

QRC

submission

Working together for a shared future

Submission in response to QCA's request for comments
– *Queensland Rail's 2012 Access Undertaking*

To the Queensland Competition Authority
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Introduction

The Queensland Resources Council (QRC) is a non-government organisation representing companies that have an interest in exploration, mining, minerals processing, gas and energy production. It is the resource industry's key policy-making body in Queensland, working with all levels of Government, interest groups and the community.

The Council works on behalf of members to ensure Queensland's resources are developed profitably and competitively, in a socially and environmentally sustainable way.

QRC welcomes the opportunity to provide this submission on behalf of its members who are existing and prospective users of Queensland Rail's regulated below-rail infrastructure. This submission responds to the Queensland Competition Authority's (QCA's) Issues Paper dated April 2012 regarding Queensland Rail's proposed 2012 Draft Access Undertaking. QRC will participate in this consultation process and intends to contribute constructively throughout this review.

QRC has a keen interest in Queensland Rail's proposed undertaking as it provides the means by which resource companies can execute fair and reasonable commercial agreements with a monopoly service-provider that is essential for the transportation of resources to both domestic and international markets. QRC's involvement will also extend to represent the interests of member companies and promote a constructive dialogue between Queensland Rail and QRC member companies that have an interest in the efficient investment in, and operation of, the regulated below-rail infrastructure.

Queensland Rail's first attempt to develop a draft access undertaking for the declared service, following the formal separation from QR Network, represents a good attempt to simplify the regulatory arrangements. It is important to recognise the efforts of Queensland Rail to engage both honestly and directly with QRC's member companies during the initial development phase. QRC will continue to constructively engage with Queensland Rail following the formal lodgement of stakeholder submissions with a view to develop workable solutions and improve stakeholders understanding to address the various issues and concerns identified in this process. There are a range of complex commercial and regulatory issues that such require meaningful consultation in order to achieve an acceptable balance between the legitimate business interests of Access Seekers, Customers and Queensland Rail. Ongoing dialogue between QRC and Queensland Rail is extremely valuable and welcomed.

Matters associated with coal traffic on the West Moreton System are of particular interest to QRC given our engagement in previous regulatory reviews which have not been able to completely finalise a range of important regulatory arrangements. QRC welcomes Queensland Rail's commitment to work together to finalise the development of an acceptable framework to development reference tariffs for the West Moreton System in the months ahead.

QRC also is keen to resolve a range of other issues prior to the expiry of the current access undertaking. Industry acknowledges the considerable task in assessing a completely new access undertaking framework and offers its assistance in order to achieve the timely finalisation of this process. As such, QRC anticipates further discussions with Queensland Rail, QCA, above-rail operators, and other key stakeholders.



Importance of the Access Undertaking

The importance of Queensland Rail's Access Undertaking cannot be over-emphasised. A profitable coal and minerals sector is vital to the Queensland economy – and Queensland Rail's below-rail infrastructure is an essential component of a number of critical export supply chains. All inputs to resource developments, including rail access charges, must be competitive.

The Queensland resource sector's long-term prospects are subject to a range of factors that require an efficient and robust regulatory access regime.

- Projects require large amounts of capital that generally require high volumes to ensure profitability.
- Reducing unnecessary costs and improving productivity will always remain key focus for industry in order to maintain our international competitiveness.
- Queensland is subject to international competition for both capital and resource developments.
- Intense international competition in resource product markets means that there is no room for complacency with respect to any inefficiency.

A monopoly with market power is incentivised to engage in price discrimination and restrict supply if left to its own devices. This promotes over-charging for captive customers (judged to have less elastic demand and therefore are forced to pay more than an efficient, reasonable cost), while under-charging those with more elastic demand (because they have an alternative source of supply and/or cannot afford to pay full costs). Restricting supply is also a key issue that needs to be addressed within the access regime.

Summary of industry's key principles

QRC considers that Queensland Rail's Access Undertaking must incorporate the following high-level principles:

- Access regime promotes efficiency and competition.
- Light handed regime – which effectively addresses information asymmetries so that Access Seekers can enter into meaningful negotiations with the access provider.
- Ring-fencing arrangements restricted to passenger services – targeting actual, rather than perceived, competition issues.
- A workable, preferably light-handed, negotiate/Arbitrate Model, in which:
 - Access Seekers (including Customers with long-term interests in Access Rights) are able to negotiate Access.
 - Dispute resolution and compliant processes to follow prescribed escalation processes.
 - Obligation that Access Charges:
 - Discriminate between Access Seekers/Customers within a relevant market only on the basis of cost or risk.
 - Are within Pricing Limits of Incremental and Stand-Alone costs (no cross subsidies).
 - Promote the efficient utilisation and operation of the Rail Infrastructure.
- Practical and fair Network Management Principles (enabling the efficient scheduling and operations).
- Commitment to maintain the Rail Infrastructure to an appropriate standard.
- Obligation to facilitate the expansion of the network.



