

# ACCC ORDERS PORT OF NEWCASTLE TO REDUCE CHARGES FOR GLENCORE

10 October 2018 | Australia

Legal Briefings – By **Michael Coutts, Richard Robinson and Matthew Bull**

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The Australian Competition and Consumer Commission has determined that Port of Newcastle Operations must reduce the current charge for ships entering the port carrying Glencore's coal by around 20%. As the first substantive arbitration under the National Access Regime, the determination provides important guidance on how the ACCC approaches its arbitration role.

## OVERVIEW

On 18 September 2018, the Australian Competition and Consumer Commission (**ACCC**) issued its determination relating to an access dispute between Port of Newcastle Operations (**PNO**) and Glencore Coal Assets Australia (**Glencore**). The access dispute concerned access charges and other conditions of access to the 'declared' shipping channel service at the Port of Newcastle (the **Port**).

The shipping channel service (the **Service**) at the Port was declared under Part IIIA of the *Competition and Consumer Act 2010* (Cth) (the **Act**) by the Australian Competition Tribunal (**Tribunal**) in June 2016. Subsequent attempts by PNO to challenge the Tribunal's decision in the Full Federal Court and High Court were unsuccessful. In January 2015, PNO increased the charge for coal ships entering the port by around 40 per cent to \$0.69 per gross tonne (**GT**). On 4 November 2016, Glencore notified the ACCC of a dispute with PNO about the price increase and requested the ACCC to arbitrate. The ACCC determined that PNO should reduce its current charge for ships entering the port carrying Glencore's coal by around 20 per cent to \$0.61 per GT.

The ACCC has previously only arbitrated one matter under Pt IIIA (Sydney Water Corporation). However, that case (unlike this one) did not involve a detailed consideration or setting of prices. Although the present determination is only applicable to Glencore, the ACCC itself noted in the determination that it provides a 'useful framework and guiding principles' for other parties in their negotiations.

## BACKGROUND

### NATIONAL ACCESS REGIME

Part IIIA of the Act establishes a regime to facilitate third party access to services provided through facilities with natural monopoly characteristics (**National Access Regime** or **NAR**). The NAR provides a number of mechanisms by which the terms and conditions of access to services may be determined. One

way is for the relevant Minister to 'declare' a service or services provided by means of a facility.

Following declaration, access seekers have a right to negotiate terms and conditions of access with the service provider and, failing agreement, may request the ACCC to arbitrate the dispute. The ACCC must then make an arbitration determination and publish an arbitration report.

## **DECLARATION OF THE SHIPPING CHANNELS AT THE PORT**

In January 2015, PNO increased the charge for coal ships entering the port by around 40 per cent to \$0.69 per GT. PNO subsequently increased the charge to \$0.76 per GT as of August 2018.

On 13 May 2015, Glencore applied to the NCC for a declaration under the NAR to access and use the Service. The NCC recommended that the Service not be declared because, amongst other things, declaration was unlikely to materially increase competition in the export coal market as charges for the Service represented a 'minor component' of the free on-board cost of coal at the Port. On 11 January 2016, the Acting Treasurer agreed with the NCC's recommendation and published a decision not to declare the Services. (For further information, see our [previous article](#).)

Glencore applied to the Competition Tribunal for a review of the Minister's decision. The Tribunal found that, because access to the Service was 'essential to compete in the coal export market', providing access to the Service 'would promote a material increase in competition'. The Tribunal set aside the Minister's decision and declared the Services until 7 July 2031. (For further information, see our [previous article](#).)

PNO applied to the Full Federal Court seeking to set aside the Tribunal's decision and have the matter re-determined by the Tribunal. The Commonwealth of Australia and the ACCC joined the proceedings. Ultimately, the Full Court unanimously dismissed PNO's application (For further information, see our [previous article](#).) On 12 September 2017, PNO applied to the High Court for special leave to challenge the Full Court's decision but the application was dismissed on 23 March 2018.

