ECONOMICS AND INDUSTRY STANDING COMMITTEE

INQUIRY INTO THE MANAGEMENT OF WESTERN AUSTRALIA'S FREIGHT RAIL NETWORK

TRANSCRIPT OF EVIDENCE
TAKEN AT PERTH
FRIDAY, 13 JUNE 2014

SESSION THREE

Members

Mr I.C. Blayney(Chair)
Mr F.M. Logan (Deputy Chair)
Mr P.C. Tinley
Mr J. Norberger
Mr R.S. Love

Hearing commenced at 11.35 am

Mr DALE GEOFFREY HARRIS
CEO, Karara Mining, examined:

The CHAIR: On behalf of the Economics and Industry Standing Committee, I would like to thank you for your appearance before us today. The purpose of this hearing is to assist the committee in gathering evidence for its inquiry into the management of Western Australia's rail freight network. You have been provided with a copy of the committee's specific terms of reference. At this stage I would like to introduce myself and the other members of the committee. I am Ian Blayney, the Chair; Hon Fran Logan is the Deputy Chair; and our other committee members are Jan Norberger, Peter Tinley and Shane Love.

The Economics and Industry Standing Committee is a committee of the Legislative Assembly of the Parliament of Western Australia. This hearing is a formal procedure of the Parliament and therefore commands the same respect given to proceedings in the house itself. Even though the committee is not asking witnesses to provide evidence on oath or affirmation, it is important that you understand that any deliberate misleading of the committee may be regarded as a contempt of Parliament. This is a public hearing and Hansard is making a transcript of the proceedings for the public record. If you refer to any documents during your evidence, it would assist Hansard if you would provide the full title for the record. Before we proceed to the inquiry's specific questions we have for you today, I need to ask you the following. Have you completed the "Details of Witness" form?

Mr Harris: Yes.

The CHAIR: Do you understand the notes at the bottom of the form about giving evidence to a parliamentary committee?

Mr Harris: Yes, I do.

The CHAIR: Did you receive and read the information for witnesses sheet provided with the "Details of Witness" form today?

Mr Harris: Yes, I did.

The CHAIR: Do you have any questions in relation to being a witness at today's hearing?

Mr Harris: No.

The CHAIR: Do you have an opening statement for us today?

Mr Harris: As you know, we made a submission as part of your inquiry, which I think set out broadly the status of our arrangements in terms of rail. We constructed and built a 90-kilometre rail spur that ties into the existing rail network in the midwest. As part of our agreement with Brookfield, Brookfield invested further money in terms of upgrading the capacity of the existing infrastructure, and we have been in operations now for over 12 months and hauling—or having Aurizon half-haul—that ore to the port of Geraldton. Operationally, and from a maintenance perspective, the service is working quite well. There are always opportunities to improve the operational performance of the system, but we have a constructive dialogue occurring with Brookfield on those opportunities. I think the key issue was really before my time; I have only been CEO of Karara for a relatively short period of time. But in terms of the original negotiations and structuring of the agreements to allow the Karara project to proceed and for access to rail to be had, when those discussions and negotiations were occurring, it became clear fairly early that the regulatory framework that was in place did not really provide any real support for a company in Karara's position to be in a stronger position to have that negotiation with an infrastructure asset that the existing rail system has there. You essentially have a monopolistic provider of those services, and unless there is a strong regulatory framework in place, it puts the balance of the negotiation power too much on one side and not enough on the company that is trying to get access to that infrastructure. We found it quite difficult to use the provisions within the regulatory framework and ultimately it ended up being a commercial negotiation directly with Brookfield without any real support from that framework. The result of that is that it is a tough negotiation when you are in that position.

Mr J. NORBERGER: You have no-one else to negotiate with?

[11.40 am]

Mr Harris: That is right. The nature of the midwest is that the resources are not of the size that you see in the Pilbara. In the Pilbara, the economics of building dedicated railways are okay, but in the midwest that is not the case and you need to do the best deal that you can with the existing infrastructure provided.

The CHAIR: I think there have been some cases where the ore has gone by road because they have not been able to reach an agreement on access to the railway line.

Mr Harris: Yes, so when you have got issues about how you assess the capacity of the existing system, there is no real mechanism in the framework to deal with that, so then it is how much capital is required to deliver an incremental capacity, or you have got no base to start with. So, you really have got nothing to underpin an engagement with the owner of that infrastructure. Inevitably, where we ended up, there was capital that we needed to spend to put the spur in there and there was capital that Brookfield put in to upgrade the system. We have effectively underwritten all of that capital, but I would argue that others have benefited from that upgrading of the infrastructure as well. But how is that actually determined?

