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**Pacific National Response to QCA
Consultation Paper: Aurizon Network's
2017 Draft Access Undertaking;
Maintenance Allowance and Practices**

June 2018

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1. Introduction

Pacific National welcomes the opportunity to respond to the Queensland Competition Authority's (QCA) Consultation Paper on Aurizon Network's 2017 Draft Access Undertaking: Maintenance Allowance and Practices (the **Consultation Paper**).

As the QCA is aware in February 2017 Pacific National provided a submission on Aurizon Network's Draft Access Undertaking (**UT5**) and in March 2018 Pacific National provided a submission on the QCA's Draft Decision on UT5 (the **Draft Decision**). In addition, in April 2018 Pacific National provided a response to a QCA Stakeholder Notice which sought information regarding the impact of Aurizon Network's changes to its maintenance practices which were announced in January 2018.

This submission addresses issues raised by the QCA in its Consultation Paper, which seeks further comment on maintenance and operational issues raised by stakeholders in response to QCA's Draft Decision on UT5. In particular, the Consultation Paper seeks comment on an appropriate maintenance allowance for the UT5 period and an appropriate level of accountability if maintenance and operational practices unreasonably disrupt train services.

Of particular importance to Pacific National are the network service levels and performance, and the development of an appropriate incentive mechanism linked to Aurizon Network performance which will drive performance improvements, involve a reduction of costs, and encourage expansion of network capacity.

This Pacific National submission updates and reinforces the positions put forward in our March submission on the Draft Decision.

Pacific National remains concerned about the impact of Aurizon Network's changes to its maintenance practices which were announced in January 2018 and which were addressed in Pacific National's April 2018 submission to the QCA. Pacific National will separately advise the QCA of further information relating to the impact of the current Aurizon Network maintenance practices as they arise.

This submission is public.

2. Appropriate Maintenance Allowance - UT5 Period

The Consultation Paper seeks further comment on determining an appropriate maintenance allowance for the UT5 period for direct maintenance costs, including:

- selection of an appropriate base-year;
- transition from actual costs to efficient costs, while maintaining network service level standards through the inclusion of a network performance incentive and maintenance performance monitoring framework; and
- calculation of non-coal allocations towards network maintenance.

The Consultation Paper (at page iv) indicates that the QCA is:

“... favourably disposed to accepting Aurizon Network's revised claim for direct maintenance costs, subject to it providing sufficient justification and evidence.”

Pacific National's position on maintenance costs is unchanged from that stated in our February 2017 submission (at page 6), namely:

“Pacific National supports maintenance costs levels which are efficient and which ensure safe and efficient train operations on the Aurizon Network at the current contracted capacity.”

Thus, as required by the QCA Act, Aurizon Network should only be permitted to recover efficient maintenance costs. We contend that allowing Aurizon Network to recover its efficient costs will ultimately result in improved outcomes for all supply chain participants. Pacific National would not oppose a revised claim for direct maintenance costs on the coal network if Aurizon Network provides sufficient information to the QCA to allow them to determine that these costs are prudent and efficient.

In particular, Pacific National believes that there should be a continued focus by the QCA on the efficient costs of ballast undercutting. This has been identified as an area for concern in previous access undertakings¹ and also under the current draft access undertaking, as outlined in the Consultation Paper (at page 2).

In relation to those specific areas set out in the Consultation Paper for comment, Pacific National's position is as follows:

¹ See for example the QCA Draft Decision on Aurizon Network 2014 Draft Access Undertaking – Maximum Allowable Revenue September 2014

- **Base year** – Pacific National has no specific concerns with the use of Financial Year 2016-17 as the base year, with any adjustments to the base year costs having to be substantiated by Aurizon Network. In particular, as outlined above the costs of ballast undercutting in this base year should be subject to a continued focus by the QCA.
- **Network service levels and performance** – Pacific National supports the introduction of performance incentives for Aurizon Network². The current regulatory model does not encourage Aurizon Network to efficiently expand existing network capacity as Aurizon Network receives an assured revenue. The regulatory model should ensure Aurizon Network has an incentive to seek improvements in operating and maintenance efficiency to reduce costs and increase capacity. An appropriate incentive mechanism linked to Aurizon Network performance (including maintenance performance) will drive improvement, via both a reduction of costs and an expansion of network capacity.

