

## Aurizon Network 2014 Draft Access Undertaking Response to the Queensland Competition Authority's Consolidated Draft Decision

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26 February 2016



## Table of Contents

Executive Summary .....	6
Context .....	9
Main sources of risk to Aurizon Network emerging from the CDD .....	10
Aurizon Network's Funding Commitment .....	12
Aurizon Network's vision for future regulatory periods .....	13
Chapter 1 – Introduction .....	16
Chapter 2 - Legislative Framework .....	18
Section 138(2) of the QCA Act .....	18
Supply chain coordination .....	19
Pricing principles .....	20
Primacy of commercial negotiations .....	20
Minor and inconsequential changes .....	21
Section 136(5) of the QCA Act .....	21
Non-exhaustive list of matters in QCA's drafting of revisions to UT4 that are beyond the QCA's power .....	22
Chapter 3 – Intent and Scope (Part 2) .....	31
Summary of Aurizon Network's Position .....	31
CDD Part 2 Scope and Intent .....	34
Chapter 4 – Ringfencing (Part 3) .....	41
Summary of Aurizon Network's Position .....	41
Underlying assumptions and principles .....	50
Practical issues with CDD and drafting of Part 3 .....	53
Legal analysis of CDD DAU of Part 3 .....	58
Practical resolution – a revised version of Part 3 .....	73
Testing Aurizon Network's proposal against the QCA Act, QCA improvement suggestions and QCA criteria .....	74
Ultimate Holding Company Support Deed .....	76
Chapter 5 – Reporting, Compliance and Audits (Part 10) .....	80
Summary of Aurizon Network's Position .....	80
CDD 5.1 Maintenance cost reporting .....	83
CDD 5.2 Network performance reports .....	86
CDD 5.3 Asset reporting .....	87
CDD 5.5 Audit requirements .....	89
Chapter 6 – Dispute Resolution and Decision Making (Part 11) .....	91
Summary of Aurizon Network's Position .....	91

CDD Part 6 Dispute resolution and decision making .....	92
Chapter 7 – Negotiation Framework (Part 4) .....	99
Summary of Aurizon Network’s Position .....	99
CDD 7.1 Process for applying for access and negotiating agreements .....	100
CDD 7.2 Providing relevant and accurate information in a timely manner .....	105
Chapter 8 – Access Agreements .....	108
Summary of Aurizon Network’s Position .....	108
Access Agreement and Train Operations Deed .....	111
Chapter 9 – Connecting Private Infrastructure (Part 9) .....	118
Summary of Aurizon Network’s Position .....	118
CDD 9.1 Voluntary inclusion of process for connecting Private Infrastructure .....	120
CDD 9.2 Transparency of process .....	121
CDD 9.3 QCA approach to costs and risks .....	122
CDD 9.4 Standard Rail Connection Agreement .....	123
9.5 – Coal Loss Mitigation Provisions .....	124
Drafting clarifications .....	124
Chapter 10 – Baseline Capacity and Supply Chain Management (Part 7A) .....	125
Summary of Aurizon Network’s Position .....	125
Background to this Part 10 response .....	133
CDD 10.1 Supply chain co-ordination .....	139
CDD 10.2 Capacity analysis .....	139
CDD 10.3 Capacity deficit .....	142
CDD 10.4 System Operating Parameters .....	142
CDD 10.5 Network Development Plan .....	143
Chapter 11 – Available Capacity Allocation and Management (Part 7) .....	146
Summary of Aurizon Network’s Position .....	146
CDD 11.1, 11.2 and 11.18 Reinstatement of the queue and capacity registers .....	153
CDD 11.4 Terms of renewal of access rights .....	155
CDD 11.5 Replacement Mine concept .....	155
CDD 11.8 Customer initiated capacity transfers .....	156
CDD 11.9 – 11.16 Short term capacity transfers .....	156
Chapter 12 – Network Development and Expansion Process (Part 8) .....	162
Summary of Aurizon Network’s Position .....	162
QCA acting beyond powers .....	162
Impractical provisions and adverse risk outcomes of QCA’s proposals .....	163
Aurizon Network’s proposal .....	164
Chapter 13 – Network Management Principles (Schedule G) .....	167

Summary of Aurizon Network's Position .....	167
CDD 13.1 Confidentiality and ring-fencing matters .....	169
CDD 13.2 Strategic Train Plan.....	170
CDD 13.3 Master Train Plan.....	171
CDD 13.4 Intermediate Train Plan .....	171
CDD 13.5 Train Service Entitlement reconciliation reports .....	172
CDD 13.6 System Rules governance .....	172
CDD 13.7 Other matters .....	172
Other Matters.....	173
Chapter 14 – Regulatory Asset Base and Customer Voting .....	174
Summary of Aurizon Network's Position .....	174
Aurizon Network's asset stranding risk .....	180
CDD 14.1 Maintenance of the RAB .....	189
CDD 14.2 Capital expenditure approval process .....	192
CDD 14.3 Asset Management Plan .....	197
CDD 14.4 Purpose and Application of the Customer Vote.....	197
CDD 14.5 - Interested Participants .....	198
CDD 14.7 - Voting and Acceptance Process .....	199
CDD 14.8 Information Provided to Interested Participants.....	200
CDD 14.9 Compliance and Audit Provisions.....	200
Other issues .....	201
Chapter 15 – Pricing Arrangements for Rail Access .....	203
Legislative framework for pricing arrangements.....	203
Review of pricing arrangements .....	205
Chapter 16 – Pricing Principles (Part 6).....	206
Summary of Aurizon Network's Position .....	206
Aspects of the CDD that are beyond power .....	213
CDD 16.1 Price Differentiation.....	216
CDD 16.2 Coal carrying train services .....	217
CDD 16.4 Pricing Limits.....	219
CDD 16.5 Price differentiation and pricing limits .....	219
CDD 16.6 Principles underpinning the expansion pricing framework.....	221
CDD 16.7 Process for approval of expansion pricing arrangements.....	222
CDD 16.8 Process for establishing expansion pricing arrangements.....	224
CDD 16.9 Endorsed Expansions .....	227
CDD 16.10 Socialisation between expanding users .....	228
CDD 16.12 Expansions funded by Aurizon Network at the regulatory WACC .....	229
CDD 16.13 Mine-specific spur lines .....	229
CDD 16.14 Commercial terms .....	230

Chapter 17 – Reference Tariffs (Part 6, Schedule F) .....	232
Summary of Aurizon Network’s Position .....	232
CDD 17.1 Reference Tariff arrangements .....	235
CDD 17.2 Allocation of GAPE project costs to the Newlands system .....	236
CDD 17.3 New Reference Tariff arrangements .....	236
CDD 17.4 Reference train service characteristics.....	237
CDD 17.5 Revenue cap adjustments.....	238
CDD 17.6 Reference Tariff variation events.....	241
Chapter 18 – Reference Tariffs for WIRP Train Services.....	243
Summary of Aurizon Network’s Position .....	243
CDD 18.1 CRIMP in the context of WIRP .....	246
CDD 18.2 WIRP access conditions.....	246
CDD 18.3 Applicable access undertaking.....	247
CDD 18.6 Allocation of capital expenditure to non-WIRP users.....	247
CDD 18.8 Volumes for WIRP train services.....	249
CDD 18.9 Assessment of WIRP pricing options .....	250
CDD 18.10 Pricing arrangements for WIRP train services in Blackwater.....	250
CDD 18.11 WIRP train services in Moura.....	251
Chapter 19 – Take or Pay Arrangements (Schedule F) .....	253
Summary of Aurizon Network’s Position .....	253
CDD 19.2 - Potential inequities between different Take or Pay arrangements.....	254
CDD 19.3 Other specific drafting .....	255
Chapter 20 – Maximum Allowable Revenue .....	256
Summary of Aurizon Network’s Position .....	256
CDD 20.1 QCA’s proposed Maximum Allowable Revenue .....	258
CDD 20.2 Transitional matters relating to UT4 MAR.....	267
Chapter 21 – Volume Forecasts .....	269
Summary of Aurizon Network’s Position .....	269
CDD 21.1 Volume Forecasts .....	269
Summary .....	270
Chapter 22 – Operating Costs .....	272
Summary of Aurizon Network’s Position .....	272
CDD 22.1 System wide and regional costs.....	276
CDD 22.2 Corporate overheads .....	278
CDD 22.3 Risk and insurance.....	280
CDD 22.4 Audit and condition-based assessment.....	281
Chapter 23 – Maintenance Costs .....	282

Summary of Aurizon Network's Position .....	282
CDD 23.1 Direct maintenance costs .....	283
CDD 23.2 Indirect maintenance costs.....	284
Chapter 24 – Ballast Undercutting Costs .....	287
Summary of Aurizon Network's position .....	287
Introduction.....	288
CDD 24.1 Ballast Undercutting Scope .....	290
CDD 24.2 Ballast Undercutting Costs .....	297
CDD 24.3 Ballast Impairment Charge .....	309
Part 25 – Opening Asset Value.....	310
Summary of Aurizon Network's Position .....	310
CDD 25.1 Opening Asset Value .....	311
CDD 25.2 Equity Raising Costs .....	311
Part 26 – Regulatory Asset Base (including capital expenditure).....	313
Summary of Aurizon Network's Position .....	313
CDD 26.1 Forecast capital expenditure .....	314
CDD 26.2 Capital expenditure carryover account.....	316
CDD 26.3 RAB roll-forward FY2014 .....	316
Chapter 27 – Return of Capital .....	318
Summary of Aurizon Network's Position .....	318
CDD 27.1 Return of capital .....	318
Summary .....	319
Part 28 – Return on Investment.....	320
Summary of Aurizon Network's position .....	320
Comparison to AER Decisions.....	322
CDD 28.1 Risk-free Rate .....	324
CDD 28.4 Debt Risk Premium .....	324
CDD 28.7 Market Risk Premium.....	325
CDD 28.9 Equity Beta.....	325
CDD 28.10 Gamma .....	326
Chapter 29 – Approach to Modelling.....	327
Summary of Aurizon Network's Position .....	327
Amendments to the Post Tax Revenue Model.....	328
Glossary .....	331

## Executive Summary

Aurizon Network welcomes the opportunity to submit this response to the Queensland Competition Authority's (QCA's) Consolidated Draft Decision (CDD).

Aurizon Network has provided a response to all Consolidated Draft Decision. In an attempt to progress to a Final Decision by April 2016, Aurizon Network's has in some cases been prepared to agree with the QCA on positions where the outcome is sub-optimal however it could operate within those obligations. The following table provides a high-level summary of Aurizon Network's positions:

Aurizon Network Position	Number of Decisions
Agree	120
Agree with Amendment	81
Disagree	113
<b>Total Number of QCA Draft Decisions</b>	<b>314</b>

A major component of the 2014 Access Undertaking is the Maximum Allowable Revenue (MAR). Aurizon Network has agreed with a range of positions outlined within the QCA's CDD. These agreed positions includes the Return of Capital and the Weighted Average Cost of Capital (WACC) of 7.17%.

The key areas where Aurizon Network does not agree with the QCA's CDD include:

- the QCA's proposed ballast undercutting allowance – the methodology to construct this allowance is incorrect and would severely impact the running of coal train services; and
- WIRP revenue deferral of capital expenditure – Aurizon Network is seeking a definitive sunset date for this deferral of 30 June 2017.

Upon review of the CDD and supporting material, Aurizon Network did also identify a number of errors in the QCA's calculations that when corrected, have impacted the individual building blocks and the MAR.

A summary of Aurizon Network Maximum Allowable Revenue position is outlined below:

Cost	QCA CDD	Aurizon Network submission	Difference	Reason for change
Return on Capital	1,533	1,532	(1)	Aurizon Network proposed to defer capital relating to GAPE Remote Control Signalling for pricing purposes
Inflation	(522)	(519)	3	
Depreciation	1,268	1,300	32	The QCA has incorrectly applied the UT2 asset lives when calculating the RAB roll-forward. This has resulted in the QCA understating depreciation in the CDD

Cost	QCA CDD	Aurizon Network submission	Difference	Reason for change
Maintenance	800	824	24	\$20m increase in Ballast and \$4m from the inclusion of Return on Inventory
Operation Costs	805	814	9	Adjustments for Train Control, business management costs and Audit Costs.
Working Capital	12	12	0	
Tax and imputation credits	141	150	9	Aurizon Mid-year timing assumption applied to tax depreciation
Capital carryover	(110)	(125)	(15)	The QCA has not deferred capital relating to NAPE and instead has included total GAPE capex in the Capital carryover account.. Aurizon Network have deferred NAPE.  Mid-year timing assumption applied by Aurizon Network
<b>Total MAR</b>	<b>3,927</b>	<b>3,989</b>	<b>62</b>	

Aurizon Network remains committed to the timely completion of UT4 in order to provide it and its industry stakeholders with some certainty in what remains an extremely challenging market environment. It anticipates a Final Decision by April 2016, as the QCA has indicated. Having regard to this imperative, there are a number of areas in the CDD where Aurizon Network has significant concerns with what the QCA has proposed, including (but not limited to), aspects of its Maximum Allowable Revenue (MAR), however has been willing to accept the QCA's proposal for the UT4 period in order to reduce the risk of further delays.

The scope and complexity of some of the further changes proposed by the QCA in the CDD has made it challenging for Aurizon Network (and it would expect, other stakeholders) to give them full and detailed consideration. However, with these time constraints in mind, it has sought to comprehensively respond to the CDD, focussing on its residual areas of disagreement. It is these issues that are the focus of this submission.

Aurizon Network retains fundamental concerns that a number of the QCA's decisions extend beyond its powers under the *Queensland Competition Authority Act 1997* (the QCA Act), noting that such concerns were expressed in its previous response to the QCA's Initial Draft Decision (IDD). Aurizon Network has address this in the following section.

In Aurizon Network's view, the CDD constitutes a prime example of regulatory over-reach and clearly embodies the problems identified by the Exports and Infrastructure Taskforce in the report it presented to the Commonwealth Government over a decade ago which is still relevant to today:<sup>1</sup>

*The greatest impediment to the development of infrastructure necessary for Australia to realise its export potential is the way in which the current economic regulatory framework is structured and administered. It is adversarial, cumbersome, complicated, time consuming, inefficient and subject to gaming by participants...*

*The manner in which regulators have approached their task has compounded the difficulties. A quest for 'first best' solutions, combined with a focus on removing monopoly rents, has distracted from what should be the regulatory task: which is not to determine whether what has been proposed by way of access conditions is optimal, but whether it is reasonable.*

This is not only a concern about the QCA extending beyond the boundaries of its powers under the legislation, although in Aurizon Network's view, this is a reason why some decisions are clearly inefficient and/or unworkable. It is about decisions that will undermine the efficient utilisation of, and investment in, the network, potentially distort competition, stifle innovation and reduce the efficiency of the entire supply chain. This comes at a time when the industry can least afford it – Aurizon Network needs to be able to adapt and respond to the changing demands of its customers and operating environment, while still having regard to its obligations under the QCA Act.

Aurizon Network submits that the CDD amended Draft Access Undertaking (DAU) extends well beyond the economic problem that regulation was designed to solve, which was recently highlighted by the Productivity Commission (PC), that of a "lack of effective competition".<sup>2</sup> A number of changes in the CDD lack clear rationale and in many cases it is evident that the practical consequences of a change – both intended and unintended – have not been fully thought through. Indeed, as will be highlighted in this response, there are a number of requirements that Aurizon Network may be unable to implement, or can only do so after expending significant time, resources and costs. There is very little evidence to suggest that the QCA has undertaken any form of cost-benefit analysis in proposing material changes, with the PC highlighting the importance of such analysis in its most recent review of the National Access Regime.<sup>3</sup>

Aurizon Network is also concerned that where it has sought to propose new mechanisms to address an identified problem and/or improve the operation of the network, the QCA has fundamentally altered the proposal based on what is largely a theoretical perspective, rather than a practical understanding of the complexities of network operations (a case in point being the short term transfer mechanism, which as noted above, Aurizon Network originally agreed with the QRC). It has also extended voluntary obligations proposed by Aurizon Network, such as applying its ringfencing obligations to any ports that it could seek to own, to mines.

Accordingly, there are therefore a number of positions in the CDD that Aurizon Network cannot accept as it considers it would be placed in an untenable position, either because it would expose Aurizon Network to an unacceptable level of risk or be required to comply with obligations that are practically unworkable.

A key example of this is the Short Term Transfer Mechanism. Aurizon Network worked constructively with the industry in order to develop an effective and workable mechanism that will provide access holders (and end users) with more flexibility in managing their capacity entitlements, which is even more essential in the current market environment. The QCA has made a number of material amendments to this

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<sup>1</sup> Exports and Infrastructure Taskforce (2005). Australia's Export Infrastructure, Report to the Prime Minister, Canberra, May. p.2.

<sup>2</sup> Productivity Commission (2013). National Access Regime, Inquiry Report no. 66, Canberra, p.6.

<sup>3</sup> Productivity Commission (2013). pp.10-11.

framework that in Aurizon Network's view, undermine its workability and effectiveness. Other examples of where the QCA has overturned positions agreed with the Queensland Resources Council (QRC) include (but are not limited to) the expansion framework, the ten year expiration of expansion tariffs and the requirement to align the terms of renewed access agreements with the prevailing Standard Access Agreement.

Aurizon Network also makes it clear that it intends to continue to seek to work constructively with stakeholders in relation to key issues identified in this submission between its lodgement and the release of the Final Decision (and beyond).

## Context

The environment remains extremely challenging for all Central Queensland Coal Region (CQCN) participants. Coal prices remain low, with producers under significant continued pressure to reduce costs. In some cases, this has seen mine closures. The global economic outlook remains uncertain and remains heavily dependent on the outlook for China. World financial markets continue to be highly volatile with concerns around the emergence of another financial crisis. Overall, however, Aurizon Network continues to have confidence in the long-term future of the coal industry it services.<sup>4</sup>

With the UT4 review process now extending well past the original expiration date for UT3, Aurizon Network has continued to invest in, and maintain, the network despite being in an uncertain regulatory position as to whether it will be able to recover its costs. Aurizon Network continues to work hard to respond to the challenges presented by its environment and optimise the efficient utilisation of, and investment in, the network infrastructure.

As part of its Draft Decision on the 2014DAU, the QCA published a revised DAU (the CDD amended DAU) which amended the 2014DAU submitted by Aurizon Network for approval.

A comparison between the QCA's CDD amended DAU and the version submitted for approval by Aurizon Network reveals that the QCA has changed virtually every single provision of Aurizon Network's 2014DAU. All but a few of the 565 pages of the QCA's CDD amended DAU show mark-ups against Aurizon Network's 2014DAU. It seems highly improbable that virtually none of the 2014DAU submitted by Aurizon Network was "appropriate" to approve. The QCA's approach to the 2014DAU is not in Aurizon Network's view a proper exercise of the QCA's powers and functions

In the first six months of FY2016, Aurizon Network has continued to set a number of operational and performance records, including:

- record volumes of 19.6 million tonnes in January, with all-time record volumes for the Goonyella system;
- delivering 114 million tonnes resulting in a 2% increase in net tonne kilometres (NTKs);
- a 2.1% increase in average payloads with 2.4% fewer services;
- a 10.9% decrease in below rail delays;
- a 1.5% reduction in system closure hours; and
- a 63% in cancellations due to a below rail cause. .

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<sup>4</sup> Refer: Aurizon (2014). Aurizon Beyond 2020, Sustainability Report 2014.

## Main sources of risk to Aurizon Network emerging from the CDD

Aurizon Network commenced the UT4 review process wanting a clear, workable and predictable regulatory framework that incentivises efficient commercial and economic outcomes, which are best achieved by being able to work constructively in partnership with customers. Aurizon Network also sought to improve its engagement with customers as part of the undertaking review process and was able to negotiate and agree a number of positions with the QRC. As noted above, Aurizon Network remains extremely concerned that the QCA has sought to reject or amend positions negotiated with the QRC and this only serves to highlight its exposure to regulatory risk.

Overall, the three exposures emerging from the CDD that are of most significant concern to Aurizon Network are as follows.

### 1. Operational risks

This submission identifies a number of provisions proposed in the QCA's CDD amended AU that are either:

- unworkable, that is, Aurizon Network will simply be unable to comply with the provision (or is uncertain if it will be able to comply, noting that some of the provisions are unclear) (for example, this includes aspects of the ringfencing provisions, negotiation framework and the Network Management Principles);
- inefficient, that is, the provision either:
  - constrains necessary flexibility (for example, ringfencing, the expansion pricing framework and the Network Management Principles);
  - results in an inappropriate allocation of risk (for example, revenue deferrals and aspects of the expansion framework);
  - constrains/deters innovation and risk taking, and instead shifts the focus to risk reduction and compliance (for example, subjecting non-standard agreements to the access conditions regime, which could require publication of matters subject to a non-standard agreement, such as an operator trial of a new rollingstock solution or technology); and/or
  - will impose costs that outweigh the benefits (noting that in some cases no clear benefit from the change has been demonstrated).

Examples of these include:

- The Train Operations Dead requires Aurizon Network to notify Operators where Aurizon Network is aware of a circumstance that could impact it meeting its schedule +/- 3 minutes. Analysis has shown that this would require over 700 phone calls per day to operators. Aurizon Network cannot comply with this without incurring substantial costs.
- The definition of confidential information and ringfencing provisions, prevents Aurizon Network from seeking its independent board approval of regulatory submission.

These operational risk will have a number of adverse consequences for Aurizon Network. First, it will increase its exposure to regulatory and/or commercial risks if it is unable to comply with an obligation. Second, it provides Aurizon Network with very limited regulatory certainty. The CDD amended DAU has had added complexity included by the QCA which results in it being unclear. This will similarly be an issue for access seekers and holders who also need to be able to understand their rights under the framework.

Third, it will prevent Aurizon Network from being able to flexibly respond to the changing needs of its customers, which is essential in such a complex and challenging market environment. Ultimately, this will be to the detriment of Aurizon Network's customers and the supply chain, at a time where the imperative for improving efficiency and competitiveness is more important than ever.

Finally, it exposes Aurizon Network to cost risks over the UT4 period. As outlined in Chapter 20 of this response, Aurizon Network anticipates that the CDD will require a material increase in resources and

costs. At this stage, it is difficult to predict the full impact on Aurizon Network's 'business as usual' costs (noting that some of these arise from processes that may (or may not) be triggered under the undertaking). It is also difficult to predict the full extent of developing, finalising and implementing key processes such as the Standard User Funding Agreement (SUFA).

## **2. Regulatory Asset Base Valuation risks**

The CDD also presents risks to the value of the business. One of the most significant is the increase in regulatory risk, which is always a source of concern for investors.

The constraints on Aurizon Network's flexibility will also discourage it from pursuing value-adding growth opportunities and/or being rewarded for risk-taking and innovation. As noted above, it has material issues with the QCA's proposed expansion framework and is concerned that it is more likely to hinder development than promote it. It also considers that aspects of the expansion pricing framework and customer voting process are unreasonably balanced in favour of incumbent users, at the expense of access seekers. This will deter entry and constrain the growth of the Central Queensland Coal Region (CQCR). Aurizon Network would expect that this could also be a source of concern for the State, given development of the CQCR's abundant high quality coal resources remains an essential contributor to its economic prosperity and is therefore strongly in the public interest.

The deterioration in market conditions that has occurred since UT3 was approved in 2010 has also highlighted what Aurizon Network considers to be its main source of valuation risk, which is asset stranding. The CDD continues to constrain Aurizon Network's flexibility in implementing mechanisms to manage these risks and exposes it to additional risks (for example, its decision to apply revenue deferrals with no sunset date). Apart from jeopardising its ability to recover its efficient costs (as required under section 168A(a) of the QCA Act), this, along with Aurizon Network's concerns with the expansion framework, will ultimately reduce Aurizon Network's investment incentives and hence fail to promote efficient investment in the network as required under section 69E of the QCA Act. Aurizon Network's asset stranding risk is discussed in more detail in Part 14 of this response.

The CDD also presents valuation risk to industry participants, which could arise from sub-optimal risk allocation, discouraging network growth and development, discouraging new entry and impeding producers' flexibility in optimising their own supply chain solutions to the extent that Aurizon Network is constrained in how it can respond to them. Mine closures also present an ongoing source of risk to existing users and the wider supply chain.

The QCA, in its CDD has altered the risk position on this, via the following examples:

- Reduction in Pricing Flexibility – this includes certain constraints on Aurizon Network's ability to allocate costs to other users under the expansion pricing framework
- The removal of Aurizon Network's ability to re-order its capacity queue to favour longer term contracts

## **3. QCA operating beyond its Statutory Powers**

Aurizon Network raised serious concerns within its response to the IDD published by the QCA in January 2015. These concerns related to whether the QCA was making those decisions in line with its statutory powers.

As mentioned above, the QCA has proposed changes to virtually every provision of the 2014DAU submitted by Aurizon Network for approval. In a very significant number of cases the QCA's proposed changes comprise either:

## **1. Changes and additions to matters volunteered by Aurizon Network that the QCA does not have power to require.**

The QCA appears to justify its position on the basis that section 136 of the QCA Act requires the QCA to consider the Undertaking given to it for approval and, if the Undertaking is refused, to provide reasons and a notice of the way in which it is appropriate to amend the Undertaking for it to be approved<sup>5</sup>.

When the QCA is considering whether an Undertaking is “appropriate” and the way in which a voluntary Undertaking should be amended, the QCA should take into account whether the elements that the QCA proposes to change are in fact matters that are not required by the QCA Act at all. In Aurizon Network’s submission it is not “appropriate” to require amendments to matters that were volunteered beyond the scope of the QCA Act. The QCA cannot regulate what is not regulated by the QCA Act.

In any case, the QCA’s approach is inefficient because:

- it encourages access providers to only ever offer what is strictly required by the QCA Act and no more – which cannot be in the public interest; and
- ultimately, the QCA can never draft and approve its own form of Undertaking for an access provider to regulate matters that are not required by the QCA Act, whether or not the access provider had previously volunteered such matters.

## **2. New provisions that go beyond the QCA Act –**

The QCA cannot ultimately impose on an access provider any matter that it has no power to require. In the case of the QCA’s CDD amended DAU, the list of matters beyond scope is extensive and are set out in Chapter 2 of this response. This section has been provided by way of illustration and is a non-exhaustive list of those matters. It only addresses changes and new provisions drafted by the QCA.

Aurizon Network has identified a range of examples that it has outlined within this submission, however for illustration purposes has outlined two below:

- Requires Aurizon Network to procure electric energy for train operators – this is a voluntary arrangement and does not form part of the declared service. The purchase of electricity falls under a different regulator
- Aurizon Network must participate within Supply Chain groups and implement action items - The Supply Chain Groups and their participation does not form part of the declared service. Aurizon Network should therefore not be bound to participate or implement actions items from such groups

## **Aurizon Network’s Funding Commitment**

In September 2013, Aurizon Network wrote to, and held discussions with, the QRC relating to its objectives and commitments to invest in expanding the CQCN. As part of that correspondence, Aurizon Network outlined:

- a range of scenarios and projects that it was prepared to fund at the regulated WACC;
- that during the UT3 period ending 30 June 2013, it had invested approximately \$800million at the regulated WACC in growth-specific projects; and

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<sup>5</sup> QCA, 2015, paragraph 9.4.3

- that it was committed to spending approximately \$900million during the term of the 2014DAU on growth related projects.

Since the discussions with the QRC in 2013, the marketplace for expansions to the CQCR has fundamentally changed. Aurizon Network did offer to complete studies on those scenarios, however stakeholders were conscious about extra costs and agreed not to pursue them any further.

In August 2014 as part of the re-submission of the DAU, Aurizon Network outlined that it would consider a funding commitment once the QCA's MAR has been assessed and Aurizon Network's ability to fund such expansions has been considered. Due to the nature of the QCA's splitting of its policy and revenue decisions, this assessment was not practical at that time.

Across Australia commercial organisations are focussed on, or operating within, a capital constrained environment where capital must be allocated to the area of greatest return (having regard to the relevant risks). Aurizon Network's investors expect it to apply this principle when considering investment in the CQCR. A funding commitment at the commencement of a regulatory cycle results in capital being locked into an unknown transaction that may not meet shareholder objectives. This position is amplified in a capital constrained market.

Although Aurizon Network and its investors are not willing to provide a funding commitment, Aurizon Network is still demonstrating its promise of investing in the CQCN by investing \$1.8billion<sup>6</sup> of its capital over the term of the 2014DAU commencing 1 July 2013. Of this amount, Aurizon Network has committed to invest over \$1billion at the regulated return. This investment commitment is delivered through the application of the capital indicator.

Being two years into the term of the 2014DAU, Aurizon Network has already committed capital, delivered growth and renewal projects and subsequently submitted two capital claims for the QCA's approval under the prudency assessments process. These claims have a combined total capital value of \$940million. Of this capital expenditure amount, approximately 60% were for growth-related projects and the remainder for renewal investment.

Aurizon Network will continue to deliver these projects, without a specific voluntary funding commitment.

## Aurizon Network's vision for future regulatory periods

Aurizon Network is in complete agreement with the following statement made by the QCA in the CDD:<sup>7</sup>

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**We consider that this changing market environment, and the challenges it presents for all parts of the supply chain, points to a need for a critical review of the way in which third-party access is considered for the CQCN.**

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<sup>6</sup> Aurizon Network has outlined its detailed response positions relating to the capital indicator within section 26 of this response document.

<sup>7</sup> Queensland Competition Authority (2015). Consolidated Draft Decision: Aurizon Network 2014 Draft Access Undertaking, Volume I – Governance and Access, p.viii.

The concern is whether the UT4 framework will achieve this – in Aurizon Network’s view it could have the opposite effect.

Aurizon Network continues to support the need for a clear, workable and predictable regulatory framework that incentivises efficient commercial and economic outcomes, which are best achieved by where Aurizon Network can work constructively in partnership with its customers and adapt and respond to the changing demands presented by this dynamic and challenging environment.

Consistent with the recommendations of the Productivity Commission, Aurizon Network’s regulatory framework needs to effectively target the economic problem it was designed to solve, which is a “lack of effective competition”. It should not extend beyond addressing that problem, or the requirements of the QCA Act.

As the regime continues to develop and evolve in the future, in Aurizon Network’s view, any changes should be substantiated based on how and why they are necessary to addressing the economic problem. Where feasible, this should be supported by evidence to demonstrate that there is a clear source of failure under the current framework. Consistent with recommendations made by the PC<sup>8</sup>, the benefits of any proposed change should be clearly articulated and should outweigh the associated costs.

The UT5 review will need to commence shortly. Consistent with the environment underpinning the UT4 development process, the focus remains on improving the efficiency and productivity of the supply chain, effectively managing risk (such as asset stranding) and reducing costs. The key areas of focus for UT5 include, but are not limited to:

- asset stranding risk;
- improving operational efficiency and flexibility, including where required, ‘fine tuning’ new processes such as the short term transfer mechanism;
- continue to improve data transparency on the operation of the CQCN;
- ensuring the regulatory framework supports innovation;
- undertaking a comprehensive review of Aurizon Network’s pricing arrangements;
- enhancing and implementing the expansion framework, including finalising the Standard User Funding Agreement;
- optimising the allocation of available capacity;
- ongoing implementation of a best practice approach to managing ballast fouling; and
- setting a rate of return that is commensurate with investors’ expectations for a stand alone coal network business.

Some of the items listed above are ideas raised by industry and some are directly from Aurizon Network. As with previous commitments made, prior to progressing any regulatory matter Aurizon Network will engage with stakeholders to understand the importance of the matter and understand individual positions, with a view to achieving common ground where possible.

Aurizon Network would welcome the involvement of the QCA in any consultation processes, to assist with its understanding and expectations of the relevant matter, which will ultimately lead to more timely and relevant decisions.

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<sup>8</sup> Productivity Commission (2013). pp.10-11.

Aurizon Network supports an efficient and timely access undertaking review process with opportunities for effective stakeholder consultation. It needs to maximise the incentive for Aurizon Network and industry stakeholders to achieve consensus, which can only be done if there is a high degree of confidence that those positions will not subsequently be overturned by the regulator, provided any such positions have regard to the relevant requirements under section 138 of the QCA Act.

## Chapter 1 – Introduction

Aurizon Network welcomes the opportunity to submit this response to the Queensland Competition Authority's (QCA's) Consolidated Draft Decision (CDD).

The CDD proposed a number of material changes from the QCA's Initial Draft Decision (IDD), which necessitated this final round of consultation. The scope and complexity of some of these changes proposed by the QCA in the CDD has made it challenging for Aurizon Network (and it would expect, other stakeholders) to give them full and detailed consideration in the timeframes available. It has also necessitated the preparation of a longer and more detailed response than Aurizon Network would have initially envisaged.

Aurizon Network is prepared to agree with a large number of the proposals contained in the CDD. The focus of this submission is on those decisions where Aurizon Network disagrees. Where Aurizon Network is prepared to agree with a proposal but requires amendments to the drafting, it has provided a short explanation of this in this response. In many cases, Aurizon Network's position on matters remains unchanged from its response to the QCA's IDD lodged in April 2015<sup>9</sup>. Instead of repeating arguments in detail, this previous response is incorporated in relevant parts of this submission by reference where indicated.

In the limited time available but in the interests of moving forward and communicating positions, Aurizon Network has been unable to finalise its proposed amendments on the complete Access Undertaking. The draft parts that have been completed are set out below. Completed drafts of the remaining sections are to follow. Aurizon Network would welcome the opportunity to discuss any aspects of this response with the QCA, including its proposed amendments, prior to its Final Decision.

This submission is presented in three Volumes:

- **Volume 1** contains Aurizon Network's response to the CDD
- **Volume 2** contains revised drafts of the following, marked up against the QCA's CDD amended Draft Access Undertaking (DAU) published on the 16<sup>th</sup> of December 2015:
  - Part 2: Intent and scope
  - Part 3: Ringfencing
  - Part 4: Negotiation framework
  - Part 11: Dispute resolution and decision making
  - Schedule A: Preliminary, additional and capacity information
  - Schedule B: Access application information requirements
  - Schedule C: Operating plan requirements (interface risk provisions only)
- **Volume 3 contains material in relation to Access Agreements, including:**
  - Appendix 1: A summary table of Aurizon Network's proposed amendments to the Access Agreement and Train Operations Deed
  - Appendix 2: Access Agreement – Coal (mark up)
  - Appendix 3: Train Operations Deed (mark up)

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<sup>9</sup> Aurizon Network (2015a). 2014 Draft Access Undertaking: Aurizon Network Response to Queensland Competition Authority's Draft Decision on Policy and Pricing Principles, April.

- Appendix 4: “Incorporated Provisions” that Aurizon Network proposes are included in the Access Agreement or Train Operations Deed (as appropriate). This includes Aurizon Network’s mark up of relevant provisions of Part 7 and Schedule C of the CDD amended DAU.
- Appendix 5: Revised Draft of Part 5 (Access Agreements) of the QCA’s CDD amended DAU.

## Chapter 2 - Legislative Framework

This section of Aurizon Network’s submission responds to Section 2 of the QCA’s draft decision dealing with the legislative framework which governs the QCA’s role in considering draft access undertakings for approval or refusal.

### Section 138(2) of the QCA Act

In various places throughout the draft decision and, in particular in section 2.4, the QCA argues that, in respect of section 138(2) of the QCA Act:

- *the QCA is required to “balance” the competing interests arising from the factors to which it must have regard under section 138(2) of the QCA Act and to make “value judgements” as to those factors;*
- *the QCA is required to apply a “relative weighting” as between those factors;*
- *the QCA is to:*
  - *“...consider the identified factors, rather than treat them as fundamental elements in the decision-making process, provided that consideration of the factors is a ‘jurisdictional prerequisite’ to the making of the decision.”<sup>10</sup>*
- *The QCA Act does not give any “statutory or contextual indication of the weight to be given to factors to which the decision-maker must have regard” and that therefore “it is generally for the decision-maker to determine the appropriate weight to be given to them”.<sup>11</sup>*

The QCA’s interpretation of its obligations in relation to section 138(2) is fundamentally at odds with the law.

Contrary to the QCA’s view, the factors in section 138(2) are unequivocally “*fundamental elements in the decision-making process*” and it is not enough to simply treat them as a “*jurisdictional prerequisite*” which once satisfied allows the QCA to make any decision that it believes is “appropriate”.

Section 138(2) requires that the QCA have regard to each of the factors and must be satisfied that the draft access undertaking is appropriate in respect of each of those factors.

Contrary to the QCA’s assertion, the QCA Act does give statutory and contextual indication of the weight to be given to some of the factors in section 138(2). For example, the list in section 138(2) refers to the object of Part 5 of the QCA Act and the pricing principles in section 168A. It is not clear on what basis the QCA asserts that it can give the objects of Part 5 little or no weight if it chooses to do so or to treat the object as less important than any other factor.

The QCA Act gives numerous “contextual indications” that the pricing principles are fundamental and must be adhered to – see for example, sections 100(4), 138A(2) and 168C. If it were otherwise, on the QCA’s reasoning it would be possible for the QCA to make a decision that would force an access provider to provide a declared service at a loss.

The QCA’s claim in section 2.4.3 that “*the explanatory material for the QCA Act [does not] prescribe the relative weight to be given to each factor*” is patently incorrect.

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<sup>10</sup> QCA’s draft decision, section 2.4.2.

<sup>11</sup> QCA’s draft decision, section 2.4.3.

The object of Part 5 and the pricing principles were both inserted under the *Queensland Competition Authority Amendment Act 2008* (Qld) as part of national reforms arising out of COAG. The relevant explanatory notes state that:

*“The inclusion of an objects clause and uniform pricing principles will provide overriding guidance for the Authority and Ministers in making regulatory decisions under the access regime in the Act.*

*The same clause and principles will be applied to all jurisdictions’ access regimes which will promote national consistency in regulatory practice, contribute to consistent and transparent regulatory outcomes and increase certainty for investors, access providers and access seekers which will benefit infrastructure investment.”*

The QCA’s approach to section 138(2) ignores the “overriding guidance” that Parliament expressly intended for the object clause and the pricing principles.

Given these facts, the QCA is simply wrong when it says it can apply whatever weight it wants to the factors in section 138(2) and that simply having regard to them is enough as they are not fundamental elements in the decision-making process.

As a consequence, the QCA’s decision is built entirely on a false premise.

## Supply chain coordination

The QCA states at section 2.5.1 that:

*“We are of the view that supply chain coordination is a key element of the object of Part 5 of the QCA Act. In the absence of instituting a regime for effective coordination, the 2014 DAU would fail to promote a critical aspect of the efficient operation of, use of and investment in, the QCN.”*

In reliance on this proposition, the QCA’s decision in various places:

- imposes on Aurizon Network a supply chain coordination role;
- regulates Aurizon Network as if it is responsible for the provision of that service; and
- requires Aurizon Network to submit itself to the decisions of supply chain participants.

The service declared under section 250(1)(a) of the QCA Act is not a supply chain coordination service. The declared service is in fact *“the use of a coal system for providing transportation by rail”*.

Whatever the object of Part 5, the QCA cannot rely on that object to require Aurizon Network to be responsible for supply chain coordination or to subordinate its interests to the interests of other elements of a supply chain.

Aurizon Network has no issue with providing information to allow participants in the supply to have information necessary to make informed coordination decisions. However, the detail contained within the draft decision, including the QCA’s proposed drafting for the access undertaking, goes much further.

In short, the QCA cannot treat supply chain coordination as part of the declared service.

## Pricing principles

In addition to our submissions above, we note that at section 2.9.5 of the QCA's draft decision the QCA states:

*“As discussed at Section 2.9.1 above, in assigning a weight to the various factors in section 138(2) and balancing the various competing considerations, we are able to at our discretion conclude that other factors (e.g. the interests of access seekers and/or the public interest) deserve greater consideration than another factor (e.g. the pricing principles).”*

This paragraph of the draft decision indicates that the QCA has an unqualified discretion to decide that, for example, the interests of an access seeker dictate that the access provider must receive less than its efficient cost of providing the service.

The clear effect of the QCA's view is that in some circumstances the QCA can expect access providers to subsidise business operations in upstream or downstream markets. That is an extreme view and completely unsupported by anything in the QCA Act. If Parliament had intended for access providers to subsidise businesses in upstream or downstream markets it would have needed to say so in express terms.

As stated previously, the QCA Act through various provisions and supported by the explanatory notes relating to the introduction of section 168A require the QCA to ensure that the price for access satisfies the pricing principles. The QCA cannot *“conclude that other factors... deserve greater consideration than... the pricing principles”*.

Aurizon Network also notes the comments in section 2.18.2 in particular the statement that:

*“...a cost allowance greater than efficient costs while possible, is inconsistent with the remaining pricing principles (s. 168A(b), (c) and (d)).”*

The QCA's statement is incorrect.

The pricing principles in section 168A(b) to (d) are not inconsistent with section 168A(a). For example:

- the principle that the price for access should provide incentives to reduce costs does not mean that an access provider should not recover at least its efficient costs; and
- allowing price discrimination to aid efficiency has no bearing on whether an access provider should get at least its efficient cost.

## Primacy of commercial negotiations

The QCA states at section 2.10.3:

*“The third party access regime in the QCA Act is underpinned by a 'negotiate–arbitrate' approach to regulation, with the regime incorporating the principle of the 'primacy of contractual negotiations'.”*

Aurizon Network agrees with the QCA's statement, in particular with the principle of the primacy of commercial negotiations. However, Aurizon Network notes that throughout the QCA's proposed amendments to the draft access undertaking the QCA acts inconsistently with this principle. For example, the QCA's drafting includes circumstances in which:

- the QCA gives itself jurisdiction to determine the appropriateness of access conditions agreed between the parties;

- the QCA's prior approval is required for Aurizon Network to seek to negotiate and agree access charges; and
- the QCA's approval is required for an access charge that has been agreed between Aurizon Network and an access seeker.

The QCA's drafting is irreconcilable with the principle that the QCA says underpins the third party access regime in the QCA Act.

## Minor and inconsequential changes

The QCA states at section 2.10.6 that it "accepts" that it:

*"...cannot refuse to approve a draft access undertaking only because we wish to propose amendments that would have no real effect or consequence."*

and that:

*"...simplification of individual clauses for inconsequential reasons, such as a simple drafting preference without any other purpose, would not be consistent with section 138(5) of the QCA Act."*

Despite these statements the QCA has proposed countless amendments to the draft access undertaking which on any objective view would be considered contrary to these principles. To cite a few examples:

- Aurizon Network's "20 Business Days" has been changed to "twenty (20) Business Days". (This number changing occurs throughout the QCA's drafting.);
- "Aurizon Network will" has been changed to "Aurizon Network must";
- "the following order of precedence" has been changed to "the order of precedence identified below".

These examples and many others like them result in no change to the meaning of the draft submitted by Aurizon Network, add nothing to clarify the draft submitted by Aurizon Network. In the language of section 138(6) the changes proposed by the QCA "*no real effect or consequence*" in relation to Aurizon Network's draft access undertaking.

## Section 136(5) of the QCA Act

At section 2.10.7 the QCA states:

*"...once we have crossed the threshold of non-approval for the DAU (i.e. that we consider that the DAU is not appropriate having regard to the factors set out in section 138(2)(a)–(h)), we have a significant discretion as to what amendments we can propose, so long as those amendments are consistent with the policy and framework provided by the QCA Act."*

The QCA is stating in this paragraph that once it decides that a "DAU" is not appropriate that it can require any changes it likes as long as it considers the amendments to be "*consistent with the policy and framework provided by the QCA Act*".

The QCA cannot, as a matter of law, require any amendments that are inconsistent with or beyond the scope of the QCA Act. In direct contravention of this legal principle, and as is detailed throughout this submission, the QCA's proposed amendments to Aurizon Network's draft access undertaking frequently stray beyond the four walls of the QCA Act.

If the QCA forms the view that a draft access undertaking section 136(5) requires no more than for the QCA to advise of what is necessary to make the draft access undertaking “appropriate”. On any objective view of the QCA’s amendments to the draft access undertaking proposed by Aurizon Network – which change virtually every single provision proposed – go well beyond the requirements of section 136(5).

## Non-exhaustive list of matters in QCA’s drafting of revisions to UT4 that are beyond the QCA’s power

Aurizon Network has identified a number of provisions in the QCA’s redrafted undertaking which it considers are inconsistent with or beyond the scope of the QCA Act.

To assist the QCA in its review of these matters, we have collated the table which is a non-exhaustive list of items included in the QCA’s redrafted undertaking that are beyond the QCA’s power to impose.

Aurizon Network has addressed each of these issues in more detail in the relevant part of its submission, and sought where possible to offer an acceptable solution “within power” solution, or indicated where the matters should be deleted or amended.

Item No.	Clause No.	Description of effect of Clause	Beyond Power	
			Creates a prohibition, obligation or provision that is inconsistent the QCA Act	Grants power or jurisdiction for QCA that the QCA does not have under the QCA Act
1	2.4(b) and 2.4(d)(iii)	Introduces a prohibition on differentiation which is broader than the prohibition in the QCA Act Changes the language and meaning of exceptions in QCA Act	✓	
2	2.4(c)	Imposes obligations in undertaking already expressly covered by the QCA Act to give QCA jurisdiction not found in QCA Act and adds a circumstance of unfair differentiation not covered in QCA Act	✓	✓
3	2.5(f)	Provides that undertaking will override access agreement terms where stated, contrary to 168 of QCA Act which expressly provides that an access agreement can differ from, exclude or vary an approved access undertaking	✓	
4	3.3(a)(i)	Requires Aurizon Network to make a compliance declaration relating to the conduct of a third party (Aurizon Holdings) that is	✓	

Item No.	Clause No.	Description of effect of Clause	Beyond Power	
			Creates a prohibition, obligation or provision that is inconsistent the QCA Act	Grants power or jurisdiction for QCA that the QCA does not have under the QCA Act
		not a provider of the declared service Exposes Aurizon Network employees to offence provisions under the QCA Act, even if they did not know the information provided was inaccurate. This is contrary to the general position within respect to provision of false information under s 230 of the QCA Act.	✓	
5	3.4(e)	Seeks to regulate Aurizon Network's rights as a port or mine operator (neither of which are part of the declared service)	✓	✓
6	3.71(a)	Obligation to provide the QCA with general purpose financial statements for Aurizon Network and to provide supplementary financial statements separately identifying the declared service business from other (non-regulated) businesses. This is beyond power to the extent it requires Aurizon Network to produce accounts with respect to its non-regulated business.	✓	
7	3.9	Despite s168 of QCA Act (which expressly contemplates that an access provider and an access seeker can agree something inconsistent with the access undertaking) clause 3.9 prohibits any attempt to agree a confidentiality regime with access seekers that waives any requirement or obligation of Aurizon Network under Part 3 and renders any purported waiver of no effect	✓	
8	3.15	Requirement for all Aurizon Group (not just Aurizon Network) employees to undertake mandatory bi-annual training. (Aurizon Network recognises the need to provide training for High	✓	✓

Item No.	Clause No.	Description of effect of Clause	Beyond Power	
			Creates a prohibition, obligation or provision that is inconsistent the QCA Act	Grants power or jurisdiction for QCA that the QCA does not have under the QCA Act
		Risk Personnel and to relevant Aurizon Network employees.)		
9	3.20	Creates complaints process relating to third party (i.e. non-Aurizon Network) conduct and seeks to have Aurizon Network waive legal rights	✓	✓
10	3.22	Transfer of rail transport infrastructure from an Aurizon Party to Aurizon Network. The QCA has no power to request or require Aurizon Network to obtain the ownership of any rail transport infrastructure. If the QCA or another party feels that rail transport infrastructure that is not owned or operated by Aurizon Network is or should form part of the declared service, then the QCA or that other party needs to deal directly with the owner or operator of that infrastructure and not seek to make Aurizon Network the owner.	✓	✓
11	5.4(a)	Power to require a review and potentially amendment of the approved form of Standard Access Agreement and Standard Train Operations Deed post-approval of the access undertaking Power for QCA to make the amendments itself Those standard agreements form part of UT4. Once UT4 is approved, the QCA can only require amendments to it if it is inconsistent with the QCA Act and in accordance with the process under the QCA Act. The QCA has no power to otherwise require amendments to an approved access undertaking.	✓	✓
12	5.4(f) and (g)	Purports to limit Aurizon Network's ability to seek	✓	

Item No.	Clause No.	Description of effect of Clause	Beyond Power	
			Creates a prohibition, obligation or provision that is inconsistent the QCA Act	Grants power or jurisdiction for QCA that the QCA does not have under the QCA Act
		amendments to the Standard Access Agreement to matters that are solely limited to “workability”. “Workability” is defined to expressly exclude commercial positions and risk allocation amongst the parties. The QCA Act does not restrict what a party can amend by a DAU.		
13	6.2.1(a), 6.2.1(b)(i) – (iii)	Introduces new prohibitions on discrimination that are different from the QCA Act prohibitions Expose Aurizon Network to new liability not arising under the QCA Act	✓	
14	6.2.1(b)(vi)	Introduces a new prohibition on preventing and hindering access that are different from the QCA Act prohibition Exposes Aurizon Network to new liability not arising under the QCA Act	✓	
15	6.2.3(a)	Restricts Aurizon Network’s ability to recover at least its efficient costs contrary to pricing principles in QCA Act. Restricts Aurizon Network’s right to negotiate access charges with Access Seekers as the QCA’s approval is required before Aurizon Network can start to negotiate. Gives QCA jurisdiction to approve access charges (as distinct from Reference Tariffs) outside of a dispute process, which is inconsistent with the negotiate/arbitrate framework of the Act.	✓	✓
16	6.2.4	Restricts differential pricing in a way which is inconsistent with the pricing principles.	✓	
17	6.2.5(a)	Creates remedy for Access Holders not recognised by the QCA Act		

Item No.	Clause No.	Description of effect of Clause	Beyond Power	
			Creates a prohibition, obligation or provision that is inconsistent the QCA Act	Grants power or jurisdiction for QCA that the QCA does not have under the QCA Act
		Ousts jurisdiction of the Courts Gives QCA jurisdiction not vested by QCA Act Purports to allow QCA to require redrafting of existing binding contracts.	✓	✓
18	6.4.5(b)	Gives QCA power to determine new Reference Tariffs after the approval date of the undertaking for inclusion in the undertaking and without knowing the actual costs that are relevant		
19	6.4.6(c)	Gives QCA sole discretion to determine new Expansion Tariffs after the approval date of the undertaking.		✓
20	6.4.6(d)	Obliges Aurizon Network to submit a DAAU, which the QCA can only do where the conditions in s139 of the Act are satisfied.	✓	
21	6.9.1(b)	Gives QCA power to require a change to the method of calculating access charges that varies the method already approved by the QCA for the undertaking. The QCA cannot require an amendment to an approved undertaking except where the conditions in s139 are satisfied.		✓
22	6.13	Restricts Aurizon Network's ability to negotiate access arrangements that differ from the standard access agreement contrary to section 168 Gives QCA power to approve 'access conditions' when none exists in QCA Act The underpinning principle of the negotiate/arbitrate regime under QCA Act requires that the parties be able to negotiate terms for access. The QCA can only become involved under the QCA Act if there is an access dispute; there is no role in the QCA Act to prevent the parties agreeing	✓	✓

Item No.	Clause No.	Description of effect of Clause	Beyond Power	
			Creates a prohibition, obligation or provision that is inconsistent the QCA Act	Grants power or jurisdiction for QCA that the QCA does not have under the QCA Act
		access conditions or requiring the QCA's prior approval.		
23	6.13.2(g)(ii)(B)	Deems negotiations to be "outside scope of undertaking" Removes statutory limits on the QCA's jurisdiction in access determinations		✓ ✓
24	7.1(a)(v), 7.4.2, 7.4.3, 7.4.4, 7.6 and 7.7	These provisions purport to regulate matters that are post-contractual in respect of an access agreement that has already be negotiated and agreed. With some limited exceptions that are not relevant here, the QCA Act does not give the QCA a right to interfere in an signed access agreement.	✓	
25	7A.1(b)	Seeks to impose Supply Chain coordination role on Aurizon Network. The QCA's role is to regulate access to the declared service, not mandate supply chain coordination. Supply chain coordination is not part of the declared service which relates solely to the use of coal systems for transportation by rail.	✓	✓
26	7A.3	Seeks to impose Supply Chain coordination role on Aurizon Network . Imposes obligations not to discriminate between Supply Chains, which is inconsistent with the provisions dealing with unfair differentiation in the QCA Act. Imposes obligation on Aurizon Network to implement Supply Chain changes to increase Capacity	✓	✓
27	8.2.1(l)	Prevents Aurizon Network from earning any profit, margin or overhead relating to an Expansion investigation and design. This is inconsistent with the pricing principle in s168A(a).	✓	

Item No.	Clause No.	Description of effect of Clause	Beyond Power	
			Creates a prohibition, obligation or provision that is inconsistent the QCA Act	Grants power or jurisdiction for QCA that the QCA does not have under the QCA Act
28	8.2.2(a)	Gives a range of entities that are not access seekers a right to dispute “any matter” that may arise in relation to Expansions under Part 8	✓	✓
29	8.2.2(h)	Prohibits Aurizon Network from proceeding to implement any decision in respect of matters under Part 8 without first obtaining QCA approval to do so	✓	
30	8.4.2(b)(ii)	Imposes a cost related to Expansions on Aurizon Network The QCA Act does not allow the QCA to impose a cost on an access provider for “extensions” other than in limited circumstances	✓	
31	8.4.4(a)	Imposes funding obligation on Aurizon Network for shortfalls arising from default of funders to a Pre-Feasibility or Feasibility study	✓	
32	8.6(b)	Gives QCA jurisdiction to arbitrate over contractual performance issues The QCA has no jurisdiction to arbitrate contractual performance issues (unless the parties to an access agreement agree)		✓
33	8.7.1(a)	Gives Access Seekers right to fund Expansions even where Aurizon Network is willing to do so	✓	
34	8.7.1(e)	Places funding obligation on Aurizon Network The QCA Act does not allow the QCA to impose a cost on an access provider for “extensions” other than in limited circumstances	✓	
35	8.8.3	Places obligation on Aurizon Network to seek statutory severance of any Expansion and to make a specific application to the ATO for a binding advice	✓	

Item No.	Clause No.	Description of effect of Clause	Beyond Power	
			Creates a prohibition, obligation or provision that is inconsistent the QCA Act	Grants power or jurisdiction for QCA that the QCA does not have under the QCA Act
36	8.9.3	Obliges Aurizon Network to fund Expansion capacity shortfalls	✓	
37	9	Gives all Private Infrastructure Owners (not just access seekers) a right to have private infrastructure connected to the Rail Infrastructure.	✓	
38	10.6.4(k) – (m)	Requirement to implement auditor report, including as an amendment of the access undertaking, power to direct compliance with an auditor's recommendation (which might be to improve an internal process, not to comply with the Act) and deemed breach of undertaking if Aurizon Network does not comply with auditors recommendations	✓	✓
39	11.1	Regulates and gives QCA and third parties jurisdiction over disputes in addition to those which the QCA can hear under the QCA Act	✓	✓
40	11.1.5(g)	QCA's drafting seeks to ensure that any determination of a dispute by it is automatically consistent with the undertaking and therefore not subject to challenge on that basis. It is beyond the QCA's power to insulate itself from the requirements of the QCA Act and judicial review		✓
41	Ultimate Holding Company Support Deed	Purports to bind non-access providers to access undertaking obligations and allows QCA to enforce obligations	✓	✓
42	1.2(b)(ii), Schedule E	Removes asset value from RAB during the term of the access undertaking as a result of deterioration in demand not caused by Aurizon Network	✓	✓
43	8.3(a)(vi), Schedule G	Gives a third party group not recognised by the QCA Act the	✓	

Item No.	Clause No.	Description of effect of Clause	Beyond Power	
			Creates a prohibition, obligation or provision that is inconsistent the QCA Act	Grants power or jurisdiction for QCA that the QCA does not have under the QCA Act
		right to determine allocation of contested train paths The QCA has no jurisdiction to vest a third party with rights that affect the rights of access provider or access holders in relation to the declared service		

## Chapter 3 – Intent and Scope (Part 2)

### Summary of Aurizon Network’s Position

In its previous response to the IDD<sup>12</sup>, Aurizon Network raised significant concerns with the QCA’s proposal in relation to Part 2 of the undertaking. Aurizon Network welcomes the QCA’s recognition of a number of these issues, and the proactive and pragmatic approach taken by the QCA to resolving them.

However, a number of significant issues remain in the CDD. These issues are addressed below. Aurizon Network has also included a marked-up version of Part 2 that includes drafting to correct the issues identified, and which volunteers a number of pragmatic solutions in the interests of resolving a lawful and workable version of Part 2.

Aurizon Network’s concerns with the form of the Ultimate Holding Company Support Deed proposed in the CDD are addressed in Aurizon Network’s response to Part 3.

Table 2.2 below describes Aurizon Network’s specific issues with the CDD.

#### Proposed Redrafting of Part 2

While Aurizon Network cannot accept the version of Part 2 included in the CDD, Aurizon Network would agree to be bound by the amended version of Part 2 included in this submission. This mark-up sets out amendments which address the concerns raised in Table 2.2.

**Table 2.1 – QCA Consolidated Draft Decision**

	QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(1)	After considering Aurizon Network’s proposed duration of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network’s proposal.	3.1	<b>Agree.</b>
(2)	The way in which we consider it is appropriate that Aurizon Network amends the 2014 DAU is to amend clause 2.1 in the manner we have proposed in clause 2.1 of our CDD amended DAU.		
(1)	After considering Aurizon Network’s proposed location of the general principles of non-discrimination and independence in Part 3 of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network’s proposal.	3.2	<b>Agree with amendments.</b>
(2)	The way in which we consider it is appropriate for Aurizon Network to amend the 2014 DAU is to move clause 3.2 to become clause 2.4 of the undertaking, and amend clause 2.4 in the manner set out in our CDD amended DAU.		

<sup>12</sup> Aurizon Network (2015a). Part 3, pp.43-52.

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(1) After considering Aurizon Network's proposed intent and scope provisions relating to the objectives of the undertaking and Aurizon Network's obligations regarding its treatment of access seekers and holders, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amends the 2014 DAU is to amend the relevant clauses in the manner set out in clauses 2.2 and 2.4 of our CDD amended DAU, including to:</p> <p>(a) provide a list of objectives of the undertaking as <b>set</b> out in clause 2.2 of our CDD amended DAU</p> <p>(b) include a clause similar to the non-discriminatory treatment clause that was included in the 2010 AU, with some amendments for clarity and to ensure it is consistent with the QCA Act, as set out in clause 2.4 of our CDD amended DAU.</p>	3.3	<p><b>(2)(a) Agree with amendments.</b></p> <p><b>(2)(b) Agree with amendments.</b></p>
<p>(1) After considering Aurizon Network's proposed intent and scope provisions regarding Aurizon Network's treatment of related parties, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amends the 2014 DAU is to amend the relevant clauses in the manner set out in clause 2.4 of our CDD amended DAU, including to:</p> <p>(a) provide that Aurizon Network must not unfairly differentiate in favour of a related competitor, related operator or third parties which have commercial arrangements with a related competitor or a related operator</p> <p>(b) provide that Aurizon Network must ensure that all transactions between Aurizon Network and any other party in relation to access are conducted on an arms-length basis.</p>	3.4	<p><b>(2)(a) Disagree.</b> Aurizon Network is concerned that the QCA's prohibitions on unfair differentiation as drafted are not only unnecessary, but alter the intended meaning of 'differentiation' as prohibited under the QCA Act, as well as exceptions specified under the QCA Act. Aurizon Network considers that the QCA's extension of this prohibition on unfair differentiation is beyond power.</p> <p><b>(2)(b) Agree with amendments.</b></p>
<p>(1) After considering Aurizon Network's proposed intent and scope provisions on the interpretation of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p>	3.5	<p><b>(2)(a) Agree.</b></p> <p><b>(2)(b) Agree with amendments.</b></p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(2) The way in which we consider it is appropriate for Aurizon Network to amend the 2014 DAU is to:</p> <p>(a) amend clause 2.2 to include a heading for clause 2.2 of 'Objective' and include the words 'The objective of this Undertaking is, without limitation, to' at the beginning of the clause, as in clause 2.2 of our CDD amended DAU</p> <p>(b) include a new 'Interpretation' clause, as set out in clause 2.3 of our CDD amended DAU.</p>		
<p>(1) After considering Aurizon Network's proposed 'Scope' clause of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it is appropriate for Aurizon Network to amend the 2014 DAU is to amend clause 2.3 of the 2014 DAU in the manner set out in clause 2.5 of our CDD amended DAU, including to:</p> <p>(a) provide that 'access', for the purposes of this clause, includes all aspects of access to the service taken to be declared under section 250(1)(a) of the QCA Act (cl. 2.5(a) of the CDD amended DAU).</p>	3.6	<b>Disagree.</b> Aurizon Network does not accept the QCA's definition of 'access'. It is given a different meaning under this clause than elsewhere in the Undertaking and arguably broadens the scope of this term.
<p>(1) After considering Aurizon Network's proposal for the supply and sale of electricity, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it is appropriate for Aurizon Network to amend the 2014 DAU is to amend clause 2.4 of the 2014 DAU to include specific provision for dispute resolution in respect of the supply and sale of electricity, as set out in clause 2.7 of the CDD amended DAU.</p>	3.7	<b>Agree with amendments.</b>
<p>(1) After considering Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's overall proposal for 'associated services'.</p> <p>(2) The way in which we consider it is appropriate for Aurizon Network to amend the 2014 DAU is to amend clause 2.3 of the 2014 DAU to:</p>	3.8	<b>Disagree.</b> Aurizon Network's concerns with the QCA's definition of 'access' in this context were outlined above. Aurizon Network also does not agree with the clarifying provision from the definition of 'access' in the 2010 AU, which made it clear that this did not include the sale or supply of electric energy.

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(a) provide that 'access', for the purposes of the scope of the undertaking, includes all aspects of access to the service taken to be declared under section 250(1)(a) of the QCA Act (as set out in clause 2.5(a) of the CDD amended DAU).		
(1) Our overall consolidated draft decision is to refuse to approve Aurizon Network's 2014 DAU proposal, but we do not consider an amendment to the 2014 DAU to provide for an incentive mechanism is required.	3.9	<b>Agree.</b>
(1) After considering Aurizon Network's proposed clauses 2.2(b)(i), 2.3(b)(ii), 3.3 of the 2014 DAU, our consolidated draft decision is to refuse to approve these clauses of the 2014 DAU.	3.10	<b>(2)(a) Agree with amendments.</b>
(2) The way in which we consider it is appropriate that these clauses are amended is set out in clauses 2.2, 2.5 and 2.6 of the CDD amended DAU, as follows:		<b>(2)(b) Agree.</b>
(a) the word 'flexible' in the list of descriptors of the processes for access negotiations and utilisation of capacity (clause 2.2(d)(i) of the CDD amended DAU)		<b>(2)(c) Agree with amendments.</b>
(b) a requirement for Aurizon Network to notify access holders in writing if it is not the owner, or does not have a legal right to authorise access to, land upon which the rail infrastructure is situated to which the access holder is seeking access (clause 2.5(c) of the CDD amended DAU)		
(c) movement of the requirements relating to the Ultimate Holding Company Support Deed from Part 3 to Part 2 (clause 2.6 of the CDD amended DAU).		

## CDD Part 2 Scope and Intent

Aurizon Network's submission in response to the IDD set out a number of important legal principles which relate to the QCA's jurisdiction and powers. These, together with Aurizon Network's specific submissions

in relation to Part 2 of the Undertaking, remain relevant and, form the basis of the analysis set out below. Aurizon Network's previous response is incorporated here by reference<sup>13</sup>.

Aurizon Network's specific issues with the QCA's CDD in relation to Part 2 are summarised in the table below.

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<sup>13</sup> Aurizon Network (2015a). Part 3, pp.43-52.

**Table 2.2 – Issues with CDD in relation to Part 2**

Item	Clause Reference	Effect of clause	Issue
1	2.3	Interpretation of undertaking to best achieve the objectives in clause 2.2.	The words “In the event of any ambiguity,” should be added at the start of the clause. The clause as expressed is very broad in nature and may affect the interpretation of clauses that are otherwise already clear in their meaning.
2	2.4(b)	Absolute prohibition on unfair differentiation	<p>(a) Clause 2.4(b)(ii) is unnecessary because its subject matter is already addressed in clause 2.4(a). Given that and having regard to the points discussed below, clause 2.4(b)(ii) should be deleted.</p> <p>(b) The QCA’s drafting changes the prohibition contained in sections 100 and 168C in a number of respects, including the following:</p> <ul style="list-style-type: none"> <li>• The prohibitions on unfair differentiation under the QCA Act are focused on the negotiation of access agreements or amendments to access agreement in the case of access seekers and on the provision of access in the case of access holders. The QCA’s drafting goes much further because it prohibits unfair differentiation across the board and because it sets out specific examples that go beyond the types of unfair differentiation referred to in the QCA Act. The QCA’s drafting is therefore beyond power.</li> <li>• The QCA’s drafting includes two exceptions to the redrafted provisions of the QCA Act dealing with unfair differentiation. One of those exceptions in paragraph (H) changes an exception that applies to the unfair differentiation provisions under the QCA Act. It does this by reference to the requirements in clause 3.1(g), which are different to the requirements for the exception in section 168C.</li> <li>• The QCA’s drafting of the exceptions in paragraphs (G) and (H) of clause 2.4(b)(ii) also require there to be “an express provision to the contrary”. This is a more onerous standard than the one required by the QCA Act, which refers to differentiation that is expressly required or <u>permitted</u> by the Undertaking or the access agreement.</li> </ul>

Item	Clause Reference	Effect of clause	Issue
			<ul style="list-style-type: none"> <li>The exception in paragraph (H) is circular because whilst purporting to permit unfair differentiation it prohibits it by reference to clause 3.1(g), which includes in paragraph (ii) an obligation not to unfairly differentiate.</li> <li>The QCA's drafting also fails to specify all of the exceptions that the QCA Act contains – for example, unfair differentiation that is permitted by an access determination.</li> </ul> <p>For all of these reasons as stated above clause 2.4(a) covers the field and clause 2.4(b)(ii) should be deleted.</p>
3	2.4(c)	Further obligations not to prevent or hinder access or unfairly undifferentiated	<p>(a) The QCA's drafting of clause 2.4(c)(i) is not necessary. Aurizon Network is already obliged under the QCA Act not to prevent or hinder access. The effect of the QCA-drafted provision is to invest the QCA with jurisdiction that it otherwise does not have under the QCA Act. It is therefore also beyond power.</p> <p>(b) Clause 2.4(c)(ii) seeks to change the unfair differentiation obligations under the QCA Act and also introduces a concept of "quality of the service", which is not possible to interpret with any certainty and is not referred to in the QCA Act.</p>
4	2.4(d)(iii)	Further obligation not to unfairly differentiate	<p>(a) This provision contains a prohibition on unfair differentiation which is different to the QCA Act.</p> <p>(b) This prohibition contains none of the exceptions referred to in the QCA Act.</p> <p>(c) It also prohibits unfair differentiation between "any Access Seekers and/or Access Holders". It is not clear how this could be applied in practice, given the global expression of the language.</p> <p>The clause is unnecessary, beyond power and should be deleted.</p>
5	2.4(f)	Reference to exception under section 100(3)	<p>This "for clarity" provision only refers to one of the relevant exceptions that apply to the conduct being referred to. If clauses 2.4(c)(ii) and (d)(iii) are to remain (despite the comments above), it should also refer to section 168C. However, given the breadth of clauses 2.4(c)(ii) and (d)(iii) it is possible that none of these exceptions may apply.</p>

Item	Clause Reference	Effect of clause	Issue
6	2.4(i), (j) and (k)	Complaint and audit	<p>(a) If a complaint is received about non-compliance “with clauses 2.4(a) to (e)” and the complainant is not satisfied with Aurizon Network’s investigation, the complainant may ask for an audit and the QCA may require one. The effect of this, when read in conjunction with the audit provisions, is that the QCA is seeking to vest itself with a power it does not have under the QCA Act - including a power to potentially re-write the undertaking and to make a decision where it has no jurisdiction.</p> <p>(b) Clause 2.4(j)(ii) refers to clause 10.8. There is no clause 10.8.</p> <p>(c) Clause 2.4(k) reinforces the fact that the QCA is seeking to grant itself additional powers that it does not have under the QCA Act.</p> <p>Clauses 2.4(i) to (k) should be deleted.</p>
7	2.5(a)	Under clause 2.5, “Access” includes all aspects of access to the service declared under section 250(1)(a).	<p>(a) This provision gives “Access” a different meaning under clause 2.5 than is otherwise the case elsewhere under the Undertaking. In particular, the QCA’s drafting arguably broadens the definition of “Access” to include all other matters not listed in the defined term that are nevertheless part of access to the declared service. This creates uncertainty as to what does or doesn’t form part of Access under the undertaking and may give rise to disputes.</p> <p>(b) It may also have ramifications for the specific provisions set out in clause 2.5. It is not possible to define with any certainty where Aurizon Network’s obligations start and finish. For example, in 2.5(b) an Access Holder is “responsible for the provision of services other than Access”. If “Access” is given the wider meaning proposed in clause 2.5(a), it will be very difficult in practice to confirm which party is responsible for what. This may have significant implications operationally, particularly for new access holders.</p>
8	2.5(e)	Nothing in the undertaking can require an Access Agreement to be varied or AN or another party to access inconsistently with an Access Agreement.	The 2014DAU as submitted by Aurizon Network also applied this clause to Train Operations Agreements (Train Operations Deeds under the QCA drafting). It is unclear why the QCA has limited the clause to Access Agreements but it implies that the Undertaking does or can have the effect of amending Train Operations Deeds. This is outside of the QCA’s powers under the QCA Act.

Item	Clause Reference	Effect of clause	Issue
9	2.5(f)	<u>Except as expressly stated in the undertaking</u> , the undertaking won't apply to the extent it is inconsistent with an Access Agreement or Train Operations Deed.	<p>(a) The introduction of the words "Except where expressly stated in this Undertaking" does not appear to be necessary, as there are no provisions in the Undertaking that expressly state that the Undertaking overrides an agreement or deed.</p> <p>(b) In any event, section 168 expressly permits parties to agree something that is inconsistent with an Undertaking. The QCA's drafting is therefore beyond power.</p> <p>(c) As the Undertaking addresses matters regarding the negotiation of access, and access agreements address post-contractual matters, it follows logically that the undertaking should not be expressly inconsistent with an Access Agreement.</p>
10	2.6(b)	The QCA has included a statement of what the UHCSD is "intended to ensure".	This clause is unnecessary and should be deleted. This is because the form of Ultimate Holding Company Support Deed (UHCSD) is set in Schedule D. Clause 2.6(b) cannot change the form of the UHCSD and once the UHCSD is executed clause 2.6(d) cannot affect the interpretation of the UHCSD.
11	2.7	Voluntary obligations for AN to sell or supply electric energy	<p>(a) The QCA has deleted the statement that the sale or supply of electric energy is not part of Access and except as expressly referred to in the Undertaking, not subject to the Undertaking. The QCA's CDD argues that the sale or supply of electric energy is part of the declared service. The QCA's arguments are flawed because the declared service under section 250(1)(a) is nothing more nor less than the use of specified rail transport infrastructure for transportation by rail. This does not include the sale or supply of electric energy.</p> <p>(b) The QCA has included a specific dispute resolution provision. There are several problems with the QCA's proposed provision:</p> <ul style="list-style-type: none"> <li>As the sale or supply of electric energy is outside the declared service, the QCA is seeking to vest itself with powers that it does not have.</li> <li>Aurizon Network's obligation does not include procuring a sale or supply of electric energy by an Aurizon Party – but the dispute provision extends to such matters.</li> <li>The dispute provision relates to Access Holders and Nominated Railway Operators. These are both post-contractual entities. Any arrangements for the sale or supply of</li> </ul>

Item	Clause Reference	Effect of clause	Issue
			<p>electric energy would have been included in or 'back to backed' with the access agreement. The QCA has no power to arbitrate over access agreements.</p> <p>(c) However, in the interest of resolving the drafting of Part 2, Aurizon Network is prepared to volunteer a version of clause 2.7 which largely reflects the QCA's drafting, but which expressly recognises the jurisdiction of electricity regulators to resolve relevant disputes.</p>
12	"Access"	Defines "Access" for the purpose of the undertaking	<p>(a) The QCA has removed a clarifying provision from the definition of "Access" that sought to make clear that while Access included the provision of "electric transmission infrastructure" it did not include the sale or supply of electric energy. Ideally, that statement would be reinstated, even though there is an express provision to sell or supply electric energy in the Undertaking.</p> <p>(b) The drafting refers to electric transmission infrastructure. This language has probably been used for some time, but is inconsistent with terminology used in the QCA Act and the <i>Transport Infrastructure Act 1994</i> (the TIA). Ideally the terms used would link directly to the definition of Rail Transport Infrastructure; and therefore refer to "overhead electrical power supply systems". This would therefore be consistent with the definition of "rail transport infrastructure" under the TIA which is integral to the definition of the declared service. Conversely, the continued use of the term "Electric transmission infrastructure" could potentially include other types of electric infrastructure possibly outside the scope of the declared service.</p>

## Chapter 4 – Ringfencing (Part 3)

### Summary of Aurizon Network's Position

As a vertically integrated business, Aurizon Network is committed to an appropriate and workable ringfencing regime in which all stakeholders can have confidence.

Like the QCA in its draft decisions, to assist stakeholders with their understanding Aurizon Network is also prepared to use the 2010AU as a basis for the ringfencing regime. This commitment aligns with the QCA latest Consolidated Draft Decision and its supporting Undertaking. Aurizon Network has proposed amendments through drafting, designed to simplify and clarify drafting, improve transparency and reflect the QCA Act and current concepts outlined within the QCA's CDD. Aurizon Network has supplied this drafting within the appendix of this submission.

Aurizon Network has agreed to the concept of a confidential information register as per the QCA's drafting, to provide additional transparency.

However, Aurizon Network does not agree with a number of the elements of the QCA's CDD on Part 3, nor with the QCA's re-drafting of Part 3. Aurizon Network believes these decisions are based on unsubstantiated reasoning and misapplication of provisions in the QCA Act.

While trying to solve the perceived issues, the QCA has continued to take an overly restrictive and theoretical approach to ring fencing which fails to adequately consider either the operational complexities of a business like Aurizon Network, or the legitimate efficiencies (such as economies of scale) that result from being a vertically integrated business. This approach has resulted in the QCA providing decisions that create inefficiency, unnecessary complexity, additional cost (with no associated compensation), including provisions that are either practically unworkable or prohibit legitimate and appropriate activities

The QCA's re-drafting of Part 3 has resulted in an overly complex document that is difficult to understand and to apply in practice. Stakeholders could find the QCA drafting very difficult to follow, particularly if they are trying to determine how their commercially sensitive information would be protected.

It also imposes unnecessarily broad obligations, processes and restrictions which, if applied, would constrain components of Aurizon Network's business, without providing any demonstrable additional protection or benefit to access seekers, access holders or train operators.

Accordingly, Aurizon Network has used the 2010AU and the principles of the QCA's CDD drafting and provided an amended revised version of Part 3. This proposal, meets the key criteria established by the QCA in the CDD for the approval of a ring fencing regime, and addresses the key concerns it has identified by the QCA. Aurizon Network is confident that this carefully considered ring fencing framework:

- is designed to remove the opportunity for the disclosure or use of third party access holder confidential information (Ringfenced Information) to a related party that would provide a competitive advantage over other above rail operators (or access holders) in the CQCR;
- ensures that Aurizon Network's day-to-day operations are managed independently from Related Parties that operate in both upstream and downstream markets;
- ensures that Aurizon Network is the entity with the responsibility for the provision of below rail services including the assessing, allocation and management of capacity and scheduling of trains;

- ensures transfers and secondments of employees within the Aurizon Group are properly managed (and where appropriate, prohibited) so that ringfenced information is not misused or disclosed as a result of those staff movements;
- expressly provides Aurizon Network with a list of those limited circumstances and reasons for which ringfenced information can be disclosed (without ever permitting such disclosure to those Aurizon personnel responsible for marketing and contracting of above rail services within the CQCR);
- creates a transparent register for the recording of disclosures of ringfenced information which will allow the QCA and other stakeholders to monitor information flow, specifically to whom and for what particular purpose the information is provided (not including decision making purposes);
- ensures that all personnel with access to ringfenced information are made aware of the ringfencing requirements and that High Risk personnel receive appropriate training that outlines the required obligations for which they must comply; and
- includes an appropriate complaints handling and investigation process coupled with appropriate record keeping and audit rights.

Aurizon Network's submission in response to the IDD raised a number of important legal principles that applied both to the QCA's general approach to Aurizon Network's DAU and to ringfencing in particular. These arguments remain relevant, and accordingly Aurizon Network re-states its earlier submission, which is incorporated here by reference.<sup>14</sup>

**Table 4.1 – QCA Consolidated Draft Decision**

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1) After considering Aurizon Network's proposed 2014 DAU ring-fencing arrangements, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.	4.1	<b>Agree with amendments.</b>
(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to adopt the ring-fencing provisions in the 2010 AU as the baseline for our proposed amendments.		
(1) After considering Aurizon Network's 2014 DAU provisions regarding its commitment to avoid anti-competitive and discriminatory behaviour, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.	4.2	<b>Agree with amendments.</b>
(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to: <ul style="list-style-type: none"> <li>(a) include an overarching principle-based set of statements (similar, but updated, to that in clause 2.2(a) of the 2010 AU) reinstated in Part 2 (clause 3.4)</li> </ul>		

<sup>14</sup> Aurizon Network (2015a).

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(b) replace clause 3.2 of the 2014 DAU with a strengthened version of clause 3.2 from the 2010 AU, clarifying the standard of competitive harm applicable with respect to the anti-competitive practices of cross-subsidisation, cost shifting and price/margin squeezing</p> <p>(c) move clause 3.2 of the 2014 DAU, dealing with principles of non-discrimination, to Part 2.</p>		
<p>(1) After considering Aurizon Network's 2014 DAU provisions regarding the UHCSD, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network's draft access undertaking be amended is to:</p> <p>(a) provide that Aurizon Network request that its ultimate holding company provides the ultimate holding company support deed in the form set out in schedule D of our CDD amended DAU</p> <p>(b) provide that, in the event the ultimate holding company does not execute the UHCSD, or the UHCSD is not maintained in full force or complied with, the undertaking will cease to permit the use and disclosure of confidential information to any person or entity within the Aurizon Group (outside of Aurizon Network), until rectified.</p> <p>(c) move clause 3.2 to Part 2 of the undertaking, and amend it to mirror the requirements of the UHCSD</p>	4.3	<p><b>Agree with amendments.</b></p> <p><b>(2)(a) Agree</b> (note this is now dealt with in Part 2) but only in respect of UHCSD in the form submitted by Aurizon Network in response to the IDD.</p> <p><b>(2)(b) Agree, with amendments.</b></p>
<p>(1) After considering clause 3.11 of the Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's definition of protected information.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:</p> <p>(a) replace the definition of protected information with an amended version of the definition of confidential information used in the 2010 AU</p> <p>(b) replace in all instances 'protected information' with confidential information'</p>	4.4	<p><b>Disagree - Definition of Confidential Information is too broad.</b></p>
<p>(1) After considering clauses 3.18 and 3.20 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to</p>	4.5	<p><b>(2)(a) Agree with amendments.</b></p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>approve Aurizon Network's disclosure process and provisions regarding the protected information register.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:</p> <ul style="list-style-type: none"> <li>(a) replace the protected information register with the confidential information register</li> <li>(b) include in the confidential information register entries as set out in clause 3.14 of the CDD amended DAU</li> <li>(c) require a record of all confidentiality agreements to be maintained as part of the confidential information register.</li> </ul>		<p><b>(2)(b) Agree with amendments.</b></p> <p><b>(2)(c) Disagree</b> - Due to wide and ambiguous definition of Confidential Information, obligations will be onerous as most agreements would contain confidentiality provisions.</p>
<p>(1) After considering clause 3.17 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's protected information register in the 2014 DAU as a credible source of information.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network's draft access undertaking be amended is for:</p> <ul style="list-style-type: none"> <li>(a) Aurizon Network, following consultation with access holders and train operators, to develop a proposed structure and definition set for inputs into the confidential information register. This must be submitted to the QCA for approval within the first four months of the operation of this undertaking</li> <li>(b) the confidential information register to be submitted to the QCA, every 12 months or upon request, for review</li> <li>(c) the QCA to undertake spot audits at its discretion, to ensure the processes and procedures underpinning the information collection are fit-for-purpose, being adhered to and used in a consistent manner</li> </ul>	<p>4.6</p>	<p><b>(2)(a) Disagree.</b> For certainty, the format of the register should be established at the commencement of the undertaking.</p> <p><b>(2)(b) Agree.</b></p> <p><b>(2)(c) Agree</b>, provided that a reasonable approach is adopted to the frequency and nature of spot audits.</p>
<p>(1) After considering relevant clauses of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's exemptions process, confidentiality and consent provisions.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend the draft access undertaking is to:</p> <ul style="list-style-type: none"> <li>(a) replace the obligations and processes for disclosure of confidential</li> </ul>	<p>4.7</p>	<p><b>(2)(a) Agree with amendments.</b></p> <p><b>(2)(b) Disagree.</b> Standard form confidentiality agreement is not required. Relevant information is already subject to significant disclosure restrictions – it is a matter for access seekers and Aurizon Network to agree on any further restrictions.</p> <p><b>(2)(c) Disagree.</b> A standard form confidentiality agreement is not required.</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>information in accordance with our marked drafting</p> <p>(b) allow any relevant party, including Aurizon Network, at any time during negotiations for access, to require the other party to enter into the standard form confidentiality agreement (Schedule I)</p> <p>(c) replace the standard form confidentiality agreement in accordance with our marked drafting</p>		
<p>(1) Our consolidated draft decision is to refuse to approve Aurizon Network's 2014 DAU in the absence of any decision-making principles.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to reinstate the decision-making principles included in the 2010 AU.</p>	4.8	<p><b>Disagree.</b> The Ringfencing Register provides transparency in relation to the flow of ringfenced information and decisions made with it. Aurizon Network proposed Part 3 includes clear and unambiguous restrictions on both use and disclosure of ringfenced information. These specific provisions, combined with the clarity provided by the Ringfencing Register, are more effective and practical than the general and ambiguous decision-making principles in the 2010AU.</p>
<p>(1) After considering section 3.21 of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's training and exit certificate provisions.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network's draft access undertaking be amended is to:</p> <p>(a) require confidential information training for all Aurizon Network personnel, as well as employees of the Aurizon Group, whose role requires access to confidential information related to the declared services of the CQC</p> <p>(b) Require Aurizon Network to obtain exit certificates for Aurizon Network high-risk personnel, and to adopt a 'best endeavours' approach for other personnel, who have had access to confidential information related to the CQC</p> <p>(c) include provisions that:</p> <p>(i) require the development of a high-risk personnel register that can be used to target training requirements</p> <p>(ii) provide for a copy of the high-risk personnel register to be given to the QCA, upon request, and to allow for the QCA to audit its development and update over time.</p>	4.9	<p><b>(2)(a) Agree with amendments.</b></p> <p><b>(2)(b) Agree.</b> While Aurizon Network is prepared to agree to a best endeavours approach, it should be noted that it is not possible to guarantee that exit certificates can be required from all departing employees.</p> <p><b>(2)(c)(i) Agree.</b></p> <p><b>(2)(c)(ii) Agree.</b></p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(1) After considering clause 3.15 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's commitments to information security.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network's draft access undertaking be amended is to propose that Aurizon Network must not use or disclose confidential information if doing so would unfairly advantage a related operator.</p>	4.10	<b>Disagree.</b> This is inconsistent with the QCA Act. Aurizon Network has proposed revised drafting.
<p>(1) After considering clause 3.22 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's commitments regarding the security of premises.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is as set out in clause 3.18 of our CDD amended DAU:</p> <p>(a) security measures to apply to all Aurizon Network personnel and all Aurizon Network premises where confidential information is located or stored</p> <p>(b) any person visiting an Aurizon Network premises to be accompanied by an Aurizon Network employee</p> <p>(c) a record to be maintained of all persons who have accessed an Aurizon Network premises where confidential information is located or stored, with the exception of Aurizon Network directors/employees</p> <p>(d) an employee of Aurizon Network on secondment with another Aurizon Group company to be considered as staff of that other company and be subject to the security measures for non-Aurizon Network employees.</p>	4.11	<p><b>(2)(a) Disagree.</b> Aurizon Network proposes a strong but simplified alternative.</p> <p><b>(2)(b) Disagree.</b> Aurizon Network proposes a strong but simplified alternative.</p> <p><b>(2)(c) Disagree.</b> Aurizon Network proposes a strong but simplified alternative.</p> <p><b>(2)(d) Agree.</b></p>
<p>(1) After considering clause 3.13 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposals allowing for Aurizon Network and third party access seekers or access holders to agree to waive the ring-fencing provisions in 2014 DAU.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network's draft access undertaking be amended is set out in clause 3.9 of our CDD amended DAU, namely to:</p>	4.12	<b>Agree with amendments.</b>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<ul style="list-style-type: none"> <li>(a) prohibit Aurizon Network from requesting an access holder, access seeker or train operator to waive Aurizon Network's ring-fencing obligations</li> <li>(b) ensure ring-fencing obligations and requirements are not superseded by: <ul style="list-style-type: none"> <li>(i) a confidentiality agreement/deed or</li> <li>(ii) an access agreement</li> <li>(iii) containing confidentiality provisions in relation to the negotiation or provision of access rights.</li> </ul> </li> </ul>		
<ul style="list-style-type: none"> <li>(1) After considering clauses 3.4 and 3.5 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposals regarding the definition of access-related functions and Aurizon Network's obligation to perform these.</li> <li>(2) The way in which we consider it is appropriate that Aurizon Network's draft access undertaking be amended is to: <ul style="list-style-type: none"> <li>(a) revise clauses 3.4 and 3.5 of the 2014 DAU</li> <li>(b) include an overarching statement that Aurizon Network's primary function is to supply the declared service and provide all relevant functions</li> <li>(c) require Aurizon Network not to: <ul style="list-style-type: none"> <li>(i) undertake any above-rail services in respect of the Rail Infrastructure</li> <li>(ii) undertake the operating or marketing of train services, unless for the provision of the declared service</li> <li>(iii) undertake any services associated with loading vessels at a port or hold any direct or indirect interest in any port connected to the rail infrastructure.</li> </ul> </li> </ul> </li> </ul>	4.13	<p><b>(2)(a) Agree with amendments</b></p> <p><b>(2)(b) Agree with amendments.</b></p> <p><b>(2)(c)(i) Agree with amendments.</b></p> <p><b>(2)(c)(ii) Agree.</b></p> <p><b>(2)(c)(iii) Agree with amendments.</b> Aurizon Network agrees in principle re unloading services at port, subject to clarification from the QCA that this refers to ship loading as distinct from train operations and unloading (e.g. RIM services).</p> <p>Disagree with absolute restriction on ownership as this is beyond power.</p>
<ul style="list-style-type: none"> <li>(1) After considering clause 3.6 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposals regarding employee separation.</li> <li>(2) The way in which we consider it is appropriate that Aurizon Network's draft access undertaking be amended is to:</li> </ul>	4.14	<p><b>(2)(a) Disagree.</b> Aurizon Network disagrees with the working group concept.</p> <p><b>(2)(b) Disagree.</b> Aurizon Network does not consider this is required, as working groups no longer contemplated.</p> <p><b>(2)(c) Agree with amendments.</b></p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<ul style="list-style-type: none"> <li>(a) include a 'working group concept' that extends to application to related entities</li> <li>(b) require the details of any Aurizon Network employee's involvement in a working group to be entered into the confidential information register, if the employee has had access to confidential information</li> <li>(c) require Aurizon Network to notify the QCA of secondments/transfers of employees to another Aurizon party prior to them being made</li> <li>(d) require Aurizon Network employees to be identified as Aurizon Network employees.</li> </ul>		<p><b>(2)(d) Disagree.</b> This level of prescription is neither lawful nor necessary in a ringfencing regime.</p>
<ul style="list-style-type: none"> <li>(1) After considering clauses 3.8, 3.9 and 3.10 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposals regarding management separation.</li> <li>(2) The way in which we consider it is appropriate that Aurizon Network's draft access undertaking be amended is to: <ul style="list-style-type: none"> <li>(a) remove clauses 3.8, 3.9 and 3.10</li> <li>(b) reinstate an updated version of clause 3.1.2 of the 2010 AU (cl. 3.8 of the CDD amended DAU), to account for related operators and related competitors, and to prevent Aurizon Network acting on direction from a related operator.</li> </ul> </li> </ul>	4.15	<p><b>Agree with amendments.</b></p>
<ul style="list-style-type: none"> <li>(1) After considering Aurizon Network's proposal, our consolidated draft decision is to refuse to approve the accounting separation and financial reporting arrangements.</li> <li>(2) The way in which we consider it is appropriate that Aurizon Network amends the draft access undertaking is to: <ul style="list-style-type: none"> <li>(a) delete clause 3.7 of the 2014 DAU</li> <li>(b) include accounting separation, financial reporting and audit arrangements, which are based on the 2010 AU arrangements (cls. 3.7 and 10.4.1 of the CDD amended DAU), which include requirements on Aurizon Network to: <ul style="list-style-type: none"> <li>(i) separately identify Aurizon Network's business in respect of the supply of the declared service from any other business conducted by the Aurizon Group</li> <li>(ii) identify costs common to both Aurizon Network and the Aurizon Group and the</li> </ul> </li> </ul> </li> </ul>	4.16	<p><b>(2)(a) Agree.</b></p> <p><b>(2)(b) Agree with amendments.</b></p> <p><b>(2)(c) Agree with amendments.</b></p> <p><b>(2)(d) Agree with amendments.</b></p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p style="text-align: center;">way in which such costs are allocated</p> <p>(c) include a requirement to report on self-insurance arrangements (cl. 3.7.2 of the CDD amended DAU)</p> <p>(d) make other amendments as reflected in our CDD amended DAU.</p>		
<p>(1) After considering clause 3.23 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposals regarding the complaints handling process.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network's draft access undertaking be amended is to reflect the complaints handling process in clause 3.20 of our CDD amended DAU.</p>	4.17	<b>Agree with amendments.</b>
<p>(1) After considering clauses 3.23 and 3.24 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposals regarding compliance with its ring-fencing obligations.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network's DAU be amended is to include an obligation for Aurizon Network to provide a six-monthly compliance declaration to the QCA.</p>	4.18	<b>Disagree</b> - This concept is beyond power, and is not required when regard is had to the confidential information register and the QCA's existing coercive powers.
<p>(1) After considering Aurizon Network's 2014 DAU proposals to remove Aurizon Network's ring-fencing obligations regarding the rail infrastructure associated with the declared service, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network's draft access undertaking be amended is to reinstate appropriately updated versions of clauses 3.8.1 and 3.8.2 of the 2010 AU (cls. 3.21 and 3.22 of the CDD amended DAU).</p>	4.19	<b>Disagree</b> - These obligations are beyond power, and are in no way relevant to a ring fencing regime. Existing public record documents such as the rail corridor sublease and the s250 declaration are sufficient.

## Underlying assumptions and principles

At the outset, it is evident that a number of the QCA's proposals in the CDD, and the extent of its re-drafting of Part 3, is based on a number of underlying assumptions, assertions and principles which are, in Aurizon Network's view, incorrect. In particular:

### 1. Asserted lack of confidence in the ring fencing framework

In the CDD<sup>15</sup> the QCA asserts that stakeholders have submitted that they lack confidence in the current ring fencing regime. The QCA goes on to say:

*We noted that despite an apparent lack of confidence, very few complaints and audit issues had been raised with respect to the existing ring-fencing provisions. This could indicate that the ring-fencing regime is effective, or it could indicate, for example, that the stakeholders are unwilling to lodge complaints or regard the complaint process as ineffective.*

The QCA goes on to say<sup>16</sup>:

*In our view, evidence (or lack thereof) of complaints of non-compliance is not determinative. **Without sufficient information**, it is difficult to gather enough evidence to support a claim for a breach of the ring-fencing provisions, and therefore evidence of a lack of complaints does not necessarily support Aurizon Network's position. (emphasis added)*

*Additionally, as noted above, a practical consideration that arises under the QCA Act is the degree to which a proposed regime is **deemed by stakeholders** to be credible and effective. (emphasis added)*

In setting out these views, the QCA has:

- Accorded greater weight to mere assertions made by stakeholders of a lack of confidence, than actual evidence. Stakeholder submissions provide no concrete evidence, or even specific examples of concern – rather, they assert a lack of confidence, and nothing more. Despite this, the QCA has, in its own words, accorded weight (and substantial weight can be inferred from the heavy handed approach taken by the QCA) to a mere “deeming” by stakeholders that they believe the regime not to be credible or effective.
- Allowed itself to be convinced that a lack of evidence of ring fencing complaints is likely to be the result of stakeholders being unwilling to lodge complaints, or regarding the complaints handling process as being ineffective. This is despite the stakeholders in this instance being large, sophisticated entities with significant legal resourcing, and being robust and frequent participants in regulatory, commercial and dispute processes.
- Failed to consider or describe at all any actual evidence gained directly by the QCA over more than 10 years of regulation of Aurizon Network, including information gained from proactive breach reporting, the complaints process, annual audits and the exercise by the QCA of coercive powers. Indeed, the absence of such evidence is in fact indicative of the opposite proposition than the one advanced by the QCA. In reality, the ring fencing regime, and Aurizon Network's compliance with it, has been tested for a decade and not found wanting.

