QUEENSLAND
COMPETITION
AUTHORITY

Our Ref: Paul Bilyk
Direct Line: 3222 0506
File Ref: 196428

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Executive Director (Rail, Ports and Freight) and
Chair Ports Competition and Regulatory Review Committee
Queensland Transport
GPO Box 1549
Brisbane, QLD 4001

Dear Sir

Submission: Review of Current Port Competition and Regulation in Queensland

Attached is a submission by the Queensland Competition Authority in response to the Department of Transport's discussion paper, *Review of Current Port Competition and Regulation in Queensland.*

The Authority would be happy to discuss any aspect of this submission with you further. In this regard, please contact Paul Bilyk on 3222 0506 in the first instance.

It would also be appreciated if the Authority was informed of any future developments relating to this review.

Yours sincerely

EJ Hall
Chief Executive

SUBMISSION BY THE QUEENSLAND COMPETITION AUTHORITY TO THE REVIEW OF CURRENT PORT COMPETITION AND REGULATION IN QUEENSLAND

The Authority notes that the Council of Australian Government's (COAG's) meeting of 10 February 2006 required the states and territories to review ports competition and regulation in accordance with an agreed terms of reference – the Competition and Infrastructure Reform Agreement (CIRA).

The Authority has prepared this short submission in response to the discussion paper prepared by the Department of Transport to satisfy these obligations.

The Authority's main concern with the discussion paper is that there appears to be an underlying premise that the existing arrangements at non-regulated ports are satisfactory. This seems to be a common theme of the discussion paper and is exemplified in the statement on page three where it is stated that the Queensland ports and port services are provided through government owned corporations and:

> …operate through commercially based contracts and agreements. This approach has stood the test of time and has provided far superior outcomes than would have developed under an imposed regulatory access and pricing system. … investments [in these terminals] were based on commercial agreements, arrived at by direct bargaining in good faith, between the terminal owner (i.e. the port authority) and coal producers. On the other hand, the progress of the expansion of DBCT was seriously delayed due to adversarial debates within the Queensland Competition Authority (QCA) framework regarding costing of the expansion and approvals to include the expenditure in the regulated asset base (p. 3).

The Authority is particularly concerned that

(a) there appears to be a presumption that a "negotiated" agreement between a monopoly service provider and a user will provide for an economically efficient outcome, indeed a "superior" outcome; and

(b) it is asserted that the regulatory process delayed the expansion of the Dalrymple Bay Coal Terminal (DBCT).

The Authority's submission examines these two issues in turn.

Do existing arrangements deliver efficient outcomes?

The discussion paper asserts that arrangements entered into between a monopolist and a user constitute "commercial" arrangements and will deliver "superior" outcomes.

Such an assertion is not supported by economic theory. More importantly, it is not supported by the Authority's experience to date.

In considering the DBCT access undertaking, the Authority's comprehensive review established an access charge that was around 20 per cent lower than had existed under the previous "commercial" arrangements at the terminal. While this was not the price the terminal operator had initially hoped for, it was sufficient for a significant expansion of the effectively privately owned terminal to proceed.

Moreover, it was apparent that, given the opportunity to be heard by an independent referee, the terminal's users were not satisfied with the pre-existing prices nor with the manner in which such prices had been "negotiated" in the past.

It is also quite possible that this situation currently exists at the other non-regulated ports and terminals in Queensland. Indeed, even though "negotiated" outcomes may have been achieved at non-regulated facilities, the nature of these outcomes may have been quite different if the parties had recourse to independent dispute resolution procedures.

The Authority's experience in relation to this is not just related to port services. In the case of rail, it is clear from user submissions to the Authority's first review that the previous situation of an unregulated monopoly had not delivered either prices or arrangements that were satisfactory to users. However, those prices and arrangements had been "negotiated" between the parties and the presumption of this discussion paper would be that they were "commercial" and "superior".

Not only did the Authority's first undertaking immediately deliver lower prices to rail users but coal companies were also able to test the market and competitively tender for the purchase of rail haulage services. Similarly, Pacific National (now Asciano) entered the Queensland market by commencing an inter-modal service between Brisbane and Cairns.

The Authority encourages the review committee to undertake a more probing consideration of the evidence to establish whether or not the existing arrangements are sufficient to generate the best possible outcomes for the State.