An incentive mechanism needs to be supported by an effective performance measurement regime. The Consultation Paper (at page 5) has identified that an incentive mechanism should focus on measures of:

- network availability (train path availability and cancellations); and
- network performance (on-time performance, transit time delays and temporary speed restrictions).

Pacific National believes that the availability and capacity performance measures identified in the Consultation Paper are appropriate provided they are transparent and defined in a manner suitable to drive the requisite performance of the infrastructure. Pacific National believes that there should also be performance measures related to cost reduction or productivity improvements.

The performance measures and incentive mechanism should be linked to individual train operators rather than aggregate network performance – this will ensure that differential treatment of operators is not concealed by aggregated performance measures.

In considering the incentive mechanism in the context of the recent Aurizon Network maintenance practices, Pacific National believes that adjustments to the Aurizon Network revenue cap arrangements need to be implemented. These changes include:

² As per February 2017 Pacific National Submission on the Aurizon Network 2016 DAU and March 2018 Submission on the QCA Draft Decision on the Aurizon network 2016 DAU.

- the mechanism should allow the QCA to re-evaluate Aurizon Network's revenue cap to reflect the portion of rail capacity that Aurizon Network actually delivers over a specified timeframe. The revenue cap should be reduced where there is a reduction in system throughput attributable to the act or omissions of Aurizon Network in its operation and maintenance; and
 - the mechanism should ensure that any reduction in rail system throughput as a result of any decisions made by Aurizon Network is not able to be recovered via take or pay provisions, the revenue cap process and the associated revenue adjustment process.
- **Non-coal allocations** – Pacific National believes that non-coal services operating across sections of the Aurizon Network rail infrastructure should only pay their marginal maintenance cost. The Aurizon Network rail infrastructure is primarily a coal network and the costs of the maintenance and operation of that network should be borne by those users conducting coal operations.

The broad drivers of marginal maintenance costs are tonnages and distance travelled, thus gross tonne kilometres (**GTK**) is a reasonable allocator for non-coal train marginal maintenance costs. Before applying such an allocator to the Aurizon Network maintenance costs, these maintenance costs should be adjusted to remove specific maintenance tasks relating to coal transport including ballast undercutting (as ballast undercutting is required due to coal fouling), maintenance related to electric traction infrastructure (which is irrelevant to non-coal trains), maintaining any turnouts specific to coal train activities and any other maintenance tasks driven by the need to maintain track infrastructure for longer and heavier coal trains.

While Pacific National supports these as theoretical allocators it reserves the right to comment further on non-coal access pricing based on these allocations as pricing required to facilitate non-coal train operations is impacted by factors other than Aurizon Network cost allocations.

Overall Pacific National would not oppose Aurizon Network's revised claim for direct maintenance costs on the coal network if Aurizon Network provides sufficient information to the QCA which in turn allows the QCA to determine that these costs are prudent and efficient.

Pacific National believes that an incentive mechanism should be introduced to ensure that maintenance costs are efficient and are incurred in such a way as to ensure network availability and

capacity are maintained and enhanced. Pacific National supports the introduction of such a mechanism as soon as practical.

3. Appropriate Accountability

The Consultation Paper seeks further comment on Aurizon Network's level of accountability if maintenance and operational practices unreasonably disrupt train services, including:

- Aurizon Network's obligations to maintain the network and minimise disruptions to train services;
- reporting requirements needed to assist access holders to identify reasons for disruption to train services;
- the involvement of Aurizon Network's Board with respect to maintenance matters generally;
- the supply chain co-ordination obligations regarding the planning and scheduling of maintenance activities; and
- any adjustments to the materiality threshold that applies to Aurizon Network's revenue-cap arrangements.

Pacific National and other stakeholders have previously submitted to the QCA that greater accountability should be applied to Aurizon Network in relation to its maintenance activities. These submissions have been further driven by the actions of Aurizon Network following publication of the Draft Decision, and Aurizon Network's subsequent decision to revise its approach to maintenance activities.

Pacific National contends that Aurizon Network has contracted to provide access to a certain number of network paths, and should be accountable if these paths cannot be delivered as a result of maintenance and operational practices within the control of Aurizon Network.

In relation to the specific areas the Consultation Paper has called for comment, Pacific National's position is as follows:

- **Obligations to maintain the network and minimise disruptions to train services** – Given Aurizon Network's recent revised approach to maintenance activities under UT4 it appears that undertaking and the current access agreements may not be sufficient to ensure Aurizon Network complies with its obligation to maintain the network and minimise disruption to train services. It is Pacific National's position that the framework in UT5 should be strengthened to ensure there are explicit requirements for Aurizon Network to maintain the network, maintain network capacity and availability, and minimise network disruptions.