QRC's Position

QRC recognises that Queensland Rail's first draft has been developed, consistent with industry requests, on a first principle basis. This approach invariably results in various issues of detail needing to be refined as part of the ongoing consultation process. While industry believes that the draft access undertaking **should not be approved** by the QCA in its current form, Queensland Rail is currently on the right track towards an acceptable regulatory regime (subject to the resolution of a number of matters of detail).

Next steps

QRC anticipates intense discussions between all stakeholders following the lodgement of submissions. QRC suggests that the QCA requests stakeholder's to provide responses on submissions as this would provide the most efficient means of clarifying positions before the QCA moving towards publishing a Draft Decision. This allows stakeholders to provide more informed input and comment than is currently possible.



Key Issues

This section identifies a number of specific matters that the QRC would like to bring to the particular attention of the QCA and Queensland Rail. Further discussion is expected to be undertaken on these, and other matters, with key stakeholders following the lodgment of submissions.

→ Resource companies (Customer) require Security and Certainty

Resource companies need to be guaranteed the opportunity to be involved in the negotiation of access terms and conditions. This is because:

- Resource projects are generally large, long-term and rail dependent – companies need certainty and transparency with respect to the management of Access Rights which are essential for the transportation of their commodities over the life of their projects.
- Contractual arrangements are such that resource companies:
 - Have project developments that have much longer lives than the term of Access Agreements and/or haulage contracts; and
 - Are Liable for Access Charges, with cost pass-through arrangements.

To provide the necessary levels of contractual certainty and confidence that the management of Access Rights is prudent, resource companies (Customers) should be afforded the following arrangements within the Access Undertaking and Standard Access Agreement.

- *Obligation to identify the Customer:* In order to avoid any confusion, QRC supports a requirement that each Access Agreement entered into for resource sector projects note the identity of the Customer.
- *Clear Rights of Renewal:* While the draft access undertaking includes a general right for Train Services with an applicable Reference Tariff to renew Access Rights, QRC contends that this right should be extended beyond this narrow group of services (that is, only some coal mines operating on the West Moreton System). For example, even though a Customer may have negotiated an Access Charge which is not subject to a Reference Tariff (for example, the Camby Downs or Colton mines), there is currently no certainty of renewal of Access Rights.
- *Customer Initiated Transfers:* Customers should have the ability to require the transfer of their existing Access Rights from the current nominated Access Holder.
- *Notification of Renewal Obligation:* Queensland Rail should notify a Customer, within a reasonable time ahead of expiry, of the requirement to renew rights for Access Rights (regardless if these are currently held by another party on the Customers behalf).
- *Customer Verification of sought Transfers and Applications for their Access Rights:* Queensland Rail should be satisfied that the management of existing Access Rights, or applications for new Access Rights, are made with the consent of the Customer. This will ensure a guaranteed seat at the table with Queensland Rail during all stages of the negotiation of Access Agreements.
- *First right to Contract Access Rights:* Customers should also have the first right to execute replacement Access Agreements in the event that an existing Access Holder defaults and their Access Agreement is terminated due to no fault of the Customer.



→ **West Moreton System reference tariffs**

Queensland Rail proposes to retain the current West Moreton System reference tariffs (as approved in 2010) with a specific reset trigger that requires Queensland Rail to submit a new tariff by 30 June 2013. QRC understands that in the event that Queensland Rail submits (or even if it fails to submit), a new reference tariff by this date, then the QCA has the ability to undertake its own process to develop an appropriate reference tariff (similar to that of a draft amending access undertaking).

QRC's preferred approach is for all West Moreton System tariff issues to be resolved by means of direct engagement between coal producers and Queensland Rail **before** the approval of the replacement access undertaking. Queensland's Rail approach represents a fall-back position in the event that this is unable to be achieved within acceptable timeframes. As such Queensland Rail's approach represents an acceptable approach.