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<sup>15</sup> Queensland Competition Authority (2015a). p.91.

<sup>16</sup> Queensland Competition Authority (2015a). p.91.

- Failed to consider or detail at all any impact or outcome arising from asserted or alleged weaknesses in the ring fencing regime, or to consider at all the contrary evidence of a competitive market for above-rail services, with both new entrants and growth in market share of incumbent competitors to Aurizon Operations. Relevantly, of the 35% increase in coal tonnages in the CQCN between 2012 and 2015, 11% has accrued to Aurizon Operations and the remainder to third party operators.

It is therefore evident that this is a flawed and insufficient basis upon which to justify a proposed ring fencing regime which, even after unnecessary complexity and drafting error is removed, is heavy-handed, restrictive and in some instances punitive. This flawed reasoning, when combined with the two assumptions discussed below, impact on the totality of the regime proposed by the QCA.

Aurizon Network is required to report on a range of metrics to both the QCA and public on areas that related directly to the level of confidence in the ringfencing regime. These include complaints, misapplication of train movement principles and ringfencing breaches. During the extended term of UT3, Aurizon Network has reported the following:

**Figure 4.1 – Operational complaints and breaches**

Annual Performance Data		FY15	FY14	FY13	FY12	FY11
Written complaints from a non-Aurizon party that Aurizon Network has breached its obligation in relation to the non-Aurizon party's confidential information		1			1	
Written complaints from a non-Aurizon party that Aurizon Network has breached its obligation in relation to the non-Aurizon party's confidential information that have been substantiated						
Written complaints that Aurizon Network Train Control has made a decision in breach of the Traffic Management Decision Making Matrix		1		3	3	
Written complaints that Aurizon Network Train Control has made a decision in breach of the Traffic Management Decision Making Matrix that are currently being assessed by Aurizon Network				1		
Written complaints that Aurizon Network Train Control has made a decision in breach of the Traffic Management Decision Making Matrix that after being assessed were verified		1			2	

These numbers are considerably small, considering the number of processes that would have been completed. For example the Traffic Management Decision Matrix is used thousands of time per year, to only have 3 validated complaints cannot be drawn upon to conclude that the system is not working properly.

The QCA's concerns in relation to evidence (despite a decade of reporting and audit) are readily addressed by the confidential information register process, with which Aurizon Network is prepared to agree.

## 2. Asserted absence of benefits of vertical integration

The QCA has made the following observations in relation to vertical integration:

*"We considered that:*

- Aurizon Network provided no compelling evidence to demonstrate that vertical integration provides it with efficiency gains in comparison to the costs it would face if it were a stand-alone entity, or that any cost efficiencies realised are material and flow through to Aurizon Network's customers*
- a vertically integrated Aurizon Network would face materially differing financial incentives to contribute to supply chain efficiency than a stand-alone Aurizon Network. It is also not clear why an effective ring-fencing regime would erode any efficiencies Aurizon Network gains from vertical integration, given it is in Aurizon Network's legitimate business interests that the*

*efficient costs of compliance with the ring-fencing framework in place should be included in its MAR*<sup>17</sup>

*“The 2014 DAU ring-fencing arrangements are, in our view, broadly inadequate to regulate the activities of a privatised integrated business whose stated goals are to leverage its integrated model. Given Aurizon Network’s changed business structure and its intention to leverage the benefits of vertical integration, we consider that the 2014 DAU ring-fencing regime could allow Aurizon Network to exercise anti-competitive behaviours, restrict transparency, and manage information flows to its advantage (or the advantage of related parties).”*<sup>18</sup>

The premise of the QCA’s IDD and CDD is therefore a rejection of any consideration of benefits accruing from a vertically integrated structure, again despite the lack of any evidence of adverse consequences actually occurring from that structure when regulated under UT1, UT2 or UT3.

In addition, both the QCA and stakeholders have made much of “Aurizon’s stated intention to leverage the benefits of vertical integration” and in doing so have assumed (without supporting evidence) that such leverage would automatically disadvantage non-related access seekers, access holders or train operators.

Vertical integration has had no impact on competition within the CQCR. There are currently 3 operators providing train services within the region, third party operators providing almost 30% of above rail services. The hunter valley coal network, which is a non-vertically integrated railway has similar operations with 4 railway operators. Vertical integration has not impacted competition within the CQCR.

No weight has been given to Aurizon Network and Aurizon’s stated intention to leverage only the lawful and legitimate benefits of vertical integration. Examples of these are:

- Economies of scale and avoidance of duplication

A vertically integrated structure allows Aurizon Network to utilise shared services it would otherwise have to duplicate. A practical example of this is being able to call on rollingstock engineering experience from Aurizon Operations rather than duplicating a specialised and costly resource.

- Alignment

Vertical integration means Aurizon Network is aligned to the needs of rail operators, and to ensuring its network is maintained and operated in a manner which is reliable and which delivers the capacity required by operators. A practical example of this is the rapid implementation by Aurizon Network of operator owned wayside monitoring equipment designed to improve rollingstock reliability. A practical example of the outcome of this alignment is the demonstrable improvement in the reliability, throughput and performance to plan of the entire CQCN.

### **3. Lack of regulation of the structure of Aurizon Network**

As can be seen in the paragraphs above, the QCA asserts in both the IDD and CDD that Aurizon Network has a business structure that requires additional regulation. It is clear that the QCA views this structure as problematic and as justification for a greater level of intervention in ring fencing and business processes.

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<sup>17</sup> Queensland Competition Authority (2015a). Consolidated Draft Decision, Aurizon Network 2014 Draft Access Undertaking: Volume 1 – Governance and Access, pp.90-91.

<sup>18</sup> Queensland Competition Authority (2015a). p.93.

This is not the case.

Aurizon Network’s structure was created by special legislation in 2008 (*Government-Owned Corporations (QR Limited Restructure) Regulation 2008*.) It was confirmed in 2010 by project directions and transfer notices made under the *Infrastructure Investment (Asset Restructure and Divestment) Act 2009*. Relevantly, section 12 of that Act states: “A thing may be done under this Act despite any other law or instrument.”

Further, Aurizon Network’s governance is regulated by the *Transport Infrastructure Act 1994* (TIA), which imposes requirements in relation to: the composition of its Board of Directors (s438G), approval by the Aurizon Network Board of access agreements with related operators (s436H), head office, management and decisions on access agreements with related operators.

It is clear that Parliament has turned its mind very clearly to the structure and governance of Aurizon Network, and has imposed specific and relevant requirements. There is no need for further regulation of structure – as distinct from regulation of the flows of ringfenced information.

Aurizon Network continues to rely on shared services, such as safety, tax, treasury and legal – as it did in 2010 and before. Aurizon Network also continues to have a separate management team and continues to directly employ the teams responsible for the negotiation and management of access agreements, assessment of capacity, planning and scheduling, train control, network operations, network engineering, regulation, finance and billing.

## Practical issues with CDD and drafting of Part 3

As discussed above, the QCA has in its IDD and CDD concluded that “strengthened” ringfencing arrangements are required for Aurizon Network – including arrangements which go beyond those currently applicable under the 2010AU. In Aurizon Network’s view, the justification for this conclusion is fundamentally flawed (for the reasons discussed above). In any event the QCA does not have power to do so (for the reasons discussed below in relation to legal analysis) or its outcome is inconsistent with the QCA Act.

In any event, the proposed arrangements are of such severe and that they result in a range of practical issues which will have a negative impact both on the legitimate operation of Aurizon Network’s business and on the service it provides its customers. Again this outcome is inconsistent with the QCA Act.

The key practical issues are set out in the following table. Please note this list sets out key issues, and is not exhaustive. To address all these issues, Aurizon Network has supplied drafting which deals with the proposed rectification of the listed issues and consequences.

**Table 4.2 – Practical issues with the QCA’s proposed ringfencing regime**

Item	Clause Ref	Issue	Consequence
1	QCA CDD Undertaking Definitions	Definition of confidential information is too broad, not limited to third parties	<ul style="list-style-type: none"> <li>Regulates information which is not ringfenced</li> <li>The CI Register and the complex disclosure regime applies to far more information than it should</li> <li>Creates unnecessary administrative burden</li> </ul>

Item	Clause Ref	Issue	Consequence
			<ul style="list-style-type: none"> <li>- Cannot comply with the QCA's CDD amended DAU</li> </ul>
<b>3.6 – Staffing of Aurizon Network</b>			
1	3.6(d)	Must record in the Confidential Information Register activities of a project working group	<ul style="list-style-type: none"> <li>Not clear how clause 3.6(d) would affect projects such as a joint customer, above rail operator and below rail projects to improve supply chain throughput for a customer</li> <li>Confidentiality deeds would no longer be binding due to the way the CDD has been drafted</li> <li>Clause is broad and could include Supply Chain coordination initiatives run across the industry</li> <li>Definition of Supply Chain is not sufficiently linked to the declared service</li> </ul>
2	3.6(e)	Cannot permit any secondments between Aurizon Network and the Aurizon Group if employee has had access to Confidential Information	<p>Example of issue – If commercial analyst is seconded into Aurizon IT (Aurizon Group) for a period of 6 months for an IT project, Aurizon Network would have to give prior notice to the QCA even if there is no risk to ringfenced information:</p> <ul style="list-style-type: none"> <li>Administrative Burden of having to inform the QCA for all non-risk secondments</li> <li>Using the QCA's confidential information definition, this would include ALL secondments, as confidential information is not limited to third party access seekers/access holders</li> </ul>
<b>3.11 Overarching commitment to information security</b>			
1	3.11(a)	Potential breach of part 3	QCA has added a clause 3.11(a) "Notwithstanding any other provisions in the Undertaking, Aurizon Network must keep Confidential Information confidential".
<b>3.12 – Process for permitted disclosure of Confidential Information</b>			
1	3.12	Clause includes all Aurizon Network personnel	Clause 3.12 currently includes all Aurizon Network personnel. This is impossible to comply with as Aurizon Network personnel require confidential information to perform their day to day tasks
2	3.12(d)	Definition of Confidential Information	Due to the QCA's definition of Confidential Information it would be impossible to record access or disclosure of all confidential information in the CI Register
3	3.12(e)	Recipient of Confidential Information must sign a declaration confirming awareness	The issue is for those personnel contracted with Aurizon IT - cannot comply with this clause
4	3.12(f)	Non Aurizon Network personnel must enter into a legally enforceable agreement	<ul style="list-style-type: none"> <li>This clause is unnecessary and similar to 3.12(e), will be hard to comply with due to Aurizon Network's shared services functions</li> </ul>

Item	Clause Ref	Issue	Consequence
			<ul style="list-style-type: none"> <li>Excessive legal implications and burden</li> </ul>
3.13 Disclosure of Confidential Information			
1	3.13(c)	Having to record confidential information into Confidential Information register when disclosed to numerous parties.	<p>1) This clause would see Aurizon Network having to record in the register each time confidential information was disclosed to external legal</p> <p>2) This would also apply if Aurizon Network sought financiers' advice eg. A sale of Aurizon Network which is not yet public</p> <p>QCA and stakeholders could view information within the Confidential Information Register, ultimately revealing the nature/content of legal advice sought.</p>
2	3.13(d)(v)	The disclosure has been authorised by the owner of the Confidential Information providing it's prior written consent	<ul style="list-style-type: none"> <li>Extreme administrative burden</li> <li>Would cause a large decrease in productivity for Aurizon Network, the party seeking the information and the owner of the confidential information</li> </ul> <p>Example – Aurizon IT needs to rectify a system error within a confidential database</p>
3.14 Confidential Information Register			
1	3.14	Change the name of "Confidential Information Register" to "Ringfencing Register"	This is to make it clear that the register only includes information related to third party access seeker/access holders and to align with Aurizon Network's preferred definition
2	3.14	Confidential Information Register input is required for Network to Network transfers of Confidential Information	An Aurizon Network person is required to handle confidential information on a day to day basis to perform their duties. Cannot comply with this clause in practice.
3	3.14(a-b)	Aurizon Network must submit the contents of the confidentiality register to the QCA for approval	This is an open ended obligation as Aurizon Network cannot foresee what changes the QCA may require, therefore posing a compliance risk.
4	3.14(c)(i)	The QCA has added a clause 'The confidential information register will contain, as a minimum (i) the identity of persons or entities who <i>request</i> access to Confidential Information' (emphasis added)	The word 'request' should be replaced by 'received'. It is not relevant who asks for the information, it is only relevant if confidential information is actually provided
5	3.14(c)(ii)(D)	The Confidential Information Register must include 'the decision made using the Confidential Information'	<u>Impossible</u> to capture this information
6	3.14(c)(ii)(E) 3.14(c)(iv)	Duplication of clause	
7	3.14(c)(v)	Refer to Exit Certificates clause 3.17	

Item	Clause Ref	Issue	Consequence
<b>3.15 Mandatory Confidential Information training</b>			
1	3.15(b)(i)	<ul style="list-style-type: none"> <li>Briefing session for employees of Aurizon Group who requires access to Confidential Information</li> <li>New employees within 1 month</li> <li>At least once in every 2 years</li> </ul>	Aurizon Network has interpreted the “Briefing Session” as a face to face session. This would require substantial resources to carry out the training and remain in compliance with the Undertaking requirements
2	3.15(b)(ii)	<ul style="list-style-type: none"> <li>Detailed training session for employees who are high-risk</li> <li>New employees within 1 month</li> <li>At least once in every 2 years</li> </ul>	Aurizon Network has interpreted the “Detailed Training Session” as a face to face training session. This would require substantial resources to carry out the training and remain in compliance with the Undertaking requirements
<b>3.16 High-Risk Persons</b>			
1	3.16(c)	Inclusion of personnel within the “High-Risk Persons” clause	It’s not plausible to require the CEO, CFO and all Directors of Aurizon Network to complete the ringfencing training every 2 years as they are the most familiar with the ringfencing provisions.
<b>3.17 Exit Certificates</b>			
1	3.17(a)(ii)	<p>Aurizon Network must use its best endeavours to (but in the case of High-Risk Personnel, must):</p> <ul style="list-style-type: none"> <li>undergo an exit debriefing</li> <li>obtain an exit certificate</li> </ul>	<p>Aurizon Network cannot comply with “High-Risk Personnel must” clause.</p> <p>There are occasions where employees leave the Aurizon Network business unexpectedly, which could result in a breach of the Undertaking</p>
2	3.17(c)	Must be a condition of employment of Aurizon Network personnel to attend the debriefing and provide an exit certificate	The QCA cannot pose a change to existing employee contracts or Enterprise Agreements
<b>3.18 Security Measures</b>			
1	3.18(b)	Aurizon Network must ensure that all Aurizon Network personnel are clearly identified as Aurizon Network personnel in their dealings with third parties	This clause cannot be monitored for compliance.
2	3.18(c)(ii)	<p>Non-Aurizon Network person is accompanied by an Aurizon Network employee at all times while in those premises</p> <p>This would include tradespersons, etc</p>	<p>Cannot comply with this clause</p> <ul style="list-style-type: none"> <li>Impossible to require that when non-network personnel enter premises where confidential information is located that they will be accompanied by an Aurizon Network employee at all times.</li> </ul>

Item	Clause Ref	Issue	Consequence
3	3.18(d)	Aurizon Network must maintain a record of all personnel (excluding Aurizon Network personnel) who have accessed each premise where confidential information is located or stored	<p>Cannot comply with this clause</p> <p>This clause would include tradespersons, cleaners etc.</p> <p>It also states a “premises”. A premises includes the land with the buildings on it. This would mean that not only would all personnel entering level 4 at 192 Ann Street, but all non-Aurizon Network personnel entering other floors within the building (i.e. completely separate organisations) would also have to be recorded on the register.</p> <p>This would also include all small buildings around the CQC which contain confidential information for a period of time.</p>

## Legal analysis of CDD DAU of Part 3

For completeness Aurizon Network has also analysed in detail the QCA’s draft of Part 3 from a legal perspective. Key issues are set out in the table below and should be read in conjunction with Aurizon Network’s submission in response to the IDD in relation to the powers of the QCA when considering a DAU<sup>19</sup>.

**Table 4.3 – Legal analysis of CDD in relation to Part 3**

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
13	3.3(a)(i)	<p>Clause 3.3(a) requires a compliance declaration. The declaration has two elements – that there has been no breach of Part 3 and separately that “none of the matters set out in clause 2.6(b) have occurred during” a specified period.</p> <p>Clause 3.3(b) requires the declaration to be signed by the Aurizon Network Executive Officer and “the other member of the senior management team at Aurizon Network who is most directly responsible for ensuring compliance” with Part 3.</p>	<p>(a) It is not possible to be absolute in declaring that there have been no breaches – none may have been brought to Aurizon Network’s attention. The best that Aurizon Network can offer is that the persons providing the declaration are not aware of any breaches.</p> <p>(b) The obligation to declare that none of the matters in clause 2.6(b) have occurred does not make sense. Clause 2.6(b) is a list of the matters that the Ultimate Holding Company Deed should ensure.</p> <p>(c) The issue is important because the Executive Officer’s and other member’s reputations will be adversely impacted if they have been deemed to have given a false or misleading declaration and because such a declaration is deemed to constitute a breach of the Undertaking. It may also constitute an offence under the QCA Act with penalties such as fines or imprisonment.</p> <p>(d) Clause 3.3(c) is also framed differently to sections 230 and 231 of the QCA Act. Both of those sections require that the person “knows” that the statement or document is false or</p>

<sup>19</sup> Aurizon Network (2015a).

<sup>20</sup> Based on QCA proposed drafting.

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
		Clause 3.3(c) makes a false or misleading declaration a breach of the undertaking.	<p>misleading. The QCA's drafting is inconsistent with equivalent provisions under the QCA Act.</p> <p>(e) Clause 10.7.3 purports to provide Aurizon Network's Executive Officer with some protection where the Executive Officer relies on information given by Aurizon Network personnel. However, that provision does not apply to protect the Executive Officer from the consequences under the QCA Act and does not in any case apply to the "other member" giving the declaration. At the very least clause 3.3(c) should be made subject to clause 10.7.3 and 10.7.3, which should apply to any person required to give a declaration or certification not just the Executive Officer.</p>
14	3.3(a)(ii)	The provision requires the declaration to set out the details of any breach and any remedial action.	<p>(c) For the reasons expressed in paragraph (a) Item 1 above, this clause should be amended so that it applies only to the extent that any breaches are within the knowledge of Aurizon Network.</p> <p>(d) To the extent that the clause relates to matters set out in clause 2.6(b) it should be resisted because it relates to matters that are beyond power.</p>
15	3.4(b)	The provision states that Aurizon Network intends to give effect to its function of supplying the "declared services" by supplying the Below Rail Services as defined.	<p>The drafting is circular but more importantly the provision should be made expressly subject to the provisions of the Undertaking.</p> <p>Please note that the QCA's amendments to the definitions of "Below Rail Services" and "Access" also give rise to issues. Those amendments have the effect of expanding the services comprising the declared service specified in section 250(1)(a) of the QCA Act – for example, the sale and supply of electric energy.</p>
16	3.4(c)(viii)	Obligation to provide electric transmission infrastructure and to procure electric energy for Access Seekers, Access Holders and Train Operators on request.	(c) As expressed, the clause arguably creates an obligation to build "electric transmission infrastructure". Aurizon Network should not have any obligation to build overhead electrical power supply systems, let alone "electric transmission infrastructure" which is not part of the declared service. If an obligation about electricity supply is otherwise acceptable to Aurizon Network, clause 3.3(c)(viii) should be redrafted to refer to "access to overhead electrical power supply systems".

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
			<p>(d) The obligation to procure electric energy is not within the declared service and therefore should not be listing in the clause as part of the Below Rail Services. Further comment is made on this in the discussion of clause 2.7.</p> <p>(e) Even if it were to be retained, it should not refer to “procuring”; it should use language consistent with clause 2.7 (which refers to selling or supplying electric energy). Similar issues arise later in the provision where it refers to Aurizon Network “providing” electric energy.</p> <p>(f) The provision also refers to Aurizon Network “managing electric energy supply from other parties”. It is not clear what this means, but it may refer to the possibility of an Access Seeker making arrangements to obtain electric energy directly rather than through Aurizon Network. If this interpretation is what is intended, it is not clear that Aurizon Network can even provide those services and, in any event, that service is not part of the declared service. The reference to managing electric energy supply should be removed.</p> <p>(g) The clause also refers to the procuring of electric energy where “requested” by an Access Seeker, Access Holder or a Train Operator. It is not clear why this applies in relation to an Access Holder, as once the Access Agreement is entered into any sale or supply of electric energy should crystallise as a contractual obligation. Likewise, once a Train Operations Deed is executed, there should be a contractual obligation to sell or supply electric energy. Any request needs to arise during the negotiation of the Access Agreement or Train Operations Deed – not afterwards. The obligations in relation to Access Holders and Train Operators are beyond power.</p>
17	3.4(e)	The clause seeks to prevent Aurizon Network from exercising any rights it might have as a port or mine operator to unfairly differentiate in the provision of the declared service.	<p>(a) The QCA’s CDD does not mention the restriction in clause 3.4. The closest CDD appears to be 4.13, which refers to amendments to clauses 3.4 and 3.5 and requires that Aurizon Network <b>not</b> undertake: (i) above-rail services in respect of the Rail Infrastructure; (ii) the operating or marketing of train services, unless for the provision of the declared service; or (iii) any services associated with loading vessels at a port or hold any direct or indirect interest in any port connected to the rail infrastructure. The drafting in clause 3.4(e) does not do what the CDD specifies -namely the prohibition in paragraph (iii) above. It is</p>

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
			<p>therefore not clear what the QCA's intent is for the proposed drafting or whether the QCA is actually intending to prohibit Aurizon Network from holding any interest in a port. (Please also note that the CDD only refers to port service whereas the drafting in clause 3.4(e) refers to both ports and mines.)</p> <p>(b) Despite the above uncertainty, even if Aurizon Network did for instance own and operate a port which was a destination in the CQCR, the QCA has no jurisdiction to regulate the way in which Aurizon Network provides access to those port services (unless the port is a regulated port). Any attempt by the QCA to regulate the port business would be outside the QCA powers.</p> <p>(c) Likewise, the QCA has no power to prevent Aurizon Network from holding an interest in a mine or a port or any other business or from providing any services in relation to mine, port or other activities.</p> <p>(d) The QCA's drafting of the proposed clause 3.4(e) is also uncertain. For example, it refers to the declared service being "provided in a manner that unfairly differentiates in a material way". While the QCA seeks to define "material way" by reference to section 137(3) of the QCA Act, it is unclear what Aurizon Network is differentiating between.</p> <p>(e) Further, paragraph (iv) requires that if a circumstance in paragraphs (i) or (ii) arises Aurizon Network must "provide supporting evidence that may be requested by the QCA". It is impossible to know what this evidence is supporting or to otherwise know what this means.</p>
18	3.5(a)	Below Rail Service are required not to be transferred, delegated, contracted out to or otherwise undertaken by a Related Operator unless the Below Rail Services fall within a specified list.	(d) While Clause 3.5(a) appears permissive, the defined terms used in it and the operation of subsequent provisions in Part 3 make the flow of Confidential Information necessary to take advantage of the right of delegation practically difficult. The drafting also calls into question the ability of Aurizon Network to achieve the objectives of the Aurizon Group's functional model, where for example an employee involved in corporate governance is performing services for both below rail and above rail service areas.

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
			(e) To address these concerns an express right to disclose confidential information without the need for compliance with other aspects of Part 3 would be the most direct solution.
19	3.6(d)	If the activities of a project working group (whose members include staff from a Related Operator or Related Competitor) associated with the operation of a Supply Chain affect or could affect the Access of Third Party access Holders of Access Seekers, then Aurizon Network must enter into the Confidential Information Register the details.	<p>(c) This clause is uncertain in meaning and broad in application. It could readily extend to legitimate meetings which have no direct impact on supply chains, but which are associated with them. For example, the negotiation of enterprise agreements which relate to employees of both Aurizon Network and Aurizon Operations.</p> <p>(d) How would this affect projects such as a joint customer, above rail operator and below rail project to improve supply chain throughput for this customer? Would a customer want this recorded in the Confidential Information Register?</p> <p>(e) This is very broad. Could it pick up supply chain coordination initiatives run across the industry – i.e. including above and below rail, other operators, customers and ports? Is this intended? If so, what is the point of including this in the register?</p> <p>(f) The definition of “Supply Chain” is not sufficiently linked to the declared service.</p>
20	3.6(f)(ii)	Aurizon Network must not assign, transfer, delegate or contract out to any Aurizon Party any regulatory function or position relating to the development, application and interpretation of the undertaking.	This provision will result in all regulatory functions and positions relating to the development, application and interpretation of the undertaking needing to be Aurizon Network employees or unrelated external contractors. This will have ramifications for the provision of corporate services within the Aurizon Group and if interpreted literally may even prevent Board approval of DAUs.
21	3.7.1(a)	Obligation for Aurizon Network to provide the QCA with general purpose financial statements for Aurizon Network and an obligation to provide supplementary financial statements separately identifying the	<p>(d) The obligation to provide general purpose financial statements in clause 3.7.1(a)(i) is beyond power. The QCA has no statutory right to see financial statements that relate to any part of Aurizon Network’s business that is not relevant to the provision of the declared service.</p> <p>(e) The QCA can ask for financial statements relating to the declared service business as contemplated by clause 3.7.1(a)(ii)(A) but cannot do so in the way the clause is expressed. It will need to be reworded.</p>

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
		declared service business from other businesses.	(f) Clause 3.7.1(a)(ii)(B) as expressed is beyond power because the QCA Act does not contemplate the provision of financial information relating to other members of the Aurizon Group. In any case, to the extent that Aurizon Network incurs a proportion of “common costs” that detail would be included in the financial statement under clause 3.7.1(a)(ii)(A).
22	3.7.1(c)(ii)	The clause includes an obligation for Aurizon Network’s Executive Officer to certify the financial statements.	There is no need for the Executive Officer to certify the financial statements because they must be audited – see clause 3.7.1(c)(iii).
23	3.7.2	The financial statement are to include details on self-insurance levels, claims and payouts.	(d) The QCA can only require this information about the level of self-insurance for the Aurizon Network’s regulated business – not all of its business as proposed by the QCA. (e) The information required by this clause is likely to be confidential. Consequently, the Undertaking should make it clear that the information must be kept confidential by the QCA. (f) It is not clear to us why the QCA needs the information about the number, type, resolution and quantum of claims.
24	3.7.3	The Auditor for the financial statements should be, or have the assistance of a person with expertise and experience in, the area of costing railway activities.	Given the nature of the audit described in clause 3.7.3(c) (which is a standard financial audit), the requirement for rail expertise is irrelevant.
25	3.8	Aurizon Network is required to ensure that it is “managed independently” from Related Operators and Related Competitors.	It is not clear what is meant by the words “managed independently”. To overcome this, the deleted clause 3.9(c) from Aurizon Network’s drafting should be reinserted. Clause 3.8(a)(ii) will also need to be amended to remove the supervision point.

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
26	Confidential Information	The QCA has deleted the concept and examples of Protected Information and resorted to a modified form of the definition of Confidential Information from UT3.	<p>Aurizon Network's previous submissions have referred to the vague nature of the definition and its reliance on the concept of affecting "the commercial affairs" of the owner of the confidential information.</p> <p>The QCA's approach has ignored the criticisms. More importantly the approach taken by the QCA to Section D on confidentiality fails to address the problem that the QCA should be concerned about and exposes Aurizon Network to significant compliance risk because of the vague nature and extent of the obligations proposed.</p> <p>In addition to other comments below, the deleted clauses 3.11 and 3.12 (perhaps amended to refer to "Confidential" rather than "Protected" information) should be reinstated.</p> <p>Please further note that the QCA's definition of "Confidential Information" is circular.</p>
27	3.9	The QCA's drafting prohibits any attempt to agree a confidentiality regime that waives any requirement or obligation of Aurizon Network under Part 3, renders any purported waiver of no effect and if you agree any different confidentiality arrangement you must apply with <b>both</b> that arrangement and Part 3.	<p>(c) As Part 3 is designed to protect Aurizon Network's counterparties, it is not clear why those counterparties cannot agree to release Aurizon Network from certain obligations particularly in respect of confidentiality. It may be in their interests to do so.</p> <p>(d) If the QCA is concerned that waiving a confidentiality obligation would give Aurizon Operations a potential advantage against other rail operators, it is within the counterparty's control to give those other rail operators the same information at the same time.</p> <p>(e) The restrictions in clauses 3.9(a) and (b) should be removed.</p> <p>(f) In any case, it is not rational or reasonable to have Aurizon Network comply with two separate sets of confidentiality obligations.</p>
28	3.11(a)	Overarching commitment to information security	<p>It needs to be made clear that where the undertaking requires disclosure of certain information (as it does in many places), Aurizon Network is not in breach of Part 3 as a result of such disclosures. Aurizon Network should not be unreasonably constrained by Part 3 in order to make the disclosures required by the Undertaking.</p> <p>The QCA's drafting appears to suggest otherwise.</p>
29	3.11(b)	Obligation not to unfairly advantage a Related Operator or Related Competitor by disclosure of Confidential	<p>(a) This clause is unnecessary. The remedy for a breach of the provisions arises under the QCA Act. An additional provision in the Undertaking is not required.</p>

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
		Information in a way that constitutes a breach of specified provisions under the QCA Act.	(b) Use of term “likely result” is inappropriate. The sections under the QCA Act referenced have a purpose, not an effects test.
30	3.12 and 3.13 (and their interplay with clause 3.14)	The QCA has drafted a complex, opaque, legally uncertain and unworkable regime for permitted disclosures of Confidential Information.	<p>(a) Clause 3.12 purports to apply both clauses to disclosures within Aurizon Network. The restrictions within clause 3.12 and 3.13 make the application of the clauses unworkable. For example, <u>each</u> and <u>every</u> disclosure <u>within Aurizon Network</u> would require:</p> <ul style="list-style-type: none"> <li>• that the Recipient first be advised that the information is confidential;</li> <li>• that each item of Confidential Information be clearly identified as such;</li> <li>• the relevant details of the information to be included in the Confidential Information Register;</li> <li>• that the Recipient sign a declaration of awareness and understanding;</li> <li>• that the owner of the Confidential Information has provided its prior written consent to such disclosure.</li> </ul> <p>(b) Disclosures outside Aurizon Network but within the Aurizon Group or to third parties is even more restrictive. Such disclosures would require compliance with all of the above as well as additional requirements. For example, a disclosure to anyone in the Aurizon Group outside of Aurizon Network would require the Recipient (e.g. a board member or an in-house lawyer) to execute a form of confidentiality agreement enforceable by both Aurizon Network and the owner of the confidential information. It is not clear why both a declaration and an enforceable confidentiality agreement would be needed.</p> <p>(c) A threshold requirement of the QCA’s regime (in clause 3.12(b)) which affects all proposed disclosures of confidential information requires that the Recipient require access to the information “for the purpose of assisting Aurizon Network to comply with any of its obligations under this Undertaking”. This means, for example:</p> <ul style="list-style-type: none"> <li>• Aurizon Network could not disclose to the Aurizon Network board of directors or to the CEO of the Aurizon Group any Confidential Information (including for</li> </ul>

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
			<p>example financial information about a particular access holder or access seeker), unless it was for the purpose of assisting Aurizon Network to comply with the undertaking;</p> <ul style="list-style-type: none"> <li>Aurizon Network could not disclose Confidential Information to its external lawyers for the purpose of seeking advice on whether Aurizon Network had complied with an access agreement. Given that external lawyers are already obliged to keep matters confidential it is not reasonable or appropriate for the QCA to restrict disclosures in the way it proposes. The QCA's drafting has the effect of denying Aurizon Network the ability to get legal advice;</li> <li>Clause 3.12(b) also does not make sense in relation to other persons – for example, financiers. Financiers may need the information for say, funds raising, or sale of business advice that does not relate to compliance with the Undertaking.</li> </ul>
			<p>(d) Clause 3.12(b) is also inconsistent with aspects of clause 3.13. For example, clause 3.13(a) only applies where Aurizon Network complies with clauses 3.12(b) and (c). However, under clause 3.13(a) disclosure is purportedly permitted where, for example, it is required or compelled by any Law. Clause 3.12(b) would seem to be directly inconsistent with this - the result in this example being that the Undertaking obligation on Aurizon Network would be inconsistent with its obligations at law to disclose information.</p>
			<p>(e) For disclosures outside of Aurizon Network where ongoing access is required, a "review date at which access or disclosure of the information expires" is to be recorded in the Confidential Information Register. The meaning of this requirement is uncertain. How would this date be determined and what happens on a review date if that is the date on which access to the information "expires" and there is not suggestion that it may be extended? Note too that this obligation applies where the disclosure is to financiers to advisers as well as to other parties outside of Aurizon Network, and in respect of those financiers and advisers there are also additional obligations under clause 3.13(c).</p>

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
			<p>(f) Clause 3.13(d)(vi) is an important provision for Aurizon Network. The provision needs to be clarified – in particular the words “to the extent permitted by this Undertaking” and the reference to “Above Rail Services” which is not limited to services relating to the declared service. Please note that this issue with the definition of “Above Rail Services” also affects other definitions such as “Related Operator” so that they apply to business units that may be entirely uninvolved with Above Rail Services relating to the declared service.</p> <p>(g) Aurizon Network requests the QCA consider whether the list of persons in clause 3.13(d)(vii) is appropriate. The list Aurizon Network had in the deleted 3.12(a) was more extensive – although used for a different purpose. Please note that effect of the list in clause 3.13(d)(vii) is that Aurizon Network won’t need to obtain the prior written consent of the owner of the Confidential Information for a disclosure to any of those persons listed and conversely Aurizon Network will need the consent for a disclosure to other persons e.g. a manager that is not employed by Aurizon Network.</p> <p>(h) It is not clear what clause 3.13(e) is intended to achieve given that clause 3.12 is subject to clause 3.13. This also appears to mean that the clause is circular.</p> <p>(i) Aurizon Network does not agree to clause 3.13(g)(ii), which contemplates that Aurizon Network must accept any request made by the owner of Confidential Information to limit a disclosure required by the ASX listing rules.</p> <p>(j) Clause 3.13(f) becomes potentially problematic for Aurizon Network given the uncertainty with the definition of Related Operator. In part this uncertainty arises because it is unclear what “functional units within the Aurizon Group” are. The Aurizon Group functional model does, for example, involve Aurizon Network calling on environment and safety advisors within Aurizon Operations. The QCA’s drafting will have serious ramifications for Aurizon Network if it prevents those types of arrangements.</p>
31	3.14	The QCA requires Aurizon Network to consult with access holders and railway operators to develop the Confidential Information Register for	(a) The obligation to consult and develop a register makes no sense given the very detailed “minimum” requirements for the register set out in clause 3.14(c). Aurizon Network questions what more could be required.

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
		approval by the QCA. The QCA can require changes.	<p>(b) Given the fundamental importance of the register to various provisions in the QCA's drafting, it is not appropriate to defer the contents of that register and to make it subject to what is effectively a post-undertaking amendment potentially drafted and approved by the QCA itself. The QCA would be acting beyond power if it requires what is in the drafting.</p> <p>(c) Please note that the register obligations relates to all Confidential Information and all disclosures whether internal or external to Aurizon Network, which is the effect of clause 3.14(c)(i) and/or (ii)(A).</p> <p>(d) Clause 3.14(c)(i) requires details on person who "request" access to Confidential Information to be included in the register. The details of such persons are not relevant. It only becomes relevant if a person has actually be provided with access to Confidential Information. Aurizon Network should not be required to keep details of persons who merely request access to Confidential Information.</p> <p>(e) Clause 3.14(c)(ii)(B) obliged Aurizon Network to continuously update the register to show when each Recipient ceased to have access to Confidential Information. This is onerous and is difficult to manage in practice, particularly given the wide range of information and recipients the QCA's draft intends to be included in the register. Clause 3.14(c)(ii)(D) requires that the register show in respect of <u>each</u> Recipient (and therefore each disclosure) "the purpose for which the Confidential Information is to be used...including the decision made using the Confidential Information". Requiring the disclosure of each decision made appears to be completely unworkable and it is not clear why it would be relevant. This could, for example, require Aurizon Network to disclose every train scheduling decision it makes, as this involves the use of Confidential Information as defined in the QCA's draft.</p> <p>(f) In addition, where the Recipient is an external legal adviser, for example, the fact of that disclosure to the legal adviser would need to be entered in the register and that alone, whether or not the provision also requires the decision made by that lawyer to also be entered in the register (which it arguably does), would have the effect of potentially waiving legal professional privilege.</p>

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
			<p>(g) Other examples may arise where this is a problem. For example, as regards financiers, Aurizon Network may not always wish to record in the register the purpose of the disclosure, if that purpose is confidential, e.g. advice on a potential bond issue.</p> <p>(h) Clause 3.14(c)(iii) requires Aurizon Network to attach to the register a record of any confidentiality agreement or any confidentiality provisions that relate to the Confidential Information. Because of the very wide and ambiguous definition of Confidential Information, this obligation will be onerous as most agreements would contain some confidentiality provisions.</p> <p>(i) Clause 3.14(f)(ii) contemplates an audit to ensure that “the processes and procedures underpinning the collection of information” for the register is “fit for purpose”. Whatever that means, the provision allows the QCA in effect to change the register requirements under the Undertaking should the audit report make any recommendations in that regard. (This flows from the audit provisions of the Undertaking.) This aspect of clause 3.14(f)(ii) is beyond power because it enable amendments to the Undertaking by the QCA.</p>
32	3.15	Mandatory training obligations	Clause 3.15(b)(i)(C) requires <u>all</u> employees of the Aurizon Group (which would include employees that have nothing to do with the CQCR) to undertake confidential information training once in every two years. This would be beyond power.
33	3.16	High risk personnel	The definition of High Risk Personnel is ambiguous and it is not possible to say with any certainty who would fall within that definition.
34	3.17	Exit certificates	<p>(a) The requirement for exit certificates is not required to address ringfencing issues and is therefore not relevant to the undertaking. It also imposes an additional cost and compliance burden on the business.</p> <p>(b) Clause 3.17(a)(ii) contains an unqualified, absolute obligation on Aurizon Network to have departing High Risk Personnel undergo a debriefing session on the obligations to manage Confidential Information and to obtain an exit certificate signed by that person. Aurizon Network has no legal ability to compel that outcome but would nevertheless be in breach of the Undertaking if a High Risk Person refused to participate.</p>

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
			(c) Clause 3.17(c) requires Aurizon Network to ensure that all conditions of employment or engagement contain an obligation to attend debriefing sessions and to provide exit certificates. Aurizon Network cannot comply with this obligation in relation to existing contracts of employment or engagement, and the QCA does not have the power to determine the terms of AN's employment or engagement contracts.
35	3.18	Security measures	<p>(a) Clause 3.18(a) is an absolute obligation to ensure security of Confidential Information and that people only obtain access to the extent permitted by the Undertaking. The obligation is extremely broad and absolute. Given all of the other protections, the obligation would appear to be unnecessary, certainly as it is currently expressed.</p> <p>(b) Clause 3.18(c)(ii) requires persons to be accompanied by an Aurizon Network employee "at all times" while in Aurizon Network's premises. This seems unnecessary and onerous.</p> <p>(c) Clause 3.18(d) is extremely broad in its application. It requires Aurizon Network to maintain a record of all non-Aurizon Network Personnel who have accessed any premises where Confidential Information is located or stored. This would include, for example, couriers, maintenance contractors etc.</p> <p>(d) The provision is not sufficiently targeted to address the ringfencing issue. Even if it was relevant to include such a provision, it would need to target restricting the access of Related Operator or Related Competitor employees.</p>
36	3.19	Decision making	A similar clause is contained in the 2010AU, however, the clause here is drafted in a materially different way. Clause 3.19(a)(ii) is beyond power because it changes the language and requirements of the QCA Act.
37	3.20	Complaints and waiver	(a) The clause purports to give Access Seekers, Access Holders and Train Operators (the clause also unnecessarily refers to Third Party Access Seekers) the right to complain to the QCA about a breach of the Ultimate Holding Company Support Deed. The process in the clause enables the QCA to require an audit of compliance and the audit provisions effectively allow the QCA to re-write the Undertaking and to find a breach if Aurizon

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
			<p>Network fails to implement the audit recommendations. These aspects of the clause are beyond power.</p> <p>(b) Clause 3.20(b) has the effect of compelling Aurizon Network to waive its right to confidentiality. This would appear to be beyond power.</p> <p>(c) Clause 3.20(c) has the effect that unless otherwise agreed by either Aurizon Network <u>or</u> the Complainant, a written complaint and all accompanying information (including documents) will not be Confidential Information. While it is not clear who the Complainant or Aurizon Network is agreeing with, it appears to allow one party to unilaterally remove the relevant information being Confidential Information. It is not clear why this clause is needed or what its purpose might be. In any event, it should (and legally cannot) have the effect of affecting a third party's or any other party's confidentiality rights. To avoid confusion, this should be expressly acknowledged.</p> <p>If the QCA is proposing to publish complaints, it should certainly not do so prior to completion of the investigation when all the facts are known.</p> <p>(d) Note also in addition to the audit and the provisions allowing the QCA to re-write the Undertaking discussed above, the QCA has amended clause 11.1.1 to give itself the additional power to treat non-compliance with the ring-fencing provisions as an access dispute. The QCA should not have two procedures dealing with the same non-compliance issue and cannot invest itself with arbitral powers in relation to ring-fencing disputes – such disputes would be covered by section 158A of the QCA Act which provides for an action for enforcement by the Supreme Court.</p>
38	3.21(d)(ii)	This provision allows the QCA, an Access Seeker or Access Holder to request Aurizon Network to review and amend the Line Diagrams if it is of the reasonable opinion that the Line Diagrams “reflect a	There is nothing in clause 3.21(c) to contravene.

Item	Clause Reference <sup>20</sup>	Effect of clause	Issue
		change to Rail Infrastructure that contravenes clause 3.21(c)".	
39	3.22	Transfer of rail transport infrastructure from an Aurizon Party	The QCA's provision is beyond power. The QCA has no power under the QCA Act that would allow it to compel Aurizon Network to acquire the ownership of any rail transport infrastructure. Additionally, ownership issues cannot be resolved by the QCA as contemplated by clause 3.22(d) – the provision is beyond power.

## Practical resolution – a revised version of Part 3

In order to address the legitimate concerns expressed by the QCA and stakeholders in relation to the requirement for a ring fencing regime, and in order to address the clear shortcomings and unworkability of the regime proposed by the QCA in the CDD, Aurizon Network proposes a version of Part 3, which uses UT3 as its base, and then go on to amend it for clarity and for certainty.

Importantly, Aurizon Network's version of Part 3 submitted as part of this response, sets out a clear definition of Ringfenced Information, which avoids confusion with the distinct and broader concept (in the general law, and also in general usage) of confidential information, and also linked clearly to the concept of a Protected Third Party, in order to prevent the regime needlessly applying also to information provided by related operators. The revised Part 3 uses this clear definition as the basis for a comprehensive Ringfencing Register, in order to provide the transparency sought by the QCA in relation to the flow of Ringfenced Information.

Aurizon Network is confident that this carefully considered, revised ring fencing framework:

- is designed to remove the opportunity for the disclosure or use of 3<sup>rd</sup> party access holder confidential information (Ringfenced Information) to a related party that would provide a competitive advantage over other above rail operators (or access holders) in the CQCR;
- ensures that Aurizon Network's day-to-day operations are managed independently from related Parties that operate in both upstream and downstream markets;
- ensures that Aurizon Network is the entity with the responsibility for the provision of below rail services including the assessing, allocation and management of capacity and scheduling of trains;
- ensures transfers and secondments of employees within the Aurizon Group are properly managed (and in some cases prohibited) so that ringfenced information is not misused or disclosed as a result of those staff movements
- expressly provides Aurizon Network with a list of those limited circumstances and reasons for which ringfenced information can be disclosed (without ever permitting such disclosure to those Aurizon personnel responsible for marketing and contracting of above rail services within the CQCR).
- creates a transparent register for the recording of disclosures of ringfenced information which will allow the QCA and other stakeholders to monitor information flow, specifically to whom and for what particular purpose (not including decision making purposes)
- ensures that all personnel with access to ringfenced information are made aware of the ringfencing requirements and that High Risk personnel receive appropriate training that outlines the required obligations for which they must comply; and
- includes an appropriate complaints handling and investigation process coupled with appropriate record keeping and audit rights.

# Testing Aurizon Network’s proposal against the QCA Act, QCA improvement suggestions and QCA criteria

## 1. QCA Act

The QCA Act requires an Access Undertaking must ‘include provisions for identifying, preventing and remedying conduct of the related access provider that unfairly differentiates in a material way’<sup>21</sup>.

Aurizon Network’s proposal includes precisely such provisions, together with a range of additional obligations and protections.

## 2. QCA improvement suggestions for previous Aurizon Network proposed ringfencing regime

The QCA’s CDD<sup>22</sup> suggested that the QCA considered it appropriate for Aurizon Network to amend its 2014DAU in the manner set out in the table below. Aurizon Network’s revised version of Part 3 meets these requirements.

**Table 4.4 – Aurizon Network’s proposal against QCA’s suggestions for improvement**

Item	QCA suggestion	Aurizon Network Solution as reflected in revised Part 3
1	strengthen the role of the ultimate holding company support deed and confidentiality agreement provisions	Robust UHCSO already proposed on a voluntary basis.  Robust definition of Ringfenced Information, robust controls on flow of information, and transparency of information flow through Ringfencing Register.
2	maintain registers of parties that have been provided information and the process for making any decisions using such information; and having this information available for audit	Robust and detailed register of ringfenced information is included in clause 3.9 of Aurizon Network’s proposed draft of Part 3
3	include tiered employee training measures regarding the treatment of confidential information	Tiered training arrangements proposed for <b>all Aurizon employees</b> (even though this is not legally required) is included in clause 3.10 of Aurizon Network’s proposed draft of Part 3
4	require secondments/transfers of employees between Aurizon Network and another Aurizon party to be notified to the QCA prior to the secondment/transfer being made	Secondments and transfers to be included in ringfenced information register and register to be available for QCA audit and inspection – refer to clause 3.9 of Aurizon Network’s proposed draft of Part 3.
5	require Aurizon Network to identify Aurizon Network employees separately from the remainder of the Aurizon Group employees, providing clearer separation when employees do transfer	Ringfenced information register will clearly identify individuals who have access to ringfenced information, and whether they are employees of Aurizon Network or otherwise

<sup>21</sup> QCA Act, 1997, Part 5, s137

<sup>22</sup> Queensland Competition Authority (2015a). p.83.

### 3. QCA criteria for ring fencing regime

The QCA's CDD<sup>23</sup> included a table setting out the QCA's approach to assessing the effectiveness of the 2014DAU ringfencing regime. Aurizon Network's revised version of Part 3 addresses each of the criteria set out in the QCA's table, as demonstrated below.

**Table 4.5 – Assessment of Aurizon Network's proposed Part 3 against QCA criteria**

Item	QCA assessment criterion	QCA rationale	Aurizon solution as reflected in revised Part 3
1	Does the regime support the objective of promoting effective competition in upstream and downstream markets?	This involves assessing whether the: <ul style="list-style-type: none"> <li>• commitments to avoid anti-competitive behaviour and unfair differentiation of a material nature; and</li> <li>• the ultimate holding company support deed (UHCSA) have sufficiently strong provisions within them to be fit for purpose.</li> </ul>	<ul style="list-style-type: none"> <li>• Commitments reflected in Part 2, and also in objectives of Part 3 (refer 3.1)</li> <li>• UHCSA is voluntary – refer Aurizon Network's response to the IDD – and includes robust requirements which ensure the declared entity complies with its obligations</li> </ul>
2	Are the management of confidential information and decision making principles credible and effective?	This involves assessing whether the ring-fencing regime: <ul style="list-style-type: none"> <li>• protects confidential information from inappropriately flowing between the owner/operator of the declared service and upstream or downstream activities or related parties</li> <li>• provide suitable decision making principles.</li> </ul>	<ul style="list-style-type: none"> <li>• Clear definition of ringfenced information</li> <li>• Clear obligations in relation to division of responsibility and resources (3.3, 3.4, 3.5)</li> <li>• Clear commitment to information security and obligations to protect information (3.7) and ensure transparency of information flows (3.9)</li> <li>• Clear disclosure regime and decision-making principles (3.8)</li> </ul>
3	Are the operational and functional separation provisions credible and effective?	This involves assessing whether the ringfencing regime effectively separates: <ul style="list-style-type: none"> <li>• Aurizon Network's operations from the remainder of the Aurizon Group</li> <li>• operations regarding the declared service from other operations.</li> </ul>	<ul style="list-style-type: none"> <li>• Clear obligations in relation to division of responsibility and resources (3.3, 3.4, 3.5)</li> <li>• Clear obligations in relation to independent management (3.9)</li> </ul>
4	Are the employee separation provisions credible and effective?	This involves assessing whether the ringfencing regime places effective controls on staff movements between Aurizon Network and related parties.	<ul style="list-style-type: none"> <li>• Significant controls on staff movements – including prohibitions</li> </ul>

<sup>23</sup> Queensland Competition Authority (2015a). Table 5, p.88.

Item	QCA assessment criterion	QCA rationale	Aurizon solution as reflected in revised Part 3
			<ul style="list-style-type: none"> <li>• Transparency through recording of all such movements in register</li> </ul>
5	Are the management separation provisions credible and effective?	This involves assessing whether the ringfencing regime ensures the independence of management and Aurizon Network corporate decision making regarding the declared service, from other commercial activities.	<ul style="list-style-type: none"> <li>• Clear obligations in relation to independent management (3.9) which reflect 2010AU drafting preferred by QCA</li> </ul>
6	Are the accounting separation provisions credible and effective?	<p>This involves assessing whether the ringfencing regime effectively separates:</p> <ul style="list-style-type: none"> <li>• Aurizon Network's accounts from the remainder of the Aurizon Group</li> <li>• the accounts, relating to operations associated with the declared service, from other operations.</li> </ul>	<ul style="list-style-type: none"> <li>• Clear obligations in relation to preparation of separate accounts for regulated business in accordance with Costing Manual, and for independent audit of same (3.14, 3.15)</li> </ul>
7	Are the reporting, compliance and auditing provisions credible and effective?	<p>This involves assessing whether the ringfencing regime:</p> <ul style="list-style-type: none"> <li>• provides transparent, timely and meaningful information reporting</li> <li>• provides an effective compliance regime</li> <li>• includes a robust and transparent audit process.</li> </ul>	<ul style="list-style-type: none"> <li>• Ringfencing Register is a clear improvement in transparency, and is supported by audit and inspection rights</li> <li>• Robust complaint handling process</li> <li>• Strengthened and practical reporting, compliance and audit provisions in Part 10</li> </ul>

## Ultimate Holding Company Support Deed

Aurizon Network restates its response to the IDD in relation to the Ultimate Holding Company Support Deed (UHCS D).<sup>24</sup> The UHCS D is a voluntary commitment and remains so. Aurizon Network is prepared to volunteer the version of the UHCS D submitted in response to the IDD. Aurizon Network is not prepared to make the changes suggested by the QCA in the CDD, as the QCA has no power to request such changes, or the UHCS D at all.

For completeness, Aurizon Network has set out in the table below the reasons why it cannot and will not accept the proposed re-drafting of the UHCS D.

<sup>24</sup> Aurizon Network (2015). s.3.13, p.52; s.4.4, pp.59-61.

**Table 4.6 – Aurizon Network’s concerns with the Ultimate Holding Company Support Deed**

Effect of clause	Issue
The terms of the UHCSD.	<p>(a) As a general principle, the QCA has no power under the QCA Act to require an UHCSD or to require another member of the Aurizon Group to comply with or assume obligations under Aurizon Network’s (AN’s) undertaking. The UHCSD proposed by AN had been offered on a voluntary basis. The QCA in its CDD has sought to substantially amend the UHCSD. AN has offered the UHCSD on a voluntary basis, and continues to do so, without the amendments proposed by the QCA.</p> <p>(b) For completeness, this table deals with the issues created by the QCA’s amendments to this entirely voluntary position offered by AN.</p> <p>(c) Clause 3.1(a)(i) requires Aurizon Holdings (AH) and other members of the Aurizon Corporate Group (Group) to comply with the arrangement in Part 3. It is neither within power nor appropriate for the QCA to make and the Group defacto parties to the undertaking. Any arrangements under Part 3 can only apply to AN, and the AN version of the UHCSD was drafted accordingly.</p> <p>(d) Clause 3.1(a) sets out a suite of obligations that (AH) must, and must use reasonable endeavours to procure that the rest of the Aurizon Corporate Group (<b>Group</b>), comply with Part 3. Some of the obligations set out in clause 3.1(a)(i) to (viii) are drafted in manner that they will apply to AN. Where this occurs, AH is effectively acting as a guarantor for AN’s compliance. This is simply not contemplated by the QCA Act, and has never been offered voluntarily by AN. The QCA has no power to require a guarantor for an access provider’s compliance.</p> <p>(e) Clause 3.1(a)(ii) requires AH and all members of the Group “to take all necessary steps” to enable to AN to comply with Part 3. The extent of this obligation is unbounded, uncertain and unnecessary.</p> <p>(f) Clause 3.1(a)(iv) requires AH and other members of the Group to ensure their conduct cannot prevent or hinder AN’s compliance with Part 3. It is not clear what this means or how they could achieve that result particularly for companies that are not AH. Given clause 3.1(a)(iii), clause 3.1(a)(iv) is unnecessary and largely of no affect. Therefore, clause 3.1(a)(iv) should be deleted.</p> <p>(g) Clause 3.1(a)(v)(A) purports to require AH and other members of the Group comply with provisions of the Undertaking relating to Confidential Information received as if bound by the same obligations as AN. The QCA cannot make AH and the rest of the Group defacto parties to AN’s Undertaking. The QCA is acting outside of power for it to do so. Additionally:</p> <ul style="list-style-type: none"> <li>• The QCA’s proposal is unworkable – for example, it would require AH and each Group member to maintain a separate Confidential Information Register that is available to Access Holders and Access Seekers, to be subject to complaints, audits and dispute resolutions provisions relating to Confidential Information. It may also potentially open up an even wider class of Confidential Information to regulation by the QCA.</li> <li>• The QCA would be vesting itself with powers that it does not have under the QCA Act; namely to hear disputes about those matters.</li> </ul>

Effect of clause	Issue
	<ul style="list-style-type: none"> <li>It is not clear that the provisions in the Undertaking relating to Confidential Information can even sensibly be applied to AH and the rest of the Group. It is also unnecessary, given the detailed and significant confidentiality and ringfencing provisions to which AN is already subject.</li> </ul>
(h)	<p>Clause 3.1(a)(v)(C) purports to require AH and the other members of the Group to “secure, protect and take all steps” necessary to prevent any use or disclosure of Confidential Information other than as permitted under the Undertaking. The QCA has already proposed a range of heavy handed obligations on AN before AN can disclose Confidential Information to an Aurizon Party – including requiring declarations and confidentiality agreements. No additional contractual obligations are needed. Additionally, the clauses also appear to require AH and the rest of the Group to effectively guarantee AN’s compliance in respect of this same conduct even though Part 3 already sets out various obligations for AN in this respect.</p>
(i)	<p>Clause 3.1(a)(vi) requires AH (and each members of the Group) to have the authority to provide or authorise access to land that an Access Seeker or Access Holder requires access to in accordance with the provision of Access under the Undertaking where the land is owned or leased, licensed or otherwise held by a member of the Group. This clause is inappropriate, outside power and unworkable including because:</p> <ul style="list-style-type: none"> <li>S250(3)(b) of the QCA Act deals conclusively with this issue – it makes such assets the subject of the declared service, and the QCA Act and the Undertaking regulate the provision of access accordingly.</li> <li>The QCA cannot require AH, for example, to provide or authorise access to land owned or controlled by a different party.</li> <li>The QCA’s drafting requires AH and each member of the Group to renegotiate existing leases and other arrangements in order for AH and each member to have the power provide or authorise access to that land. This obligation extends to leases and other arrangement to which AH and the other members are not necessarily a party.</li> <li>There is no reason why AH and each other member of the Group should have authority to provide or authorise access to land owned, leased or otherwise control by, for example, AN. Indeed doing so will not be possible under AN’s lease arrangements and gives rise to potential rail accreditation issues. Similar issues may arise with other entities.</li> </ul>
(j)	<p>Clause 3.1(a)(vii) requires AH and each member of the Group to take steps required to allow AN to procure a sale or supply of electric energy (presumably the sale or supply of electric energy to a third party Access Seeker, Access Holder or Train Operator). The obligation has no nexus with the undertaking as AN has no obligation to “procure” a sale or supply – AN’s obligation is to sell or supply not to procure. In any case, it is also unclear what steps would be required by AH or another member of the Group. AN is not aware of any steps which the QCA could legitimately require. In any event, the sale or supply of electric energy is not part of the declared service and the QCA has no jurisdiction to impose obligations even in respect of AN.</p>

Effect of clause	Issue
	<p>(k) The first part of clause 3.1(a)(viii) has no application as AH and other members of the Group are not required to comply with the undertaking. In respect of the second part, to the extent that AN is required to comply, that is a matter to AN and the obligation is not necessary in that regard. The QCA cannot impose generic obligations to enable or assist AN to comply with the Undertaking. Again, general compliance with the Undertaking is a matter for AN; not AH and the other members of the Group.</p>
	<p>(l) Clause 3.1(b) makes no sense because it purports to bind parties who are not parties to this deed, namely the Group members other than AH.</p>
	<p>(m) Clause 3.1.2 (there is no clause 3.1.1) requires that AH must, and must procure each member of the Group (although it refers to the undefined term “Aurizon Group”), to ensure all Rail Infrastructure is and remains owned by AN and to take all necessary steps to ensure AN owns all Rail Infrastructure developed by AN in accordance with Part 8 (except where otherwise required under a User Funding Agreement). Clause 3.1.2 is incorrect, inappropriate and outside power including because:</p> <ul style="list-style-type: none"> <li>• The QCA has no power to control the ownership or leasing of infrastructure or to prevent, restrict or otherwise affect any entity in disposing of, subletting or otherwise transferring ownership or control of infrastructure.</li> <li>• AN does not even own most of Rail Infrastructure now; the bulk of it is leased from Queensland Treasury Holdings.</li> <li>• AN may be required to pass ownership of newly developed infrastructure to other entities under its infrastructure leasing arrangements.</li> </ul>
	<p>In any event, the QCA’s proposed requirements are not even remotely required for the purpose of the Undertaking or the QCA Act.</p>
	<p>(n) Clause 3.2 purports to impose a condition precedent on any sale or transfer of AN or an action that results in AH ceasing to be the ultimate holding company of AN, that the new ultimate holding company enter into a similar deed poll. This is an extraordinary requirement particularly in relation to a publicly listed entity. AH was willing to voluntarily accept a reasonable endeavours obligation, but this requirement by the QCA purports to actually impose (presumably require the imposition of) a condition precedent. The QCA is well outside its powers under the QCA Act.</p>

## Chapter 5 – Reporting, Compliance and Audits (Part 10)

### Summary of Aurizon Network’s Position

Aurizon Network is committed to transparency and appropriate disclosure of relevant information to the QCA and stakeholders for compliance and performance purposes. This commitment extends to ensuring fairness for all stakeholders through reporting obligations.

Noting that the reporting, compliance and audit regime in Part 10 of the CDD amended DAU is prescriptive and detailed, Aurizon Network has agreed to majority of the QCA’s proposals. There are however a few areas within the QCA’s CDD which are unacceptable as they either:

- expose Aurizon Network to uncertain regulatory obligations; or
- cannot be complied with, due to constraints in Aurizon Network’s current reporting framework, or would require material expenditure (the cost of which, on balance may not be justified by the benefit of the additional information).

The key areas of concern discussed in this response are:

- Aurizon Network needing to ensure that the contents of the Quarterly Maintenance Cost Report is agreed and included in the approved Undertaking, as this is essential in ensuring that it will be able to comply;
- the requirement to produce separate reports for GAPE, which with the exception of a small number of metrics, is not feasible given that in effect, GAPE was only established as a separate ‘theoretical system’ for pricing purposes;
- certain requirements in relation to the Condition Based Assessment (CBA) report, one of which is being unable to feasibly comply with the timing in the finalised Undertaking (depending on its approval date) and the other being the specific provisions that are intended to deal with the disclosure of confidential information (which could ultimately have the effect of limiting the Assessor’s access to necessary information to complete the CBA);
- additional obligations introduced by the QCA in relation to the audit, including an obligation to provide a copy of the draft audit report to the QCA, and obligations in relation to the implementation of the audit recommendations (including allowing the auditor to make recommendations to amend the Undertaking).

**Table 5.1 – QCA Consolidated Draft Decision**

QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(1) After considering Aurizon Network’s proposal, our consolidated draft decision is to refuse to approve the maintenance cost reporting arrangement	5.1	<b>(2)(a) Agree.</b>  <b>(2)(b) Agree.</b>
(2) The way in which we consider it appropriate that Aurizon Network amends the draft access undertaking is to:		<b>(2)(c) Agree with amendments.</b>  <b>(2)(d) Agree with amendments.</b>
(a) Provide for a stakeholder briefing and report on the planned scope of maintenance three months before the start of each year (cl. 10.3.1 of the CDD amended DAU)		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<ul style="list-style-type: none"> <li>(b) Provide for one consolidated annual maintenance cost report to be prepared and published within four months of the end of each year, including the content set out in our attached drafting (cl. 10.3.3 of the CDD amended DAU)</li> <li>(c) Provide for the preparation and approval of a quarterly maintenance cost report template upon commencement of the approved undertaking (cl. 10.3.2 of the CDD amended DAU)</li> <li>(d) Make any other amendments as proposed in our CDD amended DAU</li> </ul>		
<ul style="list-style-type: none"> <li>(1) After considering Aurizon Network's proposal, our consolidated draft decision is to refuse to approve the network performance reporting arrangements.</li> <li>(2) The way in which we consider it appropriate that Aurizon network amends the draft access undertaking is to require: <ul style="list-style-type: none"> <li>(a) Key performance information to be displayed by months (cl. 10.3.4 of the CDD amended DAU)</li> <li>(b) Amendments to content of the report as provided for in our marked-up drafting and described above, including a new indicator that details the number of CTPDMP's run each months and the stage of the process the contested paths were allocated (cl. 10.3.4(i) of the CDD amended DAU)</li> <li>(c) Other amendments as proposed in our CDD amended DAU</li> </ul> </li> </ul>	5.2	<p><b>(2)(a) Agree.</b></p> <p><b>(2)(b) Agree.</b></p> <p><b>(2)(c) Agree with amendments.</b></p>
<ul style="list-style-type: none"> <li>(1) After considering Aurizon Network's proposal, our consolidated draft decision is to refuse to approve the asset reporting arrangements</li> <li>(2) The way in which we consider it appropriate that Aurizon Network amends the draft access undertaking is to: <ul style="list-style-type: none"> <li>(a) Include a requirement for the RAB roll-forward report to be published after the QCA accepts Aurizon Network's proposed roll-forward (cl.10.4.2 of the CDD amended DAU)</li> <li>(b) Include requirements to publish condition based assessment reports, provide assessments of</li> </ul> </li> </ul>	5.3	<p><b>(2)(a) Agree.</b></p> <p><b>(2)(b) Agree.</b></p> <p><b>(2)(c) Agree with amendments.</b></p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>Aurizon network funded assets and user funded assets for each coal system, and allow for more than one assessment per undertaking term if the term extends beyond four years (cl. 10.2(c) and 10.4.3 of the CDD amended DAU)</p> <p>(c) Make other amendments as proposed in the CDD amended DAU</p>		
<p>(1) After considering Aurizon Network's proposal, our consolidated draft decision is to refuse to approve the compliance requirements</p> <p>(2) The way in which we consider it appropriate that Aurizon Network amends the draft access undertaking is to:</p> <p>(a) Include a requirement for Aurizon Network to maintain an issues register of breaches and written complaints (cl. 10.5.3 of the CDD amended DAU)</p> <p>(b) Include a requirement for the annual compliance report to be published within four months of the end of the year (cl. 10.5.2 of the CDD amended DAU)</p> <p>(c) Make other amendments as proposed in our CDD amended DAU</p>	<p>5.4</p>	<p><b>(2)(a) Agree</b></p> <p><b>(2)(b) Agree</b></p> <p><b>(2)(c) Agree</b></p>
<p>(1) After considering Aurizon Network's proposal, our consolidated draft decision is to approve the audit arrangements</p> <p>(2) The way in which we consider it appropriate that Aurizon Network amends the draft access undertaking is to:</p> <p>(a) Include requirements for annual audits of Aurizon Network's compliance with its ringfencing and other obligations, and audits (at least annually) of its reporting obligations (cl. 10.6.1 and 10.6.2 of the CDD amended DAU)</p> <p>(b) Include a requirement for the auditor to provide draft reports to the QCA (cl.10.6.4(i) of the CDD amended DAU)</p> <p>(c) Include a requirement for Aurizon Network to prepare a plan for the implementation of audit recommendations and to provide evidence that the recommendations have been implemented</p>	<p>5.5</p>	<p><b>(2)(a) Agree.</b></p> <p><b>(2)(b) Disagree.</b> This is considered unnecessary. It could also result in delays in the audit process, or result in the submission of information to the QCA that is not correct.</p> <p><b>(2)(c) Agree.</b></p> <p><b>(2)(d) Agree with amendments.</b></p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(cl.10.6.4(k)-(m) of the CDD amended DAU)</p> <p>(d) Make other amendments as proposed in our CDD amended DAU</p>		
<p>(1) After considering Aurizon Network's proposal, our consolidated draft decision is to refuse to approve the general reporting arrangements</p> <p>(2) The way in which we consider it appropriate that Aurizon Network amends the draft access undertaking is to:</p> <p>(a) Consolidate provisions relating to:</p> <p>(i) Errors in reports – one provision applies to all reports in Part 10, that requires Aurizon Network to rectify material errors found in reports within 3 months (cl.10.7.2 of the CDD amended DAU)</p> <p>(ii) Reporting by coal system – all reports require Aurizon Network to provide information by coal system, and separately for rail infrastructure where one or more reference tariffs apply, unless agreed otherwise between Aurizon Network and the QCA (cl.10.2 of the CDD amended DAU)</p> <p>(iii) Information gathering – general information gathering powers and disclosing access agreements is provided for. At the same time, include requirements that allow us to publish below-rail aspects of the access agreements, subject to certain conditions as discussed above and set out in our drafting (cl.10.7.1(c)-(d) of the CDD amended DAU)</p> <p>(b) Make other amendments as proposed in our CDD amended DAU</p>	<p>5.6</p>	<p><b>(2)(a)(i) Agree.</b></p> <p><b>(2)(a)(ii) Disagree.</b> For the reasons set out in this response, Aurizon Network is unable to report separately for GAPE, which is only maintained as a 'system' for pricing purposes, not performance and reporting purposes.</p> <p><b>(2)(a)(iii) Agree.</b></p> <p><b>(2)(b) Agree with amendments.</b></p>

## CDD 5.1 Maintenance cost reporting

### Quarterly Maintenance Cost Report

Aurizon Network would be prepared to commit to production of a Quarterly Maintenance Cost Report (as required by clause 10.3.2 of the CDD amended DAU), but *only* if there is clarity as to what material

should be included within the report prior to final approval of the 2014DAU. Aurizon Network submits that appropriate contents are as follows:

- details of total quarterly network maintenance costs (actuals);
- maintenance costs by system (Newlands, Goonyella, Blackwater and Moura);
- maintenance costs by activity / activity:
  - ballast undercutting;
  - rail grinding;
  - resurfacing;
  - General maintenance costs category
- derailments over \$100,000;
- Overall Track Condition Index (OTCI);
- The ability for Aurizon Network to provide commentary on the relevant products;
- safety incidents; and
- Below Rail Transit Time (BRTT).

The contents of this report will provide the QCA with information comparing actual maintenance costs against the approved forecast. The proposed content will enable reconciliation with the annual maintenance cost report, reflecting information that can be compiled on a quarterly basis.

It is important that the information to be included in this report is clearly set out in the approved undertaking (provided this is information Aurizon Network is able to provide), rather than left to be determined after the final approval of the 2014DAU. This is because:

- setting the content of the regulatory obligation upfront contributes to the QCA's stated goal of achieving regulatory certainty.
- Aurizon Network cannot commit to provide a report to the QCA when its terms are unknown and can be modified by the QCA following approval of the 2014DAU. Aurizon Network cannot agree to a compliance obligation without knowing if it will be able to comply with that obligation;

For that reason, clause 10.3.2 of the CDD amended DAU should be amended to plainly state the content of the report based on the items proposed above by Aurizon Network. This should replace the provisions dealing with the submission and approval of the draft format of the report, as well as the ability for the QCA to require modifications without Aurizon Network's agreement (clause 10.3.2(b)). This exposes Aurizon Network to an unacceptable level of risk.

Aurizon Network would be happy to have further discussions with the QCA to agree the contents of this report prior to the finalisation of the 2014DAU.

### **Annual Maintenance Cost Report**

With limited exceptions, discussed below, Aurizon Network does not object to the proposed contents of the Annual Maintenance Cost Report.

#### Obligation to report details of asset renewals incurred in place of maintenance

Clause 10.3.3(c)(B)(vii) of the CDD amended DAU requires Aurizon Network to:

*...report details of all capital expenditure related to asset renewal incurred in place of planned maintenance work during the relevant Year.*

Aurizon Network does not consider this clause is appropriate for the following reasons:

First, Aurizon Network plans its asset renewals and maintenance tasks in tandem. That is, when undertaking its maintenance forecasting and planning, Aurizon Network has regard to its asset renewal program, and vice versa. As a result, reporting against this metric should be unnecessary as planned asset renewals should not result in any reduction in planned maintenance (or planned maintenance costs) during a relevant period. That is because those asset renewals will already have been factored into the maintenance forecasts during the planning process.

This has to be considered in the context of the two main types of planned maintenance work. Considering each in turn:

- **Mechanised maintenance:** consists of tasks such as resurfacing, ballast undercutting and grinding. These tasks have a pre-defined scope of work, which is separate from, and additional to, asset renewal work. Renewals are factored into the planning for such works, to ensure Aurizon Network does not maintain a section that is about to be replaced, or maintain a section that is newly installed.
- **Routine inspections:** consists of routine inspections of network assets to identify defects. Each defect is assessed for criticality and a notification raised, which specifies the time period in which the defect needs to be addressed. This work is then scoped and scheduled to be performed by maintenance teams. Inspections must occur irrespective of renewals, although their regularity can be reduced where *all* assets within a section of track have been recently renewed. As discussed above, this is already factored into Aurizon Network's maintenance planning.

Second, Aurizon Network's business system are not currently set up to distinguish between capital expenditure for asset renewals that is incurred in place of planned maintenance and renewals expenditure that does not. As explained above, Aurizon Network considers that the instances in which an asset renewal would be incurred in place of planned maintenance are relatively isolated (it would only be where an asset renewal occurs outside the scope of the asset renewal plan for the relevant year ie. upon an immediate failure of a piece of rail infrastructure). For that reason, Aurizon Network does not consider that the QCA should require Aurizon Network to report against this metric.

Aurizon Network therefore considers that clause 10.3.3(c)(B)(vii) of the CDD amended DAU is unnecessary and should be deleted.

#### Reporting by each Coal System

The QCA has included a new clause within the CDD amended DAU (clause 10.2(a)) stating that all reports under Part 10 must report separately in respect of each Coal System. This creates a number of practical issues for Aurizon Network in respect of both maintenance cost reporting and performance reporting. The key difficulty relates to the separate reporting of GAPE.

Aurizon Network does not consider it appropriate to report GAPE separately within the Maintenance Cost Report for the following reasons:

- Aurizon Network has never previously reported GAPE within the maintenance cost report separately. Aurizon Network cannot find any evidence in the QCA's CDD that stakeholders have raised this as a concern. Aurizon Network queries the utility of such reporting.
- GAPE is not a physical coal system. It is a theoretical system that has been created for pricing purposes. It is defined as:

*(a) the Goonyella Newlands Connection; and*

- (b) that part of the any other Coal System which is used by a Train Service that also uses or connects to any other part of the Goonyella Newlands Connection, except where that Train Services originates or terminates south of Gregory.*

That is, all track forming the GAPE 'system', with the exception of the section of track forming the Goonyella Newlands Connection<sup>25</sup>, has no separate physical existence but is in fact part of the Newlands or Goonyella system. As a result, it does not make sense to report maintenance costs separately for GAPE, as those costs are already captured within maintenance cost reporting for the Newlands and Goonyella system. To report these costs separately would involve double counting.

#### Annual Maintenance Plan

Clause 10.3.1 states that Aurizon Network must provide access holders and their customers (if applicable) with a briefing in the form of a report and presentation on:

- (i) Details of the planned scope of maintenance for the forthcoming Year, three months before the commencement of each Year; and*
- (ii) The contents of the maintenance cost reports, within one (1) month after the submission of the maintenance cost report to the QCA.*

Aurizon Network is happy to provide this report and presentation, however would like to amend the timing contained in the clause to make it more workable.

Aurizon Network proposes that each of the requirements in paragraphs (i) and (ii) above should be undertaken at least three months before the commencement of each financial year (i.e. by no later than 1 April). This will reduce the time and number of presentations required which is more efficient and reduces costs. While this means that the briefing in relation to item (ii) will occur later than under the QCA's proposal, Aurizon Network does not consider this should be an issue for stakeholders as the maintenance cost report itself will be publicly available from 31 October.

Aurizon Network would also look to provide as part of this briefing, an outline of the planned renewal scope for the forthcoming year.

## **CDD 5.2 Network performance reports**

Aurizon Network does not object, in broad terms, to the QCA's proposed content of the Quarterly Performance Report, subject to the comments below.

### **Reporting by each Coal System**

As discussed above, the QCA has included a new clause in the CDD amended DAU (clause 10.2(a)) stating that all reports under Part 10 must be provided separately in respect of each Coal System, which means separate reports would need to be provided for GAPE.

Aurizon Network does not consider that this is an appropriate position for the reasons stated below. Instead, it proposes that the current 2010AU reporting requirements are carried over in to UT4 reporting, so that GAPE is reported separately against the following metrics only:

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<sup>25</sup> For internal reporting purposes, maintenance which occurs on the Goonyella Newlands Connection is allocated to the Newlands system.

- Coal Carrying Train Services
- Below Rail Transit Time
- Coal Carrying Train Paths
- All Train Paths.

Aurizon Network understands from consultation with the QCA that the reason behind the change in reporting all metrics to GAPE separately is to provide GAPE access holders with more information relating to their services. Aurizon Network believes that the way the Quarterly Network Performance Report is currently written satisfies customers' needs. Aurizon Network is not aware of submissions from any stakeholders that suggest that the current report is not satisfying their requirements and cannot find any evidence whereby a stakeholder has specifically requested for GAPE to be reported separately within the reporting section.

Further, if all metrics are now changed to report GAPE separately, stakeholders and the QCA will lose the ability to track the Newlands system if they were to look at a comparative report from UT3, where GAPE is reported within the Newlands System.

As explained in respect of maintenance cost reporting, the GAPE system is not a physically distinct system but a system created for pricing purposes. It consists of parts of the Newlands and Goonyella system but only when they are traversed by a train that crosses the Goonyella Newlands Connection. For this reason, it does not make sense to report a number of these metrics against GAPE.

### **Reporting on the outcome of Contested Train Paths by GAPE**

In relation to clause 10.3.4(i) in the CDD amended DAU, the QCA has added a new clause, which contains the following information:

*...information on the outcome of the Contested Train Path decision making process contained in Clause 8 of Schedule G in respect of:*

- (i) The number of contests run each Month; and*
- (ii) The number and percentage of Train Paths allocated under each of the Contested Train Path principles set out in Clause 8.3 of schedule G...*

Aurizon Network welcomes new reporting metrics into the Quarterly Network Performance Report, however the QCA must be aware that these metrics cannot be reported separately for GAPE. This is due to how trains are scheduled and the Contested Train Paths process is managed – the paths in question are allocated to the Newlands or Goonyella system, not to GAPE. The Contested Train Paths process is based on system pathing constraints relating to only the 4 systems (Blackwater, Moura, Newlands and Goonyella).

## **CDD 5.3 Asset reporting**

Aurizon Network generally agrees with the QCA's amendments in relation to the publication of the Condition Based Assessment (CBA) report, subject to the comments below.

### **Timing**

In accordance with clause 10.4.3 of the CDD amended DAU, the CBA is due for completion six months prior to the Terminating Date, i.e. by no later than 31 December 2016. That means that Aurizon Network would need to commence the CBA process by no later than 30 June 2016, as it will take approximately six months to complete. The Assessor would need to receive QCA approval for the assessment plan prior

to that date. Given the risks associated with the timing for approval of the 2014DAU, it is conceivable that Aurizon Network will not be able to commence the CBA by 30 June 2016. As a result, it may be necessary to amend the Undertaking to extend the timeframe for completion of this report.

### **Impact on RAB**

Aurizon Network continues to have concerns with the potential implications of the CBA for the Regulated Asset Base (RAB) and the ability for Aurizon Network to recover its efficient costs. Reference is made to Aurizon Network's response to the CDD in relation to Schedule E in Chapter 14 of this response.

### **Confidentiality requirements**

Aurizon Network has concerns about the workability of the QCA's proposed confidentiality regime and its impact on stakeholders. In broad terms, it suggests that rather than adopting a prescriptive regime that is specific to the CBA, it would be more appropriate for this to be managed consistently with the existing provisions of the QCA Act which deal with confidentiality, and consistent with the QCA's proposed treatment of the publication of access agreements.

In this regard, it is suggested that Aurizon Network submit an unredacted version of the CBA report to the QCA. Aurizon Network will then publish the report, or provide it to third parties, so long as any version of the report that is published or provided to a third party excludes information, in respect of which the QCA:

- has received a request for non-disclosure; and
- is satisfied that disclosure of the information would be likely to damage the affected party's commercial activities and that disclosure would not be in the public interest.

Concerns with the QCA's proposed approach include;

- Aurizon Network has an over-arching obligation to protect the confidential information of access holders. A number of access holders have provisions in their access agreements that enable Aurizon Network to disclose their confidential information where permitted by the Undertaking, but they would not have anticipated this permission would extend to the circumstances currently contemplated by the QCA's CDD DAU. While Aurizon Network does not necessarily believe that publication of a CBA would result in publication of ringfenced information, it would prefer to have the flexibility to deal with this issue should it arise (e.g. if tonnages for individual mine-port pairs were included).
- It will be necessary to include a clear statement within the ringfencing provisions to the effect that where disclosure of confidential information is required by the access undertaking, it is not a breach of the ringfencing provisions. Otherwise there is a risk that compliance with one part of the access undertaking will result in non-compliance with another, which would place Aurizon Network in an impossible position.
- Clause 10.4.3(k) of the CDD amended DAU provides that Aurizon Network must not agree to any confidentiality obligations that prevent the disclosure of the information contained in the report or which do not permit disclosure in accordance with the Undertaking. As Aurizon Network cannot compel a third party to agree a particular confidentiality position, the practical effect of this clause may be that a third party will not agree to provide its confidential information to Aurizon Network – that may restrict its ability to procure a CBA report. In this regard, a reasonable endeavours obligation would be more appropriate.

## CDD 5.5 Audit requirements

### Provision of draft audit reports

The QCA has added a new clause in the CDD amended DAU (clause 10.6.4.(i)), which provides that “any drafts of an audit report that are provided to Aurizon Network by the Auditor must, at the same time, be provided to the QCA”.

Aurizon Network considers that inclusion of this clause is unnecessary, given the significant oversight the QCA already has of the audit process through approval of the Auditor and the Audit Liaison Group, and the practice which has developed, whereby the auditor presents its final draft report to the QCA prior to its finalisation. Aurizon Network is concerned that a requirement to provide *any* draft to the QCA at the same time it is provided to Aurizon Network may slow the process, or lead to the provision of factually incorrect or misleading information to the QCA. That is because it is often the case that issues identified in an initial auditor’s draft report need clarification or may be factually incorrect due to misinterpretation of the undertaking requirements or assumptions made with insufficient information. This gives Aurizon Network the opportunity to provide additional facts or information that was not previously requested by the auditor prior to finalisation.

### Approval of replacement auditor

Aurizon Network agrees in principle with the QCA’s decision to add a new clause, 10.6.4(iv) to the CDD amended DAU, which states that the auditor must: “be approved by the QCA. Once approved the approval will be effective for the Term, subject to the QCA having a right to require the appointment of a replacement Auditor.”

Given the auditor is now appointed for the Term, rather than appointed each year as under the 2010AU, Aurizon Network considers it would be appropriate to give it a right to request the appointment of a replacement Auditor for QCA approval. This may be considered in circumstances where, acting reasonably, Aurizon Network considers that the auditor is not acting competently in performing its duties. Examples of instances where a request for a replacement auditor may be submitted to the QCA for approval:

- Auditor not complying with Aurizon’s internal policies (e.g. safety, alcohol and drugs)
- The management of confidential information is not applied effectively
- Circumstances has resulted in a conflict of interest with the external auditor
- Substantial increase in costs for engagement

### Audit process

Aurizon Network’s primary concerns with the audit process (clause 10.6.4 of the CDD amended DAU) relate to the obligations in relation to implementing the auditor’s final recommendations. This extends to being able to direct Aurizon Network to implement recommendations, with any failure to comply with such a direction seen as a breach of the Undertaking.

It is important to note that the Auditor’s recommendations consist of additional controls which provide stronger internal procedures and processes for the Network business. These recommendations may potentially help reduce the risk of non-compliance and are based on hypothetical breaches of the Undertaking. Aurizon Network should not be required to implement recommendations suggested by an external auditor if no breaches of the undertaking have eventuated.

Aurizon Network is willing to use its reasonable endeavours to implement recommendations but cannot accept any obligation beyond that. It is not acceptable that a failure to implement an audit

recommendation is a breach of the Undertaking, as the recommendation may relate to an internal process, which although desirable, is not necessary to achieve compliance. If Aurizon Network is in breach of the Undertaking, consequences already apply under the QCA Act.

Aurizon Network also rejects the inclusion of wording whereby the auditor may recommend amendments to the Undertaking (clause 10.6.4(k) of the CDD amended DAU). An auditor should not be able to require an amendment to the Undertaking. In the first instance, it is not appropriate for an auditor to be able to determine whether the Undertaking requires amendment. In any case, apart from Aurizon Network submitting amendments, only the QCA can require an amendment, and then only in circumstances permitted by section 139 of the QCA Act. Aurizon Network submits that this section of the clause should be removed as it is inappropriate and beyond powers.

## Chapter 6 – Dispute Resolution and Decision Making (Part 11)

### Summary of Aurizon Network’s Position

While Aurizon Network understands the need to simplify and clarify the processes and procedures for disputes, the QCA’s proposed drafting in Part 11 of the CDD amended DAU does not achieve this result in a way which is consistent with the QCA’s statutory powers. For example:

**The Scope for Dispute:** The QCA has broadened the scope of the dispute resolution process by allowing a dispute to be raised in relation to all of Aurizon Network’s obligations under the Undertaking, parties to a Studies Funding Agreement, User Funding Agreement and a Rail Connection Agreement; and permitting any person to commence such a dispute. It does not have the power to do under the QCA Act and the drafting should be amended accordingly.

**Relationship with dispute provisions in the access agreement/Train Operations Deed:** Aurizon Network remains concerned that the drafting in clause 11.1.1 in the CDD amended DAU will not prevent disputes in respect of provisions that are incorporated by reference into the access agreement and Train Operations Deed being dealt with under the Undertaking. Aurizon Network has proposed a potential solution to this.

**Extent of regulatory involvement in disputes at the CEO resolution stage:** Aurizon Network should not be under an obligation to provide notices and informal correspondence to the QCA which could include settlement proposals, without prejudice offers and information that would or may have the effect of waiving legal professional privilege or incriminating any person.

**Expert determination process:** The QCA has vested itself with certain powers in relation to the expert resolution process which it does not have the power to do.

**QCA determination process:** The QCA Act expressly provides for what the QCA has power to determine in relation to access disputes and the QCA’s drafting potentially extends the QCA’s jurisdiction to hear disputes. The QCA’s arbitral powers under the QCA Act do not permit it to prevent the parties to a dispute agreeing to resolve a dispute by other means before referring the matter to the QCA for determination.

**Binding nature of the QCA’s determinations:** The QCA has included drafting to provide that its decisions are binding in the absence of manifest error. Under the QCA Act, the QCA’s access determinations are subject to judicial review and the grounds for invalidating such a determination extend to more than merely manifest error. The QCA’s drafting is therefore not appropriate.

To assist the QCA in reaching its Final Decision, Aurizon Network has provided a marked up version of Part 11 in Volume 2.

**Table 6.1 – QCA Consolidated Draft Decision**

QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(1) After considering Aurizon Network’s proposal, our consolidated draft decision is to refuse to approve the scope of the dispute resolution mechanism.	6.1	<b>Disagree.</b> The QCA only has power to determine disputes where an access provider and an access seeker cannot agree on an aspect of access to a declared service and there is no access agreement between the access provider and access seeker relating to the service.

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(2) The way in which we consider it appropriate that Aurizon Network amends its draft access undertaking is to:</p> <p>(a) expand the <b>scope</b> of the dispute resolution mechanism so that it accommodates disputes about:</p> <p>(i) the operation of the <b>undertaking</b> by any party</p> <p>(ii) the negotiation of access to prospective access <b>seekers</b>, not just access seekers and train operators</p> <p>(b) make any other amendments as proposed in our CDD amended DAU.</p>		<p>The effect of the QCA's drafting is to vest itself with an unqualified power to determine disputes on compliance with the Undertaking in general, which it does not have the power to do under the QCA Act.</p> <p>The QCA has also vested itself with the power to govern disputes between parties to a Studies Funding Agreement, User Funding Agreement and a Rail Connection Agreement, none of whom are necessarily access seekers or access holders. The QCA has no power to do so under the QCA Act.</p>
<p>(1) After considering Aurizon Network's proposal, our consolidated draft decision is to refuse to approve the processes, procedures and obligations of Aurizon Network's proposed dispute resolution mechanism.</p>	6.2	<b>Disagree.</b> Please refer to Aurizon Network's detailed comments below.
<p>(2) The way in which we consider it appropriate that Aurizon Network amends the draft access undertaking is to:</p> <p>(a) provide for disputes to be referred to the QCA for resolution if the parties cannot agree how to proceed</p> <p>(b) require Aurizon Network to keep the QCA informed of the progress of a dispute, including its outcome</p> <p>(c) simplify the expert appointment process</p> <p>(d) allow for the appointment of multiple experts</p> <p>(e) simplify the processes and procedures for disputes referred to the QCA to resolve</p> <p>(f) make the outcome of disputes resolved by the QCA binding on parties, subject to an exception for fraud</p> <p>(g) make any other amendments as proposed in our CDD amended DAU.</p>		

## CDD Part 6 Dispute resolution and decision making

Aurizon Network's key issues in relation to the QCA's proposed drafting of Part 5 are set out in the table below. Clause references are based on the QCA's CDD amended DAU.

**Table 6.2 – Part 11: Key drafting changes**

Item	Clause Reference	Effect of clause	Issue
40	11.1.1(a)	Broadens the scope for Disputes	<p>Under section 112 of the QCA Act, the QCA only has power to determine disputes where an access provider and an access seeker cannot agree on an aspect of access to a declared service and there is no access agreement between the access provider and access seeker relating to the service. The QCA has broadened the scope for Dispute by allowing a dispute to be raised in relation to all of Aurizon Network’s obligations under the Undertaking and permitting any person to commence such a dispute.</p> <p>The effect of the QCA’s drafting is to vest itself with an unqualified power to determine disputes on compliance with the Undertaking in general, which it does not have the power to do under the QCA Act. Aurizon Network’s concerns with this were detailed in its response to the QCA’s IDD26 and that response is incorporated here by way of reference.</p> <p>For this reason, Aurizon Network has amended the drafting in clause 11.1.1(a)(i) to limit the scope for disputes. It also proposes to define the term Prospective Access Seeker in Part 12 to mean “a person who notified Aurizon Network that the person wants Access, or increased Access, but has not yet provided Aurizon Network with a properly completed Access Application”. The definition is consistent with the definition of ‘access seeker’ under the QCA Act.</p>
41	11.1.1(c) and (d)	Broadens the scope for Disputes	<p>(a) The QCA has vested itself with the power to govern disputes between parties to a Studies Funding Agreement, User Funding Agreement and a Rail Connection Agreement, none of whom are necessarily access seekers or access holders. The QCA has no power to do so under the QCA Act.</p> <p>The clause is intended to cater for disputes between the parties that do not relate to a right or obligation under a Studies Funding Agreement, User Funding Agreement and a Rail Connection Agreement. It is unclear to Aurizon Network what other rights or obligations a party to these documents would have under the Undertaking.</p> <p>(b) Aurizon Network has previously expressed the concern that the approach adopted by the QCA in relation to the incorporation of terms in the Undertaking into the access agreement by reference</p>

<sup>26</sup> Aurizon Network (2015a). s.6.4, p.97.

