Queensland Competition Authority

Draft Decision

Goonyella to Abbot Point Expansion Reference Tariff - Draft Amending Access Undertaking

July 2013

Level 27, 145 Ann Street, Brisbane Q 4000
GPO Box 2257, Brisbane Q 4001
Tel (07) 3222 0555
www.qca.org.au

The Authority wishes to acknowledge the contribution of the following staff to this report:

Paul Bilyk, Emma Green and Natalya Zelenyuk

© Queensland Competition Authority 2013

The Queensland Competition Authority supports and encourages the dissemination and exchange of information. However, copyright protects this document.

The Queensland Competition Authority has no objection to this material being reproduced, made available online or electronically, but only if it is recognised as the owner of the copyright and this material remains unaltered.

SUBMISSIONS

This report is a draft and is subject to revision. Public involvement is an important element of the decision-making processes of the Queensland Competition Authority (the Authority). Therefore submissions are invited from interested parties concerning its assessment of Aurizon Network's Goonyella to Abbot Point Draft Amending Access Undertaking. The Authority will take account of all submissions received.

Written submissions should be sent to the address below. While the Authority does not necessarily require submissions in any particular format, it would be appreciated if two printed copies are provided together with an electronic version on disk (Microsoft Word format) or by electronic mail. Submissions, comments or inquiries regarding this paper should be directed to:

Queensland Competition Authority
GPO Box 2257
Brisbane QLD 4001
Telephone: (07) 3222 0555
Fax: (07) 3222 0599
Email: rail@qca.org.au

The closing date for submissions is **23 August 2013**.

Confidentiality

In the interests of transparency and to promote informed discussion, the Authority would prefer submissions to be made publicly available wherever this is reasonable. However, if a person making a submission does not want that submission to be public, that person should claim confidentiality in respect of the document (or any part of the document). Claims for confidentiality should be clearly noted on the front page of the submission and the relevant sections of the submission should be marked as confidential, so that the remainder of the document can be made publicly available. It would also be appreciated if two copies of each version of these submissions (i.e. the complete version and another excising confidential information) could be provided. Again, it would be appreciated if each version could be provided on disk. Where it is unclear why a submission has been marked “confidential”, the status of the submission will be discussed with the person making the submission.

While the Authority will endeavour to identify and protect material claimed as confidential as well as exempt information and information disclosure of which would be contrary to the public interest (within the meaning of the *Right to Information Act 2009* (RTI)), it cannot guarantee that submissions will not be made publicly available. As stated in section 187 of the *Queensland Competition Authority Act 1997*, the Authority must take all reasonable steps to ensure the information is not disclosed without the person’s consent, provided the Authority believes that disclosure of the information would be likely to damage the person’s commercial activities, and that the disclosure of the information would not be in the public interest. Notwithstanding this, there is a possibility that the Authority may be required to reveal confidential information as a result of a RTI request.

Public access to submissions

Subject to any confidentiality constraints, submissions will be available for public inspection at the Brisbane office of the Authority, or on its website at www.qca.org.au. If you experience any difficulty in gaining access to documents, please contact the office on (07) 3222 0555.

Information about the role and current activities of the Authority, including copies of reports, papers and submissions can also be found on the Authority’s website.

GLOSSARY OF ACRONYMS, TERMS AND CONDITIONS

A	
Anglo	Anglo American
B	
BMA	BHP Billiton Mitsubishi Alliance
C	
CCC	Contribution to Common Costs
CPI	Consumer Price Index
CQCR	Central Queensland Coal Region
G	
GAPE	Goonyella to Abbot Point Expansion
gtks	Gross Tonne Kilometres
M	
mtpa	Million Tonnes Per Annum
N	
NML	Northern Missing Link
nt	Net Tonnes
ntk	Net Tonne Kilometres
Q	
QRC	Queensland Resources Council
R	
RAB	Regulatory Asset Base
RTCA	Rio Tinto Coal Australia
RTI	Request to Information Act 2009
T	
the 2010 undertaking	Aurizon Network's 2010 Access Undertaking
the 2012 GAPE DAAU	Aurizon Network's 2012 GAPE Draft Amending Access Undertaking
the April 2013 GAPE DAAU	Aurizon Network's April 2013 GAPE Draft Amending Access Undertaking
the June 2013 GAPE DAAU	Aurizon Network's June 2013 GAPE Draft Amending Access Undertaking
the 2013 DAU	Aurizon Network's 2013 Draft Access Undertaking
the Act	The Queensland Competition Authority Act (1997)
the Authority	The Queensland Competition Authority

tp	Train Paths
W	
WACC	Weighted Average Cost of Capital

PREAMBLE

This preamble should not be read as a substitute for the detail contained in the body of the draft decision.

Background

On 1 October 2010, the Queensland Competition Authority (the Authority) approved Aurizon Network's 2010 access undertaking (the 2010 undertaking). The 2010 undertaking sets out the terms and conditions under which Aurizon Network provides access to relevant parts of its rail infrastructure, including reference tariffs for train services that operate over the central Queensland coal rail network.

On 19 December 2011, the first train service ran over the newly constructed Goonyella to Abbot Point Expansion (GAPE) infrastructure, including utilising the new link connecting the existing Goonyella and Newlands coal systems (the 'Northern Missing Link').

In September 2012, Aurizon Network lodged its first draft amending access undertaking in relation to the GAPE train services (the 2012 GAPE DAAU). This DAAU sought to introduce a new coal system, and a reference tariff of around $10.73/net tonne (nt), for GAPE train services. It also sought to provide mechanisms for reviewing reference tariffs, if volumes on the GAPE or Newlands systems materially increased, and determining (and recovering) equity raising costs following the commissioning of the GAPE infrastructure (on an ex-post basis).