Sufficient time is essential to resolve the various complex matters associated the development and approval of reference tariffs for this system. QRC remains hopeful that ongoing discussions between QRC members, Queensland Rail and the QCA will be able to resolve these matters within a reasonable timeframe. These discussions may include:

- Appropriate rate of return;
- Establishment of a robust Regulatory Asset Base;
- Acceptable depreciation profiles for assets;
- Recognition of past and future capital contributions;
- Pricing/revenue incentives;
- Demand forecasts for pricing; and
- Processes for including new investments.

QRC considers that it is in the interest of the coal industry and Queensland Rail that reference tariffs for coal carrying-train services operating on the West Moreton System are able to be derived based on a robust methodology, repeatable and transparent methodology. Given that QR Network and the QCA failed to agree on a robust approach to determining Western System tariffs since the commencement of rail regulation (as part of the 2001, 2006 and 2010 Access Undertakings), QRC is hopeful that direct discussions between affected parties will achieve the desired price certainty and transparency for coal producers.

→ **System operating assumptions, co-ordination and Capacity Analysis**

A fundamental requirement of any access undertaking should be a transparent approach to determining Capacity and Available Capacity – in this way, Access Seekers and Customers are able to understand the level of contracted capacity and the efficiency of expansions to the network.

Concepts and processes relating to 'Capacity', master planning and system operating assumptions require further consideration. General principles to be discussed include:

- Capacity must be better defined in relation to what factors go to quantifying it. This includes development of an agreed set of system operating assumptions for the supply chain and the expected Operational Constraints that may impact on contract performance.



- An agreed capacity model – any discrepancies in capacity modelling must be resolved in an open and transparent way.
- The process for quantifying Capacity (Capacity Analysis) should be open to independent assessment (subject to appropriate confidentiality arrangements), at the request of any Access Seeker/ Customer or recognised supply chain group.
- Access Holders should be provided with an understanding of the day-to-day operational limitations of the system that impact on contract entitlements being fulfilled.
- Capacity analysis should enable the distinction to be made between Additional Capacity for an individual Customer and for the requirements of the system.

QRC looks forward to further discussions with stakeholders about the best approach to developing system operating assumptions, improving system co-ordination and improving Capacity Analysis.

→ System Master Planning

Customers need supply chain services that combine lowest sustainable costs, reliability and adequacy. Delivering on these needs requires an ability to assess where investments are most cost-effective in terms of creating Additional Capacity or system operational requirements.

Given the features of Queensland Rail's network, transparent and robust supply chain master planning is essential. Master planning should map out clear and transparent process whereby rail expansions and related supply-chain investments can be planned in such a way that rail bottlenecks are understood well ahead of customer demand. Moreover, System Master Planning provides valuable information about operational efficiencies that are constraining the supply chain performance.

System Master Planning for specific supply chains appears to be appropriate approach given Queensland disparate corridors. Queensland Rail's preparation of System Master Plans, no less than annually, could articulate expansion path options.

QRC considers that System Master Planning should set out an expansion path to match contracted capacity as well as providing meaningful information to guide mine-site or unloading investments in order to inform expansion plans or identify other operational improvements. As a minimum, System Master Plans should set out a menu of system projects/initiatives, with details of estimated costs, the likely capacity benefits, associated lead times and the investment triggers that Queensland Rail requires to proceed with each project.

System Master Planning on capacity constrained systems would also provide valuable inform about operational inefficiencies as well as related opportunities to improve performance and throughput. QRC suggests that in the development of a whole of supply chain master plan (the development of which QRC supports); this would promote much greater engagement between all supply chain participants. Indeed, transparent System Master Planning will provide a useful means of highlighting complex interactions with Queensland Rail's passenger network and related Passenger Priority Obligations as well as opportunities for improving decisions of policymakers for path reservation practices.



→ **Duration of the Access Undertaking**

Queensland Rail proposes the Term will be between four and five years from the QCA's actual approval date. The intention is that the terminating date will fall on 30 June.

QRC is mindful that untested access undertakings generally operate for a period of around four years, as such the Term appears appropriate given the nature of the services in question and of the industries it services more generally.

A possible innovation may be the incorporation of a transparent review process to be undertaken jointly by QCA and Queensland Rail at a fixed date, which includes stakeholder consultation. This would provide a means of addressing operational deficiencies within the regime on a proactive basis. QCA could satisfy itself that the review process reflects the interests of all parties and not just of the service provider. This would counter-balance the current QCA Act provisions with respect to lodgement of draft amending access undertakings that asymmetrically favour the monopoly service-provider.

