during their evaluation even if it has not yet been gazetted.

Yours sincerely,

Mark I Paterson AO
Director General
20.8.13

Philip Gaetjens
Secretary NSW Treasury
20.8.13

Attachment – Additional Information

Impact on coal supply in the Lithgow region and in particular coal supply to the existing power stations (Mt Piper and Wallerawang)

The PAC Review has given inadequate weight to Mt Piper and Wallerawang power stations' heavy dependence on the local coal supplies from the Cullen Valley and Invincible coal mines as well as the Centennial coal mines. Apart from a relatively small supply from the Pine Dale coal mine, there are no other economic sources of coal supply to these power stations. Centennial would increase its market power over the local electricity generation in the event this Project did not proceed. In the future, this could push up offer prices for coal supply at Mt Piper and Wallerawang stations and reduce the volumes on offer.

The economics of the power supply industry are complex, but the base load coal fired power stations were sited with the intention of accessing their local coal supplies. The approval of the Coalpac proposal raises public policy issues that go well beyond the private commercial interests involved. The PAC Review gives inadequate weight to these issues.

In the absence of competition, in this case in coal supply, the economic efficiency of the market is impaired, leading to higher total cost outcomes through inefficient consumption and resource allocation decisions. Maintaining competition is therefore an important aspect of good economic policy.

The very first commitment under the National Compact on Regulatory and Competition Reform is to promote competition through effective oversight of, and support for, well functioning markets (http://www.coag.gov.au/sites/default/files/Signed%20Compact.pdf).

Potential impacts on electricity prices

Coal pricing is the main variable cost for the Mount Piper and Wallerawang power stations and as bidding prices are driven by coal prices, therefore Mt Piper and Wallerawang's place in the merit order is largely determined by coal prices. As a consequence, lower coal prices leads to overall lower power prices.

If the Mt Piper and Wallerawang power stations are forced to pay higher prices for coal as a result of no Coalpac contract to help in their negotiations then these generators may need to pay around $1.00/GJ more for their coal which would increase costs from around $50/tonne to $70/tonne. This increases the short run marginal cost (SRMC) of electricity from these generators by around $10/MWh.

The introduction by the PAC of a new constraint relating to buffers around rock formations without assessing the broader economic implications

This has significant state wide economic implication which may not be consistent with Government policy.

The existing mines within the Lithgow region of the Western Coalfield currently provide direct employment to over 1000 people and many times this number indirectly in mine and non mine related service industries.

There are also five coal project proposals in the region namely Neubecks Creek, Boulder, Wolgan Road, Running Stream and Inglenook, and these proposals could provide opportunities for medium term growth or at least sustain employment within the Lithgow region.

A decision to recommend refusal of the Coalpac Consolidation Project on non technical grounds could place in jeopardy the long term security of jobs within existing mines and the employment and other social and economic benefits that would be derived from the development of new proposals.

Coal mining has traditionally been the economic backbone of the Lithgow region and setting a precedent on a new aesthetic environmental consideration could be devastating for the economic future of this district.

Serious flaws in the previous PAC assessment of the economic benefits of the project with the PAC attaching "little weight" to the economic assessment

The PAC found that the economic assessment of the Project grossly overstated the real financial benefits of the Project and as such should be accorded little weight.

However in Treasury's view, the economic assessment report presents an economic evaluation of the Coalpac project that is basically sound and does not "*grossly overstate the real financial benefits*" as claimed by the PAC Review. It therefore should be given proper weight in the Project assessment.

PAC's implicit assessment of placing a high value on non-quantified environmental impacts

In reaching the conclusion that the Coalpac proposal should not be allowed, it appears the PAC Review is implicitly placing a high value on the non-quantified environmental impacts. This 'high' valuation is contentious and as it is critical to the overall PAC judgement on the Project, further scrutiny and analysis/quantification of the impacts seems warranted, particularly given the PAC's discounting of the economic benefits.