

Submission on the Draft Decision on the Queensland Rail 2015 Draft Access Undertaking

1 Background

Glencore's copper, zinc and lead businesses are one of the largest end users by volume of the Queensland Rail (**QR**) network on the Mount Isa – Townsville line (the **Mount Isa line**).

Glencore made submissions to the Queensland Competition Authority (**QCA**) in respect of the QR 2015 Draft Access Undertaking (**2015 DAU**) in June 2015 and again in December 2015 in response to the QCA's draft decision of October 2015 (**Draft Decision**).

This further submission responds to the issues highlighted in the QCA's further Request for Comments Paper of 19 January 2016 which are relevant to Glencore and to some additional issues raised in other stakeholders' December 2015 submissions. It should be read in conjunction with Glencore's previous submissions on the 2015 DAU.

2 Responses to Request for Comments Paper

Pricing for the Mount Isa line is individually negotiated by each user. Glencore has, in previous submissions, raised major concerns about the lack of transparency in relation to QR's pricing, and the excessively high prices (and unbalanced terms) that QR is able to achieve due to a number of factors, including monopoly power, a ceiling limit that cannot realistically be calculated and the likely prolonged duration of an access dispute challenging proposed pricing or other terms. The appropriate approach to pricing for non-reference services should be considered in that context.

2.1 Take or pay (Request for Comments Paper, page 3)

The QCA's proposal in the Draft Decision not to determine a cap on the proportion of charges for non-reference train services that should be take or pay effectively approves QR insisting on 100% take or pay arrangements. The reasons that is not appropriate are set out in Glencore's December 2015 submission.¹ To prevent over-recovery by QR, take or pay should be capped at the long run proportion of costs which are truly fixed in nature. This is critical given the market conditions currently faced by resources users. Insistence by QR on excessive take or pay during a period of volatile market conditions has the potential to result in significant under-contracting by resources users, who may subsequently be required to seek ad hoc services. That would be anticipated to give rise to:

- (a) real difficulties for QR in relation to issues like planning future maintenance and capital investments in the network, and in determining appropriate pricing; and
- (b) inefficient decisions regarding the operation, use of and investment in QR's network, contrary to the object of the Part 5 of the *Queensland Competition Authority Act 1997* (Qld) (**QCA Act**).

2.2 Pricing principles and renewal rights (Request for Comments Paper, page 4)

There are two principal issues in relation to renewal rights for non-reference tariff services:

- (a) the unduly narrow circumstances in which QR proposes renewal rights should exist; and
- (b) the price for future access following exercise of a renewal right.²

¹ See section 3.2 of Glencore's December 2015 submission.

² See sections 3.1 and 4.2 of Glencore's December 2015 submission.

Circumstances in which renewal rights should exist

Glencore acknowledges that clause 2.9.3(b) of the 2015 DAU is intended to provide a degree of protection for bulk mineral services (which it continues to strongly support). However, as noted in Glencore's December 2015 submission, those protections remain inadequate for Access Holders with substantial sunk costs in mining and processing operations.³ In particular:

- (a) **Definition of 'Renewal':** 'Renewal' is defined to be limited to a renewal of access rights that are 'equivalent to the relevant Access Holder's Access Rights immediately prior to their expiry (including with the same destination and origin)'. An existing Access Holder that wishes to renew an access agreement has no flexibility for even small changes in volume, train service description or origin (eg, changing from Cloncurry to Mount Isa). In the current commercial context where users, such as Glencore, face significant uncertainty in relation to the commodity volumes for which they may require access to QR's rail network beyond the term of existing access agreements, those restrictions are unworkable.
- (b) **Renewals for intermodal services:** As outlined in Glencore's June and December 2015 submissions, renewal rights need to extend to intermodal services, at least to the extent they support bulk minerals services (as they do on the Mount Isa line) where the same issues regarding sunk costs, asset stranding and lack of alternatives exist.