→ **Stations and platforms**

QCA has requested specific comments about the reasonableness of passenger stations and platforms for freight services not being directly covered by the undertaking.

QRC notes that Queensland Rail continues to have a legal obligation to negotiate (QCA Act, s99) and in good faith (QCA Act, s100(1)) with respect this Rail Infrastructure. While QRC is not fundamentally concerned by this proposal we are interested in the views of above-rail operators as to the practical consequences of carving out certain assets of the Declared Service from the undertaking.

A practical alternative could be the QCA is able to develop an Access Undertaking specifically for these assets in the event that the QCA considers that there is a genuine need to obtain access without triggering a formal access determination process.

→ **Clarifying that QCA is the dispute resolution body for Undertaking matters**

QRC considers there is merit in specifically including an upfront reference within the Scope section that recognises any Dispute with respect to the Access Undertaking will be resolved by the QCA (in accordance with Part 6.1 provisions). This would provide clarity to Access Seekers and Customers as to the process to resolve disputes associated with the Access Undertaking.

→ **Publishing of Line Diagrams and Related Operational Information**

Queensland Rails' proposal to publish updated key documents (such as network line diagrams and other operational publications) on its website is supported. However, QRC is interested in how Customers and Access Seekers will be informed about changes to these publications and what is the appropriate means of challenging inappropriate amendments.



→ Extensions – User Funding Arrangements

QRC supports Queensland Rail having a clear obligation to **facilitate** Extensions to its network – this **does not** include a specific obligation to invest in the expansion of the network. However, QRC does support an obligation for Queensland Rail to invest in order to maintain the network.

The current drafting outlined in section 1.4 Extensions requires substantial improvement, and should be considered as an initial working draft developed by Queensland Rail. Numerous features will require amendment and/or further discussion as they appear unnecessarily restricting, rather than facilitating Extensions to its network. For example:

- Queensland Rail will only construct Extensions if:
 - An **Access Seeker** provides the funding (clause 1.4.1(iii)(A)) – the source of the funding should not be limited solely to the Access Seeker (consideration should be given to the extending this to the Customer or their Agent);
 - Queensland Rail bears no **risk** (clause 1.4.1(iii)(B)) – this is beyond the QCA Act provisions for Access Determinations that solely refer to cost.
 - Queensland Rail bears no costs for **owning, operating or managing** the Extension (clause 1.4.1(iii)(B)) – this is beyond the QCA Act provisions for Access Determination requirements about extending a facility.
 - Access Seeker has obtained the necessary rights and interest or land or any thing that in Queensland Rail's **opinion** are necessary to construct, **own or operate and manage** the Extension **on terms satisfactory to Queensland Rail** (clause 1.4.1(iii)(D)) – there needs to a reasonable approach to addressing such requirements.
 - In Queensland Rail's **opinion (in its absolute discretion)** the extension satisfies a range of criteria (clause 1.4.1(iv)) – this clause operates effectively as an absolute right of veto over Extensions to Queensland Rail.
 - Access Agreements have been executed on **terms and conditions satisfactory to Queensland Rail** (clause 1.4.1(v)) – terms and conditions should reasonable.

QRC's preferred approach to progress User Funding Arrangements (UFA) within Queensland Rail's Access Undertaking includes:

- A set of high-level principles to guide the development of any UFA negotiation – such that the UFA must be tax effective and structured efficiently to meet the needs of User Funders. Also that a UFA Extension must not impose any material cost on Queensland Rail to which it is not compensated for. QRC will engage with Queensland Rail and the QCA in order to develop a these principles.
- QCA having the right within the Access Undertaking to require Queensland Rail to submit a detailed set of UFA (including the necessary standard agreements) for the QCA's approval. QCA should also have the right to develop a detailed UFA; if Queensland Rail's is not submitted or is rejected by the QCA.

QRC does not support the mandatory development of a UFA to be included in the Access Undertaking. The need to develop a UFA should only be triggered under specific circumstances – for example, after the QCA receives a dispute with respect to UFA principles.



→ **Absence of “Access Conditions”**

Queensland Rail has not proposed any provisions relating to the imposition or operation of Access Conditions within its proposed replacement Access Undertaking. Queensland Rail should be permitted to impose Access Conditions to offset the risk that it will cease to collect Access Charges for infrastructure before it has fully recovered the cost of that infrastructure.