Expansion of the Dalrymple Bay Coal Terminal

The Authority rejects the claim that regulatory processes delayed the expansion of DBCT. It accepts that the process preceding the approval of the DBCT access undertaking was protracted, and sometimes adversarial, but planning for the terminal's expansion continued in parallel throughout this period.

Attachment 1 provides a summary of the expansion timeline. The key issue that drove the timeline was not the regulatory process but the changing world coal situation.

In particular, when the undertaking was submitted in 2003, there was no clear timetable for implementing the next increment of capacity and the undertaking reflected the view that terminal expansion would occur as and when required to meet user demand. By early to mid 2004, that view had changed substantially and there was a scramble to determine likely future demand and the best approach to handling that demand. This naturally took some time to resolve. However, the time taken was not the result of regulatory impediments. Rather, it was the result of a need to rapidly and substantially expand the facility's capacity in the face of previously unpredicted demand.

The view that the regulatory process did not delay the expansion is supported by DBCT Management.

Attachment 1

Timeline to the terminal's expansion and the related approvals process

In September 2001, a group led by international investment bank Babcock and Brown acquired a long term lease in the terminal from the Queensland Government. Following an initial public offering, Prime Infrastructure (now Babcock and Brown Infrastructure) was listed on the Australian Stock Exchange in June 2002 with DBCT as its foundation asset.

At that time, the stage 6 expansion works to increase the terminal from 44.0 to 56.0 million tonnes per annum (mtpa) were in progress. In addition, DBCT Management's Master Plan 2003 outlined 17 incremental engineering steps to enhance DBCT's capacity to 74 mtpa. This master plan was approved by DBCT Holdings in March 2003. The stage 6 expansion was commissioned in June 2003.

DBCT Management submitted its draft access undertaking (DAU) to the Authority in mid 2003. This DAU did not propose a capital expenditure program to underpin future capacity expansions at the terminal. Rather, it indicated that there was no clear timetable for implementing the next increment of capacity and that terminal expansion would occur as and when required to meet the needs of user demand.

In considering the 2003 DAU, the Authority was obliged to conduct a consultation process with stakeholders in accordance with the provisions of the *Queensland Competition Authority Act 1997*. This process involved assessing the significant and divergent views of DBCT Management and users on a range of matters, including the access charge, asset valuation and the rate of return.

DBCT Management commenced an interim expansion of the terminal (called the 'short gain expansion') to increase capacity to 59 million tonnes per annum in February 2004, primarily to replace the collapsed yard machine RL1.

The first quarter of 2004 also saw a boom in demand for coal. As a result, the existing incremental expansion path was no longer relevant and DBCT Management sought to develop alternative expansion options in advance of the Authority's decision on the DAAU.

Due to user uncertainty surrounding demand requirements at the time, the revised Master Plan 2004 that was approved by DBCT Holdings offered 3 alternative expansion paths. Accordingly, in July and September 2004, DBCT Management approached users to determine their future capacity requirements.

On the basis of user responses, DBCT Management produced Master Plan 2005, which defined the expansion of the terminal in three phases to 85 mtpa. This master plan was approved in July 2005 by DBCT Holdings and the phase 1 expansion of the terminal commenced in September 2005, though some preliminary design work commenced as early as October 2004.

In October 2004, the Authority released a draft decision rejecting the 2003 DAU with a final decision rejecting the DAU released in April 2005.

In January 2006, DBCT Management resubmitted the 2006 DAU. With the key pricing parameters having been settled in the Authority's April 2005 decision, the terms of the 2006 DAU had been settled through negotiation between DBCT Management and the terminal's users. Only a small number of matters were left to be resolved during the Authority's consideration of the 2006 DAU. The Authority approved this undertaking in June 2006.

In August 2006, the incremental short gain expansion of the terminal was commissioned and the Ports Corporation of Queensland substantially completed dredging of the port's departure path. These works increased terminal outloading capacity to 60 mtpa.

By this time, detailed planning for, and construction of, the three phases of the stage 7x expansion were well underway. The phase 1 expansion to 68 mtpa is anticipated to be completed by January 2008 and the phase 2/3 expansion to 85 mtpa is anticipated to be completed by December 2008.