Aurizon Network revised this DAAU in April 2013 (the April 2013 GAPE DAAU) and then again in June 2013 (the June 2013 GAPE DAAU). The revised proposals sought to expedite the approval process by:

(a) responding to some key concerns raised by stakeholders – including lowering the maintenance costs to $3.4 million over 2011-12 and 2012-13 (from $19.0 million over the same period) given the low volumes railed to date; and

(b) removing content that is no longer considered relevant – given the proximity to the end of the regulatory period and given some matters would be dealt through the approval process for Aurizon Network's 2013 draft access undertaking (the 2013 DAU).

The revisions also included a GAPE transitional tariff of around $6.80/nt that will apply in 2013-14 (given the terminating date of the current access undertaking has been extended to 30 June 2014).

As such, the June 2013 GAPE DAAU included the minimal amendments necessary to give effect to the GAPE reference tariff until the new 2013 undertaking is in place.

Stakeholder Consultation

The Authority has published Aurizon Network's proposals and invited stakeholders to comment on them. The Authority received nine submissions in relation to Aurizon Network's 2012 GAPE DAAU, six in relation to the April 2013 GAPE DAAU and five in relation to the June 2013 GAPE DAAU.

The Authority's Assessment Process

The Authority has considered Aurizon Network's proposal in accordance with the requirements for approving DAAUs set out in section 143 of the *Queensland Competition Authority Act 1997* (the QCA Act).

The Authority's assessment of Aurizon Network's proposal reflects the limited nature of the amendments proposed by Aurizon Network in its June 2013 GAPE DAAU and the circumstances under which it was submitted. That is, parallel to this process, Aurizon Network has submitted the 2013 DAU to the Authority for approval. This contains a new set of proposed arrangements, including reference tariffs for the GAPE train services, to apply (ultimately and upon approval) from 1 July 2013 until 30 June 2017.

Accordingly, the Authority considers it important to recognise that Aurizon Network's removal of matters in the June 2013 GAPE DAAU, including significant matters (e.g. future pricing arrangements and equity raising cost arrangements) that were included in the earlier proposals, may expedite this approval process. Given these matters are far from being resolved, these will have to be considered as part of the 2013 DAU approval process. While this is not an approach that should be adopted as a matter of course, the Authority sees merit in adopting this approach in this instance. Importantly, it will allow a number of key issues to be resolved from a broader perspective, rather than in isolation and in regard to the specific circumstances of the GAPE DAAU proposal (e.g. pricing is a good example of such a matter).

On this basis, the Authority approached this assessment with a view to seek a reasonable solution to give effect to the GAPE train services, pending a more thorough review of the pricing and other arrangements in the 2013 DAU approval process. The Authority notes that Aurizon Network's current claims, and the Authority's consideration of them, should not form the basis for its evaluation of the 2013 DAU, or similar matters, in the future.

Outline of Draft Decision

The Authority's draft decision is to approve Aurizon Network's June 2013 GAPE DAAU.

In arriving at its decision, the Authority considered submissions from interested parties, as well as Aurizon Network's proposal and supporting claims. The Authority also engaged a technical consultant, B&H Strategic Services Pty Ltd, to provide independent advice on technical aspects of Aurizon Network's proposal (i.e. operating and maintenance costs).

In considering this, the Authority focussed on the reasonableness of the costs that Aurizon Network had proposed, including the methodology applied in determining and calculating the proposed revenues and reference tariffs.

Aurizon Network's central proposal is to set a reference tariff of around:

(a) $9.48/nt (as at January 2012) – based on forecast capital expenditure of $984 million and volumes of, on average, 6.2 million tonnes per annum (mtpa) over 2011-12 and 2012-13; and

(b) $6.80/nt (as at July 2013) – based on volumes of 20.6 mtpa in 2013-14.

The Authority notes that stakeholders have raised a number of detailed and legitimate concerns about Aurizon Network's proposal, including concerns about the future pricing arrangements. One particular issue raised was how future users of the GAPE infrastructure will be charged in order to not be unfairly differentiated between foundation and non-foundation customers. Stakeholders also queried whether it was necessary to create an independent coal system for GAPE, rather than using the existing cross-system arrangements contained in the undertaking (see Sections 2.2.2 and 3.1.2).

The Authority has not sought to address future pricing arrangements in this decision. It considers these matters are best addressed as part of the detailed full-scale review that will occur as part of the approval process for the next undertaking.

The Authority is satisfied that Aurizon Network has proposed a reasonable reference tariff for the GAPE train service and has also included other necessary undertaking amendments to recover the tariff revenue.

The Authority's draft decision and reasons are set out in the main body of this draft decision.

Way Forward

The Authority seeks submissions in relation to this draft decision. In developing its final decision, the Authority will consider submissions provided, in addition to the information already provided.

Submissions must be received no later than **23 August 2013**. The Authority will consider any submissions it receives within that time.

Table of Contents

1 BACKGROUND

Aurizon Network has submitted an application to the Authority to amend its approved 2010 access undertaking. The proposed amendments seek to provide for the use of the Goonyella to Abbot Point Expansion (GAPE) by coal train services, including by:

(a) creating a new independent coal system for the GAPE infrastructure;

(b) determining a new reference tariff to apply to the GAPE coal-carrying train services; and

(c) other amendments to the approved 2010 undertaking to give effect to the tariff, including a GAPE revenue cap for 2011-12 and 2012-13.

The Authority has taken into account stakeholders' submissions in making this draft decision. The Authority also had regard to the criteria in assessing amendments to the 2010 undertaking, in the Queensland Competition Authority Act 1997.

The Authority has made a draft decision to approve Aurizon Network's proposal. The Authority has invited stakeholders to comment on this draft decision, and will take into account any submissions it receives by the due date, before making its final decision.

1.1 Declaration of Third Party Access

There are currently four coal systems in the central Queensland coal region (CQCR), namely Blackwater, Goonyella, Moura and Newlands. The use of rail infrastructure managed by Aurizon Network in the CQCR has been declared under Part 5 of the *Queensland Competition Authority Act 1997* (the Act). It is, therefore, subject to the third party access provisions contained in Part 5 of the Act.