Item	Clause Reference	Effect of clause	Issue
			<p>creates uncertainty as to whether the Undertaking dispute resolution provisions and/or the access agreement / Train Operations Deed (AA/TOD) dispute resolution provisions apply in the event of a dispute in relation to an incorporated provision. In addition, Aurizon Network notes that the QCA cannot require disputes under access agreements to be subject to determination by the QCA or for the Undertaking to be drafted in way that indirectly achieves that outcome.</p> <p>Clause 11.1.1(c) provides that any dispute arising in respect of any right or obligation (or in respect of the enforcement) of an AA or TOD:</p> <ul style="list-style-type: none"> <li>• must be dealt with in accordance with the provisions of that agreement (even if the dispute relates to provisions included in that agreement that are similar to, required by, or inconsistent with the Undertaking); and</li> <li>• are not to be dealt with under the Undertaking.</li> </ul> <p>Clause 11.1.1(d) provides that, despite 11.1.1(c), disputes between parties to an AA or TOD (in addition to the other agreements listed above) may be dealt with under the Undertaking to the extent the dispute is not in respect of any right or obligation (or in respect of any enforcement) of the AA or TOD.</p> <p>Clause 11.1.1(c) is very broad and would appear to extend to all disputes under an AA or TOD on the basis that all disputes under the AA or TOD will relate to the rights or obligations of the parties or the enforcement of the AA or TOD.</p> <p>The inclusion of clause 11.1.1(d) (and, in particular, the inclusion of the words “despite clause 11.1.1(c)” in clause 11.1.1(d)), suggests that clause 11.1.1(c) may be subject to, and overridden by, clause 11.1.1(d).</p> <p>For this reason and the reasons stated above in relation to clause 11.1.1(a)(i), Aurizon Network has deleted clause 11.1.1(d).</p> <p>(c) Aurizon Network remains concerned that if provisions are included in the Undertaking and those provisions take effect as obligations under the Undertaking, even if they are provisions which are incorporated by reference into the AA and TOD, clause 11.1.1(c) will not prevent disputes in respect of those provisions being dealt with under the Undertaking (subject to any other limitations on disputes built into clause 11.1). One potential way to address this concern would be to:</p>

Item	Clause Reference	Effect of clause	Issue
			<ul style="list-style-type: none"> <li>include all of the provisions from the Undertaking which are intended to be incorporated by reference into the AA and TOD as a schedule to the Undertaking (Incorporated Terms Schedule), instead of in the main body of the Undertaking; and</li> <li>include in the operative provisions of the Undertaking a clause which states that the Incorporated Terms Schedule will be incorporated by reference into the AA or TOD as applicable.</li> </ul> <p>Reference is made to Aurizon Network's response in Chapter 8 of this response (Access Agreements) for further details in relation to this.</p>
42	11.1.1(e)	Provision of notice of dispute to interested parties	The QCA has included a requirement that notices of disputes be provided by Aurizon Network to Customers of Train Operators. Given the way in which Customer is defined (i.e. it is the person in respect of which an access holder or access seeker is or is intending to use the Access Rights), references to Customer are inappropriate and must be deleted.
43	11.1.1(g)	Keeping the QCA informed of any Disputes	<p>The QCA has included a provision that requires Aurizon Network to provide the QCA with copies of any Dispute Notice and copies of subsequent notices and formal correspondence exchanged between the parties in connection with the Dispute. Given that such notices and informal correspondence could include settlement proposals, without prejudice offers and information that would or may have the effect of waiving legal professional privilege or incriminating any person, Aurizon Network should not be under an obligation to provide these documents to the QCA. It is also unnecessary for Aurizon Network to provide all "subsequent notices and formal correspondence" if the QCA is being kept informed of the progress of the resolution of the Dispute.</p> <p>For this reason Aurizon Network has deleted the reference to subsequent notices and formal correspondence in clause 11.1.1(g)(i) and included a new clause to provide an express acknowledgment that Aurizon Network is not required to provide various documents such as settlement proposals, without prejudice offers and information that would or may have the effect of waiving legal professional privilege or incriminating any person.</p>
44	11.1.2	Chief executive resolution process	Aurizon Network has included a new clause 11.1.2(b) to provide a time period within which the Chief Executives of each party to the Dispute must meet, being 10 Business Days after receipt of the Dispute

Item	Clause Reference	Effect of clause	Issue
			Notice. This is consistent with the approach taken by the QCA in the dispute provisions in the AA and TOD.
45	11.1.3(d)(iv)	Mediation process	As the parties to a Dispute should have the option to refer a dispute to either an expert or the QCA, Aurizon Network has removed the additional language at the start of clause 11.1.3(d)(iv). This is consistent with the QCA's approach in the former clause 11.1.2(d) ( <i>renumbered 11.1.2(e) in Aurizon Network's marked up version</i> ) where, failing resolution by the Chief Executives, the parties may refer the Dispute to mediation, an expert or the QCA.
46	11.1.4	Expert Determination process	<p>(a) Aurizon Network has removed the additional language at the end of clause 11.1.3(d)(iv). This is consistent with the QCA's approach in the former clause 11.1.2(d) (<i>renumbered 11.1.2(e) in Aurizon Network's marked up version</i>) where, failing resolution by the Chief Executives, the parties may refer the Dispute to mediation, an expert or the QCA.</p> <p>(b) The effect of the QCA's drafting in clause 11.1.4(b)(i) is that the QCA is vesting itself with the power to be involved in the appointment of an expert if the parties cannot agree on the expert's identity. The QCA Act does not provide the QCA with the power to do so.</p> <p>The language in relation to the appointment of an expert that Aurizon Network provided in its 2014DAU is very common, very clear and should be reinstated. The QCA has provided no justification for why this original drafting is not appropriate. Aurizon Network has amended clause 11.1.4 to provide this drafting.</p> <p>(c) Clause 11.1.4(b)(iii)(F) of the QCA's drafting (<i>renumbered 11.1.4(b)(vi)(F) in Aurizon Network's marked up version</i>) requires the expert not to make a determination which is directly inconsistent with an express provision of the Undertaking, suggesting that a determination which is indirectly inconsistent is permissible. While it is not clear to Aurizon Network what such a decision may be or why a determination that is indirectly inconsistent should be permissible, it has amended the clause so that it refers to a determination which is inconsistent with the Undertaking.</p> <p>(d) The expert should only be allowed to make a determination which the QCA could make if the matter was arbitrated by the QCA under Subdivision 3, Division 5 of Part 5 of the QCA Act. Aurizon Network has included an express provision to this effect.</p>

Item	Clause Reference	Effect of clause	Issue
			<p>(e) It is unclear what is meant by the drafting in the QCA's clauses 11.1.4(b)(iii)(F)(3) and 11.1.4(b)(iii)(F)(4), where it refers to "any matter not expressly stated in this Undertaking" and any "part of a matter that is not expressly covered by this Undertaking even if another part of the matter is expressly covered by the Undertaking." The dispute that this clause relates to is a Dispute as defined under clause 11.1.1(a) therefore by definition it cannot relate to the matters referred to in these clauses. For this reason Aurizon Network has deleted clauses 11.1.4(b)(iii)(F)(3) and 11.1.4(b)(iii)(F)(4).</p> <p>(f) Aurizon Network has also clarified when an expert may make a determination on the matters in the QCA's clauses 11.1.4(b)(iii)(F)(1) and (2).</p> <p>(g) Aurizon Network has deleted reference to the Expert Determination Rules of the Resolution Institute in clause 11.1.4(c). The process for expert determination set out in the Undertaking is sufficient and appropriate. The QCA's proposed reference to Expert Determination Rules of the Resolution Institute merely creates uncertainty.</p>
47	11.1.5	Determination by the QCA	<p>(a) Aurizon Network agrees that the parties to a dispute should be able to agree to send that dispute to an expert instead of the QCA – even though the Undertaking might refer the dispute to the QCA. The right of parties to agree an alternative dispute resolution process should not be restricted by the Undertaking. Clause 11.1.5(b) has been amended to permit the parties the flexibility for first seeking to resolve the dispute by referral to an expert. The QCA's arbitral powers under the QCA Act do not permit it to prevent the parties to a dispute agreeing to resolve a dispute by other means before referring the matter to the QCA for determination.</p> <p>(b) The QCA has included a provision in clause 11.1.5(c) stating that where a Dispute is referred to the QCA for determination under the Undertaking, the parties to a Dispute agree that Division 5 of Part 5 of the QCA Act applies. The parties do not have the power to agree that a legislative provision applies. The QCA Act expressly provides for what the QCA has power to determine in relation to access disputes and the QCA's drafting potentially extends the QCA's jurisdiction to hear disputes. Clause 11.1.5 is not intended to extend the QCA's jurisdiction beyond that which exists under the QCA Act.</p>

Item	Clause Reference	Effect of clause	Issue
			<p>For this reason, Aurizon Network has deleted the clause 11.1.5(c) proposed by the QCA and inserted replacement drafting that clarifies this matter. It has not merely reinstated the previous drafting that Aurizon Network provided in its 2014DAU Submission in an effort to further clarify the provision and to avoid confusion.</p> <p>(c) As it is clear that the QCA is exercising its arbitral jurisdiction under the QCA Act, the QCA's proposed clause 11.1.4(g) is not required and has been deleted. The Undertaking does not affect the QCA's arbitral jurisdiction under the QCA Act.</p>
48	11.1.6(b)	Final and binding decisions	<p>(a) The binding nature of both an expert's decision and the QCA's decision has been included by the QCA under clause 11.1.6(b). The binding nature of an expert's decision was implicitly the case anyway under clause 11.1.4(g), but Aurizon Network has amended clause 11.1.4 (g) to specifically provide for this as it makes for clearer reading.</p> <p>(b) In relation to the binding nature of the QCA's determinations:</p> <ul style="list-style-type: none"> <li>• as these are access determinations under the QCA Act, those determinations will have effect in accordance with the terms of the QCA Act and the QCA Act sets out remedies for non-compliance;</li> <li>• the QCA Act does not state that an access determination by the QCA is final and binding on the parties subject to manifest error. The QCA's access determinations are subject to judicial review and the grounds for invalidating such a determination extend to more than merely manifest error.</li> </ul> <p>For these reasons, the QCA's proposed clause 11.1.6(b) in this respect is not necessary.</p>
49	11.1.7(b)	Application to Part 8 Disputes	<p>This clause provides that Part 8 (Network Development and Expansions) prevails to the extent of any inconsistency with Part 11. Aurizon Network has deleted this clause on the basis that it is not clear what the potential inconsistency might be and until it understands what is in the final form of Part 8, we should revert to the original language proposed by Aurizon Network in its 2014DAU.</p>

## Chapter 7 – Negotiation Framework (Part 4)

### Summary of Aurizon Network's Position

Aurizon Network considers that generally, it is prepared to agree to the principles contained within Part 4 in the CDD amended DAU. It does however have concerns around some of the drafting changes proposed by the QCA and the ability for these changes to be practically implemented. The key issues identified can be summarised as follows:

- Part 4 contains many processes and timeframes in which these are to be undertaken. In multiple circumstances, the QCA has sought to impose further timeframes which have led to inconsistencies and errors;
- processes have been overcomplicated, leading to a process that is difficult to comprehend, and contains errors; and
- as currently drafted, there are some circumstances where the QCA has proposed for the provision of information by Aurizon Network, before it could reasonably be known. Aurizon Network will therefore not be able to comply with that drafting or the Undertaking.

Aurizon Network has proposed many amendments to the CDD amended DAU to provide more clarity and realign processes however retains the overall policy intent of the QCA. These changes are required to ensure that practically, it is possible to operate and comply with the process described.

Aurizon Network has prepared a revised draft of Part 4 of the QCA's CDD amended DAU, marked up against the QCA's CDD amended DAU, which is attached at Volume 2 of this submission.

**Table 7.1 – QCA Consolidated Draft Decision**

	QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1)	After considering Aurizon Network's proposal, our consolidated draft decision is to refuse to approve the process for applying for access and negotiating agreements.	7.1	<b>Agree with amendments.</b> Aurizon Network has concerns with the drafting. It also considers that the QCA has introduced unnecessary complexity in a number of areas
(2)	The way in which we consider it appropriate that Aurizon Network amends the draft access undertaking is to: <ul style="list-style-type: none"><li>(a) address Aurizon Network's ability to use its position to delay negotiations and increase the transparency and accountability of its decision-making</li><li>(b) clarify the process for applying for access and negotiating agreements and increase certainty over the process</li><li>(c) make other amendments as reflected in our CDD amended DAU.</li></ul>		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(1) After considering Aurizon Network's proposal, our consolidated draft decision is to refuse to approve the information requirements for negotiating access.</p> <p>(2) The way in which we consider it appropriate that Aurizon Network amends the draft access undertaking is to:</p> <p>(a) better balance Aurizon Network's and other parties' rights and interests, relating to the nature and type of information provided as part of the process</p> <p>(b) clarify the nature and type of information Aurizon Network provides, and can request or require, and increase certainty over when this information is to be made available (as set out in the marked changes to Part 4, Schedule A and Schedule B in our CDD amended DAU)</p> <p>(c) make other amendments as reflected in our CDD amended DAU.</p>	7.2	<b>Agree with amendments.</b> The QCA's drafting is unacceptable from a practical sense, due to unachievable timeframes.
<p>(1) After considering Aurizon Network's proposal, our consolidated draft decision is to refuse to approve the arrangements that require a customer to nominate a train operator for particular functions in the negotiation process.</p> <p>(2) The way in which we consider it appropriate that Aurizon Network amends the draft access undertaking is to:</p> <p>(a) require Aurizon Network to continue negotiating with all train operators until the customer makes a nomination</p> <p>(b) make other amendments as reflected in our CDD amended DAU.</p>	7.3	<b>Agree with amendments.</b> In the interests of a timely resolution to UT4, Aurizon Network considers that the principles proposed by the QCA can be agreed to, however minor changes are required to correct drafting and clarify processes.

## CDD 7.1 Process for applying for access and negotiating agreements

In Part 7.3 of the QCA's CDD, the QCA notes that Aurizon Network had made an effort to streamline the negotiation process, however the QCA has rejected this on the basis that it considers the balance of interests between Aurizon Network and access seekers to be inappropriate. As such, the QCA has made a number of amendments, both in the IDD and CDD, attempting to increase transparency and accountability.

Aurizon Network is amenable to the inclusion of additional transparency requirements, however considers that the practical application of these changes within the DAU creates complexities and in some cases

fractures the process. Aurizon Network considers that in making these changes, the QCA has overlooked the objective to create a streamlined and easy to follow process.

The majority of Aurizon Network’s concerns can be addressed through comparatively minor changes to the drafting. Aurizon Network has indicated these changes and its reasoning in the table below. Aurizon Network has also provided a streamlined process map to be included within Schedule H of the 2014DAU. This will provide access seekers with a clear path for applying for and negotiating access.

**Table 7.2 – Aurizon Network’s proposed drafting changes**

Clause Reference	Issue with CDD	Change Requirements
4.1 (b)(i)	Within the drafting changes proposed by the QCA, there is an inconsistent use of the term ‘prospective access seeker’. Aurizon Network considers this to be confusing and incorrect.	Aurizon Network has proposed to include a definition of Prospective Access Seeker. It has adjusted the drafting as required to ensure the correct terminology is in place.
4.1 (e)	It is not clear why the QCA has included separate dispute mechanisms within Part 4 when Part 11 provides the dispute resolution process. Aurizon Network also notes that the QCA has included a ten day timeframe for disputes. Aurizon Network does not have any concerns with this, however is uncertain as to why this has been included.	Propose to include wording that references the link to Part 11, and that the dispute must be dealt with in accordance with this clause.
4.1 (f) 4.6 (h) 4.10.1 (c)(iv)(D)	The QCA notes in its CDD that it recognises the issue raised by Aurizon Network regarding the practicalities associated with extending the relevant timeframe where there is a dispute. Aurizon Network considers that the application of this drafting is not appropriate and fails to address the concern that the timeframe may be inadequate to enact any requirements following resolution of a dispute.  As an example, a dispute may be raised regarding an Indicative Access Proposal (IAP) on the 19 <sup>th</sup> day of the 20 day process. Any extension of time provided due to the dispute resolution period will simply leave one day for completion of matters upon resolution of the dispute. Unless the QCA notes in its resolution of the dispute that an extension is provided, this process is not workable.	In the interest of resolving matters, Aurizon Network can agree to concept proposed however considers the drafting of 4.1(f) is not required. Accordingly, it has proposed new drafting where relevant in 4.6(h) and 4.10.1(c)(iv)(D) to ensure that in making its decision regarding timeframe extensions, the QCA must have regard to the tasks required to rectify the dispute.
4.4(a)(v)	Aurizon Network considers that the way the QCA has used the term ‘Non-availability Requirements’ is incorrect. As drafted, the QCA’s drafting proposes that Non-Availability requirements are met where a notice is provided. There is a missing link to confirm that Aurizon Network is satisfied.	Aurizon Network has proposed minor changes to the terminology, as well as the definition to include the requirement for Aurizon Network to notify customers that the Non-availability requirements exist.
4.4 (g)	The QCA has proposed to extend the timeframe in which an access seeker can submit an access application from three years to five years prior to the intended commencement of the access rights.  It is important to note that Aurizon Network and the QRC were in agreement that the three year	Aurizon Network requires the position that has been agreed with the QRC to be reinstated. This includes returning the timeframe to three years, and including the option for the parties to agree to such

Clause Reference	Issue with CDD	Change Requirements
	<p>timeframe, with flexibility for such longer times where there was sufficient justification, was appropriate.</p> <p>The five year timeframe does not align with Part 5 of the DAU whereby an access agreement may only be entered into within two years of commencement. Should an application be submitted five years in advance, its negotiation process will need to be extended by at least two years before a contract could be entered into. During this time, the access rights are effectively 'reserved' for the access seeker, so other access seekers' requests may not be able to be accommodated. It is possible that a new form of access agreement may be in place and the negotiated agreement would no longer be valid.</p>	<p>longer timeframe where there is sufficient justification.</p>
4.4 (h)(ii)	<p>The QCA has used incorrect terminology, in that the drafting indicates that an access application is 'suspended' rather than withdrawn where Aurizon Network has rejected an application due to it being submitted too far in advance. This creates uncertainty as to what the process is for that application.</p>	<p>Aurizon Network considers that the correct approach is to deem the application withdrawn. Similar drafting is included within Part 4. This makes it clear that the application will not be progressed, and the access seeker will need to resubmit when the appropriate time is reached.</p>
4.5 (h) and 4.5 (i)	<p>The QCA has sought to build in a process whereby in the event that an access seeker has made a Material Variation to their access request, they can chose to proceed with a revised IAP or revert to their original request once an IAP has been issued</p> <p>Aurizon Network considers this process is not required, given an access seeker already has the ability to choose to proceed with its variation following Aurizon Network determining if that variation is material. The inclusion of this process has the potential to impose additional administration on Aurizon Network.</p> <p>It may be the case that the IAP has not yet been issued for the access request. If the access seeker advises that it wishes to continue without the Material Variation after the IAP has been issued, Aurizon Network will be required to develop an entirely new IAP.</p>	<p>Aurizon Network recommends that this process be removed. Once an access seeker chooses to proceed on the basis of its variation, any previous IAPs should be overwritten.</p> <p>In the interest of moving forward, Aurizon Network can agree to compromise should this process be necessary. If so, it requires additional drafting to recognise that an original IAP may not have been developed, and if required to do so, Aurizon Network will require additional time to achieve this.</p>
4.5 (j)	<p>Unnecessary complexity has also been built into clause 4.5(j). From Aurizon Network's interpretation, this clause is seeking to provide that a request to vary an application will not be accommodated after a notice of intent has been provided by the access seeker. This clause is a prime example of overly prescriptive drafting, which Aurizon Network considers can be removed in its entirety.</p>	<p>A minor change can be made to clause 4.5(a) to include clarification that a request can be made at any time after an acknowledgement notice is issued, up until the access seeker provides a Notice of Intent under clause 4.7. This simple change will provide a process that is less confusing and easy to understand by all parties. Should Aurizon Network's</p>

Clause Reference	Issue with CDD	Change Requirements
		interpretation not be correct, the QCA will need to clarify the intent of this clause.
4.5 (j) (vii)	<p>In the CDD, the QCA has agreed with Aurizon Network on the matter that if an access seeker requests a Material Variation, its position in the queue should not be maintained so as not to disadvantage other users. Aurizon Network notes the QCA has sought to address this issue in clause 4.5(j), and assumes this attempt is reflected in clause 4.5(j)(vii). Aurizon Network considers the application of the proposed change is incorrect, as the drafting seeks to set a deemed date that the application was received for requests that have been withdrawn. This does not address Aurizon Network's concern relating to the effect of a Material Variation on another access seeker's access request.</p>	<p>Drafting has been proposed to ensure that where a Material Variation is proposed and the access seeker chooses to proceed, the date on which the Material Variation was made is the date that the access application will be deemed to be received for the purposes of the queue.</p>
4.9.2	<p>The QRC noted its concerns regarding operators being able to progress negotiations for a Train Operations Deed (TOD) without specific support from the intended customer. Similarly to this, Aurizon Network maintains its position that negotiating with more than one operator at once for the same access rights is inefficient and has no effect on competition in the above rail market.</p> <p>The QCA has failed to provide valid reasoning for its rejection of these concerns. The QCA cites that operators can differentiate themselves via conditions of haulage agreements, cost and service quality. Aurizon Network considers that negotiations of a TOD has no impact on any of the above, as it provides equal service quality to all customers, nor can it differentiate on costs (even though these only apply to the access agreement).</p>	<p>Aurizon Network is willing to facilitate this requirement, however notes that the QCA acknowledged that some additional costs may be associated with this. Reference is made to Chapter 20 of this response for estimates of Aurizon Network's additional costs.</p>
4.10.2(e)	<p>Aurizon Network is concerned that as currently drafted, the CDD enables negotiations to proceed with an access seeker where it has met the Non-availability Requirements. Aurizon Network should not be required to enter into an access agreement with an access seeker where the Non-availability Requirements have been met.</p> <p>Aurizon Network previously noted that the operation of this clause can lead to hoarding and the inefficient allocation of capacity. This is particularly prevalent as the QCA has removed the mechanism for Aurizon Network to alter the queue, which would allow it to bring forward its ability to contract with access seekers who can provide the required evidence of Supply Chain Rights and are ready to operate. This ability has been heavily relied upon throughout all previous undertakings to reorder the queue where</p>	<p>Aurizon Network is willing to accept this clause on the basis that new drafting is included, to ensure that Aurizon Network is not obliged to execute an access agreement or TOD unless the parties have terms under which the required information will be provided within the access agreement.</p> <p>Additionally, the QCA has sought an example of how this clause can lead to inefficient allocation of capacity. Aurizon Network provides the following advice.</p> <p>It may be the case that a new exploration company submits an access application for 5mtpa commencing in five years. The access seeker may not be able to provide details of its load times, operating</p>

Clause Reference	Issue with CDD	Change Requirements
	<p>one customer has successfully secured port rights prior to another.</p>	<p>procedures, or specific mine location due to mine planning not yet being fully developed. Aurizon Network is required to accept this on the basis that: (a) the QCA has extended the lead time for the access application to five years; and (b) the information could not be reasonably made available at this early stage. As such, should capacity be available, it is effectively 'quarantined' for that customer due to its position in the queue.</p> <p>Should another access seeker submit an application after the one detailed above, but this application is to commence in two years, and all information is provided, it may be the case that this access seeker's request cannot be met due to the 5mtpa above being held due to ongoing negotiations with the first access seeker, who continues to be in negotiations validly due to meeting the Non-availability Requirements.</p> <p>In this case, in order to maximise efficient utilisation of the network it would be better that the second access seeker be granted access rights over the first, as it will commence making a contribution to common costs at an earlier stage. It is also more likely that it will proceed with negotiations as it is far more progressed. Aurizon Network considers that in situations such as this, it will be prevented from maximising the use of the network capacity until negotiations with the first access seeker are resolved.</p>
4.11.1 (d) (iii)	<p>The QCA have proposed drafting to require Aurizon Network to provide an 'evidence' based explanation of why Available Capacity is reduced. Aurizon Network has two primary concerns with this drafting. The first is how the QCA has proposed to include confidentiality provisions. Aurizon Network considers that it is more appropriate to link to Part 3 to ensure there is no inconsistency between clauses.</p> <p>Secondly, Aurizon Network considered that the QCA's explanation is confusing. Aurizon Network cannot see a situation where evidence can be provided without breaking confidentiality provisions. Additionally, Aurizon Network seeks advice from the QCA as to what it intended to be provided, as the current drafting is unworkable.</p>	<p>Aurizon Network has proposed minor changes to the drafting to ensure that information is still provided, but is not required to be evidentiary. This will allow Aurizon Network to explain such a situation as best as possible without breaching confidentiality requirements.</p>
4.10	<p>As currently drafted, the Undertaking provides for Aurizon Network to negotiate with an access seeker</p>	<p>Aurizon Network has proposed new drafting in clause 4.11.2 (e) to ensure that</p>

Clause Reference	Issue with CDD	Change Requirements
	<p>where the Non-Availability Requirements are met. There is no protection for Aurizon Network when it comes to executing an agreement. Given the QCA has proposed a five year lead time, it is possible that these conditions will still be in place when the negotiations are completed. Aurizon Network should not be required to enter into an Access Agreement where the required information has not been provided, unless the situation can be addressed through Conditions Precedent clauses within the relevant agreement.</p>	<p>the relevant information is provided prior to the operation of Train Services. This ensures that capacity is allocated efficiently, and is not contracted to parties who cannot use the access rights.</p>
<p>Schedule A Part 2</p>	<p>Aurizon Network considers that the QCA has misunderstood the changes proposed by Aurizon Network in terms of confidentiality provisions. Where Aurizon Network is providing information on a Landowner to an Access Seeker, it is unlikely that the confidentiality provisions of the Undertaking will apply. Rather, confidentiality provisions will be in accordance with the relevant arrangements with the Landowner.</p>	<p>Aurizon Network has proposed drafting to ensure that its confidentiality obligations relating to the relevant arrangements with the Landowner are taken into consideration.</p>
<p>Schedule B, Part 6(e)  Schedule B, Part 7 (e)</p>	<p>The QCA has made a change to the drafting so as to remove the requirement for an access seeker to provide information regarding its ability to use access rights where its request is a transfer or renewal request.</p> <p>Aurizon Network cannot agree to this change and considers that it must have been in error. Where an access seeker is renewing its access rights, amongst other things, it must be able to demonstrate that it has obtained port rights to unload.</p> <p>Similarly for transfers, where a transfer is occurring from one customer to another, Aurizon Network requires confirmation that the corresponding port rights have been transferred and that the new origin can accommodate the additional tonnes.</p>	<p>Aurizon Network has proposed to reinstate the reference to Clause 3 of Schedule B within the appropriate clauses.</p>

## CDD 7.2 Providing relevant and accurate information in a timely manner

In CCD 7.2, the QCA has proposed a number of changes relating to the timing and amount of information that both Aurizon Network and access seekers need to provide as part of the access process. Aurizon Network is prepared to agree to the majority of these changes, however other changes are impractical and have the potential to mislead or delay negotiations.

In forming this opinion, Aurizon Network notes that the QCA has stated “parties should not be obliged to provide any more information than what is reasonably available and necessary”<sup>27</sup>. Aurizon Network considers that the QCA has misunderstood the level of detail and complexities in the access process and has proposed requirements on Aurizon Network to provide information that is neither necessary, nor reasonably known at the relevant point in time.

Aurizon Network has identified two key issues that cannot be accepted. It considers that these issues can be rectified by restructuring certain elements of the process and making minor amendments to ensure the process is practical and facilitates the flow of information between Aurizon Network and its customers. A summary of Aurizon Network’s key issues and proposed drafting changes is provided below.

**(1) Provision of information regarding whether an access seeker has joined the queue within the acknowledgment notice**

Aurizon Network’s concerns relating to the drafting of clause 4.4(b)(ii) were highlighted in its response to the IDD and that response is restated here by reference<sup>28</sup>. Aurizon Network noted that it was premature to confirm in an acknowledgment notice as to whether the access application has entered the queue. The QCA disagreed, citing in Table 26 of the CDD that it is of the view that a queue can be formed regardless of whether or not a capacity analysis is required and that it is in the access seeker’s best interest to enter the queue on the date that it submitted the access application.

Aurizon Network considers that the QCA has misunderstood Aurizon Network’s concerns with this drafting. As clause 4.4(b) is currently drafted, it provides that Aurizon Network must confirm whether an access seeker has entered the queue in the acknowledgment notice. Aurizon Network agrees with the QCA that the access seeker’s position in the queue will reflect the date the access application was received, however Aurizon Network does not agree with the requirement to confirm that an access seeker has entered the queue in the acknowledgment notice.

Aurizon Network’s position is that an Access Seeker is only placed in the queue once it has issued a notice of intent in accordance with clause 4.7. This is to account for situations where access seekers do not wish to proceed with an application. Linking in with the operation of Part 7, as the drafting currently stands, Aurizon Network would be required to advise each access seeker in the queue of each individual change every time this occurs. This is unnecessary and impractical to implement.

Aurizon Network considers that a minor change to the drafting of clause 4.4(b) will resolve these issues. It proposes to remove the wording: “subject to confirmation under an Acknowledgement Notice”. The removal of this wording will not impact the operation of the rest of the clause, nor the position in the queue that the access seeker will receive. Aurizon Network proposes a new sub-clause be included within clause 4.7 to provide certainty to access holders that upon issuing a notice of intention to proceed, they will be placed in the queue accordingly to the date that their access application was received.

**(2) Provision of information as to whether access rights cannot be accommodated without an expansion or whether capacity is constrained, within 10 business days of receiving an access application, or a Material Variation**

In its CDD, the QCA fails to address Aurizon Network’s concerns raised<sup>29</sup> in relation to the timing of provision of information regarding expansions and whether capacity is constrained, as part of the acknowledgment process. The QCA states in Table 26 of the CDD that it disagrees with Aurizon Network’s concerns and that Aurizon Network should be sufficiently aware of the network’s capacity and

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<sup>27</sup> Queensland Competition Authority (2015a). p.215.

<sup>28</sup> Aurizon Network (2015a). s.7.4, p.104.

<sup>29</sup> Aurizon Network (2015a). s.7.4, p.105.

operational capability to be able to provide this information. In the CDD, the QCA has gone a step further to require this information be provided within 10 business days of receipt of the access application. Aurizon Network considers the QCA's response to be not fully informed regarding the processes it is seeking to change, or their practical application.

Aurizon Network is considerate of this information being valuable to access seekers and does not oppose its provision. The issue lies in the timing proposed by the QCA and the practicalities of meeting them. Aurizon Network is also concerned with the QCA's opinion that Aurizon Network should be sufficiently aware of the capacity available within the system without performing an assessment.

The purpose of the acknowledgment phase in the process is to determine whether the information contained in the application is sufficient. The 10 day timeframe is used by Aurizon Network to review the application, to determine whether there is sufficient information to properly assess the application. It is the IAP phase where the initial capacity assessment is undertaken. During this phase, Aurizon Network will undertake the required reviews to determine whether capacity is available or whether an expansion is required. It is not feasible to provide this information during the acknowledgement phase, as work has not yet been done and the information may not have been made available or known by the access seeker.

Aurizon Network considers that the QCA has overlooked the complexities of determining available capacity. Due to the increasing level of flexibility and variation in the CQCR, capacity is not static and any changes to operating procedures have the ability to increase or decrease capacity available. This effectively means that individual, static items such as the Baseline Capacity Review cannot be used to make decisions such as these.

Each access application requires individual assessment. As an example, Aurizon Network may receive two access applications, one for a non-standard operation consisting of complex reversing procedures to turn a train, and the other for a standard operation. As the first request requires more time on the network, it may be the case that there is not sufficient capacity to accommodate that request, however there may be enough capacity for the second application as it requires less time on the network. This type of information can only be determined through undertaking dynamic modelling of the operations to determine the effect on other contracted services, and the overall system.

If this requirement was to remain, Aurizon Network could only advise access seekers of expansion requirements on the best information it has at the time. This could lead to a circumstance where Aurizon Network issues an incorrect notice, stating that an expansion is required. Following this, the access process would be placed on hold. If on further review, a capacity assessment determines that capacity may be available, the access seeker may have been disadvantaged. Aurizon Network is not willing to accept the risk, nor impose the disruption to its customers that this situation would create, particularly due to the changes the QCA has made to the dispute provisions, making Aurizon Network liable even where it has complied with the access undertaking.

Aurizon Network considers that this issue can be easily resolved through moving the requirement to provide information on whether an expansion is required, or whether a system is capacity constrained, to be a step in the IAP development process. Aurizon Network considers that an IAP is the appropriate place to advise an access seeker of this as it will be based on an informed assessment. Aurizon Network has proposed drafting amendments to reflect this change within the 2014 DAU. A new clause 4.8 has been created to specifically deal with these changes. Other consequential changes have been made to ensure the drafting is workable.

## Chapter 8 – Access Agreements

### Summary of Aurizon Network’s Position

Aurizon Network has the following concerns with the QCA’s approach to the standard Access Agreement (AA) and standard Trains Operations Deed (TOD).

**Incorporation of Terms from the Undertaking into the AA/TOD:** The QCA’s proposal to incorporate terms by reference from the AU into the AA and TOD raises a number of concerns, specifically (but not limited to) the Access Charge provisions, Force Majeure provisions, Aurizon Network’s liability position and uncertainty in relation to Disputes. Aurizon Network has proposed a potential solution to its concerns in relation to liability and disputes by the inclusion of all of the provisions from the Undertaking which are intended to be incorporated by reference into the AA and TOD as a schedule to the Undertaking.

**Review of the Standard AA and Standard TOD initiated by the QCA:** Aurizon Network considers that the QCA’s role should be limited to approving or rejecting amendments proposed by Aurizon Network, rather than the QCA having the ability to impose its own amendments.

**Security:** Subject to Schedule F of the Access Undertaking being amended to clearly state that Aurizon Network may, through the revenue cap process, recover any shortfall in revenue arising from the difference between the Security amount held by Aurizon Network and the amount of a defaulting customer’s Take or Pay liability, Aurizon Network accepts the QCA’s proposal that the Security amount be equal to 6 months of the relevant Customer’s Take or Pay.

**Aurizon Network Cause:** Aurizon Network disagrees with the QCA’s decision to include Operational Constraints in the definition of Aurizon Network Cause for the reasons outlined below.

**Allowable Threshold:** Aurizon Network disagrees with the QCA’s decision in the CDD to reduce the ‘allowable threshold’, which is a long-standing part of the liability limitations for non-provision of access, within the AA from 10% to 5% for the reasons outlined below.

**Notification Requirements under the TOD:** The materiality threshold above which Aurizon Network is required to notify Operators of impacts to Train Services on a daily basis is entirely unworkable and impractical for the reasons outlined below.

**Resumption of Access Rights:** Aurizon Network’s right to resume access rights on a forward looking basis should be reinstated for the reasons outlined in Aurizon Network’s previous response to the IDD, which are incorporated here by reference.<sup>30</sup>

**Reduction of Nominated Monthly Train Services:** Aurizon Network reiterates its position that provisions allowing the Reduction of Nominated Monthly Train Services where Operators exceed the Maximum Payload, or an Access Holder / Aurizon Network seek to increase the Maximum Payloads, are appropriate for inclusion in the AA and TOD for the reasons outlined Aurizon Network’s previous response to the IDD, which are incorporated here by reference.<sup>31</sup>

Aurizon Network has prepared:

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<sup>30</sup> Aurizon Network (2015a). s.8.4, pp.111-115.

<sup>31</sup> Aurizon Network (2015a). s.8.4, pp.111-115.

- a table with detailed comments on the draft AA and TOD of the QCA’s CDD amended DAU, which is attached at Volume 3 of this submission;
- a table with detailed comments on Part 5 of the QCA’s CDD amended DAU, which is attached at Volume 3 of this submission;
- a revised draft of Part 5 of the QCA’s CDD amended DAU, marked up against the QCA’s CDD amended DAU, which is attached at Volume 3 of this submission;
- a revised draft AA, marked up against the QCA’s CDD amended DAU AA, which is attached at Volume 3 of this submission; and
- a revised draft TOD, marked up against the QCA’s CDD amended DAU TOD, which is attached at Volume 3 of this submission.
- a draft of “Incorporated Provisions” which consists of a revised draft of relevant provisions of Part 7 of the QCA’s CDD amended DAU, which is attached at Volume 3 of this submission.

Each of the table of detailed comments and the revised drafts of Part 5, the AA and the TOD form part of Aurizon Network’s Submission on Part 8 of the QCA’s CDD.

**Table 8.1 – QCA Consolidated Draft Decision**

	QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(1)	After considering Aurizon Network’s 2014 DAU, our consolidated draft decision is to refuse to approve Part 5 of the 2014 DAU.	8.1	<b>Agree with amendments.</b> Aurizon Network is prepared to agree with CDD 8.1, subject to removal of the QCA’s ability to impose its own amendments to the Standard AA or Standard TOD as it has purported to do under clause 5.4 of the CDD amended DAU.
(2)	We consider it appropriate for Aurizon Network to amend Part 5 to: <ul style="list-style-type: none"> <li>(a) provide for the standard access agreement to govern the terms of access to the CQCN, unless otherwise agreed by the access seeker and Aurizon Network; and</li> <li>(b) introduce the process for the review of the standard access agreements during the term of the access undertaking, as set out in clause 5.4 of our CDD amended DAU attached to this consolidated draft decision.</li> </ul>		
(3)	The amendments we consider to be appropriate to achieve the above are set out in Part 5 of our CDD amended DAU.		
(1)	After considering Aurizon Network’s 2014 DAU, our consolidated draft decision is to refuse to approve the suite of standard access agreements included as part of the 2014 DAU.	8.2	<b>Agree with amendments.</b> Aurizon Network agrees with the simplification of Access Agreements but has proposed drafting amendments to the AA and TOD to ensure it is still appropriate for an Operator to enter into the AA / TOD on behalf of an end user in lieu of a Standard Operator Access Agreement.
(2)	The way in which we consider it appropriate to amend the DAU is to provide the following standard access agreements, as set out in our proposed CDD amended DAU attached to this consolidated draft decision: <ul style="list-style-type: none"> <li>(a) an Access Agreement (AA)—that allows either a mining company or</li> </ul>		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>a train operator to contract directly with Aurizon Network for access rights only. This agreement does not deal with above-rail operations.</p> <p>(b) a Train Operations Deed (TOD)—that allows a nominated train operator to contract directly with Aurizon Network to operate train services, or a mining company which is also an accredited operator to contract with Aurizon Network and take on the responsibility of train operations in connection with access rights granted under an access agreement.</p> <p>(3) The amendments that we consider to be appropriate to achieve the above are set out in our CDD amended DAU.</p>		
<p>(1) After considering Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's 2014 DAU, in respect of its decision to not include particular matters within the body of the undertaking.</p> <p>(2) The way in which we propose it is appropriate to amend the DAU is to: (a) include the following matters in the body of the undertaking and then incorporate them by reference, as set out in the AA and TOD attached to this decision:</p> <p style="padding-left: 40px;">(i) access charge and reference tariff provisions</p> <p style="padding-left: 40px;">(ii) interface risk provisions</p> <p style="padding-left: 40px;">(iii) transfer, relinquishment (and reduction factor), resumption and conditional access provisions</p> <p style="padding-left: 40px;">(iv) force majeure provisions</p> <p>(3) The amendments that we consider to be appropriate to achieve the above are set out in our CDD amended DAU.</p>	<p>8.3</p>	<p><b>Disagree.</b> The QCA's proposal to incorporate terms by reference from the Undertaking into the AA and TOD raises a number of concerns, specifically (but not limited to):</p> <ul style="list-style-type: none"> <li>• Access Charge provisions</li> <li>• Force Majeure provisions</li> <li>• Aurizon Network's liability position</li> <li>• uncertainty in relation to Disputes.</li> </ul>
<p>(1) After considering Aurizon Network's proposal for the terms and conditions of SAAs under the 2014 DAU, our consolidated draft decision is to refuse to approve the proposal.</p> <p>(2) The way in which we consider it appropriate that Aurizon Network amend the terms and conditions of the 2014 DAU SAAs is to:</p>	<p>8.4</p>	<p><b>(2)(a) Disagree.</b> Aurizon Network disagrees with the QCA's removal of the provisions allowing Aurizon Network to reduce Nominated Monthly Train Services as a result of (1) exceeding the Maximum Payload or (2) increasing the Maximum Payload at the request of the Access Holder or Aurizon Network. Aurizon Network also disagrees with the QCA's removal of the additional resumption processes, specifically the ability to resume access rights on the basis of an Underutilisation Event (e.g. a</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(a) provide access holders with increased certainty and security over their access rights</p> <p>(b) ensure there is an appropriate balance between the interests of Aurizon Network and those of an access holder / train operator</p> <p>(c) better separate out the rights and responsibilities relating to an access holder and an operator</p> <p>(d) simplify arrangements and provide greater clarity around the rights and obligations of parties to an AA / TOD, reflecting our broader structural reforms.</p>		<p>mine closure).</p> <p><b>(2)(b) Disagree.</b> Aurizon Network disagrees with the QCA's reduction of the Allowable Threshold from 10% to 5%, on the basis that the QCA is seeking to alter a long-standing regulatory and contractual position that has existed over many years. This increases Aurizon Network's commercial and regulatory risk for which it is not compensated.</p> <p>Aurizon Network agrees with the QCA's decision for Security to be the equivalent of 6 months Take or Pay on the basis that, to the extent there is any shortfall in recovery of Take or Pay due to the Security amount being insufficient to offset the Take or Pay liability of a defaulting customer, Aurizon Network recovers this through the Revenue Cap process.</p>
<p>(3) The amendments we consider to be appropriate to achieve the above are set out in our CDD amended DAU.</p>		<p>Aurizon Network disagrees with the QCA's removal of provisions providing that Aurizon Network is not liable under the AA for acts or omissions required in order to maintain its Accreditation.</p>
<p>(a)</p>		<p><b>2(c) Agree with amendments.</b> Aurizon Network agrees broadly with the concept of simplifying the forms of access agreements to an AA and TOD and providing clarity around the rights and obligations of parties to an AA / TOD. This is subject to the specific comments made in the detailed table of comments on the AA and TOD and revised drafts of the AA and TOD attached to this response.</p>

## Access Agreement and Train Operations Deed

### Incorporation of terms from the Undertaking into the AA/TOD

Consistent with Aurizon Network's response to the IDD<sup>32</sup>, Aurizon Network agrees with the QCA's rationale that there should be standard provisions which act as a safe harbour where access seekers and Aurizon Network do not, or cannot, agree a different position. Aurizon Network is still of the view that the appropriate place to include all of these provisions is in the AA/TOD and not the Undertaking.

However, if the QCA insists on adopting the approach that it has taken in its CDD, the QCA's drafting requires further amendment to have the intended effect. Aurizon Network has proposed drafting to address this concern in the revised draft AA and TOD.

<sup>32</sup> Aurizon Network (2015a).

In particular, Aurizon Network considers that it is inappropriate for the Access Charge Provisions and the Force Majeure Provisions (as such terms are defined in the Undertaking) to be included in the Undertaking instead of the AA.

#### Access Charge Provisions

Under the 2010AU (as well as UT1 and UT2), the basis upon which access charges are invoiced are clearly set out in a schedule to the access agreements. The drafting in the AA in relation to the payment of access charges is very clear, well understood by industry and supported by a regulatory and commercial track record.

This is entirely logical given that the agreements are the means by which the parties agree to, in the case of Aurizon Network provide, and in the case of the access holder receive the benefit of the provision of, access rights for the operation of train services. It logically follows that the charges for the provision of these services should also be provided for in the same agreement (as is the case for most other commercial contracts). The effect of the QCA's proposed drafting will make it both challenging and cumbersome for access holders and Aurizon Network to have to refer to the Undertaking to administer the calculation of Access Charges for the purpose of billing under the AA.

#### Force Majeure Provisions

There is some duplication between the Force Majeure (FM) provisions that the QCA has included in Part 7 of the Undertaking and the provisions that are included in the AA and TOD.

As FM provisions are only of relevance to access holders, operators and Aurizon Network when an access agreement is on foot and train services have commenced, Aurizon Network can see no justification for including them in the Undertaking. Consequently, Aurizon Network has deleted the FM provisions from Part 7 of the Undertaking and included them in the AA and the TOD.

The QCA has made a number of changes to the FM provisions including:

- limiting the suspension of obligations following an FM event to only the obligation to provide access;
- requiring Aurizon Network to provide the initial FM notice (FM Notice) within 48 hours of the event or circumstance causing the FM event (FM Event), as opposed to the occurrence of the FM Event itself;
- providing that if Aurizon Network does not provide the FM Notice in the timeframe noted above, the suspension of obligations only occurs from the date the FM Notice is provided and not the date that the FM Event occurred.

The QCA amendments to the FM provisions do not reflect the usual formulation of FM clauses. That is, most FM clauses provide for the suspension of all the affected parties' obligations following an FM Event from the date of the FM event as opposed to being linked to the time of the provision of a FM Notice.

The timeframes proposed by the QCA also do not consider FM Events like cyclones, which could occur greater than 48 hours prior to it having the effect of becoming a FM Event for Aurizon Network. For this reason, Aurizon Network considers it is more appropriate for the timeframe to be triggered by the occurrence of the FM Event as opposed to the event or circumstance giving rise to the FM Event. Aurizon Network considers five business days to be an appropriate timeframe within which a FM Notice should be provided on the basis of the resources and systems available to Aurizon Network. Should the QCA maintain its proposed timeframe of 48 hours in its Final Decision, Aurizon Network will require additional resources and investments in system upgrades in order to be compliant, the costs of which are not reflected in the proposed MAR.

Aurizon Network has made a number of amendments to the operation of the FM provisions to address its concerns about the additional risk and administrative burden that has been imposed on it due to the QCA's drafting: Please refer to the revised drafts of the AA and TOD that are included with this response.

### **Extension of Aurizon Network's liability and uncertainty in relation to Disputes**

Aurizon Network remains concerned that if provisions are included in the Undertaking and those provisions take effect as obligations under the Undertaking, even if they are provisions which are incorporated by reference into the AA and TOD, this will not prevent disputes in respect of those provisions being dealt with under the Undertaking. This will potentially expose Aurizon Network to compensation claims under the QCA Act for breaches of those provisions. One potential way to address this concern would be to:

- include all of the provisions from the Undertaking which are intended to be incorporated by reference into the AA and TOD as a schedule to the Undertaking (Incorporated Terms Schedule), instead of in the main body of the Undertaking; and
- include in the operative provisions of the Undertaking a clause which states that Aurizon Network is obliged to incorporate the provisions in the Incorporated Terms Schedule in the AA or TOD, as applicable.

### **Review of the Standard AA and Standard TOD initiated by the QCA**

The QCA has included in Part 5 of the CDD amended DAU a right to initiate a review of, and impose amendments to, the Standard AA and Standard TOD that it considers appropriate to enhance the "workability" of the document. In Aurizon Network's view, the QCA should not be able to impose its own amendments to the Standard AA or Standard TOD as it has purported to do. Aurizon Network considers that the QCA's role should be limited to approving or rejecting amendments proposed by Aurizon Network. Please refer to:

- Aurizon Network's revised draft of Part 5; and
- Aurizon Network's comments in relation to these amendments in the detailed comments table on the AA and TOD that is included in Volume 3.

### **Security**

The QCA has repeated its proposal that an access holder be required to provide an amount equal to six months of its Take or Pay liability as Security. Aurizon Network remains of the view that an amount equal to 12 months' Take or Pay charges is more appropriate as a Security amount for the reasons set out in its previous response to the IDD<sup>33</sup>. This is due, in particular, to the increase in credit risk that Aurizon Network is exposed to as a consequence of the increasing trend of end users becoming access holders, with many of these access holders not having the financial capacity of incumbent operators.

The QCA in its CDD considers Aurizon Network has significant protection from such credit risk as it is entitled to recovery of any unrecovered revenue through the revenue cap adjustment mechanism, such that any credit risk is socialised across system users rather than borne by Aurizon Network.

Aurizon Network does not consider the current revenue cap adjustment mechanism in Schedule F of the Undertaking reflects this intention. Subject to Schedule F of the Undertaking being amended to clearly state that Aurizon Network may, through the revenue cap process, recover any shortfall in revenue arising from the difference between the Security amount held by Aurizon Network and the amount of a

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<sup>33</sup> Aurizon Network (2015a). Part 8.

defaulting customer's Take or Pay liability, Aurizon Network accepts the QCA's proposal that the Security amount be equal to six months of the relevant Customer's Take or Pay.

The QCA has also made a number of amendments to the Security provisions, including providing for when Aurizon Network may have recourse to Security. Please refer to Aurizon Network's comments in relation to these amendments in the detailed comments table on the AA and TOD that is included in Volume 3.

### **Aurizon Network Cause**

Aurizon Network disagrees with the QCA's CDD to include Operational Constraints in the definition of Aurizon Network Cause. The effect of the QCA's proposal would be to allocate a number of Rail Operator, environmental and Customer imposed risks to Aurizon Network, as well as to attribute a fault element to normal maintenance practices. The cumulative impact of the proposed changes would be to significantly increase the business risks faced by Aurizon Network without any corresponding adjustment to the return that Aurizon Network can earn.

Aurizon Network uses Operational Constraints to:

- manage Infrastructure defects, the root cause of which are rarely binary (i.e. solely attributed to Aurizon Network or Rail Operator);
- have an efficient and effective maintenance regime that provides Aurizon Network with the flexibility to respond to ensure proper maintenance of its infrastructure and respond to Infrastructure Defects in a pragmatic way, which minimises costs and disruptions to train services; and
- assist Customers where the imposition of an Operational Constraint is a cost efficient and safe alternative to Infrastructure upgrades, and allows the continuation of train services in circumstances where the alternative is that the costs of any Infrastructure upgrade would make it prohibitive or exceed the economic benefit of continuing to operate the train services.

If Operational Constraints remain in the definition of Aurizon Network Cause, Aurizon Network would, in the instance of Infrastructure defects, be required to investigate the root cause and seek to attribute fault to either an access holder or a Rail Operator, the latter being an exclusion to Aurizon Network Cause. As Infrastructure defects are not binary, this would be almost impossible. For example, rail breaks are Infrastructure defects which can occur as a result of Operators running with flat wheels, as well as due to extreme heat or cold conditions. It is also a defect that occurs over a period of time (i.e. one locomotive running over a section of track with a flat wheel is unlikely to cause a rail break, but several locomotives running over an extended period of time, potentially in conjunction with extreme heat or cold, will cause a rail break).

Operational Constraints are also used to prevent or minimise Infrastructure defects and minimise the risk of network outages. For example, during periods of heavy rain or high temperatures Aurizon Network imposes speed restrictions to manage the risk of initiating or exacerbating mud holes or track buckling respectively.

Aurizon Network would also be penalised where it is using Operational Constraints as part of its Maintenance regime that aims to minimise impacts to Train Services. As an example, speed restrictions are required to allow Aurizon Network to conduct maintenance activities between trains and also to allow single line running in duplicated track sections. They also allow Aurizon Network to defer repairs of Infrastructure Defects until a planned system shut. This means Aurizon Network can prioritise the remedy of defects and minimise impacts to Train Services. It is also more cost efficient, given economies of scale are achieved when undertaking maintenance work in planned system shuts, and requires lesser investment in maintenance equipment.

The imposition of speed restrictions is also commonly used in the usual course of installing new rail, with speed restrictions being imposed on relevant track sections in the interval between when new rail is installed and the legally required re-stressing activity is carried out. This approach reflects industry practice and should not expose Aurizon Network to reduced revenue. Operational Constraints are clearly important tools utilised by Aurizon Network to efficiently maintain the network and it is unreasonable to penalise Aurizon Network in such cases.

Operational Constraints can also be used by Aurizon Network to assist Operators and End Customers. This can be achieved by Aurizon Network agreeing to the imposition of Operational Constraints in order to approve a derogation from asset standards and as an alternative to Infrastructure Upgrades. This is usually in circumstances where the costs of the Infrastructure Upgrades or compliance with the asset standard would likely have exceeded the economic benefit of continuing train services by the Operator for the End User.

For these reasons, Aurizon Network disagrees with the QCA's inclusion of Operational Constraints in the definition of Aurizon Network Cause.

### **Allowable Threshold/Schedule F of the Access Undertaking**

Aurizon Network disagrees with the QCA's decision in the CDD to reduce the 'allowable threshold', which is a long-standing part of the liability limitations for non-provision of access within the Standard Access Agreement, from 10% to 5%. Aurizon Network also disagrees with the QCA's proposal to lower the 'allowable threshold' in the calculation of Total Actual Revenue in Schedule F.

Aurizon Network has sought to 'hardwire' the "Allowable Threshold" into the Standard AA rather than leaving it to be agreed by the parties on a case by case basis. This is because in every AA that has been negotiated and agreed between Aurizon Network and an access holder over many years, 10% has been included as the "Allowable Threshold". Given the track record with negotiating the "Allowable Threshold", it seems appropriate to reduce the inefficiency of negotiating what has effectively become over time a standard figure, being 10%.

Aurizon Network in its response to the QCA's IDD<sup>34</sup> stated that it could not accept the reduction in the 'allowable threshold' due to the additional risk for which it was not being compensated. The QCA is seeking to alter a long-standing regulatory and contractual position that has existed over many years in a way that increases Aurizon Network's commercial and regulatory risk. The QCA in the CDD has not addressed this material concern. Without compensation for the additional risk, the change to the allowable threshold remains unacceptable to Aurizon Network.

It is also important that the 10% threshold used in the revenue cap provisions is not an arbitrary number, as that figure has been previously approved by the QCA as appropriate on multiple occasions. Notably, on those past occasions the relevant standard AAs approved by the QCA did not hardwire an equivalent percentage figure in the relevant liability provision – that "Allowable Threshold" was left to be negotiated by the parties. This meant that it was entirely possible that parties could negotiate an "Allowable Threshold" for the purpose of an AA that was more or less than the figure used in the revenue cap calculations.

The figure is also not arbitrary, because, as noted above, the "Allowable Threshold" included in each of the AAs that Aurizon Network has executed has consistently been 10% - not 5% as currently proposed by

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<sup>34</sup> Aurizon Network (2015a).

the QCA. Aurizon Network's proposals are supported by a regulatory and commercial track record – whereas the QCA proposes to depart from both in an entirely arbitrary fashion.

In addition to the arbitrary nature of the QCA's proposed figure compared to Aurizon Network's proposal, Aurizon Network is also concerned at the QCA's underlying requirement for alignment. The QCA has stated in the CDD:<sup>35</sup>

*We note the allowable threshold links to the breach mechanism in Schedule F of the undertaking. This mechanism ensures Aurizon Network does not use the revenue cap mechanism to recover access charges which it is not entitled to under an access agreement.*

*We have amended the breach threshold in the Schedule F revenue cap provisions to align with the allowable threshold in the access agreement (i.e. 5 per cent). This means Aurizon Network will not be entitled to recover revenues via the revenue cap more (or less) than it is entitled to under its contractual arrangements. (footnotes omitted)*

In the 2010AU, the percentage used in the relevant Standard AA provision and the revenue cap provision are aligned but the provisions themselves are in fact not aligned. This is still the case based on the QCA's proposals under the CDD. Therefore, Aurizon Network does not agree that a reduction in the AA allowable threshold should also apply to the revenue cap.

Prior to the QCA's Final Decision, Aurizon Network proposes to provide amended Schedule F drafting to the QCA that does align the provisions in Schedule F more closely with the Standard AA. Specifically, this will be to amend the allowable threshold under the revenue cap to apply on an AA basis rather than an origin/destination combination and also to ensure that the other limits under the relevant provision in the Standard AA are also applied to the revenue cap provision. These changes are consistent with the QCA's requirement for alignment between the provisions.

Aurizon Network has made the above submissions in the interest of a timely settlement of UT4. Despite the above submissions, Aurizon Network cannot find any basis to agree with the QCA's approach on the linkage between the AA and revenue cap and the process around ensuring increased risk results in additional reward. Aurizon Network therefore reserves its right to review this as part of developing its proposals for UT5.

### **Notification Requirements under the Train Operations Deed**

The QCA has amended Aurizon Network's requirements to notify Operators of impacts to Train Services by removing the materiality threshold, with the result that Aurizon Network would be required to notify the Operator for any impacts +/- 3 minutes from the Train's Scheduled Time.

Aurizon Network requires a materiality threshold under the notification requirements to reflect the fact that time delays are not the only factor to consider in whether a Train Service will be materially impacted by an event or circumstance. A holistic approach is required and Aurizon Network considers a variety of factors including:

- the ability to recover to plan in the following sections of the train journey;
- delays at the port and any queuing occurring; and
- impact to the Operator's planned crew change, provisioning times, reliability examinations and planned connections

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<sup>35</sup> Queensland Competition Authority (2015a). p.251.

To the extent a delay on section of a train journey can be recovered in a following section, such that the train service is not impacted in its ability to load / unload, meet connections or crew change times, then the notification to the Operator has no practical purpose.

On average in a 24 hour period, Aurizon Network records over 1000 delays between 3 and 20 minutes. Not all these delays will result in an impact on an Operator's ability to load / unload within its cycle time. Requiring Aurizon Network to notify of all delays regardless of impact to the Train Service in its entirety would require significant additional resourcing.

Please refer to Aurizon Network's comments in relation to these amendments in the detailed comments table on the AA and TOD that is included in Volume 3.

### **Resumption of Access Rights**

The QCA has maintained its IDD position on resumption rights, reverting to the 2010AU position and rejecting Aurizon Network's right to resume access rights on a forward looking basis.

Aurizon Network disagrees with the QCA's decision for the reasons set out in its response to the QCA's IDD, which are incorporated here by reference.<sup>36</sup>

### **Reduction of Nominated Monthly Train Services**

The QCA has maintained its IDD position on the provisions allowing the Reduction of Nominated Monthly Train Services where Operators exceeded the Maximum Payload or Access Holder / Aurizon Network sought to increase the Maximum Payloads.

Aurizon Network disagrees with the QCA's decision for the reasons set out in its response to the QCA's IDD, which are incorporated here by reference.<sup>37</sup>

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<sup>36</sup> Aurizon Network (2015a). s.8.4, pp.111-115.

<sup>37</sup> Aurizon Network (2015a). s.8.4, pp.111-115.

## Chapter 9 – Connecting Private Infrastructure (Part 9)

### Summary of Aurizon Network’s Position

Aurizon Network maintains that Part 9 dealing with connecting infrastructure has been submitted on a voluntary basis as there is no requirements within the QCA that requires this commitment. Accordingly Aurizon Network is not prepared to accept amendments that increase its costs or risks, particularly in the absence of any consideration of compensation.

While Aurizon Network is not opposed to amendments that seek to improve the transparency of the process, it remains of the view that an overly prescriptive connecting infrastructure process should not be adopted given the high degree of uncertainty around key proposed mining project issues (which include fundamental matters such as the grant of mining leases, native title concerns, environmental approvals and financing). Further, there is no evidence that the amendments sought by the QCA are required to deal with demonstrated, or even perceived, risks.

Aurizon Network is naturally incentivised to negotiate and approve connecting arrangements to the CQCIN in order to protect and expand its revenue base. This is demonstrated by the fact that despite the Standard Rail Connection Agreement (SRCA) only having been introduced in 2013, Aurizon Network has negotiated and entered into a number of connection agreements over the last five years. During this time, and in the absence of a prescriptive process, the process of concluding connecting arrangements has not delayed or prevented any mining project from proceeding.

The CDD proposes that Aurizon Network should not derive any profit or even compensation for overhead costs for activities relating to design, construction, project management and commissioning of connecting infrastructure. At the same time, Aurizon Network will be exposed to costs incurred by a Private Infrastructure Owner as a result of delays, including failure to meet a Connection Milestone. Aurizon Network believes that the proposed approach, which has the effect of discriminating against Aurizon Network by imposing additional risks on it while preventing it from recovering costs (or earning a margin for assuming additional risks), is clearly inimical to its legitimate business interests.

In relation to other matters addressed in the CDD:

- the SRCA has been agreed with industry and should be retained unchanged;
- Aurizon Network maintains that the application of the CLMP provisions should not be softened.

Aurizon Network’s positions remain consistent with its response to the QCA’s IDD, which is incorporated here by reference.<sup>38</sup>

**Table 9.1 – QCA Consolidated Draft Decision**

QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(1) After considering Aurizon Network’s proposed framework for connecting private infrastructure, our consolidated draft decision is to refuse to approve Aurizon Network’s proposal.	9.1	<b>Disagree.</b> Aurizon Network has included a process for connecting Private Infrastructure in its 2014 DAU on a voluntary basis. As there is no legal requirement to include this process, Aurizon Network is not willing to accept amendments proposed by the QCA where such
(2) We consider it appropriate that Aurizon Network amend its draft access		

<sup>38</sup> Aurizon Network (2015a). Part 9, pp.116-121.

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
undertaking in the manner proposed in our consolidated draft decisions 9.2, 9.3 and 9.4.		amendments increase Aurizon Network's costs and risks beyond what has been offered.
<p>(1) After considering Aurizon Network's proposed framework for connecting private infrastructure, our consolidated draft decision is to refuse to approve Aurizon Network's process for connecting private infrastructure.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking in the manner proposed in Part 9 of the CDD amended DAU, that is:</p> <p>(e) upon the receipt of a written proposal from a PIO, Aurizon Network is required to negotiate with the PIO and to agree on the milestones</p> <p>(f) the connection milestones negotiation process should conclude within a period no longer than two months from the date Aurizon Network notifies the PIO it has decided the PIO's proposal meets the required criteria</p> <p>(g) arrangements should be clarified for where Aurizon Network is responsible for designing and building the connecting infrastructure</p> <p>(h) Aurizon Network is to pay reasonable costs incurred by a PIO arising out of Aurizon Network's unreasonable delay.</p>	9.2	<p><b>(2)(a) Disagree.</b> Aurizon Network reiterates that seeking to agree Connection Milestones at this stage is premature given the high degree of uncertainty over key aspects of proposed mining projects.</p> <p><b>(2)(b) Disagree.</b> Aurizon Network's submission is that, apart from the fact that seeking to agree Connection Milestones in relation to an embryonic mining project is premature, there is no reasonable basis for requiring that such milestones be agreed within a relatively tight timeframe.</p> <p><b>(2)(c) Disagree.</b> Aurizon Network does not volunteer to include matters relating to the design and construction of connecting infrastructure, or the inclusion of a standard construction agreement, within the framework of the Undertaking.</p> <p><b>(2)(d) Disagree.</b> It is not in Aurizon's legitimate business interests to be compelled to assume risk for which it receives no return (or even contribution toward its overheads).</p>
<p>(1) After considering Aurizon Network's proposed framework for connecting private infrastructure, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend the 2014 DAU in the manner proposed in the SRCA contained in the CDD amended DAU; that is, to provide greater clarity (without changing the intent), and to:</p> <p>(i) provide a process by which Aurizon Network may design, construct and commission the connecting infrastructure</p> <p>(j) require Aurizon Network to consult with (not just notify) the PIO in respect of proposed changes to system operating parameters as soon as practicable.</p>	9.3	<p><b>Disagree.</b> Aurizon Network re-iterates that the SRCA is voluntarily provided with the Undertaking and that there is no desire or need to renegotiate the terms of the SRCA.</p>
<p>(1) After considering Aurizon Network's proposed framework for connecting private</p>	9.4	<p><b>(2)(a) Agree.</b></p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
infrastructure, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.		<b>(2)(b) Disagree.</b> Aurizon maintains that the conditions and requirements for coal producers to minimise the impact of coal loss on the network be retained and absolute.
(2) We consider it appropriate that Aurizon Network amend its draft access undertaking in the manner proposed in the CDD amended DAU, by:		Aurizon Network further notes that section 188(2) of the QCA act calls on the Undertaking to not treat access seekers differently in negotiations or treat users differently in providing access to the service. A move away from a consistent approach to CLMP would be contradictory to this direction.
(k) including CLMPs as a schedule to the access undertaking (Schedule J)— with the SRCA referring to CLMPs as specified in the access undertaking		
(l) better aligning the CLMPs with the 2010 CDMP, while also providing an adequate framework for coal producers to implement 'best practice' strategies if it is practicable for them to do so.		

## CDD 9.1 Voluntary inclusion of process for connecting Private Infrastructure

Aurizon Network re-iterates the positions adopted in its response to IDD, which are incorporated here by reference. Specifically Aurizon Network has previously stated that:<sup>39</sup>

*...the Private Connecting Infrastructure regime proposed by the QCA seeks to direct practices which it perceives to be efficient, rather than its proper role of ensuring efficient outcomes are not inhibited by the connection process. The QCA's approach towards the manner by which private infrastructure is connected to the CQCR network represents an attempt to allocate risks, determine performance management arrangements and even impose penalties, which only the parties to a contract can properly determine through negotiation."*

The changes sought by the QCA in the CDD to Part 9 of Aurizon Network's 2014DAU do not address the substance of this concern. The QCA is still seeking to impose a more prescriptive connecting infrastructure regime without providing evidence or demonstrating why such a regime is required. This approach is particularly problematic given:

- the voluntary inclusion of the process for connecting infrastructure by Aurizon Network, which reflects an appropriate allocation of risk and cost between Aurizon Network and the owners of private infrastructure;
- Aurizon Network's voluntary undertaking to only recover the reasonable and prudent costs associated with connecting infrastructure; and
- the clear commercial incentive that Aurizon Network has to facilitate the connection of private infrastructure to the CQCN. This incentive is evidenced by the conclusion of a number of connection arrangements over the last five years and the absence of any proof that a failure by

<sup>39</sup> Aurizon Network (2015a). p.117.

Aurizon Network to conclude such arrangements has prevented a mining project from proceeding.

Further, the approach adopted by the QCA appears all the more prescriptive when compared with the high level process for connecting with ARTC's network in the Hunter Valley<sup>40</sup>, which relevantly, does not seek to determine timing or milestones, require mandatory reporting on connection matters to the ACCC or allocate costs of delay to ARTC. No factual basis has been provided by the QCA or stakeholders to demonstrate why such a contrasting approach has been adopted in relation to the CQCN.

In seeking to regulate such matters the QCA is acting beyond the power to which it has been afforded by the QCA Act. For example, the inclusion of clause 9.1 k (ii) of Part 9 in the CDD amended DAU deals with subject matter that is properly the purview of an appropriate construction agreement or rail connection agreement. Those agreements, once signed, should solely govern the time for performance of related obligations and associated consequences for non-performance. Those issues do not relate to the provision of access and therefore are not matters that should be enshrined in the Undertaking.

Further, the construction of connecting infrastructure would in Aurizon Network's view constitute an Extension under the QCA Act and as such Aurizon Network cannot be forced to fund the construction. It follows that if Aurizon Network decides to fund the construction it can do so on agreed commercial terms, which would include full recovery of its costs and an appropriate margin. If Aurizon Network chose to proceed on this basis it would properly price the risk to which it is being exposed. In contrast the QCA is seeking to impose risks such as payment of delay costs without appropriate compensation. This is not in Aurizon Network's legitimate business interest.

## CDD 9.2 Transparency of process

As noted in its response to the IDD, Aurizon Network is broadly supportive of changes to Part 9 of the 2014 DAU which promote greater transparency of process<sup>41</sup>. However Aurizon Network remains opposed to the introduction of mandatory Connection Milestones that are required to be agreed at a very early stage in the development of a proposed mining project.

Aurizon Network acknowledges that the QCA has modified its approach in the CDD to enable Aurizon Network and the Private Infrastructure Owner (PIO) to agree to delay setting Connection Milestones until an access agreement requiring the proposed connection to the network has been entered into. While this offers a somewhat more reasonable approach, this still requires agreement to be reached between the two parties failing which, Aurizon Network will be obliged to agree to what will be binding Connection Milestones where it is exposed to delay costs incurred by the PIO. Notably the CDD acknowledges that the approach adopted "may result in more disputes arising from parties being unable to agree on milestones."<sup>42</sup>

Aurizon Network wishes to emphasise that proposed mining projects are subject to a number of significant timing risks associated with key aspects such as approval of mining tenure, resolution of Native Title matters, the grant of environmental approvals and the finalisation of financing arrangements. Viewed within this context, it does not make sense to compel Aurizon Network and a PIO to agree rigid timeframes at what is usually an early stage in a proposed project's development process. Experience indicates that the majority of proposed mining projects will either not proceed for a variety of reasons or

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<sup>40</sup> <https://www.artc.com.au/customers/access-hunter-valley/library/ARTC%202014%20HVAU.pdf> (Clause 6, page 58).

<sup>41</sup> Aurizon Network (2015a). p.118.

<sup>42</sup> Queensland Competition Authority (2015a). p.269.

will experience significant delays in matters unrelated to the finalisation of connecting infrastructure arrangements.

### CDD 9.3 QCA approach to costs and risks

The CDD maintains the QCA's position that Aurizon Network may only recover direct reasonable costs (with no profit, margin or overhead) relating to design, construction, project management and commissioning of connecting infrastructure. Clearly under this approach Aurizon Network is not compensated for risks associated with design, construction, project management and commissioning activities.

The drafting of Part 9 in the CDD amended DAU has the effect that Aurizon Network is not entitled to any payment, even for direct costs, if a connection does not proceed. To the extent Aurizon Network's costs for the design, construction, project management and commissioning of connecting infrastructure relate to the provision of access, the QCA Act confirms that Aurizon Network is entitled to *at least* its efficient costs and a return on its investment commensurate with its commercial and regulatory risks. The inclusion of clause 9.1(k)(iii) by the QCA in Part 9 is therefore directly inconsistent with the pricing principles under section 168 of the QCA Act.

Having inhibited Aurizon Network's ability to recover its full costs or be compensated for risk that it is exposed to, the CDD nevertheless requires, under clause 9.1(l) of Part 9, that Aurizon Network must pay all reasonable costs (excluding consequential loss) incurred by a PIO arising from Aurizon Network's unreasonable delay in entering into Rail Connection Agreement or agreements relating to design, construction and/or commissioning of connecting infrastructure.

As discussed above, liability for delays in construction and commissioning should properly be regulated under the relevant agreements once they have been executed by the parties. These are not matters that should be included in Aurizon Network's Undertaking.

The allocation of delays costs as part of that dispute regime is beyond the power that the QCA is afforded under the QCA Act. By 'hard wiring' into Aurizon Network's Undertaking an entitlement to delay costs the QCA has, in effect, afforded itself a jurisdiction to determine and award contractual damages, which is not permitted under the QCA Act. As such clause 9.1(l) in the CDD amended DAU should be deleted in its entirety.

The inclusion of the payment of delay costs by Aurizon Network in the Undertaking will drive an unnecessarily complex contract administration regime in the construction agreement. The construction of connecting infrastructure is not a typical market-based construction project. Aurizon Network is not a contractor receiving a commercial return on its work and the customer is not a client that will ultimately own or operate the connecting infrastructure. Most notably, both Aurizon Network and the customer usually perform works during the construction of the connecting infrastructure and are interdependent when it comes to the successful delivery of the connection works.

In previous projects both the customer and Aurizon Network have agreed to flexibility in terms of timeframes in which Aurizon Network and the customer are to undertake their particular works. If connection milestones and associated delay costs are to be hard wired into the Undertaking, then this risk will need to be properly and fairly managed by Aurizon Network and the customer in the construction agreement. In practice this will mean that there may need to be an independent superintendent to assess delay claims and extension of time claims by Aurizon Network and the customer. This process will involve both increased cost, time and complexity for both Aurizon Network and the customer and will significantly alter the dynamics in which these projects have been successfully delivered in the past. In short, it will turn the construction of the connecting infrastructure into a 'traditional' market-based project when in reality it has very few of those attributes.

It is also worth noting that the QCA has sought in clause 9.1(l) of the CDD amended DAU to extend Aurizon Network's liability for delays beyond a Private Infrastructure Owner to also include access seekers and access holders. It is not clear why the QCA has sought to expand the application of this provision in this way. Beyond the submissions above regarding the QCA acting beyond its power, Aurizon Network believes that this change, which seeks to extend the application of a new liability framework to additional counterparties for delays relating to the entering into or performance of obligations under connecting infrastructure arrangements with a PIO, is beyond the QCA's power.

However, if the mischief that the QCA seeks to address is to avoid delays to the use of access rights as a result of delays in entering into a SRCA or construction agreement, Aurizon Network is happy to address this issue. Specifically, if there is a delay in entering into a SRCA by an access seeker then that is a matter that could be considered as part of the dispute regime within the Undertaking. On the basis that clause 9.1(l) is deleted Aurizon Network is prepared to accept a firm obligation to enter into a SRCA and construction agreement within two months of an access agreement being entered into. Any failure by Aurizon Network to meet this timing then could properly be the subject of a dispute. Arguably this issue does not need to be explicitly addressed given that Aurizon Network has an existing general obligation not to hinder access. Again the parties could always decide that a particular project warranted the negotiation of different risk allocations in respect of delay costs under the construction agreement, which is a more desirable outcome than regulation.

The QCA does not offer an explanation as to why it has sought to oppose such an asymmetric approach that allocates additional risks to Aurizon Network (which Aurizon Network has explicitly stated it does not volunteer to accept), while at the same time severely restricting Aurizon Network's ability to fully recover its costs (let alone earning a margin for the additional risks imposed).

This approach is clearly inconsistent with the QCA's recognition<sup>43</sup> that Aurizon Network's legitimate business interests includes being able to recover the reasonable costs for work undertaken.

## CDD 9.4 Standard Rail Connection Agreement

Aurizon Network's position in relation to the SRCA remains unchanged from its response to the IDD<sup>44</sup>, which is incorporated here by reference.

The intent of the SRCA is to provide a base agreement for parties to utilise during commercial discussion pertaining to new rail connections. It is widely understood by coal producers and Aurizon Network that individual clauses within the SRCA can be amended as agreed by the parties in the negotiation. Furthermore, the SRCA is provided on a voluntary basis by Aurizon Network as part of the suite of standard agreements under the Undertaking.

Given that the SRCA is negotiable between parties subject to the agreement and that the agreement does not form a part of the Undertaking there is no requirement to revisit its current drafting.

Aurizon Network will continue to work with its stakeholders in seeking improvement to the SRCA and agrees with the QCA's view that this agreement should seek to be flexible, transparent and consultative. Aurizon Network intends that any agreed changes to the SRCA be completed as required at required intervals.

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<sup>43</sup> Queensland Competition Authority (2015a). p.259.

<sup>44</sup> Aurizon Network (2015a). s.9.7, p.121.

## 9.5 – Coal Loss Mitigation Provisions

Aurizon Network agrees with the removal of the Coal Loss Mitigation Provisions (CLMP) from the SRCA and the inclusion in the Undertaking as new Schedule J.

Aurizon Network continues to disagree with the QCA with regard to a softening of the provisions to have CLMP, in particular the introduction of drafting that introduces a reasonable endeavours lens to this requirement.

In its response to the IDD, Aurizon Network detailed its reasoning for not agreeing with the QCA's IDD position of introducing "Limiting Factors" into the implementation of coal loss prevention measures and weakening customer obligations to prevent coal loss during the loading of wagons.<sup>45</sup>

Aurizon Network maintains that the need for CLMP remain absolute. This position is consistent with the industry approach taken at the introduction of coal loss provisions. If a party utilises the Limiting Factor drafting to not install CLMP, then this saving to that party will ultimately be borne as an additional cost to the supply chain via increased coal loss clean up and track maintenance charges related to issues caused by fouling. Therefore the sum result to the supply chain will be a cost.

Aurizon Network could agree to the amended drafting that allows for best practice and changes in technology to be adopted as practicable but not at the detriment of network protection from coal loss that is currently managed via the existing CLMP.

Aurizon Network would accept the revised Schedule J<sup>46</sup> if:

- clause 1.4 drafting changes be reversed thus removing the clause references to "Limiting Factors" and all subsequent references to Limiting Factors in clauses 1.5 (ii), 1.7 (b), 1.9 (b) and 2.3 (b);
- the words "reasonable endeavours" be retained as "must" in clauses 1.4 (a), 1.5 (a), 1.9 (b), 2.2 (c) and 2.5.

## Drafting clarifications

Aurizon Network seeks clarification of the following:

- that the reference to 'safety standards' at clause 9.1(k)(iv) of Part 9 of the CDD amended DAU should be the defined term 'Safety Standards';
- why the last paragraph of clause 9.1(n) of Part 9 of the CDD amended DAU is necessary if clause 9.1(k)(iv) is included;
- whether the scope of clause 9.1(l), in particular, the payment of delay costs by Aurizon Network, is intended to extend to a PIO, access seeker and access holder or just to the relevant counterparty to the particular agreement. The QCA's CDD would indicate that the payment of delay costs should only be restricted to PIOs. Aurizon Network would agree that if delay costs are included then they should only be payable to the counterparty to the relevant agreement.

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<sup>45</sup> Aurizon Network (2015a). p.120.

<sup>46</sup> Queensland Competition Authority (2015a). p.459.

## Chapter 10 – Baseline Capacity and Supply Chain Management (Part 7A)

### Summary of Aurizon Network’s Position

The assessment of network capacity is of critical importance in the negotiation of provision of new access rights to access seekers. It also underpins future network development planning, which needs to be undertaken in the context of the wider supply chain. By way of background, a summary of Aurizon Network’s approach to capacity assessment is provided in this chapter. This is considered important because some of the proposals made by the QCA in the CDD may reflect a lack of understanding of key capacity metrics and the way in which capacity assessment is undertaken in practice.

Overall, Aurizon Network fully supports appropriate transparency and consultation in assessing capacity and identifying and evaluating scenarios to accommodate growth and improve supply chain performance. However, it has a number of material concerns with Part 7A of the CDD amended DAU. While Aurizon Network is prepared to accept some of the QCA positions, there are others that it cannot accept and they are the focus of this response. Aurizon Network has identified amendments that are unnecessary or unreasonable, impractical or unworkable, or beyond power.

In relation to the Network Development Plan (NDP), Aurizon Network’s overarching objective is to use it to identify the medium to long term capacity options to meet the future demand for access in each system, over a ten to fifteen year horizon. Aurizon Network disagrees with the QCA’s proposed purpose of the NDP and its shorter planning horizon, as well as a number of amendments which introduce unnecessary and unreasonable prescription. Aurizon Network is also strongly opposed to the NDP being subject to dispute. Dispute is only appropriate once potential developments have entered the expansion process in Part 8, not where parties disagree with Aurizon Network’s long term network planning document.

Aurizon Network also considers that the process for rectification of any identified capacity deficits should align with the expansion framework in Part 8. Consistent with its position on expansions, Aurizon Network cannot accept any obligation that may require it to fund an expansion needed to rectify a deficit as an outcome of a dispute resolution process.

Aurizon Network has identified a number of other ‘second order’ drafting issues for Part 7A of the CDD amended DAU. These will be identified and explained with the lodgement of the revised draft of Part 7A.

**Table 10.1 – QCA Consolidated Draft Decision**

	QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(3)	After considering the 2014 DAU’s approach for Aurizon Network’s participation in supply chain groups, our consolidated draft decision is to refuse to approve Aurizon Network’s proposal.	10.1	<b>2(a) Disagree.</b> Aurizon Network has already volunteered to assume a reasonable endeavours obligation to participate in supply chain groups. It is beyond the power of the QCA to require any stronger obligation.
(4)	We instead consider it appropriate to propose Aurizon Network amend the 2014 DAU as follows:		<b>2(b) Disagree.</b> It is beyond the power of the QCA to require Aurizon Network implement supply chain group decisions.
	(a) Aurizon Network be required to participate in supply chain groups where the efficient cost of involvement is recoverable under the undertaking		<b>2(c) Disagree.</b> Part 2 already includes provisions that prohibit unfair differentiation between access seekers or between access

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(b) Aurizon Network be required to implement actionable outcomes of the supply chain group, subject to: there being no adverse effect on Aurizon Network's network management principles, SOPs and system rules; and holding the right to dispute resolution</p> <p>(c) Aurizon Network be required to participate in supply chain groups in a way that does not unfairly differentiate between:</p> <p>(i) supply chain groups, to ensure no supply chain is unfairly prioritised over another</p> <p>(ii) access seekers within a supply chain group</p> <p>(iii) access holders within a supply chain group,</p> <p>in a way that has a material adverse effect on the ability of one or more users to compete with others.</p> <p>(5) The amendments that we consider to be appropriate to achieve the above are set out in clause 7A.3 of our CDD amended DAU.</p>		<p>holders. Aurizon Network does not volunteer to include this provision as well.</p>
<p>(1) Our consolidated draft decision is to refuse to approve Aurizon Network's 2014 DAU capacity review proposal.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is as we have indicated in our CDD amended DAU:</p> <p>(a) The baseline capacity assessment process will be conducted in accordance with the way set out in Section 10.4.1 above, which proposes, among other things:</p> <p>(i) Aurizon Network must consult with access holders, access seekers (and, where applicable, their customers) in preparing its baseline capacity assessment. Aurizon Network and those parties can agree on different processes and/or outputs than those prescribed in the undertaking.</p> <p>(ii) Aurizon Network must, unless otherwise agreed with stakeholders, submit an un-redacted baseline capacity</p>	<p>10.2</p>	<p><b>2(a) Disagree.</b> There should not be a difference in requirements for a baseline capacity assessment and any other capacity assessment. Aurizon Network believes that there is an opportunity for clarity and simplification of drafting with a single approach throughout.</p> <p><b>2(a)(i) Agree with amendments.</b> Consultation should be with access holders only as this assessment deals with Committed Capacity. Access seekers are consulted when capacity is assessed as a part of their access requests.</p> <p><b>2(a)(ii) Agree.</b></p> <p><b>2(b)(i) Agree.</b></p> <p><b>2(b)(ii) Agree.</b></p> <p><b>2(b)(iii) Disagree.</b> The capacity assessment will assess whether network capacity is sufficient for Committed Capacity. There will be no measure of absolute capacity or available capacity.</p> <p>This capacity assessment is not relevant to compliance with access agreements, which will be determined in accordance with the terms of the agreements and not the undertaking. The</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
assessment report (of the CQCN and each coal system) to us for approval no later than six months after the 2014 DAU's approval.		QCA has no role in compliance matters under access agreements.
(b) the baseline capacity assessment (including subsequent capacity assessments) must outline:  (i) operation, maintenance and construction planning assumptions  (ii) network management principles, SOPs and system rules assumptions  (iii) measures of absolute capacity, existing capacity, committed capacity and available capacity.  Access holders can rely on these outputs to validate Aurizon Network's compliance with their access agreements, and access seekers can rely on these outputs to inform their access applications.		<b>2(c) Agree with amendments.</b> There is a need to have a clear process for the review. Aurizon Network's response to the IDD described a proposed terms of reference for such reviews. Also, the confidentiality obligations in the CDD amended DAU must be strengthened because it only restricts the expert from disclosing matters that could constitute a breach of Aurizon Network's obligations under Part 3. As the expert is not bound by Part 3, this obligation is ineffective and should be redrafted.  <b>2(d) Agree with amendments.</b> There should be one process of expert assistance to review Aurizon Network's capacity assessment and where not approved by the QCA, develop an alternative view (as per (c) above and this (d)). As stated above, this process should adopt Aurizon Network's proposed terms of reference.
(c) When reviewing Aurizon Network's baseline capacity assessment, we can hire a qualified and independent expert to assist with our review of that assessment. The expert will have regard to the need for independence, confidentiality and to account for any stakeholder submissions received during its review		<b>2(e) Disagree.</b> In Aurizon Network's view, there is no relevance to this being binding – it is simply the QCA approving Aurizon Network's capacity assessment or stating the outcome of its own.  <b>2(f) Agree with amendments.</b> The ongoing process should be the same as the baseline capacity assessment process.
(d) If we do not approve Aurizon Network's baseline capacity assessment, and Aurizon Network has not resubmitted a compliant assessment (or has not resubmitted the assessment at all), then we can appoint an independent expert to support us with our own baseline capacity assessment. The expert will have regard to the need for independence, confidentiality and to account for any stakeholder submissions received during its review		<b>2(g) Agree.</b>  <b>2(h) Disagree.</b> Consistent with the response to 2(e), there is no relevance to this being binding – it is simply the QCA approving Aurizon Network's capacity assessment or stating the outcome of its own.
(e) Our approval of the outputs of the baseline capacity assessment (including recommendations from any expert-review process) would be subject to us having regard to the section 138(2) matters in the QCA Act. If we approve those outputs, the outcome will be binding		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>on Aurizon Network and other stakeholders</p> <p>(f) Aurizon Network must conduct subsequent capacity assessments, annually at least, to demonstrate if existing capacity can deliver committed capacity. If requested by access holders (holding at least 60% of train paths, or representing 60% of the number of access holders) or us, Aurizon Network will (acting reasonably) engage an independent expert to review the capacity assessment(s)</p> <p>(g) Aurizon Network must undertake capacity assessments more frequently where the variations in the SOP have materially changed the relevant coal system's capacity</p> <p>(h) Our approval of the outputs of the subsequent capacity assessments (including recommendations from an expert-review process) would be subject to us having regard to the section 138(2) matters in the QCA Act. If we approve those outputs, that outcome will be binding on Aurizon Network and other stakeholders.</p> <p>(3) Our amendments are set out in clauses 7A.4.1 and 4.2 of our CDD amended DAU.</p>		
<p>(1) After considering the 2014 DAU's approach for Aurizon Network's management of capacity deficits, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is as follows:</p> <p>(a) Aurizon Network will use best endeavours to provide a capacity-deficit solution for access holders and seekers</p> <p>(b) Where a capacity deficit is revealed (i.e. committed capacity exceeds existing capacity), then Aurizon Network must provide a preliminary report to us within 20 business days that:</p> <p>(i) identifies the location and size of the capacity deficit</p>	<p>10.3</p>	<p><b>2(a) Disagree.</b> The provisions below adequately deal with deficit.</p> <p><b>2(b) Agree with amendments.</b> Aurizon Network will only be able to provide details to the extent known. Within 20 business days the preliminary views are likely to be high level and may not cover all elements included by the QCA.</p> <p><b>2(c) Agree with amendments.</b> (2)(c)(ii) is not consistent with introduction and should be deleted.</p> <p><b>2(d)(i) Agree with amendments.</b> Aurizon Network should seek to negotiate in good faith, not collaborate.</p> <p><b>2(d)(ii) Disagree.</b> Aurizon Network does not agree to allow the QCA to require Aurizon Network to fund an expansion through dispute resolution.</p> <p><b>2(d)(iii) Disagree.</b> Voting should only be required where triggered under Part 8 after the</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<ul style="list-style-type: none"> <li>(ii) identifies the access holders and seekers affected by the capacity deficit</li> <li>(iii) includes Aurizon Network's proposed plan for consulting with the affected access holders and seekers</li> <li>(iv) includes Aurizon Network's preliminary views (informed by, among other things, its participation in supply chain groups) on which of the following options can most efficiently resolve the capacity deficit               <ul style="list-style-type: none"> <li>o below-rail operational changes (e.g. SOP amendments)</li> <li>o capacity trading</li> <li>o non-below-rail supply-chain options</li> <li>o below-rail expansions</li> </ul> </li> <li>(v) is to be made publically available (subject to any reasonable confidentiality-related concerns).</li> </ul>		<p>final scope is identified. Expansions to overcome a deficit should be treated no differently.</p> <p><b>2(d)(iv) Disagree.</b> Whether or not Aurizon Network must proceed with an expansion should be determined under Part 8. Expansions to overcome a deficit should be treated no differently.</p>
<p>(c) If it is found that below-rail operational changes and/or below-rail expansions most efficiently resolve the deficit, then within six months of the capacity deficit being revealed, Aurizon Network must provide us with a report that:</p> <ul style="list-style-type: none"> <li>(i) identifies the preferred below-rail operational changes that can address the capacity deficit, including estimates of relevant costs (if any) to implement those changes</li> <li>(ii) where below-rail operational changes cannot resolve the deficit, provides evidence of Aurizon Network's consultation with stakeholders that explains why below-rail operational changes are unviable</li> <li>(iii) identifies a shortlist of the below-rail expansions explored, including estimates of costs to undertake those expansions</li> <li>(iv) identifies whether Aurizon Network and stakeholders have agreed on a specific below-rail</li> </ul>		<p><b>2(e) Agree.</b></p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>expansion to resolve the capacity deficit.</p> <p>(d) Where Aurizon Network and stakeholders agree on a below-rail expansion to resolve the capacity deficit, the following applies:</p> <p>(i) Aurizon Network must collaborate with affected access holders/seekers on the cost-sharing arrangements to apply to that expansion.</p> <p>(ii) If Aurizon Network and affected access holders/seekers are unable to agree on a cost-sharing arrangement, they can refer a proposed cost-sharing arrangement to us for a decision. For the avoidance of doubt, for a cost-sharing arrangement to be referred to us, both Aurizon Network and the affected access holders/seekers need to agree to refer that cost-sharing arrangement to us and agree to be bound by our decision on that arrangement.</p> <p>(iii) Following agreement of the cost-sharing arrangement (which may not transpire), Aurizon Network must seek endorsement of the proposed expansion via the customer-voting process in Schedule E.</p> <p>(iv) We would assess if that expansion is prudent and efficient in terms of standard, scope and cost. Aurizon Network will proceed with the expansion if we, acting reasonably, consider the expansion to be prudent and efficient.</p> <p>(e) Nothing in the provisions above affects or limits Aurizon Network's obligations or liabilities under any access agreement or other agreement.</p> <p>(3) Our amendments are set out in clause 7A.4.3 of our CDD amended DAU and Schedule E.</p>		
<p>(1) After considering the 2014 DAU's approach for Aurizon Network's information-provision obligations regarding the assumptions and methods</p>	<p>10.4</p>	<p><b>2(a) Agree.</b></p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
underpinning capacity assessments, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.		<b>2(b) Disagree.</b> Decision 10.2 (a)(i) adequately deals with consultation on the capacity assessments.
(2) The way in which we instead consider it appropriate for Aurizon Network to amend the 2014 DAU is as follows:		<b>2(c) Agree.</b>
(a) Aurizon Network should maintain SOPs at all times.		<b>2(d) Agree.</b>
(b) Aurizon Network should consult with all access holders, end customers and supply chain groups on all capacity and operating assumptions (i.e. SOPs and other parameters) that will underpin Aurizon Network's baseline capacity assessment and subsequent capacity assessments.		<b>2(e) Agree.</b>
(c) Aurizon Network's SOP amendment process must account for, among other things, expansion infrastructure being completed and new coal basins and port terminals being connected to its infrastructure.		<b>2(f) Agree with amendments.</b> If the QCA disagrees with Aurizon Network's SOPs, it may publish its own. Aurizon Network does not accept a right for the QCA to vary Aurizon Network's SOPs.
(d) Aurizon Network's SOP amendment process must account for, among other things, expansion infrastructure being completed and new coal basins and port terminals being connected to its infrastructure.		<b>2(g) Disagree.</b> Neither of these is relevant to the capacity assessment.
(e) Aurizon Network will review the SOPs for a coal system as soon as practicable after it becomes aware that a sustained change has occurred, or will occur, to the coal system that materially affects those SOPs.		<b>2(h) Agree.</b>
(f) Aurizon Network should respond to stakeholder submissions on the SOPs within 15 business days (or a later period, if we agree to such an extension).		
(g) The QCA can review or amend the SOPs if it undertakes its own baseline capacity assessment, and, in doing so, must have regard to the terms of access agreements and consider the impact those changes have on access holders.		
(h) Aurizon Network should include its track possession protocols and TSE calculation methodology in its baseline capacity assessment.		
(i) Aurizon Network should submit SOPs to us on an un-redacted basis, and publish the SOPs on its website in a way that is consistent with honouring confidentiality obligations it is unable to waive with third parties.		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(3) Our amendments are set out in clauses 7A4.1(b)(iv) and 7A.5 of our CDD amended DAU.		
(1) After considering the 2014 DAU's approach for Aurizon Network's NDP process, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.	10.5	<b>2(a) Disagree.</b> The objective of the NDP should be to identify the medium to long term capacity options to meet future demand for access in each coal system.
(2) We consider it appropriate for Aurizon Network to amend the 2014 DAU as follows:		<b>2(b) Agree with amendments.</b> Aurizon Network is prepared to agree with this subject to it being based on a static analysis only.
(a) The NDP's overarching objective should be to identify the medium-term capacity options that will meet future demand for access in each coal system and include options for developing or improving the operational performance, capacity and cost of throughput on the CQCN.		<b>2(c)(i) Disagree.</b> The NDP is developed using static, not dynamic, analysis. A five year horizon does not extend beyond the concept planning phase to the NDP period and should be longer. <b>2(c)(ii) Disagree.</b> This is an unreasonable level of prescription and may be imprudent in some circumstances.
(b) The NDP should identify the particular segments within each coal system that are capacity constrained.		<b>2(c)(iii) Agree.</b>  <b>2(d) Agree with amendments.</b> Aurizon Network is prepared to agree with this subject to the NDP assessment being based on static analysis, rather than the dynamic analysis undertaken for the capacity review.
(c) An NDP should provide all supply chain participants with:		
(i) a dynamic capacity review in a five-year planning horizon		<b>2(e) Agree.</b>
(ii) three growth scenarios within each coal system linking to a port optimisation project		<b>2(f) Agree.</b>
(iii) the scope, standard and preliminary costs of proposed expansion projects under investigation through funding agreements.		<b>2(g) Disagree.</b> It is not appropriate to have a regulatory review mechanism for a publication that does not have any implementable outcomes.
(d) The NDP need not necessarily be consistent with current SOPs, system rules and network management principles. However, Aurizon Network's flexibility in developing the NDP should be anchored to the range of capacity estimates (and assumptions where relevant) that Aurizon Network has provided as part of the approved baseline and subsequent capacity assessments.		<b>2(h) Agree.</b>  <b>2(i) Disagree.</b> Aurizon Network does not accept that the NDP should be subject to dispute resolution. If there is disagreement with an element of the NDP, this can be disputed when the scope of a study is determined under Part 8.
(e) The NDP review and update process should account for, among other things, expansion infrastructure being completed and new coal basins and port terminals		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
		being connected to Aurizon Network's infrastructure.
(f)		A draft NDP should be provided to all relevant supply chain participants who can then make submissions to Aurizon Network on the draft NDP.
(g)		The draft NDP can be peer reviewed if requested by access holders, access seekers and their customers.
(h)		Aurizon Network must take relevant supply chain participants' views into account in finalising the NDP.
(i)		Stakeholders who consider that Aurizon Network has inadequately addressed their views can refer the NDP to us for dispute resolution.
(3)		Our amendments are set out in clause 7A.6 of our CDD amended DAU.