Overall there should be more precise obligations placed on Aurizon Network to maintain a safe and efficient rail network that will deliver at least the 'contracted capacity' of the rail infrastructure.

- **Reporting requirements** to assist access holders to identify reasons for disruption to train services - Pacific National believes that reporting obligations should be enhanced such that they include requirements for reporting on maintenance works and their impact on train services. Pacific National supports the proposal set out in the Consultation Paper (at page 9) that Aurizon Network provide a written statement to an access holder adversely affected by the imposition of a constraint explaining the actions Aurizon Network has or is taking to minimise disruptions to train services. The statement should include information such as the reasons why train services were cancelled or not scheduled and whether other paths were available and able to be used by access holders.

Furthermore, it should be clear that take or pay revenue is adjusted where throughput volumes are reduced due to Aurizon Network maintenance or operational constraints (or but for the constraints throughput would have been greater had the maintenance and operational disruption not been advised, planned or executed).

- **Involvement of Aurizon Network's Board** with respect to maintenance matters - Pacific National supports a position that Aurizon Network's board certify compliance with maintenance obligations. In addition, Aurizon Network compliance with its maintenance obligations should be subject to compliance audits.
- **Supply chain co-ordination obligations** regarding the planning and scheduling of maintenance activities – Pacific National believes that supply chain co-ordination and processes, including those outlined in section 7A.3 of UT5 must to be reconsidered.

This UT5 section on supply chain co-ordination needs an increased focus on transparency and accountability in relation to Aurizon Network maintenance activities by and the impact of these activities on other supply chain participants. In particular there should be a focus on aligning possessions and maintenance works to limit the impact on the supply chain.

- **Adjustments to the materiality threshold** that applies to Aurizon Network's revenue-cap arrangements – As outlined above Pacific National believes that adjustments to Aurizon Network's revenue cap arrangements need to be implemented, these include:

- Aurizon Network's revenue cap should be adjusted where there is a reduction in system throughput as a result of the acts or omissions of Aurizon Network in its operation and maintenance of the rail infrastructure; and
- Aurizon Network's revenue cap must account for any reduction in system throughput as a result of any decisions made by Aurizon Network, such that it prevents Aurizon Network from recovering foregone revenue from access holders via take or pay provisions, the revenue cap process and the associated revenue adjustment process.

In addition to the matters raised by the QCA noted above, Pacific National has a particular concern regarding the potential for Aurizon Network maintenance and operational activities to disrupt the services of one train operator more than another train operator. In instances where Aurizon Network's maintenance and operational activities impact the train services offered by its related party train operator less frequently than those trains operated by independent third parties, the level of accountability on Aurizon Network must be greater. Pacific National is seeking that reporting requirements relating to Aurizon Network's maintenance regime report on the impact of the maintenance regime on Aurizon Network's related above rail operator and independent above rail operators independently. This will provide the required level of transparency and therefore accountability for compliance with the requirements of the access undertaking and relevant access agreements.

4. Conclusion

This submission comments on an appropriate maintenance allowance for the UT5 period and an appropriate level of accountability if maintenance and operational practices unreasonably disrupt train services.

Overall Pacific National would not oppose Aurizon Network's revised claim for direct maintenance costs on the coal network if Aurizon Network provides sufficient information to the QCA which then allows the QCA to determine that these costs are prudent and efficient. In doing this Pacific National seeks that there be a focus on the efficient costs of ballast undercutting.

In order to ensure maintenance costs are efficient and network capacity is enhanced Pacific National believes that an incentive mechanism must be introduced.

In relation to the issues of Aurizon Network accountability, Pacific National believes that Aurizon Network has contracted to provide access to a certain number of network paths and should be accountable if these paths cannot be delivered due to maintenance and operational practices within the control of Aurizon Network. Pacific National believes that to ensure this accountability various

parts of UT5 need to be strengthened to ensure that there are explicit obligations on Aurizon Network to maintain the network, maintain network capacity, minimise network disruptions and report on maintenance works.

In addition, Pacific National believes that adjustments to the Aurizon Network revenue cap arrangements need to be implemented, including revenue cap reductions where there is a reduction in system throughput attributable to maintenance and operational practices implemented by Aurizon Network.