Mr P.C. TINLEY: You do not get an offset for that?

Mr Harris: We do not think we get an offset for that.

Mr J. NORBERGER: If I can just jump in there. Thank you for your opening statement. We have heard from other organisations and members that have come before the committee, and everyone has obviously stated the same thing and it is an obvious thing, which is that Brookfield is a monopoly. We have heard from other people that one offsetting factor to help in a situation where you are dealing with a monopoly is transparency. I would be very keen to hear from you in regard to how transparent the negotiations were. When you were negotiating your access fees, how transparent was the process in relation to, “This is how much money we need to maintain it, and there is a reasonable rate of return”, or was it purely that you had no idea what it was you were paying for?

Mr Harris: Again, I should preface this by saying that I was not personally involved in the negotiation, so you would have to sort of take my comments as generalisations. The feedback I have had from my team was that there was not a great deal of transparency and it was in fact difficult to really sort through all that. Ultimately, we got a deal done with Brookfield, but it was on what we considered was a very tough negotiation where the balance of the risk–reward trade-off—we took on a lot of the risk in terms of bank guarantees required, parent company guarantees and so forth. It was a tough negotiation in the context of dealing with a monopoly supplier, effectively. If you look at the Queensland situation, at least there is a register of previous deals, if you like, and transparency on what has gone before it in terms of access. There were no registered agreements that were in place that would enable us to have any insights into what it would be costing to access a particular section of the track, so it was opaque, would be a way to describe it. It just makes the negotiation difficult.

Mr P.C. TINLEY: Negotiating with other suppliers, this is just one supplier of a service, if you like, or infrastructure as well. Surely you go into negotiations with a range of providers, including your own customers, with assumed knowledge at best about their inputs. What would be different between this and those other negotiations?

Mr Harris: If I can contrast it with, say, a mining contractor, we have a contract miner. There is quite a bit of transparency in the industry about what mining rates are, because there is a suite of providers you can go to to provide those services. In many instances, you get access to the cost model that those contract miners use at times, depending on how the negotiation goes, so there are opportunities in terms of how you have that engagement and that commercial discussion to get quite detailed information about the cost structures and the profit margins et cetera. It is very different; I think it is very different. Effectively in this case, with the rail case, there is only one realistic provider of the service and getting real insights into what their true costs are is much more difficult.

Mr P.C. TINLEY: In the case of Brookfield, what would be the characteristics around the transparency you would have liked to have seen?

Mr Harris: Really, it is an understanding of capacity. The ultimate thing is what is the existing network and those particular sections of track truly capable of. What is the true incremental cost of additional capacity?

Mr P.C. TINLEY: So what is your base capacity and what do we need to —

Mr Harris: Yes; and, therefore, what is a fair amount that we should be contributing to upgrade that —

Mr P.C. TINLEY: Got it.

Mr Harris: —and how do other users contribute in that mix. Because I think our view is that, yes, money was spent to upgrade the track and a lot of it was old track et cetera. We are underwriting all that and other users are benefitting from that.

Mr P.C. TINLEY: And you are getting no offset?

Mr J. NORBERGER: And it does not become yours.

Mr Harris: Correct. As I said, there is just not enough transparency on all those inputs into how a tariff would be calculated.

Mr P.C. TINLEY: Ultimately, this is about the price. In your experience in other jurisdictions, not just in the mining industry alone, do you believe you are now paying over the odds, relative to other miners in other jurisdictions; and, if so, percentage-wise by how much?

Mr Harris: I cannot definitively say that. I guess in my time I have probably focused on other issues within our business, because there is a deal that has been done and we have to live with it and we have other issues to address. But I would say that the rail solution that we have is an expensive one and it is a high fixed-cost one. It is one where the cost structure we have in place means we are less competitive with others in the industry. I think there is also this question about—you mentioned road transport; again, we have underwritten all that infrastructure and we are using rail. Companies that are using road transport are not necessarily underwriting the road infrastructure. I think there is a balance here; if we want to have a viable, strong rail infrastructure network, what are the incentives you can put in place, or penalties, if you like, so that people who are using road transport are truly paying for that so that they can make an informed decision as to whether they go to rail? We do not have, I guess, a rational system that makes people make the right decisions. I think some people are getting subsidised—not directly, but indirectly—and that perhaps sort of is not taken into account.