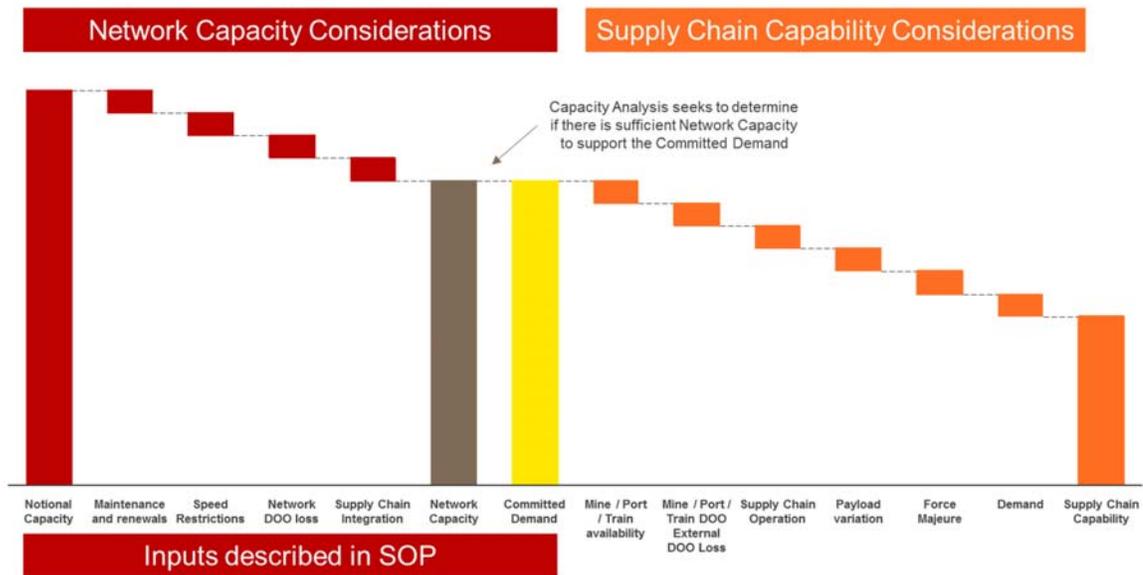
## Background to this Part 10 response

### Network capacity and supply chain capability

Capacity of the CQCN is a measure of the number of Train Service Entitlements (TSEs) that Aurizon Network can provide to access holders. In determining this capacity there are some factors that are considered within Aurizon Network's analysis - this is referred to as 'Network Capacity'. Aurizon Network measures its ability to service the Committed Capacity against Network Capacity.

The assessment does not consider supply chain capability constraints, as explained in the figure below.

Figure 10.1 - Network Capacity and supply chain capability



The definitions of key terms are provided below.

Table 10.2 – Capacity definitions

Definition	Meaning	Calculation
Nominal Capacity	<p>The maximum number of TSEs that could be provided subject to:</p> <ul style="list-style-type: none"> <li>No closure of the network for maintenance or renewal activities and no speed restrictions</li> <li>Sufficient origins and destinations to enable all paths to be utilised</li> <li>No delays or failures occurring in the below rail, above rail, mine and port systems</li> <li>Sufficient above rail assets.</li> </ul> <p>Essentially this is a theoretical, abstract measure of capacity, which is only used as a basis of calculation for static analysis.</p>	Static
Maintenance and renewals	Planned maintenance and renewals that lead to constraints being applied to the construction of a schedule.	Detailed maintenance and renewal program for dynamic modelling. Single Availability value used for the static model based on analysis of capacity unavailable due to planned maintenance and renewals.
Speed Restrictions	Speed restrictions applied to the network.	Detailed speed restriction program in the dynamic model. Part of utilisation factor applied in the static model.
Network DOO loss	Unplanned Network caused day of operation (DOO) events (i.e. signal or points failure).	DOO loss cancellations applied at start of each cycle.

Definition	Meaning	Calculation
		Part of utilisation factor applied in the static model.
Supply Chain Integration	Reflects the processes and procedures in the allocation of capacity (i.e. Schedule G and System Rules). Assesses the capacity of interfaces at mine and port to load and unload trains and the ability to schedule and operate trains to these locations.	The dynamic model has: <ul style="list-style-type: none"> <li>• demand management to reflect system rules</li> <li>• above rail fleets.</li> </ul> Part of utilisation factor applied in the static model.
Network Capacity	The capacity that Aurizon Network can provide to access holders based on access agreement requirements.	Static analysis provides an estimate of Network Capacity and if it meets the Committed Capacity.
Committed Demand	The demand that is required to be met for coal and non-coal services.	Dynamic analysis is used to determine if the Committed Demand can be achieved.
Mine / port / train availability	Losses associated with the (planned) time that mines/ports or rollingstock are not available for the movement of coal through the supply chain.	
External DOO loss	Losses associated with failures and other events outside of the control of Aurizon Network. This may include items such as load and unload time variation through to rollingstock failures.	
Supply Chain Operation	The mode of operation and how trains are ordered differ from the even railings basis by which network capacity is derived and can lead to losses.	
Payload variation	Changes to payload above and below the nominal payload affecting the throughput in tonnes (but not TSEs).	
Force Majeure	Losses associated with events that trigger network force majeure events.	
Demand	The changes in demand above and below the contracted demand.	
Supply Chain Capability	The capability of the supply chain, which can be observed as the actual throughput achieved.	

It is important to note that the availability and utilisation factors identified in network capacity relate to capacity impacting parameters, which are either enforced by Aurizon Network (maintenance and renewals program) or a consequence of a below rail issue (day of operation loss due to a signal failure).

The parameters identified under supply chain capability are a consequence of external factors to the network (i.e. operator or mine) and are factors over which Aurizon Network has no contractual control. These largely occur when an operator or customer does not perform to their contracted parameters. An example of this is when a mine loadout is slower than stipulated in an access agreement and it therefore takes longer to load a train, resulting in a lower number of trains able to be serviced than what is contracted.

Force Majeure is also excluded from the dynamic model as Aurizon Network is excused from meeting its contractual obligations under a declared state of Force Majeure, as per the access undertaking and access agreements.

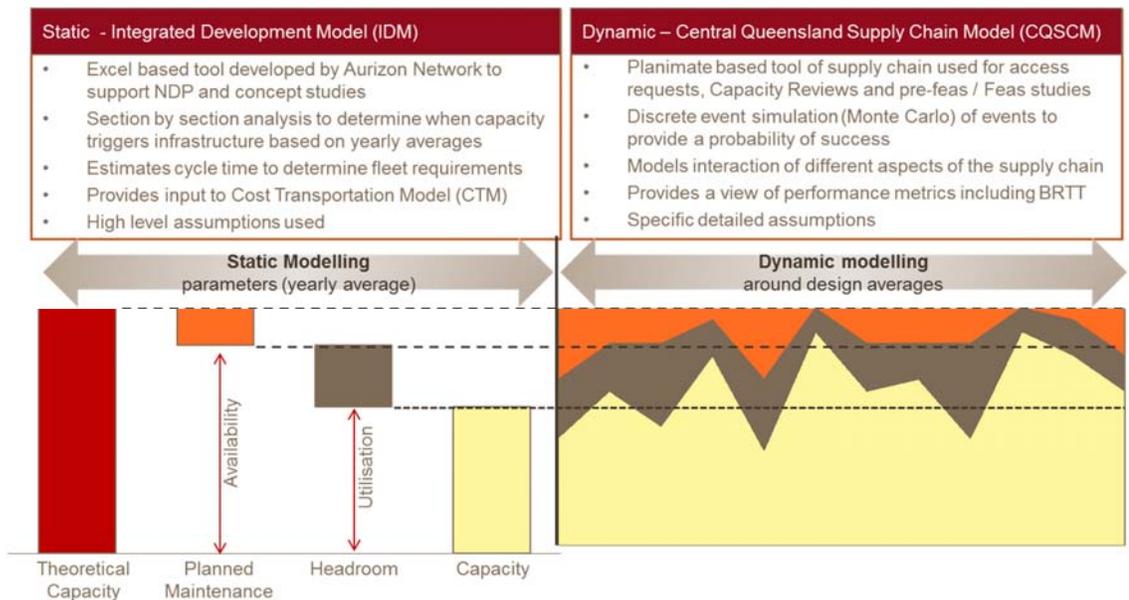
## Capacity Requirements

Aurizon Network provides capacity to its network in the form of TSEs for both timetabled and cyclic traffic. For cyclic traffic two TSEs are required to service a full cycle of depot to mine to port to depot. The tonnes transported is a function of payload and the number of TSEs. As Aurizon Network is not responsible for the payload of the service it measures capacity as a number of TSEs, not tonnes.

## Modelling Approach

Aurizon Network utilises static and dynamic modelling tools to determine if there is sufficient network capacity to meet the demand. This is illustrated below.

**Figure 10.2 – Static and dynamic models**



Dynamic modelling (or discrete event analysis) contains detailed representations of the CQCN and activities that are performed on it. The Central Queensland Supply Chain Model (CQSCM) has been under continual development by Aurizon Network over the past 15 years and provides significant detail of the entire rail network and the supply chain interfaces. The model provides an understanding of the response of the system resulting from the interaction between trains, the rail network and the supply chain boundaries at mines and ports. Variation is applied to input parameters where deemed appropriate and as detailed in the System Operating Parameters (SOP) document.

Static analysis uses an average availability and utilisation, which have been derived from a review of the outputs of the dynamic simulation.

The use of each of these approaches is broadly dependent on the following factors:

- **Confidence of input parameters**

Where there is sufficient confidence and availability of the input parameters, dynamic analysis will be the preferred approach.

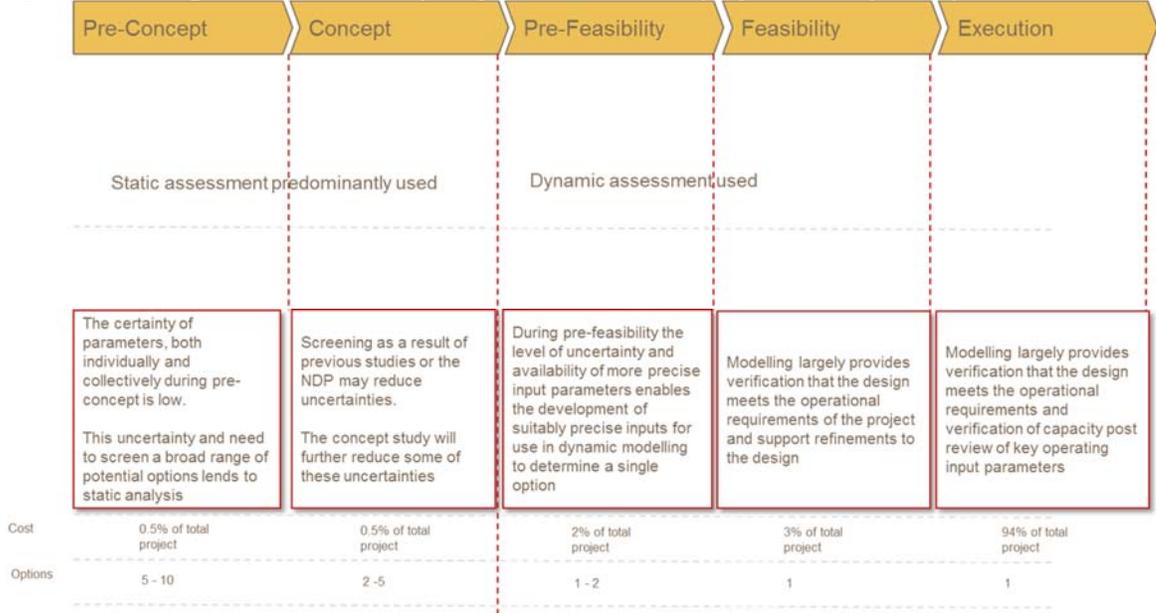
- **Range of analysis**

Where there are a range of scenarios with significantly different inputs, static analysis will be used as an initial review to identify which options have merit to take forward.

- **Design stage**

Aurizon Network seeks to align the level of analysis undertaken with the level of design undertaken. Where limited engineering design has been undertaken (pre-concept and concept stages), static analysis is typically undertaken to identify the scope of the engineering requirements. Where more detailed engineering has been undertaken this design information can be used to provide more detailed inputs for the dynamic model. This is shown in the figure below.

**Figure 10.3 – Alignment between capacity assessment and project development phases**



### System Operating Parameters

The SOP are published by Aurizon Network and contain a full description of all parameters that are used in the dynamic model to determine if there is sufficient Network Capacity to meet the Committed Demand. These input parameters are largely based on how Aurizon Network manages its network (asset management) and how it manages and provides capacity (access agreements and Network Management Principles (NMP)).

As highlighted in the description of Network Capacity provided previously, it can be seen that the majority of information contained within the SOP is defined by commercial agreements and internal standards and processes:

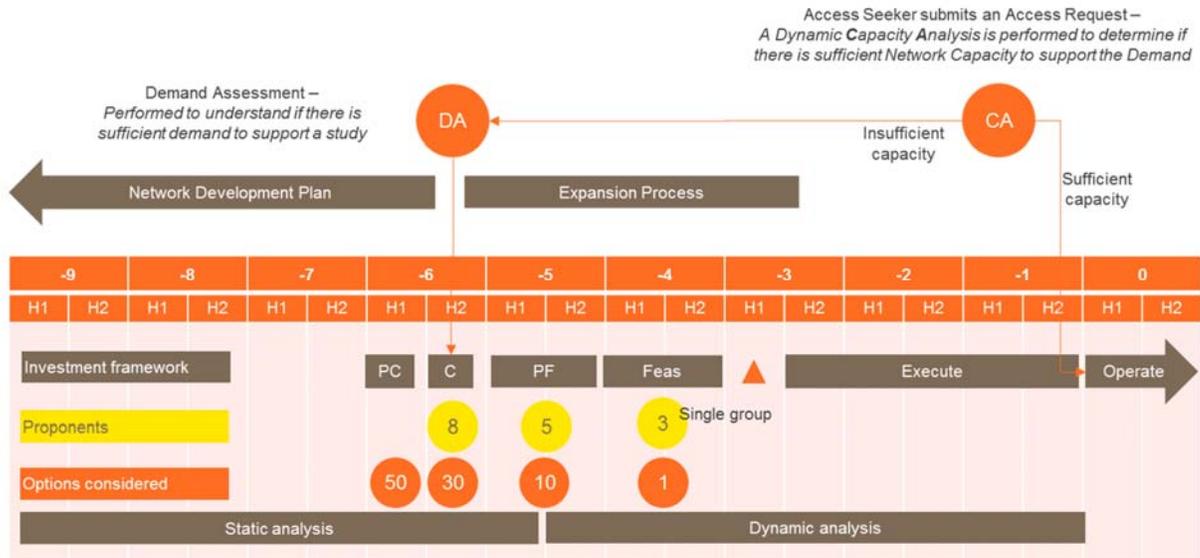
- Demand and capacity management: access agreements and access undertaking (including the NMP);
- Asset management: network processes;
- Network operation: network standards and processes, including the NMP;
- Train Operation: access agreements and operating plans. This area of the SOP will be largely redacted as it contains confidential information relating to access holders.

The Train Control Principles in Part B of Schedule G in the 2010 AU (clause (c)(ii)) include a requirement that: “Train Operators will ensure that Above Rail issues, including Train crewing, locomotive and wagon availability and loading and unloading requirements, are appropriately managed to ensure that such issues do not prevent the DTP from being met”. Operators are responsible for their own on-time performance. As a result of this provision, the SOP and capacity model reflect the operators’ contracted parameters without variation, as Aurizon Network has no control over these parameters.

## Access and development timelines

The time taken to develop a project and the number of scenarios considered is a key driver to the content and approach taken to the Network Development Plan (NDP), as shown in the figure below.

Figure 10.4 – Development timelines



The key processes referenced above include:

*Access seeker submits an access request:* Initially an access seeker will provide a Conceptual Operating Plan to Aurizon Network, who will then undertake a capacity analysis using the dynamic model. If there is sufficient network capacity to support the demand, an Indicative Access Proposal is issued confirming this capacity. The negotiation of an access agreement can then commence.

*Demand Assessment:* A demand assessment is undertaken to assess if there is sufficient demand for additional capacity to require a study to be undertaken. If there is sufficient demand, Aurizon Network will undertake a concept study (unless previously undertaken).

*Expansion Process:* If there is a requirement for a pre-feasibility (and further) study/ies to be undertaken, the relevant access seeker/s will enter into a funding agreement. Aurizon Network will perform the study/ies. Typically the study time periods for significant supply chain enhancements (such as GAPE or WIRP) are:

- Pre-feasibility: six to twelve months followed by a negotiation period of three months to enter into Feasibility;
- Feasibility: six to twelve months followed by a negotiation period of six months to enter into Execution; and
- Execution: two to three years.

Essentially the expansion process will take approximately five years from the commencement of the pre-feasibility study to commissioning. The NDP examines a longer term horizon so that it can provide guidance and input into the concept studies.

## CDD 10.1 Supply chain co-ordination

Aurizon Network disagrees with CDD 10.1. Aurizon Network's reasons for this are set out in section 10.3 of its response to the QCA's IDD<sup>47</sup> and Aurizon Network incorporates by reference the cited text into this submission.

In addition the CDD includes a new decision (10.1(2)(b)), which requires Aurizon Network to implement actionable items of the supply chain group. The QCA has no power to require Aurizon to make any binding commitment or take any action as a result of its voluntary participation in supply chain groups. Aurizon Network reserves its right to consider all matters on a case by case basis and determine what actions and commitments it is prepared to make at its own discretion.

In addition to being beyond power, the obligation to implement actionable items from any supply chain group is highly undesirable for reasons including:

- there may be safety implications and should only be implemented where the party accountable for safety (i.e. Aurizon Network) agrees;
- the costs may not be recoverable through the approved MAR;
- the supply chain group may lack the technical or operational expertise to assess the impacts of any changes;
- the changes may conflict with, or put Aurizon Network in breach of, access agreements or other commercial agreements;
- multiple supply chain groups may seek actionable items to be implemented that are in direct conflict; and
- generally, it is unreasonable to allow a third party (who may have limited information and/or conflicting commercial objectives) to develop actionable items and require implementation when it is not in any way accountable for the consequences of such actions.

## CDD 10.2 Capacity analysis

Aurizon Network agrees with the philosophy of improving transparency and consultation in undertaking its capacity analysis and recognises its importance to stakeholders. However, Aurizon Network considers that the current drafting does not reflect the processes and intended outcomes of the capacity analysis. It is therefore submitted that amendments are required as described below.

Section 10.4 of Aurizon Network's response to the QCA's IDD<sup>48</sup> sets out a range of concerns it has with the QCA's position and Aurizon Network incorporates this response by reference in this submission.

### Capacity definitions

The QCA has added definitions related to capacity. These are addressed below.

#### Absolute Capacity

Absolute Capacity is a theoretical construct derived by excluding the necessary activities that are required for the ongoing safe operation of a railway network. It is a measure that does not have any practical implications. Aurizon Network does not understand how it can provide any useful information for

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<sup>47</sup> Aurizon Network (2015a). pp.125-128.

<sup>48</sup> Aurizon Network (2015a). pp.126-128.

stakeholders and in fact would potentially mislead stakeholders into believing there is surplus capacity available. This definition and concept should be deleted. Whilst Aurizon Network does measure nominal capacity as a part of static analysis there is no equivalent measure in dynamic analysis used to perform the baseline and annual capacity assessments.

#### Available Capacity

Available Capacity is a measure of the amount of capacity remaining once capacity required for Committed Capacity is utilised. This is not an outcome that is achieved through the use of the dynamic capacity assessment that Aurizon Network performs. A dynamic simulation is operated to address the question of whether there is sufficient capacity to support the committed capacity. The analysis does not solve for additional demand.

This analysis would only be able to be applied if additional demand scenario(s) were assumed. These could be undertaken through:

- examination of a range of demand scenarios;
- a pro rate increase in demand on all existing contracts.

Aurizon Network does not consider either of the above options are of value.

The use of a range of demand scenarios would create significant workload. When Aurizon Network undertakes capacity analysis using the CQSCM dynamic model it simulates each month individually. It then simulates each month for a number of input 'seeds' (typically 10+), with each seed generating the random numbers that are used to drive the dynamic nature of the simulation, resulting in over 120 scenarios per year. If Aurizon Network was to undertake a range of demand scenarios, the modelling workload could increase by an order of magnitude for no benefit.

The application of a scenario involving a pro rata increase in demand on all existing contracts would provide limited benefit due to the ability to meet that demand being limited by a particular mine–port combination, potentially due to one of the following constraints: balloon loop capacity; port capacity; network capacity; and/or above rail operation. It is unlikely that the particular constraint that limits the available capacity determined through this method would be applicable to a specific mine-port combination that an access seeker is considering. Furthermore, it would not be able to be relied on by access seekers.

Aurizon Network proposes that the static analysis performed within the NDP is used as a means of indicatively identifying the Available Capacity. This provides prospective access seekers with an overview of the likely locations where capacity is constrained. If and when an access seeker wants to understand the implications of a demand change, this can be undertaken in more detail through an access request. This will enable resources to be prioritised in responding to specific demand scenarios rather than undertaking detailed analysis on a range of 'what if' scenarios.

Available Capacity should not be identified in the baseline or annual capacity analysis.

#### Baseline Capacity

This definition not required.

#### Capacity

This definition is appropriate.

### Committed Capacity

This definition is appropriate.

### Existing Capacity

This is referred to as Network Capacity in all discussions Aurizon Network holds with stakeholders and it is proposed to change this in the undertaking. The current definition in the CDD amended DAU is circular having regard to the definitions of Capacity, Available Capacity and Planned Capacity. This should be redefined to be the existing capability (at a point in time) of the Railway Infrastructure to accommodate Train Services.

### Planned Capacity

This definition is appropriate

## **Reliance on capacity outputs**

CDD 10.2(2)(b) provides that access holders can rely upon the baseline capacity outputs to validate Aurizon Network's compliance with their access agreements. This is incorrect and misleading. The QCA has no power or right to involve itself in any contractual matter between Aurizon Network and access holders.

No undertaking process should have any relevance to an access agreement unless Aurizon Network and each relevant access holder volunteers to allow that process to be reflected in that agreement. Whether or not Aurizon Network complies with a commercial contract with an access holder is a matter for the two parties and should be judged on the face of the agreement and the circumstances of performance under that agreement.

## **Non-approval of capacity assessments**

Aurizon Network is of the view the following structure would best suit capacity assessments:

- Where Aurizon Network has undertaken a capacity assessment and the QCA has concerns with the outputs of that process, the QCA may engage an expert to review the capacity in accordance with the Capacity Review Terms of Reference set out in section 10.4.2 of Aurizon Network's response to the QCA's IDD<sup>499</sup>. This engagement should cover:
  - advice on whether or not to approve Aurizon Network's capacity assessment; and
  - when that assessment is not approved by the QCA, assistance in development of the QCA's capacity assessment.
- Aurizon Network should not be required to endorse the QCA's capacity assessment and publish it as a 'correct' assessment of capacity. Rather the QCA should publish the assessments completed by both Aurizon Network and itself. Aurizon Network agrees that it is the QCA's assessment that will be used to trigger any consideration of a Capacity Deficit.
- There is no requirement for the QCA's approval of Aurizon Network's capacity assessment or the QCA's development of the QCA's own capacity assessment to be binding and Aurizon Network does not agree to be bound by the QCA's decision.

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<sup>499</sup> Aurizon Network (2015a). pp.126-127.

Aurizon Network agrees to this baseline and annual capacity assessment to provide greater transparency to stakeholders. It is not an “active” capacity assessment as it is not required to manage the activities of negotiating access rights. Active capacity assessments occur:

- under Part 4 where it is assessed whether there is sufficient available capacity to satisfy an access request; and
- under Part 8 where the scope of expansion projects are being determined and where Capacity Shortfall is being considered.

In these active capacity assessments the assessment is subject to dispute resolution. In Aurizon Network’s view such dispute resolution must be conducted in accordance with the Capacity Review Terms of Reference set out in section 10.4.2 of Aurizon Network’s response to the QCA’s IDD. Where that is the case Aurizon Network agrees to be bound to the outcome of those capacity assessment disputes.

## CDD 10.3 Capacity deficit

Whilst the baseline and annual capacity assessments are not ‘active’ capacity assessments (like those undertaken in Part 4 and Part 8 to deal with questions of capacity associated with access requests and expansions), Aurizon Network agrees there is merit in considering options to overcome the deficit and where agreed, implementing the preferred option.

In practice the current NDP and any pre-concept and concept studies completed generically on the coal systems will provide guidance as to the options to create additional capacity. If any capacity assessment identifies that the existing capacity is insufficient to accommodate the committed capacity the report may not provide all of the detail the QCA has required in CDD 10.3(2)(b). This is particularly the case where Aurizon Network’s capacity assessment concludes that there is no deficit, but the QCA’s capacity assessment identifies a deficit. Therefore Aurizon Network should only be obliged to provide details to the extent known.

Section 10.5 of Aurizon Network’s response to the QCA’s IDD<sup>50</sup> sets out a range of issues around the identification of options for capacity creation and rectification of any deficit and Aurizon Network incorporates by reference the cited text in this submission. The CDD includes a mechanism to allow for the failure to agree the funding of an expansion to overcome a deficit to be disputed under the undertaking where agreed. Aurizon Network does not agree to any circumstance where the QCA can require Aurizon Network to fund expansions, even through dispute resolution. Accordingly this mechanism should be deleted as it is beyond the QCA’s power and Aurizon Network does not volunteer to accept it.

## CDD 10.4 System Operating Parameters

Aurizon Network agrees with the QCA’s general philosophy of improving transparency and consultation in relation to the SOP. Aurizon Network’s position is that the proposed drafting regarding their content is confusing, repetitive and in places circular<sup>51</sup>.

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<sup>50</sup> Aurizon Network (2015a). pp.128-130.

<sup>51</sup> Clause 7A.4.1(b)(iv)(A)(1) of the CDD amended DAU states that the Baseline Capacity Assessment report must include assumptions including the System Operating Parameters, whereas clause 7A.5(b)(i) states that the SOP must include assumptions relied upon in the Baseline Capacity Assessment.

As described above, the SOP is the single document that describes all of the input parameters and how they are applied in the CQSCM for the purposes of capacity analysis. It is the sole basis by which capacity reviews are undertaken. By having a single source of information for a capacity analysis, transparency is improved for stakeholders in the supply chain. The contents of the SOP are largely based on how Aurizon Network manages its network (asset management) and how it manages and provides capacity (access agreements and the NMP).

Aurizon Network agrees to the adoption of a review and amendment process, provided that the process cannot require a change to any of the values that have been derived from access agreements and other applicable coal system agreements. To the extent that any of Aurizon Network's processes reflect regulatory requirements and agreements (for example the NMP and System Rules), these processes should not be able to be changed as a consequence of this review and amendment process.

If the QCA disagrees with Aurizon Network's SOP, the QCA should publish its own SOP alongside Aurizon Network's SOP. It should not be able to vary Aurizon Network's SOP. Aurizon Network does not agree to the QCA's opinion presented as Aurizon Network's opinion when Aurizon Network believes it to be incorrect. Aurizon Network agrees that the QCA can use its SOP for its own capacity assessments. Any QCA SOP should comply with the values derived from access agreements, regulatory requirements and agreements as well as reflect the way the network is currently operated.

Aurizon Network agrees that it should incorporate description, where relevant of how processes are implemented in the SOP. Aurizon Network proposes to describe implementation of the System Rules and NMP within the SOP.

Finally, track possession protocols refer to the short term implementation of works on the network and are not relevant to the SOP. Furthermore, the TSE calculation methodology is not relevant to the determination of whether there is sufficient network capacity. These particular requirements should be deleted.

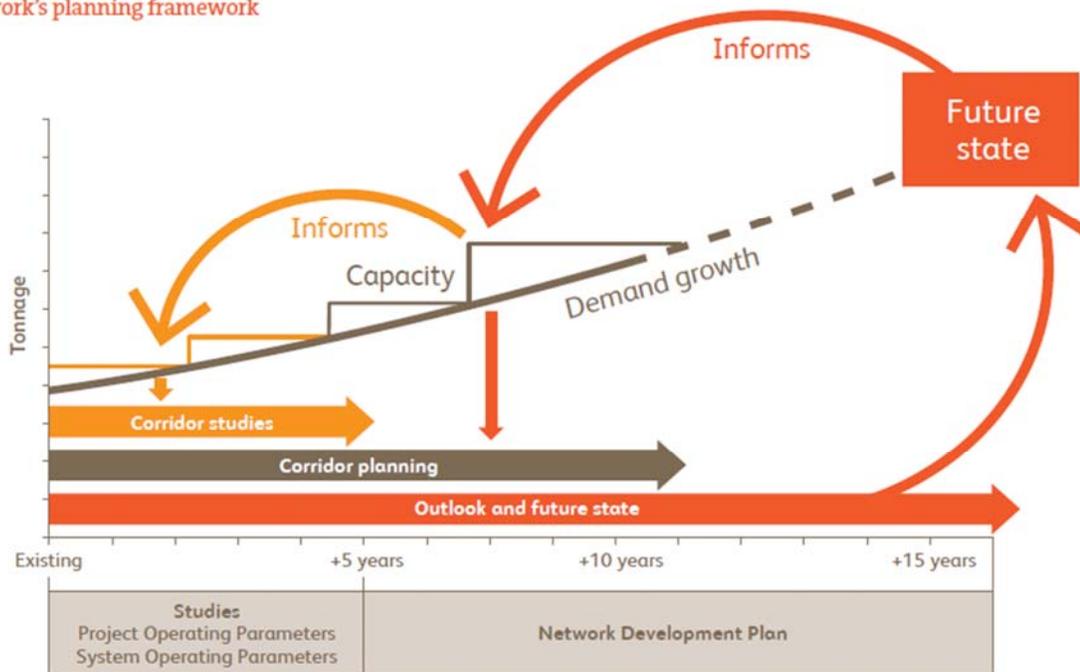
## CDD 10.5 Network Development Plan

The intent of the NDP is to create a pre-concept baseline for the long term (ten to fifteen year) horizon, which will help guide smaller incremental studies when they are initiated. By providing a medium to long term view of potential development pathways, the NDP provides guidance to incremental expansions that occur in the shorter term and are managed through the expansion process. Once Aurizon Network commits to an expansion and the associated access rights, these are reflected within the SOP and capacity review process.

Aurizon Network's planning framework is summarised in the following figure.

**Figure 10.5 – Planning framework**

**Network's planning framework**



As noted in the Access and development timelines section above, Aurizon Network considers that setting a five year horizon for the NDP will limit its effectiveness in identifying opportunities to optimise supply chain efficiencies as a consequence of future significant port and mine expansions.

On this basis it is difficult to envisage a new port expansion requiring an extra berth within the five year timeframe specified by the QCA that is not already a part of the expansion process. Any significant change to the network design or operation within a five year period would be in the expansion process and would be incorporated within the NDP as a 'base case' scenario.

The NDP should not include analysis to evaluate opportunities to improve operational performance and cost of transportation (outside of an increase in capacity). The NDP contains a static analysis of capacity, identifying the constraining sections in each coal system. As described above, it is not appropriate to undertake dynamic modelling on a wide range of scenarios where there is insufficient confidence in the inputs to warrant that level of study. Moreover, dynamic modelling requires substantial resources and imposes costs that are not currently reflected in the MAR allowance, as detailed in the response to CDD 20.1.

As described in the Modelling Approach section it is important to match the detail of the analysis undertaken with the criteria by which Aurizon Network identifies the most appropriate approach to use. These criteria include, but are not limited to: confidence in the input parameters; the level of engineering design undertaken; and the range of scenarios being considered. For this reason Aurizon Network considers that the most appropriate approach is to utilise static modelling to identify the probable

requirements for each scenario. It notes that ARTC uses a static approach when undertaking the ten year Hunter Valley Strategy<sup>52</sup>.

Aurizon Network therefore disagrees with the QCA position in the CDD on the basis that there is no requirement for such a level of prescription on the scenarios to be considered within the NDP. The requirements may differ significantly by corridor and Aurizon Network believes that the NDP should have the flexibility to assess the range of scenarios that it considers likely. In some corridors this could be more than three scenarios (if there is a number of potential new/expanded mines and expansions of ports). In other corridors, there may be less than three scenarios, particularly if there are port constraints.

The NDP should be based on a consultative approach where Aurizon Network, in conjunction with port owners and operators, identifies appropriate scenarios to consider. Aurizon Network supports the position that the NDP should include the outcomes of studies it has undertaken.

Having regard to Aurizon Network's position on the use of dynamic and static analysis as outlined above, it notes that the input parameters used for different analysis techniques will be different. Notwithstanding this, the input parameters used in the static analysis performed within the NDP (and as part of the concept and pre-feasibility stages of project development) are intended to align with the dynamic parameters. The NDP will take the existing configuration as described in the relevant SOP as the basis for the NDP analysis.

Aurizon Network does not believe that it is a reasonable assumption for mine owners (and third party financiers) to make investment decisions on a series of scenarios within the NDP that may or may not come to fruition. To establish the viability of a mine the owner would need to understand all of the costs of transportation, which is done by entering negotiations with potential suppliers. With Aurizon Network this commences with an access request and entering into the expansion process where required.

Finally, it is not appropriate to include a peer review process for the NDP given its purpose is to provide an indication of capacity expansion options to be considered as a part of the study process. None of the elements of the NDP is an implementable outcome. If there is disagreement with an element of the NDP, this can be disputed when the scope of a study is determined. It is also important to have regard to the non-binding nature of the NDP, as well as the alternative processes available for access seekers to obtain information about network expansions (including access requests).

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<sup>52</sup> <http://www.artc.com.au/projects/hv-strategy/>

## Chapter 11 – Available Capacity Allocation and Management (Part 7)

### Summary of Aurizon Network's Position

#### **Reinstatement of the queue and capacity notification register**

Aurizon Network is disappointed with the QCA's decision to reinstate the queue and capacity notification register. It considers reinstatement of the queue is only appropriate if the 2010AU provisions, which enabled Aurizon Network to re-order the queue (see clauses 7.3.4(c) to (k) of the 2010AU) in specified circumstances (including to give preference to longer term contracts), are reinstated. In addition it considers the requirement for written consent from access seekers higher in the queue prior to Aurizon Network contracting with access seekers lower in the queue are unworkable and likely to result in anti-competitive gaming.

#### **Renewals on terms of current SAA**

Aurizon Network is concerned that the QCA appears to have inadvertently introduced provision which mean renewing access holder must contract on the same terms as their expiring access agreement. Consistent with the position of the QRC in its submission on the IDD, Aurizon Network considers a renewing access holder should, subject to any agreement to the contrary, contract on the terms

#### **Short term transfers**

The introduction of a short term capacity transfer mechanism has been one of Aurizon Network's key priorities for UT4, in response to its customers requiring more flexibility in the way in which they manage their access rights. This is particularly imperative in the current market environment, where all parties need an appropriate degree of flexibility to manage their commercial risks and where possible, reduce costs. The mechanism included in Aurizon Network's 2014DAU was developed in consultation with the QRC, and rail operators (Aurizon Operations, Pacific National and BMA). Aurizon Network has made a number of submissions on this topic since the initial lodgement of its 2013DAU, which are incorporated in this response (where indicated) by way of reference.

Aurizon Network has fundamental concerns with the QCA making substantive amendments to a framework that it developed in consultation with the industry. Putting those concerns aside, there are a number of aspects of the QCA's framework that are inefficient and/or unworkable. Aurizon Network has proposed amendments to address these issues and would be happy to work with the QCA in its finalisation of the 2014DAU to arrive at a workable and effective framework that meets the needs of all stakeholders.

In respect of other transfers, relinquishments and resumptions, Aurizon Network has a number of concerns around practicality, clarity and drafting, which are addressed below.

#### **Proposed redrafting of Part 7**

To assist the QCA in reaching its Final Decision, Aurizon Network has provided in Volume 3 a marked up version of the QCA's Part 7 (excluding those parts relating to decisions 11.1, 11.2, 11.4, 11.5, 11.18), which it proposed forms part of the "Incorporated Provisions" in the Standard Access Agreement. Aurizon Network has also addressed these matters in our redrafted Standard Access Agreement (Vol 3). An explanation of our approach to "Incorporated Provisions" is provided in Chapter 8 of this submission.

**Table 11.1 – QCA Consolidated Draft Decision**

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(1) After considering Aurizon Network's proposed capacity allocation criteria our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking in the manner proposed in clauses 7.2 and 7.5 of the CDD amended DAU by replacing its criteria based allocation process with a queue process.</p>	<p>11.1</p>	<p><b>Disagree.</b> While Aurizon Network is prepared to accept the re-instatement of the queue, the only circumstances under which Aurizon Network would agree to this is where the 2010AU capacity allocation provisions are re-inserted(cl7.3.4(c) to (k)), including Aurizon Network's ability to re-order the queue to prefer longer term contracts.</p>
<p>(1) After considering Aurizon Network's proposed removal of the capacity notification register and the committed capacity register our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking by reinserting the capacity registers, in the manner proposed in clause 7.2 of the CDD amended DAU.</p>	<p>11.2</p>	<p><b>Agree with amendments.</b> While Aurizon Network is willing to agree to the re-instatement of the committed capacity register and committed capacity register, it requires reinsertion of relevant provisions from the 2010AU.</p>
<p>(1) After considering Aurizon Network's proposed treatment of force majeure as drafted in the Standard Access Agreements our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking by reinserting the force majeure provisions into the access undertaking in the manner proposed in clause 7.7 of the CDD amended DAU.</p>	<p>11.3</p>	<p>Refer to Aurizon Network's response in relation to access agreements (refer Vol 1, Chapter 8 and Vol 3).</p>
<p>(1) After considering Aurizon Network's proposed provisions in respect of treatment of renewal applications our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking to reinstate the provisions from UT3 in the manner proposed in clause 7.3 of the CDD amended DAU.</p>	<p>11.4</p>	<p><b>Disagree.</b> Aurizon Network's main concern is the clause 7.3(h) of the CDD amended DAU. Renewals should be on the terms of the SAA in force at the time of that renewal.</p>
<p>(1) After considering Aurizon Network's proposed amendment to the replacement mine concept our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access</p>	<p>11.5</p>	<p><b>Agree.</b> While unclear from the CDD itself, the CDD amended DAU appears to accept the substance of Aurizon Network's substitute replacement mine concept. Aurizon Network is therefore prepared to accept this on the basis that the drafting in the CDD amended DAU remains in place.</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
undertaking by reinserting provisions relating to the replacement mine concept from UT3, in the manner proposed in our CDD amended DAU.		
<p>(1) Our consolidated draft decision is to refuse to approve Aurizon Network's proposed amendments to remove the transfer and relinquishment fees provisions from the undertaking.</p> <p>(2) We consider it appropriate that Aurizon Network amend its 2014 DAU by reinserting the provisions dealing with fees into the 2014 DAU, in the manner proposed in clause 7.4 of the CDD amended DAU and also in a manner consistent with our consolidated draft decisions 11.7 and 11.8.</p> <p>(3) We consider it appropriate to make these decisions having regard to each of the matters set out in section 138(2) of the QCA Act for the reasons set out in this section.</p>	11.6	Refer to Aurizon Network's response in relation to access agreements (refer Vol 1, Chapter 8 and Vol 3).
<p>(1) After considering Aurizon Network's proposal in regards to its calculation of transfer and relinquishment fees our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its 2014 DAU with respect to the calculation of transfer and relinquishment fees to include a process where Aurizon Network provides an access holder with information detailing:</p> <p>(m) how it calculated the relinquishment fee, and how that meets with the relevant provisions of the access undertaking</p> <p>(n) all assumptions used in the calculation and why those assumptions are reasonable assumptions to make.</p>	11.7	<b>Agree with amendments.</b>
<p>(1) After considering Aurizon Network's proposed change to the provisions relating to customer initiated transfers our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking by reinstating provisions relating to customer initiated transfers in</p>	11.8	<b>Agree with amendments.</b>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
the 2014 DAU as proposed in clause 7.4 of the CDD amended DAU.		
<p>(1) After considering Aurizon Network's short-term capacity transfer mechanism our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking in a manner consistent with our CDD amended DAU and our consolidated draft decisions 11.10, 11.11, 11.12, 11.13, 11.14, 11.15 and 11.16 below.</p>	11.9	<b>Disagree.</b> Refer to Aurizon Network's Response to QCA Supplementary Draft Decision on 2014 Draft Access Undertaking – Capacity Transfer Mechanism, 29 May 2015 and additional information provided below.
<p>(1) After considering Aurizon Network's short-term capacity transfer mechanism, our consolidated draft decision is to approve Aurizon Network's proposal in relation to a zero transfer fee for short-term transfers.</p>	11.10	<b>Disagree.</b> Refer to Aurizon Network's Response to QCA Supplementary Draft Decision on 2014 Draft Access Undertaking – Capacity Transfer Mechanism, 29 May 2015 and Stakeholder notice - short term transfer mechanism, 30 September 2015 and information provided below.
<p>(1) After considering Aurizon Network's short-term capacity transfer mechanism our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking in a manner consistent with clause 7.4 of our CDD amended DAU so that:</p> <p>(a) access holders can permanently transfer 'as of right' if the transfer meets access criteria A:</p> <p>(i) transferred TSEs utilise the same mainline path</p> <p>(ii) transferred TSEs exit at the same destination on the mainline path</p> <p>(iii) transferee does not require additional access rights to complete the train path from the transferee's origin</p> <p>(iv) transferee can confirm a rail operator will operate the transferred capacity</p> <p>(v) transferee must confirm it has supply chain rights for the transferred access rights</p> <p>(b) transfers are short-term transfers if the following additional access criteria are met:</p> <p>(i) transferred TSEs must not be held by the transferee for</p>	11.11	<b>Disagree.</b> Refer to Aurizon Network's Response to QCA Supplementary Draft Decision on 2014 Draft Access Undertaking – Capacity Transfer Mechanism, 29 May 2015 (Decisions 3.1, 3.3 and 3.5) and Stakeholder notice - short term transfer mechanism, 30 September 2015.

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>a period longer than three months</p> <p>(ii) transferred TSEs are for use by coal-carrying services</p> <p>(iii) the same reference tariff must apply to both the transferor and transferee's access charge.</p>		
<p>(1) After considering Aurizon Network's short-term capacity transfer mechanism our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking in a manner consistent with clause 7.4 of our CDD amended DAU so that:</p> <p>(a) access criteria B differ from access criteria A in the following way: transferred TSEs use the same mainline path as the transferor, ancillary access rights required at the point of origin and/or at the destination port precinct are to be identified and subject to capacity assessment</p> <p>(b) Aurizon Network will undertake a rapid capacity assessment on transfer notices which meet access criteria B</p> <p>(c) Aurizon Network will refuse an access criteria B transfer request if the rapid capacity assessment shows that existing access holders' access to the network will be adversely affected by the transfer</p> <p>(d) transfers are short-term transfers if the following additional access criteria are met:</p> <p>(i) transferred TSEs must not be held by the transferee for a period longer than three months</p> <p>(ii) transferred TSEs are for use by coal-carrying services</p> <p>(iii) the same reference tariff must apply to both the transferor and transferee's access charge.</p>	<p>11.12</p>	<p><b>Disagree.</b> Refer to Aurizon Network's Response to QCA Supplementary Draft Decision on 2014 Draft Access Undertaking – Capacity Transfer Mechanism, 29 May 2015 (Decisions 3.1, 3.4 and 3.5) and Stakeholder notice - short term transfer mechanism, 30 September 2015.</p>
<p>(1) After considering Aurizon Network's short-term capacity transfer mechanism our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p>	<p>11.13</p>	<p><b>Disagree.</b> Refer to Aurizon Network's Response to QCA Supplementary Draft Decision on 2014 Draft Access Undertaking – Capacity Transfer Mechanism, 29 May 2015 and Stakeholder notice - short term transfer mechanism, 30</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking in a manner consistent with clause 7.4 of our CDD amended DAU so that criteria C transfers are short-term transfers if the following additional access criteria are met:</p> <ul style="list-style-type: none"> <li>(a) transferred TSEs must not be held by the transferee for a period longer than three months</li> <li>(b) transferred TSEs are for use by coal-carrying services</li> <li>(c) the same reference tariff must apply to both the transferor and transferee's access charge.</li> </ul>		<p>September 2015 and additional information provided below.</p> <p>Stakeholder notice response specifically addressed time period of proposed short term transfers, and QCA's rationale under UT3 to allow up to 2 years.</p>
<p>(1) After considering Aurizon Network's short-term capacity transfer mechanism our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p>	11.14	<p><b>Disagree.</b> Refer to Aurizon Network's Response to QCA Supplementary Draft Decision on 2014 Draft Access Undertaking – Capacity Transfer Mechanism, 29 May 2015 and additional information provided below.</p>
<p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking in a manner consistent with clause 7.4 of our CDD amended DAU so that:</p> <ul style="list-style-type: none"> <li>(a) all transfer notices must be lodged with Aurizon Network not fewer than 48 hours prior to the transfer date</li> <li>(b) Aurizon Network must respond to the transfer notice not more than two business days after the transfer notice is lodged and <ul style="list-style-type: none"> <li>(i) schedule transfers under access criteria A</li> <li>(ii) either advise access criteria B transfers that a rapid capacity assessment is required, or</li> <li>(iii) advise access criteria B transfers that a detailed capacity assessment is required and outline the scope and timing before a response to the notice can be provided</li> </ul> </li> <li>(c) where Aurizon Network has to undertake a rapid capacity assessment to respond to a transfer notice, Aurizon Network must approve or refuse the transfer within four business days of the notice being lodged</li> <li>(d) the information that should be included in an Aurizon Network transfer response contains</li> </ul>		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<ul style="list-style-type: none"> <li>(i) the result of the capacity assessment</li> <li>(ii) an indication of whether the transfer can be approved or refused</li> <li>(iii) reasons for refusing the transfer request.</li> </ul>		
<p>(1) After considering Aurizon Network's short-term capacity transfer mechanism our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking in a manner consistent with clause 7.4 of our CDD amended DAU so that:</p> <ul style="list-style-type: none"> <li>(a) Aurizon Network will keep a register of all transfer notices, its responses and the timeframes taken to respond (cl. 10.5.2(e))</li> <li>(b) Aurizon Network will provide a quarterly update of the transfer register to the QCA as part of its regulatory reporting obligations under the 2014 DAU</li> <li>(c) Aurizon Network will annually review, in consultation with stakeholders, the transfer provisions in the undertaking and submit the results of the annual review, and any proposed amendments to the transfer provisions in the undertaking, to the QCA for approval.</li> </ul>	11.15	<b>Agree with amendments.</b>
<p>(1) After considering Aurizon Network's short-term capacity transfer mechanism our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend its draft access undertaking in a manner consistent with clause 7.4 of our CDD amended DAU and the SAA so that:</p> <ul style="list-style-type: none"> <li>(a) clause 7.4 is amended to include specified access criteria, timeframes and governance processes in which Aurizon Network should administer transfers</li> <li>(b) if agreed by both parties, Aurizon Network will amend existing access agreements to incorporate the new transfer provisions</li> </ul>	11.16	<b>Agree with amendments.</b>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(c) the SAA is amended to permit Aurizon Network to address any increased or decreased credit risk arising from a transfer.		
(1) After considering Aurizon Network's proposed resumption provisions, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.	11.17	Refer to Aurizon Network's response in relation to access agreements (refer Vol 1, Chapter 8 and Vol 3).
(2) The way in which we consider it appropriate that the 2014 DAU be amended, is for the 2010 AU resumption provisions to be reinserted as proposed in clause 7.6 of the CDD amended DAU.		
(1) After considering Aurizon Network's proposed mutually exclusive access application provisions, our consolidated draft decision is to refuse to approve the proposal.	11.18	<b>Disagree.</b> Reference is made to Aurizon Network's response to CDD 11.1.
(2) We consider it appropriate that Aurizon Network amend its draft access undertaking by reinstating the queuing provisions based on those from UT3, in the manner proposed in clauses 7.2 and 7.5 of the CDD amended DAU.		

## CDD 11.1, 11.2 and 11.18 Reinstatement of the queue and capacity registers

### Reinstatement of the queue and capacity registers

Aurizon Network sought to streamline the capacity allocation process in the 2014DAU by replacing the queue and the capacity registers with a set of criteria that an access seeker must demonstrate it can meet in order to be allocated capacity. The criteria were designed to provide an efficient mechanism to allocate capacity in the event that Aurizon Network receives mutually exclusive access applications, which ultimately delivers sufficient certainty that the access holder is able to use the access rights.

In the CDD the QCA has rejected Aurizon Network's capacity allocation criteria on the basis that it gives Aurizon Network discretion which could be used to discriminate between access seekers, saying that the proposal would allow Aurizon Network to "withhold allocating capacity until it can extract unreasonably favourable terms from an access seeker."<sup>53</sup>

Aurizon Network understands the need to include mechanisms to prevent unfair differentiation, but considers that a combination of transparency and the existence of general prohibitions on unfair differentiation in Part 2, mean that the measures imposed by the QCA to achieve this objective are unnecessary.

<sup>53</sup> Queensland Competition Authority (2015b). p.60.

It is disappointed with the QCA's reluctance to approve a more progressive capacity allocation system, in favour of an inefficient 'first come, first served' principle which fails to reflect the complex and dynamic environment that is the CQCN. That said, and on the balance of other issues in the CDD, Aurizon Network is prepared to accept the reinsertion of the 2010AU queuing provisions, subject to the following issues being addressed.

### **Reordering the queue**

In the CDD amended DAU, the QCA has removed the 2010AU provisions that allowed Aurizon Network to re-order the queue (clause 7.3.4(c) to (k) of the 2010AU). In the CDD it has addressed this by concluding that the provisions in clause 7.2.1 of the CDD amended DAU, which allow Aurizon Network to remove an access seeker from the queue, are sufficient. Aurizon Network does not support the removal of the queue reorder provision.

Under the 2010AU, Aurizon Network was able to re-order the queue for commercial performance reasons (clause 7.3.4(c)(iii)). This provision enables Aurizon Network to prioritise longer term, higher value access contracts, which also helps to reduce the risk of asset stranding (refer Chapter 14). This is not only in Aurizon Network's legitimate business interests but is also consistent with the objects of Part 5 of the Act, to the extent that a failure to address asset stranding risk may ultimately impact on investment. On this basis Aurizon Network seeks the reinsertion of this provision in the 2014DAU.

Clause 7.5.3(a) of the CDD amended DAU prevents an access seeker signing an access agreement without the written consent of any access seekers who may be ahead of them in the queue. This clause is not required as Part 7 outlines the rules for the allocation of access rights. To add another layer to this process, which effectively requires a competing access seeker to sanction the application of Part 7, is anti-competitive (it hinders downstream competition) and is therefore in conflict with the object of Part 5 of the QCA Act. The queue reordering provisions in the 2010AU did not include the written consent requirement proposed by the QCA nor has any stakeholder suggested this. In an efficient supply chain it is imperative that the ability for incumbents to game processes is minimised and genuine access seekers are not frustrated by anti-competitive behaviour.

Clause 7.5.2(c)(ii) of the CDD amended DAU provides for an access seeker to be removed from the queue if it cannot demonstrate its ability to use the access rights in accordance with the criteria in clause 7.2.1. In the absence of an ability to re-order the queue, there is an increased risk of dispute and inequitable outcomes arising from Aurizon Network being required to remove an access seeker from the queue in order to prioritise another access seeker who is lower in the queue for genuine reasons. For example, if removed from the queue, access seekers that were higher in the queue will lose their position to those access seekers lower in the queue who may have been queued behind the prioritised access seeker. Under clause 7.5.2(f) of the CDD amended DAU, a dispute regarding queue position must be resolved before a position in the queue is changed, which may lead to gaming behaviour between competing access seekers. This could unnecessarily slow the process of gaining access to the rail network.

It is not in the interests of the supply chain to have an archaic and inflexible queuing mechanism which does not reflect the dynamic nature of the CQCN. Aurizon Network occupies a unique position in the CQCN supply chain and it is well placed to efficiently and equitably manage the allocation of access rights, subject always to its overriding obligations not to unfairly differentiate between access seekers.

In conclusion, Aurizon Network does not support the QCAs CDD DAU queuing provisions which reduce this ability, and seeks the reinsertion of 2010AU provisions (clause 7.3.4(c) of the 2010AU), which allow it to re-order the queue in designated circumstances (including to favour a longer term contract). To be clear, if the QCA does not reinsert these provisions, Aurizon Network does not agree with CDD 11.1 and 11.18.

## CDD 11.4 Terms of renewal of access rights

Clause 5.1 (d)(i) of the 2010AU requires an access seeker to renew access rights on terms consistent with the Standard Access Agreement (SAA) in force at the time, unless otherwise agreed.

In contrast to the views of the QRC<sup>54</sup> and Aurizon Network<sup>55</sup>, the QCA is seeking to mandate that the renewal access agreement must now be on the same terms as previously executed (i.e. UT1, UT2 or UT3 SAA), unless otherwise agreed between the parties (clause 7.3(h) of the CDD amended DAU).

Aurizon Network cannot understand why the QCA requires this change. If approved, this clause will limit alignment across CQCN access holders of substantive terms such as take or pay and, somewhat perversely, may result in renewing access seekers being unable to contract on the terms of the current QCA approved SAA .

Aurizon Network raised this question in its response to the IDD.<sup>56</sup> In its CDD, the QCA has failed to explain why it is seeking to implement this substantive change nor has it explained why this change is necessary. The QCA has not come to this position based upon evidence that it is supported by Access Holders. Interestingly , in response to the QRC seeking clarification that the “renewing Access Seeker should be required to align the terms and conditions of the renewed agreement with the SAA in force at the time”<sup>57</sup>, the QCA stated that “our drafting implies this position”<sup>58</sup>. Aurizon Network cannot understand the basis for this conclusion as the drafting clearly implies the opposite.

Aurizon Network repeats the requests made by it and the QRC, and calls for the QCA to clarify and explain the intention of its position. Aurizon Network does not support this provision as currently drafted, and submits it should be redrafted to reflect the position advanced by the QRC.

## CDD 11.5 Replacement Mine concept

The ‘Replacement Mine’ concept in the 2010AU allows a renewing access seeker to amend the origin of its Train Service Entitlements (TSEs) when renewing the access agreement to another mine in close proximity to the existing mine. The purpose is to provide the access seeker with below-rail contractual certainty when expanding operations to an adjacent or nearby mine. Aurizon Network sought to clarify the boundaries for a replacement mine in its 2014DAU submission, removing the concept in name but creating new provisions in clause 7.3(b) which provide more flexibility for renewing access seekers to amend the origin and destination of its train services.

In its CDD, the QCA rejected Aurizon Network’s submission to broaden the scope of a renewal on the basis that “in the absence of further information, the changes may lead to uncertainty regarding its operations”<sup>59</sup>. The QCA did not elaborate on what information it requires, or how the concept may lead to uncertainty in Aurizon Network’s operations.

For clarity, the QCA’s drafting in the CDD amended DAU appears to accept the substance of Aurizon Network’s substitute replacement mine concept with some minor drafting amendments. Aurizon Network is therefore willing to accept the QCA’s proposed drafting.

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<sup>54</sup> Queensland Competition Authority (2015b). p.73.

<sup>55</sup> Aurizon Network (2015a). s.11.5.2, p.140.

<sup>56</sup> Aurizon Network (2015a). s.11.5.2, p.140.

<sup>57</sup> Queensland Competition Authority (2015b). p.73.

<sup>58</sup> Queensland Competition Authority (2015b). p.73.

<sup>59</sup> Queensland Competition Authority (2015b). p.75.

## CDD 11.8 Customer initiated capacity transfers

The QCA has proposed to reinsert the 2010AU provisions that relate to Customer Initiated Capacity Transfers in Part 7 of the CDD amended DAU. Aurizon Network has no concerns in principle with this approach, however has concerns with the drafting. The CDD refers to drafting in clause 7.4 of the 2014DAU. However, there is currently no drafting included in clause 7.4 of the CDD amended DAU dealing with customer initiated transfers.

Following conversations with the QCA, Aurizon Network understands that the provisions originally proposed in clause 12.4(f) of the CDD amended DAU are intended to provide for these transfers. Aurizon Network has the following comments in regards to this clause:

- clause 12.4 applies only to pre-UT4 access agreements, and picks up the provisions applying under clause 7.3.7 of the 2010AU;
- the existing clause 7.3.7 of the 2010AU has the following shortcomings:
  - it does not allow for a customer to initiate a transfer to itself if it wishes to enter a new access agreement as the access holder (only allows for transfer between rail operators);
  - it requires the transferee receiving the access rights to maintain the relinquishment and take or pay provisions from the existing access holder's access agreement. This is contrary to Aurizon Network's preference for new access agreements to move towards the current standard form provisions under the prevailing access undertaking at the time of the transfer taking effect. It also increases the time required to effect such transfers as it necessitates bespoke amendments to the standard access agreement.

Aurizon Network has proposed amendments to reflect the customer initiated capacity transfer provisions that it believes will overcome these concerns. Aurizon Network has used the customer initiated transfer provisions originally suggested in its 2014 Standard Operator Access Agreement (as submitted in August 2014), with minor amendments to translate the provisions into the DAU. Aurizon Network understands that the QCA agrees that it has not adequately dealt with customer initiated capacity transfers in the CDD amended DAU and as such will review the proposed drafting provided with this submission.

## CDD 11.9 – 11.16 Short term capacity transfers

As outlined in Aurizon Network's previous responses to the QCA on the short term capacity transfers process, Aurizon Network's position is that, unless it can be found that the mechanism Aurizon Network proffered is inappropriate having regard to the requirements of the QCA Act, it should be accepted<sup>60</sup>. Aurizon Network consulted closely with access holders and industry representatives in regards to the mechanism for managing short term capacity transfers. In each round of consultation undertaken by the QCA on Aurizon Network's proposals, stakeholder submissions received by the QCA generally support the short term transfer mechanism as originally proposed by Aurizon Network<sup>61</sup>. For example:

Aurizon Operations<sup>62</sup>:

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<sup>60</sup> Aurizon Network (2015d). Response to QCA Supplementary Draft Decision on 2014 Draft Access Undertaking – Capacity Transfer Mechanism, 29 May; Aurizon Network (2015e). Response to Stakeholder Notice - Short Term Transfer Mechanism, 30 September.

<sup>61</sup> Queensland Competition Authority (2014). Discussion Paper on Potential Short Term Transfer Mechanism, 19 December.

<sup>62</sup> Aurizon Operations (2015). Response to Stakeholder Notice 11: Short-term Transfer Mechanism, 30 September.

*...the STTM proposal submitted by Aurizon Network does not fundamentally differ from the historical transfer mechanisms. The objective of the framework is to improve the timeliness of the administrative arrangements for execution and the predictability as to whether a transfer would be approved... -*

QRC<sup>63</sup>:

*The QRC was largely supportive of the mechanism as proposed by Aurizon Network, with our submission of February 2015 suggesting relatively minor amendments to Aurizon Network's approach.*

Vale<sup>64</sup>:

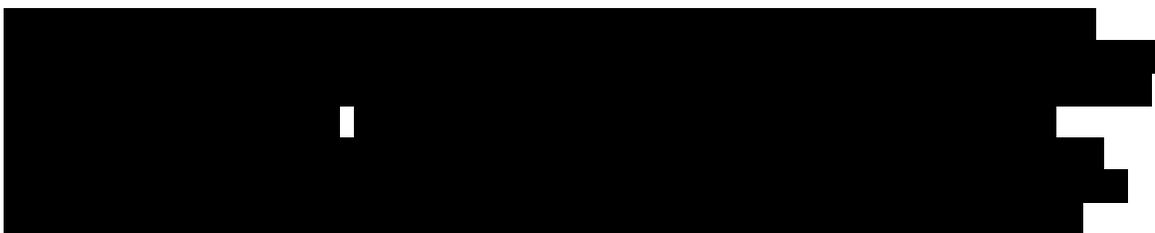
*Vale appreciates the approach by Aurizon to address this issue and supports a short term transfer arrangement. Vale agrees the objectives of a short term transfer mechanism should be to provide flexibility to manage access rights through a timely transfer process... While generally supporting this initial proposal Vale believes the transfer mechanism should incorporate the ability for both the holder of access rights and the end user whose access rights are held by their train operator to actively participate.*

As such, it is disappointing that the QCA continues to propose alternate processes for managing these capacity transfer requests. Further to previous arguments raised in these responses, Aurizon Network provides the following further comments on the QCA's proposed mechanism.

### **Merging of transfer processes (existing access request process and short term transfers)**

The QCA has maintained its position from its 2015 Supplementary Draft Decision<sup>65</sup> in regards to combining the short term transfer process within the existing access request process to deal with requests for transfers of a longer duration. Aurizon Network has previously raised a number of concerns with this proposal, including the potential for confusion and hence disputes from customers as the drafting proposed by the QCA is quite complex and not easily understood. Aurizon Network has also raised concerns around administrative issues and complexity surrounding how the QCA's proposal will be managed in practice.

The mechanism proposed by Aurizon Network in its Discussion Paper<sup>66</sup> for short term transfers was designed in a way that minimised administrative effort in effecting short term transfers via incorporating deeming provisions in the access agreement. As well as removing the requirement to execute a variation to access agreements for the transferor and transferee, this also enabled Aurizon Network to comply with its legislative requirements under the *Transport Infrastructure Act 1994* (TIA).



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<sup>63</sup> Queensland Resources Council (2015). QRC's response to Supplementary Draft Decision – Capacity Transfer Mechanism, 15 June.

<sup>64</sup> Vale (2015). Vale's Response to Aurizon Network's Discussion Paper on potential short term transfer mechanism, 30 January.

<sup>65</sup> Queensland Competition Authority (2015h). Supplementary Draft Decision - Aurizon Network 2014 Draft Access Undertaking: Capacity Transfer Mechanism, 30 April.

<sup>66</sup> Aurizon Network (2014c). Discussion Paper on Potential Short Term Transfer Mechanism, 19 December.

Aurizon Network therefore proposes that provisions be included in the access agreements to have deemed replacement schedules following a short term transfer. Aurizon Network has included this drafting in the marked up standard access agreement and Train Operations Deed submitted with this response.

### **Administrative and practicality concerns**

While the QCA has considered some administrative issues in the CDD compared to the Supplementary Draft Decision (for example the transferee needing to have an existing access agreement to avail of the short term transfer mechanism), the QCA's proposal still results in a number of issues around the practicality of implementing the process. For example, the QCA's process still requires variations to be made to agreements to enable transfers to occur within the two business day timeframe. This very short timeframe does not reflect the practical reality involved in negotiating, drafting and seeking approval for variations to agreements, and is likely to conflict with the approval processes utilised by access holders. This issue is compounded in the case of transfers involving Aurizon Operations, for the reasons described above.

Other issues around practicality result from the QCA's proposed process for the rapid capacity assessment. By hard wiring the rapid capacity assessment to only consider the most recently completed annual capacity review (as required under Part 7A), this does not allow Aurizon Network the ability to consider variations which have already been agreed to TSEs with customers since the last capacity assessment report was finalised. The implications of this is that Aurizon Network may be forced to accept a transfer being effected even if the current available capacity is not sufficient, and therefore conflicts with the efficient allocation of capacity, and the object of Part 5 of the QCA Act. Practically, Aurizon Network would consider the most recent capacity assessment as one of the items considered to determine if capacity is available. It is more appropriate that the assessment be linked to the most recent annual capacity assessment, taking into account any subsequent changes to Available Capacity that have arisen due to transfers and other changes in contractual entitlements that have taken place in the interim.

The overlay of the QCA's proposed short term transfer process with the requirements under Schedule G also causes a number of issues in the scheduling environment, particularly with the interaction with the Master Train Plan (MTP) as the QCA has proposed in its Schedule G in the CDD amended DAU (reference is made to Aurizon Network's response to CDD 13.3 in Chapter 13 for further discussion on Aurizon Network's concerns with the MTP). Further amendments are required to Schedule G to incorporate Aurizon Network's short term transfer provisions, however these have not been included in the marked up Undertaking sections provided with this submission.

### **Assessment criteria**

In regards to the criteria for determining if a short term transfer should be permitted, Aurizon Network agreed some concessions that are workable in its response<sup>67</sup> to the Stakeholder Notice<sup>68</sup>, including the requirement for short term transfers to be limited to only 25% of annual TSEs and considering previous usage of access rights at a level of 85%. Aurizon Network is also willing to extend the short term transfer process to allow for a change of destination within the same port precinct (e.g. Port of Hay Point, Port of Gladstone), subject to confirmation being received that the different unload terminal has the capacity to be able to accept the additional services. Aurizon Network is still willing to provide these concessions, and has made relevant amendments to reflect these matters.

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<sup>67</sup> Aurizon Network (2015e).

<sup>68</sup> Queensland Competition Authority (2015i). Stakeholder Notice 11 Short Term Transfer Mechanism, 16 September.

## **Application of short term transfer provisions to legacy access agreements**

The QCA has included in its drafting an obligation for existing access holders under pre-UT4 access agreements, where requested by the party, to negotiate to amend the access agreement to include provisions to allow use of the short term transfer provisions. Aurizon Network agrees with this in principle, and suggested drafting in its original proposal to allow for this.

Aurizon Network is uncertain about how the QCA intends this process to be completed. Aurizon Network understand the QCA's thinking was that in amending the access agreement the access holder and Aurizon Network would wholly replace all transfer provisions with the new clauses from the 2014DAU. Aurizon Network pointed out the concern that rather than being in a position where there is greater consistency between the transfer provisions which apply to access holders, it would lead to there being a more diverse range of capacity transfer processes. This is due to the access holders, through the negotiation to amend the access agreement, requiring some provisions which are favourable to be maintained while also getting the 'best parts' of the new UT4 processes.

Aurizon Network believes this should be managed by including a clause in the Undertaking that provides that Aurizon Network is under no obligation to amend UT1, UT2 or UT3 access agreements in relation to transfers in a manner which is not consistent with the UT4 Undertaking provisions. The intent of this is to prevent access holders from picking and choosing relevant transfer provisions. Aurizon Network has proposed drafting to address this.

## **Reporting and review of short term transfer provisions**

The QCA proposes that in order to allow it to monitor whether access holders have undertaken any gaming behaviours when using the short term transfer provisions, Aurizon Network should keep a register of all transfer transactions which take effect during the year. Aurizon Network agrees in principle to this, as records of transfer transactions would already be captured through the usual process for administering access requests. Aurizon Network has existing processes to report compliance with the Undertaking and can include in the annual compliance report specific details regarding transfer requests.

The QCA's intent and drafting for this provision is confusing. The QCA's CDD references clause 10.5.2 of the CDD amended DAU, however it is not clear where this has been included. Aurizon Network understands the clause reference is incorrect and it has been included in the annual reporting provisions contained in Part 10.

The QCA has included provisions in its drafting which require Aurizon Network, within three months of commencement of the UT4 Undertaking, to undertake a review of the operation of the transfer provisions, consult with access holders and train operators and submit to the QCA proposed amendments or reasons for not making amendments. The QCA is required to assess Aurizon Network's submission and either approve or not approve the proposed amendments. Aurizon Network agrees in principle with this position, as it aligns with the original proposal contained in its Discussion Paper<sup>69</sup>.

The QCA's proposed drafting then goes further to state that if the QCA does not approve the amendments proposed by Aurizon Network, or if Aurizon Network fails to make the required submission, then the QCA may develop amendments to improve the workability of the transfer provisions which Aurizon Network will be required to accept. Aurizon Network does not agree to give the QCA a unilateral ability to amend Aurizon Network's Undertaking and/or the resulting commercial agreements. This introduces a degree of regulatory risk which Aurizon Network and its customers cannot control and for which Aurizon Network is not rewarded.

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<sup>69</sup> Aurizon Network (2014c).

## **Transfer fees**

### Free transfer period

The QCA's CDD provides that for transfers of access rights up to three months in duration, no transfer fee will be payable. The rationale is to reduce the impact of socialisation of transfers amongst users of the rail network. While financially, Aurizon Network will be kept whole regardless of the timeframe for transfers for which no fee is payable, it does have some concerns with the QCA's position.

For example, the likely outcome of this shorter three month timeframe is that customers will be incentivised to request transfers for a period of three months at a time to avoid having to pay a fee, even if the overall outcome is to have a transfer for a longer period of time. This would result in increased administrative effort for both Aurizon Network and the access holder to manage these rolling transfers. It would also result in reduced contractual certainty for Aurizon Network and could have an impact on Aurizon Network's ability to fully understand available capacity and what is required for new access seekers. This is because Aurizon Network will be undertaking capacity reviews using contractual information that is unlikely to reflect what the access holders are actually intending to do with its contracted access rights. This increases the risk associated with expansion projects for Aurizon Network and the expanding customers.

Further to this, reducing the 'free' transfer flexibility for Aurizon Network's customers does not fully consider the genuine benefit for access holders of being able to ensure increased efficiency of the supply chain by better aligning raiing and shipping requirements. The ability for access holders to manage supply chain alignment has also been further impacted by the QCA's changes to Schedule G, which remove the mainline path pooling process in scheduling train services.

Aurizon Network understands the QCA may be willing to consider increasing the proposed time period of three months for free transfers to two years. This aligns with current provisions in the 2010AU and recent decisions from the QCA for UT1 and UT2 access agreements.<sup>70</sup> Under these provisions, Aurizon Network will not be charging transfer fees for transfers of access rights for under two years relating to coal-carrying train services operating within the same coal system under UT2 access agreements. Aurizon Network has agreed to offer the same treatment on transfer fees to all remaining UT1 and UT2 access holders, subject to amendment of the relevant agreements.

### Transfer fee calculation

Aurizon Network notes a minor error in the provisions of Part 7 of the CDD amended DAU regarding the calculation of transfer fees. The current provision requires Aurizon Network to calculate the present value of the take or pay charges for the remainder of the term of the access rights. For a transfer of access, in practice, Aurizon Network would only consider the change in present value of the access rights for the period of the transfer. Aurizon Network understands that the QCA agrees that the calculation of transfer fees should be limited to the period of the transfer of the access rights, not the remainder of the term of the relevant access agreement. Aurizon Network has proposed amendments to this effect.

### Provision of information on the calculation of relinquishment and transfer fees

The QCA has provided for Aurizon Network to make information available to access holders regarding the calculation of relinquishment and transfer fees (where payable). Aurizon Network has no concern with

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<sup>70</sup> UT2 Transfer Fees, 16 February 2016; <http://www.qca.org.au/getattachment/781c0052-a441-4617-85a5-bd2f29b82196/QCA-in-principle-approval.aspx>; <http://www.qca.org.au/Rail/Aurizon/Intro-to-Aurizon/2010-Access-Undertaking/Aurizon-s-2010-AU-Ongoing-Compliance/Transfer-Fees/In-Progress/UT2-Transfer-Fees>

this provision in principle, however notes that the drafting needs to provide for Aurizon Network making reasonable assumptions about future events e.g. reference tariffs, which impacts the inputs to the calculations.

Aurizon Network also seeks clarification of the level of detail to be provided, for example if the fee calculation is for a relinquishment and Aurizon Network has managed to find another party to contract these paths, the level of information provided to the new party needs to enable Aurizon Network to still adhere to confidentiality and ringfencing requirements.

### **Longer term transfers (criteria C)**

#### Combination of short term transfer process and existing provisions

As previously outlined by Aurizon Network<sup>71</sup>, the short term transfer process should be a separate process from existing provisions, with criteria applying as per Aurizon Network's proposal (with some agreed variations as discussed above).

Aurizon Network remains of the view that short term transfers and longer term transfers should be managed through different processes. Combining the mechanisms in the way proposed by the QCA results in a number of practical issues with processing transfer requests. There could be increased administrative effort on the part of both Aurizon Network and the access holders where it is unclear how the requested transfer meets the criteria for a short term transfer (e.g. where the transferor/transferee is unaware whether the other party already has an existing access agreement).

The current drafting is difficult for access seekers and access holders to interpret, and this could lead to increased disputes regarding the way the request is being processed by Aurizon Network. While Aurizon Network would over time educate access holders wanting to avail of the short term transfer mechanism (by going back and forth where insufficient information is provided by a transferor or transferee), this leads to an increase in administration costs for all parties, and increases the time required to process and effect transfers.

Aurizon Network has included amendments to Part 7 to separate short term transfers from the existing transfer process. The drafting for existing processes reflects what was originally proposed by Aurizon Network in the Standard Access Agreement submitted as part of its 2014 DAU in August 2014 (with relevant amendments as required to move these provisions into the Undertaking).

#### Additional concerns with the QCA's drafting

The QCA has also amended the proposed transfer provisions that remove the priority of Ancillary Access Rights (being access rights in addition to the nominated transfer access rights which are required for the transfer to occur). Aurizon Network has concerns with these changes as it has the potential to discriminate against access seekers in favour of existing access holders. As such, Aurizon Network has not reflected this in its proposed amendments.

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<sup>71</sup> Aurizon Network (2015d); Aurizon Network (2015e).

## Chapter 12 – Network Development and Expansion Process (Part 8)

### Summary of Aurizon Network's Position

As evident elsewhere in this response, Aurizon Network has accepted some aspects of the QCA's CDD in the interests of ensuring a resolution to UT4. However, Aurizon Network cannot accept the QCA's CDD in relation to the network development and expansion process.

Aurizon Network considers that:

- if the QCA were to make a Final Decision consistent with its CDD in respect of Part 8 of the CDD amended DAU, the QCA would be acting beyond its powers under the QCA Act; and
- the CDD amended DAU has numerous impractical provisions and adverse risk outcomes for Aurizon Network.

An explanation of each of these views is provided below.

Accordingly Aurizon Network is not prepared to accept Part 8 of the CDD amended DAU and the CDD amended SFA. Aurizon Network proposes that UT4 incorporate the expansion framework Aurizon Network proposed in its 2014 DAU (the Aurizon Network/QRC Expansion Process). Aurizon Network is willing to accept in addition a process obligation as part of UT4 to submit a Standard User Funding Agreement (SUFA) DAAU within three months of the approval date of UT4, which is consistent with the QCA's position on SUFA in the CDD amended DAU. In respect of the SFA, Aurizon Network wishes to engage with the QCA over the numerous differences between the SFA in the 2014 DAU and the CDD amended SFA, and is willing to accept a process obligation as part of UT4 to submit a SFA DAAU, which would draw on the outcomes of that engagement, within three months of the approval date of UT4.

### QCA acting beyond powers

Aurizon Network considers that if the QCA were to make a Final Decision consistent with its CDD in respect of Part 8 of UT4, the QCA would be acting beyond its powers under the QCA Act. This view is taken on the basis of various aspects of the CDD amended DAU, including but not limited to the following items:

- If Aurizon Network decided not to fund a project and an access seeker disputed that decision, the QCA would be able in its dispute resolution capacity to compel Aurizon Network to fund that project (see clauses 8.2.2(a)(i) and 8.2.2(g) of the CDD amended DAU). Similarly, if Aurizon Network decided to seek 'Access Conditions' and an access seeker disputed that decision, the QCA would have the ability in its dispute resolution capacity to compel Aurizon Network to accept 'Access Conditions' as thought fit by the QCA. In both of these instances, the QCA has no power to impose a funding obligation on Aurizon Network that it does not volunteer to accept.
- The proposed obligation upon Aurizon Network to fund a capacity shortfall expansion without the conditions<sup>72</sup> that Aurizon Network requires in order to volunteer to assume this funding obligation. The QCA has no power to impose a funding obligation on Aurizon Network that it does not volunteer to accept.

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<sup>72</sup> Refer: Aurizon Network (2015a). p.171.

- Allowing user funding to be the project funding option adopted should access seekers wish notwithstanding Aurizon Network's election on a timely basis to fund a project on regulatory terms (clause 8.7 of the CDD amended DAU).<sup>73</sup> The availability of user funding in these circumstances under UT4 would significantly impair the private property rights of Aurizon Network. Aurizon Network considers that this proposed approach increases the sovereign risk faced by investors in Queensland infrastructure that is subject to the QCA's economic regulation.
- The absence of a protection of Aurizon Network's legitimate business interests in the event of an expansion project. In the conduct of an access determination that entails an expansion, the QCA has a mandatory statutory requirement to ensure that the legitimate business interests of the access provider are protected (section 119 of the QCA Act). Explicit protection of the access provider's legitimate business interests should also be afforded in respect of any expansion project under an access undertaking.
- The modification of the statutory process that governs how a DAAU is to be addressed (see clauses 8.8.4(c) to (f) inclusive of the CDD amended DAU) and in particular, the establishment of an unfettered right of the QCA to make changes to SUFA documentation 'to enhance its workability'. The QCA should not have any greater power under the undertaking to require an amendment to a DAAU than it does under the QCA Act to require submission of a DAAU.

## Impractical provisions and adverse risk outcomes of QCA's proposals

Aurizon Network considers that the CDD amended DAU and the CDD amended SFA feature many impractical provisions and numerous adverse risk outcomes for Aurizon Network. Examples include, but are not limited to, the following items:

- The definition of the Pre-feasibility Study (see clause 12.1 in the CDD amended DAU) requires Aurizon Network to identify and assess "all possible technical solutions". There is an almost limitless number of possible technical solutions. Aurizon Network does not consider it appropriate that it should be required to assess options such as a rail tunnel or an above-ground rail structure between mine and terminal, for example, even though they are *possible* technical solutions.
- In the event of 'step-in' under a SFA on the basis of the SFA template, Aurizon Network is required to provide "reasonable assistance and information" to the nominated replacement study manager without having any means of recovering its costs of doing so (see clause 17.6(b) of the CDD amended SFA).
- In response to Aurizon Network's concerns, as expressed in section 12.6.6 of its response to the IDD<sup>74</sup>, the QCA has introduced in section 11.1.1 of the CDD amended DAU the concept that, unless otherwise agreed, a dispute in respect of a right, an obligation or enforcement of an executed agreement, such as a SFA, must be dealt with in accordance with that agreement. However, the QCA has failed to reflect this concept in its provisions on disputes under Part 8 (clause 8.2.2 of the QCA amended DAU) and consequently those provisions permit access seekers to dispute "any matter that may arise under this Part 8". The treatment of disputes under Parts 8 and 11 of the CDD amended DAU is therefore inconsistent as to whether a dispute right under the undertaking is available if a contractual dispute right is available.
- Part 12 of the CDD amended DAU applies to any rail infrastructure project that has the primary purpose of achieving better operational outcomes, such as the installation of a higher quality

<sup>73</sup> Refer also: Queensland Competition Authority (2015b). Consolidated Draft Decision: Aurizon Network 2014 Draft Access Undertaking, Volume II – Capacity and Expansions, p.186, section 8.7.1(a) item in the table.

<sup>74</sup> Aurizon Network (2015a). p.159.

asset that has a lower lifecycle cost due to its lower ongoing maintenance cost, but does not constitute asset replacement or renewal (see the definition of 'Expansion' in clause 12.1 of the CDD amended DAU, which already excludes asset replacement and renewal). The expansion process to be included in Part 8 of UT4 is inappropriate for the investigation and development of projects of this nature, as was submitted in Aurizon Network's response to the IDD (see section 12.12)<sup>75</sup>. Although the QCA has stated in the CDD that "Expenditure to achieve better operational outcomes, with no increase in capacity, would also be excluded" (from the definition of 'Expansions' in Part 12)<sup>76</sup>, the QCA has omitted to amend the definition of 'Expansion' in the CDD amended DAU to give effect to this additional exclusion.

- When a funder of a multi-funder study elects to terminate for convenience, Aurizon Network lacks a watertight means of terminating the other SFAs or gaining the agreement of the non-terminating study funders to meet the funding shortfall. The QCA's proposed mechanism to effect increased contributions from other study funders is legally ineffective as it relies on an 'agree to agree' provision (see clause 9.5(b) of the CDD amended SFA) and would not provide any relief to Aurizon Network if any non-terminating study funder were to fail to agree on revised project funding arrangements or if such agreement were delayed indefinitely. In its justification of these arrangements, the QCA concedes that "...remaining study funders **may** choose to proceed under different arrangements, subsequent to a meeting. This should offset **some** of the risk to Aurizon Network."<sup>77</sup> (emphasis added) Aurizon Network should have strong suspension/termination rights in respect of the continuing study funders so that Aurizon Network is at no risk whatsoever of being required to fund any part of the study should a study funder terminate its SFA for convenience.
- The QCA requires that an independent firm of accountants should make a determination as to whether pre-feasibility or feasibility study costs were reasonable (clause 11.3(a) of the CDD amended SFA). Based on its experience and understanding of the issues involved, Aurizon Network considers that accountancy firms lack the requisite professional expertise in the conduct of managing the investigation of large rail infrastructure projects required to opine as to whether Aurizon Network's project investigation costs were incurred reasonably. It is standard business practice to engage professional advisers for matters in respect of which they have appropriate professional expertise.

In addition to these material deficiencies and adverse risk outcomes there are many drafting ambiguities in both Part 8 of the CDD amended DAU and the CDD amended SFA. These ambiguities create at best, a degree of uncertainty where there should be certainty and at worst, a range of multiple and contradictory positions.

## Aurizon Network's proposal

As Aurizon Network's concerns with the QCA's CDD in relation to the network development and expansion process are so extensive, Aurizon Network is not prepared to volunteer to accept Part 8 of the CDD amended DAU and the CDD amended SFA in their current forms. The QCA's timeframe for responses to the CDD and the nature and extent of Aurizon Network's concerns over the CDD have made it impossible for Aurizon Network to submit a comprehensive and detailed response to address its concerns about Part 8 of the CDD amended DAU and the CDD amended Studies Funding Agreement (SFA).

Aurizon Network is particularly disappointed with this outcome given the significant time and resources devoted by it and the QRC in developing what both organisations considered to be an effective and

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<sup>75</sup> Aurizon Network (2015a). p.168.

<sup>76</sup> Queensland Competition Authority (2015b). p.167.

<sup>77</sup> Queensland Competition Authority (2015b). p.194.

workable framework that enables the growth and development of the CQCR. Aurizon Network considers that this framework would directly promote the object clause of Part 5 of the QCA Act. It is critical to note that the Aurizon Network/QRC Expansion Process was substantively agreed with the QRC – the only material issue of contention was the absence of a voluntary funding commitment, which is clearly beyond Aurizon Network’s obligations under the QCA Act. The CDD does not explain why the QCA considers that the framework agreed between Aurizon Network and the QRC is unacceptable, or why the QCA considers that its extensive changes to that framework were required as a result of submissions from other stakeholders.

Aurizon Network restates by reference all of the arguments for the adoption of the Aurizon Network/QRC Expansion Process set out in section 12.2 of Aurizon Network’s response to the IDD<sup>78</sup>.

The QCA’s rejection of the Aurizon Network/QRC Expansion Process fundamentally undermines the negotiate-arbitrate framework on which Part 5 of the QCA Act is based. This rejection, which went far beyond what was necessary to address issues raised by stakeholders other than the QRC about that version of the expansion process, will therefore have a material and detrimental impact on the incentives of Aurizon Network and stakeholders to attempt to agree any position in relation to the regulatory framework in future, as it risks being overturned by the QCA.

A business perspective is essential in developing the expansion process, as it is ultimately about investing in the CQCR, which entails a range of complex technical, operational, commercial and financial risks. This perspective was adopted by both organisations in the development of the Aurizon Network/QRC Expansion Process. Aurizon Network respectfully submits that the QCA is not as well placed as either

- Aurizon Network, which has extensive experience in conducting all stages of the major rail infrastructure project lifecycle, or
- end users, which are predominantly global mining companies with extensive experience in conducting all stages of the major infrastructure and mining project lifecycle, as represented by the QRC

to develop an expansion process that best meets the object clause of Part 5 of the QCA Act. Aurizon Network considers that the regulatory framework for expansions proposed by the QCA is practically unworkable and extends well beyond addressing the economic problem that regulation was designed to address, which, as highlighted by the Productivity Commission (PC), is a “lack of effective competition”<sup>79</sup>.

Aurizon Network considers that the QCA has played a more active role than is either appropriate or required by the QCA Act in its consideration of the expansion process. Aurizon Network notes that the PC has identified the potential for regulatory over-reach. As part of its most recent review of the National Access Regime, the PC concluded:<sup>80</sup>

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<sup>78</sup> Refer: Aurizon Network (2015a). section 12.2, p.148.

<sup>79</sup> Productivity Commission (2013). National Access Regime, Inquiry Report no. 66, Canberra, p.6.

<sup>80</sup> Productivity Commission (2013). p.141.

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**Increased discretion for regulators to determine the conditions of directed extensions, as proposed by the QCA and Glencore, would increase regulatory risk for infrastructure service providers and could have an adverse effect on their investment incentives.**

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In respect of Part 8 of UT4, Aurizon Network instead proposes that it incorporates the Aurizon Network/QRC Expansion Process, which is set out in clauses 8.1 to 8.10 inclusive of the 2014 DAU (the balance of Part 8 of the 2014 DAU, namely clauses 8.11 to 8.13 inclusive, addressed issues that are no longer addressed within Part 8 of the CDD amended DAU). The drafting of other parts of the DAU, such as Part 11 (Dispute Resolution and Decision Making) and Part 12 (Definitions and Interpretation), would need to be consistent with that form of the expansion process.

The Aurizon Network/QRC Expansion Process was developed on the basis that SUFA would be approved before UT4. As SUFA is now due to be approved after the approval of UT4, Aurizon Network is willing to assume, as part of the UT4 expansion process, an obligation to make an initial submission of proposed SUFA documents in the form of a DAAU by three months after the UT4 approval date. If this position changes, or the QCA provides a position on UT3 SUFA, Aurizon Network would see that the timings required to respond should be in recognition of the UT4 timeline. Aurizon Network would be responsible for determining the form of the proposed SUFA documents, which would take into account the outcomes of the previous SUFA DAAU process. The normal process for consideration of a DAAU should apply.

In respect of the SFA, Aurizon Network notes that it has yet to engage with QCA officers over the numerous differences between the form of SFA in the 2014 DAU, which was submitted 18 months ago, and the forms of SFA in the IDD and CDD. Examples of these differences are the issues set out in section 12.17 of Aurizon Network's response to the IDD<sup>81</sup>. Aurizon Network is keen to engage with QCA officers over these differences and considers that such an engagement would result in a better mutual understanding. In the expectation that the QCA will engage with Aurizon Network on a timely basis, Aurizon Network proposes that UT4, as at its approval date, does not include an approved SFA. Aurizon Network is willing to accept a process obligation as part of UT4 to submit a SFA DAAU, which would draw on the outcomes of that engagement, within three months of the approval date of UT4. The normal process for consideration of a DAAU should also apply here.

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<sup>81</sup> Refer: Aurizon Network (2015a). section 12.17, p.182.

## Chapter 13 – Network Management Principles (Schedule G)

### Summary of Aurizon Network’s Position

Aurizon Network has a number of outstanding concerns in relation to the Network Management Principles (NMP), which are contained in Schedule G. The key areas of disagreement with the QCA’s CDD are:

- the QCA’s proposal that the Strategic Train Plan (STP) be reviewed by an independent expert and then subject to audit by the QCA. Aurizon Network cannot accept the position where it may be bound by the independent expert’s recommendation on revising the STP or a capacity shortfall. This exposes Aurizon Network to risk for which it is not compensated;
- the QCA’s proposed inclusion of a greater level of detail for information originally intended to be included in the System Rules, as well as the governance arrangements for System Rules, has reduced the value in maintaining separate System Rules. To address the concerns that have arisen here, Aurizon Network instead proposes that the System Rules now be included as an Appendix to Schedule G which is consistent with its previous responses;
- the QCA’s proposals that require Aurizon Network to communicate changes to the Master Train Plan (MTP), Intermediate Train Plan (ITP) and Daily Train Plan (DTP) and to track these changes in the MTP through to the ITP and DTP. This does not provide any additional transparency to access holders or their operators but significantly increases the administration burden and costs for both Aurizon Network and Access Holders;
- the inclusion of the Supply Chain Group in the Contested Train Path process. This will constrain Aurizon Network’s capacity to fulfil its QCA Act obligations in the efficient operation and management of the network.

**Table 13.1 – QCA Consolidated Draft Decision**

	QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(3)	After considering Aurizon Network’s NMP included in Schedule G of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network’s proposal.	13.1	<b>Agree with amendments.</b>
(4)	The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is to amend the NMP to increase transparency and availability of train plans as set out in Schedule G of our CDD amended DAU.		
(3)	After considering Aurizon Network’s NMP included in Schedule G of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network’s proposal.	13.2	<b>(2)(a)-(e). Agree with amendments.</b> <b>(2)(f) Disagree.</b> Aurizon Network does not wish to be bound by the independent expert’s recommendation on revising the STP or capacity shortfall, as it is an uncompensated risk for Aurizon Network.
(4)	The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is to, among other things: <ul style="list-style-type: none"> <li>(d) (a) include its purpose, consistent with the provisions for the MTP, ITP and DTP</li> <li>(e) (b) include a deadline to submit initial STP, conditional on Aurizon Network first submitting its baseline capacity assessment(s) to us within</li> </ul>		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>six months of the 2014 DAU's approval</p> <p>(f) (c) specify to whom the STP will be submitted each year</p> <p>(g) (d) include additional details on the contents of the STP</p> <p>(h) (e) include an obligation for an annual preparation of the STP by coal system and in aggregate</p> <p>(i) (f) to provide for the QCA to require the STP be reviewed by an independent expert and audited by us,</p> <p>as set out in the marked changes in our CDD amended DAU.</p>		
<p>(3) After considering Aurizon Network's NMP included in Schedule G of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(4) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is to, among other things:</p> <p>(j) (a) require the MTP to cover a period of at least one month</p> <p>(k) (b) include the factors considered in preparing the MTP</p> <p>(l) (c) specify all types of traffics and train paths to be identified on the MTP</p> <p>(m) (d) set out the material assumptions made in preparing the MTP</p> <p>(n) (e) publish the MTP in tabular form on Aurizon's website every month. Aurizon Network can provide additional time/distance (location) formats for the MTP,</p> <p>as set out in the marked changes in this consolidated draft decision.</p>	13.3	<p><b>Agree with amendments.</b> Aurizon Network's main concern with these requirements is an obligation to notify and consult with access holders when a change to the MTP does not affect an access holder's access rights. Aurizon Network does not agree with this requirement.</p> <p>The QCA's proposals that require Aurizon Network to communicate changes to MTP, ITP and DTP and to track these changes in the MTP through to the ITP and DTP does not provide any additional transparency to access holders or operators but significantly increases the administration burden on Aurizon Network.</p>
<p>(4) After considering Aurizon Network's NMP included in Schedule G of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(5) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is to, among other things, revise the ITP to specify the train paths to be identified and to whom copies should be provided. These amendments are set out in the marked changes in our CDD amended DAU.</p>	13.4	<p><b>Disagree.</b> Reporting on the number of paths planned in the MTP, ITP and DTP and cancelled in the ITP and DTP will be resource-intensive and will require changes to IT systems to capture and track this data. Aurizon Network wishes to highlight the significant implementation risk and costs this imposes, which are currently not included in the MAR.</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(3) After considering Aurizon Network's NMP included in Schedule G of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(4) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is set out in the marked changes attached in our CDD amended DAU.</p>	13.5	<b>Disagree.</b> Reporting on the number of paths planned in the MTP, ITP and DTP and cancelled in the ITP and DTP will be resource intensive and will require changes to IT systems to capture. Aurizon Network would require an increase in its approved MAR to cover these costs.
<p>(1) After considering clause 7.6 of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is set out in clause 7A.2 of our CDD amended DAU.</p>	13.6	<b>Disagree.</b> Aurizon Network proposes that the System Rules now be included as an Appendix to Schedule G.
<p>(1) After considering Aurizon Network's NMP included in Schedule G of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) We would approve the NMP (and relevant parts of the 2014 DAU) with, among other things, the following proposed amendments, as set out in the marked changes in our CDD amended DAU:</p> <p>(o) (a) Define the 'day of operation' as 00:00 on the day of operation's start to 23:59 at its conclusion.</p> <p>(p) (b) Aurizon Network must notify access holders of the requirements, at the approval date, for any request or notice to schedule the DTP in variation to the ITP from time to time.</p> <p>(q) (c) Aurizon Network, acting reasonably and adhering to the TMDMM's rules, must minimise the length of its departure from the TMDMM.</p>	13.7	<p><b>(2)(a) Disagree.</b> Aurizon Network cannot be obligated to make a variation to a DTP once it is scheduled.</p> <p><b>(2)(b) Disagree.</b> Aurizon Network disagrees with the inclusion of the Supply Chain Group in the Contested Train Path process.</p> <p><b>(2)(c) Agree with amendments.</b> Pooling for the Contested Train Path process does not affect Take or Pay obligations and should be reinstated.</p>

## CDD 13.1 Confidentiality and ring-fencing matters

Whilst Aurizon Network is not opposed to the disclosure requirements, the proposed drafting will create an additional administrative burden for Aurizon Network to prepare reports and manage the various different levels of disclosure across access holders. Aurizon Network would prefer one level of disclosure across all access holders.