While Part 5 of the Act imposes broad obligations on an access provider, it also provides for the development, and the Authority's approval, of an access undertaking.

The approved 2010 undertaking

Aurizon Network's current access undertaking was approved in October 2010 and sets out the terms and conditions under which Aurizon Network will provide access to the parts of its rail infrastructure covered by the undertaking. Among other things, the 2010 undertaking includes reference tariffs for coal-carrying train services that are approved by the Authority.

The reference tariffs consist of a number of parts, including an incremental maintenance charge (AT_1), capacity and allocative components (AT_2-AT_4) and, if required, an electric access tariff (AT_5). The tariffs are derived to allow Aurizon Network to recover the efficient costs of providing network services, including a return on its assets.

When a new coal train service commences, the 2010 undertaking contains arrangements to determine whether that service will pay the reference tariff of an existing system, or whether a new one is required (and what should be included in its calculation).

This 2010 undertaking will be in place until June 2014 (extended by Aurizon Network, with the approval of the Authority, from June 2013) – although, under section 142 of the Act, Aurizon Network can seek to amend an approved undertaking at any time.

In this circumstance, the Authority is required to consider and either approve, or refuse to approve, a Draft Amending Access Undertaking (DAAU) submitted by Aurizon Network.

1.2 The GAPE project

In December 2011, Aurizon Network opened the new $1.2 billion GAPE project. This project consists of a series of works undertaken to bridge the 69 kilometre gap between the Goonyella and Newlands rail systems in order to:

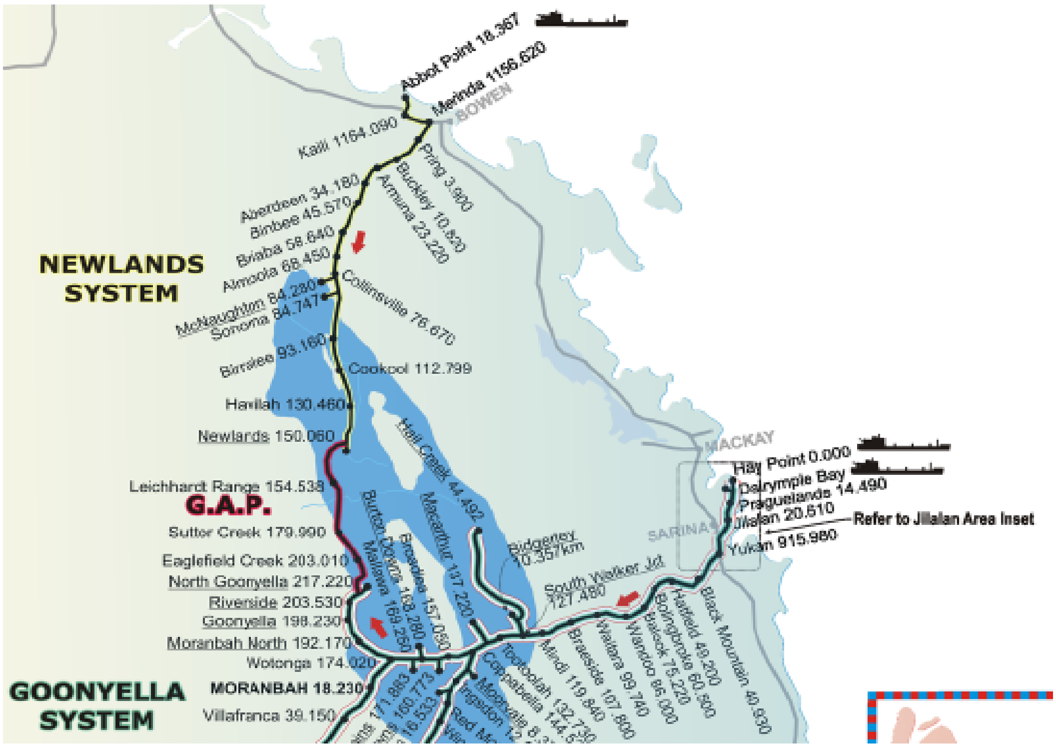
(a) alleviate capacity pressures on the Goonyella rail and port infrastructure; and

(b) utilise the expansion of the Abbot Point Coal Terminal.

The Goonyella and Newlands systems were also upgraded as part of the GAPE project to facilitate the additional GAPE tonnages.

While the tonnes railed to date have been lower than expected, Aurizon Network expects the GAPE project to create an increase on the Newlands system of up to 50 million tonnes per annum (mtpa) to the upgraded Abbot Point Coal Terminal.

Figure 1.1 Map of Goonyella, GAPE and Newlands Systems



1.3 Aurizon Network's GAPE DAAU Proposals

On 10 September 2012, Aurizon Network sought to revise its 2010 undertaking to include a reference tariff for coal traffics on its GAPE infrastructure (i.e. the 2012 GAPE DAAU).

The amendments included creating a new coal system, and reference tariff of $10.73/net tonne (nt), for train services utilising the GAPE infrastructure. While the first train service commenced railing on 19 December 2011, Aurizon Network proposed that the reference tariff apply from 1 January 2012 (when its contracted services were due to commence) until 30 June 2013.

Aurizon Network also proposed a range of other undertaking amendments, which were either:

(a) required to give effect to the new GAPE coal system and reference tariffs, such as those that set out the revenue caps in Schedule F of the undertaking – which allows Aurizon Network to recover revenues associated with the GAPE train services; or

(b) not essential to introduce the GAPE tariff now (e.g. recovery of equity raising costs, review of reference tariffs for volume variations and cost recovery principles for new customers connecting to the new GAPE infrastructure).