## **ACCC ARBITRATION PROCESS**

On 4 November 2016, Glencore notified the ACCC of an access dispute in relation to the Service provided by PNO. On 22 December 2016, the ACCC commenced the arbitration.

As a first step, the ACCC sought comments from the parties on the information about port services and port charges that would be necessary for the arbitration. A key issue that arose in their responses was the scope of the arbitration. Following the parties providing views on the scope of the arbitration (including at a hearing), the ACCC provided the parties with its preliminary view on the scope of the arbitration on 19 March 2018. On the same day, the ACCC directed the parties to jointly develop and submit to the ACCC a model and inputs to the model that both parties agreed to use for the formulation of prices, together with a report detailing the aspects of the pricing model and other terms and conditions of access on which they were able to agree. The ACCC also directed the parties to provide separate submissions in relation to aspects of the pricing model, inputs to the model and other terms and conditions of access that the parties were unable to agree.

On 7 May 2018, the parties jointly submitted a 'building block model' (**BBM**) as their agreed access pricing methodology. This was a modified version of the Australian Energy Regulator's (**AER's**) publicly available Post-Tax Revenue Model. The BBM is used to determine the maximum allowed revenue and prices for the Service. The parties also jointly submitted a Depreciated Optimised Replacement Cost (**DORC**) methodology as their agreed asset valuation methodology to determine the initial value of assets required to provide the Service, with depreciation to be assessed on a straight line basis over the useful life of the asset. The parties, together and separately, provided submissions setting out the aspects of the pricing

model and other terms and conditions of access on which they agreed. They also made separate submissions in relation to aspects of the pricing model, inputs to the model and other terms and conditions of access on which the parties were unable to agree, and submissions in response.

On 20 July 2018, the ACCC provided the parties with its draft determination and supporting statement of reasons in relation to the issues raised in the course of the arbitration. The ACCC also directed the parties to provide submissions in response to these draft documents, and submissions in reply to each other.

## **ACCC'S DECISION**

The ACCC accepted the parties' agreed pricing and asset valuation methodologies, and agreed inputs to, and implementation of, these methodologies. The ACCC then made determinations on those aspects where the parties were unable to agree.

### **SHIPPING CHARGES**

PNO submitted to the ACCC that the 2018 charge for coal ships entering the port should be increased to \$1.36 per GT. In contrast, Glencore submitted the charge should be reduced to \$0.41 per GT.

The ACCC derived the charges for ships entering the port from the value of the assets used to provide the Service. A key part of this exercise was whether PNO should be able to charge for shipping channel dredging that had been undertaken or funded by users of the Port. The ACCC excluded these user funded amounts from the costs that PNO could recover and determined Glencore should pay a lower price, backdated to 2016.

### **TERM OF DETERMINATION**

Glencore submitted that an initial term of 15 years was appropriate. PNO submitted that any agreed or arbitrated terms should apply for the balance of the period of declaration, provided that the five-yearly review, annual price setting and annual true up process mechanisms would apply throughout the duration of the determination term.

The ACCC considered that it was appropriate to align the duration of the arbitrated terms of access with the period of declaration (i.e. 8 July 2016 to 7 July 2031). In the ACCC's view, this approach provided the parties with certainty over the period of the declaration, and therefore assisted the legitimate business interests of PNO, as well as the interests of those with rights to use the Service.

## **NOTABLE ASPECTS OF THE ARBITRATION**

### **ADJUSTMENTS TO DORC**

The parties agreed to use the DORC valuation methodology to establish PNO's initial regulatory asset base (**RAB**) for the purposes of this arbitration. A DORC valuation involves: estimation of construction costs for the 'optimised' asset; calculation of interest during construction (**IDC**); and calculation of depreciation.

Throughout the negotiations, the parties did not agree on the following issues relating to the DORC valuation:

- whether certain assets neither owned nor leased by PNO should be included in the construction costs estimates;

- estimates of construction costs for certain assets that are included;
- the valuation date, which also informed the applicable rate of interest for the calculation of IDC;
- the construction period for the calculation of IDC;
- whether user funded capital contributions to construction of assets should be deducted; and
- the asset lives and remaining useful life for the calculation of depreciation.