Any existing or new reporting must be in line with Aurizon Network's agreed Ringfencing provisions outlined within Part 3 of the 2014DAU.

## CDD 13.2 Strategic Train Plan

While Aurizon Network generally agrees with the proposed contents of the Strategic Train Plan (STP), it requires amendments to clause 2 of Schedule G. Aurizon Network has outlined these below:

### **Estimates of available capacity**

Clause 2(f)(i) in Schedule G of the CDD amended DAU requires the STP contain an estimate of existing capacity based on a number of different metrics (being million tonnes per annum, Train Service Entitlements and Train Paths). The purpose of the STP should not be to provide an estimate of available capacity. Instead, it should be used to demonstrate Aurizon Network's ability to satisfy its contractual obligations. To be clear, this contractual obligation is for TSEs, not millions of tonnes per annum. It is not possible to show available capacity by train path for each month and year. Aurizon Network's reasons for this were set out in its response to the QCA's IDD<sup>82</sup> and these reasons are restated here by reference.

Aurizon Network has significant concerns regarding the value of any outcome of an available capacity process derived from capacity modelling due to the input assumptions and process used (refer Chapter 10). Available capacity in this context assumes a continuation of the cycles operating during the capacity assessment, however this may not reflect the requirements or operational plans of the access seeker. In addition, maintenance plans used in capacity assessment modelling are based on the gross tonne kilometres (GTKs) and net tonne kilometres (NTKs) used in providing access as per access agreements. Additional capacity requires additional maintenance, therefore any outcome will have been assessed against a conservative maintenance regime and may not actually be available.

Aurizon Network believes that there is more value in access seekers using the mechanism available through access requests to understand what is required to support their access needs. This approach would enable a more robust and informative customer specific answer to be provided to each access seeker. This process would be needed if an access seeker sought access in any event via the access application process. Aurizon Network contends that any declaration of estimated available capacity may lead to the misconception by access seekers that there is no requirement to build additional infrastructure and they may well proceed to develop their own project assumptions without testing this through the appropriate access application process.

Aurizon Network does not see the benefit of including in the STP an estimate of available capacity. Aurizon Network does not agree to include an estimate of available capacity in either the STP, MTP, ITP or DTP.

### **Review of STP by independent expert**

Aurizon Network disagrees with CDD 13.2(2)(f), which requires the STP to be reviewed by both an independent expert and then subject to audit by the QCA. Aurizon Network's reasons for this were set out in its response to the QCA's IDD<sup>83</sup> and these reasons are restated here by reference. In summary, an independent expert's scope should be limited to:

- a review of the assumptions used in the STP with reference to contractual commitments; and
- an audit of the mathematical accuracy of any formulas and calculations used in the development of the STP.

Aurizon Network does not consider it necessary to also have the STP audited by the QCA in addition to having an independent expert review. This is a duplication of tasks and not an efficient use of resources.

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<sup>82</sup> Aurizon Network (2015a). s.13.4.1(c) and 13.3, p.191-193.

<sup>83</sup> Aurizon Network (2015a). s.13.4.1(e), p.193.

## CDD 13.3 Master Train Plan

In relation to CDD 13.3, the matters Aurizon Network wishes to note are in relation to:

- planned system outages;
- tracking changes in the Master Train Plan (MTP); and
- communication of changes to the MTP.

### **Planned system outages**

Aurizon Network notes that the QCA agrees with Aurizon Network that planned system outages need to consider the planned system outages of other supply chain participants in preparing the Master Train Plan<sup>84</sup>. However, it considers that an amendment should be made to clause 3 to make this clear.

### **Tracking changes in the Master Train Plan**

Aurizon Network is prepared to accept the QCA's requirements in relation to tracking changes in the MTP, however wishes to highlight the additional resourcing implications and costs, which are not reflected in the current operating cost allowance. Aurizon Network has outlined this within Part 20 – Maximum Allowable Revenue of this response.

### **Communication of changes to the Master Train Plan**

Aurizon Network will seek to keep access holders sufficiently informed about MTP amendments that affect their access rights. Aurizon Network rejects the QCA's requirement to notify and consult with access holders when a change to the MTP does not affect an access holder's access rights (clause 3.2(b) in Schedule G of the CDD amended DAU). The concern the QCA has raised about ensuring all access holders are advised of any capacity becoming available (on a non-transient basis) as a result of a change to the MTP is already communicated to rail operators at the weekly forum.

Aurizon Network also rejects the QCA's requirement for written acknowledgement from access holders on MTP amendments as this will increase its administrative costs in the absence of an automated system. In addition, it is not practically possible to comply with this obligation to give five days written notice ahead of the forum to discuss changes as the timeframe approaches the seven day period prior to Day of Operations. Aurizon Network proposes that the changes will be discussed at the weekly forum and recorded in the minutes.

Aurizon Network also rejects the QCA's requirement to consult with infrastructure service providers and railway managers of private infrastructure who may be affected by changes in the MTP. Aurizon Network proposes to amend the CDD amended DAU to include "who would reasonably be determined may be affected" as the threshold in determining who may be affected.

## CDD 13.4 Intermediate Train Plan

While Aurizon Network supports the full transparency in relation to paths allocated to maintenance and is prepared to accept CDD 13.4, it continues to have some practical concerns with its implementation as this will require system changes. In particular, it is concerned that it will lead to an increase in costs for

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<sup>84</sup> Queensland Competition Authority (2015b). p.228.

which Aurizon Network is currently not compensated. Aurizon Network's reasons for this were set out in its response to the QCA's IDD<sup>85</sup> and these reasons are restated here by reference.

In order to allow the maintenance paths to be displayed in the ITP, Aurizon Network will need to undertake IT changes to amend both the Network Operations Pathing Planner (NOPP) and the ViziRail software (as required).

## CDD 13.5 Train Service Entitlement reconciliation reports

Aurizon Network continues to disagree with CDD 13.5. Its reasons for this were set out in its response to the QCA's IDD<sup>86</sup> and these reasons are restated here by reference.

Reporting on the number of paths planned in the MTP, ITP and DTP and cancelled in the ITP and DTP will be resource intensive and will require changes to IT systems to capture and track this data. Aurizon Network wishes to highlight the significant implementation risk this imposes, noting that these costs are not currently reflected in the MAR, Part 20 of this response.

## CDD 13.6 System Rules governance

Aurizon Network disagrees with CDD 13.6. Its reasons for this were set out in its response to the QCA's IDD<sup>87</sup> and these reasons are restated here by reference.

Aurizon Network does however acknowledge that the evolution of the NMP from the 2013DAU and 2014DAU has resulted in a duplication of a significant proportion of the existing Capricornia System Rules and also the draft Northern Bowen Basin System Rules. To remove this ambiguity and to simplify the governance arrangements for System Rules, Aurizon Network proposes that the System Rules now be included as an Appendix to Schedule G. This would also address the stakeholder feedback on governance arrangements.

## CDD 13.7 Other matters

CDD 13.7 addresses a range of other drafting matters in Schedule G. Aurizon Network has two main outstanding concerns here.

The first are the circumstances where an access holder can request variation to a Daily Train Plan (DTP) once it is scheduled. Aurizon Network cannot accept an obligation to have to make any change, notwithstanding the attempt to limit the scope of such changes. It is essential that it retains its discretion here as network manager.

Second, for reasons set out in its response to the QCA's IDD<sup>88</sup>, which are restated here by reference, Aurizon Network disagrees with the inclusion of the Supply Chain Group in the Contested Train Path principles. This will constrain Aurizon Network's capacity to fulfil its obligations in the efficient operation and management of the network.

Other concerns that Aurizon Network would like to raise are:

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<sup>85</sup> Aurizon Network (2015a). s.13.4.3(b), p.194.

<sup>86</sup> Aurizon Network (2015a). s.13.5, pp.196-197.

<sup>87</sup> Aurizon Network (2015a). s.13.3, pp.197-198.

<sup>88</sup> Aurizon Network (2015a). s.13.4.3 (c), pp.194-195.

1. in relation the Monthly Train Service Entitlement Notice (clause 7.6), it requests that the QCA clarifies:
  - o the intent of the term “used” for the purposes of this report and whether it is intended to be consistent with the term as used in clause 8.2(b). In this regard, Aurizon Network notes that the report will not reconcile as the definitions are not mutually exclusive (e.g. “used” includes “operated”);
  - o the year to date TSE position this is supposed to reconcile to;
2. in scheduling a DTP variation to an ITP, the word “must” should be changed to “may” in order to reflect the intent of this provision;
3. for consistency with other Schedule G reporting requirements, Aurizon Network proposes that Train Paths be replace with System Paths in all measures included in the report; and
4. the QCA has proposed inclusion in the Monthly TSE reconciliation report the reasons for cancellations. Determination of the reasons for cancellations each month is an iterative process that involves consultation with access holders to confirm the reasons for cancellation e.g. mine, port, above rail, below rail. This information is already shared with access holders and their train operators. Aurizon Network therefore agrees to include this information in the Monthly TSE notice, on the basis that the timeframe required to distribute the notice to customers allows for the consultation process at month end to be finalised prior to issuing the notice.

## Other Matters

Aurizon Network is in the process of moving from is historical paper based planning system to computer based. Therefore this areas is subject to evolutionary change over the coming period. Due to the current paper-based system it can make implementation of certain positions difficult and may only be relevant for a small window of time.

Upon implementation of the computer based system, Aurizon Network will be looking to review the level of transparency it provides users of the CQCN to determine and realise any further benefits from the software for the supply chain.

## Chapter 14 – Regulatory Asset Base and Customer Voting

### Summary of Aurizon Network's Position

#### Maintenance of the RAB

Aurizon Network is prepared to accept a number of aspects of the CDD in relation to the maintenance of the RAB. Its primary concern emerging from this section is the QCA's reinstatement of the optimisation provision from the 2010AU (with amendments), which allows the value of the RAB to be reduced in the event of a long term and sustained reduction in demand. Aurizon Network considers that this needs to be considered within the context of its broader context of its exposure to asset stranding risk and has included a separate discussion on this issue in this chapter.

#### Capital expenditure approval

Aurizon Network also has concerns with aspects of the QCA's proposed capital expenditure approval process. Aurizon Network has proposed amendments that will improve the clarity and/or certainty of that process. It also considers it important to have the flexibility to seek pre-approval of the scope and standard of a project separate from costs, which is consistent with its views on the customer voting process, as outlined below.

#### Customer voting

The customer voting process is extremely important, as it is a means of providing regulatory certainty before participants make investment commitments (where the QCA adopts the outcome of the vote). The regulatory risk associated with the inclusion of assets in the RAB is a major consideration for funders of infrastructure.

Aurizon Network has a number of concerns with the CDD. Some of the changes proposed by the QCA, such as requiring that a vote must now always encompass scope, standard and cost, and only at the same time, reflect a material departure from the intent of Aurizon Network's 2014DAU and indeed, the 2010AU. Overall, consistent with a number of other aspects of the CDD amended DAU, including the (related) expansion process, the QCA's proposed customer voting framework reduces necessary flexibility and risks imposing delays to the development process. Indeed, some of the changes risk rendering the process irrelevant, particularly if there is residual uncertainty as to whether the QCA will accept expenditure following a positive customer vote. This will incentivise parties to bypass the vote in an effort to minimise the risk of wasting resources, time and costs.

Recognising that the participants in a voting process are also competitors, whose objectives in relation to an expansion could be in direct conflict, the framework proposed by Aurizon Network in the 2014DAU was designed to reduce the incentive for gaming. This incentive is particularly strong for incumbent producers who have no interest in expanding. Having regard to the requirements of section 138(2) of the QCA Act, Aurizon Network considers that the QCA has given too much weight to the interests of existing access holders (or end users), at the expense of access seekers and potential new entrants (whose interests are not always represented in the undertaking review process). Aurizon Network considers that its 2014DAU proposal achieved a more appropriate balance of interests, which is necessary in order to support the growth and development of the CQCR and hence directly promote the Objects of Part 5 of the QCA Act.

#### Proposed Redrafting of Schedule E

To assist the QCA in reaching its Final Decision, Aurizon Network will provide a marked up version of the QCA's Schedule E, which, if accepted by the QCA, would resolve the issues set out in this section.

Table 14.1 – QCA Consolidated Draft Decision

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(1) After considering Aurizon Network's proposal for maintaining and adjusting the RAB, reporting on capital expenditure and the RAB roll-forward and equity raising costs, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p>	<p>14.1</p>	<p><b>(2)(a) Disagree.</b> Propose reinstatement of Aurizon Network's original drafting that clarifies an asset disposal excludes any assets associated with renewals.</p>
<p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is for Aurizon Network to be required to:</p>		<p><b>(2)(b)(i) Disagree.</b> This</p> <ul style="list-style-type: none"> <li>• leaves Aurizon Network uncompensated for asset stranding risk;</li> <li>• does not lead to a net present value neutral outcome for Aurizon Network, rather a negative net present value outcome;</li> <li>• does not provide potential investors in the CQCN with an appropriate level of confidence that they will receive a prudent and efficient investment back through time.</li> </ul>
<p>(r) for asset disposals:</p> <p>(i) remove the value of the asset from the RAB</p> <p>(ii) be able to seek our approval for any alternate approach to account for asset disposals</p>		<p><b>(2)(b)(ii) Agree with amendments.</b> Aurizon Network is prepared to agree to this, subject to the QCA's incorporation of its proposed drafting to:</p>
<p>(s) for adjusting the RAB:</p> <p>(i) reinstate demand deterioration as a reason for reducing the RAB, only where we determine that demand deterioration is long-term and sustained and include a process to reset (increase) the RAB if it can demonstrate demand has increased sufficiently to justify it</p>		<ul style="list-style-type: none"> <li>• include a process to the value of the RAB to be increased if asset condition subsequently improves</li> <li>• clarify that long term and sustained deterioration is not the case where Aurizon Network has a credible plan to address deterioration.</li> </ul>
<p>(ii) reinstate the link to condition based assessment as a reason for reducing the RAB in certain circumstances</p> <p>(iii) include a QCA consultation process where we are considering adjusting the value of the RAB</p>		<p><b>(2)(b)(iii) Agree with amendments.</b> Aurizon Network is prepared to agree to this, subject to the QCA's approval of its proposed drafting amendments.</p>
<p>(t) for the capital expenditure and RAB reports:</p>		<p><b>(2)(c)(i) Agree.</b></p>
<p>(i) combine the requirements for reporting into one</p> <p>(ii) include a process for us to approve RAB roll-forwards as part of the reporting requirements</p>		<p><b>(2)(c)(ii) Agree with amendments.</b> Aurizon Network is prepared to agree to this, subject to clarification that the QCA must approve the RAB roll forward if it is satisfied that Aurizon Network has complied with the principles set out in clause 1.1 of Schedule E.</p>
<p>(iii) include timeframes for providing reports and information to be contained in them</p>		<p><b>(2)(c)(iii) Agree.</b></p>
		<p><b>(2)(c)(iv) Agree with amendments.</b> Aurizon Network is prepared to agree to this, subject to the QCA's approval of Aurizon Network's proposed drafting amendments. Capital Expenditure and RAB Reports should be subject to confidentiality where appropriate.</p>
		<p><b>(2)(d) Agree with amendments.</b> Aurizon Network is prepared to agree to this, subject to the QCA's approval of Aurizon Network's proposed drafting amendment to include</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(iv) remove provisions for keeping information in these reports confidential</p> <p>(u) for equity-raising costs—seek inclusion of costs into the RAB on a case by case basis, as set out in our CDD amended DAU.</p>		<p>reference to the AER's equity raising cost approach.</p>
<p>(1) After considering Aurizon Network's proposed capital expenditure approval process in the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is as indicated in our CDD amended DAU and consistent with our proposed approach to capital expenditure approvals as detailed in our initial draft decision, and in Schedule E of our CDD amended DAU.</p>	<p>14.2</p>	<p><b>Disagree.</b> Aurizon Network has proposed amendments to address a number of issues, including, but not limited to:</p> <ul style="list-style-type: none"> <li>• permit pre-approvals of standard and scope, separate from costs;</li> <li>• reinstate the criteria used to assess prudence of capital expenditure as per Aurizon Network's 2014 DAU;</li> <li>• include clarification that an assessment of prudence of capital expenditure is limited to information available, or reasonably available, at the time of making the decision to incur the capital expenditure;</li> <li>• reinstate the ability for Aurizon Network to claim any capital expenditure for concept studies, pre-feasibility studies and feasibility studies in respect of the project that has not proceed to execution;</li> <li>• clarify that capital approvals are not limited to assets that are "used by Aurizon Network to provide Train Services";</li> <li>• clarify that only funding access seekers or funding customers can required Aurizon Network to submit a capital expenditure claim;</li> <li>• replace "may" with "must" in circumstances where it should have used "must".</li> </ul>
<p>(1) Our consolidated draft decision is to refuse to approve Aurizon Network's AMP proposals in the 2014 DAU.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is, as we have indicated in our CDD amended DAU, to allow Aurizon Network to:</p> <p>(a) provide the QCA with an AMP</p> <p>(b) request that the QCA accept the capital expenditure for asset replacement and renewal in the AMP as prudent and efficient. Any such request will be subject to the capital expenditure approval process set out in the undertaking.</p>	<p>14.3</p>	<p><b>Agree with amendments.</b> Aurizon Network is prepared to agree to this, subject to the QCA's approval of Aurizon Network's proposed amendment to ensure the non-disclosure of information if Aurizon Network or another party claims confidentiality over the information under the QCA Act.</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(1) After reviewing Aurizon Network's proposed approach with respect to the purpose and application of the customer voting process in the 2014 DAU, our consolidated draft decision is to refuse to approve the proposal.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is as we have indicated in our CDD amended DAU, as follows:</p> <p>(c) Aurizon Network must include a process that encompasses standard, scope, cost and the capacity implications of any capital project, rather than just scope.</p> <p>(d) The voting proposal must be in relation to either:</p> <p>(i) the prudence and efficiency of the scope, standard and cost, and identify the capacity implications of the capital project</p> <p>(ii) a material change to scope, standard, cost or capacity implications of a capital project previously accepted by interested participants.</p> <p>(e) There should be a requirement that a customer vote can only take place for a capital project for which there is a completed feasibility study, the results of which have been provided to the QCA and interested participants.</p> <p>(f) Aurizon Network should promptly notify the QCA if it is seeking a vote and inform the QCA of the outcome of that vote.</p> <p>(g) An access seeker (or its customer), an expansion funder or interested participant should have the ability to require Aurizon Network to undertake a vote for a capital project for which a feasibility study exists.</p> <p>(h) If interested participants accept a voting proposal, Aurizon Network should promptly seek QCA pre-approval of the relevant capital expenditure.</p>	14.4	<p><b>(2)(a) Disagree.</b> There should be flexibility to undertake voting on scope alone.</p> <p><b>(2)(b)(i) Disagree.</b> There should be flexibility to undertake voting on scope alone.</p> <p><b>(2)(b)(ii) Disagree.</b> There should be flexibility to undertake voting on scope alone.</p> <p><b>(2)(c) Disagree.</b> There should be flexibility to do earlier. A late vote has potential to delay projects or weaken the benefit of a vote.</p> <p><b>(2)(d) Agree.</b></p> <p><b>(2)(e) Disagree.</b> Only funders should be able to require this.</p> <p><b>(2)(f) Disagree.</b> There should be flexibility of whether to seek pre-approval or not.</p>
<p>(1) After reviewing Aurizon Network's proposed approach to the identification of Interested Participants in the 2014 DAU,</p>	14.5	<p><b>(2)(a) Disagree.</b> Expanding the network does not impact on any existing contracts or the capacity entitlements contained in those contracts. There may be implications in relation to the allocation of costs, which is addressed</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>our consolidated draft decision is to refuse to approve the proposal.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is to:</p> <p>(i) include in the definition of 'interested participants' customers, access holders and access seekers without customers where the proposed capital expenditure will impact on the person's contracted capacity or train paths</p> <p>(j) require any person who believes they are entitled to be an interested participant but has not been classified as such, to notify the QCA as well as Aurizon Network</p> <p>(k) require Aurizon Network to promptly notify the person and the QCA as to whether or not they will be treated as an interested participant.</p> <p>(3) The detailed drafting to reflect our positions is provided in the CDD amended DAU attached to this consolidated draft decision.</p>		<p>separately under the expansion pricing framework.</p> <p><b>(2)(b) Agree.</b></p> <p><b>(2)(c) Agree.</b></p>
<p>(1) Our consolidated draft decision is to accept Aurizon Network's proposed approach to the identification of interested participants voting rights, subject to minor amendments.</p>	14.6	<b>Agree.</b>
<p>(1) After reviewing Aurizon Network's proposed approach to the voting acceptance process in the 2014 DAU, our consolidated draft decision is to refuse to approve the proposal.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is as we have indicated in our CDD amended DAU to:</p> <p>(l) delete clauses 8.13.5(d),(f) and (g) of the 2014 DAU</p> <p>(m) require that if an interested participant votes 'no' they must provide reasons for that vote in sufficient detail that the QCA may understand their reasons</p> <p>(n) require Aurizon Network, when providing information, conducting forums and engaging in discussions with interested participants in relation to a voting proposal at the request of interested participants, to</p>	14.7	<p><b>(2)(a) Disagree.</b> There should be clarity around how votes with insufficient detail or inappropriate reasons are dealt with and in a manner that deters any perceived incentives to game the process.</p> <p><b>(2)(b) Agree.</b></p> <p><b>(2)(c) Disagree.</b> Aurizon Network should not be required to do whatever is sought regardless of cost.</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
adopt a 'best endeavours' approach.		
<p>(1) After considering Aurizon Network's proposed approach to information provision for Interested Participants in the 2014 DAU, our consolidated draft decision is to refuse to approve the proposal.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is as we have indicated in our CDD amended DAU:</p> <p>(o) Aurizon Network must make available to interested participants and the QCA information on the relevant capital expenditure project, including the report prepared as a result of the feasibility study for the relevant capital expenditure project</p> <p>(p) Aurizon Network may require an interested participant to sign a confidentiality agreement substantially in the form set out in Schedule I prior to providing information in relation to a customer vote on a voting proposal.</p>	14.8	<p><b>(2)(a) Disagree.</b> There should be flexibility to do earlier than completion of feasibility.</p> <p><b>(2)(b) Disagree.</b> The other Interested Participants (in the QCA's definition) are among the parties that an access seeker is likely to not want to be able to see confidential information that is included in the feasibility study. An obligation not to pass it onto others does not overcome their concerns.</p>
<p>(1) After considering Aurizon Network's proposed approach for compliance with, and audit of, the customer voting process in the 2014 DAU, we refuse to approve the proposal.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU, is in the manner we have indicated in our IDD amended DAU; that is, to provide for:</p> <p>(q) removal of clauses 8.13.7(b),(f) and (g) from the 2014 DAU</p> <p>(r) a requirement for interested participants to notify Aurizon Network and the QCA, in writing, of any concerns regarding non-compliance with the voting process including providing reasons or other information in support of those concerns prior to the end of the voting period</p> <p>(s) a requirement for Aurizon Network to take whatever action is reasonably required to comply with the customer voting process in response to such concerns</p> <p>(t) a requirement for Aurizon Network to redo the voting process if the</p>	14.9	<p><b>(2)(a) Agree.</b></p> <p><b>(2)(b) Agree.</b></p> <p><b>(2)(c) Agree.</b></p> <p><b>(2)(d) Disagree.</b> Depending on the outcome of the vote and the nature of the flaws identified by the auditor, it may be unnecessary to redo the entire vote. This could also have MAR implications as it will result in Aurizon Network incurring additional costs.</p> <p><b>(2)(e) Disagree.</b> This devalues the voting process – if the QCA is not obliged to accept its outcome then the preapproval process is expected to be the preferred initial course of action.</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(u) auditor identifies a flaw in the voting process clarification that an accepted voting proposal that successfully passes an audit does not infer QCA 'acceptance' that a capital expenditure project is prudent and efficient.		

## Aurizon Network's asset stranding risk

### Summary of Aurizon Network's Position

As the owner of some 2,600km of dedicated coal network infrastructure, Aurizon Network is a major stakeholder in the CQCR. While long-term volume growth expectations have recently slowed (with Aurizon's expectations aligning with International Energy Agency forecasts), it remains confident in the long-term fundamentals underpinning the Queensland export coal industry.

All industry stakeholders, including the QCA, acknowledge the challenges presented by the current market environment. While Aurizon Network has always been exposed to asset stranding risk, it is only in these difficult market conditions that the true nature of this risk becomes apparent. Effectively managing asset stranding risk requires a long-term view. It is too late to address asset stranding risk if and when it becomes more likely, as the mechanisms that can practically be used to address the risk could be more limited. A proactive and flexible approach is needed.

The current regulatory framework provides very limited means of mitigating this risk, which Aurizon Network is not otherwise compensated for in the cashflows or the regulated WACC. A number of decisions in the CDD will exacerbate this risk, either by further reducing Aurizon Network's ability to effectively manage its asset stranding risk or increasing its exposure to that risk (such as revenue deferrals). This is unacceptable to Aurizon Network.

The ability to address stranding risk in such a complex and dynamic environment requires an appropriate degree of commercial and regulatory flexibility, having regard to the requirements of the QCA Act. There are a number of mechanisms that could be considered to enable Aurizon Network to ensure it can recover its efficient costs, while appropriately balancing the interests of system users including aligning the economic life of the network with the average life of the mines it services, socialisation of costs and cashflow compensation (similar to self-insurance). However, given the significance and scope of these issues, in the interests of the timely completion of the UT4 process Aurizon Network has not sought to propose in detail how it should be addressed in this response to the CDD. It intends to do this following the conclusion of the UT4 review, which will include consultation with the QCA and stakeholders.

Stranding risk is the main threat to Aurizon Network's ability to recover its efficient costs, include a return on capital, which is a requirement of the QCA Act (section 168A(a)). Ultimately, this will flow through to Aurizon Network's investment incentives, which need to be maintained in order to promote efficient investment in the network and therefore support the future growth and development of the CQCR (consistent with the object of Part 5 of the QCA Act). Addressing stranding risk is also in the interests of access seekers and holders, who may otherwise be affected by a decrease in network investment and poorer operational performance.

In the short-term, Aurizon Network has identified a number of items in the CDD which should be addressed to mitigate asset stranding risk. Aurizon Network submits that it is imperative that the QCA considers Aurizon Network's response to these decisions in this broader context.

In summary, the key issues in the CDD include:

- The QCA's reinstatement of clause 1.2(b) of Schedule E (a former UT3 clause), which permits the QCA to optimise the RAB where demand has "deteriorated to such an extent that regulated prices on an unoptimised asset would result in a further decline in demand". In circumstances where:
  - Aurizon Network has not been compensated through cashflow or WACC for asset stranding risk; and
  - is exposed to significant regulatory risk as to whether any future uplift in MAR will be approved,

Aurizon Network submits inclusion of this former UT3 clause is contrary to the pricing principles, and the object of Part 5 of the QCA Act, given the potential impact of a RAB optimisation of this type on Aurizon Network's ability and incentive to invest in its network. It is also contrary to the long term interests of end users, given the likely impact on investment, and potential effect on future WACC or cash flow allowances.

If the clause is retained, it is imperative that the clause is modified, to ensure that it operates only as a last resort, where all other pricing mechanisms (for example a change to the way in which existing regulated prices are established) have been exhausted. Aurizon Network will submit drafting to the QCA for consideration in this regard, and is happy to discuss this issue further with the QCA.

- The CDD's current bias against socialisation from the expansion pricing framework, which Aurizon Network submits should be reversed (refer Chapter 16).
- The QCA's decision to defer WIRP revenues without a sunset date, which Aurizon Network submits should be reversed (refer Chapters 17 and 18).
- The QCA's amendments to Part 6 and Schedule F which reduce Aurizon Network's flexibility to respond promptly and pro-actively through pricing mechanisms to prevent a demand spiral well prior to its commencement, which Aurizon Network submits should be reversed (refer Chapters 16 and 17).
- The QCA's amendment of security provisions in the access agreements. Aurizon Network submits these provisions should be reviewed to ensure they give Aurizon Network the flexibility to appropriately and effectively address counterparty risk in its access agreements (refer Chapter 8).
- The QCA's decision not to reinstate UT3 provisions which allow Aurizon Network to reorder its capacity queue to give preference to longer term contracts. Aurizon Network submits these provisions should be reinstated (refer Chapter 11).
- The QCA's decision to impose an access conditions regime, which limits Aurizon Network's ability to put in place measures to address stranding risks within its access contracts. Aurizon Network submits this decision should be reversed (refer Chapter 16).

It is imperative that the QCA consider and address these issues in its Final Decision, and that it does so against the broader context of addressing asset stranding risk.

For the future, post-approval of UT4, Aurizon Network considers that a broader range of options will need to be considered including alternate depreciation schedules, stronger take or pay provisions, socialisation of network costs across a broader pool of users and a review of compensation for asset stranding risks. This will be the subject of a future regulatory engagement involving consultation with all stakeholders.

Aurizon Network's concerns are set out in more detail below.

## Overview

### The changing market environment

Asset stranding is the risk that an asset owner is unable to recover a full return on, and of, the capital it has invested. For an infrastructure owner such as Aurizon Network, the primary cause of this would be a long term and sustained reduction in demand for its network services.

Aurizon Network has always been exposed to asset stranding risk. However, the material change in market conditions that has occurred since UT3 was approved in 2010, has highlighted how significant this exposure has become, noting the significant new investment that has been undertaken in response to the coal boom that emerged in the last decade. The recent reduction in coal prices has already resulted in cash operating losses or even mine closures for a number of mining companies.

Recently, the QRC has commissioned a report from Wood Mackenzie to provide an update on the current position of Queensland mining industry in the global market. The report confirms the tough market condition for Queensland coal producers. Specifically, the QRC wrote:

*One-third of all our coal mines in Queensland are running at a loss – in other words they are not earning enough revenue to cover their cash costs. Breaking that down further, more than half of Queensland's thermal coal mines (producing coal for power generation) and one in four of our metallurgical coal mines (producing coal for steel making) are not covering their cash costs.<sup>89</sup>*

The revenue cap regime and mechanisms such as long-term contracts and take-or-pay could be seen as reducing Aurizon Network's exposure to asset stranding risk. In practice, however, their effectiveness is practically limited, noting that: (1) the revenue cap only provides protection for the length of the regulatory period; and (2) take or pay only provides protection for the term of the relevant contract and then only while the counterparty remains solvent. The nature of railway assets is that they are built for periods longer than these two timeframes.

Moody's recent credit rating review of Aurizon Holdings highlights this issue:<sup>90</sup>

*... we believe that both the take-or-pay component of Holdings' haulage operations and Network's regulated returns for provision of track access will be increasingly subject to higher volatility due to potential counterparty failure or a failure to renew contracts.*

...

*However, other participants in the coal logistics infrastructure chain, such as the dedicated coal terminals, also rely on take-or-pay contracts and will likely similarly seek to increase their tariffs to remaining miners in the event of counterparty failure. Such an event will result in a generalized level of increased transport costs for remaining mines which they may not be able to afford, and therefore elevates the uncertainty around Aurizon Network's ability to fully recapture lost revenue.*

DBCT Management also shares these concerns, as set out in its 2016 DAU submission.<sup>91</sup> Aurizon Network further notes the material deterioration in the creditworthiness of DBCT's customers that led to the downgrade of DBCT Finance's credit rating to BBB by S&P, where S&P acknowledged that DBCT's

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<sup>89</sup> Queensland Resources Council (2015). QRC State of the Sector December Quarter 2015, p. 1.

<sup>90</sup> Moody's Investors Service (2016). Moody's Reviews Aurizon Holdings and Aurizon Network for Possible Downgrade.

<sup>91</sup> DBCT Management (2015). 2016 DAU Submission, 9 October.

performance is “inextricably linked to the long-term sustainability of the Bowen Basin and global metallurgical coal demand.”<sup>92</sup> As the owner of the dedicated rail network servicing the CQCR, Aurizon Network considers that its performance is similarly “inextricably linked” to the export coal industry.

#### Aurizon Network’s concerns with the CDD

The export coal market has and always will be inherently volatile. While Aurizon Network remains confident in the long-term outlook for the industry<sup>93</sup>, it considers that the recent events are symptomatic of a ‘structural shift’ in Aurizon Network’s risk profile, rather than just another downturn in the cycle. Asset stranding risk has become a key concern for Aurizon Network and it is one that Aurizon Network strongly urges the QCA to take account of when making its Final Decision on the 2014 DAU.

Aurizon Network notes the QCA has not responded directly to concerns surrounding asset stranding risk contained in its response to the QCA’s IDD<sup>94</sup>. The concerns included:

- asset stranding risk not being compensated in WACC
- the implicit regulatory assumption behind the zero Net Present Value (NPV)
- the consequence of asset write-downs.

Aurizon Network also considers that there are a number of aspects of the CDD that either prevent it from mitigating its asset stranding risk or further increase its exposure (as explained in the summary section at the start of this submission).

Denying Aurizon Network reasonable and efficient means of addressing its exposure to asset stranding risk is inconsistent with section 168A(a), which requires it to recover its efficient costs, including a return on and of capital. The re-inclusion of the demand-based optimisation clause provides the QCA with a clear mechanism to prevent Aurizon Network from recovering its efficient costs. Ultimately, this will flow through to Aurizon Network’s investment incentives. Even if the QCA only sought to do this for an isolated part of the network infrastructure, this would have a significant and adverse impact on Aurizon Network’s confidence to undertake *any* future network investment, whether that be to accommodate growth or maintain existing service levels via renewals. This is in direct conflict with section 69E of the QCA Act.

The following sections will discuss these concerns in more detail.

#### **Asset stranding risk and the regulatory framework**

Apart from exposing Aurizon Network to the ultimate risk of optimisation under Schedule E, the regulatory framework provides very limited means of either mitigating, or providing compensation for, Aurizon Network’s exposure to asset stranding risk.

If standard risk management principles are applied, the most efficient allocation approach is where the party that is best able to manage the risk bears the risk. Aurizon Network has little if any ability to influence the demand for its coal network services, which is ultimately driven by conditions in world markets (and recognising that access charges comprise only a relatively small proportion of producers’ total costs). Producers have a greater ability to influence this although it is acknowledged that Australian export coal producers are largely price takers in the world market.

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<sup>92</sup> S&P in DBCT Management (2015). p.13.

<sup>93</sup> For example, refer:

<http://www.aurizon.com.au/~media/aurizon/files/sustainability/sustainability%20reports/fy%202014%20sustainability%20report.ashx>

<sup>94</sup> Aurizon Network (2015a). 2014 Draft Access Undertaking: Aurizon Network Response to Queensland Competition Authority’s Draft Decision on Policy and Pricing Principles. Refer Appendix 5.

However, what this clearly suggests is that at minimum, asset stranding risk should be shared. It is neither reasonable nor efficient to expect Aurizon Network to bear the majority of this risk without compensation, as is the case now. Recognising the limited mitigants available under the regulatory framework, this section briefly reviews some of the key issues that emerge from a regulatory perspective.

#### WACC and asset stranding risk

Asset stranding risk is asymmetric, that is, investors in regulated assets do not obtain any upside potential but bear the full downside risk. The majority of Australian regulators, including the QCA, use the Capital Asset Pricing Model (CAPM) to calculate the cost of equity for WACC. The CAPM builds on the Markowitz model, which assumes asset returns are only characterised by mean and variance. Implicitly, the CAPM assumes that returns are multivariate normally distributed. The asymmetric nature of asset stranding risk means there is no compensation for investors of regulated companies through CAPM. This is further supported by the fact that asset stranding risk contains idiosyncratic risk.<sup>95</sup>

Aurizon Network notes the QCA shares Aurizon Network's view that a WACC derived from CAPM does not compensate investors for asset stranding risk. There are numerous examples in previous regulatory determinations and papers. For example, in its Discussion Paper on the Form of Regulation, the QCA said:<sup>96</sup>

*The implication of this assumption [normal distribution of return] is that the CAPM does not compensate investors for 'asymmetric' risk. In a regulatory context, asymmetric risks include asset stranding and exposure to unlikely (and typically uninsurable) events such as certain natural disasters.*

#### Regulatory assumption behind zero NPV

The potential for asset stranding, which could be crystallised by the QCA's demand optimisation provision in Schedule E, is ultimately inconsistent with the zero NPV principle that the QCA firmly applies. The zero NPV principle does not contemplate the removal of assets from the RAB.

From an investor's perspective, the cash flow received each year comprises the return on capital and return of capital. The NPV of the investment for the investor is:

$$NPV = -\text{Capital Invested} + \sum_{t=1}^n \frac{\text{return of capital}_t + \text{return on capital}_t}{(1+r)^t}$$

The adoption of the zero NPV principle assumes the regulated entity is always able to recover its full return on and of capital. This is an unrealistic assumption in Aurizon Network's case, particularly given its exposure to asset stranding risk.

A simple example illustrates this point. Assume the following:

- capital Invested: \$1000

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<sup>95</sup> A more detailed discussion is contained in Section 4.1 of the Appendix 5 to Aurizon Network's response submission to the Pricing and Policy Draft Decision.

<sup>96</sup> Queensland Competition Authority (2012). Discussion Paper: Risk and the Form of Regulation, p.2. Reference is also made to the following documents published by the QCA: (1) Draft Decision: Dalrymple Bay Coal Terminal Draft Access Undertaking, p.192; (2) Draft Decision: QR Network's 2010DAU - Tariffs and Schedule F, p.10; (3) Final Decision: QR Network 2010 Access Undertaking, p.108; (4) Discussion Paper: Risk and the Form of Regulation, p.2; (5) Discussion Paper: Workshop on the Electric Infrastructure Tariff (AT5), p.3; (6) Draft Decision: Aurizon Network 2013 Blackwater Electric Traction Pricing Draft Amending Access Undertaking, p. 38.

- straight Line Depreciation: 10 Years
- WACC: 10%
- three alternative capital recovery scenarios:
  - asset stranded at year 5
  - asset stranded at year 8
  - no asset stranding.

The NPV outcomes are shown in the following table.

**Table 14.2 - NPV Scenarios with Stranded Asset**

Year	1	2	3	4	5	6	7	8	9	10
Return on Capital	100	90	80	70	60	50	40	30	20	10
Return of Capital	100	100	100	100	100	100	100	100	100	100
Total Cash Flow	200	190	180	170	160	150	140	130	120	110
NPV (Asset stranded at t=5)	-310.5									
NPV (Asset stranded at t=8)	-93.3									
NPV (No asset stranding)	0									

As shown above, the only scenario where investors can achieve a zero NPV is when there is no asset stranding, which will only be known at the end of year 10.

This problem was recognised by the QCA in a workshop paper on the Blackwater Electric Traction Pricing DAAU:<sup>97</sup>

*The weighted average cost of capital for Aurizon Network is currently set on the assumption that assets will only be optimised once, at the time the asset enters the asset base... If the current approach is changed to allow for subsequent optimisation of the asset base, the WACC may have to be reviewed (upward).*

The reason this issue needs to be specifically addressed in this context is due to the return truncation resulting from regulation. This was recognised by the Productivity Commission (PC) in its review of the National Access Regime:<sup>98</sup>

*Asymmetric truncation is expected to expropriate above-normal returns to infrastructure service providers but not compensate for below-normal returns, resulting in the investor's expected rate of return being driven lower than their hurdle rate of return – deterring or delaying investment.*

<sup>97</sup> Queensland Competition Authority (2013). Discussion Paper: Workshop on the Electric Infrastructure Tariff (AT5), p. 3.

<sup>98</sup> Productivity Commission (2013). Productivity Commission Inquiry Report – National Access Regime, p. 228.

In an unregulated setting, investors are exposed to both sides of the return distribution. The probability-weighted average of the future expected outcomes (which could be that asset stranding either does or does not occur) will mean that the ex-ante expected return should (appropriately) compensate for the risk. However, for regulated entities, the highest possible return an investor can achieve is the regulated WACC, which does not currently include compensation for asset stranding. If asset stranding occurs, the actual return will be less than the WACC and the outcome will be NPV negative.

#### Consequences of a RAB reduction

The practical consequences of an asset stranding event – which could be crystallised if the QCA sought to make a determination under clause 1.2(b) of Schedule E – are as follows.

In practice, if Aurizon Network was subject to asset stranding – even if this was only on part of its network – investors' required returns will increase, as Aurizon Network will be regarded as a more risky investment. This in turn should flow through to Aurizon Network's regulated tariffs. However, even though it is entitled to be compensated for this return under section 168A(a), in practice, having regard to the theoretical approach applied by the QCA based on the CAPM, Aurizon Network has no confidence that its allowed return would be increased in this way (and expects it would be strongly resisted by stakeholders). As a consequence, Aurizon Network will face difficulties in raising capital to fund future investments. Any efforts to reduce the RAB would likely lead to a significant distortion or long-term reduction in network investment.<sup>99</sup> If a regulated infrastructure provider considers that it has a material exposure to the risk of a RAB reduction after an investment has been accepted into that RAB, this will materially reduce its investment incentives.

A RAB reduction will also affect the nature of the investment. For example, the risk of future asset stranding may induce regulated entities to prefer investing in shorter life assets, or assets that require higher levels of operating expense rather than capital costs.<sup>100</sup> In its submission to Senate Standing Committee's inquiry into electricity network companies, the Australian Energy Regulator (AER) noted:<sup>101</sup>

*We would caution against an asset write down policy. Electricity network assets have long economic lives, in some cases of 30-40 years. Changing the regulatory treatment of these investments after a few years may create significant sovereign risk issues for network businesses and creates disincentives for future efficient investment.*

In summary, a reduction of the RAB will overturn the regulatory assumption that optimisation for assets will only occur once upon entering the RAB. This would affect investors' confidence in the recovery of investments with long economic lives. The required increase in returns by investors as well as the distortion in capital investments suggest that a RAB reduction will not be a viable solution to addressing a long-term and sustained deterioration in demand.

The QCA's ability to subsequently increase the RAB should demand increase does not address this issue. Firstly, demand may not increase. Secondly, given likely stakeholder resistance to a RAB uplift, there must be substantial regulatory risk that an uplift will not be approved. Thirdly, there is no compensation for the period in which the RAB is reduced. Finally, the impact on investor confidence will be triggered immediately upon the reduction, with a resulting impact on Aurizon Network's ability to raise capital to invest in its network.

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<sup>99</sup> Energy Networks Association (2014). Written-down Value? Assessing Proposals for Electricity Network Write-downs, p. 19.

<sup>100</sup> Energy Networks Association (2014). p. 19.

<sup>101</sup> Australian Energy Regulator (2014). Submission to Senate Standing Committee Inquiry into Electricity Network Companies, p. 10.

## The QCA's CDD

As noted above, there are a number of aspects of the QCA's CDD that either limit or preclude its ability to mitigate asset stranding risk or increase its exposure to that risk.

### Revenue deferrals

An example of the latter is its proposal to defer significant WIRP revenues on new investments. While Aurizon Network may be willing to consider mechanisms such as revenue deferrals or alternative depreciation profiles in appropriate circumstances, it is generally reluctant to do so if it considers that this would expose it to an unacceptable level of risk (particularly revenue deferrals with no defined end date). It considers that any such mechanisms should only be proposed by Aurizon Network as part of consideration of a range of feasible alternatives and only applied with its agreement. It would also be unwilling to agree to this for an unspecified or indefinite term.

### Socialisation

Aurizon Network believes that where feasible, socialisation within or across systems could be an efficient and effective solution to a long-term and sustained reduction in demand. However, Aurizon Network notes the QCA has already commented that ex post socialisation of stranded assets may not provide the correct incentive for Aurizon Network, specifically:<sup>102</sup>

*With respect to asset stranding risk issues raised by Aurizon Network, we are not of the view that an ex post mechanism is the appropriate way to deal with this risk. Providing infrastructure funders with such a mechanism has the potential to reduce the incentive for infrastructure funders to fully take account of the asset stranding risk associated with an investment project. We consider that this does not promote the economically efficient investment in infrastructure, and thus does not align with the object of Part 5 of the QCA Act.*

Aurizon Network strongly disagrees with this statement. At least in its case, as outlined above, the mechanisms that it can apply to mitigate asset stranding risk are extremely limited. In the first instance, it is subject to a highly prescriptive expansion pricing framework which places significant constraints on Aurizon Network's ability to socialise costs (with GAPE and WIRP both presenting clear examples of this in this CDD). Its ability to apply other mechanisms, such as accelerated depreciation, are also subject to QCA approval.

Practically, the regulatory uncertainty that Aurizon Network faces in looking to apply such mechanisms is extremely high. In the absence of any such mechanisms, Aurizon Network's investors are ultimately left bearing the risk, for which they are not compensated, especially if Aurizon Network is only permitted to earn a regulated CAPM-derived WACC.

### RAB reduction vs optimisation

As noted previously, one of Aurizon Network's key concerns with the CDD is the QCA's reinstatement of the demand-based optimisation provision in clause 1.2(b) of Schedule E in the CDD amended DAU. In the CDD the QCA stated that a reduction in RAB is unlike asset optimisation as Aurizon Network has the opportunity to restore the optimised amount later:<sup>103</sup>

*We do not agree that reducing the RAB in the circumstances of deteriorating demand goes against the optimisation principle or that the annual reset is an appropriate mechanism for making an adjustment. Unlike the optimisation arrangements, there is a scope for any asset reduction in this*

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<sup>102</sup> Queensland Competition Authority (2015b). p.262.

<sup>103</sup> Queensland Competition Authority (2015b). p. 261.

*instance to be re-included in the RAB should they be required to meet future needs. Therefore, it is not so much optimising the asset, but reducing it to address demand issues, with a view to resetting at a later date when the circumstances permit.*

Aurizon Network strongly disagrees with this statement. It does optimise the asset as it prevents Aurizon Network from recovering the costs of that asset. Aurizon Network can have no confidence that circumstances will subsequently permit full re-inclusion of that optimised asset, or when that might occur.

Even with some possibility that demand does recover in the future, it is unlikely that Aurizon Network could recover all of its foregone revenue and associated opportunity costs. This is because a removal of any asset value from the RAB will require escalation to compensate Aurizon Network for its foregone returns. This arrangement is consistent with the QCA's treatment for timing issues associated with revenue recovery, for example, the revenue cap adjustment.

This escalation, however, could require a significant tariff increase, which may not be sustainable for the remaining users of the network. For example, a \$100 reduction in RAB, if escalated at WACC of 10%, will become \$161 in 5 years' time, \$259 in 10 years' time and \$673 in 20 years' time. Aurizon Network therefore does not consider there to be any difference between a RAB reduction (including reinstatement) and RAB optimisation given it is highly unlikely that it will be able to recoup the full return on and of capital that it is entitled to recover under the QCA Act.

In summary, Aurizon Network does not consider that the clause in Schedule E is appropriate to address asset stranding risks, because it:

- disproportionately allocates the risks of asset stranding entirely to Aurizon Network, which is the party least well placed to manage such risks; and
- does not require the QCA to consider other alternative feasible regulatory pricing options, such as socialisation of volume risk across a broader pool of access holders (for example, across all users of the CQCN), prior to its implementation.

Ultimately, optimisation is inconsistent with the pricing principles in section 168A(a) of the QCA Act. If the RAB were optimised to address falling demand, Aurizon Network would be unable to generate revenue for the services that is at least enough to meet its efficient cost, including a return on capital. For the reasons outlined above, this risk is not otherwise compensated via the WACC. This in turn would have a material and adverse impact on Aurizon Network's investment incentives, which undermines section 69E of the QCA Act.

## **Conclusions and way forward**

Asset stranding risk is a significant and complex issue that has potentially wide-reaching implications across Aurizon Network's commercial and regulatory framework. There are a number of mechanisms that could be considered, including aligning the economic life of the network with the average life of the mines it services, socialisation of costs and cashflow compensation (similar to self-insurance).

In the interests of the timely completion of the UT4 process, Aurizon Network does not propose to canvass all of these options as part of the UT4 process. It will do so as part of a separate regulatory engagement, at which time it will consult with all stakeholders.

That said, there are key aspects of the QCA's CDD that have increased Aurizon Network's asset stranding risks or reduced its ability to mitigate those risks. The QCA can, and should, address these issues now as part of the UT4 review.

Specifically, in respect of its final decision on UT4, the QCA should

- Reverse its decision to reinstate 1.2(b) of Schedule E, which permits the QCA to optimise the RAB where demand has deteriorated to such an extent that regulated prices would result in a further decline in demand. In circumstances where Aurizon Network:
  - has not been compensated through cashflow or WACC for asset stranding risk; and
  - is exposed to significant regulatory risk as to whether any future uplift in MAR will be approved,

Aurizon Network submits inclusion of this former UT3 clause is contrary to the pricing principles, and the object of Part 5 of the QCA Act, given the potential impact of a RAB optimisation in these circumstances on Aurizon Network's ability and incentive to invest in its network. It may also be contrary to the interests of end users, given the likely impact on investment, and potential effect on future WACC or cash flow allowances.

If retained, it is imperative that the clause is modified, to ensure that it operates only as a last resort, where all other pricing mechanisms (for example a change to the way in which existing regulated prices are calculated) have been exhausted. Aurizon Network will submit drafting to the QCA for consideration in this regard, and is happy to discuss this issue further with the QCA.

- Reverse the CDD's current bias against socialisation from the expansion pricing framework (refer Chapter 16).
- Reverse its decision to defer WIRP revenues without a sunset date (refer Chapters 17 and 18).
- Reverse its amendments to Part 6 and Schedule F that reduce Aurizon Network's flexibility to respond promptly and pro-actively through pricing mechanisms to prevent a demand spiral well prior to its commencement (refer Chapter 17).
- Effect Aurizon Network's proposed changes to security provisions in the proposed standard form access agreements to ensure they give Aurizon Network the ability to appropriately and effectively address counterparty risk (refer Chapter 8).
- Reinstate UT3 provisions that allow Aurizon Network to reorder its capacity queue to give preference to longer term contracts (refer Chapter 11).
- Reverse its decision impose an access conditions regime, which materially limits Aurizon Network's ability to put in place measures to address stranding risks within its access contracts (refer Chapter 16).

## CDD 14.1 Maintenance of the RAB

### Asset disposals

The QCA proposes to maintain its IDD that, if an asset is disposed of during the year, the value of that asset recorded in the RAB will be removed from the RAB unless Aurizon Network can demonstrate to the QCA's satisfaction that less than that amount should be removed from the RAB<sup>104</sup>.

In its response to the QCA's IDD, Aurizon Network agreed with this position on the basis that there were likely to be minimal disposals. However, further review of the QCA's current wording of the CDD amended DAU, has led Aurizon Network to the conclusion that there may in fact be a significant number of disposals caught by this provision and in respect of which this treatment is inappropriate. That is because at present the QCA's CDD amended DAU does not exclude assets disposed of due to asset replacements from the concept of 'asset disposal'.

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<sup>104</sup> Schedule E clause 1.1 (c)

There are a number of instances where Aurizon Network will remove and replace network assets prior to the expiry of their RAB life. Such replacements are vital to the safety and integrity of the network and include where:

- assets are destroyed as a result of a flood or derailment event;
- assets are replaced as part of Aurizon Network's normal asset renewal program to maintain the safety, integrity and operational efficiency of the network;
- assets have developed flaws or have reached the end of their physical life; or
- assets have been replaced as part of an extension, expansion, augmentation or duplication of the rail infrastructure.

In such instances, it would be inappropriate to deduct the remaining RAB value of the asset unless its RAB life had expired. To do so would result in a situation where Aurizon Network failed to recover the cost of its original investment and would be inconsistent with the pricing principles, NPV neutrality and to the extent that it deters future investment, the object of the QCA Act.

Aurizon Network submits it would be appropriate to address this by reinstating Aurizon Network's original drafting on this issue, which provided that:

*...a disposal does not include circumstances where an asset is replaced (in whole or part) by an extension, enhancement, expansion, augmentation, duplication or replacement of all or part of the Rail Infrastructure of which that asset forms a part.*

Aurizon Network considers this upfront exclusion of asset replacements from the concept of disposals is a better outcome than the QCA's proposal of dealing with these issues on a case-by-case basis. That is because it will:

- materially reduce the cost and time, for each of the Aurizon Network and the QCA, associated with collating and assessing claims for routine asset disposals associated with asset renewals, avoiding significant delays in the annual RAB roll forward process;
- enhance regulatory certainty for Aurizon Network, hence encouraging investment in renewal of the network (consistent with section 69E of the QCA Act);
- remove any perverse incentives for Aurizon Network to delay necessary asset renewals (potentially compromising safety or operational efficiency) because it lacks certainty that it will be compensated for its investment in that asset.

When considering the administrative burden, it is important to understand that calculating the value of individual assets within the RAB is time consuming as the RAB is rolled forward on a system basis, not asset by asset. Therefore to determine the residual RAB value of any individual item in that RBA requires a series of calculations and assumptions. It would therefore be preferable to limit the instances in which such calculations (and the QCA's assessment of such calculations) are required to the bare minimum. Excluding asset disposals associated with renewals would achieve that objective.

### **Reducing the RAB for demand deterioration**

In its 2014DAU Aurizon Network originally proposed removal of the clause from the 2010DAU that allowed the QCA to optimise the RAB for a deterioration in demand, on the basis that such a situation should be addressed via a pricing review. The QCA has reinstated this provision in clause 1.2(b) in Schedule E of the CDD amended DAU. This allows the QCA to reduce the RAB due to demand deterioration that is determined to be long-term and sustained, following stakeholder consultation.

Aurizon Network remains of the view that the issue of demand deterioration should not be resolved through a RAB reduction and is concerned that the retention of this clause materially increases its exposure to asset stranding risk. This was addressed in the section on asset stranding presented above. For this reason, it cannot agree to inclusion of this clause in its Undertaking unless it is amended to make

it plain that RAB optimisation will not occur except as a last resort, when all alternative pricing proposals have proved ineffective to address the further material deterioration in demand.

### **Linking results of the Condition-Based Assessment to the RAB**

Aurizon Network has previously agreed, in principle, to the QCA's proposal to link the Condition Based Assessment (CBA) to the RAB. However, following its detailed review of the QCA's CDD amended DAU, Aurizon Network has the following comments:

- if the RAB has been optimised for this reason, the QCA has not provided any process for the RAB to be subsequently increased when asset condition has been restored to the standard required under this clause. Incorporation of such a process is logical and reasonable. Aurizon Network requests that the drafting is amended to include such a process;
- the QCA has offered no guidance as to what is meant by "long term and sustained". Aurizon Network submits that it would not be long term and sustained where Aurizon Network has a credible plan in place to remedy and has suggested drafting to this effect;
- Aurizon Network considers that it would be unreasonable if the RAB was optimised where the reason for the deterioration in network condition is because the QCA has not approved an adequate maintenance allowance.

Aurizon Network remains willing to accept the QCA's proposal on the linkage between the CBA and the RAB, subject to the above issues being addressed in the Final Decision.

### **Capital expenditure and RAB reporting**

Aurizon Network largely agrees with CDD 11(2)(c), subject to the following:

- clarification that the QCA must approve the RAB roll forward if it is satisfied that Aurizon Network has complied with the principles set out in clause 1.1 of Schedule E;
- a drafting clarification to ensure that capital expenditure and RAB Reports should be subject to confidentiality claims (consistent with section 239 of the QCA Act) where appropriate.

### **Equity raising costs**

Clause 1.4 in Schedule E of the 2014DAU addresses the process by which Aurizon Network can seek inclusion of equity raising costs in the RAB. Aurizon Network agrees with the QCA's approach to equity raising costs in principle. However, it seeks clarity around the drafting in clause 1.4 and requests that amendments are made to more clearly reflect the intended approach that will be used to assess an equity raising costs claim.

Aurizon Network in its 2014 DAU proposed a benchmark approach to assess equity raising costs, consistent with the methodology and assumptions applied by the Australian Energy Regulator (AER).<sup>105</sup> In its CDD on the MAR, the QCA considers both the benchmark methodology and cost assumptions to be reasonable<sup>106</sup>. Aurizon Network's main concern is that the drafting in clause 1.4(b) in Schedule E of the CDD amended DAU does not seem to reflect this decision.

The drafting in Schedule E requires Aurizon Network to demonstrate that equity-raising costs "have been incurred as up-front costs, with little or no ongoing cost over the life of the asset" and are prudent and efficient for investment in the CQCN. Aurizon Network does not understand what is meant by these criteria and considers they are inappropriate in circumstances where the QCA has approved a benchmark

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<sup>105</sup> Queensland Competition Authority (2015d). pp.160-162.

<sup>106</sup> Aurizon Network (2015d). p.161.

approach. One of the key reasons why Aurizon Network proposed the inclusion of the AER's approach was to provide a clear and reasonable methodology in assessing the prudence and efficiency of those costs, providing it with more certainty that such a claim will be accepted as long as Aurizon Network clearly demonstrates that it has applied this approach. The current drafting lacks guidance as to what Aurizon Network needs to do in order to demonstrate that an equity raising costs claim is prudent and efficient.

The current drafting requirement to demonstrate "incurred as up-front costs" could be interpreted to suggest that the QCA will undertake a prudence and efficiency assessment, where Aurizon Network would demonstrate "actual costs" incurred. Though this may not be the QCA's intention, it is important the drafting in clause 1.4 is clarified to give certainty to all parties.

*Aurizon Network considers that more certainty should be provided by allowing these costs to be accepted as prudent and efficient, provided Aurizon Network demonstrates the estimates reflect the AER benchmark approach. Thereby Aurizon Network suggests the CDD drafting be replaced with 2014DAU drafting on Equity Raising Costs clause 1.5 which details the AER approach.*

In summary:

- Aurizon Network submits that clause 1.4 in Schedule E should reference the AER's benchmark methodology, which would also be consistent with the QCA's CDD in relation to MAR. The current drafting gives no guidance on how Aurizon Network is to demonstrate that equity raising costs are "prudent and efficient". Aurizon Network submitted drafting in clause 1.5 of its 2014DAU that reflected the AER's approach.
- The current drafting requirement to demonstrate "incurred as up-front costs" could be interpreted as referencing 'actual costs', which would be inconsistent with the AER's benchmark approach. Aurizon Network requires deletion of the wording of "incurred as up-front costs" as it could be easily misinterpreted.

Aurizon Network is willing to accept the QCA's CDD on the inclusion of equity raising costs in the RAB, subject to the above issues being addressed in the Final Decision.

## CDD 14.2 Capital expenditure approval process

In its response to the QCA's IDD, Aurizon Network indicated that while it was willing to work with the QCA to develop a new capital expenditure review process, until it had had the opportunity to do so it considered that it was more appropriate to revert to the framework that is currently in the 2010AU<sup>107</sup>. In its CDD, the QCA appears to have understood this to mean that Aurizon Network was broadly content with the amendments that the QCA had made to Aurizon Network's original proposed 2014DAU. That is not the case. If it had been, Aurizon Network would not have suggested reverting to the 2010AU.

It is therefore incorrect for the QCA to assume that: "there is general consensus amongst stakeholders to accept the initial draft decision amendments"<sup>108</sup>, unless "general" is intended to exclude Aurizon Network, which would seem unreasonable given Aurizon Network is the party that is directly affected by this decision.

Aurizon Network has a number of concerns with the QCA's proposed framework. To ensure this is plainly understood, we will set these out below.

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<sup>107</sup> Aurizon Network (2015a). s.14.3, pp.203-204.

<sup>108</sup> Queensland Competition Authority (2015b). p.268.

## **Approval of the RAB roll forward**

The QCA has inserted a provision to the effect that it must approve the RAB roll forward. In practice, under UT3, Aurizon Network submits the RAB roll forward to the QCA and does not publish its public RAB roll forward report until the initial RAB roll forward has been accepted by the QCA.

Aurizon Network has no objection, in principle, to the QCA approving the RAB roll forward, but notes that the QCA's approval should be limited to ensuring that Aurizon Network has conducted the RAB roll forward properly in accordance with Schedule E. In this regard, Aurizon Network considers that it would be useful to provide that the QCA must approve the RAB roll forward if it is satisfied that in rolling forward the RAB, Aurizon Network has complied with the principles set out in clauses 1.1(a) to (e) of Schedule E.

## **RAB roll forward principles**

Aurizon Network notes that the QCA has added the words underlined in the extract below to clause 1.1(d):

*...prudent and efficient capital expenditure for an asset will be added to the Regulatory asset Base, where that expenditure is approved by the QCA in accordance with clause 2 and the value of that asset has not otherwise been recovered by Aurizon Network...*

While Aurizon Network is prepared to accept the inclusion of the words "and efficient", the QCA has provided no explanation for the words "and the value of that asset has not otherwise been recovered by Aurizon Network". Aurizon Network is concerned the words add uncertainty to the circumstances in which it may include capital expenditure into its RAB. For this reason, it considers the words should be deleted.

Alternately, if the QCA can explain the purpose of the words to Aurizon Network, it would be happy to discuss in order to determine whether it is appropriate that they form part of the final Undertaking.

## **Confidentiality of material submitted to the QCA for capital approvals and RAB roll forward**

Aurizon Network does not have an objection to the removal of the confidentiality clause. However, it does reserve its right to make a confidentiality claim under the QCA Act in respect of any material it is required to submit to the QCA and which the QCA proposes to publish. This is particularly important where sensitive documents, such as business cases, as well as feasibility studies (which may contain commercially sensitive Aurizon Network or access seeker information), are provided to the QCA as part of the capital expenditure approval process.

In this regard, Aurizon Network proposes a small amendment to clause 2.3(a) to ensure that the QCA must have regard to its obligations under section 239 of the QCA Act, prior to disclosure of any feasibility study or asset management plan.

## **Pre-approvals – separate scope, standard and cost**

Aurizon Network has the following concerns about the pre-approval process proposed by the QCA:

- It only allows for a combined pre-approval of scope, standard and cost. Under Aurizon Network's original proposal it was possible to split these elements, so that a pre-approval of just scope, or of just scope and standard was possible. That is because scope and standard will be known at the start of the feasibility study, well ahead of accurate cost estimates, which are only determined at the end of feasibility. Allowing pre-approval of these aspects in advance of pre-approval of costs will reduce delays to project development (as it will be more time consuming to do all three at once after the end of feasibility study) and give funders earlier certainty with respect to approvals, which may assist in securing finance.

- Under the QCA's drafting, the pre-approval process can only commence at the end of feasibility. This is likely to introduce significant delays to a project and means that funders will not have any certainty as to any element of approval (which may be needed to secure their project finance) until very late in the process. These delays may deter investment in the network.

Reference is made to the response to CDD 14.4 below, which considers these issues in the context of the customer voting process. The issues raised in that response are directly relevant here.

For these reasons, Aurizon Network submits that the QCA's Final Decision should permit pre-approvals of standard and scope, separate from costs, and should revert to Aurizon Network's 2014DAU drafting in this regard.

### **Criteria for assessing prudence and efficiency**

The amended DAU CDD has no detailed criteria by which the QCA must assess prudence and efficiency except those set out in clause 2.2(b), which are very limited in nature compared to the 2010AU drafting. It is unclear why these provisions were removed from the 2014DAU, as the QCA has provided no explanation of this.

Aurizon Network considers it is important that the key criteria to which a regulator should have regard in making an important administrative decision are clearly understood by all. To do so promotes regulatory transparency and certainty and promotes consistent and efficient decision making. Aurizon Network cannot see any justification for removing these clauses and consider it is important they are reinstated. If the QCA considers these factors should be adjusted in any way, Aurizon Network would be happy to meet and discuss this, with a view to reaching agreement on this issue. For this reason, Aurizon Network submits that the CDD amended DAU needs to be updated to reinstate the criteria against which the QCA will conduct its assessment of prudence and efficiency of scope, standard of works and cost (as set out in clauses 3, 4 and 5, Schedule E of the 2014DAU).

### **Information considered for prudence and efficiency review**

According to clause 2.2(b) in Schedule E of the CDD amended DAU, Aurizon Network may request the QCA to take into account of only information and analysis that Aurizon Network could reasonably be expected to have considered or undertaken at the time that it undertook the relevant capital expenditure. The QCA will consider this request as part of its determination.

This clause gives the QCA the power to consider information as part of its determination, which Aurizon Network did not have access to, or was not reasonably known, at the time of making the investment decision. This is unfair to Aurizon Network as it leads to material uncertainty when investing in the CQCN. It is also inconsistent with the interests of users and the object of Part 5 of the QCA Act, as it is likely to undermine Aurizon Network's ability and incentive to invest in the network. Aurizon Network cannot accept this position.

Aurizon Network notes in this regard that for many capital projects, pre-approval is not a viable option, given pre-approval is a lengthy process and delays in may well prevent a capital project proceeding when it is required to do so. As a result, it is critical that Aurizon Network have a fair, reliable and predictable framework for ex-post capital approvals to facilitate investments.

For this reason, Aurizon Network submits the CDD amended DAU to be amended such that in assessing whether capital expenditure is prudent and efficient, the QCA will only consider information available, or reasonably available, at the time of making the decision to incur that expenditure. Reference can be made to clause 2.3 in Schedule E of the 2014DAU.

## Transfer of existing Rail Infrastructure into the RAB

Clauses contained in the 2010 AU in relation to increasing the RAB have been removed from the CDD amended DAU with no comment or explanation. This includes the transfer of existing Rail Infrastructure into the RAB, which was contained in clause 1.3 in Schedule A of the 2010AU. This clause was initially excluded in the QCA's IDD in January 2015, also with no explanatory notes.

Clause 1.3 in Schedule A of the 2010AU stated that:

*The value of assets contained in the Regulatory Asset Base may be increased by Aurizon Network if:*

*(a) it is at the end of the Term and Aurizon Network is seeking to include a valuation for intangible assets, being a matter that was not considered as part of the initial valuation of assets contained in the Regulatory Asset Base; or*

*(b) additional sections of existing Rail Infrastructure are incorporated into the Central Queensland Coal Region, in which case the additional sections will be initially valued in accordance with the Depreciated Optimised Replacement Cost methodology...*

Aurizon Network understands that the QCA's rationale may be that clause 1.3 (a) would not be required anymore given the initial RAB is well established. However, clause 1.3 (b) is still required in situations where Aurizon Network would have a need to transfer existing Rail Infrastructure from an Aurizon Party or a Third Party. There is no other process available in the Undertaking to include transferred assets in the RAB.

For the above reasons Aurizon Network proposes that the drafting be amended to reinstate the 2010AU clause addressing the transfer of existing Rail Infrastructure, (clause 1.3 (b) of the 2010AU), into Schedule E.

## Recovery of costs of projects that do not proceed

The QCA appears to have also removed the ability of Aurizon Network to submit any capital expenditure claim for projects that do not proceed. (See clause 2.2(a) of the CDD amended DAU, which limits the QCA's approval of capital expenditure to "the prudent and efficient value of assets that are used by Aurizon Network to provide Train Services". (emphasis added))

In addition, the QCA has deleted the second part of clause 2.1(g), which enabled Aurizon Network to claim capital expenditure for Concept Studies, Pre-feasibility Studies and Feasibility Studies in respect of which the project has not proceeded. This is a significant departure from UT3 and from Aurizon Network's original proposal.

Aurizon Network considers that this position is inappropriate because:

- with respect to studies, to the extent Aurizon Network is obliged to undertake studies without third party funding through other parts of the Undertaking (i.e. its obligation to fund Concept Studies under the Expansion Framework in Part 8), it is inappropriate that Aurizon Network has no mechanism to recover these costs should the project not go forward. In this regard, Aurizon Network notes that the QCA has no legislative power to oblige Aurizon Network to incur expansion costs unless Aurizon Network expressly volunteers to do so;
- the nature of studies is to determine whether a project should proceed. If there is no compensation for the costs of a study in the event that a study determines the project should not proceed, this is a very significant disincentive for undertaking studies. A barrier to recovering these costs is likely to act as a disincentive to investment, which is inconsistent with the object of Part 5 of the QCA Act and the interests of network users; and
- it is unnecessary to prevent imprudent and inefficient investment or to protect the interests of end users. Any decision to include capital costs for a project that did not proceed within the RAB would be subject to the general capital expenditure approval framework: that is, if the decision to

undertake the study, or to undertake the other work, was imprudent or inefficient, the QCA would not be obliged to approve its inclusion within the RAB. As a result, there is no need for the QCA to exclude the prospect of recovery of such costs up-front. This decision can and should be undertaken on a case-by-case basis.

The capital expenditure process should be modified to ensure that Aurizon Network has the option to submit for approval a capital expenditure claim in respect of study and other costs of a project that did not proceed, and so that the QCA has the ability to approve such expenditure (subject to its normal prudence and efficiency review) in appropriate circumstances.

### **Application of capital expenditure approval to certain assets**

Because capital approvals are limited to assets that are “used by Aurizon Network to provide Train Services”, there is an issue as to whether capital costs which support the provision of train services (but which arguably are not used directly to provide those services) can be the subject of a capital approval claim. Examples might include Aurizon Network specific IT projects, such as the NAMs IT project that Aurizon Network is implementing to facilitate efficient network asset maintenance across the CQCN.

Aurizon Network assumes this position is unintended. It is critical that Aurizon Network has the ability and incentive to invest in such systems. To facilitate this it is critical that there is clarity that such items can be claimed. To provide otherwise would be inconsistent with the object of Part 5 of the QCA Act (as it would discourage efficient use of, and investment in, the network). It would also be inconsistent with the interests of end users (who benefit from a more efficient network), the pricing principles and the legitimate business interests of Aurizon Network.

Aurizon Network will submit drafting to clarify this issue, and submits this should be addressed in the final decision.

### **Ability of an access seeker (or its customer) to initiate a capital expenditure claim**

Aurizon Network does not understand why an access seeker or its customer should be able to initiate a capital expenditure claim, or would want to initiate such a claim, unless they are funding the relevant infrastructure. Aurizon Network submits this clause should only permit funding access seekers or funding customers to be able to require Aurizon Network to submit a claim.

### **Excluded capital expenditure**

The QCA has deleted clause 3.3 in Schedule E of the 2014DAU, which addressed the treatment of expenditure where the scope of a project exceeded what is required to meet Reasonable Demand, noting that this was previously addressed in clause 3.3.2 from Schedule A of the 2010AU. The QCA removed this clause based on a view that it was not necessary. The reason provided in its IDD was that “the proposed process does not preclude interested parties to a capital project that has had a proportion of capital costs excluded from the RAB submitting subsequent proposals for its inclusion in the RAB.”<sup>109</sup>

While Aurizon Network welcomes the QCA’s position that a subsequent claim remains possible, it notes that the QCA’s current proposed drafting does not permit a proportion of capital costs to be excluded from the RAB in the circumstances dealt with in clause 3.3 of Aurizon Network’s 2014DAU (i.e. where capacity was installed in excess of Reasonable Demand). Without this clause, the QCA may not have the flexibility to approve part of a claim only. Aurizon Network submits this clause be reinstated to provide clarity on this issue.

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<sup>K</sup> Queensland Competition Authority (2015b). p.308.

## Inappropriate use of “may” and “must” throughout Schedule E

There are a number of instances where the QCA has used “may”, in circumstances where it should have used “must”. Aurizon Network assumes these are drafting errors and have identified them in the table at the end of this section.

## CDD 14.3 Asset Management Plan

Aurizon Network is prepared to agree to this, subject to the QCA’s approval of Aurizon Network’s proposed amendment to ensure the non-disclosure of information if Aurizon Network or another party claims confidentiality over the information under the QCA Act.

## CDD 14.4 Purpose and Application of the Customer Vote

With the exception of CDD 14.4(2)(d), Aurizon Network disagrees with the CDD. Aurizon Network’s reasons for this are set out in section 14.10 of its response to the QCA’s IDD and incorporates by reference the cited text into this submission<sup>110</sup>. Aurizon Network does not consider that the QCA has specifically addressed the key points that Aurizon Network submitted in that response. Key examples of this are set out below.

### Scope and timing of the voting process

In its response to the QCA’s IDD, Aurizon Network emphasised the importance of being able to seek as much regulatory certainty as possible prior to the end of the feasibility study, which requires more flexibility in the voting process (CDD 14.4(2)(a), (b) and (c)).<sup>111</sup> Similar issues arise in relation to the QCA’s proposed timing of the pricing proposal for an expansion, where it may be important to provide participants with certainty in relation to the *methodology* that will apply in allocating the costs of an expansion, even if the actual costs of the expansion are at a pre-feasibility study level of accuracy. Reference is made to Aurizon Network’s response to CDD 16.7.

Aurizon Network is concerned that unless regulatory certainty as to the scope and standard can be achieved soon after the start of the feasibility study, significant time, costs and resources could be wasted in investigating options that are later rejected or not included in RAB. It should be noted that the expansion process includes a process of dispute resolution over the scope of the Feasibility Study. Where Access Seekers and Aurizon Network cannot agree on the scope to be studied in the Feasibility Study the QCA determines the scope. The Feasibility Study focusses on the final scope and any change to that scope will require a further Feasibility Study to be undertaken with the varied scope. This is why it is important to have the vote on scope (and possibly standard) soon after the scope is agreed or determined at the start of the Feasibility study. This allows confirmation or rejection before delay and costs are incurred. If the scope is not preapproved at this time the funders have the option of:

- continuing the expansion process with no regulatory certainty;
- re-determining a further scope (and restarting the Feasibility Study); or
- ceasing the expansion.

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<sup>110</sup> Aurizon Network (2015a).pp.208-210.

<sup>111</sup> Aurizon Network (2015a). pp.208-209.

Further, if a vote must be delayed until after the completion of the feasibility study, this risks delaying the entire process and could jeopardise the ability of participants to secure their own investment and funding approvals. The QCA does not specifically address this point other than saying that “we believe this flexibility comes at the expense of efficiency and effectiveness.”<sup>112</sup> Noting that the voting process in the 2010AU only permits a vote in relation to scope (and not standard and cost), Aurizon Network questions why it must now always encompass all three aspects and at the same time. Noting that Aurizon Network originally proposed the ability to potentially extend the voting process to encompass standard and/or cost, there is no evidence from previous votes that have been conducted which on consideration in light of the issues raised above justifies such a material shift in approach, to effectively be ‘all or nothing’.

Aurizon Network does not agree that requiring the vote to encompass scope, standard and cost provides “better information” as the effectiveness of the voting process depends on the quality of information provided in addressing each of those three elements in their own right. The QCA suggests that “locking in” one or more elements prior to another is “not ideal”.<sup>113</sup> Aurizon Network considers that the QCA has not given sufficient regard of the implications of this position for project costs, timeframes and participants’ own investment approval requirements.

Aurizon Network therefore remains firmly of the view that clause 4.1(b) in Schedule E of the CDD amended DAU needs to be amended to provide more flexibility in relation to the conduct of the voting process.

### **Initiation of a vote**

Aurizon Network disagrees with the QCA’s CDD 14.4(2)(e), which requires that an access seeker (or its customer), an expansion funder or interested participant should have the ability to require Aurizon Network to undertake a vote for a capital project for which a feasibility study exists. For the reasons set out in its response to the QCA’s IDD<sup>114</sup>, Aurizon Network remains of the view that this decision should be at the sole election of the funder/s of the project.

The QCA has not addressed this point directly in the CDD and instead seems to interpret this as Aurizon Network wanting to retain sole discretion as to whether or not a vote is undertaken. This seems to have missed Aurizon Network’s key point, which is that that party/ies responsible for bearing the risks and costs associated with funding a project should have this discretion. It should similarly be at the funder’s discretion as to whether pre-approval should be sought following the vote (CDD 14.4(2)(f)). The funder/s may or may not be Aurizon Network.

## **CDD 14.5 - Interested Participants**

Aurizon Network disagrees with CDD 14.5(2)(a) and its reasons for this are set out in section 14.11 of its response to the QCA’s IDD and incorporates by reference the cited text into this submission<sup>115</sup>.

Aurizon Network does not agree that the decision to have the vote open to existing access holders and access seekers not gaining capacity from the expansion with equal (not reduced weight) voting rights appropriately balances the interests of stakeholders. The impact of an expansion not proceeding for

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<sup>112</sup> Queensland Competition Authority (2015b). p.275.

<sup>113</sup> Queensland Competition Authority (2015b). p.275.

<sup>114</sup> Aurizon Network (2015a). section 14.10.2, p.209.

<sup>115</sup> Aurizon Network (2015a).pp.210-212.

expanding access seekers is an absolute loss of business opportunity versus minor impacts (if any) on other stakeholders proposed to be included.

This is also a further example of Aurizon Network's concern that the QCA has not fully engaged with the material submitted in its previous response to the IDD. For example, in that response Aurizon Network sought clarification from the QCA "on how contracted capacity or train paths can be impacted after construction is completed."<sup>116</sup> The QCA's response in the CDD is limited to: "a customers' ability to use its contracted entitlements may be impacted due to network performance factors. E.g. access to the network, cancellations or speed restrictions." This does not provide any specific cause and effect between these impacts and a completed expansion. This is a very important issue – Aurizon Network considers that the compression process addresses concerns about existing access holders' ability to use their contracted access rights.

Having regard to the various factors that the QCA must consider in deciding whether or not to approve a DAU under section 138(2) of the QCA Act, one of Aurizon Network's key concerns with the QCA's position is that does not give sufficient regard to the interests of access seekers. This includes smaller mining companies who may be looking to compete with incumbent existing producers and do not have the resources to adequately participate in complex regulatory processes and/or have not yet sought to enter the market.

Aurizon Network considers that too much weight is given to the interests of existing access holders. Further, the voting process presents a significant opportunity for incumbents that are not seeking capacity from an expansion to game the process by voting 'no' to any expansion – indeed in what is an intensely competitive market environment they are likely to consider it in their commercial interests to do so. The QCA refers to "lowering barriers for participation, thus providing an appropriate balance between the interests of Aurizon Network and access seekers."<sup>117</sup> This is not about Aurizon Network – it is about the interests of new and/or expanding producers versus non-expanding incumbents.

Aurizon Network considers that the expansion framework, of which the customer voting process is one aspect, is of fundamental importance in supporting the growth and development of the CQCR and hence promoting the Objects of Part 5 of the QCA Act. Aurizon Network considers that a better balance of interests under section 138(2) of the QCA Act by excluding existing access holders and access seekers not gaining capacity from the expansion

## CDD 14.7 - Voting and Acceptance Process

Aurizon Network disagrees with CDD 14.7(2)(a) and(c) and its reasons for this are set out in section 14.12 of its response to the QCA's IDD and incorporates by reference the cited text into this submission<sup>118</sup>.

Aurizon Network considers it essential that there be greater clarity around how votes with insufficient detail or inappropriate reasons are dealt with and in a manner that deters any perceived incentives to game the process. In its CDD, the QCA acknowledges that it "would not accept a 'no' vote where we considered there were insufficient reasons."<sup>119</sup> However, it is not clear from the QCA's drafting in clause 4.4(c) of the CDD amended DAU as to how it intends to give effect to this. In any case, this is after Aurizon Network has concluded the vote.

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<sup>116</sup> Aurizon Network (2015a). p.210.

<sup>117</sup> Aurizon Network (2015a). p.282.

<sup>118</sup> Aurizon Network (2015a).p.212.

<sup>119</sup> Aurizon Network (2015a).p.357.

Aurizon Network retains its view that it should have the ability to make that assessment as part of the voting process, noting that the ability of it and other participants to be able to rely on the outcome of that vote depends on the integrity of that voting process. Aurizon Network further notes that this will also be subject to audit prior to Aurizon Network being able to rely on this in seeking the QCA's approval of the relevant capital expenditure.

Aurizon Network has no incentive to unreasonably exclude a 'no' vote and in any case, remains accountable under the regulatory framework to conduct the vote in a fair and proper manner.

Aurizon Network therefore submits that its acceptance process that was previously contained in clause 8.13.5 of the 2014DAU be retained.

## CDD 14.8 Information Provided to Interested Participants

Aurizon Network disagrees with CDD 14.8 and its reasons for this are set out in section 14.13 of its response to the QCA's IDD and incorporates by reference the cited text into this submission<sup>120</sup>.

In being required to provide a copy of the feasibility study report, Aurizon Network's key issue here is that this could result in the disclosure of access seekers' confidential information. The QCA considers that this can be addressed by the information being disclosed to Aurizon Network under a confidentiality agreement. This has largely missed the point of Aurizon Network's concerns and accordingly has not been directly addressed by the QCA.

Given the most likely recipients of this report will be an access seeker's direct competitors, it will be extremely reluctant to provide this information (which is necessary in order to progress the feasibility study). The fact that Aurizon Network has received it subject to a confidentiality agreement becomes irrelevant if that information could still be disclosed to those competitors.

## CDD 14.9 Compliance and Audit Provisions

CDD 14.9(2)(d) requires Aurizon Network to redo the voting process if the auditor identifies a flaw in that process. Depending on the outcome of the vote and the nature of the flaws identified by the auditor, it may be unnecessary to redo the entire vote. Aurizon Network disagrees with this proposal. This could also have MAR implications as it will result in Aurizon Network incurring additional costs.

The QCA's response to this in the CDD is very general and unclear, stating that "Otherwise, there is no consequence to the audit, and there would be a risk that Aurizon Network could unfairly differentiate in a material way."<sup>121</sup> As highlighted above, the materiality of any problem identified in the audit and the actions required will determine what the outcome needs to be – this may or may not necessitate the conduct of a new vote. It therefore remains unclear to Aurizon Network as to why this must be required in all circumstances.

Aurizon Network also disagrees with CDD 14.9(2)(e), which requires amendments to clarify that an accepted voting proposal that successfully passes an audit does not infer QCA 'acceptance' that a capital expenditure project is prudent and efficient. As set out in Aurizon Network's previous response, this

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<sup>120</sup> Aurizon Network (2015a),pp.212-213.

<sup>121</sup> Aurizon Network (2015a),p.290.

change materially dilutes the benefit of conducting a vote and is more likely to result in it being bypassed to go straight to the capital expenditure approval process.

In its previous response to the IDD, Aurizon Network questioned why the QCA has changed its position from the 2010AU (clause 3.3.2(b)(ii), Schedule A), where the QCA was deemed to accept scope as prudent where there is a positive customer vote (noting that under the 2010AU, the customer voting process only applied to scope).<sup>122</sup> Other than seek to justify its preferred approach, the QCA has not specifically addressed this question in the CDD. Its main justification appears to be to allow it with an opportunity to “analyse” the voting outcomes, which underlines the concerns Aurizon Network has with this proposal as it could be inferred that the QCA could seek to overturn the outcome of a customer vote.

In conclusion, Aurizon Network submits that the drafting needs to be amended to revert back to Aurizon Network’s proposed drafting in the 2014DAU, including removing the requirement in relation to undertaking a new vote if the auditor identifies a flaw/s in the process (clause 4.6(f) in Schedule E of the CDD amended DAU).

## Other issues

There are a significant number drafting and policy issues scattered throughout the capital approval process in Schedule E. As flagged in the introduction to this section, Aurizon Network will be submitting a proposed redraft of Schedule E to address these issues. The table below seeks to consolidate a selection of these issues.

**Table 14.2 – Schedule E: other drafting issues**

CDD Reference	CDD Drafting	Issue
1.3 (a) (iii)	It is required that capacity modelling undertaken as part of the business case or Feasibility Study and on commissioning of the asset, is provided as evidence in determining prudence and efficiency of the expenditure.	There will not always be capacity modelling conducted e.g. when a project is not an expansion. Aurizon Network requires drafting to be amended to so that capacity modelling is provided only if conducted.  The proposed amendment is:  <i>(iii) capacity modelling <u>if</u> undertaken as part of the business case or Feasibility Study and on commissioning of the asset.</i>
2.2 (a)	The QCA may approve the inclusion of capital expenditure into the RAB if that expenditure is for the prudent and efficient value of the assets that are used by Aurizon Network to provide Train Services.	The use of the word “may” creates unnecessary uncertainty around capex approvals. Suggest reinstating similar to the 2010AU that the QCA will accept all prudent capital expenditure into the RAB.
2.2 (c)	(c) If the QCA is requested to determine the prudence and efficiency of capital expenditure before the capital expenditure is incurred, the	The QCA is setting a time period for a pre-approval to be effective. While Aurizon Network agrees that it is not unreasonable to have a time limit for which an approval

<sup>122</sup> Aurizon Network (2015a). p.213.

CDD Reference	CDD Drafting	Issue
	<p>QCA may include as conditions of its approval for any capital expenditure project...</p> <p>(iii) the period of time in which the approval has effect (and if the project is not completed within the nominated time, the QCA may decide the approval ceases to have effect).</p>	<p>remains valid, subject to it being from the approval date until the time a project is committed (without linking to construction timeframes).</p> <p>Aurizon Network therefore proposes the drafting is revised so that it is clear that the time refers to the time a project is committed and not linking to construction timeframes.</p>
2.2 (e)	(ii) the QCA may take that vote into account when approving whether the capital expenditure is prudent and efficient;	<p>At present there is significant optionality for the QCA to ignore the outcome of a customer vote. Aurizon Network considers this is inappropriate. Its view is that the QCA should be bound by the vote. Even if the QCA takes an alternate view, it <u>must</u> at least have regard to it.</p>
2.3 (a)	<p>In making its determination the QCA may, disclose any Feasibility Study in respect of a capital expenditure project or the Asset Management Plan to persons while seeking submissions.</p>	<p>Aurizon Network has no issues disclosing information in the Asset Management Plan (AMP), however some of the information in Feasibility Studies could be commercially sensitive customer information that cannot be disclosed publicly.</p> <p>This clause should be modified to ensure that it is plain that the QCA must not disclose this if Aurizon Network or another party claims confidentiality over the information via the QCA Act.</p>
2.3 (d) and (e)	<p>If the QCA refuses to approve capital expenditure;</p> <p>-the QCA may issue a draft of its decision</p> <p>-the QCA may issue a notice of its decision</p>	<p>The current drafting creates unnecessary regulatory uncertainty around capex approvals.</p> <p>Responsible administrative decision-making requires at a minimum, provision of a final decision with reasons. For significant decisions such as capex approval, a draft decision is a good process to ensure affected parties are given the right to comment. Aurizon Network submits that this should not be at the option of the QCA.</p> <p><i>Aurizon Network suggests the drafting be amended to use the term "must" instead of "may", similar to 2014DAU clause 2.2(e), (f) and (g)</i></p>
	<p>The QCA has deleted the clause which deemed prudent scope, standard or costs of capital expenditure where the capital expenditure was mandated by the QCA or an expert through a dispute resolution process.</p>	<p>Reinstate clause. This is necessary to protect a party's or parties' interests where the QCA or expert determines in a dispute that a particular scope, standard or cost is necessary.</p>

## Chapter 15 – Pricing Arrangements for Rail Access

No draft decisions have been issued in this chapter. As outlined in the CDD, the purpose of this chapter is to:<sup>123</sup>

*...set out the legislative framework applying to pricing arrangements and to our consideration of all pricing matters set out in this Volume, and to address higher level issues about pricing arrangements...*

### Legislative framework for pricing arrangements

When considering the pricing arrangements in the 2014DAU, the QCA must have regard to the following sections of the QCA Act:

- the object of Part 5 (section 69E);
- the factors specified in section 138(2); and
- the pricing principles (section 168A).

While Aurizon Network generally agrees with aspects of the QCA's commentary in this chapter, there are matters which raise particular concern, which are outlined below.

There are two key provisions in the legislation that Aurizon Network would like to focus on here, which is the interpretation and application of 168A(a) and the exclusion of assets for pricing purposes (section 138(2)(f)), which is highly relevant in the case of revenue deferrals.

#### Interpretation and application of section 168A(a)

Section 168A (a) requires that prices should “generate expected revenue for the service that is *at least enough* to meet the efficient costs of providing access to the service and include a return on investment commensurate with the regulatory and commercial risks involved” (emphasis added). In its assessment of 138(2)(e), the QCA states that the interests of current and future access seekers and access holders are best served where they pay access prices that: “...generate expected revenue for the service that is *no more than sufficient* to meet the efficient costs of providing access to the service...” (emphasis added).

This is not a matter of interpretation of section 168A(a). It is not possible to read “at least enough” as meaning “no more than sufficient” – indeed, they have the opposite meaning. In effect, the QCA has re-written section 168A(a) based on its assessment of section 138(2)(e).

The QCA's assessment is clearly incompatible with the QCA Act. It is of significant concern to Aurizon Network that the clear meaning and intent of a key provision in the QCA Act, being 168A(a), has been deliberately reinterpreted by the QCA to have the opposite meaning after consideration of the matters in 138(2)(e). Aurizon Network does not consider that it is open to the QCA to reinterpret the legislation in this way. It also exposes Aurizon Network to an unacceptable level of regulatory risk as it has no certainty as to how the QCA Act's provisions will be interpreted and applied in the future.

The QCA has also stated that the inclusion of the words “at least” in section 168A(a) was “to ensure that the relevant measure of cost is not short-run marginal cost, but a measure that enables Aurizon Network to recover its efficient costs”<sup>124</sup>. While the QCA is not explicit on this in the CDD, this would appear to

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<sup>123</sup> Queensland Competition Authority (2015c). Consolidated Draft Decision, Aurizon Network 2014 Draft Access Undertaking Volume III – Pricing and Tariffs, p. 1.

<sup>124</sup> Queensland Competition Authority (2015c). p.17.

imply that while Aurizon Network may not be able to be ensured that it can recover its efficient costs in the short run, it can do so in the long run.

To the extent that this must be implied, this then raises questions as to how this can be interpreted and applied. In particular, this can be seen as implying that Aurizon Network may be under-compensated for certain costs 'in the short run' (because the QCA has taken other matters into account in making its decision), on the assumption that it will eventually recover these costs 'in the long run'. Long run outcomes are also subject to considerable uncertainty – an issue that the regulatory framework does not satisfactorily address. Instead, the QCA's CDD seeks a high level of prescription and precision, even where doing so is both impractical and unrealistic.

For example, Aurizon Network has concerns that the QCA has also applied this logic when assessing the level of efficient maintenance and operating costs, which at least need to be assessed over the length of the regulatory period. Aurizon Network develops the expected maintenance scope for the undertaking period on the basis of time- and volume-based activities that are required over that period. Furthermore, the volume-based activities will be driven by the volume forecasts set by the QCA.

Aurizon Network incurs significant maintenance and operating costs on annual basis. As noted above, if the assumption is that Aurizon Network is entitled to recover its efficient costs, but only in the 'long run', this could imply the under-recovery of efficient costs in some periods and the over-recovery of costs in others. The regulatory framework is not currently applied in this way. In practice, this would only ever be applied asymmetrically, to Aurizon Network's detriment. That is, at least based on its experience to date, Aurizon Network could not envisage a situation where the QCA would approve an allowance that would enable Aurizon Network to recover more than the efficient costs for a period to the extent that it had under-recovered its efficient costs in a prior period. An example of this is the QCA's rejection of Aurizon Network's claim for actual audit costs incurred during UT3 that while efficiently incurred, were in excess of the approved allowance.<sup>125</sup>

Aurizon Network's financial performance is continually scrutinised by its shareholders and the wider market. To the extent that the regulatory allowance knowingly under-compensates Aurizon Network for its efficient costs will be a source of concern, even if this was only in a year, let alone over the course of a regulatory period.

Finally, it is also imperative that the QCA's assessment of 'efficient costs' takes into consideration the unique characteristics of the CQCR. Such characteristics may not typically be apparent in other comparator firms that Aurizon Network is benchmarked against by the QCA. While the full extent to which the QCA has done so is not apparent from the CDD, an example of this is where the QCA has based Aurizon Network's working capital allowance after having regard to what it has approved for other regulated businesses, without given any specific consideration as to whether this is appropriate to Aurizon Network's operating environment.<sup>126</sup>

### **Relevance of section 138(2)(f)**

The QCA states that section 138(2)(f), which is "the effect of excluding existing assets for pricing purposes" should be given less weight as it is not relevant in this case.<sup>127</sup> Aurizon Network disagrees with the QCA's assessment.

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<sup>125</sup> Queensland Competition Authority (2015d). Consolidated Draft Decision, Aurizon Network 2014 Draft Access Undertaking: Volume IV – Maximum Allowable Revenue, section 22.5.2.

<sup>126</sup> For further information, please refer to Aurizon Network's response to CDD 29.1

<sup>127</sup> Queensland Competition Authority (2015c), p. 2.

