



Resourcing Queensland's future

28 February 2018

Mr Linus Power, MP
Chair, Economics and Governance Committee
Parliament House
George Street
BRISBANE QLD 4000
Email: c/o Committee Secretary egc@parliament.qld.gov.au

Dear Committee Chair

Thank you for the opportunity to comment on the *Queensland Competition Authority Amendment Bill 2018* (the Bill). QRC fully supports the objectives of the Bill, particularly to "ensure Queensland's regime continues to be easily understood and addresses the economic problem of natural monopoly in markets for infrastructure services."

The Queensland Resources Council (QRC) is the peak representative organisation of the Queensland minerals and energy sector. QRC's membership encompasses exploration, production, and processing companies, energy production and associated service companies. The QRC works on behalf of members to ensure Queensland's resources are developed profitably and competitively, in a socially and environmentally sustainable way.

Recommendation

QRC supports the policy objective of providing regulatory certainty, as outlined in the Explanatory Notes. QRC recommends that the Bill should be expanded to include an extension of the declaration of the Aurizon Network Pty Ltd (Aurizon Network) Central Queensland coal rail network (Rail Network Services), which is due to expire on 8 September 2020. QRC submits that such a declaration should be indefinite, but an extension of at least 10 years is immediately necessary.

Context

As the peak industry body for Queensland's mining and energy industries, QRC has taken a keen interest in the review of the legislation underpinning the Queensland Competition Authority (QCA). The QCA plays an essential role in managing the adverse consequences of monopoly excess which could effectively undermine the global competitiveness of Queensland's resource industries.

QRC supports the QCA's role, and considers that the QCA has been instrumental in improving the efficiency of Queensland's coal supply chain and opening the path to above rail competition. QRC supports improvements to the QCA's statutory framework, to provide it with the tools and clear powers required to properly and efficiently regulate monopoly infrastructure providers.

All stakeholders were frustrated by the time taken to approve the fourth rail access undertaking for Aurizon Network's central Queensland coal network. That undertaking has now been extended due to delays in the development of the fifth undertaking. The causes of these delays have been:

- Aurizon Network's late submission of the initial draft of the fourth undertaking (provided shortly before the scheduled expiry of the third undertaking);
- Aurizon Network's ambit claims across financial and non-financial elements of these undertakings, which lead to draft undertakings not being approved;
- The need for QCA to seek additional information from Aurizon Network in order to assess unsubstantiated claims; and
- Aurizon Network's claims regarding limitations of the QCA's powers (claims with which QRC disagrees).

The effective administration of competition policy is of critical importance to Queensland's resources sector. Industry relies on essential multi-user infrastructure services such as rail, ports and water which are monopoly businesses. Effective regulation of this monopoly power is necessary to enable the resources sector to realise its potential for growth and contribution to the State's economy.

The QCA's experience of developing coal access regimes for port and rail have provided the QCA with a valuable understanding of how natural monopolies plan, manage and operate key links in the Queensland coal supply chain. The QCA's practical knowledge and capacity to provide an accurate appraisal of Queensland's monopoly operations is a crucial part of the state's economic framework and QRC would be loath to see the value of these hard-won insights dissipated or diluted.

The experience of individual QRC member's 'commercial' negotiations with regulated service providers highlight the lack of alignment with the interests of developing the State's natural resources – in that they seek to extract monopoly rents from resource companies rather than maximise the efficiency of the supply chain or facilitate industry development. The commercial reality of dealing with a monopoly is that the discussions are inherently skewed. Information is asymmetric and there is a lack of viable alternatives to provide a countervailing check on pricing, efficiency and service standards.

QRC members rely on the QCA to independently assess the claims of these natural monopolies and to thoroughly scrutinise how capital is allocated to maintenance and operations of these businesses in determining a fair, transparent and efficient pricing regime.

QRC members are also members of the Dalrymple Bay Coal Terminal (DBCT) User Group, and QRC supports the submission made by that user group, including that the Bill be amended to include an extension to the declaration of the coal handling services at Dalrymple Bay Coal Terminal.

Central Queensland Coal Network

The Rail Network Services were designed, developed and operated by the Queensland Government as a multi-user facility prior to the privatisation of QR National Limited (now Aurizon Holdings Limited). Declaration of the Rail Network Services was appropriate in that context and has resulted in fair access to (and the efficient operation of) what is the critical piece of economic infrastructure for the coal industry. This has sustained

investment in Queensland coal mines, led to significant employment opportunities and substantially boosted Queensland's overall economic performance.

Notably in 2016-17 the coal industry produced \$3.376 billion in royalties, paid \$2.7 billion in wages to 21,200 full time employees and made more than \$11 billion in purchases from over 8,500 local businesses. When the indirect benefits to the Queensland economy are tallied up, Queensland's coal industry contributed \$37.8 billion to the gross state product or 12% of the state economy.

Distracting review process

Under the Queensland Competition Authority Act, the QCA will soon be forced to undertake a process to consider whether the Rail Network Services should remain declared. That arises because at the time of floating Aurizon the government of the day declared the Rail Network Services for 10 years only. At that time, no one, including government or the coal industry, seriously contemplated a circumstance in which such a significant piece of public-use infrastructure such as the Rail Network Services would not be declared.

