GLENCORE

8 July 2016

The Board
Queensland Competition Authority
Level 27, 145 Ann Street
GPO Box 2257
Brisbane QLD 4001
Australia

Dear Sirs

**DBCTM – Draft Decision in relation to 2015 Draft Access Undertaking**

I am writing in connection with the Draft Decision. Glencore has participated in the DBCT User Group and is supportive of the submissions made by the DBCT User Group. However, there are three matters on which we wish to make individual submissions, as set out in this letter.

**Definition of Capital Expenditure**

The Draft Access Undertaking envisages that the QCA should have the right to approve expansionary and non-expansionary Capital Expenditure for inclusion in the Regulated Asset Base. The definition set out in the Draft Access Undertaking is as follows:

> "**Capital Expenditure** means expenditure (incurred by DBCT Management) which:
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> (a) relates to replacement or expansion of any part of the Terminal;
>
> (b) relates to refurbishment or upgrade of any part of the Terminal which can reasonably be expected to extend the life of the relevant part beyond its original useful life or is undertaken for environmental or safety reasons;
>
> (c) otherwise relates to the refurbishment or upgrade of Terminal plant and/or infrastructure which is reasonably expected to improve whole of life cost, or is incurred with the agreement of the Operator; or
>
> (d) is ancillary or incidental to paragraphs (a), (b) or (c)."

Glencore is concerned that the breadth of the definition above is such that DBCTM has an overly broad discretion to include items in its claims for "Capital Expenses" which are not appropriate classified as capital expenditure. This produces opportunities for gaming of the treatment of expenditure depending on the prevailing economic circumstances and reduces transparency and certainty of decision making. An inappropriate characterization might result in the QCA being obliged to include in the Regulated Asset Base items which are more properly identified as operating expenses. Therefore, we would suggest that

the first part of the definition to read as follows:

> "means expenditure (incurred by DBCT Management) which (x) is classified as capital expenditure according to generally accepted accounting principles and (y) creates or contributes to an enduring asset; and which"

We do not believe that it is appropriate for expenditure more appropriately classified as operating expenditure to be included in the definition of "Capital Expenditure" or to be eligible for inclusion in the Regulated Asset Base. We believe that the change sought would create greater regulatory certainty and transparency, without imposing any overly onerous requirements on DBCTM.

**Cost of finance during construction**

Our understanding is that the QCA has a practice of approving financing costs during construction projects, both in the case of expansionary and non-expansionary projects, in addition to applying a WACC rate to these costs. This practice is not documented in any detail in the Access Undertaking, although in the case of expansionary projects reference is made to finance costs being approved as "Other Costs" in addition to the applicable WACC rate. The Access Undertaking provides for specific WACC rates to apply during expansionary projects, but in the case of non-expansionary capital we understand that in practice the normal regulatory WACC for the relevant period is applied.

We do not believe there is any justification for applying an additional financing cost during construction projects in addition to the normal regulatory WACC (or in the case of expansion projects the differential WACC rates specified by the Access Undertaking). The WACC already specifically incorporates an allowance for debt raising costs. The corporate overheads that DBCTM is permitted to earn are based on the notional costs for a listed company, which therefore implicitly include the costs involved in raising equity since a listed company is able to raise equity through issue of new shares. For expansionary projects, the additional risk inherent in such projects can be recognised through the differential WACC rates. For non-expansionary projects, which are an essential component of the operation of the regulated business, there can be no justification for the application of a WACC rate which is anything other than the normal regulated WACC rate. Any allowance of finance costs above and beyond the applicable WACC in respect of any construction project represents a windfall gain for DBCTM which is without any appropriate justification.

Given that this matter is not addressed in any detail in the Access Undertaking, we consider that it would be sufficient for the QCA's decision to set out its policy on such matters which will be applied during the period of the Access Undertaking. We believe that the appropriate policy would be for DBCTM only to be permitted to earn the relevant WACC on its capital expenditure during construction periods. This would be consistent with the approach in other regulatory regimes.

**Socialisation of user default**

DBCTM has sought a change to the definition of "Notional Contracted Tonnage" which would have the effect of socialising the risk of early termination of user agreements. While Glencore notes that this is a change from the previously applicable definition, we do not see any reason in principle why expiring contracts should necessarily be treated differently from contracts which are terminated by reason of default. However, we do wish to make some further points in relation to this proposal, as well as agreeing with the bulk of the submissions made by the DBCT User Group in relation to this matter.

As identified by the DBCT User Group, this change results in a diminution in the risks faced by DBCTM. In our view, the nature of the DBCTM business is such that the risk faced by DBCTM is largely determined by the content of the regulated regime to which it is subject. That being the case, any significant change to

the risk allocation in the regulatory arrangements should be carefully considered to determine whether it should be reflected in a change to the regulatory WACC parameters.

The ability for DBCTM to socialise the risk of default among remaining users also substantially reduces any justification for DBCTM to be able to insist on any security being provided by users of the terminal. Default by a user can be addressed by termination of their user agreement and socialisation of the required revenue over fewer tonnes. There is therefore very little continuing justification for any security to be demanded from terminal users – the only limited justification there would be is to cover charges which would be due in the minimum possible period between the user default and the application of termination (and hence socialization).

Finally, Glencore would not accept that socialisation should be applied at any point prior to the termination of the relevant user agreement. The decision to terminate or not terminate any user agreement rests with DBCTM and therefore the risks associated with such decision should also be borne by DBCTM. If DBCTM is able to socialise any revenue risks prior to the termination of the user agreement it is difficult to see why DBCTM would ever actually terminate a user agreement since it would not be exposed to the costs of leaving it in place.

Yours faithfully

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