Mr R.S. LOVE: Mr Harris, I take you back to an ASX announcement that was put out in 2011, talking about the original agreement with WestNet then—now Brookfield—to undertake the upgrade of the existing line to Geraldton. It announced that Karara is required to provide $300 million in security, and Brookfield Rail is required to confirm its debt financing is in place to support the works. Does that mean that, in effect, you were paying $300 million up-front in access fees, or what does that mean?

Mr Harris: No; through our financial arrangements with our banks, as part of that deal there is a bank guarantee that that Brookfield could call on if we could not fulfil our obligations to utilise the rail. We have a take-or-pay contract. If, for some reason, we were not fulfilling that, then Brookfield has a bank guarantee and so on demand they could call on that $300 million. That bank guarantee is obviously part of the overall financing solution, and the banks have security against the assets of Karara. They also have parent company cross-guarantees, so Ansteel and Gindalbie—there are shares as part of that—and, ultimately, all that sort of goes back to the entities of Ansteel and Gindalbie. It does complicate the financing of this, where you have, again, another commitment hanging over you to put this deal together.

[11.50 am]

Mr J. NORBERGER: That is above and beyond the access fees?

Mr R.S. LOVE: The agreement is in place for, I think, 15 years; is that correct?

Mr Harris: Correct, yes.

Mr R.S. LOVE: Is there any understanding within that agreement as to an extension at the end of that 15 years —

Mr Harris: No.

Mr R.S. LOVE: — or perhaps renegotiation? What is the process? Your mine life, correct me if I am wrong, is much more than 15 years.

Mr Harris: It is, yes; we have a very large resource base. To be honest, I have not looked into the minutiae of the options to extend, but I think it would be the intent that we would obviously look to negotiate an extension. I have not, sort of, delved into the details of that contract.

Mr R.S. LOVE: If, for instance, we look at the line that was constructed, it is constructed as, potentially, a dual line, with provision made for standard gauge as well as narrow gauge.

Mr Harris: That is correct.

Mr R.S. LOVE: At whose suggestion was that provision made? Presumably, that must have added to the cost of the rail network that you are underwriting.

Mr Harris: Again, I preface this with saying that I was not involved in the detail, but I think it was a joint position that was developed by Karara and Brookfield, and it had, I guess, an eye to the future infrastructure development in the midwest. We wanted to make sure that we were not closing off options in terms of whether, ultimately, Oakajee gets developed and there was an infrastructure solution there. As I understand it, Karara was positive in terms of its stance on that, and that was a sensible thing to do at the time.

Mr R.S. LOVE: As you have largely underwritten the original upgrade for that section, which is at least owned by the state and leased to Brookfield, if other users were to come on stream, does that have an effect on the price that you would be expected to pay?

Mr Harris: As I understand it, no; we are locked into a take-or-pay arrangement.

Mr J. NORBERGER: What would be the benefit for Karara if at some stage you did go to standard gauge?

Mr Harris: I think it is all sort of linked to what the ultimate port solution looks like in the midwest. At the moment we can only accept panamax-sized vessels into Geraldton. Geraldton port, while it is adequate for what we are doing now, is not the greatest port in the world for bulk export; it is impacted by swell and conditions, and with panamax vessels there is a cost penalty there. It is about twice the cost for a panamax vessel to take ore to China as it is for a capesize vessel. It is an economic driver that, ultimately, you can get a lot of cost solution if you have a capesize port. Of course, that is all dependent on what the economics are around that port development as well. I guess the view that would have been taken was that we did not want to close that option off or make it more expensive to deliver that standard gauge option, which would have to be covered with a better port solution, whatever that may be.

Mr F.M. LOGAN: I want to ask a couple of fairly basic questions. In terms of the new railway and the upgraded existing rail capacity, what is the axle load now on that? I am not too sure whether you know these questions, but if you do not know them, you can provide them. What is the axle load, what is the speed, and what tonnage is hauled per train movement?

Mr Harris: The axle load is 21 tonnes. Each train carries 6 800 tonnes, approximately, of ore. I could not tell you the speed off the top of my head; I know that a rail cycle from mine to port and back is about 22 or 23 hours, and it is about 290 kilometres. We can provide that information if you want it.

The CHAIR: It is eight hours, I think, is it not? That is figure it comes to?

