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Submitted via online submissions portal

## DBIM's Application for a price ruling – 8X expansion

28 September 2021

Dear Charles,

Aurizon Network welcomes the opportunity to make a submission to the Queensland Competition Authority's (QCA) Draft Determination on Dalrymple Bay Infrastructure Management's (DBIM's) application for a pricing ruling on the 8x Expansion (**8x Expansion**).

Aurizon Network is not a user of the Dalrymple Bay Coal Terminal (DBCT) and therefore is not directly impacted by the QCA's draft determination to accept DBIM's application to socialise the complete 8x Expansion with the price of using the existing terminal. However, Aurizon Network may be indirectly impacted due to potential inefficient utilisation or investment in rail transport infrastructure, which might arise from a decision to socialise all or part of the 8x Expansion costs.

The 8x Expansion is comprised of four sequential phases, with each phase having its own discrete capacity increment and costs as shown in table 1.

**Table 1. DBCT 8X Expansion Phases – Project Costs<sup>1</sup>**

| Phase        | Capacity Increment<br>(million tonnes) | Cost<br>\$millions | Cost / Increment<br>\$/tonne |
|--------------|--|--------------------|------------------------------|
| 1            | 3.1                                    | 246                | 79.4                         |
| 2            | 3.9                                    | 229                | 58.7                         |
| 3            | 5.5                                    | 461                | 83.8                         |
| 4            | 2.4                                    | 340                | 141.7                        |
| <b>Total</b> | <b>14.9</b>                            | <b>1,276</b>       | <b>85.6</b>                  |

<sup>1</sup> Queensland Competition Authority (2021) Draft Determination: DBIM's application for a price ruling—the 8X expansion, Appendix A, August, p. 52

A key consideration in the draft determination to accept DBIM's proposal to socialise the 8x Expansion with existing users of DBCT are the benefits to those users:

*There will be cost savings to the NECAP program (as a reduction to the future asset replacement program), regardless of whether the 8X expansion is socialised<sup>2</sup>.*

Aurizon Network supports the proposition that where an expansion replaces existing assets that would otherwise be required to be replaced in the foreseeable future, it is reasonable for these cost saving benefits to be taken into account for future price determinations. These cost saving benefits are distinct from other benefits which may accrue from the upgrade of existing infrastructure.

The benefits from the 8x Expansion, expressed in terms of avoided costs associated with the future Non-Expansion Capital Expenditure Program (**NECAP**), are largely identified by the QCA as being<sup>3</sup>:

- the replacement of reclaimer (RL2) in Phase 4, which saves \$54 million: and
- the installation of a new shiploader (SL4) in Phase 1, which will allow the existing shiploaders (SL1–SL3) to be refurbished, rather than the more expensive alternative of replacement (saving \$150m).

These benefits can be attributed to the relevant phase to obtain a net cost per phase as shown in Table 2.

**Table 2. DBCT 8X Expansion Phase – Net Project Costs**

| Phase        | Capacity Increment<br>(million tonnes) | Net Cost<br>\$millions | Cost / Increment<br>\$/tonne |
|--------------|--|------------------------|------------------------------|
| 1            | 3.1                                    | 96                     | 30.9                         |
| 2            | 3.9                                    | 229                    | 58.7                         |
| 3            | 5.5                                    | 461                    | 83.8                         |
| 4            | 2.4                                    | 296                    | 123.3                        |
| <b>Total</b> | <b>14.9</b>                            | <b>1,072</b>           | <b>71.9</b>                  |

The DBIM application seeks to socialise the complete 8x Expansion with the current cost base and the QCA has assessed that application as a single expansion as opposed to four discrete expansions of the terminal. In this regard, the net cost per capacity increment of phases 3 and 4 is approximately twice that of phases 1 and 2 as outlined within Table 3.

**Table 3. DBCT 8X Expansion Phase – Staged Net Costs**

| Phase   | Capacity Increment<br>(million tonnes) | Net Cost<br>\$millions | Cost / Increment<br>\$/tonne |
|---------|--|------------------------|------------------------------|
| 1 and 2 | 7.0                                    | 325                    | 46.4                         |
| 3 and 4 | 7.9                                    | 757                    | 95.8                         |

<sup>2</sup> Ibid, p. 39

<sup>3</sup> Ibid, pp. 38-39

The bundling of the four phases into a single socialised expansion project has the potential to distort investment incentives and pricing signals. This is relative to the circumstance where expansion users in phases 3 and 4 may otherwise be faced with the marginal costs of expanding the terminal relative to the alternate options of utilising existing supply chain infrastructure.