Aurizon Network contends that section 138(2)(f) is extremely relevant to the QCA's assessment of revenue and pricing arrangements for the UT4 period. For instance, the practical effect of the QCA's proposal to defer revenue associated with WIRP train services is to exclude these assets for pricing purposes for the period of the deferral.

Revenue deferral exposes Aurizon Network to additional volatility and risk for circumstances which are outside of its control. Aurizon Network should not be exposed to such risks where its investment in infrastructure is deemed to be prudent and efficient and accepted into the RAB. This not only fails to meet the requirements of section 138A(a), as well as section 138(2)(b) (Aurizon Network's legitimate business interests), but it will materially dilute its investment incentives, contrary to section 69E.

As already identified in Chapter 14, the QCA's proposals to defer revenue increase its exposure to asset stranding risk. Aurizon Network considers that it is not reasonable to impose such measures and they should only be implemented following consultation and agreement with Aurizon Network, including the application of a sunset date.

## Review of pricing arrangements

Aurizon Network acknowledges the remarks made by the QCA and stakeholders regarding the need for a comprehensive review of access pricing arrangements for the CQCR. This will also encompass pricing arrangements for electric services, noting that Aurizon Network has already had preliminary discussions with operators in order to provide additional transparency around the current electric pricing arrangements.

Aurizon Network is fully supportive of undertaking this pricing review and is committed to engaging with stakeholders, including industry and the QCA, on this matter beyond the final approval of the 2014DAU.

## Chapter 16 – Pricing Principles (Part 6)

### Summary of Aurizon Network's Position

#### Pricing principles

Chapter 16 in the CDD encompasses a number of significant issues governing how Aurizon Network can set prices for access, including the pricing of expansions. Having regard to its obligations under the QCA Act, one of the key things that Aurizon Network needs as a commercial infrastructure provider operating in a dynamic and challenging market environment is appropriate flexibility. This is essential in order for it to be able to manage its risks and allow it to recover its efficient costs (including its return on capital), as it is entitled to do under section 168A(a) of the QCA Act. In what is an extremely challenging environment for the CQCR, flexibility is also important in ensuring that price signals maximise the efficient utilisation and operation of, and investment in, the network infrastructure.

Aurizon Network is concerned that a number of requirements contained in the CDD will materially reduce Aurizon Network's flexibility well beyond what is reasonably required. It has identified a number of drafting changes proposed by the QCA in its CDD amended undertaking that it considers are beyond power (refer Table 16.2 below).

#### Expansion pricing

While conceptually, the QCA's proposed expansion pricing framework has some merit, Aurizon Network remains concerned that elements of the framework as outlined in the CDD are:

- beyond the power of the QCA to impose (see Table 16.2);
- practically unworkable; and
- heavily biased in favour of non-expanding users, who are clearly incentivised to either delay or seek to insulate themselves from the costs and volume risks associated with the expansion.

The potential for gaming poses significant risks to the expansion pricing framework and ultimately, could have the effect of deterring entry by new or expanding users, which will stifle competition and impede the growth and development of the CQCR.

The key issues Aurizon Network has identified include, but are not limited:

- the QCA's timing for the lodgement of a pricing proposal, which is too late in the process for participants that need to secure investment approval. Further, the QCA is proposing to be able to revoke its approval of a pricing proposal if there is subsequently a material change in circumstances, noting that participants will have secured their approvals based on the information available at the time the decision was made;
- the requirement that a Consensus Expansion requires 100% agreement of the Expansion Stakeholders, which is an extremely unrealistic goal in such a highly competitive market environment. This process is highly vulnerable to gaming, particularly by non-expanding users;
- the limitations on Aurizon Network's ability to subsequently socialise Expansion Tariffs and the base system tariff, which should be available at any stage;
- the general limitations on Aurizon Network's ability to socialise expansion costs, which significantly increase its stranding risk but could also serve to limit the growth and development of the network by discouraging the development of new mines and the expansion of existing ones (noting that the historical development of the CQCR has been predicated on the socialisation of costs).

In establishing a credible and workable expansion pricing framework, Aurizon Network considers that the following overarching objectives should be achieved:

- enhance the growth and development of the CQCR by encouraging new entrants and the expansion of existing mines;
- socialisation between expanding and existing users must be an option, which may be contemplated at any stage, where doing so is consistent with the requirements of the QCA Act;
- the framework must be workable and avoid unnecessary complexity; and
- the framework maintains an appropriate balance between flexibility and predictability in its application.

These objectives are consistent with Aurizon Network’s previous submissions.

In the interests of achieving a timely resolution to the 2014DAU process, Aurizon Network is prepared to accept elements of the QCA’s CDD subject to the amendments outlined below. If the QCA cannot agree to Aurizon Network’s amendments, Aurizon Network proposes to reinstate the expansion pricing framework as outlined in the 2014DAU, noting that these were substantially agreed with the QRC.

Aurizon Network will endeavour to address these matters with the QCA prior to the finalisation of the 2014DAU. It also recognises that some of these issues will need to be captured as part of the comprehensive review of rail access pricing arrangements in the CQCR to be undertaken beyond the finalisation of the 2014DAU (refer Chapter 15).

**Table 16.1 – QCA Consolidated Draft Decision**

	QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(3)	After considering Part 6 of Aurizon Network’s 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network’s omission of the price differentiation provisions.	16.1	<b>(2)(a) Disagree.</b> The QCA has inserted a different and unqualified prohibition on non-discrimination to the one that is contained in the QCA Act, which is considered beyond its statutory power.
(4)	The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to make the following adjustments as set out in clause 6.2 of our CDD amended DAU:		The QCA Act does not prohibit differentiation unless it is unfair and would have a material adverse effect on the ability of access seekers to compete with other access seekers - (s.100(2)) - or on users of a declared service to compete with other users - (s.168C(2)). The prohibition drafted by the QCA does not contain those qualifications.
	(a) Include an express prohibition against Aurizon Network establishing access charges for train services that unfairly differentiate in favour of any (i) related operator, (ii) related competitor, or (iii) third party that has commercial arrangements with a related competitor.		<b>(2)(b) Disagree.</b> The CDD is beyond the power of the QCA. The QCA’s drafting: <ul style="list-style-type: none"> <li>• creates a remedy for Access Holders where the QCA Act does not;</li> <li>• has the effect of ousting the jurisdiction of the courts;</li> </ul>
	(b) Enable an access holder to have its access charge amended in the event that Aurizon Network breaches the price differentiation principle in the 2014 DAU when developing access charges for an access seeker.		<ul style="list-style-type: none"> <li>• gives the QCA jurisdiction it does not have under the QCA Act; and</li> <li>• purports to allow the QCA to redraft existing, binding contracts.</li> </ul>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(1) After considering Part 6 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's drafting to provide additional discretion in differentiating the pricing for coal-carrying train services.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to reinstate the 2010 AU access condition provisions (with appropriate refinements to better balance the interests of various stakeholders as set out in clause 6.2.3 of our CDD amended DAU) and expand them to require non-standard terms that have cost and risk implications to Aurizon Network to be subject to our approval.</p>	16.2	<b>Disagree.</b> Aurizon Network does not consider that the access conditions provisions should be applied to non-standard terms.
<p>(1) After considering Part 6 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's drafting addressed at price differentiation insofar as it applies to non-coal-carrying train services.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to make the following adjustments as set out in clauses 12.1 and 6.7.1(b)(ii) of our CDD amended DAU:</p> <p>(a) Remove the reference to Aurizon Network's assessment from the definition of a 'change in market circumstances'.</p> <p>(b) Require Aurizon Network to demonstrate the available capacity on the CQCN is limited, and any expansion is commercially infeasible, before it can quote the maximum access charge to non-coal access seekers.</p>	16.3	<p><b>(2)(a) Agree.</b></p> <p><b>(2)(b) Agree.</b></p>
<p>(1) After considering Part 6 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal to use a DORC value of assets for establishing the ceiling prices for individual train services or combination of train services.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to use the RAB value for all circumstances, except where it is unavailable, in which case the DORC value can be adopted (as set out in</p>	16.4	<b>Agree.</b>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
clause 6.6.3(e) of our CDD amended DAU).		
<p>(1) After considering Part 6 of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's provisions about how the price differentiation and pricing limits principles interact with each other.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to require it to apply both price differentiation and pricing limits principles when establishing access charges, as long as they do not contradict each other.</p>	16.5	<b>Disagree.</b> Aurizon Network considers that the QCA's approach could lead to significant complexity in establishing access charges for existing train services. It is also not clear what the QCA intends will happen if the principles do contradict each other.
<p>(1) Our consolidated draft decision is to approve Aurizon Network's proposal that:</p> <p>(a) the user(s) requiring the expansion should generally pay an access charge that reflects at least the full incremental costs (capital and operating) of access</p> <p>(b) existing users should not experience a material increase in tariffs due to an expansion triggered by access seekers</p> <p>(c) if new/expanding users face a higher cost than existing users, a zero contribution to common costs from expanding users is generally acceptable</p> <p>(d) an allocation of expansion costs to existing users may be appropriate where an expansion has clear benefits to those users.</p>	16.6	<p><b>(2)(a) Agree.</b></p> <p><b>(2)(b) Agree with amendment.</b></p> <p><b>(2)(c) Agree.</b></p> <p><b>(2)(d) Agree with amendment.</b></p>
<p>(1) After considering relevant clauses of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve the provisions with respect to the pricing proposal.</p> <p>(2) We consider it appropriate that Aurizon Network amend the draft access undertaking (as set out in clause 6.4 of our CDD amended DAU) to:</p> <p>(a) provide a pricing proposal as part of the feasibility study report for an expansion that includes information regarding the allocation of the expansion costs between existing and expanding users, the proposed pricing arrangements for the expansion, the results of the</p>	16.7	<p><b>(2)(a) Agree with amendments.</b></p> <p><b>(2)(b) Disagree.</b> The pricing proposal will be relied upon to inform investment decisions affecting stakeholders across the whole supply chain, including coal producers, terminals, rail operators, Aurizon Network and third-party funders. The QCA's decision on a pricing proposal must be binding – failure to do so will create unacceptable uncertainty for expansion funders and will not promote efficient investment.</p> <p><b>(2)(c) Agree with amendment.</b> The QCA cannot require Aurizon Network to submit a specific DAAU (except in the limited circumstances specified in section 139 of the</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>socialisation test (where applicable), as well as indicative tariffs consistent with the proposed pricing arrangements.</p> <p>(b) calculate the pricing proposal socialisation test (if applicable) based on forecast costs and forecast volumes as set out in the feasibility study. The QCA is allowed to revise any decisions with respect to pricing arrangements for an expansion if there is a material change in circumstances.</p> <p>(c) upon the QCA's approval of a pricing proposal, require Aurizon Network to, where feasible, submit to the QCA a DAAU to apply for approval of a new or varied reference tariffs.</p>		<p>QCA Act), but provided the expansion proceeds, it is in the interests of Aurizon Network (and stakeholders) to submit a DAAU, which reflects the methodology and pricing approach as outlined in the pricing proposal.</p>
<p>(1) After considering relevant clauses of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposed expansion pricing framework.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend its 2014 DAU is to require (as set out in clause 6.4 of Part 6 of our CDD amended DAU):</p> <p>(a) Aurizon Network to approach expansion stakeholders in good faith to seek to facilitate a consensus (consistent with the expansion pricing principles) on the way in which expansion costs and volume risks are allocated. If Aurizon Network facilitates a consensus, the pricing proposal is to be based on consensus pricing approach. If Aurizon Network cannot facilitate a consensus, the pricing proposal is to be based on:</p> <p>(i) a 'customised' pricing approach considered on a case-by-case basis, where the expanding user(s) have substitutable train service entitlements in the existing system; or</p> <p>(ii) an 'endorsed' pricing approach where the expanding user(s) does not have substitutable train service entitlements in the existing system.</p>	<p>16.8</p>	<p><b>Disagree.</b> Aurizon Network has a number of concerns with the QCA's proposed expansion pricing framework, including, but not limited to: (1) the 100% agreement threshold under the consensus approach; and (2) limiting the customised pricing approach to circumstances where the TSEs of an expansion are substitutable</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1) After considering relevant clauses of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposed expansion pricing framework.	16.9	<b>(a) Agree</b> , subject to the QCA's acceptance of Aurizon Network's position on CDD 16.8.
(2) The way in which we consider it appropriate for Aurizon Network to amend its 2014 DAU is to make the 'endorsed' pricing approach entail the following (as set out in clause 6.4.4 of our CDD amended DAU):		<b>(b) Agree</b> , subject to the QCA's acceptance of Aurizon Network's position on CDD 16.8.
(a) A separate expansion tariff, based on contracted volumes, will be established in the event that an expansion is triggered.		<b>(c) Agree with amendments.</b>
(b) Aurizon Network is required to implement a 'fixed cost' take-or-pay regime, based on contracted volumes, for users paying an expansion tariff.		
(c) If the incremental costs associated with providing access for expanding users are lower on a \$ per contracted nt basis than the system reference tariff, a positive common cost contribution will be included in the expansion tariff, to align the expansion tariff with the system reference tariff on a contracted nt basis. Otherwise, users paying an expansion tariff will not be required to make any contribution to common cost.		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(1) After considering relevant clauses of Aurizon Network's 2014 DAU, our consolidated draft decision is refuse to approve Aurizon Network's proposed five per cent criterion for socialisation and 10-year expiration of expansion tariffs in the endorsed pricing approach.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend the draft access undertaking is as follows (as set out in Part 6 of our CDD amended DAU):</p> <p>(a) If socialisation of a new expansion with the highest expansion tariff (the existing expansion tariff that is highest on the nt basis) leads to lower tariff on a unit basis, these costs will be socialised.</p> <p>(b) If socialisation leads to an increase in the highest expansion tariff, the QCA will consider on a case-by-case basis whether to socialise or to establish a separate expansion tariff for this new expansion.</p> <p>(c) To undertake an annual review, by re-running the socialisation test based on latest information, to determine if expansion tariffs should be socialised where more than one expansion tariff exists for a system.</p>	16.10	<p><b>(1) Disagree.</b> Aurizon Network remains of the view that the 10-year expiration of expansion tariffs under the endorsed pricing approach should apply, noting that this was a position developed and agreed with the QRC.</p> <p><b>(2)(a), (b), (c). Agree with amendments.</b> Aurizon Network is prepared to accept this provided the QCA accepts Aurizon Network's proposal to remove the requirement for a 'customised' pricing approach to only be triggered where train services are substitutable (CDD 16.8). Furthermore, socialisation between an expansion tariff and a system tariff must be within the scope of any annual review process.</p>
<p>(1) After considering relevant clauses of Aurizon Network's 2014 DAU, our consolidated draft decision is to approve Aurizon Network's proposal that, where a system has multiple reference tariffs (due to previous expansions), the reference tariff used to establish access charges for new access seekers should be the existing reference tariff that is highest on a nt basis.</p>	16.11	<p><b>Agree with amendments.</b> The QCA must confirm in its Final Decision that the new access seekers also become a part of the 'highest reference tariff' for TOP and revenue cap purposes, even where they do not explicitly utilise the infrastructure of the 'highest reference tariff'.</p>
<p>(1) After considering relevant clauses of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve the 2014 DAU providing an exception to the consideration of an expansion tariff for expansions funded by Aurizon Network at the regulatory WACC.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend the draft access undertaking is to omit this exception, as set out in Part 6 of our CDD amended DAU.</p>	16.12	<p><b>Agree.</b> Aurizon Network is prepared to accept this provided it is exempt from any form of funding obligation</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(1) After considering relevant clauses of Aurizon Network's 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposed pricing approach for new train services utilising a mine-specific spur line connected to the CQCEN.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to reinstate the 2010 AU pricing approach, with further amendments (as set out in clause 6.3 of our CDD amended DAU) to:</p> <p>(a) address information disclosure concerns</p> <p>(b) make it consistent with the expansion pricing framework for expanding users.</p>	16.13	<p><b>(2)(a) Disagree.</b> It is unnecessary for the undertaking to include a process requiring an access seeker or access holder to present its private incremental costs to the QCA for approval.</p> <p><b>(2)(b) Agree with amendments.</b></p>
<p>(1) After considering Aurizon Network's proposal for the commercial term provisions in the 2014 DAU, our consolidated draft decision is to refuse to approve the proposal.</p> <p>(2) The way in which we consider it appropriate for Aurizon Network to amend its 2014 DAU is to reinstate the 2010 AU access condition provisions, with further amendments (as set out in clause 6.13 of our CDD amended DAU), to:</p> <p>(a) simplify the drafting</p> <p>(b) expand its application to all non-standard terms that have cost and risk implications</p> <p>(c) provide that if the QCA refuses to approve some or all access conditions, Aurizon Network can enter into negotiations for a separate arrangement with access seekers that will be regarded as entirely outside of the scope of the access undertaking, and will be subject to Division 5 of Part 5 of the QCA Act.</p>	16.14	<p><b>(2)(b) Disagree.</b> Aurizon Network reiterates that it is inappropriate for the access conditions provision to apply to all non-standard terms that have cost and risk implications, where such terms are not linked to the provision of funding</p> <p><b>(2)(c) Disagree.</b> It is inappropriate for the QCA to seek to impose access conditions on Aurizon Network where the only alternative is to proceed on the basis of a 'non-undertaking' option.</p>

## Aspects of the CDD that are beyond power

Aurizon Network considers that a number of decisions proposed by the QCA in relation to Part 6, and particular aspects of its drafting, are beyond its statutory power to impose. A number of these are outlined in the table below.

**Table 16.2 – Decisions in Part 6 that are beyond power**

Item	Clause	Comment
1	6.2.1(a)	<p>The QCA has, without power to do so, inserted a different and unqualified prohibition on differentiation to the one that is contained in the QCA Act.</p> <p>The QCA Act does not prohibit differentiation unless it is unfair and would have a material adverse effect on the ability of access seekers to compete with other access seekers (s.100(2)), or on users of a declared service to compete with other users (s.168C(2)). The prohibition drafted by the QCA does not contain those qualifications.</p> <p>The QCA Act does not prevent differentiation as between “combinations of Access Seekers and combinations of Access Holders” (whatever that may mean) as prohibited by the QCA’s drafting of clause 6.2.1(a).</p> <p>The QCA cannot expose Aurizon Network to potential liabilities beyond those in the QCA Act.</p> <p>The QCA cannot grant itself jurisdiction (as it does by its combined amendments to clause 6.2.1 and Part 11) beyond that with which it is vested under the QCA Act.</p>
2	6.2.1(b)(i) – (iii)	<p>The QCA has inserted new, unqualified prohibitions on price differentiation that go well beyond what is prohibited by the QCA Act. In particular, the QCA has prohibited any price differentiation in favour of a Related Operator, a Related Competitor and third parties that have commercial arrangements with a Related Competitor.</p> <p>The relevant prohibitions in the QCA Act are not absolute – they are qualified. For example, see section 104(3).</p> <p>There are no prohibitions in the QCA Act attaching specifically to differentiation in favour of “Related Competitors” or a “Third Party that has a commercial arrangement with a Related Competitor”.</p> <p>The QCA cannot expose Aurizon Network to potential liabilities beyond those in the QCA Act.</p> <p>The QCA cannot grant itself jurisdiction (as it does by its combined amendments to clause 6.2.1 and Part 11) beyond that with which it is vested under the QCA Act.</p>
3	6.2.1(b)(iv)	<p>The QCA’s drafting introduces an additional unqualified prohibition on preventing and hindering access “without derogating in any way from Aurizon Network’s obligations under sections 104 and 125 of the Act.”</p> <p>The QCA does not have power to introduce additional, unqualified obligations or prohibitions for subject matter expressly covered by the QCA Act.</p> <p>The QCA cannot expose Aurizon Network to potential liabilities beyond those in the QCA Act.</p> <p>The QCA cannot grant itself jurisdiction (as it does by its combined amendments to clause 6.2.1 and Part 11) beyond that with which it is vested under the QCA Act.</p>
4	6.2.3(a)	<p>Contrary to QCA Act, the QCA’s drafting seeks to limit the right of Aurizon Network to negotiate terms that might be inconsistent with the Reference Tariff.</p> <p>The QCA’s drafting only allows a variation from the Reference Tariff where there is a “<u>material</u> increase in cost or risk” (emphasis added) associated with the provision of access. By contrast, the QCA Act requires that the price for access must ensure that Aurizon Network receives at least its efficient costs and a required return. The materiality of cost or risk increases is not relevant under the QCA Act and cannot be imposed as a required standard by the QCA.</p> <p>The QCA drafting also requires that an access charge that varies from the Reference Tariff be approved by the QCA. The QCA Act does not give the QCA a role in approving access charges, as opposed to Reference Tariffs, except in an access dispute, and the QCA cannot grant itself a role it does not have under the QCA Act. It is inappropriate, and likely to add material delay to the determining access charges if QCA</p>

Item	Clause	Comment
		approval must be sought prior to determination of any access charge that varies from a Reference Tariff, Access seekers always have the option of raising a dispute to be determined by the QCA if they disagree with an Access Charge proposed by Aurizon Network that differs from the Reference Tariff.
5	6.2.4	<p>Contrary to QCA Act, the QCA's drafting seeks to limit the right of Aurizon Network to negotiate access charges that might be inconsistent with other access charges for similar services to circumstances where, relevantly, there is a "material" change or difference in cost or risk.</p> <p>The QCA Act requires that the price for access must ensure that Aurizon Network receives at least its efficient costs and a required return. The materiality of "changes or differences in the cost or risk of providing the service" is not relevant under the QCA Act and cannot be imposed as a required standard by the QCA.</p>
6	6.2.5(a)	<p>This clause gives Access Holders a right to complain to the QCA if the Access Holder believes that Aurizon Network has entered into a subsequent access agreement in contravention of Part 6. The QCA's drafting</p> <ul style="list-style-type: none"> <li>• gives the QCA jurisdiction it does not have under the QCA Act; and</li> <li>• purports to allow the QCA to redraft existing, binding contracts (which it cannot legally do)</li> <li>• More fundamentally, it is unnecessary to deal with this issue in the Undertaking as it is already dealt with in clause 38 of the UT4 Access Agreement.</li> </ul>
7	6.2.5(b)	<p>The obligation to provide the QCA with all information requested by the QCA to determine if there has been a breach of Part 6 by Aurizon Network:</p> <ul style="list-style-type: none"> <li>• strips Aurizon Network of protections afforded to access providers under the QCA Act for requests by the QCA for such information;</li> <li>• gives the QCA jurisdiction it does not have under the QCA Act because of the way in which the provision and the QCA's draft of Part 11 operate in combination.</li> </ul>
8	6.3.2	The QCA does not have a role under the QCA Act in approving capital expenditure associated with Private Infrastructure.
9	6.4.1(b)	The link to clause 6.3 renders clause 6.4.beyond power because clause 6.3.2 is beyond power for the reasons discussed above.
10	6.4.5(b)	<p>The QCA cannot grant itself power to determine new Reference Tariffs after the approval date and thereby effectively amend an existing approved Undertaking.</p> <p>A new Reference Tariff can only be approved if it is the subject of a DAAU and the QCA is satisfied that the DAAU meets the statutory criteria for the approval of a DAAU. The QCA's drafting ignores these processes.</p>
11	6.4.6(c)	<p>The QCA cannot grant itself the unilateral power to determine new Expansion Tariffs after the approval date and thereby effectively amend an existing approved undertaking.</p> <p>A new Expansion Tariff can only be approved if it is the subject of DAAU and the QCA is satisfied that the DAAU meets the statutory criteria for the approval of a DAAU. .</p>
12	6.4.6(d)	The QCA has no power under the QCA Act to require an access provider to submit a DAAU, except in the circumstances set out in section 139 of the Act.

Item	Clause	Comment
13	6.13	<p>The QCA Act expressly permits access providers and access seekers to agree matters that are inconsistent with an approved undertaking – s.168. The QCA Act does not limit such agreements to matters reflecting “additional costs or risks” as is required by the QCA’s drafting.</p> <p>The QCA has no statutory role in approving access agreements or access conditions that have been agreed by the parties.</p> <p>If the access conditions have been agreed, there is no dispute to enliven the QCA’s jurisdiction.</p> <p>The QCA cannot through an access undertaking require an access provider to disclose to all potential stakeholders’ commercially sensitive and confidential information, including the confidential information of a prospective access seeker, without regard to the protections afforded under the QCA Act.</p> <p>The QCA cannot grant itself jurisdiction to approve access conditions.</p>
15	6.13.2(g)(ii)(B)	<p>The QCA cannot amend a voluntary access undertaking to expressly treat access seekers and the access provider as negotiating “outside the scope of the undertaking” about access conditions.</p> <p>The QCA Act requires the QCA to make access determinations that are consistent with an access undertaking – s.119 – and the QCA cannot require that any dispute thereafter about a matter that is to be negotiated will be adjudicated by the QCA as if the undertaking and all of its protections for both parties did not exist.</p>
16	6.13.3(c)	<p>As the QCA Act expressly contemplates that access providers and access seekers can agree matters that are inconsistent with the access undertaking, clause 6.13.3(c) is beyond power.</p>

Aurizon Network’s response to this CDD should be read in conjunction with the comments made in the summary table above.

## CDD 16.1 Price Differentiation

### 16.1.1 Express prohibition on unfair differentiation

The QCA’s CDD 16.1(2)(a) requires amendments to the 2014 DAU (clause 6.2.1) to include “...an express prohibition against Aurizon Network establishing access charges for train services that unfairly differentiate in favour of any (i) related operator, (ii) related competitor, or (iii) third party that has commercial arrangements with a related competitor.”<sup>128</sup>

Aurizon Network disagrees with the requirement to include such an express prohibition and contends that it is beyond the QCA’s power under the QCA Act to impose such an express prohibition. While Aurizon Network acknowledges and agrees with the prohibition on unfair differentiation as outlined in section 137(1A) of the QCA Act, it submits that adequate protections against this behaviour are already entrenched in the 2014 DAU; specifically in Part 2 (non-discrimination), Part 6 (prescriptive pricing principles) and Part 11 (dispute resolution). Further, detailed drafting within each individual sections of

<sup>128</sup> Queensland Competition Authority (2015c). p. 18.

the Undertaking, create ambiguity when applying those obligations. A principles-based approach, with the overarching QCA Act obligation, is sufficient.

Aurizon Network considers that the QCA's CDD is too broad and could have the effect of unfairly penalising a related party, even where that party has a cost or risk profile that warrants efficient price differentiation. Any prohibition on differentiation should be limited to conduct prohibited under the QCA Act, which is conduct that would have a material impact on competition. Preventing legitimate price differentiation not only would be inconsistent with s.168A of the QCA Act but it would also contravene section 69E.

As noted in its response to the QCA's IDD,<sup>129</sup> Aurizon Network suggests that the requirement in section 137(1A) could still be captured with the inclusion of the following qualifications, which are that the prohibition on unfair differentiation be:

- limited to unfair differentiation that has a material impact on competition between users or access seekers; while recognising that
- differentiation may be reasonably justified because of different circumstances applicable to the relevant access provider, access seeker or users.

Alternately, and more appropriately, this clause could be deleted and reliance placed instead on the more general principles set out in Part 2 of the Undertaking.

## CDD 16.2 Coal carrying train services

The QCA's CDD 16.2(2) requires Aurizon Network to reinstate the 2010AU access condition provisions for agreements which support expansions of the CQCR and to widen their scope such that any non-standard terms, which have cost and risk implications to Aurizon Network, will be treated as Access Conditions and subject to the QCA's approval.

Aurizon Network disagrees with the QCA's CDD for the reasons outlined in its response to the QCA's IDD, which are restated here by reference.<sup>130</sup> In the first instance, Aurizon Network disagrees with the QCA's reinstatement of the access conditions provisions from the 2010AU. This is addressed in response to CDD 16.14 below.

The other issue in relation to CDD 16.2 is the broadening of the access conditions provisions to include non-standard terms. Aurizon Network is firmly of the view that the access conditions provisions should not be applied to non-standard terms. This is addressed in the balance of this section.

If the QCA remains minded to require an access conditions regime linked to the provision of funding for expansion, a clear distinction must be maintained between access conditions linked to the provision of funding for expansions and the provision of access on non-standard terms. Under the 2010AU, access conditions were linked to 'Significant Investments'<sup>131</sup> and in this context, could be sought to mitigate Aurizon Network's exposure to costs and risks that were materially in excess of those contemplated under the standard Access Agreement.

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<sup>129</sup> Aurizon Network (2015a). p. 44.

<sup>130</sup> Aurizon Network. (2015a). p. 223.

<sup>131</sup> In the 2010AU, a Significant Investment was defined as: "...a Major Investment projected to cost in excess of \$300million."

Noting the significant concerns that Aurizon Network has with the QCA's involvement in the negotiation and agreement of access conditions, Aurizon Network maintains that it is inappropriate for these provisions to apply to non-standard terms that are not linked to the provision of funding.

Aurizon Network contends that the QCA's CDD regarding non-standard terms is impractical. In addition, section 102 of the QCA Act states that "...an access provider is not required to provide access on the same terms under each agreement." The CDD has the effect of creating greater inflexibility in the regulatory framework.

Furthermore, Aurizon Network has obligations under both the Undertaking and the QCA Act, which already provide robust protections to ensure there is no unfair differentiation between access seekers and access holders (or conduct that would have a material impact on competition in the relevant market):

- If an access seeker believes that Aurizon Network is seeking to impose unreasonable conditions on its access to the service, it has can utilise the dispute resolution provision in Part 11 of the Undertaking. There is no need for the QCA to insert itself into this process unless and until a dispute arises.
- If an access holder believes that Aurizon Network is acting in contravention of Part 6 of the access undertaking (which already imposes significant restrictions on Aurizon Network's ability to differentiate access charges), it has the ability to dispute its access charge under Schedule 4 of the 2014DAU standard access agreement.

While the intent of the reference to access conditions in clause 6.2.3(a) is not clear, to the extent that Aurizon Network "intends to commence negotiating" (see clause 6.13.2) a varied access charge to reflect the cost or risk differences arising from non-standard terms, the QCA's CDD would appear to require that the access conditions process (clause 6.13 of the QCA's CDD amended DAU) be applied, which includes full disclosure to access seekers, customers (potentially competitors) and the QC A.

If this is the QCA's intent, this will mean that the access condition provisions are now applicable to terms within access agreements that may be required for circumstances such as:

- rail operator trials;
- ad-hoc train services; or
- initiatives to promote supply chain efficiencies.

The above list is not intended to be exhaustive, but Aurizon Network considers that it is inappropriate for the access condition provisions to apply in such circumstances as it restricts access holders from innovation and developing or exploiting potential sources of competitive advantage. Consider the following examples:

- A rail operator may seek to conduct a trial to assess the operational performance and capacity implications of consists that do not comply with the reference train characteristics, for example, longer trains. The CDD would require a public consultation of such initiatives, thereby giving all rival operators visibility of the trial prior to its commencement. This is likely to create strong disincentives for innovation by preventing dynamic efficiency and eroding any competitive advantage the access seeker may wish to obtain. It would therefore fail to promote effective competition. The current ringfencing obligations within Part 3 of the CDD amended DAU do not provide protections in these circumstances.
- Access seekers looking to rail an ad-hoc train service may wish to be exempt from the take-or-pay provisions outlined in the standard access agreement. Where capacity is available, such train services benefit the supply chain by making a contribution towards the System Allowable Revenue (SAR) of the relevant coal system.

- TSEs associated with the above examples are also likely to be of a short term nature (for example, less than 12 months). By the time the QCA was able to consult stakeholders, and make a decision as per the access conditions process, the window of opportunity to rail the ad-hoc train service would have well and truly passed.

The QCA's CDD does not offer any examples where Aurizon Network has exhibited the behaviours it is seeking to remedy. In this context, the QCA's CDD creates additional and unnecessary regulatory burden, with no incremental benefit over and above the protections already provided under the existing framework. Furthermore, it has the impact of stymieing dynamic efficiency, which is inconsistent with section 69E as it is unlikely to promote the efficient use, operation of and investment in the network.

The access conditions process should only be required where Aurizon Network seeks to vary terms and conditions that mitigate its exposure to additional costs or risks in relation to the provision of funding.

## CDD 16.4 Pricing Limits

The QCA's CDD 16.4 is to refuse to approve Aurizon Network's proposal to use a DORC valuation of assets for establishing the ceiling prices for individual train services or combination of train services.

For the reasons outlined in its supporting documentation accompanying the 2013DAU<sup>132</sup> and its response to the QCA's IDD,<sup>133</sup> Aurizon Network maintains that having the ability to establish pricing limits for individual services or combination of services based on Depreciated Optimised Replacement Cost (DORC) will result in economically efficient pricing outcomes for users. The QCA acknowledges that in some instances, more flexible pricing may lead to more efficient economic outcomes, it suggests that price differentiation (within the pricing limits) is a better means of achieving this<sup>134</sup>. However in practice, Aurizon Network is highly constrained in its ability to price differentiate.

Notwithstanding these concerns, Aurizon Network is prepared to accept the CDD in the interests of a timely resolution of UT4. Aurizon Network intends to include this matter as part of the review of access pricing arrangements for the CQCR to be conducted beyond the final approval of 2014DAU.

## CDD 16.5 Price differentiation and pricing limits

The QCA's CDD 16.5(2) requires Aurizon Network to apply both price differentiation and pricing limits principles when establishing access charges, as long as they do not contradict each other.

Aurizon Network disagrees with the QCA's CDD and maintains the reasons outlined in its response to the QCA's IDD.<sup>135</sup> Aurizon Network's concerns on this matter primarily relate to:

- the material increase in complexity when establishing access charges for incumbent train services; and
- the uncertainty created where there is a conflict of these principles.

### Increased complexity

The CDD will materially increase the complexity of the revenue and reference tariff modelling required to establish access charges for incumbent train services, the majority of which are currently subject to a

<sup>132</sup> Aurizon Network (2013). Volume 2: The 2013 Undertaking Proposal, 9.3, p. 194.

<sup>133</sup> Aurizon Network (2015a). pp. 224 - 225.

<sup>134</sup> Queensland Competition Authority (2015c). p.28.

<sup>135</sup> Aurizon Network (2015a). p. 225.

socialised pricing arrangement within each coal system. These additional modelling costs are not included within the current MAR submitted under the 2014DAU.

Aurizon Network's initial RAB valuation was set in 1999 based on a DORC methodology. This valuation was set at an 'asset class' level and included mine specific infrastructure of incumbent producers, which are not separately identifiable.

The QCA's CDD would require Aurizon Network to determine a MAR for each individual train service operating within the CQCR, i.e. up to 75 separate MARs. This would require the identification of:

- the residual RAB value of all assets utilised by each train service;
- the residual asset lives of each asset class utilised by each train service;
- the tax depreciation associated with all assets utilised by each train service;
- incremental maintenance and operating costs associated with mine specific infrastructure; and
- the contribution to common costs for each train service.

As mentioned above, the value of mine specific infrastructure for many incumbent producers operating within the CQCR was aggregated with the original RAB valuation and is not separately identifiable. It is practically impossible to accurately determine the necessary MAR inputs for these producers for the purpose of determining whether they meet their incremental costs, thus satisfying the lower bound of the pricing limits. In past undertaking periods, this practice was deemed acceptable because it was applied consistently to other producers, where their mine specific infrastructure was aggregated with the original RAB valuation. This is one possible example where the pricing limit principle conflicts with the price differentiation principle.

For clarity, where mine specific infrastructure is separately identifiable, Aurizon Network calculates the relevant pricing limits when establishing reference tariffs for the CQCR.

The QCA's CDD will result in a material increase in the complexity of Aurizon Network's Reference Tariff modelling. This may also lead to fundamentally different pricing outcomes for incumbent producers, which is contrary to promoting a stable regulatory framework.

### **Priority in the event of a conflict**

The QCA's CDD has the effect of increasing regulatory uncertainty in the event that there is a conflict between the price differentiation and pricing limit principles. To date, the price differentiation principle has had clear priority over the pricing limit principle.

In UT1 the QCA required (then) QR to amend the access undertaking so that: "QR is obliged to observe the limits on price differentiation irrespective of whether the resulting access charges cover the incremental cost of the individual train service".<sup>136</sup>

In the UT2 review process, the QCA noted that over the course of the UT1 period, conflicts had emerged between the pricing principles, however the undertaking provided no guidance as to how they should be resolved.<sup>137</sup> This was addressed by amending the access undertaking to put the principles in order of priority. The QCA reaffirmed that the limits on price differentiation had priority over observing the pricing limits. This priority was carried over into UT3.

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<sup>136</sup> Queensland Competition Authority (2000). Final Decision: Queensland Rail's Draft Access Undertaking, p.139.

<sup>137</sup> Queensland Competition Authority (2005). Decision: QR's 2005 Draft Access Undertaking, p.143.

While the priority order of the pricing principles remains in clause 6.1(b) of the CDD amended DAU, Aurizon Network's interpretation of the CDD is that the QCA proposes to remove the priority of the price differentiation principle over observing pricing limits by requiring that "Aurizon Network should comply with all pricing principles in the access undertaking, to the extent they do not conflict with each other."<sup>138</sup> The QCA does not address what it expects to happen where the two principles contradict each other, which is essential in maintaining an effective and workable pricing framework.

In conclusion, Aurizon Network reinforces the need for the price differentiation principle to continue to take priority over the pricing limit principle in the event that a conflict does occur.

## CDD 16.6 Principles underpinning the expansion pricing framework

The QCA's CDD 16.6 is to approve the expansion pricing principles proposed by Aurizon Network. Aurizon Network agrees with CDD 16.6, subject to amendments for clarity. However, it has residual concerns regarding the practical application of the principles, in particular, 16.6(1)(b) and 16.6(1)(d) (clause 6.4.1(d)(iv) in the CDD amended DAU).

Principle 16.6 (d) provides for an allocation of expansion costs to existing users where an expansion has clear benefits to those users. In its CDD, the QCA states:<sup>139</sup>

*In regards to proving that an expansion benefits existing users, we maintain that the onus of proof should lie with Aurizon Network and expanding users.*

Aurizon Network agrees with the QCA, but notes that the notion of a "benefit" may not always be quantifiable in financial terms. For example, expansions may create operational efficiencies, such as:

- schedule optimisation;
- improvements in performance to plan;
- fewer 'whole of system' possessions for maintenance activities; and
- reducing the impact of disruptions to the network.

All of the above examples improve the performance, robustness and reliability of the whole supply chain and, consistent with section 69E of the QCA Act, have the effect of promoting the economically efficient operation and use of the CQCR. The fact that the value of the above efficiencies can be difficult to quantify in financial terms should not preclude them for being considered an economic benefit to the supply chain, including to non-expanding users of the CQCR. On this basis, an allocation of expansion costs on the basis of infrastructure utilisation may be appropriate.

Principle 16.6 (b) notes that existing users should not experience a material increase in tariffs due to an expansion triggered by access seekers. This principle needs qualification - to the extent that existing users receive a benefit from an expansion, they may see their tariffs increase in recognition of these benefits. The assessment of pricing impacts on existing users must take place after the benefits (and associated costs) of the expansion have been allocated.

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<sup>138</sup> Queensland Competition Authority (2015c). p.30.

<sup>139</sup> Queensland Competition Authority (2015c). p. 37.

## CDD 16.7 Process for approval of expansion pricing arrangements

The QCA's CDD 16.7(2) requires Aurizon Network to make certain amendments with respect to the development of a pricing proposal for an expansion. Aurizon Network's main concerns, which are summarised below, relate to:

- aspects of the content and timing of the pricing proposal;
- the QCA's proposed ability to subsequently revise its decision on a pricing proposal if there is material change in circumstances, which creates uncertainty for all parties and increases their exposure to regulatory risk.

### Contents of the pricing proposal

While Aurizon Network generally agrees with the contents of the pricing proposal, it has material concerns with some of the QCA's information requirements. Specifically, clause 6.4.2 (b) of the QCA's CDD amended undertaking requires Aurizon Network to:

*"...keep the QCA informed of progress in facilitating a Consensus, including providing copies of all correspondence and a summary of all verbal communications with Expansion Stakeholders as requested by the QCA."*

Aurizon Network considers that this adds additional regulatory burden and is unnecessary. The QCA has not provided any reasoning in the CDD as to why this is necessary. The written acknowledgement provided by all Expanding Stakeholders as part of a consensus pricing proposal will be sufficient evidence for the QCA to satisfy itself that a consensus has either been reached or not.

The QCA seeks to impose this obligation on Aurizon Network prior to the submission of the pricing proposal. Further, the definition of "consensus" in clause 6.4.1 (e) requires all Expansion Stakeholders to provide written acknowledgement that the proposal represents an acceptable distribution of expansion costs and volume risks. Further, clause 6.4.3 of the CDD amended undertaking contains provisions which Aurizon Network considers would be best articulated in stakeholder submissions on a pricing proposal, rather than as part of Aurizon Network's pricing proposal. Specifically:

- 6.4.3 (vii) which requires "...an explanation of the position of each Expansion Stakeholder..."; and
- 6.4.3 (ix), which requires the pricing proposal to contain "...submission(s) by Expanding User(s) explaining the manner in which the Pricing Proposal is consistent with the Expansion Pricing Principles and the factors set out in section 138(2) of the Act..."

Aurizon Network has proposed amendments to reflect this.

### Timing of the pricing proposal

Aurizon Network disagrees with CDD 16.7(2)(a), which requires the pricing proposal to be provided as part of the feasibility study report. Aurizon Network understands that the QCA's rationale is to align the timing of the pricing proposal with the expansion approval process. Aurizon Network remains of the view that it should be able to submit the pricing proposal for approval within 80 days of a feasibility Study Funding Agreement becoming unconditional. It would then seek a further binding ruling from the QCA following the conclusion of the feasibility study.

As outlined in its response to the QCA's IDD,<sup>140</sup> Aurizon Network maintains that potential expansion funders will be seeking to rely on the QCA's decision on a pricing proposal before making a commitment to invest. Aurizon Network remains concerned that the QCA's proposed timing will create unnecessary delays to the expansion process, which may adversely impact the ability of parties to attract funding. It is for this reason that the pricing proposal needs to be able to be submitted as early as possible. In particular, participants require certainty as to the approach that will be used to allocate costs, as this will be essential to their assessment of the risk profile of their investment.

At the start of the feasibility study the precise access rights (volumes) and the scope is known. The costs are estimated at pre-feasibility accuracy levels. There is no reason why the pricing proposal should not be able to be developed and submitted at this time. Recognising that the costs of the expansion are indicative, as noted above, at this stage in the development process a key issue for the expansion's access seekers will be whether they will be required to bear all of the costs of the expansion or whether they will be shared with relevant existing access holders. The feasibility study does not need to be completed before this can be determined. It is extremely unlikely that the appropriate allocation approach would change between pre-feasibility and feasibility.

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**Apart from potentially jeopardising the ability of participants to secure the necessary approvals they will require at this stage, the practical impact is that it is likely that this QCA position will increase the construction costs of an expansion.**

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For example, where Aurizon Network submits the pricing proposal at the end of feasibility, it will require construction contracts with firm prices fixed for an extended period of time to allow for the QCA's assessment timeframes. In practice, the price quoted increases the longer it must be held prior to commitment. Depending on the construction market and the time period required, such arrangements may not be achievable.

Aurizon Network considers that a more appropriate mechanism to deliver network expansions in a timely and cost effective manner is to retain its 2014DAU proposal, i.e. to submit the pricing proposal within 80 business days after the feasibility Study Funding Agreement becomes unconditional. The QCA could make a draft determination on the basis of the pricing proposal. The expansion costs can then be refined at the conclusion of feasibility, at which point the QCA would be required to make a binding decision on the updated pricing proposal. Aurizon Network believes that this would achieve an appropriate balance between the QCA's desire for accuracy and the interest of expansion funders who need certainty and more timely decision making. To be clear, if the expansion proceeds the final proposed expansion tariffs will be included as part of Aurizon Network's DAAU.

### **QCA's ability to revise any decision to approve a pricing proposal**

While Aurizon Network has no material objection to calculating the pricing proposal socialisation test on the basis of forecast costs and forecast volumes, it disagrees with CDD 16.7(2)(b), which allows the QCA to subsequently revise any decisions with respect to pricing arrangements for an expansion if there is a material change in circumstances. The only circumstances under which it should be able to do this is where information provided to it by Aurizon Network, and/or the expansion user(s), is intentionally misleading and would have resulted in a materially different outcome.

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<sup>140</sup> Aurizon Network (2015a). p. 235.

Aurizon Network reiterates that it is inappropriate for the QCA to unwind its decisions with respect to the pricing proposal based on information that was not known by participants at the time. Doing so completely undermines the intent of the expansion pricing framework developed by Aurizon Network and the QRC, which was to provide greater transparency and certainty to investors and all expansion stakeholders across the whole supply chain, including coal producers, terminals, rail operators, third-party funders and Aurizon Network.

The QCA's final decision on a pricing proposal will be only be made after a comprehensive public consultation process with stakeholders, including non-expanding users, who all have an opportunity to assess, critique and comment on the proposed expansion pricing arrangements. Once this decision is made, it will be relied upon by expansion funders when either making a commitment to invest or choosing not to do so. These commitments are not to be taken lightly - the QCA must make its decision on the basis of information that was reasonably known at the time that parties made the decision to proceed with their investments. Failure to do so does not promote the interests of expansion stakeholders, exposing coal companies and financiers to significant regulatory risk and would undermine section 69E of the QCA Act.

In rationalising its decision about the timing of the pricing proposal, the QCA states that the degree of accuracy provided at feasibility will allow it to "...confidently approve a pricing proposal and to provide a sufficient level of certainty to expanding users..."<sup>141</sup>. Yet on the other hand, it reserves the right to reverse any decision it has made in the event of a material change in circumstances, which will only occur after that decision has been made.

As outlined in its response to the QCA's IDD,<sup>142</sup> Aurizon Network proposes that in this instance, the concept of materiality should be limited to an agreed set of circumstances and subject to a clearly defined threshold. The QCA failed to acknowledge or address this proposal in its CDD.

Aurizon Network therefore disagrees with the CDD as it creates unacceptable uncertainty for expansion stakeholders. Aurizon Network contends that the QCA must be bound by its final decision on a pricing proposal and proposes that the QCA may only seek to revise its final decision in the event that information provided to it by Aurizon Network, and/or the expansion user(s), is intentionally misleading and would have resulted in a materially different outcome.

## CDD 16.8 Process for establishing expansion pricing arrangements

The QCA's CDD 16.8(2)(a) requires Aurizon Network to amend the 2014DAU to base a pricing proposal on either a consensus, customised or endorsed pricing approach. Aurizon Network disagrees with the QCA's proposed approach and has set out a number of amendments that it considers are essential to improve the efficiency, effectiveness and practical workability of the framework. These are summarised below.

For clarity, Aurizon Network submits that if the QCA does not accept these proposed amendments, the expansion pricing framework contained in its 2014DAU should be reinstated.

### **Consensus Expansion**

#### Issues with the 100% threshold for consensus

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<sup>141</sup> Queensland Competition Authority (2015c). p. 40

<sup>142</sup> Aurizon Network (2015a). p. 236.

Aurizon Network considers that the requirement to obtain 100% agreement from all Expansion Stakeholders under a Consensus Expansion is neither realistic nor necessary (particularly when compared against the 60% threshold that applies under the voting process). Such a process is highly vulnerable to gaming and will lead to delays in the expansion process.

Under a Consensus Expansion, Aurizon Network must seek agreement (in writing) from all Expansion Stakeholders (including all Expanding and Non-Expansion users) that the pricing proposal represents an acceptable distribution of the costs and volume risks of an expansion. Aurizon Network must continue to seek a consensus until the completion of the Feasibility Study, at which point Aurizon Network (or any Expansion Stakeholder) can seek the QCA's approval for an extension of time to facilitate a consensus. If no extension is granted, the expansion proceeds as either a Customised or Endorsed Expansion.

Aurizon Network acknowledges that achieving consensus with all Expansion Stakeholders is an ideal scenario. Indeed, in its 2013DAU, Aurizon Network recognised the importance of providing expanding and non-expanding users with the opportunity to provide input into how expansion costs should be treated.

Aurizon Network considers that it is extremely unlikely that 100% consensus could ever be achieved. As noted previously, the export coal industry is a highly competitive environment and this competition has only intensified in the current challenging market conditions. Producers are naturally incentivised to promote their own commercial interests, which in the case of an expansion, will invariably be in conflict as long as one or more existing users have no interest in expanding their own volumes.

These competing interests effectively render the consensus process impotent. Non-expanding users have limited incentive to reach a consensus and the situation could emerge where one user withholds consent for no good reason. These users have a strong incentive to manipulate the QCA's expansion pricing framework to their advantage by:

- creating unnecessary delays for rival firms; or
- trying to obtain a price advantage by seeking to force expansions (and expanding users) into more stringent pricing arrangements.

If Aurizon Network seeks to facilitate a consensus under the QCA's CDD, non-expanding user(s) are incentivised to 'hold out'. In essence, they do not even have to participate in the process in order for a consensus to be ruled out.

If a non-expanding user holds out, the requirement for a consensus under the CDD would not be met. Aurizon Network is then required to submit a pricing proposal containing either:

- a Customised pricing approach, in which there is a chance that the costs will be socialised or an expansion tariff will apply; or
- an Endorsed pricing approach, in which the only option for expanding users is to pay an expansion tariff.

Under either option, there is a chance that the QCA may impose an expansion tariff on the expanding user(s), with more stringent pricing and take-or-pay terms. In the event this occurs, non-expanding users are likely to gain a cost and/or risk advantage over their competitors based on time of entry into the market. It is extremely unlikely that a non-expanding user would be made worse off by 'holding out' on Aurizon Network's attempt to reach a consensus. From their perspective, they are incentivised to push for a customised or endorsed pricing approach because there is a chance that the QCA will impose an expansion tariff on the expanding user(s).

Aurizon Network notes that the potential for gaming similarly exists within the capital expenditure voting process, which has a lower approval threshold and the requirement for 'no' votes to be accompanied by

sufficiently detailed reasons. It is unclear why a materially higher threshold should apply to the expansion pricing framework.

#### Aurizon Network's proposal

Aurizon Network therefore proposes that the Consensus Expansion provisions (clause 6.4.2) needs to be amended to align the consensus threshold to the 60% threshold contained in the customer voting process in Schedule E. If a consensus cannot be reached on this basis, Aurizon Network must be able to propose a pricing approach for approval which best fits the specific characteristics (and expected outcomes) of the expansion, whether that be a Customised or Endorsed pricing approach.

Further, if the QCA retains its decision on the timing of the pricing proposal as outlined above (which Aurizon Network does not accept) and it becomes apparent that a consensus will not be reached, Aurizon Network should not be obligated to wait until the completion of the feasibility study before submitting a pricing proposal on either a Customised or Endorsed basis. The requirement for Aurizon Network to continue to seek consensus until a nominated date where it will clearly not be achieved is an inefficient waste of resources and could result in further delays.

To be clear, if this amendment is not made Aurizon Network cannot accept the QCA's drafting of the Consensus Expansion approach in its current form as it considers it to be unrealistic and unworkable.

Aurizon Network is also concerned by clause 6.4.6(c) of the CDD amended DAU, under which the QCA reserves the right to develop its own expansion tariff, including whether socialisation should apply, at its own discretion. This clause is beyond the power of the QCA to require and must be deleted. It is of particular concern that the QCA could seek to apply this in the event that a consensus is reached with expansion stakeholders, which would be inconsistent with a 'negotiate-arbitrate' approach (acknowledging that Aurizon Network considers that 'consensus' is only likely to occur if a threshold lower than 100% is applied). Aurizon Network contends that it is best placed to develop and propose an expansion tariff, and that the role of the QCA is to either approve, or refuse to approve its proposal (providing its reasons).

### **Customised Expansion**

#### Issues with limiting a customised approach to circumstances where the TSEs are substitutable

Aurizon Network understands that under a customised pricing approach, it is afforded the flexibility to propose either:

- an expansion tariff; or
- a socialised pricing approach (with or without system premium).

Aurizon Network disagrees with the QCA's CDD, which limits the customised pricing approach to circumstances where the Train Service Entitlements (TSEs) of an expansion are substitutable.

In some circumstances, it may be appropriate for an expanding user with non-substitutable TSEs to be socialised with the rest of the system, provided that doing so is consistent with the expansion pricing principles (refer to CDD 16.6). The QCA also notes that stakeholders commented that socialisation of an expansion with an existing system may benefit all stakeholders in some instances.<sup>143</sup>

Consider the example of a single mine expansion requiring privately funded mine specific infrastructure and a new mainline passing loop. The access seeker has no existing TSEs (i.e. not substitutable). The

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<sup>143</sup> Queensland Competition Authority (2015c). p.43.

costs of the privately funded mine specific infrastructure would not be included in SAR or a Reference Tariff.

Provided the volumes associated with the new TSEs are sufficient to fully cover the capital costs of the passing loop and any incremental maintenance costs, it would be in the interests of non-expanding users for this expansion to be socialised, because the average price for all users would decrease. Under the QCA's CDD, if a single non-expanding customer 'holds out' for strategic reasons, consensus will be impossible to reach and the non-substitutability of TSEs immediately forces this expansion into an endorsed pricing approach.

In this instance, the expanding user would not only be subject to the more stringent pricing conditions of an expansion tariff, but it would also be subject to the volume risk of non-expanding users through the contribution to common cost provisions. From Aurizon Network's perspective, it will see additional and unwarranted fragmentation of the CQCR.

#### Aurizon Network's proposal

Aurizon Network considers that there should be no limitation placed on the 'customised' pricing approach, i.e. a customised pricing approach should be able to be considered on a case by case basis, irrespective of the substitutability (or lack thereof) of an expanding user's TSEs in the existing system. Otherwise, it could lead to outcomes that are not economically efficient, as illustrated above.

If warranted, Aurizon Network must be afforded the flexibility to propose a socialised pricing approach through a customised pricing proposal, even where TSEs are not substitutable. To this end, Aurizon Network has proposed amendments to clause 6.4 that remove the requirement for TSEs to be substitutable in order to submit a customised pricing proposal. To be clear, Aurizon Network does not accept CDD 16.8(2) if the QCA rejects this proposed amendment.

In addition, while it is unclear from the CDD, the QCA's CDD DAU (clause 6.4.5 (a)) implies that it is the expanding users who are responsible for submitting the proposed Reference Tariff to Aurizon Network (copying the QCA). Aurizon Network disagrees with the QCA's drafting. While Expanding users (and all other expansion stakeholders), have the right to comment on a pricing proposal as part of the QCA's consultation process, Aurizon Network reserves the sole right to submit a pricing proposal (and any other amendment or replacement to its voluntary access undertaking).

The QCA Act clearly sets out the circumstances in which either Aurizon Network or the QCA may seek an amendment to an approved voluntary access undertaking. To the extent the QCA is seeking to give a third party a right to require an amendment to the Undertaking, its actions are beyond its statutory power. Similarly the QCA cannot give itself a unilateral right to amend an access undertaking, other than in the circumstances specified in section 139 of the QCA Act.

## CDD 16.9 Endorsed Expansions

The QCA's CDD 16.9(2) requires Aurizon Network to make certain amendments to the endorsed pricing approach contained in clause 6.4.4 of the CDD amended DAU. Overall, Aurizon Network acknowledges the QCA's concern that an 'endorsed' pricing approach may be inappropriate for substitutable train services and agrees that the mechanistic test applied under the 'endorsed' pricing approach should be limited to circumstances where TSEs are not substitutable.

Aurizon Network is prepared to agree with CDD 16.9(2)(a) and 16.9(2)(b), provided the QCA accepts Aurizon Network's proposal to remove the requirement for a 'customised' pricing approach to only be triggered where train services are substitutable, as explained under CDD 16.8 above. To be clear, if the QCA rejects Aurizon Network's requested change to CDD 16.8, Aurizon Network must also disagree with 16.9(2)(a) and 16.9(2)(b).

Aurizon Network is also prepared to agree with 16.9(2)(c), provided the reference to net tonnes is replaced with net tonne kilometres (NTK). The reasoning for this is summarised below.

Aurizon Network acknowledges that a positive contribution to common costs (CCC) may be appropriate where an expansion tariff is lower than the system Reference Tariff. However, it has some concerns regarding the QCA's methodology for determining whether a CCC is payable by expanding users, in particular, the fact that the average price comparison does not take distance hauled into account. Aurizon Network contends that a calculation based on \$ per NTK is likely to provide a more appropriate balance between the characteristics of expanding and existing users.

## CDD 16.10 Socialisation between expanding users

The QCA's CDD 16.10 refuses to approve Aurizon Network's proposed five per cent criterion for socialisation and 10-year expiration of expansion tariffs in the endorsed pricing approach and requires certain amendments to clauses 6.4.4 and 6.4.6 in the CDD amended DAU.

Aurizon Network is prepared to agree with CDD 16.10(2)(a), 16.10(2)(b) and 16.10(2)(c), provided the QCA accepts Aurizon Network's proposal to remove the requirement for a 'customised' pricing approach to only be triggered where train services are substitutable (refer to CDD 16.8 above). For clarity, if the QCA is not minded to accept Aurizon Network's response to CDD 16.8, Aurizon Network disagrees with CDD 16.10.

Aurizon Network considers that it remains imperative that the potential socialisation between an Expansion Tariff/s and an existing system tariff must remain an option that it can propose to do at any time, provided that doing so remains consistent with the expansion pricing principles and the requirements of the QCA Act.

Aurizon Network disagrees with the QCA's rejection of the 10-year expiration of expansion tariffs under the endorsed approach.

Aurizon Network's interpretation of the expansion pricing principles is that both the consensus and customised pricing approaches provide the opportunity for expansions to be socialised with the existing system (where appropriate). Nevertheless, Aurizon Network disagrees with the QCA's CDD to refuse to approve the 10-year expiration of expansion tariffs. Aurizon Network reiterates that this 2014DAU proposal was an outcome developed and agreed with the QRC.

Aurizon Network is disappointed with the CDD and believes the QCA should give more weight to positions agreed with stakeholders. In reaching its CDD, the QCA does not make reference to any stakeholders who have objected to Aurizon Network's proposal. Furthermore, the QRC notes that the 10-year expiration of expansion tariffs represents an acceptable risk for the existing users. In this instance, the QCA has simply imposed its own view over a policy position that stakeholders agreed with. This undermines any incentives for Aurizon Network and industry to negotiate and agree positions, consistent with a 'negotiate-arbitrate' framework.

In disagreeing with the CDD, Aurizon Network reiterates that over time, an expansion tariff is not only exposed to more stringent pricing and take-or-pay conditions, but may also be exposed to the volume risk of non-expanding users through the contribution to common cost provisions. Aurizon Network contends that it is inappropriate to indefinitely quarantine expansion tariffs from the existing system and that the eventual socialisation between an expansion tariff and the existing system must be a policy option contemplated by the access undertaking.

The implications of the CDD are that it will:

- unfairly penalises expanding users;

- create additional complexity within the regulatory pricing framework;
- create inefficient fragmentation within the CQCR; and
- over time, expose Aurizon Network and third-party funders to additional risks (including third-party credit risk and asset stranding risk), without providing effective mechanisms to mitigate them.

Overall, this will not promote section 69E of the QCA Act.

In rejecting Aurizon Network's 2014DAU proposal, the QCA refers to differences in take-or-pay arrangements between users paying expansion tariffs and those paying the existing system Reference Tariff. Aurizon Network proposes that over time, it is desirable to transition all access holders on to similar take-or-pay arrangements, thus reducing the potential for unfair differentiation on the basis of timing of entry. Aurizon Network will seek to address this matter more broadly as part of the comprehensive pricing review.

## CDD 16.12 Expansions funded by Aurizon Network at the regulatory WACC

The QCA's CDD 16.12 refuses to approve the 2014DAU proposal to socialise expansions funded by Aurizon Network at the regulatory WACC.

As outlined in its response to the QCA's IDD,<sup>144</sup> Aurizon Network is prepared to agree with the CDD, subject to being exempt from any form of funding obligation. It should be noted that as part of its 2014DAU proposal, Aurizon Network has elected to fund CQCR projects with a combined value in excess of \$1 billion (through the UT4 Capital Indicator).

The CDD has the effect of increasing Aurizon Network's concerns about the ability to mitigate asset stranding risks. In the absence of the ability to socialise investments, Aurizon Network will be less willing to fund on standard terms, which provide very limited protection against these risks.

Aurizon Network's decision to revert to the 2014DAU form of drafting for Part 8 (expansions) includes an obligation on Aurizon Network to fund Shortfalls in certain circumstances. That undertaking was provided on the basis of the expansion pricing framework outlined in the 2014DAU. Where the QCA does not approve Aurizon Network's submitted 2014DAU in respect of expansion pricing, the commitment in the Part 8 drafting must be modified to restrict Aurizon Network's obligation to fund to circumstances where the Shortfall Expansion is socialised with the original expansion.

## CDD 16.13 Mine-specific spur lines

The QCA's CDD 16.13 refuses to approve Aurizon Network's proposed pricing approach for new train services utilising a mine-specific spur line connected to the CQCN. Aurizon Network is required to amend its draft access undertaking to reinstate the 2010 AU pricing approach, with further amendments to address information disclosure concerns (16.13(2)(a)) and make it consistent with the expansion pricing framework for expanding users (16.13(2)(b)).

Aurizon Network disagrees with CDD 16.13(2)(a). It is unnecessary for the undertaking to include a process requiring an access seeker or access holder to present its private incremental costs to the QCA for approval. From Aurizon Network's perspective, the QCA should simply inform Aurizon Network of the

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<sup>144</sup> Aurizon Network (2015a). p. 237.

value of any private incremental costs once approved. Until such time as this happens, the value of private incremental costs will be deemed to be zero.

It is also unclear how 16.13(2)(b) could be practically implemented in the event that an 'endorsed' pricing approach applies. Under an endorsed pricing approach, the QCA proposes that an Expansion Tariff is calculated on the basis of 100% contracted volumes and full take-or-pay. If the expanding user(s) have Private Infrastructure Costs (PIC), the QCA's CDD proposes that they should be entitled to a discount. Where the Expansion Tariff is based on the full expansion costs (excluding PIC), the application of a discount would mean that Aurizon Network (or the expansion funder) would not be able to recover the revenue it is entitled to.

Aurizon Network disagrees with CDD 16.13(2)(b) and proposes that a discount for PIC should only be applied in the following circumstances:

- where the expansion is socialised with the existing system; and/or
- there are multiple expanding users, at least one of whom has mine specific infrastructure funded by Aurizon Network and included in the RAB.

For clarity, a PIC discount should not be applied to single mine expansions paying an Expansion Tariff.

## CDD 16.14 Commercial terms

The QCA's CDD 16.14 is to refuse to approve the commercial term provisions proposed in the 2014DAU. Aurizon Network is required to amend its 2014 DAU is to reinstate the 2010 AU access condition provisions, with further amendments. For the reasons outlined in its response to the QCA's IDD<sup>145</sup>, Aurizon Network disagrees with the CDD.

The obligations in relation to access conditions are inextricably linked to the network development and expansion process. As outlined in Chapter 12 of this response, Aurizon Network cannot accept the QCA's proposed expansion framework, as set out in Part 8 of the CDD amended DAU. Aurizon Network has proposed to replace this with the proposal it agreed with the QRC and submitted in the 2014DAU.

Therefore, Aurizon Network's position is that the QCA should approve Aurizon Network's original 2014DAU Commercial Terms provisions. Aurizon Network notes in particular the following issues with the QCA's proposed amendments:

- In the context of CDD 16.14(2)(b), Aurizon Network reiterates that it is inappropriate for the access conditions provision to apply to all non-standard terms that have cost and risk implications, where such terms are not linked to the provision of funding. These matters are discussed in Aurizon Network's response to CDD 16.2 above.
- CDD 16.14(2)(c) provides that where the QCA refuses to approve some or all access conditions, the QCA must publish its decision regarding the access conditions it approves, which may include access conditions not initially sought by Aurizon Network. Aurizon Network must then choose to either:
  - accept the QCA's approved access conditions (which may include conditions not sought by Aurizon Network); or
  - enter negotiations with access seekers for a separate arrangement outside the scope of the undertaking.

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<sup>145</sup> Aurizon Network 2015(a). In particular, refer: s.15.4.2 pp.152-153.

- It is inappropriate for the QCA to seek to impose access conditions on Aurizon Network where the only alternative is to proceed on the basis of a 'non-undertaking' option. Aurizon Network has proposed drafting amendments which preserve its right to either:
  - revert to the standard form of access agreement; or
  - terminate an existing access agreement,

where the QCA seeks to impose non-standard terms, or access conditions not sought by Aurizon Network.

For clarity, Aurizon Network contends that the QCA's role is to either approve, or refuse to approve access conditions sought by Aurizon Network and it should not be able to seek to either impose access conditions, or propose alternate access conditions. Aurizon Network has proposed drafting amendments which preserve its right to revert to the standard form of access agreement or terminate an agreement where the QCA seeks to impose alternative access conditions not sought by Aurizon Network.

## Chapter 17 – Reference Tariffs (Part 6, Schedule F)

### Summary of Aurizon Network's Position

Aurizon Network is prepared to accept most of the amendments required by the QCA in the CDD, recognising that many of the issues relating to Reference Tariffs will be reviewed as part of the comprehensive review of rail access pricing arrangements in the CQCR to be undertaken beyond the finalisation of the 2014DAU (refer Chapter 15). Aurizon Network's residual concerns relate to the extent to which the CDD will enable it to recover its efficient costs and/or effectively manage risk. The most significant issues addressed in this chapter are:

- the QCA's proposed allocation of GAPE costs to the Newlands system, which Aurizon Network does not consider would reasonably reflect the scope of works required in the absence of the GAPE project;
- the removal of rebate adjustments from the calculation of adjusted SAR, which following the rejection of other amendments proposed by Aurizon Network, will expose it to an unacceptable level of volume risk for which it is not compensated;
- the rejection of certain Reference Tariff variation events and limitations placed on the calculation of revenue adjustment amounts proposed by Aurizon Network, which exposes it to the risk that it will not be able to fully recover its efficient costs during a regulatory period.

Aurizon Network is concerned with a number of drafting changes proposed by the QCA in its CDD amended undertaking. A detailed mark-up of the QCA's drafting will be provided to the QCA shortly after this submission.

**Table 17.1 – QCA Consolidated Draft Decision**

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1) After considering Aurizon Network's proposed changes to its tariff arrangements, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	17.1	<b>(2)(a) Agree.</b>  <b>(2)(b)(i) Agree with amendments.</b>
(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:		<b>(2)(b)(ii) Agree.</b>  <b>(2)(c) Agree.</b>
(a) escalate the 2012–13 AT2 tariffs from the 2010 AU by CPI over the 2014 DAU regulatory period		<b>(2)(d) Agree with amendments.</b>
(b) remove the adjustments that were made to address the impact of the increase in AT2 tariffs as follows:		<b>(2)(e) Agree</b> , however the 2010AU rebate arrangements provided for rebate variations to be included in the revenue cap process. Acceptance is conditional on the QCA accepting Aurizon Network's response to CDD 17.5(2)(c).
(i) revert the calculation of minimum contribution to common costs to the 2010 AU approved approach		
(ii) reset the AT4 tariffs for the Newlands system to the standard calculation approach used in other		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>systems for all years in the 2014 DAU regulatory period.</p> <p>(c) remove the proposed capacity 'diesel' multiplier from reference tariff calculations.</p> <p>(d) escalate the AT1 according to the MCI over the 2014 DAU regulatory period.</p> <p>(e) remove the system discount and revert to the rebate arrangements in place under the 2010 DAU.</p>		
<p>(1) After considering Aurizon Network's proposed pricing arrangements for the GAPE project, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:</p> <p>(a) adjust the allocation of costs so that the difference between the Newlands capital indicator and approved capital expenditure for 2011–12 is allocated to all GAPE and NAPE Deed customers.</p>	17.2	<p><b>(2)(a) Disagree.</b> Aurizon Network's proposed allocation remains a reasonable reflection of the scope of works required in the absence of the GAPE project.</p>
<p>(1) After considering Aurizon Network's proposed new reference tariff arrangements, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:</p> <p>(a) derive an alternative reference tariff for the Middlemount to DBCT train service based on the 2010 AU pricing principles</p> <p>(b) derive the reference tariff for the Caval Ridge to HPSCT train service based on 2010 DAU pricing principles</p> <p>(c) apply revenue smoothing to the Rolleston electric train services over 2014–15 to 2016–17</p> <p>(d) apply an incremental cost test to Rolleston electric assets using forecast volumes rather than with reference to 85 per cent of contract volumes.</p>	17.3	<p><b>(2)(a) Agree.</b></p> <p><b>(2)(b) Agree.</b></p> <p><b>(2)(c) and (d) Agree,</b> but Aurizon Network notes that its financial modelling indicates that an AT<sub>5</sub> system premium should not be applicable to Rolleston train services.</p>
<p>(1) After considering Aurizon Network's proposed changes to its reference train</p>	17.4	<p><b>(2)(a) Disagree.</b> Reference train characteristics must specify the requirement to operate using</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
service characteristics, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.		the most direct route between and origin and destination.
(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:		<b>(2)(b) Agree.</b>
(a) remove the requirement for a reference train service to operate using the most direct route		<b>(2)(c) Agree.</b>
(b) remove the requirement relating to capital costs		<b>(2)(d) Agree.</b>
(c) align a reference train to comply with Aurizon Network's coal loss mitigation provisions		
(d) amend the requirement relating to conditions of access.		
(1) After considering Aurizon Network's proposal for revenue cap adjustments in Schedule F of the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	17.5	<b>(2)(a)(i) Agree.</b>
(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:		<b>(2)(a)(ii) Agree.</b>
(a) remove proposed revenue adjustments in relation to		<b>(2)(b) Disagree.</b> The CDD limits Aurizon Networks ability to be compensated for its efficient costs.
(i) short-run variable maintenance costs		<b>(2)(c) Disagree.</b> This will expose Aurizon Network to volume risks that are outside of its control.
(ii) AT1 revenue		<b>(2)(d) Agree with amendments.</b>
(b) include in the calculation of adjusted allowable revenue the cost of audits required under this undertaking by the QCA, but only to the extent that the QCA has approved that these costs have been efficiently incurred and these costs are not recoverable elsewhere in this undertaking		<b>(2)(e) Agree.</b>
(c) remove rebate adjustments from the calculation of adjusted allowable revenue		
(d) include overload charges and ancillary revenues in the calculation of total actual revenue		
(e) remove the increment calculation and application.		
(1) After considering Aurizon Network's proposed suite of reference tariff variation events in Schedule F of the 2014 DAU, our	17.6	<b>(2)(a) Agree with amendments.</b>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
consolidated draft decision is to refuse to approve Aurizon Network's original proposal.		
(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to limit reference tariff variation events to:		
(a) a change in law or relevant taxes with a 2.5 per cent materiality threshold		
(b) a change in the pricing related to distribution and/or transmission entities with a 2.5 per cent materiality threshold		
(c) a review of the QCA levy		
(d) force majeure.		

## CDD 17.1 Reference Tariff arrangements

The QCA's CDD 17.1 requires Aurizon Network to amend the tariff arrangements proposed in the 2014DAU. Aurizon Network agrees with CDD 17.1(2)(a), 17.1(2)(b)(i), 17.1(2)(b)(ii) and 17.1(2)(e) on the basis that it reserves the right to re-evaluate these matters as part of a comprehensive review of access pricing arrangements for the CQCR.

Aurizon Network agrees with CDD 17.1(2)(d), but disagrees with the manner in which the QCA has determined the 'initial' AT<sub>1</sub> Reference Tariff for FY2014. Consistent with the intent of CDD 17.1(2)(d), Aurizon Network proposes to escalate the 2009/10 AT<sub>1</sub> reference tariff (as approved by the QCA for UT3) in accordance with the 'actual' MCI applicable for the UT3 regulatory period.

Aurizon Network is prepared to accept 17.1(2)(c), which relates to the capacity multiplier, provided that the impact of this CDD is limited to the reference tariff modelling only. This is explained below.

Aurizon Network notes that in clause 6.2.3(c) of the CDD amended undertaking, a Capacity Multiplier may still be applied to the extent an access holder or access seeker's nominated train configuration differs from the reference train and has a capacity impact. Section 168A(b) of the QCA Act, allows for "...price discrimination when it aids efficiency". Aurizon Network must be able to apply fair price differentiation to reflect differences in cost and/or risk in relation to the capacity consumption of train types that do not conform to the published reference train characteristics.

In addition, Aurizon Network has proposed minor drafting amendments to clarify the practical application of Reference Train Paths (rtp) for a train service, in accordance with clause 6.2.2(d) of the 2014DAU. The formula outlined in this clause is applied to identify capacity consumed by a train service relative to the reference train. Where the capacity consumed by the train service:

- is equivalent to the reference train, rtp is equal to 1
- exceeds that of the reference train, rtp may be greater than 1.

As currently drafted, the calculation of rtp may result in a decimalised capacity multiplier. For example, the rtp for a train service may be calculated to consume 1.2 paths relative to the reference train. In reality, a decimalised multiplier will understate the true capacity impact of this train service because a train

service cannot consume part of a train path. Once a train service commences operation on a train path, that train path is essentially sterilised for other users of the CQCR.

Aurizon Network has proposed amendments to clause 6.2.3(c)(ii) of the CDD amended DAU, such that the resulting rtp is to be rounded up to the nearest whole number. Aurizon Network considers this amendment appropriately balances the interests of access seekers, access holders and train operators.

## CDD 17.2 Allocation of GAPE project costs to the Newlands system

The QCA's CDD 17.2 requires Aurizon Network to adjust the allocation of GAPE costs so that the difference between the Newlands capital indicator and approved capital expenditure for 2011/12 is allocated to all GAPE and NAPE Deed customers.

Aurizon Network disagrees with the QCA's CDD for the reasons outlined in its response to the QCA's IDD.<sup>146</sup> The QCA has not taken account of the benefits to Newlands customers from the GAPE Project as stated in Aurizon Network's response to the CDD, in particular:

- asset renewals, replacements and upgrades because of the GAPE scope of works resulting in lower required spend in the Newlands System. This was evidenced by the \$30.3m lower spend over the 2010AU period compared to the Capital Indicator;
- the Newlands system can operate longer and heavier trains; and
- improved operational efficiencies have been achieved, which avoided investment in additional infrastructure that would otherwise been required.

Aurizon Network reiterates that the \$30.3million allocation of GAPE costs to the existing Newlands system is appropriate and is a reasonable reflection of the scope of works required in the absence of the GAPE project. As a result, Aurizon Network proposes to retain the 2011/12 allocation of GAPE costs to the existing Newlands system for the purpose of calculating the UT3 capital carryover adjustment and the Opening Asset Value for the 2014DAU.

In the event that the QCA refuses to approve Aurizon Network's proposal, Aurizon Network confirms that the methodology outlined in the QCA's CDD<sup>147</sup> is appropriate, i.e. \$30.3million is to be allocated between both GAPE and NAPE customers on the basis volumes contracted. As outlined in its response to the QCA's IDD,<sup>148</sup> Aurizon Network will submit a DAAU for NAPE train services once there is more certainty around their commencement date.

## CDD 17.3 New Reference Tariff arrangements

The QCA's CDD 17.3 requires Aurizon Network to amend the new reference tariff arrangements proposed in the 2014DAU. Aurizon Network agrees with CDD 17.3(2)(a) and 17.3(2)(b). However, it has concerns regarding the pricing arrangements for Rolleston train services (CDD 17.3(2)(a) and (b)). Aurizon Network is prepared to accept the CDD provided it can verify that the QCA's calculations are correct.

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<sup>146</sup> Aurizon Network (2015a). p. 251.

<sup>147</sup> Queensland Competition Authority (2015c). p. 102.

<sup>148</sup> Aurizon Network (2015a). p. 252.

In order to appropriately assess the accuracy of this CDD, Aurizon Network requested that the QCA provide it with a detailed breakdown of the volume forecasts prepared by Energy Economics. Unfortunately, the QCA was not able to provide Aurizon Network with the details by each origin and destination combination underpinning those forecasts in a timely manner, which prevents it from fully considering the QCA's proposed forecasts. This was due to confidentiality claims by some producers resulting in some aggregation of information.

Aurizon Network's financial modelling suggests that the Rolleston train service should not be required to pay a system premium on either AT<sub>3</sub> or AT<sub>5</sub>. As a result, Aurizon Network would welcome the opportunity to discuss its financial modelling with the QCA in more detail upon submission of its response to the QCA's CDD.

## CDD 17.4 Reference train service characteristics

The QCA's CDD 17.4 requires Aurizon Network to amend the reference train characteristics proposed in the 2014DAU. Aurizon Network agrees with CDD 17.4(2)(b), 17.4(2)(c) and 17.4(2)(d) on the basis that no material consequences are anticipated by doing so. To the extent that these changes become necessary in the future, Aurizon Network will seek to address this through a DAAU. Aurizon Network disagrees with the QCA's rejection of the requirement for a reference train service to operate using the most direct route and provides an example of why this is important below. Further, Aurizon Network has concerns about the QCA's removal of system-specific reference train service characteristics for Blackwater and Goonyella, which should be reinstated.

### Most direct operating route

Aurizon Network disagrees with CDD 17.4(2)(a) for the reasons outlined in its response to the QCA's IDD.<sup>149</sup>

Aurizon Network proposed this requirement for additional clarity because network capacity is assessed on the basis that a train service loads at a single mine and operates directly to the port to unload. Train services that do not directly operate from mine to port are likely to impose additional costs or risks, or consume more network capacity relative to the reference train. In such instances, it would be appropriate to fairly differentiate the pricing arrangements for these train services from the reference train.

 This type of operation is clearly inconsistent with a reference train, as it increases scheduling complexity, consumes more network capacity and creates additional interface risks.

Aurizon Network reiterates that the reference train characteristics must specify the requirement to operate using the most direct route between and origin and destination.

### System specific reference train service characteristics

The CDD states that the QCA did not receive any stakeholder submissions opposing its Draft Decision to accept the system specific reference train service characteristics proposed by Aurizon Network in the

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<sup>149</sup> Aurizon Network (2015a), p. 256.

2014DAU.<sup>150</sup> Aurizon Network notes that both the QCA's DD and CDD accepted Aurizon Network's system specific reference train service characteristics.

Despite this, Aurizon Network notes that the requirement for Blackwater and Goonyella system reference trains to operate to a "Nominated Separation Time over the Constrained Section of no greater than 20 minutes" has been deleted from the QCA's CDD amended undertaking. This characteristic should be reinstated, as it is a critical factor for determining available capacity over the constrained section. To the extent a nominated train service does not meet this criterion over the constrained section, it will consume additional network capacity and as a result, should be subject to a capacity multiplier, in accordance with clause 6.2.3(c) of the CDD amended undertaking.

The QCA's CDD amended undertaking has also removed the term 'Comparative Length' from the system specific reference train characteristics in favour of 'length'. The QCA has not provided any justification for this change. For clarity, 'Comparative Length' must be reinstated as it incorporates a degree of tolerance which allows for immaterial variances, for example: minor differences in wagon design; and couple stretch.

## CDD 17.5 Revenue cap adjustments

The QCA's CDD 17.5 requires Aurizon Network to amend the revenue cap adjustments proposed in Schedule F of the 2014DAU. Aurizon Network agrees with CDD 17.5(2)(a)(i), 17.5(2)(a)(ii) and 17.5(2)(e). Aurizon Network proposes to review the ability to make revenue adjustments in relation to short-run variable maintenance costs and AT1 revenue in the future, including as part of its review of pricing arrangements.

Aurizon Network agrees with CDD17.5(2)(d), subject to the QCA agreeing to amend the definition of Ancillary Revenues and to include the qualification whereby ancillary revenues will only be included in Total Actual Revenue (TAR) to the extent that the costs associated with the ancillary service has been included in Aurizon Network's MAR allowance.

### **Removing rebate adjustments from the calculation of adjusted allowable revenue**

For the reasons outlined in its response to the QCA's IDD,<sup>151</sup> Aurizon Network disagrees with the QCA's CDD 17.5(2)(c), which exposes Aurizon Network to volume risks which are outside of its control.

Aurizon Network initially proposed this amendment in conjunction with its proposals to remove rebateable revenues from the SAR and apply upfront Reference Tariff discounts to effect the rebate arrangements. This would have completely isolated the rebate arrangement between Aurizon Network and the Access Facilitation Deed (AFD) holder. The QCA has refused to approve this change.

Aurizon Network in its response to the IDD stated that it was unable to agree an arrangement with the AFD holder for the payment of a 'net' access charge (i.e. outside revenue cap arrangements) as the current definition of TAR includes revenues associated with the payment of a rebate. Aurizon Network therefore proposes the reinstatement of the proposed clause 3.3(b)(v) in Schedule F of the 2014DAU to include rebate adjustments in the revenue cap.

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<sup>150</sup> Queensland Competition Authority (2015c). p.117.

<sup>151</sup> Aurizon Network (2015a). pp.258-259.

Aurizon Network would also like to ensure that the QCA is aware of the unintended consequences for access holders and Aurizon Network that could occur if the CDD is applied and Aurizon Network's proposal is not accepted.

Under the 2010AU, if an AFD holder did not rail any services, then a rebate is not paid to the AFD holder. This rebate variation would be included in the revenue cap as a return to all access holders. This is because rebateable assets are included in the RAB and all access holders that rail contribute to TAR for rebateable and non-rebateable assets. In the event the AFD holder did not rail, there would be a shortfall in the SAR. Aurizon Network recovers this shortfall via the revenue cap process. Under the 2010AU this recovery is reduced by the amount of the under-paid rebates (rebate variation).

Under the CDD methodology, Aurizon Network would continue to recover the shortfall via the revenue cap but the non-AFD holders would not be compensated by the rebates under-paid. The following example compares the position under the 2010AU and the CDD.

- System forecast: 50,000 net tonnes (nt)
- Actual volumes: 45,000nt (Nil tonnes railed by the AFD holder)
- SAR: \$250m (including \$10m of rebateable assets)
- Average access charge rate per tonne: \$5.00
- Take or pay does not trigger.

The outcomes are shown in the following table.

**Table 17.2 – Rebates: comparison of 2010AU and CDD**

	2010AU \$M	CDD \$M
Total Actual Revenue (45,000Nt x \$5)	225	225
System Allowable Revenue	250	250
<b>Revenue Cap Under Recovery</b>	<b>25</b>	<b>25</b>
Rebate Variation	(10)	Nil
<b>Adjusted Revenue Cap Recovery</b>	<b>15</b>	<b>25</b>

The example above shows the impact of an under railing AFD holder:

- in the 2010AU example the under-payment on the rebateable asset (\$10million) is adjusted off the revenue cap under recovery (\$25million - \$10million = \$15million). Aurizon Network pays no rebate to the AFD holder;
- if the CDD approach is applied, despite the AFD holder not railing the system is not compensated for the amount of rebates not paid to the AFD holder and Aurizon Network earns \$10million additional revenue.

The alternative also applies where an AFD Holder over-railed and contributed above forecast SAR to the revenue cap calculation:

- in the 2010AU case the amount of rebate over-payment would be added to the revenue cap adjustment (increasing any under-recovery or reducing any over-recovery) and Aurizon Network would pay the AFD over-railer a rebate reflecting its full payment above forecast on the rebateable asset;
- if the CDD approach is applied, despite the AFD holder over railing, the revenue cap is not adjusted and Aurizon Network earns less than the SAR.

If the QCA does not agree that the rebate variation should be reinstated in the Final Decision then the only alternative that Aurizon Network can see is to pay the AFD holder the exact amount of the SAR that relates to rebateable assets irrespective of railings. This would ensure Aurizon Network only retains the SAR that it is entitled to, but does not prevent the anomalies as noted above. This would result in:

- a non-railing AFD holder being paid \$10million in rebates reflecting (\$25million - \$15million) additional recovery in revenue cap which is paid for by other system users; and
- an over-railing AFD holder only being paid a \$10million rebate and all system users benefiting from the AFD over-railer's additional access revenue.

This example illustrates the importance of amending Schedule F to restore Aurizon Network's proposed treatment of rebates, as contained in clause 3.3(b)(v) in Schedule F of the 2014DAU.

### **Other drafting amendments to Schedule F**

Aurizon Network will be submitting revised Schedule F drafting following the lodgement of this submission relating to the revenue cap provisions to align with this response to the CDD. This will include the following.

The QCA stated:<sup>152</sup>

*We do not consider the 12 months take or pay security amount proposed by Aurizon Network to be appropriate, as we do not consider this appropriately balances the interests of an access holder with the legitimate business interests of Aurizon Network. As such, we maintain our decision that six months take or pay charges be the security amount an access holder may be required to provide Aurizon Network.*

*We consider the 12 month security amount is a significant and potentially burdensome amount for an individual access holder to provide as security, and we do not consider that such an amount is necessary in order to sufficiently protect the legitimate business interest Aurizon Network has in mitigating its exposure to credit risk.*

*We consider Aurizon Network already has significant protection from credit risk through the revenue cap form of regulation under which it operates, as this will allow it to recover any unrecovered revenue through the existing revenue adjustment mechanisms already in place.*

Aurizon Network will amend the Schedule F drafting to ensure that the Revenue Cap provisions reflect the intent of the CDD made by the QCA.

Clauses 4.3(d)(iii) and 4.3(g)(ii) of the CDD relate to the allowable threshold on which Aurizon Network's revenue cap is adjusted for breach or negligence in the provision of Below Rail Services. The QCA arbitrarily changed the allowable threshold percentage in the Revenue Cap provisions from 10% to 5% in CDD 8.4. Aurizon Network disagrees with the QCA's changes to the percentage and the QCA statement that the Standard Access Agreement and Revenue Cap provisions are linked. Full details have been provided in Aurizon Networks response to CDD 8.4. Aurizon Network will amend the Schedule F drafting to reflect its response to CDD 8.4.

Finally, as per Aurizon Network's commentary in Chapter 20 of this submission, it has identified a number of draft decisions that have been made by the QCA that, if included in the QCA's Final Decision on UT4, would give rise to increased costs that are not currently included in the calculation of the MAR.

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<sup>152</sup> Queensland Competition Authority (2015a). p.252.

Where possible, Aurizon Network has provided an estimate of the costs that are likely to be incurred as a result of the relevant QCA draft decisions (refer Chapter 20) and proposes that the aggregate amount of these costs be included in the final MAR. Where it is not possible to provide an estimate of the likely costs that would be incurred as a result of the relevant QCA draft decisions, if included in the QCA's Final Decision on UT4, Aurizon Network considers it appropriate that any such costs should be recoverable by Aurizon Network through the revenue cap process. Consequently, Aurizon Network proposes to amend the drafting in Schedule F to facilitate the process by which Aurizon Network can recover all of these additional costs.

## CDD 17.6 Reference Tariff variation events

The QCA's CDD 17.6 requires Aurizon Network to amend the suite of Reference Tariff variation events in Schedule F of the 2014DAU. For the reasons outlined in its response to the QCA's IDD,<sup>153</sup> Aurizon Network agrees with the Reference Tariff variation events proposed by the QCA in the CDD, but reiterates that the following should be reinstated:

- Aurizon Network's ability to recover maintenance costs that have been prudently and efficiently incurred, but are greater than the maintenance cost allowance (subject to a 2.5 per cent materiality threshold); and
- the provisions relating to a material change in volumes or other circumstances where there are reasonable grounds to amend a Reference Tariff.

### Recovery of prudent and efficient costs in excess of UT4 allowances

During the course of an undertaking period, Aurizon Network may be required to incur costs in excess of the UT4 allowances. Where such costs are prudently and efficiently incurred and not otherwise provided for under the UT4 allowances, consistent with section 168A(a) of the QCA Act, Aurizon Network should be entitled to recover these costs through a Reference Tariff variation. As it currently has no other mechanism to recover these costs, Aurizon Network considers that this provision should be reinstated, noting that in any case, any such variation needs to be approved by the QCA. In the event the QCA does not approve a defined Reference Tariff variation event that covers such costs, Aurizon Network will seek to claim the recovery of its efficient costs through the revenue cap process contained in Schedule F.

### Material change in volumes

While Aurizon Network has a responsibility to ensure it can meet its contractual obligations, it ultimately has no control over the volumes railed by its customers. In its CDD, the QCA states that:

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**“...reference tariff variation events should be limited to events that are not foreseeable and not within the control of Aurizon Network.”<sup>154</sup>**

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A mine closure may result in a material change in volumes. This is one such example of an unforeseeable event, which is certainly not within the control of Aurizon Network. The QCA's CDD appears to directly contradict the logic it stated was applied when arriving at its CDD. Aurizon Network

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<sup>153</sup> Aurizon Network (2015a). p. 261.

<sup>154</sup> Queensland Competition Authority (2015c). p.129.

seeks the reinstatement of this provision, noting that the QCA is required to either approve, or refuse to approve, any proposed variation submitted by Aurizon Network for a material change in volumes.

## Chapter 18 – Reference Tariffs for WIRP Train Services

### Summary of Aurizon Network’s Position

Aurizon Network has agreed with most aspects of the QCA’s proposed pricing arrangements in relation to WIRP. There are two main issues that have emerged with WIRP that are symptomatic of broader concerns that Aurizon Network has with pricing arrangements. The first is the allocation of costs and demonstrating the extent to which existing customers will benefit from investments made to enable an expansion. In this case, Aurizon Network remains of the view that duplications in the Blackwater system will deliver important operational benefits to Blackwater users, which warrants the allocation of costs to Blackwater users.

The second is Aurizon Network’s significant exposure to asset stranding risk. This has been clearly highlighted in the case of WIRP where Aurizon Network made commitments to undertake major expansions in a very different market environment. The QCA is now seeking to impose revenue deferrals. As outlined in Chapter 14, consideration needs to be given to efficient and effective solutions to manage Aurizon Network’s exposure to asset stranding risk and this will be a key priority going into the UT5 review.

**Table 18.1 – QCA Consolidated Draft Decision**

	QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(1)	Our consolidated draft decision is that we do not consider it appropriate to treat the customer endorsement of the 2008 CRIMP as a determinative factor in forming our view on the appropriate allocation of WIRP costs to existing Blackwater users.	18.1	<b>Disagree.</b> The CDD undermines the Customer Voting and investment pre-approval processes, which were relied upon by Aurizon Network and WIRP Customers when making their respective investment decisions.
(1)	Our consolidated draft decision is that it would not be appropriate to exclude consideration of the WIRP access conditions when forming our consolidated draft decision.	18.2	<b>Agree with amendments.</b>
(1)	Our consolidated draft decision is that while the 2010 AU provisions relating to WIRP pricing are relevant to our consideration of the reference tariffs for WIRP under the 2014 DAU, we do not consider these provisions are determinative.	18.3	<b>Agree</b> , subject to the partial socialisation and System Premium pricing approach (outlined in the CDD) being retained for the Final Decision.
(1)	After considering Aurizon Network’s proposed capital indicator for WIRP in the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network’s original proposal.	18.4	<b>(2)(a) Agree.</b>
(2)	The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to: <ul style="list-style-type: none"> <li>(a) adjust the capital indicator for WIRP to use the post-tax nominal vanilla</li> </ul>		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
WACC for calculating interest during construction.		
(1) After considering Aurizon Network's proposed capital cost allocation approach for WIRP users, our consolidated draft decision is to approve Aurizon Network's original proposal.	18.5	<b>Agree.</b>
(1) After considering Aurizon Network's proposed capital cost allocation to non-WIRP users, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	18.6	<b>(2)(a) Agree with amendments.</b>
(2) The way in which we consider it is appropriate to amend the 2014 DAU is as follows:		<b>(2)(b) Disagree.</b> The QCA's CDD fails to recognise the benefits that WIRP Infrastructure will create for the Blackwater and Moura systems. Aurizon Network has provided additional evidence to quantify these benefits.
(a) Adjust the capital allocation for the WICET balloon loop to reflect that existing Blackwater train paths are expected to use this project segment.		<b>(2)(c) Agree.</b>
(b) Remove the capital allocation of Blackwater duplication costs to existing Blackwater system customers, for the purposes of defining incremental capital costs associated with WIRP infrastructure.		
(c) Remove the cost items identified above as renewals in nature from the WIRP capital indicator and reallocate them to the Blackwater capital indicator.		
(1) After considering Aurizon Network's proposed allocation of operating and maintenance costs to WIRP train services, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	18.7	<b>(2)(a) Agree.</b>
(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:		
(a) use Aurizon Network's December 2014 proposed WIRP operating and maintenance costs for 2015–16 and 2016–17.		
(1) After considering Aurizon Network's proposed volume forecasts for WIRP train services, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	18.8	<b>(2)(a) Agree</b> , subject to verification of QCA's calculations, which requires the provision of its detailed volume forecasts.