The treatment of user funded contributions was the most significant driver of the different prices proposed by the parties. Glencore was of the view that all user funded capital contributions should be recognised and deducted, whereas PNO considered that this was inappropriate.

The ACCC found that user funded capital contributions should be recognised and deducted from the DORC value used to establish PNO's initial RAB and to calculate prices to ensure that PNO was able to reasonably recover its efficient costs. The ACCC considered that PNO's efficient costs for the provision of the Service did not include capital costs that had been funded by users because including user contributions in PNO's initial RAB would result in users paying for the same assets twice: once through their initial investment and again through PNO's charges.

## **BACKDATING OF CHARGES**

Under the Act, any or all of the provisions of a final determination can be backdated to any date after the date on which negotiations commenced or the date on which the declaration began to operate. In considering the appropriate period of backdating, the ACCC noted that the backdating provisions are intended to provide incentives for the parties to not cause unreasonable delay during negotiations and during the arbitration process.

The ACCC considered that the parties commenced negotiations on 17 June 2016, which was before the date on which the Service became a declared service. The ACCC therefore decided to backdate the terms of its determination to apply from 8 July 2016, the commencement of the declaration of the Service.

PNO objected to the backdating provision extending to a period when PNO claimed it was unaware that Glencore was accessing the Service, and also where instances of Glencore's use of the Service had not been established. However, the ACCC considered that, from at least the date on which the parties commenced negotiations, PNO would have been (or should reasonably have been) aware that Glencore purported to be accessing or using the Service (or intended to do so), justifying the backdating of the determination to include such periods.

## **INTEREST PAYMENTS**

The Act also enables the ACCC to require the payment of interest on the whole or part of the payments that arise from a backdated period as a result of the ACCC's determination. The ACCC considered the proposed backdated payment should include an interest component.

Interest is not intended to operate as a sanction or penalty, but to place the parties, as far as possible, in the position that they would have been in had the arbitrated price applied from the outset. The ACCC therefore considered it appropriate to adopt the June 2016 Large Business Weighted Average Rate on Credit Outstanding Variable Rate published by the Reserve Bank of Australia.

## SUSPENSION OF ARBITRATION PROCESS

The Act allows the parties to agree to suspend the ACCC's arbitration process. In this case, the parties agreed to suspend the arbitration from 2 February 2017 until the Full Federal Court made a decision on PNO's application for judicial review of the Tribunal's decision to declare the Service. Following the decision of the Full Federal Court on 16 August 2017, the ACCC recommenced the arbitration. No suspension occurred while PNO (unsuccessfully) sought leave to challenge the Full Federal Court's decision in the High Court.

## WHERE NEXT

The ACCC's determination takes effect 21 days after the date on which it was made, providing the parties with an opportunity to challenge the decision. It has been reported that PNO intends to challenge the ACCC's decision in the Tribunal.

Strictly speaking, the scope of the determination is restricted to Glencore. Any potential future dispute between an access seeker and PNO in relation to access to the Service would need to be decided on merits. However, in its determination, the ACCC noted that it considers that its approach in this dispute provides a useful framework for guiding the negotiations of other parties.

This said, following changes to the NAR brought about by the Harper Review, it may be difficult for other parties to achieve a similar outcome due to the risk of the declaration of the Port being revoked. The amended competition criterion requires a detailed factual analysis of the likely future with and without declaration, which is likely to make it harder for access seekers to secure declaration in situations where access is already being provided voluntarily. PNO is already providing access, albeit on terms that have been successfully challenged by Glencore. It should be noted that PNO will be bound by the ACCC's arbitration decision for Glencore even if the Port's declaration is revoked.

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## ENDNOTES

1. [Determination of the access dispute between Port of Newcastle Operations and Glencore Coal Assets Australia](#)
2. [National access regime under Part IIIA](#)

## KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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