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Airly Coal Mine project

Submission to Planning Assessment Commission

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September 2015

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INTRODUCTION

The Airly Coal Mine project is a small, underground mine in the Capertee Valley, north of Lithgow, NSW. It is currently being assessed by the NSW Planning Assessment Commission (PAC).

The economic assessment of the project has consisted of the following documents:

- Initial economic assessment, AIGIS group, August 2014
- Submission on economic assessment, The Australia Institute, October 2014
- Peer review of economic assessment, Centre for International Economics, January 2015
- Response to submissions including appendix F response to The Australia Institute submission, February 2015
- Revised economic assessment, AIGIS group, March 2015
- Submission by Division of Resources and Energy, April 2015
- Peer review of revised economic assessment, Centre for International Economics, June 2015

In The Australia Institute's experience of economic assessment of coal mines in NSW, rarely has the assessment of a project been so problematic and poorly conducted. The first review by the Centre for International Economics (CIE) stated:

Overall, the CBAs for the Projects have been undertaken in a manner that is inconsistent with well-established principles and the NSW Government's November 2012 Guideline for the use of CBA in mining and coal seam gas proposals. The analysis presented also lacks transparency and it is, therefore, difficult to verify the calculations undertaken. (Page 2)

Six months later, despite the revised assessment, little has changed, with the CIE finding:

It is not possible to verify Aigis' estimate of employee benefits due to a lack of information on key assumptions including the stated average wage at Airly Mine. (Page 2)

There are a number of inconsistencies with Aigis' approach to estimate the economic value of environmental impacts and also a lack of clarity about the environmental impact being assessed in some cases. (Page 2)

It is not possible to verify Aigis' estimates due to the lack of information on key assumptions such as the profitability of the mine. (Page 2)

It is hard to understand why the Department of Planning and Environment (the Department) continues to rely on an analysis that does not comply with government guidelines and is not replicable – see Secretary’s Environmental Assessment Report, p50, section 6.5 Socio-economic Assessment.

The economic assessment by AIGIS group is highly unreliable and its conclusion that the project would provide economic net benefit to the state has no robust analysis to support it. Given the project’s environmental and social impacts are likely to be negative, it is likely the project represents a net loss of economic welfare to NSW.

PROJECT VIABILITY

A key flaw with the economic assessment, the Secretary’s report and most of the other documents discussed above is that they ignore the question of whether the project is financially viable. As CIE describe, this is a “key assumption”, but one that is hardly discussed aside from in our earlier submission.

It is clear that the Airly mine is financially marginal at best. As noted in the Secretary’s report, the project was mothballed, or put in “care and maintenance” between 2002 and 2009 and again from 2012 to 2014.¹ These periods include some of the highest coal prices in history, yet the Airly mine was able to operate only intermittently.

While Centennial refuses to publish any details on the mine’s financial prospects, it is not difficult to understand why the Airly mine is marginal. It uses a high-cost mining method, bord and pillar, it sells much of its production to domestic power stations, earning lower prices and it is further from a port than most competitors meaning it will also struggle on the export market.

The viability of the project is important. If it is not profitable to run, it will not operate continually and provide the benefits of employment and royalties claimed in the economic assessment and by the DRE. Furthermore, the operators will have a strong incentive to cut corners on safety and environmental standards and be unlikely to afford proper rehabilitation and mine closure expenses.

Centennial Coal and its economic consultants AIGIS Group have a poor record in predicting the viability of their mines. In the economic assessment of the nearby Angus Place mine AIGIS wrote:

¹ Note the Secretary’s report p1 is inconsistent with Centennial’s website on the issue of when the mine has been in care and maintenance,
<http://www.centennialcoal.com.au/Operations/OperationsList/Airly.aspx>

It should also be noted that in relation to the Angus Place Colliery, the mine has operated continuously since 1979. Figure 1 demonstrates volatility in thermal coal prices over a 30-year period. As noted, this volatility has not affected continuation of mining at Angus Place Colliery.

Centennial Coal submits that this would amply establish the viability of continued operation of the mine. Centennial Coal's extensive community consultation programs have not produced any material questioning the operational viability of Angus Place or other Centennial Coal mines operating in the area. (Angus Place Response to Submissions, Response to TAI Submission, p5)

Just months later, Angus Place was closed as it was not economic to run.