Pricing for renewals (and Mount Isa line pricing generally)

Glencore continues to have the significant concerns regarding the QCA's proposals for regulation of QR's pricing in respect of renewals for non-reference services that were canvassed in Glencore's December 2015 submission, principally due to the outcome of locking in an unknown opaque methodology that reflects QR's market power.⁴ The combination of the increased information disclosure requirements, a cap on pricing and the ability to bring an access dispute where necessary (proposed by Glencore in its December 2015 submission) would result in a better informed negotiation and a swifter resolution by arbitration on future pricing issues.

That would be an improvement, and may be all that is achievable for the term of this undertaking, but Glencore considers the QCA should also be ensuring this undertaking provides for the disclosure of information required to properly determine whether a reference tariff for the Mount Isa line is appropriate as part of the subsequent undertaking. To achieve that objective, QR should be required to report to the QCA, access holders and end users for each year of this undertaking in relation to the Mount Isa line (including dividing the data by type of services, e.g. bulk minerals, intermodal, agricultural freight or passenger) each of the following:

- (a) QR's view on the asset base for the Mount Isa line and the methodology used to determine that;
- (b) the weighted average rate of return QR is using to calculate the return on investment it is seeking in respect of Mount Isa line access;
- (c) aggregate capital expenditure in a year (and the scope of the projects delivered);
- (d) aggregate maintenance costs in a year (and the scope of maintenance projects delivered);
- (e) aggregate operating costs in a year;
- (f) aggregate access revenue for the year;

³ See sections 4.1 and 4.2 of Glencore's December 2015 submission.

⁴ See section 3.1 of Glencore's December 2015 submission.

- (g) aggregate volumes of contracted services and services actually operated;
- (h) aggregate contracted and forecast volumes over the next 10 years (updating on a rolling basis); and
- (i) any other information the QCA would want in order to calculate a Mount Isa line reference tariff.

If these sort of requirements are not included now, then it is hard to escape the conclusion that at the time the subsequent undertaking is being considered end users and the QCA will be back in the same position of acknowledging the current arrangements are not appropriate, but not being able to assess what an appropriate reference tariff would be.

2.3 Standard Access Agreement (Request for Comments Paper, page 4)

As a general proposition, Glencore considers that optimal risk allocation in the Standard Access Agreement would involve risks being borne by the party that is best able to control or mitigate the adverse outcomes of them. Each of the issues raised in the Request for Comments paper and other provisions of the Standard Access Agreement should be considered on that basis.

- (a) **Varying the standard terms of access:** Glencore supports QR being required to substantiate why a request for access cannot be achieved through altering the terms of the standard access agreement and requirements to negotiate in good faith regarding productivity improvements raised by the Access Holder and end user.
- (b) **Allowable threshold:** there is no basis for QR to seek inclusion of a 10% threshold in respect of liability for non-provision of access. QR must be incentivised to manage the service it provides effectively and efficiently, including bearing the liability for non-provision of access (given that it is best placed to manage any relevant risks).⁵
- (c) **Indemnity and liability regimes:** Glencore is willing to accept the re-balanced indemnity and liability position reflected in the QCA's Draft Decision. While Glencore considers this position does not go far enough, and still leaves QR with limited real risk (in a way that is not reflected in the pricing of at least non-reference services), it is clearly more appropriate than the significantly one-sided positions proposed by QR.
- (d) **Operational efficiencies (and relinquishment fees):** Glencore strongly supports the proposal that where an operator is seeking to implement operational efficiencies, the relinquishment fees associated with a variance to train service entitlements and rolling stock configurations should be capped at the variation to access revenue arising from that change. That concept should also be extended to changes to train service entitlements more generally (such as changes in origin or destination within the same system, or changes for operational efficiencies sought by the end user). Given the 'lumpy' nature of contracting services on the Mount Isa line, Glencore also considers that relinquishment fees should be refunded for any subsequent use of relinquished paths, not just those recontracted within the 6 months immediately following relinquishment.
- (e) **Ad hoc services:** Services that are ordered on an ad hoc basis should be counted toward an Access Holder's take or pay requirement. However, given their nature as a service that will only operate if there is sufficient spare capacity, they should not attract take or pay obligations when they are not ultimately operated. Any new clause regarding Ad Hoc Train Services needs to be consistent with that approach (which QR's provision appears not to be).

⁵ See section 5.2 of Glencore's December 2015 submission.