However, a key concern for QRC is that equitable and efficient arrangements apply when a new user is required to underwrite all the incremental costs of an increase in system capacity where this capacity is subsequently shared across a number of other users. With this in mind, QRC considers that there is merit including provisions within the Access Undertaking regarding the treatment of rebates to ensure that Queensland Rail does not recover more than the value of the funded asset (by means of the operation of the rebates).

→ **Resumption of Access Rights – Standard Access Agreement (clause 19.1)**

Queensland Rail has proposed resumption provisions for coal carrying train services operating on the West Moreton System to trigger if more than seven services fail to operate, out of any twelve (this excludes Force Majeure Events and failure of Queensland Rail to make the network available). Following the resumption trigger being satisfied, then Queensland Rail is able, at its discretion, to issue a notice to commence deleting train paths from an Operators train service entitlement.

Capacity resumption provisions should permit Queensland Rail to resume some, or all, of an existing Access Holder's capacity when the Access Holder consistently under-utilises its allocated capacity at an unacceptable level. However, the proposed resumption trigger appears to be developed for general freight services rather than for mining projects that have a higher level of production variability – which directly impacts on the ability to rail on a more consistent basis. By way of example, QR Network's 2010 Access Undertaking provides a resumption trigger for cyclical coal carrying train services for failure to operate over 85% of services (excluding Force Majeure and the failure of QR Network to make the Access Holder's Access Rights).

QRC considers that a better trigger test is required that achieves a balance between reasonable mine production variability and ensuring that Access Holders utilise contracted network capacity entitlements.

→ **Negotiation Cessation Notice - Payment of Queensland Rail's costs (Clause 2.6.3(c))**

Queensland Rail proposes that it is entitled to request the reasonable costs incurred during negotiations with an Access Seeker following a Negotiation Cessation Notice being provided. Under this approach, it is important that the Access Seeker is aware of the expected costs to be incurred, the amount incurred during the negotiation period, and that any costs to be recovered are incremental. Overall, the approach taken should reflect a balance the intensity of the Access Application process on Queensland Rail and how the negotiation process places unnecessary burden on Queensland Rail – given Access is its core business.



→ **Capacity Allocation – Competing Applications**

Queensland Rail has proposed criteria to decide as between competing Access Applications in order to determine the most favourable commercial outcome for Queensland Rail. This approach is a departure from the current queue-based approach to a principles-based approach to allocate capacity.

QRC notes that appropriate right of renewal arrangements are necessary to ensure that contracted capacity rights are not inefficiently subject to periodic capacity allocation processes, which put at risk investment in long-term mine developments.

The objective of any capacity allocation process is to provide Access Seekers with certainty regarding the process and criteria for the allocation of capacity. This is particularly important where there are competing applications for capacity. QRC considers that for all Access Seekers to be treated fairly, the processes and criteria need to be clear and transparent.

Further discussion is required to ensure whatever the approach undertaken that it balances providing certainty to Access Seekers, recognizes the legitimate business interests of Queensland Rail, and generates good efficient outcomes.

→ **Development of Standard Access Agreements to assist the negotiation process**

The development of workable contractual frameworks that promote choice and greater flexibility are supported by QRC's members. This includes the development of contracting arrangements that provide a Customer with the genuine option to directly contract with Queensland Rail for Access Rights. A number of QRC member companies have expressed a desire to hold Access Rights directly and industry notes that the QCA has, in previous regulatory reviews, developed standard Access Holder agreements and is currently considering a new contracting framework that removes Customers being exposed to liabilities and obligations relating to the operation of trains.

QRC supports Queensland Rail developing Standard Access Agreements to apply to assist negotiations for particular supply chains. For example, there is merit in the development of such a standard agreement for Queensland Rail's Mount Isa Line. This will ensure that access negotiations are targeted towards commercial issues of specific traffics, rather than trying to make a coal standard agreement the template for *all* negotiations.

→ **Proposed Standard Access Agreement requires a better balance**

As a general comment, there are a number of provisions within the proposed Standard Access Agreement which require reconsideration by Queensland Rail. For example, the proposed liability and indemnity positions as well as the maintenance obligations are not appropriately balanced in their current form (refer to clauses 10.2, 11.1, 11.3 and 5.1).

Conclusion

QRC considers that a certain level of prescription is required to guide the appropriate operation of a light-handed access regime. In a number of key areas Queensland Rail needs to provide greater detail to ensure an efficient negotiation framework.