The project should be rejected if it is unable to demonstrate strong financial foundations. Leaving a mine in indefinite care and maintenance, with ongoing but unfulfilled promises of jobs is not in the interests of the community. In addition to Angus Place, an example of where the finances of a coal project have been ignored to the detriment of the community and the taxpayer is the Cobbora coal project near Dunedoo. Despite repeated submissions showing the project was unviable, it was approved, but has not proceeded, leaving locals disappointed and taxpayers contributing to a compensation fund.²

EMPLOYMENT AND WAGES

The cost benefit analysis in the revised economic assessment includes a value of \$55.8 million for 'additional/sustained employment'. As pointed out in our earlier submission, under government guidelines on cost benefit analysis, this value would not be included at all, as it is assumed that workers will get other jobs:

As a general rule, it is recommended that analysts assume that labour, as with other resources, is fully employed. Moreover, unless the project is specifically targeted towards the goal of reducing unemployment, it can be expected that many of the jobs will be filled by individuals who are currently employed but who are attracted either by the pay or by other attributes of the new positions.³

Cost benefit analysis only includes wages as a benefit if it can be shown clearly that workers on the Airly project would not otherwise have a job, or be engaged in any productive activity. This is possible in times of very high unemployment, but with NSW

² <http://www.wellingtontimes.com.au/story/2457575/dunedoo-wins-in-cobbora-funding/>

³ (Department of Finance and Administration 2006) p40

unemployment at around 5.8 per cent, this is not an appropriate assumption. To include wages as a partial benefit, it has to be shown that some degree of the labour on the project would otherwise be unused, as is emphasised by NSW Treasury:

It can be argued that in times of unemployment the opportunity cost of labour employed on a project is less than the wage costs, and project costs and benefits should be adjusted accordingly. However, in practice such adjustments are not generally made and are not recommended.⁴

AIGIS Group make no attempt to estimate what portion of workers on the project might otherwise be unemployed and therefore assume that all workers would be otherwise unemployed for the duration of the project. In a highly skilled industry like mining this is clearly incorrect, as these skills would be used in other mining, construction and engineering projects.

Furthermore, the wage estimates AIGIS base their estimates on are very high - \$152,781 per worker per year. It is unclear why a mine that faces so many financial hurdles would pay a wage fifty per cent above the industry average, as assumed by AIGIS. As the CIE state in their peer review:

Aigis's estimated value of the wage premium hinges on the stated average wage at Airly Mine of \$152 781. There is no information available on which to independently test this proposition. (p5)

The CIE's inability to replicate or verify this estimate confirms our view that this part of the cost benefit analysis is particularly unreliable.

The Secretary's report claims the project would result in:

Indirect employment of an estimated 550 people across NSW (p3)

This claim is not based on the EIS and has not been considered by the CIE in their peer reviews. It comes from the submission by DRE which claims:

Based on other mine projects, DRE believes the indirect employment within the region and in NSW as a whole from the Project could be 550 positions. (p4)

DRE provide no reference or basis for this claim. It is contradicted by economic assessment of similar sized mines, such as that of the Ashton South East Open Cut. In that case before the Land and Environment Court, the proponent's economists estimated the project would employ around 160 people, but result in a net job increase of only around 80 jobs as many workers simply move from one job to another. This is the economic reality that DRE and the Department ignore.

⁴ (NSW Treasury 2007) p48

ROYALTIES

Royalty estimates by AIGIS are almost 50 per cent higher than those of DRE. DRE bases its estimates of the coal price of between AUD\$97 and AUD\$117. The current price is AUD\$87, despite DRE's claim that "the bottom of the price cycle appears to have occurred in late 2014. (p4)" Federal Treasury's long term AUD price forecast for thermal coal is \$80 per tonne, suggesting DRE's price forecasts are optimistic.

More important for royalty payments than the price of coal is whether the mine is financially viable and able to operate consistently in the current coal market. As discussed above, if it is not, these payments will not be realised. Neither DRE, the Department nor AIGIS acknowledge this simple fact.

ENVIRONMENTAL VALUATION

As pointed out in our earlier submission and emphasised in the CIE's review, the environmental valuation attempted by AIGIS has been poorly conducted. In general we agree with the CIE's assessment:

There is a lack of clarity about the environmental impact Aigis has evaluated.

Environmental valuation is difficult and subjective. AIGIS's approach is difficult to understand and in places clearly contrary to the EIS and common practice. This section of the assessment should be considered highly unreliable.

CONCLUSION

Despite several attempts and two peer reviews, decision makers have still not been presented with robust economic assessment for the Airly mine. AIGIS group's work, even when supplemented by assisting material from DRE, falls far short of government guidelines and standard practice among professional economists. This is obvious to the peer reviewers and should be obvious to the Department.

The reason the assessment for the Airly mine has been so difficult is that it does not stack up economically. The mine has scarcely been able to operate through the biggest coal boom in our nation's history and is most unlikely to run consistently in the challenging market conditions Australian coal is facing today. This project should be rejected by the PAC so that remediation and relinquishment can occur as soon as possible.

References

Department of Finance and Administration, 2006. Handbook of Cost-Benefit Analysis. *Financial Management*, (6).

NSW Treasury, 2007. *NSW Government Guidelines for Economic Appraisal*, Office of Financial Management: Policy & Guidelines Paper.