In assessing the DBIM application the QCA is required to have regard to whether socialisation of the 8x Expansion is in the public interest. In this regard, the public interest should consider:

- the efficient utilisation and investment in supply chain capacity; and
- the promotion of competition in relevant markets, including the market for coal handling services at a coal terminal.

DBIM's application and the draft determination focusses on the efficient investment in the DBCT and the comparison of the Terminal Infrastructure Charge (**TIC**) with and without socialisation. The draft determination would benefit from further analysis that compares the marginal costs of phases 3 and 4 against the public interest matters described in the list above.

DBIM's application does provide some detail as to the prospective incremental costs of the 8x expansion and concludes<sup>4</sup>:

*If 8X is Differentiated, especially if depreciation of the expansion assets occurs over a 10-year period, it will place pressure on profit margins for new mines seeking access to DBT. This would be higher than the existing TIC by around \$13/tonne, which the QCA's analysis suggested could be a material difference (i.e. a difference that is considerably greater than \$3.50 per tonne).*

Aurizon Network acknowledges the existing terminal users submissions, specifically regarding the applied economic life and therefore whether the prospective incremental costs as submitted by DBIM are reasonable<sup>5</sup>. Notwithstanding whether a 10-year economic life assumption is reasonable for this assessment the incremental costs for phase 3 and phase 4 are expected to be at least double that of phases 1 and 2.

Phases 3 and 4 are expected to be completed in 2028 and 2029 respectively. These timeframes also coincide with the cessation of the Goonyella to Abbot Point Expansion (**GAPE**) foundation customer agreements and it is therefore feasible that available capacity may exist for GAPE services in competition for DBCT services. It is also feasible the total supply chain costs for the use of GAPE services would be lower than the total supply chain costs of the incremental phase 3 and 4 expansions.

Accepting a socialised pricing proposal for phases 3 and 4 should require a high degree of confidence that the marginal investment in phases 3 and 4 represents the least cost expansion of supply chain capacity in the CQCN and it is not necessary to price on an incremental basis to provide the necessary price signals to promote the efficient investment and utilisation of supply chain capacity.

Aurizon Network acknowledges there is significant uncertainty regarding the input assumptions required to assess phase 3 and 4 against alternate supply chain options. However, assessing

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<sup>4</sup> DBI (2021) 8X Expansion – FEL 2 Study Application for Ruling on Pricing Method, March, p. 47

<sup>5</sup> Synergies (2021), DBIM pricing method for 8X expansion, Submission from Selected Users, June, p.16

the level of confidence that socialising the phase 3 and 4 components of the 8x Expansion will promote the public interest necessarily requires an understanding of the incremental cost and benefits of those phases for comparison against possible alternatives.

In addition, the public interest of socialising phases 3 and 4 will be substantially diminished where the utilisation of the expansion capacity is comprised of the redistribution of mining output as opposed to an expansion of total CQCN mining output. In this respect DBIM's application states<sup>6</sup>:

*The Queue now includes a majority of Access Seekers with existing access at DBCT or other coal terminals,*

In summary, Aurizon Network considers if there is a high degree of confidence that phase 3 and 4 of the 8x Expansion represents the least cost expansion of supply chain capacity then the public interest would be promoted whether those phases are priced on a socialised or incremental basis. If the confidence level is low then the QCA should evaluate whether socialisation of all phases of the expansion would promote the public interest having regard to:

- the incremental costs and benefits of 'each' phase and a comparison of the total supply chain costs of each phase with the total supply chain costs of alternate supply chain options; and
- the composition of the DBCT Access Queue and whether the expansion is supporting expansion of total CQCN contracted output or redistribution of current contracted output.

Aurizon Network would welcome any relevant information requests from the QCA to support an assessment of the public interest in the proposal to socialise the 8x Expansion. Should you have any questions in relation to this submission please contact Dean Gannaway by email at [dean.gannaway@aurizon.com.au](mailto:dean.gannaway@aurizon.com.au).

Kind regards,



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<sup>6</sup> DBI (2021) 8X Expansion – FEL 2 Study Application for Ruling on Pricing Method, March, p. 21