The Authority received nine stakeholder submissions that were critical of key aspects of the 2012 GAPE DAAU, in particular, the GAPE tariff was based on estimates of maintenance costs that were more relevant for an aged rather than new asset. This critique was supported by the Authority's own expert review of the proposed cost estimates.

In response, on 12 April 2013, Aurizon Network withdrew its 2012 GAPE DAAU and submitted a new DAAU (i.e. the April 2013 GAPE DAAU) that proposed:

(a) a lower GAPE reference tariff of $9.48/nt in 2011-12 and $9.63/nt in 2012-13 based on:

  (i) revised (lower) maintenance costs of $0.5 million in 2011-12 and $2.9 million in 2012-13 (as against the $10.73/nt tariff based on maintenance costs of $4.1 million and $14.9 million respectively); and

(b) a transitional tariff of $6.80/nt to apply in 2013-14 to GAPE train services – given the extension of the term of the approved 2010 undertaking to 30 June 2014.

Aurizon Network also removed earlier claims that were not necessarily required to give effect to the new GAPE tariff, including those in relation to a volume review and recovery of equity raising costs.

Aurizon Network made these revisions in response to submissions made by stakeholders and also to expedite the approval process. However, it also considered that some matters were best addressed as part of the 2013 draft access undertaking (the 2013 DAU) approval process – i.e. those relating to equity raising costs.

The Authority received six stakeholder submissions that were again critical of the April 2013 GAPE DAAU, this time focusing on the pricing principles for connections to the new GAPE infrastructure.

On 5 June 2013, Aurizon Network withdrew its April 2013 GAPE DAAU and submitted a new one (i.e. the June 2013 GAPE DAAU).

June 2013 GAPE DAAU

Aurizon Network's June 2013 GAPE DAAU proposed the same arrangements for the GAPE coal system and reference tariff, but removed some of its earlier claims – in particular, the provisions that specify how access charges for customers connecting to the new GAPE infrastructure would be determined. It considered these matters would best be addressed as part of the 2013 DAU assessment and approval process.

Specifically, Aurizon Network's June 2013 DAAU proposed:

(a) to create a new coal system for the GAPE infrastructure;

(b) in 2011-12 and 2012-13:

  (a) set the GAPE tariff at $9.48/nt and $9.63/nt respectively;

  (b) a revenue cap of $17.5 million and $91.7 million respectively;

  (c) volume forecasts of 2.0 mtpa and 10.4 mtpa respectively;

(c) in 2013-14, set the GAPE transitional tariff at $6.80/nt; and

(d) consequential amendments to give effect to the GAPE system and reference tariff, including amending the definition of the CQCR to include GAPE infrastructure.

This draft decision focuses on the proposals contained in the June 2013 DAAU, and also takes into account information submitted as part of, and in response to, earlier related proposals.

1.4 Process for considering Aurizon Network's proposal

The Authority has considered Aurizon Network's proposal in accordance with the requirements of the Act and the 2010 undertaking.

The Act requires the Authority to consider a DAAU given to it and either approve, or refuse to approve it. In doing so, the Authority must publish the DAAU, invite and consider comments on it.

The factors affecting the Authority's consideration and approval of a DAAU are set out in the Act. Relevant factors also include the pricing provisions in the 2010 undertaking.

The Act

Section 138(2) of the Act states that the Authority may approve a DAAU only if it considers it appropriate to do so having regard to:

(a) the object of Part 5 of the Act, which is:

> *to promote the economically efficient operation of, use of and investment in, significant infrastructure by which services are provided, with the effect of promoting effective competition in upstream and downstream markets (s. 69E).*

(b) the legitimate business interests of the owner or operator of the service;

(c) the public interest, including the public interest in having competition in markets (whether or not in Australia);

(d) the interests of persons who may seek access to the service;

(e) the effect of excluding existing assets for pricing purposes;

(f) the pricing principles in section 168A of the Act including, among other things, that the price of access to a declared service should:

   (i) 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;

   (ii) allow for multi-part pricing and price discrimination where it aids efficiency;

   (iii) not allow a related access provider to set terms and conditions that discriminate in favour of the downstream operations of the access provider, except to the extent the cost of providing access to other operators is higher; and

   (iv) provide incentives to reduce costs or otherwise improve productivity; and

(g) any other issues the Authority considers relevant.

The 2010 undertaking

The 2010 undertaking contains pricing principles to guide the development of reference tariffs for coal-carrying train services using the declared network (Part 6). In particular, there are requirements that deal with:

(a) developing reference tariffs for new train services, including:

(i) a test to determine if a new train service can enter an existing system (and pay that system's tariff) or whether a new tariff must be determined;

(ii) that a new train service must cover its incremental costs and makes a contribution to the common costs of the coal system it uses;

(iii) that the commencement date of a new reference tariff be the date of the first train service or some other date as approved by the Authority; and

(b) pricing for cross-system services – so that a train service using more than one coal system to travel to the port pays a specified mix of the origin and destination systems' reference tariffs.

1.4.1 Stakeholders' comments

Key issues raised in response to Aurizon Network's 2012 GAPE DAAU

Stakeholders had mixed responses to the general, and more specific, aspects of Aurizon Network's 2012 GAPE DAAU. Most noted that the circumstances surrounding GAPE are unique as most current systems comprise infrastructure that connects loading facilities to unloading facilities, rather than the sharing of infrastructure between systems (QRC, sub no. 6:3). This fact in itself raised concerns of how to deal with aspects of the GAPE proposal (most notably pricing) and whether Aurizon Network's approach is reasonable, or whether an alternative would have been more appropriate.

BHP Billiton Mitsubishi Alliance (BMA) did not consider Aurizon Network's proposal delivered a low cost, efficient option for rail customers, but simply sought to maximise revenues, including not recognising existing synergies in the current Goonyella and Newlands operations. It also considered that the commercial negotiations were conducted in significantly different market conditions and without the regulatory protections to prevent Aurizon Network from seeking above regulated returns (BMA, sub no. 3: 1).

