BMA
BHP Billiton Mitsubishi Alliance

05 February 2015

Dr Malcolm Roberts
Chairman
Queensland Competition Authority
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Dear Malcolm,

Proposed New Reference Tariffs for train services to Wiggins Island Coal Export Terminal

BHP Billiton Mitsubishi Alliance (BMA) welcomes the opportunity to provide a submission on Aurizon Network's proposed new reference tariffs for train services to Wiggins Island Coal Export Terminal (WICET). Aurizon Network in its pricing proposal on new reference tariffs for WICET is proposing to socialise the Wiggins Island Rail Project (WIRP) infrastructure within the Blackwater and Moura systems. This submission should be read with BMA's earlier submissions made in response to Aurizon Network's August 2014 Draft Access Undertaking.

BMA would like to take this opportunity to highlight some principles that should be considered when assessing Aurizon Network's proposal. BMA's view is that pricing for train services to WICET should:

- be based on efficient and prudent costs;
- be based on realistic volume forecasts;
- ensure that there is no cross subsidisation between users;
- not commercially disadvantage existing users; and
- not increase commercial uncertainty for existing users through increases in either tariffs or take or pay liability.

As noted in BMA's earlier submissions, BMA reiterates the fundamental principle that existing customers must not bear any of the commercial risk or cost associated with expansions of the network that, if included in the existing pricing of the coal system, would result in the reference tariffs increasing for existing customers. BMA's view is that non-expanding customers should not bear:

- any additional costs if they do not receive any clear and significant financial or operational benefit by way of increased system throughput at efficient costs or if they are not involved in the negotiation of the expansion project; or
- any default or asset stranding risk of an expansion project commercially negotiated between Aurizon Network and expanding users.

BMA is of the view that any pricing proposal should not allow socialisation of risk arising from an expansion project (irrespective of the funding source) with existing users either directly through the pricing principles or indirectly through the capital expenditure approval process for expansions or duplications. This is particularly important in the case of WICET as the Aurizon Network has been compensated for risk through access conditions or above regulatory rates of return approved by the Queensland Competition Authority (QCA).

Network upgrades - planning and reliability

BMA, as an existing Blackwater system customer, believes that socialisation of tariffs should not be used as a means of passing on asset stranding risk to existing customers while securing additional returns on WIRP through the WICET access conditions. Aurizon Network has claimed that the Blackwater duplications were previously endorsed by existing Blackwater system customers through the 2008 Coal Rail Infrastructure Master Plan (CRIMP) process. BMA however notes that Aurizon Network has subsequently demonstrated that these duplications were not required in the absence of WICET expansion. Aurizon Network then secured above regulated rate of return on these assets through QCA approved access conditions. BMA is concerned that there appears to be inconsistency in Aurizon Network's assessment of capacity and associated upgrades required for meeting additional demand. This is concerning as it raises a question on the robustness and reliability of Aurizon Network's capacity and network planning.

Operational efficiency

Aurizon Network in its submission claims that 94% of the capital value of WIRP relates to multiuser infrastructure and that 70% of the capital value of WIRP related infrastructure will be utilised by non-WIRP customers in the Blackwater and Moura systems delivering considerable operational efficiencies. Most of the WIRP project relates to duplication or upgrades to existing rail infrastructure to cater for an additional 27 million tonnes per annum which will provide additional flexibility and operational efficiency. However, it raises the question as to whether all of the associated upgrades and duplications were efficient and essential to deliver supply chain efficiency. Whilst operational efficiency will be delivered to all users, the majority of the capital spent was to support WICET throughput.

Capital costs

Capital cost should be allocated to systems and users in proportion to the benefit received. There is no clear and transparent process regarding allocation of capital cost between systems and between expanding and non-expanding users that form the basis for reference tariffs. The Goonyella to Abbot Point Expansion (GAPE) and WICET projects clearly demonstrate the need for the 2014 Draft Access Undertaking to have a clear framework for the allocation of capital cost and the associated pricing to support future development. BMA believes that here should be complete transparency with regard to economic benefits arising as a result of any expansion between expanding and non-expanding users, or between coal systems, and the corresponding allocation of cost. As a matter of principal, the regulatory system should not incentivise a regulated entity to earn a regulated rate of return as well as a commercial return on its capital costs.

Forecast volumes

Aurizon Network's proposal is based on a volume forecast developed by John T Boyd Company as part of the WICET Stage 1 development. BMA understands that this forecast was based on mine production plans at the time of WICET Stage 1 development. BMA now has concerns regarding the validity of these volumes and believes that the QCA should have regard to the current forecasts in assessing pricing for train services to WICET consistent with its approach to adopting volume forecasts vis-à-vis other coal systems in the Central Queensland Coal Network (CQCN).

The volume forecast used for pricing has important implications in terms of triggering take or pay obligations for customers. It is also important to note that since the release of the volume forecast report the commercial circumstances of some of the users have changed. This could potentially alter the risk profile of existing users in regards to take or pay liability and it is BMA's view that variance between forecast and actual volumes should not alter liabilities for existing customers.

Summary

As an existing Blackwater system customer BMA is concerned that the socialisation of WIRP costs and prices with the existing Blackwater and Moura system could be used as a means for Aurizon Network to pass on its asset stranding, credit or volume risks to existing customers. This is important given that Aurizon Network has already been compensated for any additional risk that could have eventuated by the development of WICET project through the QCA approved access conditions.

This submission only identifies some of BMA's key concerns in relation to Aurizon Network's proposed new reference tariffs for train services to WICET. BMA is relying on the QCA for a comprehensive review of Aurizon Network's proposal and the pricing model and the underlying assumptions as it is difficult for users to assess the impact of Aurizon Network's proposal in the absence of a detailed pricing model.

If you have any queries or require further information, please feel free to contact Ruchi Gupta on 07 3239 2348.

Yours Sincerely,

Gary Dyer

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