Mr Harris: Yes, but when you have the unloading and loading times at each end, it is almost a day but not quite a day in total.

Mr P.C. TINLEY: Cycle to cycle?

Mr Harris: Yes.

Mr F.M. LOGAN: The only reason I ask is because obviously we are looking at the whole network and where rail lines have been upgraded, like yours. It gives us an idea of what the capacity is, whether others should be upgraded or whether there are proposals to upgrade them. Can I move on to your company's press release on the rail access agreement in 2011? It noted that Karara will, as well as the rail access tariff, pay a capital recharge fee over the life of the contract. Obviously you would not want to go into detail with some of those figures, but is Karara aware of all the elements of what is in the tariff? Is Karara happy with the breakdown of the elements of the tariff, if you are aware of them?

Mr Harris: There are two components that we pay. We pay effectively a capital charge component and then there is a variable cost component which is based on actually how many train parts were used and so forth. The capital charge component is the biggest chunk of that. I cannot recall the exact percentages. We have a very high fixed cost arrangement. Variable costs are quite low. Over the 15 years, it is about $1.5 billion in total. It is about $100 million a year for us to access that rail. We would prefer to have a lower cost solution obviously but that is the arrangement we have. It is a high fixed cost component. Our variable costs are quite low.

Mr F.M. LOGAN: The tariffs themselves—that fixed cost, is that what you would determine as the tariff or the variable?

Mr Harris: The fixed cost is really the capital charge component.

Mr F.M. LOGAN: But there is a tariff as well?

Mr Harris: Yes, on top of that. There is a fixed and variable component of the overall charge. That is the two components.

Mr R.S. LOVE: On matters of access to the lines: when you did the negotiations, I think CBH was still using some of those lines at least—not on your line, but on the rest of the network there. Was there any factoring in of other users having access to those lines and what effect would it have had on the costs to you?

Mr Harris: I really cannot answer that question. I am not aware of that.

Mr R.S. LOVE: Specifically on your own line, you constructed to spur on there, if at some point in the future another company for some reason—I do not know; I do not have a crystal ball—wanted to have access to that line, what is your understanding of how that would operate?

Mr Harris: I have not given any thought to that at all. I would note, though, that we are actually hauling ore that we purchase from other parties at the moment. In essence we are providing an infrastructure solution to others through that rail spur. But the commercial arrangements that we have come to are around Karara purchasing the ore at Karara and then we are railing it from there. We are quite happy to have others access that infrastructure through that mechanism because it helps us offset some of the high fixed costs that we have with the current arrangement.

Mr R.S. LOVE: That section of line is operated by Brookfield for you; or who maintains that section?

Mr Harris: Effectively it is the same maintenance arrangements. It is just that the ownership is slightly different in that section. We are the owner and operator of that line.

Mr R.S. LOVE: Does that give you an understanding of the costs of maintaining that line, both now and future costs of replacement et cetera?

Mr Harris: Because it is a brand-new line, the costs have been quite modest to date. Again, I have not got those details in front of me. It has not been significant in terms of costs. I think as you go forward you will start to see those costs increase as you get wear on your track and you have to get into a replacement regime. At this stage we have not —

Mr R.S. LOVE: As of yet you have not done any detailed numbers yourself?

[12 noon]

Mr Harris: No, we have not done a detailed review about it at this stage.

The CHAIR: Can you just clarify: when you are talking maintenance on your spur line you are saying it is being done by the same body—how about paying for it? Are you paying for the maintenance on your line?

Mr Harris: Correct, yes.

The CHAIR: So basically you just get an invoice and pay it—is that how it works?

Mr Harris: Yes. It is our asset. We are accountable. We are leasing the asset from the PTA, so we are accountable for the maintenance of that asset. We pay that charge, yes. It is not Brookfield; it is ours under the lease arrangement that we have.

Mr R.S. LOVE: Was that to Brookfield or to John Holland? Who does the maintenance on it?

Mr Harris: It is through Brookfield. As I said, from an operational and maintenance perspective we are more than happy with the way Brookfield are running that. There are no issues that we have on that front.

Mr J. NORBERGER: In relation to when you were negotiating with Brookfield, I believe you tried to get some assistance, if you like, from the ERA and there was a floor and ceiling pricing mechanism in that. Could you maybe outline for us what your experience was with the floor and ceiling pricing mechanism? Was that mechanism effective in assisting your negotiations with Brookfield?