Stakeholders also considered that Aurizon Network should have consulted more in developing its proposal and, if it had, a number of issues could have been resolved (BMA, sub no. 3: 2; QRC, sub no. 6: 9; RTCA, sub no. 7: 5; Xstrata, sub no. 9: 1).

Pricing issues

The Queensland Resources Council (QRC) and Anglo American (Anglo) considered it reasonable to create an independent GAPE system for the purpose of determining the tariffs – which would mean that GAPE users pay all incremental costs associated with the GAPE project (QRC, sub no. 6: 3, Anglo, sub no. 1: 1). The QRC also noted that, while an alternative would have been to use the existing arrangements in the 2010 undertaking (i.e. for cross-system traffics), Aurizon Network's approach was practical and less complex (QRC, sub no. 6: 3).

Nevertheless, the QRC said that Aurizon Network's proposal for new users to pay the incremental costs (private or mainline) plus the GAPE reference tariff would result in a potentially large contribution to common costs. In this regard, it said the Authority should assess the equity of such arrangements, particularly in the context of new users not being parties to the GAPE commercial arrangements (QRC, sub no. 6: 5).

Some stakeholders said that pricing should be done consistently across all systems and were concerned that Aurizon Network has proposed a DAAU, rather than using the existing arrangements set out in the 2010 undertaking (Asciano, sub no. 2: 4; RTCA, sub no. 7: 9; Vale, sub no. 8: 2).

Middlemount was concerned about how future pricing arrangements would affect foundation customers, particularly if expansion costs are 'socialised' in the future and lead to lower reference tariffs (Middlemount, sub no. 4: 1).

BMA said that the Authority should endorse a set of pricing principles to facilitate greater certainty in how new investments will be managed and incorporated into future approved reference tariffs (BMA, sub no. 3: 2). RTCA said it was not clear that the GAPE pricing protected foundation customers from future users 'free riding' on their investment – i.e. it is not clear that future expansions will be socialised with the costs incurred by foundation customers (RTCA, sub no. 7: 3).

Xstrata wanted to ensure that it did not pay higher access tariffs because infrastructure was subsequently built to service GAPE or Newlands to Abbot Point Expansion (NAPE) customers, of which it received no material benefit from (Xstrata, sub no. 9: 3).

Transparency

Stakeholders raised concerns about the transparency of the cost allocators, methodology, variables and assumptions used to calculate the reference tariffs (Anglo, sub no. 1: 2; QRC, sub no. 6: 2; RTCA, sub no. 7: 2). Other concerns were raised in relation to the lack of understanding of the commercial arrangements in the GAPE and NAPE deeds and their associated impacts on Aurizon Network's proposed GAPE arrangements (Anglo, sub no. 1: 2; QRC, sub no. 6: 8; RTCA, sub no. 7: 3).

Cost issues

All stakeholders raised concerns with the level of maintenance costs that Aurizon Network had proposed, saying it appeared high for a greenfield railway operating in its early years at low volumes (Anglo, sub no. 1: 1; BMA, sub no. 3: 4-5; Middlemount, sub no. 4: 1; QCoal, sub no. 5: 2; QRC, sub no. 6: 3; RTCA, sub no. 7: 4, 12).

Others also raised concerns that Aurizon Network included a 'risk premium' in the allowance for operating costs and said it was not possible to determine whether this is the same rate used in existing tariffs, as Aurizon Network has suggested (Anglo, sub no. 1: 1).

Most supported deferring depreciation, rather than charging a 'full cost recovery', at a time when the newly commissioned asset is not fully utilised (QRC, sub no. 6: 2).

Capacity

Stakeholders were keen to understand the capacity effects of the GAPE coal train services, in terms of the overall capacity created and the impacts (if any) on the existing Goonyella and Newlands systems (Anglo, sub no. 1: 2; BMA, sub no. 3: 3-4; RTCA, sub no. 7: 10).

Complex issues

Stakeholders considered that Aurizon Network's proposal to recover equity raising costs raised a number of complex issues, including its link with other issues (such as WACC), is best considered in the development of the next undertaking (Anglo, sub no. 1: 6; Middlemount, sub no. 4: 1; QRC, sub no. 6: 3; RTCA, sub no. 7: 4, 14). Asciano also said that pricing systems and principles are better examined and finalised as part of the approval of the next undertaking (Asciano, sub no. 2: 10).

Middlemount requested the Authority to consider the issue of recognising user contributions – i.e. in the past, mines have had the cost of their spur and balloon loops socialised within the Goonyella or Newlands system assets, whereas it contributed significant private costs and does not receive a discount to the GAPE tariff (Middlemount, sub no. 4: 2).

New comments on the April and June 2013 GAPE DAAU

While some stakeholders did not support Aurizon Network deferring the consideration of important aspects of the GAPE proposal, most did not object to the revisions that Aurizon Network made to its April and June 2013 GAPE DAAUs. On this, Asciano accepted that Aurizon Network had taken into account some of the issues previously raised by stakeholders (Asciano, sub no. 12: 3), but BMA said such revisions undermined the industry's confidence and highlighted that the costs initially proposed for maintenance were an ambit claim (BMA, sub no. 13: 1).

Stakeholders also took the opportunity to reiterate concerns previously raised, including in relation to pricing, transparency and capacity.

A new submission was received from Adani that strongly opposed the pricing approach for new users connecting to GAPE infrastructure. It said it was not consistent with past practices and results in a potentially larger contribution to common costs when compared with the existing pricing arrangements. Also, Adani considered that the proposed tariff should be considered independently of the commercial agreements made and, if socialisation delivers clear benefits to existing users through reduced tariffs, then such an approach would be equitable (Adani, sub no. 10: 1-2).