The declaration review process which the QCA is required to follow will be lengthy. It will require significant submissions and representations from economic, engineering and legal advisers. The costs of participating in such a process will be significant. The effort required to participate will be distracting. The review process is creating investment uncertainty in the mining industry that will only become greater, affecting regional growth, the Queensland economy and employment opportunities.

We note that extending the declaration date would not affect Aurizon Network's existing ability to challenge the declaration at any time. It is perhaps tacit recognition of their status as a natural monopoly that Aurizon Network has never sought to exercise this right.

Importance of regulation.

The Rail Network Services are a monopoly. There is no economic alternative to transport coal from a mine to an export port or a domestic point of sale (such as a power station). The amount of below rail access that a mine has dictates port access.

The declaration and associated access undertaking provides a fair framework for access to the Rail Network Services and a fair price for access. Without regulation of the Rail Network Services:

- There would be no regime to negotiate access;
- There would be no framework to determine price and below rail charges will significantly increase;
- Expansions of the Rail Network Services would only be undertaken on Aurizon Network's terms, such that only a few mine expansions would be commercially feasible;
- Port selection could be dictated by Aurizon Network; and
- There would be no check or supervision of Aurizon Network's monopoly power.

Without a declaration, competition in the above rail market would also be severely impaired or would cease. Aurizon is a vertically integrated business. The existing access undertaking includes protections against conflicts of interest. Those protections are essential to establishing a level playing field for obtaining access to below rail services

and ensuring fair terms of that access. Without those protections, Aurizon Network could freely use its monopoly power to favour customers that use Aurizon's own above rail business (Aurizon Operations Limited) or could deny access to other rail operators, extending the monopoly to the above-rail market.

Aurizon Network's recent behaviour

Since its privatisation, Aurizon Network has at each turn sought to maximise its commercial interests. The QCA's regulatory decisions are littered with examples of Aurizon Network over-reaching. The experience during the approval process for access undertaking number 4 (UT4) is a perfect example of this. Aurizon Network's approach to UT4 (which was unbalanced and uncommercial) resulted in an approval process which cost industry tens of millions of dollars and took more than three years to complete. Another example is Aurizon Network's submissions in respect of more than seven years work on the Standard User Funding Agreement (SUFA), and particularly Aurizon Network's recent decision to withdraw SUFA after receiving an unfavourable QCA final decision.

Aurizon Network's recent behaviour in response to the QCA's draft decision on access undertaking number 5 is also particularly instructive. Aurizon Network has advised customers of the rail services of its intention to implement a range of operating practice and business decisions which will degrade supply chain performance.

In emails to coal producers and rail haulage operators dated 30 January 2018 and 12 February 2018, Aurizon Network advised that the Draft Decision "prescribes that Aurizon Network uses certain maintenance and operating practices". Aurizon Network goes on to say that "the net result of the QCA's draft decision, if implemented, would be a degradation of supply chain performance" and the "net impact of initial changes" will be 20 million tonnes per annum, with an expectation of "further significant impact to throughput". Similar commentary is reflected in Aurizon Holdings Limited's ASX announcement dated 12 February 2018. Customers are already feeling the effects of these changes.

QRC issued a [media statement](#)¹ on Aurizon Network's behaviour on 12 February, which noted industry's extreme disappointment at Aurizon Network's move to pre-empt the regulatory process by moving to change its maintenance program before the QCA process is completed.

For the sake of approximately \$25 million in its annual maintenance allowance Aurizon would cost Queensland 20 million tonnes of coal exports per year, which is worth \$4 billion in export income and would cost the State Government around \$500 million in lost royalties each year. That lost royalty revenue is enough to pay the wages for 7,388 teachers, or 7,060 police constables or 7,430 registered nurses.

QRC's Chief Executive said:

"This latest announcement shows Aurizon is willing to use its power as the monopoly operator of the network and further highlights why the regulatory process needs to be followed to maintain a level playing field."

¹ <https://www.qrc.org.au/media-releases/statement-qrc-chief-executive-ian-macfarlane-aurizon/>

The Queensland Resources Council (QRC) is calling on Aurizon to step back from its decision and is seeking reassurances from them to instead engage constructively with the regulator to review any concerns with maintenance."

Queensland's Deputy Premier and Treasurer, the Hon Jackie Trad was quoted the following day in *The Australian* (page 19) as saying:

"I would encourage all stakeholders to make a submission to the QCA and to work productively for the best outcome, instead of attempting to hold the independent regulator to ransom." (emphasis added)

In conclusion

For the reasons outlined above, QRC supports the Bill but requests that the Committee recommend an extra amendment to immediately extend the declaration of the Rail Network Services. QRC submits that such a declaration should be indefinite, but an extension of at least 10 years is immediately necessary.

QRC would welcome any opportunity to elaborate on any of the points made in this submission or for the opportunity to appear before the Committee to give evidence. I can confirm that the submission is not confidential and the Committee is welcome to publish it on the Parliamentary website. The contact at QRC is [REDACTED]
[REDACTED]

Yours sincerely



Ian Macfarlane
Chief Executive