Mr Harris: It was ineffective because there was no real mechanism to get a floor and ceiling price and there was no information on existing floor and ceiling prices. It was completely ineffective and of no use.

Mr J. NORBERGER: So you were basically left to your own devices?

Mr Harris: Correct.

Mr P.C. TINLEY: At the risk of exposing my own ignorance on this: did your modelling contemplate identifying and establishing your own land access corridor? Builders in the north west and Pilbara have had to do their own—was that ever contemplated by Karara?

Mr Harris: Not that I am aware. One option that was contemplated was a slurry pipeline in lieu of rail access. Again, I was not involved in the detail but ultimately the decision was to go with rail. Really that was based, I think, on rail is more expandable. If you have a view that you want to double and triple the size of your business and the ore body would allow that, that is the way you would go.

Mr P.C. TINLEY: It would seem to me, though, that you did a deal. You are a publicly listed, responsible company, you did a deal, the market has worked; otherwise we would not be mining this resource and we would not be getting this resource to market. How would you respond to the fact that this project happened and it happened using the current system; the market worked—what is wrong?

Mr Harris: I think you are right—a deal was done. Whether it was a good deal or a bad deal, we are all big boys; a deal was done between Karara and Brookfield. The point I would make is that I think there could have been a better deal that Karara could have done with Brookfield if there was a stronger regulatory framework that supported getting a better deal.

Mr P.C. TINLEY: Just to tease that out: what did the taxpayers of Western Australia potentially miss out on, currently or into the future, on the basis of the deal you did with Brookfield?

Mr Harris: I would say that Karara as a project is in a difficult position at the moment. It is not necessarily about rail. We have some technical issues that we have to work through. We have disclosed that publicly in the past. In terms of where we move forward from here, it is about the competitiveness; where we have to put more capital into the business, where we have to look to the phase 2 expansion. Again, you have to look at the economic case for that. If you have a better deal that you can cut on infrastructure or with your mining contractors, that all goes into the mix. I think if you are looking at how do you know the framework that ensures there is a competitive iron ore industry in the midwest, if we want to develop the midwest, having reasonable access to infrastructure at a fair price is a prerequisite, I would have thought, to seeing the midwest region's full potential. That is an issue that needs to be wrestled.

Mr P.C. TINLEY: So, it might be an impediment to future expansion?

Mr Harris: I think that is right. It is all about infrastructure. You have got to have competitively priced infrastructure to give yourself the chance of developing the resources that you have got.

Mr F.M. LOGAN: I have a question about the PTA. To the best of your knowledge, because you were not there at the time, were you aware that the PTA played any role in the negotiations or contributed to the negotiations between Brookfield and Karara? Would you express any views on the responsibilities and role of PTA in the management of the network, other than the spur line that you are aware of?

Mr Harris: I am not aware of the PTA playing any role in negotiation. It certainly has not been raised with me. I think it was very much a Brookfield–Karara negotiation. That is where our relationship is.

Mr F.M. LOGAN: Does Karara have any views about the role—because obviously there is the rest of the line, which is owned by the PTA—and responsibilities of the PTA?

Mr Harris: No, I do not at this stage. I am focusing my energies further up the value chain.

Mr F.M. LOGAN: Fair enough.

Mr R.S. LOVE: Following up on what Fran has said, when your company was negotiating, was the Department of State Development involved with any of these negotiations at any point? You have never been involved with State Development?

Mr Harris: Not to my knowledge, and certainly when I have talked about this issue with people who were around, they have not mentioned DSD being involved; it was very much Karara and Brookfield having the negotiation because there was really no mechanism to get others involved.

Mr R.S. LOVE: You had negotiations which take place with landholders, for instance, to get the Western Power solution out to the mine. You built a considerable length of that power infrastructure yourself.

Mr Harris: Yes.

Mr R.S. LOVE: You built your own railway line and you plugged into an existing corridor, which was presumably the simplest solution at that stage, though not necessarily the most direct, all without direct involvement of the Department of State Development within that?

Mr Harris: No, I would not say that. We have a good relationship with DSD and I think they have been supporting us where we have been trying to navigate our way through, and where they can play a role and support us, they have. I guess my point is: when it came down to a commercial negotiation with Brookfield, it is Karara and Brookfield; there was no third party in that, and that is probably appropriate.

The CHAIR: I think with Karara, when I came into my job, their hold-ups were with environmental clearances and State Development may have played a role in there.

Mr Harris: Yes.