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:</p> <p>(a) use expected railings of WIRP and non-WIRP volumes option rather than a apportionment mechanism</p> <p>(b) adopt the forecast volumes for WIRP and non-WIRP train services consistent with Energy Economics' forecasts with adjustments to cap WIRP volumes to contracted volumes.</p>		<p><b>(2)(b) Agree</b>, subject to verification of QCA's calculations, which requires the provision of its detailed volume forecasts.</p>
<p>(1) After considering Aurizon Network's proposed pricing approach for WIRP train services, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:</p> <p>(a) use a system premium pricing approach.</p>	18.9	<p><b>(2)(a) Agree with amendments.</b></p>
<p>(1) After considering Aurizon Network's proposed pricing approach for WIRP train services in Blackwater, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.</p> <p>(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to:</p> <p>(a) address the impact of WIRP users that are not expected to rail during the 2014 DAU period, by application of our proposed revenue deferral mechanism to address the impact on expanding users resulting from the underutilisation of WIRP capacity over the remainder of the 2014 DAU period</p> <p>(b) apply the pricing arrangements outlined in this chapter for WIRP users, including applying a system premium for Rolleston train services.</p>	18.10	<p><b>(2)(a) Disagree.</b> Aurizon Network considers that this will expose it to an unacceptable level of stranding risk.</p> <p><b>(2)(b) Agree with the proposal for Blackwater users. Aurizon Network disagrees with the application of a system premium for Rolleston electric and non-electric train services.</b></p>
<p>(1) After considering Aurizon Network's proposed pricing approach for WIRP train services in Moura, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.</p>	18.11	<p><b>(a) Agree.</b> Noting that the QCA has flagged that it had insufficient time to consider the implications of Cockatoo Coal being placed into administration, Aurizon Network submits that no further revenue deferrals should be applied.</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to: <ul style="list-style-type: none"> <li data-bbox="354 310 808 422">(a) apply a system premium for WIRP Moura train services consistent with the pricing arrangements outlined in this consolidated draft decision.</li> </ul>		
(1) After considering Aurizon Network's proposed pricing approach for WIRP NCL train services from Colton, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	18.12	<b>(a) Agree.</b>
(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to: <ul style="list-style-type: none"> <li data-bbox="354 737 808 940">(a) apply the approach outlined in Aurizon Network's December 2014 WIRP pricing proposal, with the CCC for WIRP NCL train services escalated in accordance with CPI over the 2014 DAU regulatory period.</li> </ul>		

## CDD 18.1 CRIMP in the context of WIRP

The QCA's CDD 18.1 states that the QCA does not consider it appropriate to treat the customer endorsement of the 2008 CRIMP as a determinative factor in forming a view on the appropriate allocation of WIRP costs to existing Blackwater users.

For the reasons outlined in its response to the QCA's Draft Decision on WIRP pricing arrangements,<sup>155</sup> Aurizon Network disagrees with the QCA's CDD.

## CDD 18.2 WIRP access conditions

The QCA's CDD 18.2 states that it would not be appropriate to exclude consideration of the WIRP access conditions when forming its CDD on the WIRP pricing arrangements.

For the reasons outlined in its response to the QCA's Draft Decision on WIRP pricing arrangements,<sup>156</sup> Aurizon Network agrees with the QCA's CDD but suggests that the QCA also take the limitations of the WIRP access conditions into consideration.

In its CDD, the QCA acknowledges the limitations of the WIRP access conditions, but notes that "...it is unclear to us how that would deem the access conditions irrelevant to our assessment."<sup>157</sup> For clarity, Aurizon Network did not suggest this to negate the relevance of the WIRP access conditions, but to

<sup>155</sup> Aurizon Network (2015b). Aurizon Network Access Undertaking (2010): Reference Tariffs for Wiggins Island Rail Project Services, Response to QCA Draft Decision, p. 30.

<sup>156</sup> Aurizon Network (2015b). p. 33.

<sup>157</sup> Queensland Competition Authority (2015c). p. 140.

reinforce that the QCA should consider these limitations in seeking to appropriately balance the legitimate business interests of Aurizon Network with the interests of the relevant access holders.

In CDD 18.10, the QCA proposes to apply a revenue deferral mechanism on the basis that some WIRP users have delayed commencement of their WIRP train services until after the 2014DAU period ('WIRP deferral users') – a commercial decision of the producers, which is outside of Aurizon Network's control. As identified in its response to the QCA's Draft Decision on WIRP pricing arrangements, the WIRP Fee arrangement did not cover the entire scope of the WIRP project, with WIRP capex to the value of [REDACTED] not subject to any form of WIRP Fee.<sup>158</sup>

The QCA could appropriately recognise the limitations of the WIRP access conditions in the following manner:

- of the capex allocated to WIRP deferral users, identify the proportion not subject to access conditions. Aurizon Network has estimated this to be approximately \$17.3 million; and
- agree that revenue associated with this proportion of capital will not be deferred. For clarity, doing so will not require WIRP Blackwater or WIRP Rolleston train services to pay a system premium.

Aurizon Network considers this to be appropriate as the infrastructure not subject to access conditions is not specific to the WIRP deferral users and will be utilised by other WIRP train services which rail during the 2014DAU period.

### CDD 18.3 Applicable access undertaking

The QCA's CDD 18.3 states that while the 2010AU provisions relating to WIRP pricing are relevant to its consideration of the Reference Tariffs for WIRP under the 2014 DAU, it does not consider these provisions are determinative.

For the reasons outlined in its response to the QCA's Draft Decision on WIRP pricing arrangements,<sup>159</sup> Aurizon Network disagrees with the QCA's CDD and considers that regulatory decisions must place a significant weight on the approved principles that were relevant and relied upon by all parties at the time of committing to the investments.

Nevertheless, in the interests of achieving a timely resolution to the 2014DAU process, Aurizon Network is prepared to agree with the QCA's CDD, subject to the partial socialisation and system premium pricing approach (refer to Aurizon Networks response to CDD 18.9 – 18.11) being retained for the Final Decision. If this approach is not retained, Aurizon Network disagrees with CDD 18.3.

### CDD 18.6 Allocation of capital expenditure to non-WIRP users

The QCA's CDD 18.6 refuses to approve Aurizon Network's proposed capital cost allocations to non-WIRP users. Aurizon Network agrees with CDD 18.6 (a) and 18.6 (c). However, it disagrees with the QCA's proposal to remove the capital allocation of Blackwater duplication costs to existing Blackwater system customers, for the purposes of defining incremental capital costs associated with WIRP infrastructure (CDD 18.6(2)(b)).

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<sup>158</sup> Aurizon Network (2015b). p. 33.

<sup>159</sup> Aurizon Network (2015b). pp. 33-34.

In its response to the QCA’s Draft Decision on WIRP pricing arrangements, Aurizon Network provided a detailed commentary on the operational benefits that the Blackwater duplication programme will create for the Blackwater system.<sup>160</sup> In its CDD, the QCA does not consider that the benefits identified are sufficient to warrant any allocation of WIRP costs to existing Blackwater system customers for the purposes of defining incremental WIRP capital costs.

Aurizon Network disagrees with this CDD and maintains that the Blackwater duplication programme has created a number of material operational benefit in the Blackwater system. These benefits are evident in Aurizon Network’s WIRP submission.<sup>161</sup>

For example, the graph below also shows a material reduction in crossing delay minutes as a result of the Blackwater duplication programme.

**Figure 18.1 – Reduction in crossing delay minutes (Bluff – Callemondah)**



The Blackwater duplication programme has also resulted in scheduling efficiencies and improved cycle times for access holders. The net result of these improvements is that it delivers additional train services for the same consist requirements. Consider the worked example below:

<sup>160</sup> Aurizon Network (2015b). pp.18-27.

<sup>161</sup> Aurizon Network (2015b). pp.18-27.

Nominal Rollingstock Capacity	Blackwater System Consists	Hours available per week per consist	Total Consist Hours per Week	Average Cycle Time Hours per Train	Trains per Week
Pre-duplication	28	168	4,704	25.00	188.2
Post-duplication (45min / 0.75hr Cycle time reduction)	28	168	4,704	24.25	194.0
<b>Increased trains with same Rollingstock Fleet</b>					<b>5.8</b>

Additional Trains per Week	5.8
Value per Train Service	\$50,000
Weeks per Year	48
<b>Value per Year</b>	<b>\$13,966,515</b>

Aurizon Network contends that Blackwater duplications have facilitated the realisation of scheduling efficiencies, with the potential to deliver value of up to \$14million per annum in benefits to access holders. The Blackwater duplication program therefore creates tangible benefits which promotes the Objects of Part 5 of the QCA Act.

Aurizon Network would welcome the opportunity to discuss with the QCA how best to reflect these benefits as part of the cost allocation between WIRP and non-WIRP users.

## CDD 18.8 Volumes for WIRP train services

The QCA's CDD 18.8 refuses to approve Aurizon Network's original volume forecasts proposed for WIRP train services. As outlined in its response to the QCA's Draft Decision on WIRP pricing arrangements,<sup>162</sup> and in its response to CDD 21.1 below, Aurizon Network notes that the QCA was constrained in its ability to provide Aurizon Network with the detailed Energy Economics volume forecasts in relation to each origin and destination combination (due to confidentiality claims by some producers resulting in some aggregation of information). The practical consequence for Aurizon Network is that it has not had an adequate opportunity to fully assess the implications of the CDD.

While Aurizon Network would be prepared to agree with CDD 18.8(2)(a) and 18.8(2)(b), it is unable to give effect to these decisions in the absence of access to the detailed forecasts for each origin and destination combination. The only option available to Aurizon Network would be to apportion the aggregate forecast presented between WIRP customers, which would contravene CDD 18.8(2)(a).

In the interests of achieving a timely resolution to the 2014DAU process Aurizon Network is prepared to agree in principle with the QCA's aggregate CDD volume forecasts for WIRP Train Services. Aurizon Network notes that in the absence of the detailed Origin / Destination forecasts for all WIRP users, Aurizon Network cannot practically comply with either CDD 18.8(2)(a) or 18.8(2)(b) and has no option but to apportion the aggregate WIRP forecasts between individual WIRP Train Services.

<sup>162</sup> Aurizon Network (2015b). pp. 44-45.

## CDD 18.9 Assessment of WIRP pricing options

The QCA's CDD 18.9 refuses to approve Aurizon Network's proposed pricing approach for WIRP train services. Aurizon Network is required to amend its draft access undertaking to use a system premium pricing approach.

In the interests of achieving a timely resolution to the 2014DAU process, Aurizon Network is prepared to agree with the QCA's CDD, provided the QCA's final decision confirms the outcomes of Aurizon Network's financial analysis (as outlined in its responses to CDD 18.10, CDD 18.11 and CDD 18.12 below).

Aurizon Network remains concerned with elements of the QCA's assessment methodology as outlined in its response to the QCA's Draft Decision on WIRP pricing arrangements.<sup>163</sup> For example, the QCA's CDD to deduct the CCC from the 'base system' tariff, where these costs would be incurred in the absence of the new train service.

Unfortunately, the QCA was constrained in its ability to provide Aurizon Network with the detailed Energy Economics volume forecasts in a timely manner. The practical consequence for Aurizon Network is that it has not had an adequate opportunity to fully assess the implications of the CDD.

## CDD 18.10 Pricing arrangements for WIRP train services in Blackwater

The QCA's CDD 18.10 refuses to approve Aurizon Network's proposed pricing approach for WIRP train services in Blackwater.

Aurizon Network disagrees with the QCA's proposed revenue deferral mechanism (CDD 18.10(2)(a)). On the pricing arrangements to apply to WIRP users (CDD 18.10(2)(b)), Aurizon Network accepts the proposal for Blackwater users, however disagrees with the application of a system premium for Rolleston, particularly in the absence of the QCA's detailed volume forecasts.

### Revenue deferral

The QCA's CDD 18.10(2)(a) requires Aurizon Network to defer revenue associated with WIRP train services that are not expected to rail for the remainder of the 2014DAU period. In its response to the QCA's Draft Decision on WIRP pricing arrangements, Aurizon Network stated it could agree to defer revenue under the following conditions:<sup>164</sup>

- that the QCA calculates the quantum of the deferral with reference to Aurizon Network's volume forecasts (due to the lack of transparency of the Energy Economics forecasts); and that
- an explicit time limit be placed on the duration of the deferral. Aurizon Network proposed the end of the 2014DAU period, 30 June 2017.

The QCA has not agreed to either of these conditions in its CDD.

Aurizon Network is concerned that the QCA has not approved Aurizon Network's proposal to limit the duration of the revenue deferral. The QCA's CDD creates additional regulatory uncertainty for both Aurizon Network and network investors, and is inconsistent with the pricing principles in s168A(a) of the QCA Act. The risks associated with revenue deferral are biased against the legitimate business interests

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<sup>163</sup> Aurizon Network (2015b). pp. 49-52.

<sup>164</sup> Aurizon Network (2015b). p.56.

of Aurizon Network and network investors, who are penalised for risks that are entirely outside of its control and not contemplated at the time of making the investment decision. Further, the majority of WIRP infrastructure is not specific to individual WIRP users and will be utilised by both WIRP and non-WIRP users.

The proposed WIRP deferral is a primary example of Aurizon Network's exposure to asset stranding risk (refer Chapter 14), for which Aurizon Network is not compensated. As outlined in Chapter 14, this issue is a major priority for Aurizon Network and will remain so going into the UT5 review.

Aurizon Network therefore disagrees with CDD 18.10(2)(a) and proposes that:

- the revenue deferral should not apply to WIRP infrastructure that was exempted from the WIRP Fee arrangements (refer to Aurizon Network's response to CDD 18.2); and
- on 1 July 2017, the WIRP revenue deferral will cease to apply. The affected capital expenditure will be included in MAR and Reference Tariffs from this date onwards.

### **Pricing arrangements for WIRP Blackwater users**

Aurizon Network agrees with the QCA's CDD 18.10 (b) that the Blackwater system reference tariff will apply to WIRP Blackwater users.

Aurizon Network disagrees with the QCA's CDD to apply a system premium to WIRP Rolleston Train Services. Aurizon Network's financial modelling indicates that WIRP Rolleston should pay the Blackwater system reference tariff. Aurizon Network reiterates the comments made on this matter in its response to the QCA's Draft Decision on WIRP pricing arrangements.<sup>165</sup> Furthermore, Aurizon Network would welcome the opportunity to discuss the results of its modelling with the QCA in more detail.

### **Rolleston electric access charge**

Aurizon Network disagrees that Rolleston electric train services should be subject to an AT<sub>5</sub> system premium. Aurizon Network contends that Rolleston electric train services (to both RG Tanna and WICET) not only cover the incremental costs associated with the Bauhinia electrification project, but will also reduce the average electric price of the existing Blackwater system through greater utilisation.

Aurizon Network's financial modelling indicates that WIRP Rolleston should pay the Blackwater system AT<sub>5</sub> reference tariff, with no premium. Aurizon Network reiterates the comments made in this matter its response to the QCA's Draft Decision on WIRP pricing arrangements.<sup>166</sup> Aurizon Network would welcome the opportunity to discuss the results of its modelling with the QCA in more detail.

## **CDD 18.11 WIRP train services in Moura**

The QCA's CDD 18.11 refuses to approve Aurizon Network's proposed pricing approach for WIRP train services in Moura. The CDD requires Aurizon Network to apply a system premium for WIRP Moura train services. Aurizon Network agrees with the CDD. However, it would also like to flag concerns it has over any further changes that the QCA might seek to make in view of Cockatoo Coal being placed in administration.

Cockatoo Coal was placed into administration on 16 November 2015. The QCA's CDD states that it is yet to consider the implications of this development, but that it may require amendments to address the

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<sup>165</sup> Aurizon Network (2015b). p. 56.

<sup>166</sup> Aurizon Network (2015b). p. 56.

impact on volume forecasts for WIRP Moura and the pricing impact. In light of the QCA's CDD 18.10(2)(a), Aurizon Network has material concerns that the QCA will seek to address this development through the imposition of an additional revenue deferral mechanism.

The pricing arrangements proposed by the QCA in CDD 18.10(2)(a) requires Aurizon Network to defer revenue [REDACTED]. As outlined above, this exacerbates Aurizon Network's already significant exposure to asset stranding risk.

Aurizon Network reiterates that it is inappropriate for the QCA to seek to impose further WIRP revenue deferrals in relation to Cockatoo Coal. If the QCA is minded to do so, Aurizon Network considers it imperative that it be given the opportunity to discuss this with the QCA prior to it making any determination on this matter. If such a deferral were contemplated, Aurizon Network would wish to make submissions to the effect that:

- the extent of any such deferral must be limited to Cockatoo Coal's share of WIRP capex in the Moura system only;
- Cockatoo Coal's contribution towards the capital costs of the Wiggins Island Balloon Loop should be reallocated among all WIRP customers forecast to rail during the 2014DAU regulatory period;
- the deferral must be for a defined period (i.e. there must be a sunset date).

## Chapter 19 – Take or Pay Arrangements (Schedule F)

### Summary of Aurizon Network’s Position

Overall, there are no material issues emerging from the CDD in relation to Take or Pay provisions. As outlined in Chapter 15, it is intended that Aurizon Network undertake a major review of its pricing arrangements for UT5. The QCA has agreed that this needs to include consideration of Take or Pay.<sup>167</sup>

The CDD also requires amendments to improve the clarity and consistency of the Take or Pay liabilities. Aurizon Network agrees with the revised drafting in Schedule F of the CDD amended DAU except where noted in this response and has proposed alternative amendments.

A more material change proposed for UT4 was the introduction of operator capping provisions, which was intended to allow operators to better manage their Take or Pay liabilities. Aurizon Network has accepted the QCA’s removal of these provisions as it agrees that the short term capacity transfer mechanism should provide a better way to manage Take or Pay exposures.

Aurizon Network’s residual comments on the issues emerging from the CDD are outlined below.

**Table 19.1 – QCA Consolidated Draft Decision**

	QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(1)	After considering Aurizon Network’s proposed changes to its take-or-pay capping arrangements, our consolidated draft decision is to refuse to approve Aurizon Network’s original proposal.	19.1	<b>2(a) Agree.</b>  <b>2(b) Agree.</b>
(2)	The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to: <ul style="list-style-type: none"> <li>(v) improve the clarity and consistency of this provision</li> <li><b>(w)</b> remove the operator capping provisions.</li> </ul>		
(1)	After considering Aurizon Network’s proposed changes to its take-or-pay capping arrangements, our consolidated draft decision is to refuse to approve Aurizon Network’s original proposal.	19.2	<b>(2)(a) Agree.</b>  <b>(2)(b) Agree with amendments.</b>
(2)	The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to remove: <ul style="list-style-type: none"> <li><b>(a)</b> the exclusion of WICET gtk’s from the take-or-pay trigger test for UT1 access holders</li> <li><b>(b)</b> the provision to shift Aurizon Network Cause paths from a post-UT1 agreement to a UT1</li> </ul>		

<sup>167</sup> Queensland Competition Authority (2015c). p.10.

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
agreement regarding a particular origin-destination pair.		
(1) After considering Aurizon Network's proposed drafting relating to take-or-pay arrangements, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	19.3	<b>(2)(a) Disagree.</b> Clause 2.4(h) (i) of Aurizon Network's 2014 DAU should be reinserted to enable Network to apply Take or Pay to a capacity multiplier.
(2) The way in which we consider it is appropriate that Aurizon Network amend its draft access undertaking is to: <ul style="list-style-type: none"> <li data-bbox="354 590 792 674">(c) remove subclause 2.4(h)(i) in Schedule F of Aurizon Network's 2014 DAU</li> <li data-bbox="354 674 792 821">(d) amend Aurizon Network's take-or-pay provisions (as presented in our CDD amended DAU) to improve the clarity and certainty of take-or-pay arrangements.</li> </ul>		

## CDD 19.2 - Potential inequities between different Take or Pay arrangements

CDD 19.2(2)(a) is to remove the exclusion of WICET gross tonne kilometres (gtks) from the Take or Pay trigger test for UT1 access holders. While the QCA has applied volumes that are different from those proposed in Aurizon Network's response to the MAR Draft Decision, it has agreed with Aurizon Network that forecasts are based on expected railings and not a percentage of contract. This is important because UT1 access holders' Take or Pay liabilities are not subject to capping so would bear a disproportionate level of volume risk if the CDD forecast is inaccurate.

Aurizon Network is also prepared to accept CDD 19.2(2)(b), which requires Aurizon Network to remove the provision to shift Aurizon Network Cause paths from a post-UT1 agreement to a UT1 agreement regarding a particular origin-destination pair. In the CDD the QCA stated that it agrees with Aurizon Network's alternative proposal that allocation for all access holders in the circumstances where the access holder and origin-destination pair are the same, is aligned with the consumption of TSEs.<sup>168</sup>

In its response to the MAR Draft Decision<sup>169</sup>, Aurizon Network proposed alternative drafting to give effect to its proposed allocation of paths not operated due to an Aurizon Network Cause, which was:

- firstly to UT1 Access Agreements;
- then to UT2 Access Agreements; and
- then to UT3 Access Agreements; and
- then to UT4 Access Agreements (once signed).

<sup>168</sup> Queensland Competition Authority (2015c). p.221.

<sup>169</sup> Aurizon Network (2014a). s.18.4, p.265.

Aurizon Network proposed this alternative because access holders do not currently nominate TSE consumption by contract when placing train orders where there is more than one access agreement for the same origin-destination pairing.

Aurizon Network recognises that in the event that an access holder did nominate when placing train orders that the TSE consumption should be different to the alternative drafting proposed above, then the Schedule F drafting would also need to cover that event. Aurizon Network has proposed a further change to Schedule F to improve clarity. Aurizon Network is therefore prepared to agree with CDD 19.2(2)(b) on the basis that the QCA accepts the alternative drafting that Aurizon Network has proposed in order to reflect the intent of the CDD.

## CDD 19.3 Other specific drafting

CDD 19.3(2)(a) is to remove clause 2.4(h)(i) in Schedule F of Aurizon Network's 2014 DAU, which relates to determining the capacity multiplier for the purpose of Take or Pay. Aurizon Network disagrees with the CDD. This clause is required to ensure that a capacity multiplier can be included in the Take or Pay calculation where it is applicable. The QCA considers that the clause is not required as the application is covered in clauses 6.2.2(d) (Part 6) and clause 3.3(d)(iii) (Schedule F) of the CDD amended DAU. However, Aurizon Network believes that the clause is required in order to apply the intent of those clauses in the Take or Pay calculation. Accordingly, this clause needs to be reinstated.

## Chapter 20 – Maximum Allowable Revenue

### Summary of Aurizon Network’s Position

Aurizon Network disagrees with the QCA’s CDD on MAR, which it considers insufficient to meet its efficient costs of providing access to the CQCR, including a return on investment commensurate with the regulatory and commercial risks involved.

The delays in the QCA’s assessment of the 2014DAU has created considerable uncertainty for both Aurizon Network and the industry. Given the importance of a timely resolution of UT4, and based on discussions with industry, Aurizon Network has therefore been willing to agree to the QCA’s CDD for the majority of the decisions that relate to the MAR, as set out in Chapters 21 to 29 of this response. It will review all of these matters in detail for the UT5 review, including the methodology and assumptions applied in setting Aurizon Network’s WACC. As noted previously, this will also need to be considered in the context of Aurizon Network’s broader exposure to asset stranding risk.

The key areas where it cannot agree are:

- the QCA’s proposed ballast undercutting allowance (refer response to CDD 24);
- the QCA’s refusal to approve GAPE cost allocations to the Newlands system (refer response to CDD 17.2); and
- WIRP revenue deferral of capital expenditure not subject to a WIRP Fee arrangement (refer response to CDD 18.10);
- modelling inconsistencies in the CDD (refer response to CDD 29).

Otherwise, the other amendments proposed in this response are not material.

Aurizon Network has proposed amendments to the MAR outlined in the QCA’s CDD. These amendments are summarised as follows:

**Table 20.1 - Summary of MAR proposal (\$ million)**

Cost	QCA CDD	Aurizon Network submission	Difference	Reason for change
Return on Capital	1,533	1,532	(1)	Aurizon Network proposed to defer capital relating to GAPE Remote Control Signalling for pricing purposes (refer response to CDD 26.1)
Inflation	(522)	(519)	3	
Depreciation	1,268	1,300	32	The QCA has incorrectly applied the UT2 asset lives when calculating the RAB roll-forward. This has resulted in the QCA understating depreciation in the CDD (refer response to CDD 27.1 & 29.1)
Maintenance	800	824	24	\$20m increase in Ballast and \$4m from the inclusion of Return

Cost	QCA CDD	Aurizon Network submission	Difference	Reason for change
				on Inventory (refer response to CDD 23.2 and 24.2)
Operating Costs	805	814	9	Adjustments for Train Control, business management costs and Audit Costs( refer response to CDD 22.5)
Working Capital	12	12	0	
Tax and imputation credits	141	150	9	Aurizon Mid-year timing assumption applied to tax depreciation ( refer response to CDD 29.1)
Capital carryover	(110)	(125)	(15)	The QCA has included capital relating to NAPE in the Capital Carryover for GAPE, which Aurizon Network had deferred (refer response to CDD 26.2)  Mid-year timing assumption applied by Aurizon Network ( refer response to CDD 29.1)
<b>Total MAR</b>	<b>3,927</b>	<b>3,989</b>	<b>62</b>	

Note: Numbers may not sum due to rounding.

**Table 20.2 – QCA Consolidated Draft Decision**

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1) Our consolidated draft decision is to refuse to approve the 2014 DAU insofar as it relates to the MAR. Our proposed reasons for this refusal are set out in detail in this consolidated draft decision and are, in essence, that the MAR proposed by Aurizon Network is too high. In this consolidated draft decision, our proposed MAR for the 2014 DAU period (2013–14 to 2016–17) is the (Adjusted) Total MAR identified in Table 6.	20.1	<b>Disagree.</b>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1) After considering Aurizon Network's proposal to smooth the difference between 2013–14 allowable and actual revenues over the 2014–15, 2015–16, 2016–17 period, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.	20.2	<b>(1) Agree.</b>
(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is to calculate the difference between the 2013–14 approved allowable and transitional revenues and recover this amount over the 2014–15, 2015–16, and 2016–17 period.		<b>(2) Agree.</b>
(3) The difference between 2014–15 and 2015–16 approved allowable and transitional revenues should be recovered or returned to access holders via an adjustment charge approach under the normal revenue cap arrangements.		<b>(3) Disagree.</b> The variance between FY2015 approved allowable and transitional revenues should not be recovered through an adjustment charge. Aurizon Network has proposed an alternative. However an adjustment charge is appropriate to account for the difference between FY2016 approved allowable and transitional revenues (incorporating any revenues associated with the UT4 reconciliation).

## CDD 20.1 QCA's proposed Maximum Allowable Revenue

The QCA's CDD 20.1 is to refuse to approve Aurizon Network's proposed MAR for the 2014DAU period.

Aurizon Network disagrees with the QCA's proposed MAR. As outlined in its response to the QCA's Draft Decision on MAR,<sup>170</sup> Aurizon Network maintains that the amendments it has made to the 2014DAU result in a MAR that provides for the lowest sustainable and efficient prices while still providing for an efficient level of service. It submits that the amended 2014DAU gives regard to:

- the object clause of Part 5 of the QCA Act;
- the matters set out in section 138(2) of the QCA Act, including the legitimate business interests of Aurizon Network, the public interest and the interests of persons who may seek access to the service; and
- the pricing principles in section 168A of the QCA Act, including that the proposed MAR should provide for prices that should generate expected revenue for the service that is at least enough to meet the efficient costs of providing access to the service and include a return on investment commensurate with the regulatory and commercial risks involved.

Aurizon Network has, throughout this and its previous submissions to the QCA, obtained independent expert advice from economic and financial advisers, benchmarked against meaningful comparator firms, and applied its own considerable experience in operating the CQCR. Where available, it has sought to update the MAR to reflect actual costs incurred during the UT4 period to date, even where this has been to Aurizon Network's detriment.

<sup>170</sup> Queensland Competition Authority (2014a). Draft Decision: Aurizon Network 2014 Draft Access Undertaking – Maximum Allowable Revenue. p. 4.

The table below summarises the proposed MAR adjustments. For more detail, please refer to the relevant sections of this submission.

**Table 20.3 Aurizon Network’s proposed MAR for the CQCR (\$’000, nominal)**

Building Blocks	2013/14	2014/15	2015/16	2016/17
Return on Capital	343,547	359,985	411,818	417,039
Inflation	(154,292)	(75,943)	(143,620)	(145,440)
Depreciation	280,698	301,568	353,893	364,310
Maintenance	193,462	207,437	207,018	216,026
Operating Costs	190,621	194,559	213,993	215,273
Working Capital	2,562	2,963	3,129	3,202
Tax and imputation credits	26,365	42,786	39,010	42,233
<b>Total (unsmoothed) MAR</b>	<b>882,962</b>	<b>1,033,356</b>	<b>1,085,242</b>	<b>1,112,642</b>
UT3 capital carryover	(29,151)	(30,463)	(31,834)	(33,267)
<b>Adjusted Total MAR</b>	<b>853,811</b>	<b>1,002,893</b>	<b>1,053,408</b>	<b>1,079,375</b>

*Note: Numbers may not sum due to rounding.*

As submitted in the response to the Policy and Pricing Draft Decision<sup>171</sup>, Aurizon Network has identified a number of decisions, if implemented would give rise to increased costs for Aurizon Network beyond what is allowed in the MAR. Aurizon Network has updated the list in Table 20.4 to reflect the changes in the CDD.

Aurizon Network’s position regarding each of the items remains consistent with this response submission. Provision of the cost estimation should not be considered as the acceptance of the decisions. However, to the extent that the QCA remains committed to the decisions on the specific item, Aurizon Network requests the additional costs to be included in the final MAR.

Where possible, Aurizon Network has provided an estimate of the costs that are likely to be incurred as a result of the relevant QCA decisions and proposes the aggregate amount to be included in the final MAR. Where it is not possible to provide an estimate of the likely costs, Aurizon Network considers it appropriate that any such costs should be recoverable through the revenue cap process. Aurizon Network has proposed to amend the drafting in Schedule F to facilitate the process by which Aurizon Network can recover all these additional costs.<sup>172</sup>

<sup>171</sup> Aurizon Network (2015a). pp. 32-35.

<sup>172</sup> Refer to Section CDD 17.5 in Chapter 17.

**Table 20.4 – MAR Implications of QCA’s Consolidated Draft Decision**

Clause/ CDI	QCA Proposal	Aurizon Network View of MAR Implication	High-level Cost Estimation (\$)	Comment
Clause 3.12(f)	All recipients not within Aurizon Network to enter into a legally enforceable agreement with Network	Additional administrative costs on Aurizon Network, and it will slow down operations	\$120,000 per annum	The amount covers the additional administrative costs.
Clause 3.12(h)	Prior written consent of the owner of the Confidential Information is provided for the access or disclosure to the Recipient for the nominated purpose	Additional costs associated with gaining written consent from the third party for Aurizon Network to complete daily tasks		
Clause 3.14	Confidential Information Register requirements	Additional IT costs associated with building a database to interlink with internal systems to record all required information, and generate reports for auditing purposes	\$140,000	This is the indicative cost for IT changes. Given the uncertain nature of IT project, Aurizon Network will seek to recover the efficient costs through Schedule F if additional costs arise.
Clause 3.15	<p>The QCA requires: A briefing session – All Aurizon Group employees whose role requires access to Confidential Information (300-400 persons)</p> <p>Detailed Training sessions – High Risk Personnel (100 persons)</p> <p>There is a requirement for new employees in any of the 2 categories to be trained within a certain timeframe. It would be required to continuously train these persons</p>	A session is understood to be a face to face session undertaken by a Ringfencing expert.	\$140,000 per annum	The amount covers the cost of the trainer and the travelling expenses associated with the briefing sessions.

Clause/ CDI	QCA Proposal	Aurizon Network View of MAR Implication	High-level Cost Estimation (\$)	Comment
Clause 3.18	The QCA expands security measure to all Aurizon Network premises and requires accompaniment of non Aurizon Network staff at all times.	Additional security costs Additional administrative costs with the stringent requirement.	-	Refer to the definition issue of premise located in CDD Response Part 4. The requirement will result in the non-compliance of Aurizon Network and the cost is unquantifiable at this stage. Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
Clause 3.18(d)	The QCA requires all personnel who enter an Aurizon premise which holds ringfencing information to be recorded within a register	This would require resources at all CQCR sites to record who is entering their premises at all times. This would also include all personnel on all floors not a part of the Aurizon Group	\$10,000	Refer to the definition issue of premise located in CDD Response Part 4. The amount covers the necessary IT upgrades.
CDD 6.1	The QCA has broadened the scope of disputes and allowed any party to raise a dispute.	This increases the risk of excessive claims and increase the administrative costs.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
CDD 7.3	Clause 4.8(a)(ii)(D) requires Aurizon Network to negotiate with multiple operators and access seekers for the same access rights before the end user appoint a rail operator.	Additional administrative costs associated with multiple concurrent negotiations.	\$130,000 per annum	This estimation assumes 10 concurrent negotiations each year, and provides allowance for additional legal fee and administrative costs associated. However, this amount excludes other additional resources that may be required in the negotiation.
CDD 10.1	The QCA requires Aurizon Network to participate in any coal supply chain group's master plan, review capacity options and investigate operational capacity enhancing improvement.	This requires additional modelling and planning resources to operate across all the relevant supply chain groups in accessing operation enhancements, which means additional administrative costs.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
CDD 10.2	The QCA can require an independent review of the capacity.	Aurizon Network would have to support the review through provision of staff to demonstrate the model, explain the logic and undertake scenarios to support the review	-	The most recent GCEE audit required significant time to support. We anticipate slightly greater time to reflect a broader scope. Aurizon Network will seek to recover the costs through Schedule F if the cost arises.

Clause/ CDI	QCA Proposal	Aurizon Network View of MAR Implication	High-level Cost Estimation (\$)	Comment
CDD 10.4	The QCA requires Aurizon Network to consult with all access holders, end customers and supply chain groups on all capacity and operation assumptions which underpin baseline capacity review.	This level of consultation requires substantial amount of time and resources. It increases the administrative costs for Aurizon Network.	\$60,000 per annum	Expanding consultation to individual operators and access holders increases the administrative costs. It is expected that the additional amount of consultation requires half full-time equivalent employee.
CDD 10.5	The QCA requires dynamic assessment to be performed on all options examined in the NDP.	This would significantly increase the cost of each study. Additional IT costs to facilitate this will also be incurred.	\$2.88 mil per annum	Typically 1% of the total project costs is allocated to cover pre concept and concept studies. It is reasonable to allocate 1% of this amount to engineering requirements for dynamic simulation development. Take 2014 NDP for example, this amount equals \$2.88 m.
CDD 11.2	Clause 7.2.3(a)(iii) requires any party that has an interest in existing access rights to be included in the committed capacity register.	This increases the administrative costs associated with maintaining the committed capacity register.	\$30,000 per annum	This amount covers costs associated with continuous communication with additional parties listed in the committed capacity register. It may vary with demand for capacity.
CDD 12.4	The QCA requires all processes and decisions made with respect to the expansion process are subject to the dispute resolution mechanism.	The fact everything in expansion domain can go for resolution is likely to increase the costs.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
CDD 12.11	The QCA includes additional triggers to review Standard User Funding Agreement (SUFA) framework.	Any review of SUFA will entail substantial costs, demonstrated by the current SUFA development process.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
CDD 12.12	The QCA requires Aurizon Network to commit to developing a suite of tax efficient financing options for small to medium expansion projects.	Exploring a new suite of options requires substantial resources and involves substantial costs.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.

Clause/ CDI	QCA Proposal	Aurizon Network View of MAR Implication	High-level Cost Estimation (\$)	Comment
CDD 13.1	Additional ringfencing and confidentiality requirements around train plans.	This will increase workload to manage the various levels of disclosure permitted under existing Access Agreements.	\$120,000 per annum	Additional administrative burden for Aurizon Network to prepare reports and manage various different levels of disclosure across Access Holders.
CDD 13.3	The QCA has requested Aurizon Network setting out of the assumptions used in development of the Master Train Plan (MTP) and to track all changes to the MTP.	This will increase workload and delay delivery and requires software enhancements for both ViziRail and Network Operations Pathing Planner (NOPP).	\$410,000 per annum	Option 1: This amount covers the costs associated with generating CQCN MTP monthly from PlaniMate to be published in ViziRail. It also provides allowance for a report outlining assumptions used and the software upgrade. Option 2: The cost can be reduced to \$170,000 per annum if it is tabled out from PlaniMate as a static snapshot without track changes.
CDD 13.4	The QCA has requested additional transparency in NOPP and ViziRail for the Intermediate Train Plan (ITP).	This will require software enhancements for both ViziRail and NOPP and training for resources which use these systems.	\$120,000 per annum	Aurizon Network will extend the scheduling horizon in ViziRail from 4 days to 7 days (Goonyella System) using the existing approach, which is resource intensive. It is estimated to cost around \$120,000 per year.
CDD 13.5	The QCA requires Aurizon Network to provide full transparency of train paths allocated to maintenance.	To facilitate the inclusion of maintenance paths, the NOPP and ViziRail software need to be upgraded. This increases the IT costs.	\$100,000	The amount covers the IT upgrade costs. Given the uncertain nature of IT project, Aurizon Network will seek to recover the efficient costs through Schedule F if additional costs arise.
CDD 13.6	The QCA requires Aurizon Network to include reporting of planned services in the ITP and Daily Train Plan (DTP) in the monthly train service entitlement (TSE) notice, and also publish a monthly aggregate TSE reconciliation report by systems.	Including planned services in DTP is especially resource intensive and may require changes to IT systems. Therefore, additional IT costs and administrative costs. Moreover, additional administrative costs is required for the reconciliation report.	\$240,000 per annum	Including DTP is resource intensive and requires additional staffing for both north and south scheduling team.

Clause/ CDI	QCA Proposal	Aurizon Network View of MAR Implication	High-level Cost Estimation (\$)	Comment
CDD 14.4	The QCA extends the voting process to include scope, standard, cost and capacity.	It will increase the resources required for the voting process given the increased voting scope.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
CDD 14.5	The QCA has broadened the interested parties in the voting process.	It costs more to consult more widely.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
CDD 14.7	The QCA requires Aurizon Network to adopt a 'best endeavours' approach when providing information, conducting forums and engaging in discussions with interested participants in relation to a voting proposal.	'Best endeavours' means Aurizon Network needs to spend whatever is required rather whatever is reasonable in the process.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
CDD 14.9	The QCA requires Aurizon Network to redo the voting process if the auditor identifies a flaw in the vote of interested participants.	Redoing the voting process even if the flaw is minor and does not affect the outcome will unduly increase the voting costs.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
Clause 8.8.1(a)(ii) of the DAU	This clause requires Aurizon Network to negotiate with funders (not just access seekers).	Parallel negotiation will increase the associated costs.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
16.14	The QCA expands UT3 access condition provisions to require non-standard terms that have cost and risk implications to Aurizon Network to be subject to QCA approval.	The approval process increases the administrative costs with non-standard agreements.	-	Aurizon Network will seek to recover the costs through Schedule F if the cost arises.
Clause 3.2 AA and TOD	The QCA has amended the Access Agreements (AA) and Train Operations Deed (TOD) such that certain terms are incorporated by reference from the Access Undertaking (AU).	This will result in Aurizon Network potentially being required to amend at the same time, a large number of AA / TOD to reflect Change in Undertaking each 4 year regulatory period where AA's usually run for 10 year terms.	\$25,000 for each change in Undertaking	This amount assumes one set of amendments will be developed and then updated consistently. If extensive negotiation is allowed, it will increase considerably more. Aurizon Network will seek to recover the efficient costs through Schedule F if additional costs arise.

Clause/ CDI	QCA Proposal	Aurizon Network View of MAR Implication	High-level Cost Estimation (\$)	Comment
	With the exception of Access Charge Provisions and Reference Tariff Provisions, all other Incorporated Provisions are those provisions in the AU in force at time of entering into the AA/TOD. Where there is a change to those Incorporated Provisions in subsequent AU's (Change in Undertaking) either party may elect to amend the AA / TOD to reflect the Change in Undertaking.	This will create additional workload for Aurizon Network and require extra resources to ensure Aurizon Network complies with its obligations to amend the AA/TOD within the specified timeframes – particularly in the potential scenario where all Access Holders seek amendments immediately following a Change in Undertaking.		
Clause 28 – AA and TOD	The QCA has amended the Force Majeure Provisions such that Aurizon Network is required to provide initial and further FM notices within specified timeframes and included detailed requirements in relation to information to be provided in the FM notices.	<p>The QCA amendments will require Aurizon Network to consider:</p> <ul style="list-style-type: none"> <li>• changes to business systems including ViziRail reporting, CLMS systems and workflow automation systems to meet QCA timeframes and information requirements in the initial and further notices;</li> <li>• additional resourcing to ensure adherence to proposed timeframes and information requirements are met – specifically having dedicated resources to monitor and manage the FM governance process</li> </ul>	\$30,000 per annum and \$100,000 for IT costs	<p>\$30,000 covers the additional workload in managing the FM governance process.</p> <p>The IT costs is an indicative amount and may change due to the uncertain nature of IT project. Aurizon Network will seek to recover the efficient costs through Schedule F if additional costs arise.</p>
Clause 16.4 TOD	The QCA have amended to require Aurizon Network to notify Operators where Aurizon Network is aware of a circumstance that has or could impact a Train from meeting it's Scheduled Time (+/- 3 minutes)	This will require Aurizon Network to significantly increase its resourcing in the Train Control Centre in order to comply with this obligation and is likely to require several dedicated resources to meet this obligation.	-	It requires a dedicated 24x7 call centre for each of the 9 control boards as well as IT system upgrade costs. The total costs will be in millions of dollars.

Clause/ CDI	QCA Proposal	Aurizon Network View of MAR Implication	High-level Cost Estimation (\$)	Comment
		On an average 24 hour day there are upwards of 700 delays between 3-19 minutes. On the basis it will take 2 minutes per call to an Operator and there being 3 Operators in the system, it would take over 24 hours to notify the Operators. This means Aurizon Network would potentially require at least 2 dedicated resources on a 24 hour shift to meet this obligation.		However, as per Aurizon Network's submission, this clause is not workable in practice.  If the QCA retains the clause in the Final Decision, the QCA should ensure appropriate allowance is provided in the MAR.
Transfer Provisions	<p>The QCA have amended the Transfer Provisions such that Aurizon Network is required to conduct capacity assessments for transfers within very short timeframes, the shortest being 2 business days of receipt.</p> <p>As the QCA have merged the Short Term Transfer process with the transfer process under the Access Agreement – Aurizon Network will need to assess whether the agreements will need to be formally amended.</p>	<p>Aurizon Network will require additional resources in order to meet the capacity assessment requirements under the QCA timeframes.</p> <p>Aurizon Network may also require additional resources in the commercial teams to reflect any transfers in the Access Agreements.</p>	\$120,000 per annum	<p>This amount covers the capacity assessment costs within such as short timeframe and is based on the volume of recent requests. The cost may increase if transfer requests increase.</p> <p>This amount does not include the costs of potential additional resources in the commercial teams. Aurizon Network will seek to recover the efficient costs through Schedule F if additional costs arise.</p>

## CDD 20.2 Transitional matters relating to UT4 MAR

Clause 12.4 of the CDD amended undertaking deals with matters relating to the transition from the 2010AU to the 2014DAU. The original termination date of the 2010AU was 30 June 2013. The 2010AU has since been extended on a number of occasions to ensure that transitional arrangements for FY2014, FY2015 and FY2016 were in place during the QCA's consideration of the 2014DAU. The final approval of the 2014DAU will require a reconciliation between the transitional allowable revenues and 'final' allowable revenues approved by the QCA for the UT4 regulatory period.

Aurizon Network has proposed a number of drafting changes to section 12.4 to give effect to the reconciliation process (as outlined below) upon approval of the 2014DAU.

### **FY2014**

The QCA's CDD 20.2(1) is to refuse to approve Aurizon Network's proposal to smooth the difference between FY2014 allowable and actual revenues over the FY2015, FY2016 and FY2017 years. In CDD 20.2(2), the QCA requires Aurizon Network to calculate the difference between the FY2014 approved allowable and transitional revenues and recover this amount over the FY2015, FY2016 and FY2017 years.

Aurizon Network accepts the QCA's CDD on the basis that in July 2014, Aurizon Network reimbursed approximately \$70 million to access holders in the Blackwater and Goonyella systems.<sup>173</sup> The reimbursement reflected the difference between actual and approved transitional revenues for FY2014.

### **FY2015**

The QCA's CDD 20.2(3) is to recover (or return) the difference between approved allowable and transitional revenues for FY2015 and FY2016 via an adjustment charge approach under the normal revenue cap arrangements. Aurizon Network disagrees with CDD 20.2(3).

The effect of the QCA's CDD is that a retrospective adjustment charge would apply, backdated to 1 July 2014. Aurizon Network notes that the QCA's proposed treatment for FY2015 is likely to be based on comments made by both the QRC and Aurizon Network at the time when a Final Decision on the 2014DAU was expected to be made in 2014/15. These comments are no longer relevant because a Final Decision was not made in FY2015 and Aurizon Network is now operating under transitional arrangements for FY2016.

Aurizon Network proposes that the difference between the approved FY2015 allowable and transitional revenues is smoothed over the FY2016 and FY2017 years.

Aurizon Network intends to work with the QRC and the QCA to seek to agree the most appropriate mechanism, in terms of future recovery, for this amount. For clarity, Aurizon Network's position is that the amounts will not be recovered on an individual Access Holder basis by reference to the actual railings during FY2015. This is consistent with the QCA's proposed approach (as per the CDD) for FY2014 adjustments, under which the adjustment has been built into the reference tariffs for FY2015, FY2016 and FY2017.

The FY2015 revenue cap adjustment will be included in the tariffs for FY2017.

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<sup>173</sup> For more information, refer to Aurizon Network's 'FY2014 Adjustment Charges' submission, available at: [www.qca.org.au](http://www.qca.org.au)

Aurizon Network understands that the proposal to defer the recovery of all adjustments relating to FY2015 to later years is supported by the QRC.

### **FY2016**

Aurizon Network agrees that the QCA's CDD 20.2(3) is appropriate in the context of the FY2016 adjustment. The difference between the transitional actual revenues and the approved allowable revenues will be recovered (or returned) to access holders via a single Adjustment Charge, in accordance with clause 6 in Schedule F of the 2014DAU.

To achieve this, the following would need to occur:

- the QCA makes a Final Decision on MAR by 30 June 2016, which confirms the 'final' Reference Tariffs for FY2016, based on:
  - the approved 'final' MAR for FY2016; and
  - the approved 'final' volume forecast for FY2016;
- the final Reference Tariffs for FY2016 will be backdated to 1 July 2015;
- Aurizon Network invoices access holders on the basis of the transitional Reference Tariffs for FY2016, with the full adjustment to be collected from, or returned to, access holders via an Adjustment Charge;
- by 31 August 2016, Aurizon Network submits to the QCA a single Adjustment Charge, equivalent to the difference between the final and transitional Reference Tariffs applied to actual volumes for the full year ending 30 June 2016.

Take or Pay and revenue cap arrangements for FY2016 would continue to operate but based on the final gtk forecasts and SAR approved by the QCA for this year. This proposal is similar to the process applied in finalising the pricing arrangements for the first year of UT3.

## Chapter 21 – Volume Forecasts

### Summary of Aurizon Network's Position

Aurizon Network is prepared to agree with the QCA's volume forecasts, subject to amending the FY2014 and FY2015 years to reflect actual volumes railed. Aurizon Network also notes that the QCA was not able to provide it with the details by each origin and destination combination underpinning Energy Economics' forecasts in a timely manner, which prevents it from fully considering the QCA's proposed forecasts. This was due to confidentiality claims by some producers resulting in some aggregation of information.

**Table 21.1 – QCA Consolidated Draft Decision**

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1) After considering Aurizon Network's proposed forecast volumes, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	21.1	<b>Agree with amendments.</b>
(2) We consider that Aurizon Network's December 2014 submission that actual volumes be used for 2013–14 and 2014–15 is appropriate. For the remaining years we consider that Energy Economics' revised forecast are appropriate. Therefore the way in which we consider it appropriate that Aurizon Network amend its 2014 draft access undertaking is to use the actual and forecast volumes as specified in Section 21.7 Table 13.		

### CDD 21.1 Volume Forecasts

In order to appropriately assess the pricing implications for the CQCR as a result of the QCA's proposed volume forecasts, Aurizon Network requested that the QCA provide it with a detailed breakdown of the volume forecasts prepared by Energy Economics. Unfortunately, the QCA was not able to provide Aurizon Network with this information requested in a timely manner. This was due to confidentiality claims by some producers resulting in some aggregation of information. It is therefore difficult for Aurizon Network to comprehensively comment on the reasonableness of the QCA's CDD.

In reviewing the CDD forecasts at a system level, Aurizon Network notes that the QCA's forecasts for the Goonyella system in FY2016 and FY2017 are lower than expected, whilst Moura and Newlands are higher than expected. Despite this, and in the interests of achieving a timely resolution to the 2014DAU process, Aurizon Network is prepared to agree with the QCA's CDD volume forecasts at a system level, subject to the QCA accepting the following:

- Aurizon Network agree that actual volumes be used for FY2014 and FY2015 but they require correcting to reflect actual volumes railed, as published in Aurizon Network's revenue cap adjustment submissions and approved by the QCA;
- in the interests of promoting regulatory stability, forecasts for FY2016 and FY2017 are to be considered 'final' forecasts for the 2014DAU period and should not be revised;

- Aurizon Network reserves the right to critique the origin/destination level forecasts if the QCA provides the full details without aggregation, which may necessitate the submission of a DAAU if Aurizon Network identifies any material concerns;

- [REDACTED]

In light of the comments made by Energy Economics,<sup>174</sup> Aurizon Network also wishes to clarify the basis upon which it determines volume forecasts for the CQCR. Aurizon Network’s volume forecasts for the regulatory period are based on expectations of future railings in each coal system at a point in time. The factors that it takes into account include:

- the demand outlook for domestic and export coal in the CQCR;
- contracted volumes;
- capacity of the supply chain;
- expected production growth; and
- incremental capacity delivered by expansions and new mines.

Aurizon Network prepares detailed estimates for each producer on the basis of expected railings between each origin and destination pair. This process is used to determine the aggregate forecasts for each coal system.

There is obviously a degree of judgement applied when setting forecasts at an origin/destination level. For the purpose of calculating the Reference Tariffs applicable to each coal system, it is important that the process for doing so is consistent and equitable for all producers. As a result, Aurizon Network apportions the aggregate forecasts for the individual coal system (based on expected railings) between each origin/destination pair in accordance with its share of total volumes contracted in that coal system.

This removes the potential for volume forecasts to bias the Reference Tariffs and ensures that Reference Tariffs are set on an impartial, consistent and equitable basis for all producers.

## Summary

Noting the above concerns about the lack of transparency through to the detail of Energy Economics’ volume forecasts, Aurizon Network agrees with CDD 21.1 subject to amending FY2014 and FY2015 to reflect actual volumes railed, as published in Aurizon Network’s revenue cap submissions. The table below presents Aurizon Network’s revised proposal for the 2014DAU.

**Table 21.2 – Aurizon Network’s revised volume forecasts (million tonnes)**

Volume Forecast	2013/14 (actual)	2014/15 (actual)	2015/16 (forecast)	2016/17 (forecast)
Blackwater	66.4	63.7	66.2	67.8
Goonyella	111.2	119.6	112.1	115.6
Moura	12.4	12.3	13.6	14.3

<sup>174</sup> Queensland Competition Authority (2015b). p.23.

<b>Volume Forecast</b>	<b>2013/14 (actual)</b>	<b>2014/15 (actual)</b>	<b>2015/16 (forecast)</b>	<b>2016/17 (forecast)</b>
Newlands (excl GAPE)	12.0	14.7	12.0	11.5
GAPE	12.5	15.3	15.3	17.0
<b>Total</b>	<b>214.5</b>	<b>225.7</b>	<b>219.1</b>	<b>226.3</b>

## Chapter 22 – Operating Costs

### Summary of Aurizon Network’s Position

Aurizon Network accepts the QCA’s CDD to amend the system-wide and regional costs, except for the business management costs and adjustments for non-coal traffic. Aurizon Network is firmly of the view that it is appropriate to estimate the portion of costs related to non-coal services based on the Full Time Equivalent (FTEs) dedicated to train control for non-coal traffic for those sections of the track for which the proportion of non-coal traffic is non negligible.

Aurizon Network also proposes that business management costs be increased by approximately \$0.8 million for FY2014 and escalated each subsequent year, reflecting an increase to regulation and policy costs to reflect a more normalised base year (which also aligns to actual costs for FY2014).

While Aurizon Network is prepared to accept the QCA’s CDD in relation to its corporate overhead allowance in the interests of the timely resolution of UT4, it does not agree with the methodology the QCA has applied. Aurizon Network supports the use of an allocation method supported by benchmarking. However, it believes that the use of a blended allocator remains appropriate and also that the benchmarking Aurizon Network previously submitted remains appropriate. Aurizon Network intends to revisit this in UT5.

Aurizon Network maintains that the AWOTE index has the best capacity to take into account changes in the quality or quantity of work performed and is therefore the most appropriate index for labour cost escalation. However, Aurizon Network is prepared to accept the CDD to apply the ABS Wage Price Index for the escalation of labour costs.

As outlined elsewhere in this response, Aurizon Network also has significant concerns as to the implications of the QCA’s CDD, including its CDD amended DAU, for its ongoing costs. While it anticipates that its costs will materially increase as a consequence, it is difficult to forecast the precise impact on Aurizon Network’s operating costs, noting that some of this will only be known on an ex post basis. In order for Aurizon Network to be able to recover its efficient costs, this will need to be addressed in the future setting of the allowance, as well as ex post adjustment mechanisms (such as the annual tariff review process and review event provisions).

Aurizon Network’s questions the discounts applied to its cost estimates which were validated as reasonable by the QCA’s consultants. The QCA has not sort to address this and has outlined that our questions remain<sup>175</sup>.

**Table 22 - Aurizon Network’s Response Operating Costs (Nominal \$millions)**

	FY2014	FY2015	FY2016	FY2017	Total
CDD	188.8	192.2	211.4	212.5	804.9
<i>Proposed changes</i>					
Audit costs (refer CDD 22.4)	0.2	0	0	0	0.2

<sup>175</sup> Queensland Competition Authority (2015d). p.48.

	FY2014	FY2015	FY2016	FY2017	Total
Train Control (refer CDD 22.1)	1.4	1.5	1.5	1.6	6.0
Business Management (refer CDD 22.1)	0.9	0.9	0.9	1.0	3.7
Insurance (refer CDD 22.3)	(0.8)	0	0.1	0.3	(0.4)
AN proposed	190.6	194.6	214.0	215.3	814.4

Note: Numbers may not sum due to rounding

**Table 22.1 – QCA Consolidated Draft Decision**

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1) After considering Aurizon Network's proposal for system-wide and regional costs (excluding corporate overheads), our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	22.1	<b>(2)(a) Disagree.</b> Aurizon Network accepts the QCA's CDD to amend its system-wide and regional costs, except for the business management costs and adjustments for non-coal traffic.
(2) The way in which we consider it appropriate for Aurizon Network to amend the 2014 DAU is to make the following adjustments:		<b>(2)(b) Agree.</b> While Aurizon Network remains of the view that the AWOTE index is the most appropriate index for labour cost escalation, it is prepared to accept the QCA's CDD to apply the ABS Wage Price Index for the escalation of labour costs.
(b) Amend its proposed system-wide and regional costs (excluding corporate overheads) to reflect our estimate of efficient costs as set out in Table 29.		<b>(3) Agree.</b>
(c) Amend its labour cost escalation rate to reflect escalation in line with the ABS Wage Price Index.		
(3) We approve the following aspects of Aurizon Network's proposal for system-wide and regional costs (excluding corporate overheads):		
(a) Aurizon Network's proposal to escalate non-labour costs by CPI.		
(b) Aurizon Network's proposal not to include a CPI-X adjustment factor to be applied for the 2014 DAU.		
(3) After considering Aurizon Network's proposal for corporate overheads, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	22.2	<b>Agree.</b> However, while Aurizon Network is prepared to accept this in the interests of the timely resolution of UT4, it remains of the view that the use of a blended allocator is appropriate and also that the benchmarking it previously submitted is also reasonable.

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(4) We consider it appropriate for Aurizon Network to amend the 2014 DAU to make the following adjustments:</p> <p>(a) Replace the use of its blended allocator with our proposed direct cost allocator</p> <p>(b) Reflect our current estimate of the efficient corporate overheads costs that is associated with all aspects of Aurizon Network's business, as identified in Table 34.</p>		<p>Aurizon Network intends to revisit this in UT5.</p>
<p>(1) After considering Aurizon Network's proposal for risk and insurance costs, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.</p> <p>(2) We consider it appropriate for Aurizon Network to amend the 2014 DAU to make the following adjustments:</p> <p>(3) resubmit its cost escalations for self-insurance to be adjusted for updated volumes and turnover, consistent with Table 43</p> <p>(a) escalate insurance premium costs at 2.5 per cent, not at the proposed 4 per cent, and</p> <p>(b) allocate the insurance premium costs of feeder stations to the operating costs for electric assets only.</p>	<p>22.3</p>	<p><b>Agree.</b> While Aurizon Network accepts the QCA's CDD on this matter, it believes there has been an error in the calculation of the insurance premiums in Table 43, which is explained below</p> <p>Aurizon Network was willing to resubmit the costs for self-insurance once volumes and turnover had been agreed with the QCA, as noted in section 4.6 of its response to the MAR Draft Decision.</p>
<p>(1) After considering Aurizon Network's proposal for audit costs, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal. We consider it appropriate for Aurizon Network to amend the 2014 DAU to:</p> <p>(c) remove the Aurizon Network's proposed allowance reflecting the difference between its actual and forecast audit costs over the UT3 period.</p> <p>(2) We approve the following aspects of Aurizon Network's proposal for audit and condition-based assessment costs:</p> <ul style="list-style-type: none"> <li>o proposed costs for the annual</li> </ul>	<p>22.4</p>	<p><b>(1)(a) Disagree.</b> Aurizon Network rejects the disallowance of the recovery of UT3 audit costs.</p> <p><b>(2)(a) and (b). Disagree.</b> Aurizon Network accepts the QCA's CDD on the inclusion of audit and condition-based assessment costs. However, it disagrees with audit costs not being subject to an ex post review and maintain its position that it would be able to recover any additional costs not included in the forecast due to changes in scope which are prescribed by the QCA.</p>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>audit process to be included as part of the system-wide and regional costs, but not subject to an ex post review</p> <p>(b) the condition-based assessment costs proposed by Aurizon Network, including recovery of the condition-based assessment costs from UT3 of \$0.8 million in 2013–14, and including \$0.6 million in 2016–17 for a UT4 condition-based assessment.</p>		
<p>(1) After considering Aurizon Network's proposal for environmental charges, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.</p> <p>(2) We consider it appropriate for Aurizon Network to amend the 2014 DAU to make the following adjustment:</p> <p>(a) Remove environmental charges from the operating expenditure allowances. These costs are to be included in the electric charge only.</p>	22.5	<b>Agree.</b>
<p>(1) After considering Aurizon Network's proposal for transmission connection charges, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.</p>	22.6	<b>Agree.</b>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(2) We consider it appropriate for Aurizon Network to amend the 2014 DAU to make the following adjustments:</p> <p>(a) use Aurizon Network's revised transmission connection charges as presented in its December 2014 response to our MAR draft decision and as part of its endorsed variation event application in July 2015.</p>		

## CDD 22.1 System wide and regional costs

### Adjustments for non-coal traffic

In relation to an allocation of train control costs to non-coal traffic (and hence not forming part of the system wide and regional cost allowance), the QCA states that “we consider the use of train kilometres is more likely to be representative of the resources used by Aurizon Network in providing train control service to non-coal customers, given train control costs are a function of scheduling and the time spent on the track”<sup>176</sup>. Aurizon Network firmly believes that it is appropriate to estimate the portion of costs related to non-coal services based on the FTEs dedicated to train control for non-coal traffic for those sections of the track for which the proportion of non-coal traffic is non negligible. Given that more than 95% of the total costs of the train control function relate to labour and oncosts, FTEs are representative of the resources used in providing the train control services.

Aurizon Network notes that for allocating costs of the business support functions between regulated and non-regulated services, in the CDD the QCA has approved the percentage of non-regulated revenue to total revenue as a basis for apportionment of the costs of these functions to non-regulated services. If Aurizon Network was to apply the same methodology to the allocation of costs to non-coal services, the percentage would be less than 1.5%. The FTE allocation basis proposed in Aurizon Network's response to the MAR Draft Decision results in an allocation of approximately 2% of costs to non-coal traffic. Aurizon Network considers that this is more reflective of activity and accordingly how costs should be allocated.

Aurizon Network restates by reference the response previously submitted in section 4.2.4 of its response to the MAR Draft Decision.<sup>177</sup> In particular, this set out why the management of coal traffic accounts for the vast majority of train control costs. This includes the fact that coal traffics are cyclic (not timetabled, as are non-coal traffics) and has accounted for most of the growth in volume. The consequent complexity that arises in managing coal services (including ad hoc services, cancellations and reschedules), not coal versus non-coal services.

### Business management costs

For all system wide and regional costs other than those relating to business management, the actual costs of FY2013 have been used as the base year for adjustments and escalation. Aurizon Network understands that the QCA has not used FY2013 actual costs as a base for the regulation and policy costs component. Instead, Aurizon Network's originally proposed 2014 DAU costs of \$1.9 million for FY2014

<sup>176</sup> Queensland Competition Authority (2015d). p. 50.

<sup>177</sup> Aurizon Network (2014a).

have been included in the cost allowance to normalise for FY2013 (\$4.1 million) including significant UT4 preparation costs (approximately \$2 million).

Aurizon Network's actual regulation and policy costs (including reduction for non-regulated services) for FY2014 were \$2.8 million. The originally proposed 2014 DAU costs were based on forecasts for FY2013 (actuals were not available at time of submission). Aurizon Network considers that at a minimum, in order to be more consistent with all other system-wide and regional costs, \$2.1 million be used as the base year allowance (being \$4.1 million FY2013 actuals less the \$2 million in UT4 preparation costs).

Since the original submission of the 2014 DAU operating cost allowance, there has been an increase in staff of the Regulation and Policy team including the appointment of a Vice President Regulation. These additional costs will not be reflected in the allowance by using FY2013 actual costs or forecast costs and hence will not be reflective of the ongoing costs of the regulation and policy function for the UT4 period.

Further, Aurizon Network does not consider that excluding all UT4 costs incurred in FY2013 is reasonable given the preparation of a new DAU is a core activity of that function of the business. Aurizon Network agrees it is necessary to normalise the base year so that it does not include the majority of the costs related to the preparation of the DAU, but not that it should exclude any costs in relation to the DAU. Aurizon Network therefore proposes that the actual regulation and policy costs for FY2014 of \$2.8 million be used as the first year of the UT4 allowance and be escalated each subsequent year.

## CDD 22.2 Corporate overheads

### **Benchmarking of corporate costs**

The QCA states that “we do not consider that Aurizon Network has provided any new information or arguments to justify the use of its benchmark costs as the primary estimation approach for its corporate overheads allowance. In particular, Aurizon Network did not address concerns raised by our consultant, RSMBC, in relation to the appropriateness of the Ernst & Young benchmarking results.”<sup>178</sup> Aurizon Network will respond to this below.

#### Benchmark costs as primary estimation approach

In the revised cost proposal contained in section 4.3.2 of Aurizon Network’s response to the MAR Draft Decision<sup>179</sup> it used the Cumulative Industry Benchmark (CIB) as the basis of the corporate cost allowance. However, Aurizon Network noted that it believed that its original cost allocation methodology, supported by the use of benchmarks to validate that the methodology results in a reasonable allocation overall, is a better approach. Using the CIB approach was an attempt to use a bottom up build as the primary estimation approach (based on the costs obtained from the American Productivity and Quality Centre (APQC) database ,as explained in Appendix 4.1 of Aurizon Network’s response to the MAR Draft Decision<sup>180</sup>). Aurizon Network’s preferred primary estimation approach is the allocation methodology as originally proposed, with benchmarks to validate and support the resulting allowance. This approach will provide a basis for comparison of actuals to the approved allowance. Hence, Aurizon Network supports the QCA’s decision to use an allocation methodology for the determination of the corporate cost allowance.

In its response to the MAR Draft Decision, Aurizon Network engaged ITNewcom, one of the Asia Pacific’s leading IT advisory and benchmarking firms, to provide a costing for IT services required if Aurizon Network was a stand-alone company, not part of the Aurizon Group. This was submitted as Appendix 4.3 of the response.<sup>181</sup> This benchmarking exercise found the costs to be \$18.1 million, which was within a reasonable range of the Ernst & Young benchmark and also the costs derived using Aurizon Network’s allocation methodology. This report was new information submitted in the response to the MAR Draft Decision to support the IT component of the corporate cost allowance.

#### Ernst & Young Benchmarking.

As noted above, the QCA stated that Aurizon Network failed to address concerns raised about its benchmarking response. Aurizon Network considers that this information was presented in its previous response to the MAR Draft Decision.

Appendix 4.1 of Aurizon Network’s response to the MAR Draft Decision<sup>182</sup> detailed the process undertaken in the Ernst & Young report to obtain the benchmark costs for each functional area. It also addressed why costs were normalised based on revenue. The costs were built up by attributing benchmarked costs to processes and functions matched from the APQC publicly available database to Aurizon Network functions using mostly Level 3 of the Process Classification Framework (PCF). The first three levels of the PCF are:

- Level 1 – represents the highest level of process in the enterprise e.g. manage finance resources;

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<sup>178</sup> Queensland Competition Authority (2015d), p. 73.

<sup>179</sup> Aurizon Network (2014a).

<sup>180</sup> Aurizon Network (2014a).

<sup>181</sup> Aurizon Network (2014a).

<sup>182</sup> Aurizon Network (2014a).

- Level 2 –represents a group of processes sitting under that function e.g. manage treasury operations;
- Level 3 – represents a series of interrelated activities that convert inputs into results (outputs); processes consuming resources and requiring standards for repeatable performance; and processes responding to control systems that direct the quality, rate and cost of performance, for example, manage treasury policy and procedures, manage cash, manage financial risks.

The benchmarking analysis involved matching corporate activities for which costing data was available in the APQC database to functions of the Aurizon Network business. This enabled Ernst & Young to construct a reliable comparison of costs on a like for like basis, regardless of the organisational structure and whether overhead costs are centralised or not.

The participants in the Distribution/Transportation Industry were provided in Appendix 4.2 of Aurizon Network’s response to the MAR Draft Decision<sup>183</sup>. The QCA considers that Aurizon Network did not provide analysis in relation to the appropriateness of the comparable entities and that it is not possible to determine whether the large range of companies selected would have a similar cost structure to Aurizon Network. It is not possible using the APQC database to isolate costs for any of the participants individually, that is, there is no lower level of granularity than the Distribution/Transportation Industry, as to do so would compromise the confidentiality of the participants’ business data. This is why the benchmarking using the APQC database was supplemented with the benchmarking from the two rail companies who provided data to Ernst & Young on a confidential basis. To maintain their confidentiality it is also not possible to provide further detail on their operations than was included in the submission.

### **Allocation methodology**

The QCA has not accepted the use of a blended allocator (comprising revenue, FTEs and assets) for allocating corporate costs for which a causal allocator cannot be ascertained. While Aurizon Network is prepared to accept the QCA’s decision in the interests of the timely resolution of UT4, Aurizon Network maintains that a blended allocator is still appropriate. Its response to the QCA’s concerns with the blended allocator are set out below.

First, the QCA suggests that revenue will be affected by changes in policies which have no direct link to overhead costs, such as depreciation rates. Changes in accounting policies for depreciation have no impact on revenue since depreciation for regulatory purposes (included in MAR) and accounting depreciation are not aligned.

Second, the QCA suggests that revenue includes the pass-through of electricity costs, which appear to have no strong relationship to overheads. Aurizon Network agrees with this point and would amend the calculation of Network percentage of revenue to exclude AT5 and EC revenue if this was used in the blended allocator.

Finally, the QCA asserts that “given that the carrying value of assets is largely fixed from year to year, this would not correlate well with factors that cause Aurizon Network’s overhead costs to vary”.<sup>184</sup> It should be noted that overheads include both fixed and variable costs – both of which need to be allocated to Network. Significant amounts of the overhead costs are relatively fixed in nature and there is not a causal driver for the allocation of these costs, which is why they are being allocated using the blended allocator rather than another causal allocator such as FTEs (where the cost is driven by the number of FTEs).

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<sup>183</sup> Aurizon Network (2014a).

<sup>184</sup> Queensland Competition Authority (2015d). p. 74.

Using the percentage of direct costs will not correlate any better than the percentage of assets for corporate overheads such as rent of commercial premises, safety licences and accreditation, software licences and CEO remuneration. Since Aurizon Network is a capital intensive business, much of the costs incurred by the company are capitalised onto the balance sheet as assets under construction and ultimately infrastructure or plant and equipment assets. This includes sustaining capital expenditure such as rail renewal, ballast undercutting, track and culvert replacements etc. These costs are not reflected on the Income Statement that has been used to calculate the direct cost percentage and the QCA has not allowed capital costs to be included in the calculation of the direct cost percentage. Hence for these reasons Aurizon Network believes that it is appropriate to include assets in the blended allocator.

Aurizon Network intends to further explore the use of blended allocator in the cost methodology for UT5, including consideration of direct costs replacing revenue.

## CDD 22.3 Risk and insurance

Aurizon Network accepts the QCA's CDD on this matter, however believes there has been an error in the calculation of the insurance premiums in Table 43 of the CDD. Aurizon Network understands that those costs have not been adjusted for volumes and turnover and have only been adjusted to apply different escalation rates than originally submitted. Aurizon Network was willing to resubmit the costs for self-insurance once volumes and turnover had been agreed with the QCA, as noted in section 4.6 of its response to the MAR Draft Decision.<sup>185</sup>

The correct amounts are as set out below:

**Table 22.3 – Correction of insurance premium calculation**

Insurance Premiums (Nominal)	FY2014	FY2015	FY2016	FY2017
Non-electric	2,553,549	2,934,298	3,089,820	3,157,609
Electric	723,740	731,133	738,603	746,148
<b>Total</b>	<b>3,277,289</b>	<b>3,665,431</b>	<b>3,828,422</b>	<b>3,903,757</b>

Self Insurance	FY2014	FY2015	FY2016	FY2017
\$ 2013/14 Real	4,970,000	5,440,000	5,800,000	6,140,000
MCI (from 2013/14)	0%	1.61%	4.16%	6.89%
<b>Total</b>	<b>4,970,000</b>	<b>5,527,846</b>	<b>6,041,001</b>	<b>6,563,151</b>

<sup>185</sup> Aurizon Network (2014a).

## CDD 22.4 Audit and condition-based assessment

CDD 22.4(1) requires Aurizon Network to remove its proposed allowance reflecting the difference between its actual and forecast audit costs over the UT3 period. Aurizon Network restates by reference the response previously submitted in section 4.7 of its response to the MAR Draft Decision.<sup>186</sup>

While Aurizon Network accepts the QCA's CDD on the inclusion of audit and condition-based assessment costs, it disagrees with audit costs not being subject to an ex post review. Aurizon Network maintain its position that it should be able to recover any additional efficient costs not included in the forecast due to changes in scope that are prescribed by the QCA. The rejection of the ex post review is contradictory to the comments made by the QCA in section 17.7.4 of its response, which accepted Aurizon Network's proposal that the cost of unplanned audits should be included in adjustments to allowable revenue, subject to its review on a case-by-case basis that such costs have been efficiently incurred.<sup>187</sup>

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<sup>186</sup> Aurizon Network (2014a).

<sup>187</sup> Queensland Competition Authority (2015c). p.124.

## Chapter 23 – Maintenance Costs

### Summary of Aurizon Network’s Position

With respect to maintenance costs, Aurizon Network accepts the majority of the positions that the QCA has proposed in response to Aurizon Network’s 2013DAU and 2014DAU. However, it remains concerned that its maintenance cost allowance will not be sufficient to recover its efficient costs, as outlined below.

Aurizon Network has an obligation to manage, operate and maintain the CQCR in accordance with good operating practices including safety and environmental requirements. To maintain these standards, Aurizon Network must be permitted to recover at least the efficient costs of delivering an efficient maintenance program, as is required under section 168A(a) of the QCA Act.

As outlined in Part 15 of this response, it is disappointing to see that the QCA continues to re-interpret the “at least” wording in section 168A(a) to mean “no more”. In the context of its maintenance cost review, the QCA has justified this “no more” position on the basis that it will provide incentives to “incur costs efficiently and will have less scope for discrimination in favour of its downstream operations”<sup>188</sup>, although that interpretation has been contradicted in the application of the Maintenance Cost Index (MCI)<sup>189</sup>. This risk is increased without a clear mechanism or ex post Review Event mechanisms that was within the 2010 AU, which included allowing Aurizon Network to apply to the QCA where its efficient maintenance costs exceeded the approved allowance by more than 2.5%.

Aurizon Network maintains that the legislative requirement of “at least”, coupled with its obligations to demonstrate efficient costs, provide Aurizon Network with a strong incentive to incur costs efficiently if the allowance is set correctly. Assurance to stakeholders on the management of assets is delivered through both the operational delivery of access as per access agreements and transparency through reporting.

Aurizon Network’s response to the QCA’s CDD on its maintenance allowance (excluding ballast undercutting) is provided below, focussing on the areas of disagreement. Aurizon Network will undertake a further comprehensive review of its maintenance cost allowance, and key measures such as the MCI, as part of UT5.

**Table 23.1 – QCA Consolidated Draft Decision**

QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
After considering Aurizon Network’s proposed direct maintenance costs (excluding ballast undercutting), our consolidated draft decision is to refuse to approve Aurizon Network’s original proposal.	23.1	<b>(2) Agree.</b>
We consider it appropriate for Aurizon Network to amend the 2014 DAU to make the following adjustments (as specified in Table 55, Table 56, and Table 57 above):		<b>(3) Agree with amendments.</b>
a) reallocation of re-railing costs to renewals starting from 2015–16		

<sup>188</sup> Queensland Competition Authority (2015d). p. 104.

<sup>189</sup> Queensland Competition Authority (2015d). p. 126.

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<ul style="list-style-type: none"> <li>b) allocation of maintenance costs to non-coal traffic</li> <li>c) Adjustments for updated volume profile.</li> </ul> <p>We also consider it appropriate for Aurizon Network to amend Part 10 of the 2014 DAU (Reporting) to provide more transparency in its maintenance performance.</p>		
<p>After considering Aurizon Network's proposal of indirect maintenance costs, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.</p> <p>We consider it appropriate for Aurizon Network to amend the 2014 DAU to make the following adjustments (as specified in Table 60):</p> <ul style="list-style-type: none"> <li>a) applying the historical cost approach to calculate return on maintenance assets</li> <li>b) removing cost allowances for return on inventory and working capital</li> <li>c) removing allocations for corporate overheads.</li> </ul>	23.2	<p><b>2(a) Agree.</b></p> <p><b>2(b) Disagree.</b> The QCA's rejection of an end of year modelling approach means that a specific return on working capital should be provided for maintenance. It should also therefore apply a return on inventory.</p> <p><b>2(c) Agree.</b></p>
<ul style="list-style-type: none"> <li>(1) After considering Aurizon Network's proposed MCI, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.</li> <li>(2) We consider it appropriate for Aurizon Network to amend the 2014 DAU to make the following adjustments: <ul style="list-style-type: none"> <li>a) Limit the application of MCI to the direct maintenance costs less depreciation.</li> <li>b) Apply the MCI structure specified in Table 66.</li> <li>c) Escalate depreciation by the CPI all groups Brisbane.</li> </ul> </li> </ul>	23.3	<b>Agree.</b>

## CDD 23.1 Direct maintenance costs

Aurizon Network welcomes the QCA decision in relation to these matters. Its further comments are provided below.

### Volume adjustments

Aurizon Network agrees with the QCA's proposed volume adjustments, however acknowledges that the QCA has rejected Aurizon Network's proposal that the FY2014 actual costs be accepted into the

maintenance allowance. As articulated in previous responses, the delay in gaining approval for the 2014DAU has resulted in Aurizon Network operating the network in good faith and continuing to incur costs where it risks not being fully compensated. Noting that the QCA has had multiple sources of information (e.g. maintenance reports, capital reports, 2013DAU material), at no stage has the QCA been able to demonstrate that the FY2014 costs were not efficient.

## **Reporting**

Aurizon Network has addressed the QCA's CDD on the additional maintenance reporting requirements within its response to CDD 5.1.

Finally, Aurizon Network does have concerns relating to the QCA's statement that "we will explore alternative frameworks for the approval of maintenance costs, if a considerable variation against maintenance forecasts continues"<sup>190</sup>.

At no time during the 2010AU period did Aurizon Network seek to recover any additional revenue from access holders for any overspend on any maintenance activities. Any such overspends have been absorbed by Aurizon Network. Therefore any variation from forecast did not in any way impact access holders. If the QCA was to consider an alternative framework, it must be considered in line with the applicable legislation and not an alternative interpretation or extension of that legislation that results in a materially different outcome.

## **CDD 23.2 Indirect maintenance costs**

### **Working capital**

There has been no evidence to suggest there is specific and adequate compensation for the return on working capital allowance for maintenance costs in the QCA's CDD. Aurizon Network has asked to be provided with further information from the QCA through a further request for information, however minimal detail was provided in response.

As per Aurizon Network's MAR response, Aurizon Network considers that the return on working capital that relates to maintenance should be included within the maintenance allowance. Reference is made to Part 29 for Aurizon Network's response to the CDD on its modelling methodology. Aurizon Network intends to review this in future regulatory periods.

### **Return on inventory holdings**

With the change in modelling approach to half-yearly in the QCA's CDD, a return on inventory holding is now considered appropriate. The QCA's modelling was not updated to with their modelling change.

Aurizon Network is required to hold various inventory types and products due to the size and scale of its operations. This ranges from holding rail and sleepers, through to data cabling and telecommunications equipment. Some of the products are not available for immediate delivery and require long lead times to purchase, this includes rail, which upon average takes around a year to procure and then up to 6 months to install. Other items like telecommunications equipment are required to be purchased and stored due to the critical nature of the product. Some of these telecommunications spares maybe obsolete due to the movement in technology. A cost/benefit analysis would be completed to determine if storing critical

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<sup>190</sup> Queensland Competition Authority (2015d). p.116.

spares instead of replacing entire telecom's systems would be undertaken, which in most cases result in the purchase and storage of spares being by far the more efficient method.

To procure inventory, deposits and payments are required to secure delivery during the manufacturing stage. This results in a cash flow difference between cash-flow going out and revenue coming in through depreciation and return on assets. Hence the importance of an inventory allowance to Aurizon Network.

Holding an efficient level of critical inventories is essential to the timeliness and effectiveness of maintenance activities. It forms part of the efficient business costs. Aurizon Network has submitted an allowance for return on inventory in the 2014 DAU. However, the QCA rejected the proposal in the MAR Draft Decision, and considered it to be inconsistent with the end-of-year cash flow assumption.

Specifically, the QCA stated:<sup>191</sup>

*Aurizon Network receives a full year's compensation for the opportunity cost of its funds used to cover the working capital movements throughout the year. Therefore, providing Aurizon Network with working capital /return on inventory under an 'end-of-year' assumption would result in additional revenues for Aurizon Network.*

In the CDD, the QCA has reverted back to a mid-year cash flow assumption and provided an allowance for working capital. As a matter of logic, the QCA should also provide allowance for return on inventory as it rejected both the return on working capital and return on inventory for the end-of-year cash flow assumption which has now been replaced by a mid-year assumption.

Instead, the QCA has considered return on inventory to be a separate issue. It has stated in the CDD:<sup>192</sup>

*Having determined that a working capital allowance is appropriate, we do not consider it appropriate that Aurizon Network obtains a separate return of inventory allowance. To do so would overcompensate Aurizon Network and it would fail to create the necessary incentives to promote the object of the Part 5 of the QCA Act. That is, we have included the cost of materials that form inventories in the operating and maintenance costs and we have included operating and maintenance costs in the calculation of the working capital allowance.*

Aurizon Network agrees with the QCA that return on inventory is a separate issue to return on working capital. Return on working capital is seeking to compensate for the cash flow timing difference, while return on inventory is seeking to compensate for the cost of holding an efficient level of inventory. This is exactly the reason why the QCA's statement is incorrect. Providing return on inventory will not overcompensate Aurizon Network as it is a different concept to return on working capital. In contrast, Aurizon Network will be undercompensated if no allowance for return on inventory is provided. This can be illustrated by using the following example.

Assume QCA maintenance allowance for material is \$1,000 and the average inventory holding during the year is \$100. As shown in Table 23.2 Aurizon Network is undercompensated by \$7.17 if return on inventory is not provided.

**Table 23.2 – Example of under-compensation without a Return on Inventory allowance**

	Amount
<b>Allowance</b>	
Maintenance Allowance	\$1,000
Return on Working Capital (0.3%)	\$3

<sup>191</sup> Queensland Competition Authority (2014a). p. 283.

<sup>192</sup> Queensland Competition Authority (2015d). p. 276.

	Amount
Total QCA Allowance	\$1,003
<b>Cost</b>	
Material Payment	\$1,000
Timing Difference in Cash Flow (0.3%)	\$3
Cost of Holding Inventory (at WACC of 7.17%)	\$7.17
Total Cost	1,010.17
<b>Net Profit/Loss</b>	<b>-\$7.17</b>

Without any allowance for holding inventories, the QCA is assuming Aurizon Network will always purchase the necessary materials immediately prior to undertaking the maintenance tasks, which is never the case in practice and does not contribute to the efficient operation of maintenance program.

For reasons described above, Aurizon Network is therefore including \$3.29million (Real FY12) for return on inventory in the maintenance cost allowance. Aurizon Network has amended its proposal to reflect the updated pre-tax WACC rate (from 6.832%, reduced to 4.66%). The resulting return on inventory allowance is shown below below.

**Table 23.3 – Return on Inventory for updated WACC (\$FY12)**

Inventory Holding Allowance	\$nominal	
Value of Inventory (as at April 2013)	\$17,653,168	
x pre-tax WACC (updated 4.660%)	\$822,638	
x 4 year regulatory term	\$3,290,551	\$3,452,049

Aurizon Network agrees with the movement of overheads into the operating cost allowance. Reference is made to Part 22 of this submission.

## Chapter 24 – Ballast Undercutting Costs

### Summary of Aurizon Network's position

The QCA proposes to reject Aurizon Network's ballast undercutting allowance submitted as part of its 2014DAU. In reaching its conclusions the QCA has heavily relied upon analysis undertaken by its consultant, CMT.

Aurizon Network's ballast undercutting program has undergone considerable development and review since the 2013 DAU was submitted, including (but not limited to) the deployment of Ground Penetrating Radar (GPR) technology to assist in more accurately targeting the scope of work required. Initiatives have also been put in place to improve efficiency while maintaining Aurizon Network's core priority of Zero Harm. This development has continued in parallel with the very long UT4 process. In the meantime, Aurizon Network has continued to invest in maintaining the network, incurring costs in good faith despite the uncertainty as to whether it will be fully compensated.

Aurizon Network does not consider that the QCA's proposed allowance is sufficient to recover its efficient ballast undercutting costs for the UT4 period.

While it has some concerns with the methodology applied by the QCA in assessing the scope of ballast undercutting works for the mainline, Aurizon Network is prepared to accept this as it aligns with Aurizon Network's cost model. However, it does not agree with the QCA's proposed turnout scope for FY2016 and FY2017, which it submits should remain as per Aurizon Network's originally submitted scope. Aurizon Network also submits that if the QCA proposes to make any further changes to scope (anticipating a Final Decision in April 2016), it is limited in its ability to make any consequent adjustments to its maintenance program having regard to its planning horizon.

The more significant area of disagreement is the QCA's proposed ballast undercutting cost allowance. Based on the advice of CMT, the QCA's proposed allowance underestimates the costs of an efficient ballast undercutting program and seeks to cap the unit rate at \$400,000 per km. Aurizon Network has significant concerns with the methodology and analysis employed by CMT and accepted by the QCA. These concerns are addressed in detail in this response.

Noting its concerns with the methodology, Aurizon Network is prepared to accept the QCA's allowance for FY2014 and FY2015, noting that its expenditure in FY2015 aligned with that allowance. However, it does not accept the allowance for FY2016 and FY2017. Aurizon Network submits that the allowance proposed by the QCA is in no way reflective of an efficient ballast undercutting program that needs to be delivered in a complex and dynamic operating environment. It will therefore not allow Aurizon Network to recover its efficient costs, which it is entitled to do under section 168A(a) of the QCA Act.

Aurizon Network also disagrees with the QCA's exclusion of the costs of any future GPR runs (which it instead proposes to address via the revenue cap adjustment process) and submits that an allowance of \$1.5 million be provided for one GPR run during the remaining term of the 2014DAU.

Finally, while Aurizon Network has previously detailed significant concerns with the rationale and approach underpinning the QCA's decision to adopt an impairment charge in UT3, it accepts the QCA's decision in relation to impairment.

Ballast fouling remains a significant and complex issue that will continue to require the cooperation of all supply chain participants. Aurizon Network's work in this is ongoing as it implements what it considers will be a best practice approach to addressing ballast fouling. Given its significance for not only maintenance costs but network operations, this will remain an important area of focus for the UT5 review.

**Table 24.1 – QCA Consolidated Draft Decisions**

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(5) After considering Aurizon Network's proposal of ballast undercutting costs our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	24.1	<p><b>Disagree</b></p> <p>Aurizon Network understands that the QCA has to reject the 2013DAU. Aurizon Network has responded in line with the positions outlined within its December 2014 Response to the MAR Draft Decision.</p>
(6) We consider it appropriate for Aurizon Network to amend the 2014 DAU to make the adjustments as specified in Table 77.		<p>Aurizon Network agrees with the scope recommended by the QCA.</p> <p>The QCA's consultant's recommendations contains factual inaccuracies, incorrect assumptions and are missing critical elements of an undercutting program. In relying on that advice, the QCA's \$400,000 capping of the mainline undercutting allowance is not appropriate and is not supported by any fact-based evidence from a comparable entity/ies.</p> <p>The QCA's removal of the GPR funding from the Ballast undercutting allowance is inappropriate as this is an expense for the ballast undercutting program. The QCA's proposal to recover it through Revenue Cap is inappropriate as GPR is deployed on a CQCR wide whereas the revenue cap is applied on a system basis.</p>
(3) After considering Aurizon Network's proposal of the ballast impairment charge, our consolidated draft decision is to refuse to approve any reversal of the ballast impairment charge for the UT3 period (or simulating such an effect by reconciliation payments), but we approve the removal the ballast impairment charge associated with the 2014 DAU period.	24.2	<p><b>Agree</b></p>
(4) We consider it appropriate for Aurizon Network to amend the 2014 DAU as per Aurizon Network's December 2014 submission. The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to remove the proposal to reverse the ballast impairment charge attributable to the UT3 period.		

## Introduction

The QCA has provided a material update to its previous MAR Draft Decision from September 2014, to take into the account operational advancements that Aurizon Network utilises to manage its ballast undercutting program.

Since the original 2013DAU submission and the QCA's MAR Draft Decision, Aurizon Network has outlined in multiple submissions, forums and presentations that it is going through a development period relating to its ballast undercutting program. These advancements result in the original scoping methodology employed to develop the 2013DAU (within Volume IV – Maintenance) and the QCA's subsequent decision upon that 2013DAU submission having less relevance compared with today's current practices.

In December 2014, Aurizon Network provided a comprehensive outline of its ballast program in response to the QCA's MAR Draft Decision. To assist the QCA with its review of Aurizon Network's revised ballast undercutting program outlined in that response, the QCA appointed CMT Solutions (CMT) to assist with creating the positions outlined within the CDD. CMT's scope of engagement included conducting an independent assessment of the efficiency of Aurizon Network's ballast undercutting scope and costs for the 2014 DAU.

The QCA did not provide a Draft Decision on the ballast undercutting scope and has therefore only provided a recommendation based upon CMT's review. CMT's review of Aurizon Network's scope primarily focussed upon the use of Ground Penetrating Radar (GPR) data. There are a range of errors and inaccuracies with CMT's methodology to construct the scope, however the QCA has agreed with CMT on the scope for turnouts, whilst it has recommended that the mainline scope should be aligned to Aurizon Network's cost model.

As well as reviewing scope, CMT provided an independent costs build up, including a recommendation to the QCA. This independent costs build was used to assess the efficiency of Aurizon Network's undercutting allowance. CMT's assessment negates a range of relevant factors that are required to execute a reasonable ballast program. These factors, coupled with fact that no benchmarking was undertaken to assess reasonableness of the independent costs build up, brings into question the QCA's ability to meet the requirements of section 168A(a) of the QCA Act.

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### As part of the QCA's independent cost build up '...a detailed industry benchmarking exercise was not included'<sup>193</sup>

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Although no detailed industry benchmarking was completed, CMT has provided commentary on expected market ranges and have recommended to cap Aurizon Network's mainline undercutting program on a \$/km basis. This cap is less than comparable Australian railway managers and would not be enough to generate expected revenue that is at least enough to meet the efficient costs.

During its review, Aurizon Network provided CMT to access of all information that was used to develop its MAR response and further data (February 2015 GPR data drop) that was not available at the time of the MAR Response. Aurizon Network has not been afforded the same level of transparency by way of visibility of the independent cost model developed by CMT. This has limited Aurizon Network's ability to respond.

CMT has provided the QCA with a report that the QCA has published as part of this CDD. CMT has made recommendations which in most cases the QCA has adopted into its CDD. In various areas, CMT has misinterpreted (and misunderstood) Aurizon Network's operational practices and has applied these to the independent costs build up, which ultimately results in a material reduction of the ballast undercutting

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<sup>193</sup> CMT (2015). Aurizon Network Review of Ballast Undercutting Scope and Costs, Footnote 1, p. v.

allowance. The QCA has also given commentary outlining that Aurizon Network has had a historical underperformance that could be driven by Aurizon Network's scope model<sup>194</sup>. Statements like this are mis-leading as neither the QCA nor its consultant reviewed Aurizon Network's Network Strategic Asset Plan (NSAP) to substantiate this statement.

Aurizon Network relies on the NSAP to model the scope for the majority of its maintenance and renewal tasks. Aurizon Network acknowledges that year-on-year, the scope for some products may not have been achieved, however the Overall Track Condition Index (OTCI) and turnout faults indicate that the CQCR is performing at a steady state with no accelerated rate of faults that could imply track quality deterioration.

Noting the volume of information and analysis Aurizon Network has submitted to the QCA on this issue, the acceptance of most of CMT's recommendations without question in such a critical aspect of Aurizon Network's maintenance program is not only disappointing but is of significant concern. Aurizon Network submits that the QCA's reliance on this flawed analysis risks leading it into error, which would result in Aurizon Network failing to be compensated for its efficient costs. This in turn fails to meet the requirements of section 168A(a) of the QCA Act.

## CDD 24.1 Ballast Undercutting Scope

### **Aurizon Network's 2014DAU proposal**

Aurizon Network, in response to the QCA's MAR Draft Decision, provided an updated methodology used to create the ballast undercutting scope for the 2014DAU period. This change was significant as Aurizon Network commenced utilising technology to assist in delivering a ballast undercutting program that objectively and more accurately targets ballast fouling, efficiently manages the planning associated with delivering the undercutting program and minimises the flow-on cost to access holders.

Aurizon Network felt that it was appropriate at the time to update the scope development as it had substantially changed its methodology with technological advances in this field. Previous methods involved spot sample testing and laboratory assessments which were no longer appropriate due to the minimal level of data that could be obtained and the level of disruption those methods had on the operation of coal trains within the CQCR.

Aurizon Network moved to a GPR method to assist in the development of the scope of the mainline ballast undercutting program. This technology far exceeded the level of granularity of the previous spot sampling methodology, with GPR being able to detect ballast fouling rates at the rate of 3 data points every 5 metres of track.