3 Other Critical Issues Raised in QR's December Submissions

3.1 Pricing principles

Glencore supports the QCA's treatment of the hierarchy of pricing principles and the QCA's positions on pricing differentiation for non-reference services, pricing limits and not prescribing a particular asset valuation methodology. Given the extremely limited nature of the information QR has been willing to provide about how it determines pricing for non-reference services and the difficulties Glencore has encountered in the past in relation to negotiating pricing on the Mount Isa line, these positions should be being strengthened (not watered down as QR proposes in its December 2015 submissions).⁶ The renewal pricing provisions are not sufficient to provide reasonable oversight of QR's pricing as by their nature they only apply to 'Renewals' (and, however that is defined, the general pricing principles are required for new Access Seekers).

3.2 Investment framework

The amendments to the 2015 DAU required by the QCA alleviate, to some extent, Glencore's concerns regarding the framework for negotiation of a network extension.⁷ However, the drafting of clause 1.4.2 and Schedule I still fall short of providing certainty regarding the circumstances in which Glencore (or another user) can require an extension. Schedule I gives QR a significant amount of discretion and far too much scope for QR to frustrate Access Seekers that need to progress an extension of QR's network and/or to provide user funding for such an extension. For non-reference services this can be a material issue, as delay provides the opportunity to seek a higher price for access. Schedule I should require mandatory investment in appropriate circumstances, with the criteria to be satisfied being objective in nature.

3.3 Network planning

Glencore strongly supports the QCA's approach to network planning. Too often in previous access negotiations with QR, Glencore has been led to believe the pricing offered was based on a particular scope of maintenance and capital works, which subsequently did not appear to be implemented within the term of the relevant agreement. Glencore is hopeful that clear network planning (such as that proposed by the QCA) will, in time, allow for better informed access negotiations and swifter resolution of any access disputes about pricing issues. QR has provided no evidence for its assertion that regulating network planning is beyond the QCA's powers, and there is no basis in the QCA Act for that assertion.

3.4 Standard Access Agreement

Glencore is supportive of the QCA's approach to the standard access agreement.⁸ In addition to the comments provided in section 2 above, Glencore particularly notes its strong support for:

- (a) a contracting structure under which users directly hold access rights, given the difficulties Glencore experienced with negotiating such an arrangement with QR in the past;
- (b) the inclusion of provisions in relation to a KPI regime (although it would strongly prefer real financial incentives to incentivise QR's performance);
- (c) strengthened maintenance obligations, given previous experiences with the level of maintenance on the Mount Isa line and claims by QR that it then needs to raise prices to

⁶ See section 6.1 of Glencore's December 2015 submission.

⁷ See section 7 of Glencore's December 2015 submission.

⁸ See section 5 of Glencore's December 2015 submissions.

fund capital projects (noting that section 119 of the QCA Act has no relevance to the terms of either a standard access agreement or an access undertaking);

- (d) restrictions on amendments to the Operating Requirements Manual, given that those changes can fundamentally alter the Access Holder's and end user's ability to utilise the access rights in the manner intended at the time of contracting (and noting QR's objection to paying reasonable compensation for additional costs caused by such changes); and
- (e) the inclusion of force majeure in the 'Queensland Rail Cause', given the experience of QR's frequent claims for force majeure in respect of the Mount Isa line.

4 Conclusions

As indicated in this and the December 2015 submission, Glencore is generally supportive of the Draft Decision and strongly supports the QCA's proposed decision to refuse to approve the 2015 DAU. In order for the 2015 DAU to be in an appropriate form to be approved by the QCA, in addition to the changes proposed in the Draft Decision, the QCA will need to:

- (a) introduce greater flexibility in relation to the requirement to qualify as a 'Renewal';
- (b) increase the rigour of the renewal pricing regime, so that it is not such a direct adoption of the existing methodologies;
- (c) prescribe a cap on the proportion of charges which can be take or pay for non-reference services;
- (d) refine aspects of the Standard Access Agreement;
- (e) increase the level of disclosure to Access Seekers required in access negotiations; and
- (f) increase the robustness of the investment framework.

Glencore looks forward to these points being duly considered by the QCA in the preparation of its final decision on the 2015 DAU.