The CHAIR: And, of course, we had to pass an act for you to be allowed to build a railway line. If you are going to build a railway line, it takes an act of Parliament, so I remember that going through. That is about it.

Mr J. NORBERGER: Dale, I promise that I will be as succinct as possible. As I am talking, he is rolling his eyes! I will just try to be very succinct and try to summarise something and just see whether you agree with my summary or not. Obviously at the core of our terms of reference, we are trying to look at whether the current system is assisting or hindering state development, which we have just spoken about. It is really a follow-on from what Peter said. From the state's point of view, the state benefits when mining companies like yourself do well. If you do well and you are able to bring your ore to market, the state will get royalties from that which we can inject into our economy, people get employed and the like. However, in order for you to do that, if you want to use a state-owned asset—which from the state's point of view we would like to see you use if that is going to help you achieve your outcome, which means we get our income—you cannot deal with the state to use that state asset because we have leased it at a fixed cost to a third party; you have got to deal directly with that third party. The Department of State Development cannot help you, the ERA cannot help you and the PTA is hands off; it is just you and a monopoly. However much they charge, there is no benefit to the state for that because whatever extra profits they make, there is no variable to the state, so that profit just goes to Brookfield. Potentially, that has the danger of putting a higher capital cost; you have got higher risk now and you have got a higher fixed cost. That is potentially putting an imposition on Karara, which is not in our best interest; we want to see you put as much tonnage on a ship—panamax or otherwise—so we can get our royalties. Would that, broadly speaking, be a good summation of the situation you found yourself in in relation to the rail aspect? Obviously, I know there are many other aspects, including environmental, but in regard to the rail aspect would that be the summary there?

[12.10 pm]

Mr Harris: That is a reasonable summary. I think, clearly, as we said, Karara as a company did reach an agreement with Brookfield; we have signed up for that. As I think you are alluding to, you want to have a framework in place that enables a fair negotiation to occur with a monopoly infrastructure provider that delivers reasonable outcomes on both sides and a reasonable sharing of risk, because ultimately if too much risk is put on the mining proponent, it makes it difficult for the mining proponent to finance and develop that business. So, at the moment, as it stands, it is difficult because you have not got a regulatory framework that really supports that objective; therefore, as a result, there is a risk that you do not get development in the state that you would otherwise get and the royalties that you talked about. That is a fair summation.

Mr R.S. LOVE: In the submission you talk about healthy and unhealthy trains. Perhaps you might like to explain a little bit about that and what effect that has on your business.

Mr Harris: I would not overplay this. As I said, I think operationally and from a maintenance perspective, we are quite happy; we have got some opportunities, and this is really about an opportunity. The way it works is you have got a window within which you can run a train through the system. If the train is within that window it is considered healthy and therefore gets priority through the system. If it is late for some reason and falls outside that window, then it is unhealthy, and an unhealthy train is subservient to healthy trains that might be elsewhere in the system. That is, I guess, what I would call a fairly regulated scheduling approach. The alternative way to do it is to have a more integrated dynamic scheduling approach to trains, so you have an overall plan as to how many trains need to move in a week but you have some flexibility around that and you actually optimise in real time, and if you do that you can get more capacity in the same system. Certainly, if you look at the Pilbara, where I have quite a bit of experience, you have Rio Tinto with a whole stack of mines and an integrated system, they do not have fixed windows; they manage it dynamically to optimise in real time and get more capacity out of the same infrastructure. We believe that there are opportunities for further efficiency gains and improvement. We are having discussions with Brookfield and Aurizon on that path. That is the essence of it. It is an opportunity to do better, I guess, than what we have got.

Mr R.S. LOVE: Presumably Aurizon are operators nationwide and would have an understanding of these matters. Brookfield does not operate too many other rail systems throughout the world.

The CHAIR: This is the only one.

Mr R.S. LOVE: Would you characterise their management in some way as needing to be brought up to the standards that are considered normal in other areas?

Mr Harris: I would not want to be sitting here criticising Brookfield. I think the relationship we have got is a good one. We have talked to them about this and I think they are listening and willing to engage on that. I think the system here can be improved and I think it is going to require all the stakeholders to work together to get that improvement, and I am sure that Brookfield, from what I have seen, are willing to engage in that, so I do not have an issu**e** on that point. They are fairly commercial in their approach. I think that is just the nature of their shareholders and they are looking for a return on the investment they have got. That is fine, I think that is just the commercial reality of business.