1.5 Authority's approach

In considering this issue, the Authority has had regard to the assessment criteria in the Act, the provisions of the undertaking, the information provided by Aurizon Network supporting its proposal and stakeholders' submissions. Where approaches differ, the Authority has sought to weigh the arguments and information provided, taking into account the intended purpose of the DAAU – which it considers is ultimately to put in place an appropriate set of arrangements for the new GAPE train services for the remainder of the current regulatory period.

In particular, the Authority has sought to ensure that Aurizon Network’s June 2013 GAPE DAAU:

(a) contains a reference tariff based on:

- (i) reasonable costs, including forecast capital expenditure, operating and maintenance costs;
- (ii) to the extent possible, the methodology used to calculate existing central Queensland reference tariffs;

(b) contains amendments to the 2010 undertaking that are reasonable to give effect to the GAPE train services, including revenue cap and volume estimates based on the proposed reference tariff; and

(c) will provide a suitable set of arrangements for the short term until the arrangements can be further assessed and considered as part of the next undertaking (the 2013 DAU) approval process.

As mentioned earlier, the Authority's draft decision has not sought to address some of the more significant concerns raised by stakeholders at this time. This is largely due to the reduction in the number of matters before the Authority for approval in the June 2013 GAPE DAAU, and also because the Authority is of the view that many of these matters would best be considered in a broader context.

In this regard, the Authority notes Aurizon Network's proposed arrangements for the coming regulatory period (in the 2013 DAU) are on the Authority's website, with submissions on it due by October 2013.

The Authority notes that it has also not sought to obtain the confidential GAPE and NAPE deeds from Aurizon Network at this time. This is because it is not clear that the deeds would be necessary for the Authority to make a decision on this DAAU. On this, the Authority is satisfied that the pricing arrangements proposed by Aurizon Network will only affect (and apply to) GAPE customers (who were already aware of the contents of those deeds). Whether or not Aurizon Network uses the deeds as 'rationale' for aspects of the proposal is a matter for it, but is not something the Authority has considered as relevant in deciding the reasonableness of the proposal. The Authority also found it difficult to see how the deeds would have negative implications for the DAAU, which are not apparent from the information publicly available – particularly given the limited nature of the proposed amendments as part of the June 2013 GAPE DAAU.

The Authority will, therefore, assess this matter on its merits if and when the need arises in the future.

2 COSTS OF THE GAPE SYSTEM

Aurizon Network has proposed a reference tariff for the GAPE train services equivalent to $9.48/nt in 2011-12 and $9.63/nt in 2012-13. This reference tariff allows for the recovery of associated GAPE infrastructure costs of around $39.8 million in 2011-12 and $79.3 million in 2012-13.

The proposed tariff for 2011-12 and 2012-13 is considerably higher than the existing reference tariffs in central Queensland. This is due to:

(a) the significant capital cost of the GAPE infrastructure – at $984 million for 2011-2013;

(b) the low contracted tonnages utilising the infrastructure.

In considering this matter, the Authority has formed the view that the proposed costs for the GAPE tariff are reasonable. Accordingly, the Authority accepts the forecast costs for the GAPE tariff.

2.1 Annual Revenue Requirement

Aurizon Network has developed the GAPE train service reference tariff on the basis of services that utilise the Northern Missing Link (NML) to Abbot Point coal terminal.

The Authority has confirmed that the elements of Aurizon Network's costs (see Table 2.1) have been based on parameters or approaches which the Authority has relied on, in approving the current reference tariffs for central Queensland coal-carrying services, namely:

(a) for the return on capital – a weighted average cost of capital (WACC) rate of 9.96%; and

(b) for inflation – a forecast inflation rate of 2.5% that is consistent with the development of the revenue requirement approved as part of the undertaking.

These aspects will not be discussed further in this draft decision.

The Authority also notes that Aurizon Network has not proposed to recover the following costs from the GAPE train services:

(a) depreciation – it will defer the depreciation of GAPE system capital expenditure until the commencement of the next regulatory period due to low volumes railed through the infrastructure;

(b) tax – this is not applicable due to negative taxable income; and

(c) a contribution to Goonyella and Newlands systems' common costs – as the GAPE tariff is significantly higher than other reference tariffs even without such a contribution.

Table 2.1 GAPE System Annual Revenue Requirement ($ million)

Building Block Components	***2011-12***	***2012-13***
Return on Capital	$46.9	$97.1
Inflation	($11.7)	($24.4)
Depreciation	$0.0	$0.0
O&M (operating and maintenance)	$4.6	$6.6
Tax	$0.0	$0.0
Total Annual Revenue Requirement	**$39.8**	**$79.3**

While stakeholders did not comment on the tax aspect, they did support deferral of the depreciation while GAPE was 'ramping up' tonnes. Some stakeholders did not support the GAPE services making no contribution to the common costs of other systems. This, along with other aspects of Aurizon Network's proposal, including the estimated capital costs and allocation of operating and maintenance costs, is discussed below.

