



Fortescue Metals Group Ltd

ACN: 002 594 872
87 Adelaide Terrace, East Perth
Western Australia 6004
PO Box 6915, East Perth, Western Australia 6892

Telephone: + 61 8 6218 8888
Facsimile: +61 8 6218 8999
Website: www.fmgl.com.au

Our Ref: LS-160-O-0012

13 October 2008

Mr Russell Dumas
Director, Gas and Rail Access
Economic Regulation Authority
Level 6, Governor Stirling Tower
197 St George's Terrace
PERTH WA 6000

Dear Russell

RAILWAYS (ACCESS) ACT 1998 – THE PILBARA INFRASTRUCTURE PTY LTD

On 3 July 2008, The Pilbara Infrastructure Pty Ltd (TPI) submitted to the ERA, its draft segregation arrangements, required under Section 29 of the above Act. The ERA released the draft for public comment with 5 parties making comments.

The ERA has since agreed to TPI providing a response to the public comments.

Please find attached TPI's response to selected issues raised in public comments.

If you require additional information or clarification of comments in this letter and the attachment, please do not hesitate to contact me.

Yours sincerely

FORTESCUE METALS GROUP LTD

GREG DELLAR

for
The Pilbara Infrastructure Pty Ltd

Review of Submissions on TPI's Proposed Segregation Arrangements

In accordance with its obligations under Clause 16(8) of the Railway and Port (The Pilbara Infrastructure Pty Ltd) Agreement, on 3 July 2008, The Pilbara Infrastructure Pty Ltd (TPI) submitted its proposed railway segregation arrangements to the Economic Regulation Authority (ERA) for approval. The ERA has released TPI's proposed Segregation Arrangements for public comment.

TPI has reviewed the five public submissions made in response to the proposed Segregation Arrangements by the following organisations:

- Australian Rail Track Corporation (ARTC)
- Hancock Prospecting (HP)
- North West Iron Ore Alliance (NWIOA)
- United Minerals Corporation NL (UMC)
- Yilgarn Infrastructure.

Having reviewed the submissions by these organisations, TPI offers the following responses in relation to these issues.

Main Themes

The main themes that emerge from submissions are summarised in the following with appropriate responses.

Conflicts of interest faced by FMG/TPI

According to submissions:

- FMG/TPI has significant market power in negotiating with access seekers as a result of its ownership of a vertically integrated supply chain from mine through to port;
- The proposed two stage implementation of the Segregation Arrangements and exclusion of FMG as an access seeker exacerbates this market power;

- The proposed two stage implementation approach is inconsistent with the Rail Access Code (the Code) and is unlikely to encourage third party access to the rail line; and
- The second stage of the proposed arrangements should be implemented immediately.

TPI's response

TPI reiterates its commitment to an appropriate segregation arrangement before and after third party haulage arrangements are pursued. That is, before contracts are entered into, the negotiation of access is undertaken by officers who are ringfenced from the rest of the organisation.

Consequently, pursuing more prescriptive or extensive Segregation Arrangements at this stage will do nothing to reduce the issues surrounding conflicts of interest because no third party train services are being run. This is a crucial point – nowhere do the submissions substantiate why the proposed two stage process increases exposure to conflicts of interest – the negotiation of contracts will have the same exposure to conflicts of interest irrespective of whether or not partial or full segregation is in place during the negotiation process.

Lack of detail in proposed arrangements

According to submissions:

- There is a lack of detail in the proposed Segregation Arrangements, as elements of the arrangements to be developed at a later stage form part of the Segregation Manual;
- The Segregation Manual should be made available for public comment .

TPI's response

Westnet committed to develop a Segregation Arrangements Awareness Manual (SAAM) in its approved Segregation Arrangements (April 2008). However, it is not clear whether a SAAM has been approved by ERA. Certainly, no draft Westnet SAAM has been released by ERA for public comment. On equity grounds, TPI would anticipate a similar process to be adopted.

Supply chain issues

According to submissions:

- No conclusive evidence has been provided by TPI to indicate that separation of haulage and below rail would materially affect safety, operation & cost for a greenfields railway; and
- The proposed Segregation Arrangements appear to be driven by port and/or supply chain priorities. In contrast, the Code requires efficient use of the rail network.

TPI's response

TPI's network and haulage operations are administered by the Office of Rail Safety (ORS) under the Rail Safety Act 1998. A Railway Safety Management System has been approved by the ORS where network and haulage functions share a common safety system. The need for very close harmonisation of safety activities is best illustrated by the close interaction between track and wheel maintenance teams. It is critical in establishing a new railway that track hardening and grinding of the rail profile be conducted in close liaison with wheel machining programs. This ensures both safer operations and reduces maintenance overheads during early operations.

The importance of effective co-ordination in bulk commodity supply chains is best highlighted by the Queensland and NSW coal industry. These are self evident examples of what can happen when adequate co-ordination is lacking. Moreover, effective supply chain coordination requires efficient use of the rail network and is consistent with the interests of all access seekers/holders.

In the context of the Code, the coordination between the rail and port operations is covered more directly by the Train Management Guidelines and Train Path Policy documentation rather than the Segregation Arrangements.

Other Issues

Comparability of access terms and conditions

According to submissions:

- “Broadly comparable” terms and conditions for FMG and third party access agreements are not acceptable; and
- If TPI does not intend to observe Parts 2 to 4 of the Code in negotiating access agreements outside the Code, additional comfort is required on how the duty of fairness is to be observed.

TPI's response

The reference to “broadly comparable” terms and conditions is incorporated in the Westnet segregation arrangements.

The Code provides that access agreements need not contain the same provisions provided they comply with the Code (Clause 37).

In response to comments about TPI potentially negotiating access agreements outside of the Code, it is not clear why TPI needs to provide additional comfort on how the duty of fairness is to be observed in this circumstance given Code obligations/requirements are not relevant for such negotiations.

Indicative access prices

According to submissions:

- Indicative pricing for the most common access service should be published as part of TPI's duty of fairness.

TPI's response

There is no requirement under the Code for the development of indicative access prices.

Under the Code, a railway owner must provide an access seeker with the floor price and ceiling price for access (Clause 9). In addition, an access seeker has the right to seek ERA's opinion on whether the railway owner's proposed access price meets the relevant requirements of the Code (Clause 21(1)).

All access agreements provided to ERA

According to submissions:

- All access agreements, including the FMG agreement should be provided to ERA.

TPI's response

There is no requirement under the Code for an access provider to submit access agreements to the ERA, nor does Westnet appear to make such a commitment in its segregation arrangements.

Release of capacity contractual details

According to submissions:

- Parties should know the nature and extent of current contractual commitments over particular routes on the TPI network.

TPI's response

Under the Code, an access seeker can request from the railway owner capacity-related information for the route to which it seeks access, including 3 year gross tonnes data, the working timetable for the route, and the origin and destination of any train paths proposed by the railway owner for the route (Clause 7).

However, beyond this, there is no requirement under the Code for a railway owner to reveal to the industry the nature & extent of current contractual commitments over particular routes on the TPI network.

Liquidated damages

According to submissions:

- Liquidated damages should be paid when a breach of TPI's Segregation Arrangements occurs.

TPI's response

There is no requirement under the Code, nor precedent established by Westnet's segregation arrangements, that necessitates TPI committing to such a penalty provision.