Aurizon Network however still uses a tonnage based method, through the use of its NSAP model to develop the undercutting scope for turnouts. This is because GPR cannot penetrate the steel componentry within turnouts which exist above the ballast layer.

In addition to the GPR methodology being used to construct the scope, Aurizon Network also proposed a consistent reporting methodology that requires it to report all ballast undercutting in terms of a standard ballast profile. This standard ballast profile is classified as being 300mm deep from the bottom of the sleeper. It is important to have a consistent reporting method, as reporting on a basic linear kilometre

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<sup>194</sup> Queensland Competition Authority (2015d). p. 138

basis will not accurately reflect the amount of ballast undercutting actually taking place. As detailed in the MAR response<sup>195</sup>, ballast undercutting is a volumetric activity where ballast is screened/cleaned and replaced on a cubic metre basis; looking at linear metrics alone will not provide a consistent nor explicit view of ballast undercutting requirements.

Overall, Aurizon Network developed a GPR scope of 558km (or 1.395 million m<sup>3</sup> of ballast) for the period of the 2014DAU. However, this was beyond Aurizon Network's capacity to deliver, therefore this was revised down to 538km (or 1.345 million m<sup>3</sup> of ballast) over that same term. This scope included 118km of ballast undercutting that was already delivered in FY2014.

It is important to re-emphasise that there is a non-linear the relationship between ballast fouling and ballast cleaning. Therefore, one should not expect that by completing 140kms per year, there should not be any ballast fouling at the end of the 2014DAU period. Aurizon Network outlined this within its response to the QCA's MAR Draft Decision.<sup>196</sup>

Since that submission, Aurizon Network has delivered another year of maintenance activities and reported these within the FY2015 Maintenance Cost Report. This report detailed that Aurizon Network delivered 152km (volumetrically converted) against the proposed scope of 140km of mainline ballast undercutting during the year and completed ballast renewal on 48 turnouts.

### **The QCA's response**

The QCA, in reliance on CMT, has reviewed the ballast undercutting scope. Although the recommendations have not been fully included within the QCA's draft decisions (i.e. its MAR Draft Decision and the CDD), the QCA confirmed that the ballast undercutting scope proposed by Aurizon Network was not efficient as it was beyond its capability and subsequently reduced the mainline scope to be in line with Aurizon Network's costs model.

Aurizon Network confirms that while it has concerns with adopting the QCA's proposed efficient mainline scope for UT4, it is prepared to accept it as this was what was reflected within its costs model used to develop its response to the QCA's MAR Draft Decision.<sup>197</sup> This agreement is in light of two of the four years of the regulatory period having been completed.

In terms of turnout scope, the QCA has recommended that Aurizon Network should operate to the turnout scope proposed by CMT, which reduces the scope (and variable allowance) during the last three last years of the undertaking term. While Aurizon Network has more significant concerns with the CMT analysis (summarised below), it is also prepared to accept the QCA's turnout scope for both the first (FY2014) and second (FY2015) years of the 2014DAU term as these years have already been delivered. Aurizon Network does not accept scope of FY2016 and FY2017, due to the flaws in scope methodology outlined within this response.

Below is a summary of the individual positions put forward by both the QCA and Aurizon Network in regards to the ballast undercutting scope for the 2014DAU period.

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<sup>195</sup> Aurizon Network (2014a). s.6.4, p. 135.

<sup>196</sup> Aurizon Network (2014a). s.6.3.3, p.125.

<sup>197</sup> Aurizon Network (2014a).

**Table 24.2 – Ballast Undercutting Scope**

	FY2014 <sup>^</sup>	FY2015	FY2016	FY2017	Total
<b>Aurizon Network – December 2014</b>					
Turnout	41	54	57	58	210
Mainline	118	140	140	140	538
Volume m <sup>3</sup>	354,011	350,000	350,000	350,000	1,404,011
<b>QCA Consolidated Draft Decision - December 2015</b>					
Turnout	41	40	40	41	162
Mainline	118	129	133	140	520
Volume m <sup>3</sup>	354,011	322,500	332,500	350,000	1,300,000
<b>Aurizon Network Revised Proposed scope</b>					
Turnouts	41	40	57	58	196
Mainline	118	129	133	140	520
Volume m <sup>3</sup>	354,011	322,500	332,500	350,000	1,359,011

Sources: QCA CDD Table 73,

Aurizon Network MAR Response, December 2014, Tables 6.7 and 6.8

<sup>^</sup>FY2014 figure are actuals

With the timing of the QCA's Final Decision currently earmarked for April 2016, by the time an approved undertaking is in place, three of the four years of the 2014DAU will have already been completed and the QCA may have made retrospective decisions on the ballast allowance allowances for the three already completed years.

During this time, Aurizon Network has been operating in good faith within the unapproved and uncertain allowances. The QCA's decision to make any material retrospective changes to these allowances, 75% of the way through the term, results in considerable regulatory risk to Aurizon Network. This flows through to the ability to alter the scope of the ballast undercutting program. Assuming the Final Decision is released in April 2016, FY2017 is the only year where the scope can be altered to reflect the QCA's recommendation.

### **Aurizon Network's response to the QCA's CDD on ballast undercutting scope**

The QCA engaged CMT to review and provide a recommendation on the appropriateness of Aurizon Network's proposed undercutting scope. Aurizon Network has provided a response to the recommendations contain within the report below.

#### Mainline Scope

CMT has recommended that the GPR scope for Aurizon Network's ballast undercutting program be reduced from Aurizon Network's 500.9km to 421.0km for the remaining three years of the 2014DAU period.

This is primarily due to CMT re-estimating the scope, based on the latest GPR data (not available at the time of Aurizon's response to the QCA's MAR Draft Decision), which resulted in some sections of scope that were over-estimated and some which were under-estimated. As Aurizon Network has re-iterated, the use of GPR and the associated analytical tools to support the analysis of the data is still developing and the findings from CMT's review will be considered in the development of future ballast scopes.

Upon a detailed review of CMT's report, Aurizon Network has identified numerous errors with its methodology and assumptions to create the scope for the ballast undercutting program. These errors have varying degrees of materiality.

One major error that Aurizon Network would like to highlight is the QCA's assumption that Aurizon Network "ignores both adverse impacts on the infrastructure such as tonnage usage rates and beneficial impacts on the rate of fouling such as the recently implemented coal management veneering program"<sup>198</sup>. This statement is fundamentally incorrect.

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## The GPR methodology will inherently take into account tonnages and operational improvements such as veneering.

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As more coal traffic traverses a section of the network, at the time of the next GPR run, one would expect to see an increase in the level of ballast fouling. When planning the GPR runs, Aurizon Network prioritises those sections that have high tonnage throughput, therefore leading to certainty that the data collected at these sections is fully considered in planning of the ballast undercutting program. The GPR data, being intrinsically objective, cannot ignore the fouling impacts associated with increased tonnages on the infrastructure.

In terms of operational improvements such as veneering, the QCA's statements are again misleading. That is, these practices should result in a slowing in the rate of fouling and not a decrease in the level of fouling, as this can only be achieved through an intervention activity such as maintenance/undercutting.

The veneering program was progressively introduced into the CQCR with a significant uplift in implementation in 2012 and 2013. This coincides with the establishment of the GPR program. As there was not a complete CQCR-wide GPR run completed before the introduction of veneering, an exact quantification of the benefits of these operational improvements cannot be completed through analysis of past GPR results. If all other variables within the network remained constant (tonnes, train numbers, coal particle size distribution, train configuration), an analysis could be completed, however this is not possible due to the dynamic nature of the CQCR and its operations.

The QCA's reduction of scope still remains in line with the scope that Aurizon Network is resourced to complete (i.e. 140kms per year). As stated in its response to the MAR Draft Decision, Aurizon Network will manage the asset in line with its standard practices<sup>199</sup> and can deliver this scope during the term of the 2014DAU.

It should also be noted that in Aurizon Network's response to the MAR Draft Decision, it was outlined that Aurizon Network was in the process of acquiring an RM74 Ballast Undercutter. During the process of leasing the machinery, it was identified that driver visibility issues would prevent it from being accredited to operate within the CQCR. Therefore, it has been decided not to lease this machinery. Any work that this machinery was due to complete will now be undertaken by the leased excavator undercutter/s.

Aurizon Network therefore agrees with the overall mainline ballast scope, although is concerned about some of the detail within CMT's report and reiterates that its application of GPR to assess scope inherently accounts for network tonnages and operational improvements such as veneering. Aurizon Network will review this scope again in detail for the development of future undertakings.

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<sup>198</sup> CMT (2015). p.v.

<sup>199</sup> Aurizon Network (2014a). s.6.4.6, p.132.

### Turnout Scope

Aurizon Network has delivered two full years of ballast undercutting for the 2014DAU term. The QCA has correctly recognised this and confirmed that the FY2014 scope was appropriate. The FY2015 scope that the QCA has proposed, is seven less turnouts than Aurizon Network has delivered during that year as reported within the Maintenance Cost Report. However, Aurizon Network is not looking to contest this scope (nor the costs) for FY2015.

Aurizon Network's main issue is with the overall methodology and how this is applied to create the FY2016 and FY2017 turnout scope. Aurizon Network has not changed the methodology or scope (barring corrections outlined within its response to the MAR Draft Decision<sup>200</sup>) throughout the time taken to resolve the 2014DAU. This, coupled with the previous QCA consultant's review of the ballast program, which concluded 'that no adjustments are necessary to the proposed scope for turnouts'<sup>201</sup>, makes it difficult to understand why the QCA has recommended that the scope be changed at this stage of the 2014DAU process.

CMT has developed an undercutting scope for turnouts based upon the GPR data sourced from either side of the turnout. It is unclear to Aurizon Network what parameters CMT has used to create this scope i.e. what data was used to reflect the locality of the turnouts as well as distance used on either side of the turnout. Aurizon Network believes that this process is substantially flawed due to the lack of data that could support such a methodology. Aurizon Network has received the data as an output of CMT's model, however is unable to replicate the results.

Due to the increased amount of steel through turnouts, GPR cannot be used to assess the ballast fouling immediately beneath turnouts - the GPR machine returns a null result. When the results are overlaid upon a map, these 'non-results' are displayed as grey lines over the rail. This is shown in Figure 24.1 below.

**Figure 24.1 – GPR Results at Caval Ridge Turnout. Grey lines indicate no data available**



<sup>200</sup> Aurizon Network (2014a). s 6.4.6, p. 134.

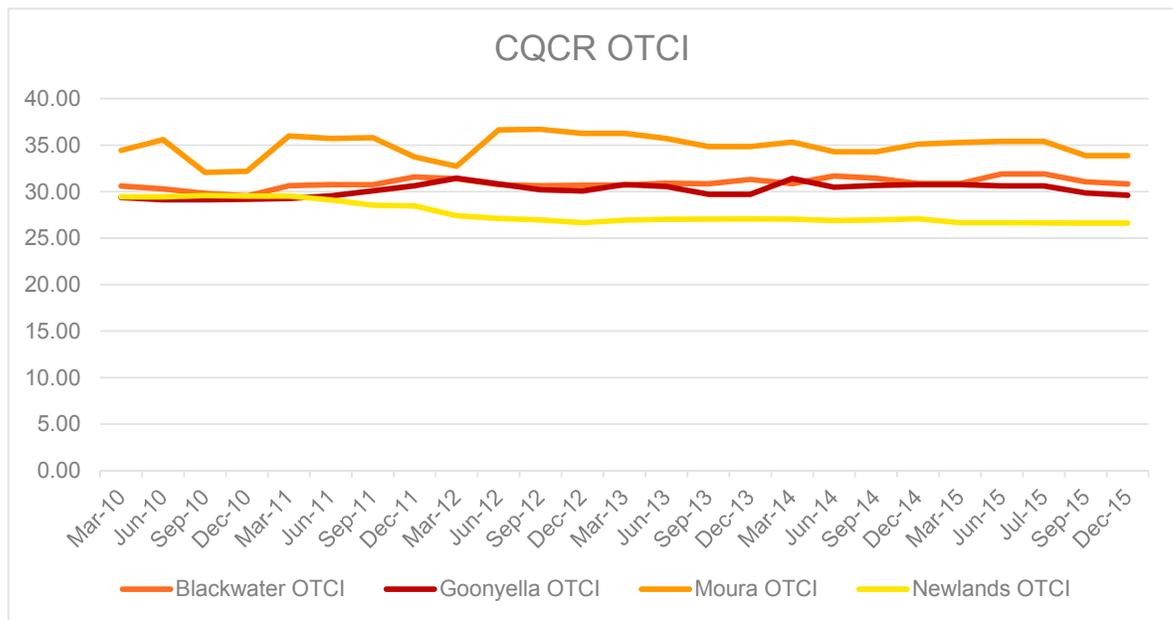
<sup>201</sup> Jacobs SKM (2014). Engineering Technical Assessment of Maintenance, Operating and Capital Expenditure Forecast, s.2.2.4, p. 34.

Due to this technological barrier, Aurizon Network uses the NSAP to determine the number of turnouts that are required to be undercut during a regulatory period. This is based on a number of factors including tonnages within the relevant systems. Aurizon Network extended an invitation to CMT on multiple occasions to review the NSAP model, however this was not taken up.

The QCA has also suggested that either Aurizon Network’s NSAP model is inaccurate or there is an accumulation of backlog of turnout undercutting.<sup>202</sup> This is purely speculative - Aurizon Network does not agree with this statement, nor has the QCA provided any empirical evidence to support it.

The Evan’s and Peck Condition Based Assessment conducted in 2013 did not draw any such conclusion from its detailed desk-top and field assessment of the CQCR. Further analysis of the relevant data indicates that overall track condition (measured by the Overall Track Condition Index (OTCI)) remains constant along with turnout faults that could be attributable to ballast. This has occurred in an environment of annual increases in tonnages hauled across the CQCR. This is shown in the following figure.

**Figure 24.2 – CQCR Overall Track Condition Index**



The QCA recommended scope of approximately 40 turnouts each year. This could not possibly take into account the increase in tonnages from 213million tonnes in FY2014 to 226 million tonnes in FY2017. Any yearly increase in tonnes should have a direct relationship with an increase in the required number of turnouts that need undercutting.

As CMT has relied upon GPR data solely to arrive at this scope, it is certain it has omitted the majority of Aurizon Network’s turnouts within major yards such as Callemondah, Jilalan, Yukan, Blackwater, Coppabella and Pring. It is certain that these were not considered as only the mainline through these

<sup>202</sup> Queensland Competition Authority (2015d),p. 138.

yards have had a GPR measurement applied against them. To put this into context, In Callemondah, there are 120 turnouts, of which 11 have GPR data leading up to them.

Turnouts within yards still require undercutting. This is yet another reason why Aurizon Network uses a tonnage-driven model across all turnouts.

The QCA's recommended scope, which being solely based on GPR, fails to consider several hundred turnouts in the CQCR, contradicts its statement relating to the importance of considering tonnages when establishing the required mainline scope. The lack of consideration given to tonnages coupled with GPR being unable to provide any definitive results, puts at question the methodology and resultant scope applied by the QCA.

Aurizon Network does not agree with the QCA's methodology to achieve the turnout undercutting scope as:

- it has no definitive basis;
- it does not take into account any increase in tonnages;
- it does not consider the actual number of turnouts that exist in the CQCR.

The QCA has also made statements that are incorrect that may have impacted its assessment. When these factors are combined with the time taken to approve the 2014DAU, this means that Aurizon Network can only agree with the scope for FY2014 and FY2015, noting that these two years have already been delivered.

Aurizon Network will continue to use the NSAP model to develop the turnout scope for its future regulatory proposals. This will continue until improvements in GPR technology and the associated analytical tools enable it to be used to assess ballast fouling at turnouts.

### **Conclusion: ballast undercutting scope**

Given it is now into its third year of the 2014DAU term and Aurizon Network has continued to invest in maintaining the network in good faith during this time, Aurizon Network partially agrees with the QCA's recommendation on the efficient ballast undercutting scope. However, questions of the methodology and process remain. Aurizon Network agrees with the mainline scope as this aligns with Aurizon Network's cost model. However, it does not agree with the QCA's proposed turnout scope for FY2016 and FY2017, which it submits should remain as per Aurizon Network's originally submitted scope.

The ballast undercutting program (like all other maintenance activities) has a long planning horizon prior to the execution of individual work activities. The timing of the QCA's Final Decision (currently April 2016), means that if there are further scope changes following this CDD, Aurizon Network will have limited ability to amend any planned work as a result of those further changes.

Aurizon Network therefore proposes that the 2014DAU ballast scope is as detailed within the table below.

**Table 24.3 – Ballast Undercutting Scope**

	FY2014 <sup>^</sup>	FY2015	FY2016	FY2017	Total
Aurizon Network Proposed Scope – February 2016					
Turnout	41	40*	57	58	196
Mainline	118	129**	133	140	520
Volume m <sup>3</sup>	354,011	322,500	332,500	350,000	1,359,011

<sup>^</sup>Actuals used

\*Noting Aurizon Network's FY2015 delivery of 48 turnouts

\*\*Noting Aurizon Network delivery of 152km in FY2015

## CDD 24.2 Ballast Undercutting Costs

The QCA has largely incorporated CMT's recommendations relating to the costs associated with Aurizon Network's ballast undercutting program. A summary of the QCA's proposed allowances is provided in Table 24.4 below.

**Table 24.4 – CDD: Ballast Undercutting Allowance (\$million, nominal)**

	FY2014	FY2015	FY2016	FY2017	Total \$m
Aurizon Network Proposed Allowance – December 2014					
Total	54.6	66.2	76.2	80.4	277.4
Less QCA Consolidated Draft Decision Adjustments - December 2015					
Mainline undercutting	0	(2.6)	(9.4)	(8.5)	(20.5)
Turnout	0	(1.0)	(1.0)	(1.1)	(3.1)
GPR Measurement	0	(1.2)	(1.2)	(1.2)	(3.6)
QCA CDD (Nominal)	54.6	61.5	64.6	69.7	250.4

The QCA's reasoning for the reductions in the ballast allowance from Aurizon Network's proposal can be summarised as follows:

- mainline undercutting – capping of the mainline undercutting costs at \$400,000 per kilometre;
- turnout undercutting – a reduction in the variable element, directly related to the reduction in scope as a result of the QCA's CDD 23.1;
- GPR measurement costs – removal of the proposed allowance as the QCA believes that there will be no further GPR runs during the 2014DAU period.

### CMT's review of Aurizon Network's ballast undercutting allowance

As outlined above, Aurizon Network assisted CMT with the review of its ballast undercutting program. As part of that assistance, Aurizon Network provided GPR data sets, multiple briefing (and educational) workshops, access to cost and planning models and extended invitations to visit site and see the NSAP model.

As part of CMT scope of work, it was a requirement that an independent costs build up for a ballast undercutting program be developed. CMT has confirmed in its report that its costs within its independent build up "have not been cross checked with current industry rates"<sup>203</sup>. The QCA has relied upon this costs build up in making its CDD.

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## How an independent cost build up can be completed and a material regulatory decision be made without any consideration to current industry practice to form a basis for efficient costs is inconceivable.

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If CMT's independent costs build up was implemented using the assumptions that were used to create it, no coal carrying trains would be able to run on the network due to the issues with the track geometry as a result of its program, constant interruptions to coal services and a lack of any safety or protection mechanisms for the ballast undercutting program, which is untenable for Aurizon Network given its core priority of Zero Harm.

As part of the QCA's engagement, personnel from Aurizon Network made themselves available to meet with CMT and did so over nine times. Given this level of engagement, it would be expected that the foundations of Aurizon Network's ballast undercutting program (and certainly the principles embedded within it) would have been fairly well understood. It is therefore disappointing to see that CMT has continued to misinterpret operational practices of Aurizon Network. These issues are addressed below.

### On-site sourcing

CMT was briefed multiple times and provided with a written explanation as to what on-site sourcing was<sup>204</sup>. It appears from the CMT report, that it has interpreted 'on-site sourcing' as situations where Aurizon Network sources ballast from an alternative method other than from its standard quarries.

Aurizon Network does not source any ballast from any other source apart from the quarries detailed within its cost model. To source ballast from any other locations is impossible as:

- ballast is not located conveniently adjacent to the rail infrastructure throughout the 2600km of the CQCR;
- if there was ballast available elsewhere, it is highly likely to be of an unsuitable quality or quantity;
- environmental requirements (and most likely financial considerations too) would not permit developing a small scale quarry at alternative locations or within the corridor to excavate ballast;
- land surrounding the corridor is not owned by Aurizon Network, and therefore land access issues (and legal concerns) to excavate the ballast and manage spoil would be extremely problematic, time prohibitive and costly. It is also not Aurizon Network's core area of operation and the skillset and machinery would need to be hired in.

Aurizon Network confirms that all ballast used within the CQCR is sourced from the six quarries outlined within Table 10 of CMT's report. This is because these are the only quarries within the CQCR that have the quality of ballast that is suitable for heavy haul railways<sup>205</sup>.

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<sup>203</sup> CMT (2015). p. 45.

<sup>204</sup> QCA RFI List v30, RFI B57

<sup>205</sup> Aurizon Network (2014a). Chapter 6, p. 137.

The only difference in the sourcing of ballast employed by Aurizon Network is the way in which the ballast is delivered to the undercutting worksite. For delivery of ballast, Aurizon Network employs two methods:

- **Rail** – Truck delivery from quarry to stockpile and then delivered via a locomotive and ballast wagons to worksite. This is the most cost effective method;
- **On-site sourcing** – Delivered on road via truck directly to worksite. It is then stockpiled at site and front-end loaders and trucks deliver it to the precise worksite. The QCA highlights Aurizon Network’s previous acknowledgment that this is a less efficient method. However, it is important to emphasise that Aurizon Network only employs this ‘less efficient’ method out of necessity, that is, in situations where it is not feasible for ballast to be delivered by rail.

Overall, the costs of ballast is increasing due to the mainline undercutter mechanism (excavator undercutting) to complete the required work. This form of undercutting is used to supplement the fully utilised RM900 and is used to complete approximately 30km of undercutting per annum. The excavator undercutting requires 100% of the replaced ballast to be trucked in from the relevant quarry. With the majority of excavator undercutting being completed within the Goonyella System, the majority of the ballast is being sourced from the Waitara quarry, which is the most efficient quarry to source the raw material from.

Access into ballast quarries has been another driver for the increase in the use of on-site sourcing to some sites. For example, in the Blackwater system, Yarwun and Blackwater are the only two quarries that have ballast train load-out facilities. In the event that the actual undercutting worksite was between the two quarries, it is more efficient to truck ballast to site and stockpile prior to works commencing. The ballast train would then be refilled at site to avoid it making multiple empty journeys back to the relevant quarry.

CMT has recommended that the ballast undercutting allowance be reduced by approximately \$1million in FY2016 and FY2017 to take into account the perceived cost increase of on-site sourcing. This was recommended based upon the flawed assumptions described above.

Upon a further review of the cost and planning models, Aurizon Network has identified an error where values had been entered incorrectly. This error has resulted in Aurizon Network reducing its ballast costs by \$0.694million and \$0.707million respectively for years FY2016 and FY2017. This error was related to Waitara and the “On Site” sources being entered incorrectly.

#### Procurement of more efficient machinery

CMT has stated that “due to the age and inefficiencies of the current undercutting machine the RM900 a significant volume of ballast is not able to be screened and returned. Changing to newer machines could facilitate cleaning of more ballast with elevated PVC levels and reduce fleet maintenance cost and expected ballast costs”<sup>206</sup>. It is unclear from Aurizon Network’s review how CMT formed this opinion and on what basis, nor did it raise this as a question in discussions with Aurizon Network. There has been no data or references used to support this statement.

CMT then goes onto to comment that there is an “average loss”<sup>207</sup> that may be attributable to the aging RM900 ballast undercutter. This ballast loss is not the inability of the RM900 to screen that fouled ballast, but is in fact the ballast return rate applicable to each of the financial years listed. CMT should have been able to justify its position based upon research of manufacturers of ballast equipment, however this factual basis is lacking.

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<sup>206</sup> CMT (2015). p.vi.

<sup>207</sup> CMT (2015). p.42.

At no stage of the report does CMT acknowledge that if Aurizon Network was to procure a more operationally efficient ballast undercutter, this would come at a higher cost through the return on and depreciation of that new machinery. This ignores the investment approval process that a commercial business must follow in making a replacement decision. At Aurizon Network, any decision to replace machinery with newer machinery must go through a rigorous investment appraisal process that assesses the risk, costs and benefits of the investment. The decision to procure machinery is ultimately a business decision of Aurizon Network's, although it also needs to be able to demonstrate that it is prudent and efficient in seeking approval of those costs under the regulatory framework.

Aurizon Network confirms that it is in the process of procuring a new mainline undercutter to replace the RM900. The purchase of the RM902 ballast cleaner followed Aurizon's investment approval process. It is currently in the design phase and is scheduled to be commissioned into operation in February 2019.

The RM902 is a Very High Production Ballast Cleaning Machine (VHPBCM) that consists of a ballast shoulder cleaner unit, ballast transfer wagon and ballast undercutting unit. The VHPBCM is specially designed to separately remove and screen the ballast shoulders, then the main undercutting chain excavates the ballast from beneath the sleepers, sending this material to separate screening units. The reusable ballast from the shoulder cleaner and main undercutting unit is separated from the waste material and returned back into the track behind the main undercutting chain. A system of conveyors transports the waste material to the end of the machine, where it is discharged into the spoil management wagons.

#### Other Issues with the independent costs build up

Aurizon Network has not been provided with, nor had any visibility of, the independent costs build-up model created by CMT. Aurizon Network has only reviewed CMT's report as part of the CDD.

Upon review of the assumptions used to develop the independent costs build up, Aurizon Network has identified substantive flaws and variations from standard ballast undercutting practices that most heavy haul railways employ. CMT has only provided an allowance for the cost of one mainline ballast undercutter and assumes that no other machinery is utilised by Aurizon Network in executing its ballast undercutting program.

Aurizon Network has detailed on multiple occasions that the ballast undercutting scope cannot solely be completed using the RM900 and that other machinery, including excavator undercutters are required to make up the balance of work (as explained above). CMT has negated any consideration of this.

If the ballast undercutting program was implemented as per CMT's cost build up, the network would not be able to have any rail traffic due to it being unsafe to operate. The exclusion of other machinery, such as tampers, regulators and stabilisers, will result in track failure, loss of 'top and line'<sup>208</sup> and substantial speed restrictions. Overall, these issues result in the QCA's CDD to cap Aurizon Network's undercutting unit rate at \$400,000 per km being substantially flawed.

Aurizon Network has summarised the major issues with that costs build up in the table below.

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<sup>208</sup> Top & Line' refers to the 'smoothness' of the running surface at the interface between the rail and a locomotive or wagon wheel. 'Top & Line' deterioration can occur to the extent at which the running surface becomes too 'rough' and wheel unload can occur, that is, loss of contact between the rail and the locomotive or wagon wheel. Clearly such a condition is unsafe and upon inspection (or reporting thereof from train crew), track will be closed to traffic.

**Table 24.5 – Issues with CMT’s independent costs build up**

Issue with CMT costs build	Why item is required	Included within Aurizon Network’s \$/km unit rate ?	Cost for machinery \$/km
<b>No provision for Regulator machinery</b>	<p>Provides a consistent ballast profile to reduce track instability</p> <p>The Regulator is a critical piece of equipment as it ‘regulates’ the ballast profile and ‘tidies up’ and maintains the ballast profile. Without this machine, ballast profiles across the CQCR will be very ‘lumpy’. It removes surplus ballast and distributes ballast into zones having deficient ballast.</p> <p>It is essentially mechanised ‘brooming’ and localised ballast distribution and is essential to the process as it is a requirement to ensure the overall ballast profile complies with Aurizon Network’s Safety Management System.</p>	Yes	<p>The regulator has a total depreciation and maintenance cost of \$0.3million per year and this would convert to circa \$3,000 per km within the mainline RM900 undercutting unit cost.</p> <p>This also has additional labour costs attributable to include this within the Aurizon Network’s ballast consist.</p>
<b>RM900 cannot complete CMT’s required scope</b>	<p>As detailed in previous submissions, the RM900 cannot solely complete the full scope that CMT, the QCA and Aurizon Network all agree is appropriate. The balance of works must be completed by other machinery, such as an excavator undercutter, which can complete up to 25% of the annual mainline scope.</p>	Yes	<p>This alternative method is as efficient when compared to the RM900. It is used not only to deliver the mainline undercutting scope which the RM900 can complete, but is also used to undercut in difficult areas and near signals where the RM900 would not be able to get close enough too due the spoil wagons being part of the consist. Over the period from FY2015 to FY2017, an average scope per year of 25kms will be done at an annual average cost of \$13.4M.</p>

**Table 24.5 – Issues with CMT’s independent costs build up**

Issue with CMT costs build	Why item is required	Included within Aurizon Network’s \$/km unit rate ?	Cost for machinery \$/km
<p><b>No provision for Resurfacing machinery</b></p>	<p>The Resurfacing machine is essential to the undercutting process and is used post ballast undercutting. It enables the re-establishment of:</p> <ol style="list-style-type: none"> <li>1) track alignment; and</li> <li>2) top (vertical) and line (lateral) to bring the track back to design alignment and within Civil Engineering Track Standards (CETS) tolerances for track geometry.</li> </ol> <p>It minimises variations in track geometry, which along with ballast consolidation (i.e. stabilising), enables a return to full line speed.</p>	<p>Yes</p>	<p>The resurfacing equipment within the undercutting consist has two tampers. The average annual maintenance and depreciation costs of these machines are \$1.7million per year over FY2015 - FY2017. This equates to approximately \$15,200 per km.</p> <p>It is estimated that approximately 50% of the ballast undercutting program labour costs are incurred by resurfacing.</p>
<p><b>No provision for Stabiliser machinery</b></p>	<p>The Stabiliser or 'DTS' effectively consolidates the entire ballast profile and all things being equal, creates 'stable' track by vibrating the ballast particles at a particular frequency to enable ballast interlocking.</p> <p>If this activity was not completed, re-opening the track post-undercutting could only be done with considerable speed restrictions.</p> <p>Along with resurfacing, enables a return to full line speed, subject to a track geometry review.</p>	<p>Yes</p>	<p>The Stabiliser has a total depreciation and maintenance cost of \$0.25million per year and this would convert to circa \$2,200 per km within the mainline RM900 undercutting unit cost.</p> <p>This also incurs additional labour costs in including this within the Aurizon Network ballast consist.</p>
<p><b>Exclusion of 24 additional MFS spoil wagons</b></p>	<p>These wagons enable significant efficiency gains when undercutting in difficult (re. topographically and/or environmentally troublesome) areas. They allow for the undercutter to work for longer periods before having to temporarily cease works in order to detach MFS wagons and dispose of spoil in an</p>	<p>Yes</p>	<p>The MFS wagons have a total depreciation and maintenance cost of (on average) \$2.1million per year. This would convert to circa \$19,000 per km within the mainline RM900 undercutting unit cost.</p>

**Table 24.5 – Issues with CMT’s independent costs build up**

Issue with CMT costs build	Why item is required	Included within Aurizon Network’s \$/km unit rate ?	Cost for machinery \$/km
	appropriate area and then re-attach the MFS wagons to re-commence operations.		
<b>No provision for ballast wagons</b>	<p>The benefits of having ballast wagons include:</p> <ul style="list-style-type: none"> <li>• allowing significant volumes of ballast to be introduced into track as efficiently as possible as opposed to a significant number of trucks and front end loaders using a road haulage method followed by double-handling on site;</li> <li>• efficiently transports ballast directly from stockpile (i.e. quarry, ‘local’ storage area) to the track, minimising double-handling on site.</li> </ul>	Yes	Aurizon leverages its benefit of being an integrated railway and these reduced costs are passed through to Aurizon Network’s customers. On average, the cost differential is \$37 per m <sup>3</sup> versus trucking (on-site sourcing).
<b>Ballast delivery method does not reflect actual practice</b>	CMT has only assumed that the ballast is to be delivered to stockpile. There is no further transportation via either road or rail to the actual undercutting worksite. Aurizon Network uses ballast wagons to transport ballast from stockpile to worksite via rail or trucks via road.	Yes	Over the FY2015 to FY2017 period, this will costs on average \$4.7million per year. From a unit cost perspective this is on average \$42,000 per km.
<b>Assumes continuous operation of the ballast cleaning machine<sup>209</sup></b>	CMT’s independent costs build up has assumed 24 hours of continuous operation of the ballast undercutter. At a high level, the issues with this assumption include:	Yes	

<sup>209</sup> CMT (2015). p.45.

**Table 24.5 – Issues with CMT’s independent costs build up**

Issue with CMT costs build	Why item is required	Included within Aurizon Network’s \$/km unit rate ?	Cost for machinery \$/km
(CMT contradicted within Appendix B)	<ul style="list-style-type: none"> <li>labour agreements would not allow for such operation;</li> <li>there would be a requirement to have approximately an additional 107 spoil wagons attached to the ballast undercutting consist<sup>210</sup> (CMT has not costed these wagons nor allowed for the additional variable costs such as locomotives, fuel or reduced travel speed/access);</li> <li>the flawed assumption that there will be no stoppages to rectify mechanical, operational or labour related issues; and</li> <li>it being highly unlikely that there will not be turnouts, signals or electrical infrastructure that require additional time to prepare the site and operate within.</li> </ul> <p>A typical ballast undercutting 24 hour period for Aurizon Network would result in 6.5 hours of undercutting. The remainder of the time would be spent on travel, safety briefings, pre-start preparation, cut-ins, cut-outs, adding new ballast, resurfacing, stabilising, regulating, travel and storage.</p>		
<b>No allowance for managing disruptions to coal services</b>	Mainline undercutting operation does not receive an entire day’s access to operate, or 10 hours as per the costs build up. Aurizon Network’s receives blocks of time to complete the works to enable the continued	Yes	

<sup>210</sup> Using the performance rate of the existing spoil wagons outlined within Aurizon Network’s response to the MAR Draft Decision: Aurizon Network (2014). section 6.4.2 – Historical Performance Against Scope, p. 129.

**Table 24.5 – Issues with CMT’s independent costs build up**

Issue with CMT costs build	Why item is required	Included within Aurizon Network’s \$/km unit rate ?	Cost for machinery \$/km
	<p>operation of coal services. The only case where this would not apply is where the works are part of a larger system closure.</p> <p>As per the independent costs build up, it would be more efficient for 10 hour blocks to be granted to reduce the unit cost. However this is impractical/impossible as coal services will be severely impacted.</p>		
<p><b>No provision for additional locomotives to assist ballast consist</b></p>	<p>CMT has assumed that the RM900 travels at an average of 48km per hour between sites.</p> <p>No allowance has been provided for additional locomotives to assist the ballast consist. The RM900 can only propel itself and this can only occur on straight, flat rail.</p> <p>Aurizon Network utilises locomotives to move between sites due to the size of the consist when all MFS wagons, water, fuel and undercutter are within the consist, resulting in it being approximately one km long.</p>	<p>Yes</p>	<p>The cost of the additional locomotives required to assist the ballast consist was \$4.558million in FY2015. The expected cost for FY2016 is expected to be around \$4.4million, based on an average cost of \$40,000 per km for 110km of work.</p>
<p><b>Depreciation limited to the RM900</b></p>	<p>CMT has only included depreciation on the RM900 whereas Aurizon Network unit rate includes depreciation for all machinery used for ballast undercutting purposes (as listed within this table).</p> <p>Aurizon Network has purchased new machinery to replace age expired, inefficient machinery. This includes the MFS wagons and new tampers. These</p>		<p>Depreciation accounts for \$12,000 per km in FY2015, but this increases to \$26,000 per km and \$28,000 per km in FY2016 and FY2017 respectively. This increase is driven by the arrival of the new 24 spoil wagons that are being commissioned in a staggered manner.</p>

**Table 24.5 – Issues with CMT’s independent costs build up**

Issue with CMT costs build	Why item is required	Included within Aurizon Network’s \$/km unit rate ?	Cost for machinery \$/km
	machines facilitate the cleaning of more ballast, open the track with no speed restrictions and reduced fleet maintenance costs.		

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Based upon the scope proposed in the QCA's CDD, Aurizon Network confirms that including all items listed in the table above, its efficient unit rate for the 2014DAU period is as follows.

**Table 24.6 – Aurizon Network's proposed unit rate for ballast undercutting**

	FY2014	FY2015	FY2016	FY2017
\$ per km	\$368,216	\$420,069	\$480,906	\$481,191

The following table shows the unit rate proposed by the QCA, reflecting the independent costs build up determined by CMT, and the consequent under-recovery that Aurizon Network would incur each year.

**Table 24.7 – QCA's proposed unit rate for ballast undercutting and consequent under-recovery**

	FY2014	FY2015	FY2016	FY2017
\$ per km	\$368,216	\$400,000	\$410,000	\$420,782
QCA vs AN (\$ per km)	-	(\$20,069)	(\$70,906)	(\$60,409)

Aurizon Network strongly disagrees with the cap that the QCA proposed to apply to such a critical aspect of Aurizon Network's maintenance program, noting that it has not been tested against other external railway managers.

Aurizon Network would like to point out that in FY2015, it delivered 152 km of undercutting and 48 turnouts at a total cost of \$61.7 million (reflecting a unit rate of \$378,000 per km and \$87,000 per turnout). This was delivered through finding efficiencies within the ballast undercutting program, coupled with the ability to re-use more of the existing ballast than was what was originally planned.

The key reason for Aurizon Network's projected increase in the efficient unit rate from FY2015 onwards are:

- the increase in depreciation and maintenance costs for the 24 additional spoil wagons. The procurement of these wagons was completed following a detailed cost benefit analysis;
- the increase in ballast volume (11%), which relates to the nature of the scope (that is, lower screen ability due to the worksites that are more difficult to access). The additional 24 MFS wagons being available for the full FY2016 allows Aurizon Network to more efficiently undercut these areas due to the volume of fouled ballast that these wagons can handle;
- the increase in freight costs due to moving the additional 24 spoil wagons around the network. This is seen through the requirement to have locomotives to facilitate the movement of the machinery to site as well as whilst operating; and
- the incremental storage costs at Jilalan for the additional equipment. As the ballast consist is longer than previous, locating appropriate storage locations is limited within the network without impacting coal services.

As outlined in this section, Aurizon Network's ballast undercutting program and therefore its unit rate is inclusive of these elements and not just limited to the operation of the RM900 or the limited assumptions that CMT have used to create their independent costs build up. For this reason, there is a substantial difference between the programs and comparing the unit rate of the two programs is not appropriate (noting that as stated above, if CMT's program was implemented the network would not be able to have any rail traffic due to it being unsafe to operate).

In addition to the shortcomings, CMT has acknowledged that this is “not a benchmark value”<sup>211</sup>. Aurizon Network in developing its response to the MAR Draft Decision, did make enquiries with a comparable railway infrastructure manager and identified that Aurizon Network’s unit rates were less expensive than the market tendered rate that the other manager was incurring.<sup>212</sup>

Because of the substantial shortfalls in the number of assumptions CMT used to build its independent costs model, coupled with it not being tested against industry rates, Aurizon Network therefore disagrees with the QCA’s decision to cap the mainline undercutting unit rate. Aurizon Network therefore submits that its mainline allowance for FY2016 and FY2017 as proposed in its response to the MAR Draft Decision (see below) remains appropriate and will allow it to recover its prudent and efficient costs.

#### GPR allowance

The timing to obtain approval of the 2014DAU has increased the regulatory risk associated with the operational decisions that Aurizon Network is obliged, as Railway Infrastructure Manager, to make on a daily basis. The GPR program has been affected by these delays.

In its CDD, the QCA proposes to remove the GPR allowance and that the costs should instead be addressed via the revenue cap process. The reasons stated include that Aurizon Network was waiting for “new analytical software”<sup>213</sup>.

Aurizon Network confirms that it is purchasing additional software to manage the amount of data that is generated by the GPR program and integrate other data streams (such as track geometry). Aurizon Network will seek approval for the recovery of these costs as a future capital expense claim. However, this is not the reason that the GPR program was not completed in FY2015 - it was solely due to the delays in the decision on UT4.

To recover the costs of the GPR program, Aurizon Network believes that an adjustment to the MAR is the appropriate method to recover these costs. The QCA’s proposal to include it within the revenue cap adjustment process is not appropriate due to the system-specific nature of the revenue cap versus, whereas the GPR program is managed on a network-wide basis.

As the majority of the GPR program is externally resourced, Aurizon Network is responsible for managing the costs. Therefore any risk of under-budgeting should be borne by Aurizon Network, meaning that a true-up mechanism through revenue cap is not required.

As a result of the delays in the 2014DAU decision, Aurizon Network will only complete one further GPR run during the term, most likely in FY2017. As a result of the reduction in number of runs, the scope of the one run will be larger than previous, resulting in a slight increase in costs of \$1.5million.

#### **Conclusion: ballast undercutting costs**

In summary, Aurizon Network reiterates that

- agrees with the revised turnout allowance, when reviewed against the turnout scope recommended by the QCA;
- disagrees with the QCA’s proposed mainline cost capping, and consequent cost allowance, as that allowance is in no way reflective of an efficient ballast undercutting program that needs to be

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<sup>211</sup> CMT (2015). p. 47.

<sup>212</sup> Aurizon Network (2014a).s.6.2, p. 122.

<sup>213</sup> Queensland Competition Authority (2014d). p. 146.

delivered in a complex and dynamic operating environment. It will therefore not allow Aurizon Network to recover its efficient costs; and

- disagrees with the QCA's exclusion of the costs of any future GPR runs and submits that an allowance of \$1.5 million be provided for one GPR run during the remaining term of the 2014DAU, ;
- disagrees with the methodology to create the FY2015 allowance, however as this reflects the actual costs incurred in that year, Aurizon Network is not proposing the allowance be adjusted.

Aurizon Network proposed allowance is as follows.

**Table 24.8 – Revised Ballast Undercutting Allowance (\$ million, nominal)**

	FY2014 <sup>^</sup>	FY2015	FY2016	FY2017	Total \$m
QCA Consolidated Draft Decision Allowance – December 2015					
Total	54.6	61.5	64.6	69.7	250.4
Add back the Consolidated Draft Decision Adjustments					
Mainline undercutting	0	0	9.4	8.5	17.9
Turnout	0	0	1.0	1.1	2.1
GPR Measurement	0	0	1.5	0	1.5
On-site Sourcing Correction	0	0	(0.7)	(0.7)	(1.4)
Aurizon Network 2014DAU Ballast Allowance (Nominal)	54.6	61.5	75.8	78.6	270.5

<sup>^</sup>Actual amounts used.

Note: Numbers may not sum due to rounding.

## CDD 24.3 Ballast Impairment Charge

The QCA has approved not to continue the Ballast Depreciation charge for the 2014DAU term. Noting the reasons summarised in its response to the MAR Draft Decision<sup>214</sup>, Aurizon Network welcomes this decision. Aurizon Network submits that if the QCA is minded to change its view on this matter prior to the Final Decision, it is given the opportunity to discuss this with the QCA.

<sup>214</sup> Aurizon Network (2014a). s.6.2, p.121.

## Part 25 – Opening Asset Value

### Summary of Aurizon Network's Position

Aurizon Network disagrees with the QCA's Opening Asset Value. There are two sources of this difference:

- Aurizon Network does not accept the QCA's refusal to allocate \$30.3 million in GAPE project costs to the Newlands system, instead requiring them to be allocated to GAPE and NAPE Deed customers (refer response to CDD 17.2);
- Aurizon Network does not accept the QCA's rejection of equity raising costs for GAPE on the basis that it would be a retrospective adjustment. The decision to defer the consideration of these costs until the UT4 review has been previously acknowledged by the QCA.

The QCA has accepted Aurizon Network's proposal to allow for equity raising costs to be approved for new investments. However, Aurizon Network has proposed some further amendments so that this is clearly aligned with the Australian Energy Regulator's (AER's) benchmark approach, as was its original intent.

**Table 25.1 – QCA Consolidated Draft Decision**

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1) After considering Aurizon Network's proposed opening RAB, our consolidated draft decision is to refuse to approve Aurizon Network's original proposal.	25.1	<b>Disagree.</b> \$30.3million allocation of GAPE costs to the existing Newlands system is appropriate and is a reasonable reflection of the scope of works required in the absence of the GAPE project.
(2) We consider that the opening RAB proposed in Aurizon Network's December submission is appropriate subject to the reallocation of capital expenditure as discussed in Section 6.1.5. Therefore, the way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to set the opening RAB as specified in Section 6.1.5.		
(1) After considering Aurizon Network's proposal to include \$5.77 million in equity-raising costs in respect of UT3 in the regulatory asset base as at 30 June 2013, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.	25.2	<b>(1) &amp; (2) Disagree.</b> Aurizon Network has a legitimate case for the inclusion of equity raising costs for GAPE during UT3, which was postponed for inclusion as part of UT4 by agreement with the QCA.
(2) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to not include any amount in equity-raising costs in respect of UT3 in the regulatory asset base as at 30 June 2013.		<b>(3) Agree with amendments.</b> While the QCA has agreed with Aurizon Network's proposal to apply the AER's benchmark approach, amendments need to be made to Schedule E drafting to reflect this.
(3) After considering Aurizon Network's proposal to include future equity raising costs in the RAB at the conclusion of a		

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
regulatory period, our consolidated draft decision is to approve Aurizon Network's proposal as contained in its December 2014 submission.		

## CDD 25.1 Opening Asset Value

The QCA rejected Aurizon Network's proposed Opening Asset Value in its 2014DAU. Consistent with CDD 17.2 on GAPE pricing, the QCA has reallocated \$30.3million of capital expenditure, previously allocated to the Newlands system, to NAPE and GAPE Deed customers, according to their contract tonnages. As outlined in its response to CDD 17.2, Aurizon Network reiterates that the \$30.3million allocation of GAPE costs to the existing Newlands system is appropriate and is a reasonable reflection of the scope of works required in the absence of the GAPE project.

As a result, Aurizon Network proposes to retain the FY2012 allocation of GAPE costs to the existing Newlands system for the purpose of calculating the UT3 capital carryover adjustment and the Opening Asset Value for the 2014DAU. This is reflected in Aurizon Network's Opening Asset Value.

In the event that the QCA refuses to approve Aurizon Network's proposal, Aurizon Network confirms that the methodology outlined in the QCA's CDD<sup>215</sup> is appropriate, i.e. \$30.3million is to be allocated between both GAPE and NAPE customers on the basis of volumes contracted. As outlined in its response to the QCA's IDD,<sup>216</sup> Aurizon Network will submit a DAAU for NAPE train services once there is more certainty around their commencement date (refer response to CDD 17.2).

Aurizon Network also believes the QCA have incorrectly applied the UT2 asset lives when calculating the RAB roll-forward (refer response to CDD 27.1). Aurizon Network's financial modelling reflects the correct UT3 asset lives, where appropriate.

Refer section 26.3 for Aurizon Network's revised opening asset values.

## CDD 25.2 Equity Raising Costs

In CDD 25.2 the QCA rejects Aurizon Network's proposal for equity raising costs, consistent with the MAR Draft Decision. It considers that:

- retrospective review of the capital expenditure costs approved in UT3 does not achieve an appropriate balancing of the interest set out in section 138(2) of the QCA Act;
- as no equity raising costs were included in Aurizon Network's initial proposal, or raised by the QCA when the decision was made to defer inclusion in the RAB until commissioning, the QCA does not consider it reasonable for access holders to expect their inclusion.

Consistent with Aurizon Network's response to the QCA's MAR decision, Aurizon Network disagrees with the QCA's reasons for rejecting the \$8.27m<sup>217</sup> claim for UT3 equity raising costs into the Opening Asset Value for UT4.

<sup>215</sup> QCA, CDD, Volume 3, 17.4.5, pg. 102.

<sup>216</sup> Aurizon Network, Response to QCA's Draft Decision on Policy and Pricing Principles, 17.7.2, pg. 252.

<sup>217</sup> Aurizon Network (2014a). s. 7.7.3, p. 154.

Aurizon Network reiterates the following arguments for the inclusion of equity raising costs in relation to GAPE project costs approved in UT3:

- equity raising costs were not part of the early works claim in 2007/08 because the GAPE scope wasn't sufficiently progressed;
- the original GAPE DAAU (September 2012) submitted by Aurizon Network included a claim for equity raising costs<sup>218</sup>. However, upon further discussion with the QCA, it became apparent that retaining the claim for equity raising costs in the GAPE DAAU would delay the approval of a GAPE Reference Tariff;
- as a result, Aurizon Network resubmitted the GAPE DAAU without the claim for equity raising costs, while stating an intention to include it as part of the UT4 submission. This approach has also been endorsed by QCA;<sup>219</sup>
- Aurizon Network does not seek any change to the approved capital expenditure. Therefore it is not a retrospective review of the capital expenditure costs approved by UT3. Rather, Aurizon Network is seeking the inclusion of these costs in the RAB.

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<sup>218</sup> September 2012 GAPE DAAU , Attachment A Page 34

<sup>219</sup> QCA Draft Decision GAPE, July 2013 Page v

## Part 26 – Regulatory Asset Base (including capital expenditure)

### Summary of Aurizon Network's Position

Aurizon Network accepts most of the decisions contained in Part 26 of the CDD. The main points it wishes to highlight are as follows.

- **Capital Indicator:**

Aurizon Network is willing to accept the QCA's proposed Capital Indicator subject to it accepting Aurizon Network's proposal that: (1) the revised WIRP revenue deferral extends no later than 30 June 2017 (refer Aurizon Network's response to CDD 18.10) ; (2) the GAPE deferral extends no later than completion of all RCS works in the Newlands system. If this is not accepted, Aurizon Network does not accept the QCA's proposed Capital Indicator.

- **Capital carryover account:**

The main point of disagreement is the QCA's proposal to reallocate \$30.3 million in FY2012 of capital expenditure from the Newlands system to GAPE and NAPE Deed customers. As noted previously, Aurizon Network considers this capital should be allocated to the Newlands system (refer response to CDD 17.2).

**Table 26.1 – QCA Consolidated Draft Decision**

	QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1)	After considering Aurizon Network's proposal to change the methodology for calculating interest during construction to a post-tax nominal classic WACC, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.	26.1	(1) <b>Agree.</b>  (2) <b>Agree.</b>
(2)	The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to use the post-tax nominal vanilla WACC for calculating interest during construction.		(3) <b>Agree with amendments.</b> Aurizon Network is willing to accept the changes made to QCA's Capital indicator subject to the following being approved by the QCA: (1) the revised WIRP revenue deferral extending no later than 30 June 2017 (refer Aurizon Network's response to CDD 18.10); (2) the GAPE deferral extending no later than completion of all RCS works in the Newlands system.
(3)	After considering Aurizon Network's proposed capital indicator, as at December 2013, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.		(4) <b>Agree.</b>
(4)	The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to use the post-tax nominal vanilla WACC for calculating interest during construction and include approved capital expenditure for 2013–14.		(5) <b>Agree.</b>  (6) <b>Agree.</b>
(5)	After considering Aurizon Network's proposal to treat re-railing costs as maintenance expenditure, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.		(7) <b>Agree with amendments.</b> Having regard to its existing obligations within the regulatory framework, Aurizon Network agrees to complete this through the maintenance briefing outlined in Part 5 of this CDD

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
<p>(6) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to treat re-railing costs as renewals expenditure and include them in the capital indicator from FY2016, as set out in <b>Error! Reference source not found.</b></p> <p>(7) We consider it appropriate that Aurizon Network provide an annual forecast of asset renewal costs and scope to the QCA prior to the commencement of each financial year, with renewals activities to be included as part of the reporting arrangements for the annual maintenance report.</p> <p>(8) We consider it appropriate that the capital indicator for UT4 be amended, as set out in <b>Error! Reference source not found.</b></p>		<p><b>(8) Disagree.</b></p>
<p>(1) After considering Aurizon Network's proposed carryover account for the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to update the carryover account to reflect approved capital expenditure for 2012–13 and to account for the deferral of GAPE early-works capital expenditure from 2008–09 to 2011–12 as specified in <b>Error! Reference source not found.</b></p> <p>(3) We propose to smooth the return of over-recovery of the capital indicator from the UT3 across the 2014 DAU period.</p>	<p>26.2</p>	<p><b>(1) and (2) Disagree.</b> Aurizon Network disagrees with the QCA's proposal to reallocate \$30.3 million in FY2012 of capital expenditure from the Newlands system to GAPE and NAPE Deed customers. The QCA also appears to have made some errors that are highlighted in this submission.</p> <p><b>(3) Agree.</b></p>
<p>(1) After considering Aurizon Network's proposed 2013–14 RAB roll-forward, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.</p> <p>(2) The way in which we consider it appropriate that Aurizon Network amend its proposal by amending it to reflect <b>Error! Reference source not found.</b> above.</p>	<p>26.3</p>	<p><b>Disagree.</b> Based on the reasons outlined above, Aurizon Network submits its proposed RAB roll forward for FY2014.</p>

## CDD 26.1 Forecast capital expenditure

### Capital indicator

The QCA rejected Aurizon Network's Capital Indicator in its 2014DAU. The key changes it has made are:

- updating the Capital Indicator for FY2014 approved capital expenditure;

- material deferral of [REDACTED] Wiggins Island Rail Project (WIRP) capital expenditure submitted by Aurizon Network for FY2016;
- capitalising re-railing costs as renewals expenditure from FY2016; and
- calculating Interest During Construction (IDC) using the post-tax nominal vanilla WACC.

#### Changes proposed by Aurizon Network

- The QCA's proposed Capital Indicator for FY2014 needs to be adjusted to reflect the deferral of GAPE Remote Control Signalling (RCS) expenditure. GAPE RCS expenditure of \$11.6million was deferred for pricing purposes until all RCS works in the Newlands system is complete. The table below reflects Aurizon Network's proposed capital indicator with the deferral of GAPE RCS.
- Aurizon Network also proposes a revised WIRP deferral for FY2016. Of the capex allocated to WIRP deferral users a proportion has been identified which is not subject to access conditions. Aurizon Network has estimated this to be approximately [REDACTED]. This results in a revised FY2016 deferral of approximately [REDACTED] for WIRP. (refer Aurizon Network's response to CDD 18.2 on WIRP access conditions)

**Table 26.1 – Aurizon Network's updated Capital Indicator (\$ million, nominal, Start of Year)**

	FY2014	FY2015	FY2016	FY2017	Total UT4
Non –Electric					
Blackwater	100.56	98.45	730.90	77.34	1,007.25
Goonyella	165.27	87.69	95.58	67.90	416.44
Moura	3.69	5.29	70.17	7.61	86.76
Newlands	7.92	4.54	7.00	5.33	24.78
GAPE	6.13	25.86	-	-	31.99
Total Non - Electric	283.57	221.83	903.64	158.18	1,567.22
Electric					
Blackwater	5.11	138.31	75.70	1.95	221.07
Goonyella	15.25	8.80	2.76	2.28	29.09
Total Electric	20.36	147.11	78.46	4.23	250.16
Total Capital	<b>303.94</b>	<b>368.94</b>	<b>982.10</b>	<b>162.40</b>	<b>1,817.39</b>
CDD	<b>315.59</b>	<b>368.94</b>	<b>965.38<sup>220</sup></b>	<b>162.41</b>	<b>1,812.32</b>

Note: Numbers may not sum due to rounding.

Aurizon Network is willing to accept the changes made to QCA's Capital Indicator subject to the following:

- the WIRP revenue deferral extending no later than 30 June 2017 (refer Aurizon Network's response to CDD 18.10);
- the revised WIRP deferral for FY2016

<sup>220</sup> Correction of error in QCA's published table

- the GAPE deferral extending no later than completion of all RCS works in the Newlands system, as incorporated in the table above.

If these are not accepted by the QCA, Aurizon Network does not accept the QCA's proposed Capital Indicator.

### Reporting of asset renewals cost forecasts

Aurizon Network agrees with amendments to report on the requirement for asset renewals. Aurizon Network proposes that this is dealt with through the maintenance forum as outlined in Aurizon Network's response to CDD 5.1

## CDD 26.2 Capital expenditure carryover account

The QCA rejected Aurizon Network's 2014 DAU capital carryover account. The key changes it has made are as follows:

- the QCA has revised the carryover account to also reflect its proposal to reallocate \$30.3 million in FY2012 capital expenditure from the Newlands system to GAPE and NAPE Deed customers. As noted previously, Aurizon Network disagrees with the QCA's proposed allocation and considers this capital should be allocated to the Newlands system (refer response to CDD 17.2);
- The QCA has included capital relating to NAPE in the Capex Carryover for GAPE, which Aurizon Network had deferred
- This would appear to be in error;
- further, if the QCA confirms its rejection of Aurizon Network's end of year modelling approach, the capital carryover balance needs to be converted to mid-year from end of year (refer response to CDD 29).

Aurizon Network has amended the capital carryover to reflect what it considers to be the appropriate treatment as outlined above. This is presented in the following table.

**Table 26.2 – Aurizon Network's updated capital carryover account (\$'000, 2012-13)**

System	Non-Electric	Electric	Total
Blackwater (Incl Rolleston & Minerva)	(8,502)	(28,073)	(36,574)
Goonyella (Incl Hail Creek & Vermont)	(46,773)	(11,929)	(58,702)
Moura	(2,948)		(2,948)
Newlands	996		996
GAPE (Incl GSE)	(11,444)	172	(11,273)
Aurizon Network Response Total	<b>(68,671)</b>	<b>(39,830)</b>	<b>(108,500)</b>
QCA CDD Total	<b>(52,257)</b>	<b>(39,830)</b>	<b>(92,087)</b>

*Note: Numbers may not match with MAR Section 20 due to smoothing of Capital Carryover.*

## CDD 26.3 RAB roll-forward FY2014

The QCA has rejected Aurizon Network's FY2014 RAB roll-forward. The key changes the QCA has made, and Aurizon Network's position on those changes are summarised below:

- reallocated \$30.3 million of capex (initially allocated to the Newlands system in FY2012) to GAPE and NAPE Deed customers: Aurizon Network disagrees with this and remains of the view that this should be allocated to Newlands;
- deferred the depreciation for NAPE (since there is no railing for NAPE forecast for UT4 period), resulting in higher total opening value as at FY2014: Aurizon Network agrees with this;
- applied a 20-year asset life for GAPE (electric): Aurizon Network agrees with this; and
- used UT2 approved lives instead of UT3 : Aurizon Network disagrees with this modelling error.

Aurizon Network's proposed RAB roll forward is presented below.

**Table 26.3 Revised RAB roll-forward proposed by Aurizon Network (\$'000)**

	Opening Asset Value FY2013	Plus FY2014 Capex	Plus Inflation	Less Depreciation	Closing Asset Value FY2014	Disposals and Transfers	Opening Asset Value
Non Electric							
Goonyella	1,315,228	165,271	47,665	80,554	1,447,610	-	1,447,610
Vermont	43,421	-	1,398	2,892	41,927	-	41,927
Blackwater	1,103,347	97,544	38,663	64,342	1,175,211	-	1,175,211
Rolleston	225,339	3,014	7,352	13,570	222,134	-	222,134
Minerva	69,669	-	2,243	3,366	68,546	-	68,546
Moura	251,089	3,689	8,203	10,334	252,647	-	252,647
Newlands	341,364	7,924	16,260	11,225	354,323	-	354,323
GAPE	1,030,865	17,786	38,414	41,697	1,045,368	-	1,045,368
Electric							
Goonyella	227,084	15,250	7,802	21,163	228,974	424	228,551
Vermont	7,883	-	254	525	7,612	-	7,612
GAPE	4,421	-	142	228	4,335	-	4,335
Blackwater	284,040	5,114	9,309	28,492	269,972	272	269,700
Aurizon Network Response Total	<b>4,903,750</b>	<b>315,592</b>	<b>177,705</b>	<b>278,388</b>	<b>5,118,659</b>	<b>696</b>	<b>5,117,963</b>
QCA CDD Total	<b>4,907,025</b>	<b>315,590</b>	<b>178,082</b>	<b>284,498</b>	<b>5,116,200</b>	<b>696</b>	<b>5,115,499</b>
Variance	<b>(3,275)</b>	<b>2</b>	<b>(377)</b>	<b>(6,110)</b>	<b>2,459</b>	<b>0</b>	<b>2,464</b>

Note: Numbers may not sum due to rounding.

## Chapter 27 – Return of Capital

### Summary of Aurizon Network's Position

Aurizon Network is prepared to agree with the QCA's CDD and retain the UT3 approach to depreciation, however intends to revisit the application of the Weighted Average Mine Life depreciation method (the WAML method), along with other potential mechanisms, as part of a broader review of its asset stranding risk.

**Table 27.1 – QCA Consolidated Draft Decision**

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1) After considering Aurizon Network's proposal to determine the depreciation periods in the 2014 DAU, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.	27.1	<b>(1) Disagree.</b> Modelling inconsistency in CDD to be addressed in Final Decision. <b>(2) Agree.</b>
(2) We consider that retaining the UT3 approach to depreciation as per Aurizon Network's December 2014 submission is appropriate. The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to retain the existing depreciation approach, as follows:  (a) A 20-year rolling depreciation approach will be used for assets included in the RAB post 1 July 2009.  (b) Depreciation based on physical asset lives will be used for assets included in the RAB prior to 1 July 2009.		

### CDD 27.1 Return of capital

#### Modelling inconsistencies

Aurizon Network believes the QCA have incorrectly applied the UT2 asset lives when calculating the RAB roll-forward. Aurizon Network's financial modelling reflects the correct UT3 asset lives, where appropriate. This has resulted in the QCA understating depreciation in the CDD. This is the main reason for the variance in Aurizon Network's revised depreciation proposed for UT4.

As mentioned in Aurizon Network's response to CDD section 29.1, the errors identified need to be reflected in the Final Decision. Upon submission of its response to the QCA's CDD, Aurizon Network would welcome the opportunity to discuss these changes with the QCA in more detail.

### UT3 approach to depreciation

Aurizon Network agrees to retain the UT3 approach to depreciation, as outlined in the CDD.

Aurizon Network does not, however, agree with the QCA's statement that the UT3 depreciation approach adequately deals with the level of asset stranding risk.<sup>221</sup> Aurizon Network reiterates its view that the WAML method proposed in the 2014DAU is consistent with the requirements of sections 138 and 168A of the QCA Act. The WAML method applies a consistent depreciation treatment to all assets in the RAB and aligns the recovery of the economic value of its assets to the expected life of users of the declared service.<sup>222</sup>

Aurizon Network considers the QCA's assessment that the WAML method is "biased" in favour of its interests is unreasonable, noting that asset lives for coal network infrastructure in the Hunter Valley has always been based on this approach, which makes inherent sense for sunk investment in a dedicated, single commodity railway for which there is no alternative use. Aurizon Network intends to further investigate its suitability for future regulatory periods as part of its broader review of the mechanisms that it can use to address its asset stranding risk (refer response CDD section 14).

## Summary

While Aurizon Network does not agree with the QCA's rejection of the WAML approach to all assets, it is prepared to accept the QCA's CDD requiring the reinstatement of the UT3 approach to depreciation.

However Aurizon Network proposes that the identified modelling errors be resolved prior to Final Decision.

The table below compares the Return of Capital Building Block under the CDD, to Aurizon Network's revised proposal. Variance driven by modelling inconsistencies in the CDD.

**Table 27.2 – Aurizon Network's revised depreciation (\$million)**

Return of Capital	2013/14	2014/15	2015/16	2016/17	Total UT4
QCA CDD (Dec 15)	273.8	294.5	345.6	354.6	1,268.5
Aurizon Network (Feb 16)	280.7	301.6	353.9	364.3	1,300.5
<b>Variance</b>	<b>6.9</b>	<b>7.1</b>	<b>8.3</b>	<b>9.7</b>	<b>32</b>

*Note: Numbers may not sum due to rounding.*

<sup>221</sup> Queensland Competition Authority (2015d). Consolidated Draft Decision: Aurizon Network 2014 Draft Access Undertaking – Volume IV Maximum Allowable Revenue, p. 181.

<sup>222</sup> Under the 2014DAU, Aurizon Network proposed that the WAML would be reviewed and updated prior to the commencement of each regulatory period, using independent data sourced from Wood Mackenzie.

## Part 28 – Return on Investment

### Summary of Aurizon Network’s position

Return on capital is a major component in the MAR build up. It is estimated that a 1% change in WACC will have a revenue impact of around \$200million for Aurizon Network over the four year regulatory period.

Setting an appropriate WACC over the access arrangement period is essential in order to satisfy the requirements under the QCA Act. It is particularly critical to:

- promoting the primary objective of Part 5 of the QCA Act, namely to promote the economically efficient operation of, and use of, and investment in, significant infrastructure by which services are provided, with the effect of promoting competition in upstream and downstream markets (section 69E);
- having regard to the legitimate business interests of the owner/operator of the service (section 138(2); and,
- allowing the entity to generate expected revenue for the relevant service that is **at least** enough to meet the efficient costs of providing access to the service and include a return on investment commensurate with the regulatory and commercial risks involved (section 168A(a)).

Aurizon Network is disappointed with the unchanged WACC parameters in the QCA’s CDD, despite the strong evidence presented in Aurizon Network’s response to the QCA’s MAR Draft Decision.

However, after consultation with stakeholders, Aurizon Network is prepared to agree the QCA’s proposed WACC to facilitate the timely resolution of the 2014 DAU, despite its impact on Aurizon Network’s incentive to invest in the network. This should not be interpreted as an endorsement of the QCA’s reasoning behind each of the WACC parameters.

In this submission, Aurizon Network has identified the key issues with the QCA’s CDD on WACC. The list is not meant to be exhaustive and these issues will be revisited in more detail in future submissions. Aurizon Network intends to comprehensively set out the methodologies and assumptions underpinning its WACC estimate in the UT5 review and future submissions.

**Table 28.1 – QCA Consolidated Draft Decision**

	QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(7)	After considering Aurizon Network’s indicative estimate of the risk-free rate of 3.15 per cent per annum, our consolidated draft decision is to refuse to approve Aurizon Network’s proposal.	28.1	<b>Agree.</b> However, while Aurizon Network is prepared to accept the QCA’s proposed WACC for UT4, it does not agree with matching the risk-free rate term to the regulatory cycle. This is
(8)	The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to set a risk-free rate of 3.21 per cent per annum.		<ul style="list-style-type: none"> <li>• inconsistent with commercial practice; and</li> <li>• involves the incorrect assumption that the end of period asset value is known with certainty at the start of the regulatory period.</li> </ul>
(1)	After considering Aurizon Network’s proposal for a benchmarked capital structure of 55 per cent debt and 45 per cent equity, our decision is to approve Aurizon Network’s proposal.	28.2	<b>Agree.</b>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
(1) After considering Aurizon Network's proposal for a benchmark BBB+ credit rating, our decision is to approve Aurizon Network's proposal.	28.3	<b>Agree.</b>
(1) After considering Aurizon Network's indicative proposed debt risk premium estimate of 3.28 per cent per annum, our decision is to refuse to approve Aurizon Network's proposal.  (2) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to apply a debt risk premium of 2.72 per cent per annum.	28.4	<b>Agree.</b> However, while Aurizon Network is prepared to accept the QCA's proposed WACC for UT4, the QCA has not revised the DRP estimate upwards given the sample bias identified. Aurizon Network intends to also revisit the use of independent data sources to estimate the debt risk premium in UT5.
(9) After considering Aurizon Network's proposed debt-raising transaction costs of 12.5 basis points per annum, our decision is to refuse to approve Aurizon Network's proposal.  (10) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to set debt-raising transaction costs of 10.8 basis points per annum.	28.5	<b>Agree.</b>
(1) After considering Aurizon Network's proposal in relation to an interest rate swap cost (or, more accurately, the absence of any proposal), our decision is to refuse to approve Aurizon Network's proposal.  (2) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to set the interest rate swap costs at 11.3 basis points per annum.	28.6	<b>Agree.</b>
(1) After considering Aurizon Network's proposed market risk premium of 7.0 per cent per annum, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.  (2) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to set a market risk premium of 6.5 per cent per annum.	28.7	<b>Agree.</b> However, while Aurizon Network is prepared to accept the QCA's proposed WACC for UT4, the QCA has not disclosed the weights afforded to each of the estimation approaches. There are a number of other issues with its approach, including: <ul style="list-style-type: none"> <li>• inconsistent risk-free rate terms;</li> <li>• reliance on the Siegel approach;</li> <li>• lack of consideration of the Wright approach;</li> <li>• incorrect estimates from independent expert reports and the Cornell approach; and</li> <li>• inconsistent conversion between with- and ex-imputation returns.</li> </ul>

QCA's Consolidated Draft Decision	Reference	Aurizon Network's Position
		This results in a MRP that is not commensurate with prevailing market conditions.
(1) After considering Aurizon Network's proposed debt beta of 0.12, our consolidated draft decision is to approve Aurizon Network's proposal.	28.8	<b>Agree.</b>
(1) After considering Aurizon Network's proposed equity beta range of 0.90 to 1.0, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.  (2) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to reflect our estimate of an equity beta of 0.80.	28.9	<b>Agree.</b> However, while Aurizon Network is prepared to accept the QCA's proposed WACC for UT4, it continues to strongly disagree with the comparator companies relied upon by the QCA. The QCA has also not given any consideration to the Black CAPM.
(1) After considering Aurizon Network's proposed gamma of 0.25, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.  (2) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to set a gamma of 0.47.	28.10	<b>Agree.</b> However, while Aurizon Network is prepared to accept the QCA's proposed WACC for UT4, it considers that the he QCA has made a number of errors, including: <ul style="list-style-type: none"> <li>• incorrect definition for distribution rate; and</li> <li>• incorrect interpretation of theta (utilisation rate).</li> </ul>
(1) After considering Aurizon Network's proposed post-tax nominal (vanilla) WACC of 8.18 per cent per annum, our consolidated draft decision is to refuse to approve Aurizon Network's proposal.  (2) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to set a post-tax nominal (vanilla) WACC for the 2014 DAU of 7.17 per cent per annum, incorporating: <ul style="list-style-type: none"> <li>(e) a cost of equity of 8.41 per cent per annum</li> <li>(f) a cost of debt of 6.15 per cent per annum</li> <li>(g) benchmark gearing of 55 per cent.</li> </ul>	28.11	<b>Agree.</b> However, while Aurizon Network is prepared to accept the QCA's proposed WACC for UT4, it does not agree with a number of aspects of the methodologies and assumptions applied by the QCA. Aurizon Network intends to revisit this in detail for the UT5 review.

## Comparison to AER Decisions

The QCA continues to draw parallels between Aurizon Network and regulated energy network businesses. While Aurizon Network strongly refutes the relevance of these businesses as comparators, in its response to the QCA's MAR Draft Decision, Aurizon Network compared the QCA's WACC allowance with the Australian Energy Regulator's (AER's) Draft Decision for the NSW energy businesses (amended

to reflect Aurizon Network's averaging period).<sup>223</sup> This showed that the approach employed by the AER would deliver a post-tax nominal WACC of 8.1% (notably, while applying a lower equity beta of 0.7), compared to the QCA's WACC of 7.17%.

The QCA in the CDD highlights that the difference is due to different methodologies used in deriving the WACC parameters. Aurizon Network understands the methodologies are different. However, this has missed the key point of this comparison, which was that the QCA only allows a WACC of 7.17%, while the AER would have considered an 8.10% WACC appropriate over the same time period. The higher allowance is for a business which the QCA considers has a very similar risk profile to Aurizon Network (even though the AER applies a lower beta, as outlined above). The fact that Aurizon Network has a materially higher risk profile<sup>224</sup> than an energy network business makes this comparison even more stark. The QCA has not addressed this point in the CDD.

In a subsequent March 2015 response to the QCA's MAR Draft Decision on WACC<sup>225</sup>, the QRC also commented on Aurizon Network's comparison to the AER decisions. Aurizon Network does not agree with the QRC's views on this matter.

The QRC considers that the more appropriate comparison is the equity risk premium (ERP). In particular, the QRC compared the QCA's Draft Decision to the latest decisions by the AER, the Australian Competition and Consumer Commission (ACCC) and the Economic Regulation Authority (ERA). Since the QRC submission, the ERA has changed its WACC allowance in the Mid-West and South-West Gas distribution system (which it cited in its submission). The ERA has now allowed an equity beta of 0.7 and a MRP of 7.6%, which results in an ERP of 5.32% relative to 5 year risk-free rate (or 4.82% relative to a 10 year risk-free rate). This is higher than the 4.35% ERP allowed by the QCA.

Nevertheless, the QRC has at least made three errors in its comparison of ERPs, which is that it has assumed that:

- investors calculate Aurizon Network's ERP relative to 4 year risk-free rate;
- the ERP is comparable across time (i.e., not time varying); and
- the ERP is comparable across firms with different risks.

Contrary to the QRC's claim that the ERP is higher for Aurizon Network, the QCA's allowed ERP is actually lower than the AER's decision. The 5.2% ERP allowed by the QCA is with reference to 4 year risk free rate, while the 4.55% ERP allowed by the AER is relative to 10 year risk free rate.

It is unclear why the QRC assumes Aurizon Network's investors calculate their ERPs relative to 4 year risk free rate, while energy networks' investors use a 10 year risk free rate. If this obvious mistake is corrected and the QCA's ERP for Aurizon Network is calculated relative to a 10 year risk free rate, the ERP allowed by the QCA is only 4.35%, lower than 4.55% allowed by the AER. This is extremely difficult to reconcile, particularly given the higher risk that Aurizon Network bears.

Moreover, the ERP is not a constant. Similar to the MRP, it will vary with prevailing market conditions. If the risk is perceived to be higher, the ERP will be higher. This is not dissimilar to the debt risk premium (DRP), which also depends on market conditions. For example, during the global financial crisis, both the DRP and ERP would have been much higher as the uncertainty and risk increased dramatically (noting

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<sup>223</sup> Aurizon Network (2014a). p.167.

<sup>224</sup> Synergies Economic Consulting (2013). Aurizon Network's Commercial and Regulatory Risks.

<sup>225</sup> Queensland Resources Council (2015). QRC Response to Aurizon WACC Submission.

that global financial market conditions still remain highly unstable now as evidenced by the global share market fall in January 2016). Therefore, it is not reasonable to compare ERPs across time without taking into account different market conditions.

Further, as emphasised above, given the different risk profiles of different industries, it is not sensible to make comparisons with decisions made for energy network businesses without any consideration of the underlying risk. As Aurizon Network has reiterated in various submissions<sup>226</sup>, the systematic risk of a single commodity heavy haul railway is much higher than the risk profile of energy networks, water businesses and telecommunication. It would be expected to have higher ERP. On the contrary, Aurizon Network is now provided with a *lower* ERP than the energy network businesses. Recognising that Aurizon Network is competing for capital in the broader infrastructure asset class, this clearly will hinder Aurizon Network's ability to raise capital as investors can achieve a higher return elsewhere on comparatively lower risk investments.

Aurizon Network reiterates its position that the return on equity allowed by the QCA is too low given Aurizon Network's risk profile and the prevailing capital market conditions. It is also lower than the allowance provided by the AER, noting that nearly all aspects of the WACC methodology applied by the AER are currently subject to appeal with the Australian Competition Tribunal.

## CDD 28.1 Risk-free Rate

In the CDD, the QCA has maintained the approach in its MAR Draft Decision, which matches the term of the risk-free rate to the 4-year regulatory period. Aurizon Network does not agree on the term matching of risk-free rate term to the length of the regulatory period, as it is:

- contrary to commercial practice and the approach investors would apply when setting their return expectations over a long time horizon; and
- based on the unrealistic assumption that there is no uncertainty as to the asset value at the end of the regulatory period.

Aurizon Network therefore considers that it will undercompensate its investors, which could have a detrimental impact on its ability to raise capital to fund investment.

As noted above, Aurizon Network is prepared to accept the QCA's decision to facilitate a timely resolution of UT4. However, it intends to revisit its concerns with the QCA's approach in future submissions.

## CDD 28.4 Debt Risk Premium

In Aurizon Network's response to the MAR Draft Decision<sup>227</sup>, it highlighted the bias in the bond sample used by Incenta. In response, Incenta has argued that:

- the results Aurizon Network submitted cannot be replicated;
- the insignificant difference between BBB and BBB+ bonds is due to aberrant bonds identified.

Regarding the first point, Aurizon Network has responded to the QCA's Request for Information (RFI) in July 2015 to clarify the potential difference. Aurizon Network initially used linear interpolation of the risk-free rate to be consistent with the linear regression of the DRP. However, Aurizon Network had recognised that this may not be the most common approach in calculating risk-free rate. Therefore, in the

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<sup>226</sup> For example, Aurizon Network's 2014 DAU submission and its 2014 response to the MAR Draft Decision.

<sup>227</sup> Refer: Aurizon Network (2014). s. 10.3.

RFI Aurizon Network re-estimated the results, which suggests a DRP of 2.81% if the sample bias is accounted for. This is consistent with Incenta's analysis. Aurizon Network is committed to transparency and is not clear why Incenta has not been able to replicate the results after the RFI response.

Aurizon Network does not agree with the removal of the DBCT bonds. Incenta has speculated that the DBCT bonds may be 'tainted' by their downgrade<sup>228</sup> and therefore attract a higher yield than the typical BBB+ bond, without any proof. One could also equally exclude some BBB+ bonds that exhibit 'abnormally' low yields due to other reasons. It is normal to have variation in the yields for bonds with the same credit rating - this is exactly why it is important to maximise the sample size to infer the best estimate. Therefore, Aurizon Network does not agree with modifying the sample without valid reasons.

As shown in Table 91 of the QCA's CDD<sup>229</sup>, the DRP estimate after correcting for sample bias should be 2.81%, being the average of 2.80% (from BBB/BBB+ combined) and 2.82% (from the A- dummy). The estimate of 2.74% from BBB+ only should be disregarded as the number of observations is not sufficiently large (only 18 observations). However, the QCA has not considered it material enough to move the estimate of the DRP, even though the change will have a MAR impact of around \$10million.

As noted above, Aurizon Network is prepared to accept the QCA's DRP decision to facilitate a timely resolution of UT4. Aurizon Network will revisit the most appropriate estimation approach for the DRP in future submissions, including the potential adoption of independent third party data sources, such as the RBA and/or Bloomberg.

## CDD 28.7 Market Risk Premium

In the CDD, the QCA has maintained a MRP of 6.5% from the MAR Draft Decision. The QCA has indicated that it has not found sufficient evidence to change its position, despite strong evidence presented in Aurizon Network's response to MAR Draft Decision<sup>230</sup>. The key issues Aurizon Network has with the QCA's approach include the:

- weights applied to each estimation approach;
- inconsistent risk-free terms used;
- continuing reliance on the Siegel approach;
- lack of consideration given to the Wright approach;
- incorrect estimates from independent expert reports and the Cornell approach; and
- inconsistent conversion between with- and ex-imputation returns.

Aurizon Network intends to review the estimation of the MRP in detail in future submissions.

## CDD 28.9 Equity Beta

In the CDD, the QCA has maintained an asset beta of 0.45 for Aurizon Network, which results in an equity beta of 0.8 using a 55% leverage ratio. This asset beta relies solely on energy and water utilities as comparators.

Aurizon Network believes the QCA has erred in:

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<sup>228</sup> Incenta (2015). Aurizon Network 2014 DAU – response to submissions on WACC, p.27.

<sup>229</sup> Queensland Competition Authority (2015d). p. 211.

<sup>230</sup> Refer: Aurizon Network (2014). s.10.4.

- selecting inappropriate comparators for Aurizon Network; and
- rejecting the application of Black CAPM.

However, after consultation with stakeholders, Aurizon Network is prepared to accept the QCA's beta decision to facilitate the timely resolution of UT4. Aurizon Network intends to further consider these issues, and other matters relevant to the estimation of beta, in future submissions.

## CDD 28.10 Gamma

Gamma is the value of imputation credits and is calculated as the product of the distribution rate and theta (or utilisation rate in QCA's CDD). The QCA in the CDD has maintained its position from the MAR Draft Decision to value imputations credit at 0.47, well above Aurizon Network's preferred estimate of 0.25. Aurizon Network's concerns with the QCA's approach include its:

- incorrect definition of the distribution rate, with its annual report approach;
- unspecified weights applied to each of the utilisation rate estimation approaches; and
- incorrect interpretation of theta (utilisation rate) to be the redemption rate.

The AER and ERA have applied a gamma of 0.40 in recent decisions. Notably, the AER's position is currently subject to challenge by NSW and ACT network businesses, who have submitted that the value of gamma is 0.25. The Australian Competition Tribunal's decision is expected in March 2016.

Although Aurizon Network does not agree with the QCA on the gamma estimate, after consultation with stakeholders, Aurizon Network is prepared to accept the CDD to facilitate a timely resolution of UT4. Having regard to the issues identified above, Aurizon Network intends to review the value of gamma in future submissions.

## Chapter 29 – Approach to Modelling

### Summary of Aurizon Network’s Position

While initially accepting in its Draft Decision on MAR, the QCA now proposes to reject Aurizon Network’s proposed modelling approach. Aurizon Network is disappointed with this decision. Its proposed approach, which was to align with the well-accepted Post Tax Revenue Model (PTRM) applied by the AER, would materially improve transparency and reduce complexity.

The other key implication of this decision is that reverting to a mid-year cashflow timing assumption necessitates the application of a working capital allowance. While the QCA proposes to do this, Aurizon Network has concerns with the transparency of the QCA’s allowance and its applicability to Aurizon Network’s circumstances. However, it has not had the opportunity to give this full consideration and proposes to do this as part of the UT5 review.

Aurizon Network also treats the QCA’s proposal in relation to significant projects that may have a delay in achieving full volumes with caution. While it agrees with this in principle, and notes that consideration is proposed on a case by case basis, it has significant concerns if this could result on an outcome being imposed on Aurizon Network that increases its exposure to asset stranding risk. Network has prioritised a comprehensive review of its exposure to asset stranding risk following the conclusion of the UT4 process.

**Table 29.1 – QCA Consolidated Draft Decision**

QCA’s Consolidated Draft Decision	Reference	Aurizon Network’s Position
(1) After considering Aurizon Network’s proposed modelling approach, our consolidated draft decision is to refuse to approve Aurizon Network’s proposal.	29.1	<b>(2) Agree.</b>  <b>(3) Agree.</b>
(2) The way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to amend the Post Tax Revenue Model to ensure that revenues are adjusted to a mid-year basis and to include a working capital allowance.		<b>(4) Agree in principle.</b> However, any proposal which varies the depreciation profile is to be made by Aurizon Network in its sole discretion.
(3) We consider that commencing depreciation in the year an asset is commissioned as per Aurizon Network’s December 2014 submission is appropriate. Therefore, the way in which we consider it appropriate that Aurizon Network amend its draft access undertaking is to amend the Post Tax Revenue Model to ensure that regulatory depreciation commences in the year in which an asset is commissioned.		
(4) We consider there is merit in a case-by-case consideration of the appropriate depreciation profile for significant projects where there is likely to be a delay between asset commissioning and full volumes being achieved. Such considerations could form part of an expansion tariff pricing proposal.		

## Amendments to the Post Tax Revenue Model

The QCA's CDD 29.1 is to refuse to approve Aurizon Network's proposed approach to modelling. Aurizon Network is required to amend the proposed Post Tax Revenue Model (PTRM) as follows:

- CDD 29.1 (2) requires revenues to be adjusted to a mid-year basis and to include a working capital allowance: Aurizon Network disagrees with the CDD and while it agrees that a working capital allowance is necessary if mid-year timing is to be applied, it disagrees with the way that the QCA has determined its allowance;
- CDD 29.1 (3) requires that that regulatory depreciation commences in the year in which an asset is commissioned: Aurizon Network agrees with the CDD.

Further, in CDD 29.1 (4), the QCA states that it sees merit in a case-by-case consideration (as part of the expansion pricing proposal) of the appropriate depreciation profile for significant projects where there is likely to be a delay between asset commissioning and full volumes being achieved. Aurizon Network is prepared to agree with this but remains concerned with the increasing scope for revenue deferrals, which increases its exposure to asset stranding risk.

The key issues arising from the CDD are summarised below.

### Timing of cash-flow

The AER's PTRM expresses cashflows and MAR in end of year terms. Aurizon Network adopted the AER's PTRM with minimal changes. The QCA proposed to accept this approach in its Draft Decision on MAR<sup>231</sup>, which contained allowable revenues and Reference Tariffs in end of year terms.

Disappointingly, the QCA's CDD 29.1 (2) is inconsistent with its Draft Decision and requires Aurizon Network to discount its cashflows back to mid-year terms. The QCA's analysis states that 'all else being equal', the end of year timing assumption provides a bias in favour of Aurizon Network.<sup>232</sup>

While there could be a bias, it ensures Aurizon Network is compensated for its opportunity cost due to intra-year cash flow differences. This approach aligns with Section 168(A)(a) of the QCA Act.

It is therefore prepared to accept the QCA's proposed allowance for UT4 in the interest of its timely resolution. However, Aurizon Network proposes to review this in more detail as part of the UT5 review.

### QCA's calculation of mid-year cashflows

Aurizon Network notes that the QCA has discounted all cashflows, with the exception of:

- tax depreciation; and
- the UT3 Capital Carryover adjustment.

Aurizon Network contends that if the QCA is minded to retain the mid-year timing assumption in its Final Decision on the 2014DAU, then it must also discount the above cashflows to ensure that the resulting MAR and Reference Tariffs are internally consistent. Failure to do so would mean that the QCA is inappropriately mixing end of year and mid-year cashflows.

The QCA's CDD discounts the regulatory depreciation building block, so there is no reason why tax depreciation should not also be treated on a consistent basis. Similarly, the UT3 Capital Carryover adjustment was originally calculated for consistency with the end of year cashflow assumption. As the

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<sup>231</sup> Queensland Competition Authority (2014a).

<sup>232</sup> Queensland Competition Authority (2015d). p. 273.

QCA's CDD requires MAR to be discounted to reflect a mid-year timing assumption, the UT3 Capital Carryover adjustment should also be discounted to a mid-year value for consistency.

### **Working capital allowance**

To the extent that the QCA wishes to retain a mid-year timing assumption, Aurizon Network agrees with the QCA's CDD to apply a working capital allowance, consistent with previous practice.<sup>233</sup> The issue that remains is the quantum of this allowance, which the QCA proposes to align with the 0.3 per cent applied to Queensland Rail in its October 2015 Draft Decision. In referring to that decision, there is no detail underpinning the derivation of that allowance, which is only referred to in a footnote.<sup>234</sup> In the absence of information underpinning how it has been derived, which is also important in assessing its applicability to Aurizon Network's circumstances, it is not possible to comment on its reasonableness.

Aurizon Network has not had the opportunity to review this issue in detail given the QCA's Draft Decision on MAR proposed to accept its end of year timing. It is therefore prepared to accept the QCA's proposed allowance for UT4 in the interest of a timely resolution. However, it proposes to review this in more detail as part of the UT5 review.

### **Modelling inconsistencies**

Aurizon Network has identified the following errors in the QCA's financial modelling

- in calculating the UT3 capital carryover account balance, the QCA has inadvertently included GAPE capital, which was deferred for pricing purposes and subsequently excluded from the UT3 capital indicator. As a result, no access charges were earned on this capital and it should not be part of the UT3 capital carryover adjustment;
- as noted in its response to CDD 27.1, the QCA has incorrectly applied the UT2 asset lives when calculating the RAB roll-forward instead of UT3 lives. Thereby the QCA have understated Aurizon Network's depreciation in the CDD;
- the QCA has also included capital expenditure incurred in FY2014 relating to GAPE RCS, which Aurizon Network proposed to defer for pricing purposes.

These modelling inconsistencies and errors impact Aurizon Network's MAR. Upon submission of its response to the QCA's CDD, Aurizon Network would welcome the opportunity to discuss these issues with the QCA in more detail and have them resolved prior to Final Decision.

Other modelling adjustments to be resolved prior to Final Decision:

- the QCA has applied incorrect escalation rates to self-insurance allowances;
- Aurizon Network contends that tax depreciation and the UT3 Capital Carryover adjustments also need to be discounted for consistency, as outlined above; and
- Aurizon Network has derived its initial AT<sub>1</sub> Reference Tariffs for FY2014 on the basis of the final maintenance cost index (MCI) for the UT3 period.

As Aurizon Network has not had the opportunity to independently assess the QCA's financial models, this list of inconsistencies should not be deemed complete.

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<sup>233</sup> Queensland Competition Authority (2015d). p.274.

<sup>234</sup> Queensland Competition Authority (2015e). Draft Decision: Queensland Rail's 2015 Draft Access Undertaking, p.157.

### **Revenue smoothing**

Aurizon Network acknowledges the QCA's comments regarding revenue smoothing (or lack thereof). Aurizon Network believes that a degree of revenue smoothing is necessary to deal with, for example, the reconciliation of transitional revenues with the final revenues approved by the QCA for the UT4 regulatory period.

### **Case-by-case consideration of depreciation profile**

In CDD 29.1(4) the QCA states that there is merit in a case-by-case consideration of the appropriate depreciation profile for significant projects where there is likely to be a delay between asset commissioning and full volumes being achieved and that such considerations could form part of an expansion tariff pricing proposal.

Aurizon Network agrees that in certain circumstances, the application of an alternative depreciation profile may have merit. Nevertheless, any proposal which amends a depreciation profile is akin to a revenue deferral and exposes Aurizon Network to potentially significant additional risks and cashflow volatility.

Aurizon Network's particular concern is where any such delays are not consistent with the gradual ramp-up profile that might be typical of a new mine development. The situation with WIRP is a case in point, which has been driven by the material change in market conditions (relative to the environment prevailing when investment commitments were made) and even mine closures. This underlines Aurizon Network's significant exposure to asset stranding risk, which it proposes to comprehensively review.

The QCA must consider the implications of any such proposal in conjunction with the requirements of section 138(2)(b) of the QCA Act. From Aurizon Network's perspective, it is imperative that any such changes are developed by Aurizon Network in its sole discretion. It cannot accept the risk of changes being imposed upon it that will only further exacerbate its exposure to asset stranding risk.

## Glossary

2010AU	2010 Access Undertaking
2014DAU	2014 Draft Access Undertaking
AA	Access Agreement
ABS	Australian Bureau of Statistics
ACCC	Australian Consumer and Competition Commission
AFDs	Access Facilitation Deeds
AER	Australian Energy Regulator
AMP	Asset Management Plan
AN	Aurizon Network
ARTC	Australian Rail Track Corporation
ASX	Australian Stock Exchange
BCR	Baseline Capacity Review
CA	Construction Agreement
CBAs	Condition Based Assessments
CCC	Contribution to Common Cost
CDD	Consolidated Draft Decision
CQCN	Central Queensland Coal Network
CQCR	Central Queensland Coal Region
CQSCM	Central Queensland Supply Chain Model
CTP	Contested Train Path
DAAU	Draft Amending Access Undertaking
DBCT	Dalrymple Bay Coal Terminal
DORC	Depreciated Optimised Replacement Cost
DTP	Daily Train Plan
egtk	Electric Gross Tonne Kilometres
EPA	Expansion Project Agreement
EPM	Engineering and Project Management
EUAA	End User Access Agreement
GAPE	Goonyella to Abbot Point Expansion
gtk	Gross Tonne Kilometres
HPST	Hay Point Services Coal Terminal
HVCN	Hunter Valley Coal Network
IAP	Indicative Access Proposal
IDD	Initial Draft Decision
ILC	Integrated Logistics Centre
ITP	Intermediate Train Plan

IRMP	Interface Risk Management Plan
MAR	Maximum Allowable Revenue
MCI	Maintenance Cost Index
MRC	Minimum Revenue Contribution
MSI	Mine Specific Infrastructure
MTP	Master Train Plan
NAP	Newlands to Abbot Point
NAPE	Newlands to Abbot Point Expansion
NDP	Network Development Plan
NML	Northern Missing Link
NMP	Network Management Principles
NOPP	Network Operations Pathing Planner
NPV	Net Present Value
nt	Net Tonnes
ntk	Net Tonne Kilometres
PIO	Private Infrastructure Owner
QCA	Queensland Competition Authority
QRC	Queensland Resources Council
RAB	Regulatory Asset Base
SCMP	Supply Chain Master Plan
SFA	Study Funding Agreement
SOP	Standard Operating Parameters
SRVC	Short Run Variable Cost
STP	Strategic Train Plan
SUFA	Standard User Funding Agreement
TMDMM	Traffic Management Decision Making Matrix
TOD	Train Operations Deed
TSE	Train Service Entitlement
UHCD	Ultimate Company Holding Deed
WICET	Wiggins Island Coal Export Terminal