2.2 Estimated Capital Costs

2.2.1 Aurizon Network's Proposal

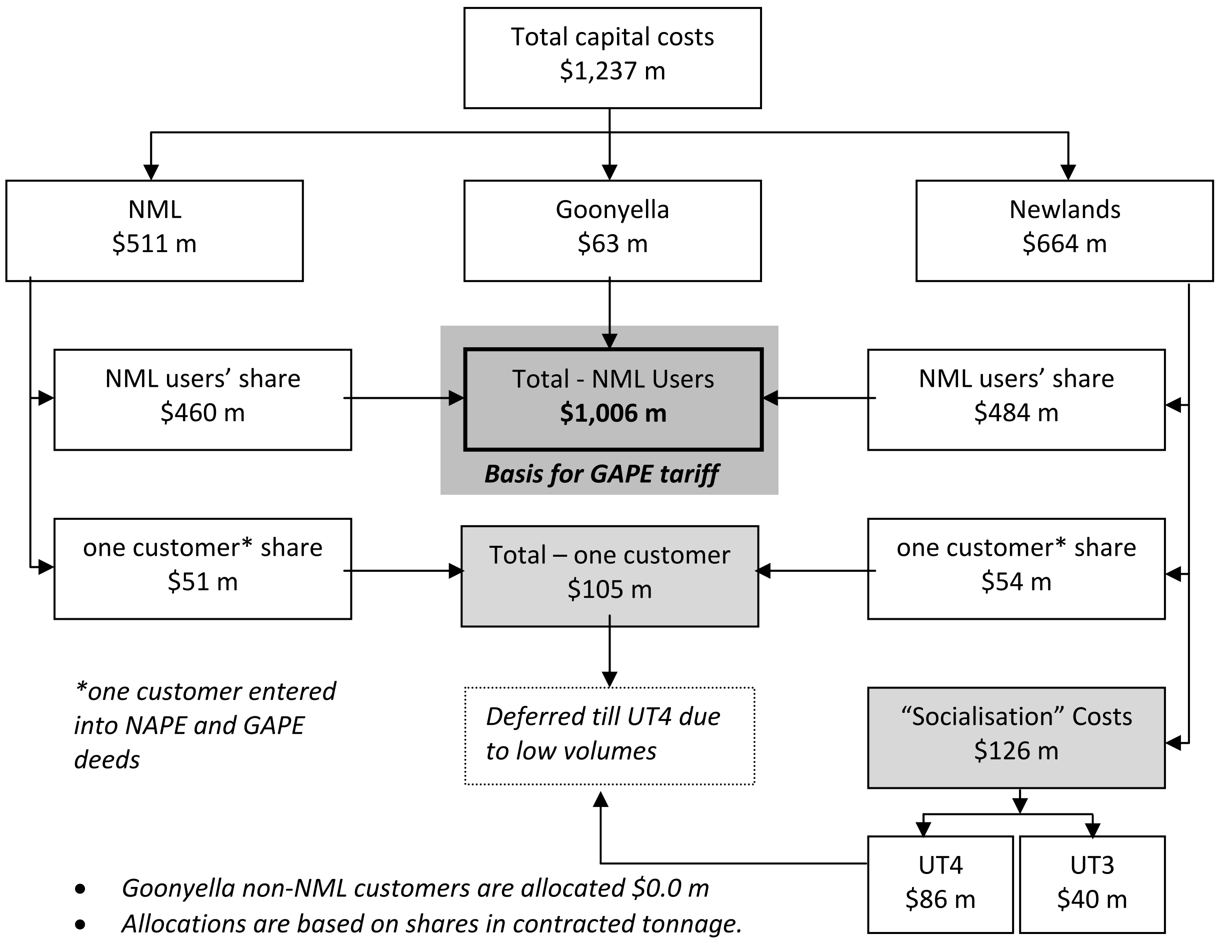
Aurizon Network has proposed a forecast capital expenditure of $1.24 billion for its GAPE infrastructure. As not all aspects of the GAPE project were completed upon the commencement of train services, Aurizon Network has calculated its proposed GAPE reference tariff based on a forecast capital expenditure of:

(a) $984 million in 2011-12 and 2012-13; and

(b) an additional $20 million in 2013-2014.

The forecast expenditure includes construction of the NML and associated infrastructure enhancements in the Goonyella and Newlands systems (reflected in the GAPE reference tariff) (see Figure 2.1).

Figure 2.1 Total GAPE Project Capital Costs and Allocations



Aurizon Network's proposal allocates GAPE capital costs in accordance with customer type to ensure that customers who benefit from the capital works will be the ones who pay for them, in particular:

(a) the usual Goonyella system reference tariff applies to customers located in the Goonyella system and do not utilise the NML. The GAPE project does not affect these customers as far as pricing is concerned. Capital costs for Goonyella infrastructure are allocated to the GAPE costs and are reflected in the GAPE tariff (see (b));

(b) the GAPE reference tariff applies to customers who utilise the NML. These customers will pay the GAPE tariff only (no Goonyella or Newlands systems tariffs). Accordingly, this tariff reflects 90% of capital costs of the NML, 100% of the costs of the Goonyella enhancements (including electric costs associated with additional passing loops) and about 73% of the costs of the Newlands enhancements. The proposed cost allocation is based on the proportion of the new tonnes that is subject to the relevant reference tariff;

(c) a system premium will apply to all the Newlands customers starting in the next regulatory period. 19% of the Newlands system capital expenditure is 'socialised' as part of this expenditure would have been required in the Newlands system even if the GAPE project did not proceed; and

(d) a system premium on top of the Newlands tariff will apply to one customer (who entered into NAPE and GAPE Deeds) starting from the next regulatory period (due to low volumes in the current period). Accordingly, 10% of the NML costs are allocated to this customer based on its contracted tonnages plus 8% of the Newlands system capital costs.

Aurizon Network's June 2013 GAPE DAAU only provides information on GAPE reference tariffs. It does not seek to revise tariffs for the upgrades to the Newlands system.

In terms of recognising capital expenditure, Aurizon Network submitted that, where a new reference tariff is developed, the capital costs can be recognised as either an increase in the value of the regulatory asset base (RAB), or an increase in the value of the Capital Indicator.

As construction costs were not finalised when Aurizon Network prepared the submission, Aurizon Network proposed to establish an independent GAPE system with its own Capital Indicator. Aurizon Network also proposed to reflect the incremental NAPE customer share of capital costs as an increase in the existing Newlands Capital Indicator.

Aurizon Network said that the capital expenditure amounts form part of its 2011-12 capital expenditure claim (which is still being assessed by the Authority) and the 2012-13 capital expenditure amounts has not yet been submitted to the Authority for approval. As such, any variance between the capital indicator and the approved capital expenditure amounts would be reflected in the capital carryover account balance and reflected in future tariffs. This is consistent with the approach applied in the past for establishing other reference tariffs, e.g. the Lake Vermont reference tariff.