Mr R.S. LOVE: You did speak a while ago about risk and the potential to put people off, I suppose, investing or changing their investment. When you were negotiating the original take-or-pay situation, you had a mine that was still yet to be proven as a process, so there was considerable risk that you might not have been able to make that take-or-pay system work. Is there a schedule of penalties laid out if you were unable to take?

Mr Harris: We are actually in that position now where the magnetite processing plant is not performing and we have got some significant technical issues that we are working through, which means that we are at significantly lower production levels than we otherwise thought we would have been. Because we have got take-or-pay obligations on rail, they are very high fixed costs so we are incurring additional costs, if you like, to buy third party ores, develop additional high-cost haematite operations to mitigate that high fixed cost we are exposed to. There is no relief under the contract that we have got that because we are struggling, we can push some of those out. Clearly, that is something that we probably will be talking to Brookfield about at some stage. Yes we have to make those take-or-pay payments under the contract, notwithstanding the fact that we are not up to full capacity. That is the risk coming back to us. That is what I meant by, when you are looking at the risk and those sorts of problems.

Mr R.S. LOVE: So, in terms of risk sharing on that project, you have one section of rail that is completely owned and then you have a section of rail that is a common-user facility.

Mr J. NORBERGER: Underwritten by them.

Mr R.S. LOVE: I was going to say, what is the balance; are you carrying the full risk of that full network in your opinion, or is there a sharing of that risk if, in the event, you cannot actually make the grade?

Mr Harris: We are carrying the full risk of the Karara project, I guess. People argue that that is fair in some respects but when you are looking at putting together an overall project, you have got to have port, rail. It is one package so, again, if you contrast that to a Rio who is doing the whole thing, they can manage that risk, as one package, whereas when you have separated it, you can push the risk one way or the other, so it is a project which is a magnetite iron ore project. Where does the risk sit? It sits with Karara because the others have got take-or-pay bank guarantees. They are de-risked if you think about it. They are all stakeholders in the project; it is where the risk is shared.

Mr R.S. LOVE: But you are carrying the can?

Mr Harris: Carrying more risk, not to say that Brookfield is not carrying any risk—they are.

The CHAIR: With the rail access code 2000, would that assist you with your negotiations for your network access agreement and does it have any function once an agreement has been reached?

Mr Harris: It did not support us in the negotiations and I would add that the final agreement with Brookfield that we reached has an exclusion around being able to use that code in the future. As part of the commercial negotiation, that was one of the outcomes that Karara agreed that it would not revert back to any code in future.

The CHAIR: So your agreement had to have a clause in there saying that you could not use that access code at any point in the future?

Mr Harris: Yes, the agreement also came at the express exclusion of any future right to be treated under the code for the duration of the 15-year agreement, so it is for the duration but, again, it was carving out any potential protection that that code might afford.

[12.20 pm]

Mr F.M. LOGAN: Enforcement of the agreement then would not come back to the original contract between PTA and Brookfield; you would have to enforce it in court as a contract?

Mr Harris: Yes, the agreement is between us and Brookfield and is a commercial agreement and would be enforceable.

The CHAIR: Brookfield is the sole operator of the southern freight rail network and that lease is subject to PTA management. Given your experiences to date, what do you see as PTA's responsibilities in managing that network? Are those responsibilities clear and how do you see them fulfilling those responsibilities?

Mr Harris: I really not had any engagement with PTA and I have not really delved into understanding what the role of PTA is, so I am a bit naive on that question. Really our, I guess, engagement in the relationship is with Brookfield, not with the PTA. I am not aware of any real engagement with the PTA.

Mr F.M. LOGAN: Your agreement overrides it?

Mr Harris: Yes, our agreement is with Brookfield, as I understand it, not with PTA.

The CHAIR: I would like to thank you very much for coming in to talk to us and for your evidence before the committee today. A transcript of this hearing will be forwarded to you for correction of minor errors. Any such corrections must be made and the transcript returned within 10 days from the date of the letter attached to the transcript. If the transcript is not returned within this period, it will be deemed to be correct. New material cannot be added by these corrections and the sense of your evidence cannot be altered. Should you wish to provide additional information or elaborate on particular points, please include a supplementary submission for the committee's consideration when you return your corrected transcript of evidence. There may be some other questions that occur to us. Is it okay if we send those questions to you?

Mr Harris: That is fine.

Hearing concluded at 12.22 pm