2.2.2 Stakeholders' comments

Most stakeholders did not comment on the quantum of the proposed capital expenditure. However, some stakeholders were confused about what the total forecast cost was - for instance, Asciano said:

> *The capital cost of the GAPE is variously referred to as:*
>
> - *$0.942 billion (including interest during construction) on p. 23 of Aurizon Network's submission;*
> - *$1.066 billion (excluding interest during construction); and*
> - *$1.237 billion (including interest during construction) on p. 13 of Aurizon Network's supporting submission.*
>
> *Asciano strongly believes that these differing valuations should be reconciled. (Asciano sub no. 12: 8).*

Stakeholders had mixed views on the proposed capital costs and cost allocation of GAPE infrastructure. For example, the QRC supported Aurizon Network's proposed allocation of costs incurred for GAPE customers and the associated impacts on the Goonyella and Newlands systems. In particular, the QRC noted:

> *Expanding customers (i.e. GAPE customers) effectively pay the full incremental cost of the expansion (including capital and operating cost), such that the tariffs of Goonyella users do not change... Aurizon's proposed approach is consistent with the QRC's preferred approach to pricing...Costs deemed to be incurred for GAPE customers within the Newlands system are allocated to the GAPE system... – QRC view: Support Aurizon's proposed approach (QRC, sub no 14 : 4-5).*

Conversely, Asciano wanted greater clarity on how the capital costs were allocated amongst the GAPE, Goonyella and Newlands systems, and whether the allocation was appropriate or whether there was an inappropriate shifting of costs between systems. Similarly, Anglo questioned the appropriateness of allocating the costs of Goonyella electrification works to the GAPE system (which is a diesel only system).

2.2.3 Authority's Analysis and Draft Decision

Quantum of costs and the capital indicator

The Authority has not sought to assess the quantum of estimated capital expenditure at this time. Aurizon Network has submitted its capital expenditure claim for 2011-12 (in November 2012) which includes the GAPE infrastructure, and this is currently being assessed by the Authority. A separate decision on this matter will be made via another process in due course.

Of interest, Aurizon Network's 2011-12 capital expenditure claims include $1.03 billion of GAPE capital expenditure[1] (which has not yet been approved by the Authority). This relates to the NML and the Newlands system enhancements. While around $68 million of GAPE Goonyella system enhancements (including the Wotonga angle and duplication and the Teviot Brook passing loop) have received pre-approval via the 2010 customer vote process[2], this expenditure has not formed part of any capital expenditure claim to date.

1 This includes interest during construction amounts.

2 See the Authority's approval of regulatory scope for projects in the 2010 Coal Rail Infrastructure Master Plan at http://www.qca.org.au/files/R-QCA-FinalDecision2010CustomerVote-0511.pdf .

The Authority notes Asciano's concerns regarding the exact amount of forecast capital expenditure. This should be made clear from the diagram in Figure 2.1 above, but the Authority notes that:

(a) $0.942 billion (including interest during construction (IDC)) corresponds to the forecast capital expenditure in 2011-12. Another $42 million is forecast in 2012-13 ($984 million in total);

(b) $1.066 billion (excluding IDC) is the total cost forecast for the GAPE project (including the Goonyella and Newlands enhancements) that covers 2011-12, 2012-13 and beyond; and

(c) $1.237 billion (including IDC) is the total cost forecast for the GAPE project (as above), the difference being the interest amount.

In terms of using forecast capital expenditure to determine a tariff, Aurizon Network's approach is consistent with approaches applied to other reference tariff approval processes in the past (i.e. the Vermont reference tariff). Once capital expenditure is approved, Aurizon Network can apply to have future tariffs (and revenues) adjusted for any over or under spending relative to forecast.

Accordingly, the Authority accepts that it is appropriate to use an estimated capital expenditure amount for calculating the reference tariff. Any adjustment that needs to be made to recoup or return revenues in the future will be approved by the Authority.

Capital Expenditure Allocation

The Authority considers that the allocation of forecast capital costs applied by Aurizon Network to determine the GAPE reference tariff is, on balance, appropriate at this time.

Aurizon Network has not proposed any amendment to the Newlands system or Goonyella system reference tariffs. Therefore, the matter of the allocation of GAPE costs to these systems is not something the Authority can assess and approve within this process. To the extent that any reference tariff Aurizon Network proposes in the future includes such an allocation, this will necessarily form part of any future assessment on reference tariff that the Authority makes.

The Authority notes that Aurizon Network has sought to allocate the majority of costs associated with GAPE to GAPE customers in some form. This includes the costs of the NML itself, the Newlands system enhancements and, in the future, Goonyella system enhancements.

This approach is consistent with the *preliminary* principles proposed by the Authority in its April 2013 paper on Capacity Expansion and Access Pricing for Rail and Ports[3]. The key proposition set out in this paper is that:

> *….if average costs are increasing substantially with capacity, a separate access price should normally be calculated and charged to those whose capacity underwrites the new tranche of capacity that reflects the average cost of that new capacity (p. iv).*

This approach ensures that new users do not pay less than the cost their incremental demand causes (and conversely that existing users do not pay more).

However, it is recognised that there are some more complex features of the GAPE proposal that impact on the situation. For instance, even though GAPE train services are non-electric based, Aurizon Network has proposed to include electric costs relating to the Goonyella enhancements (for additional passing loops) to the GAPE costs as it consistent with the 'incremental cost

[3] See the Authority's website for information and to download the paper at http://www.qca.org.au/files/CI-CapExpAccPRP-QCA-PricePaper-0413.pdf.

approach' (Aurizon Network sub: 22). This raises the issue of potential cross-subsidisation, as GAPE customers will be paying for passing loops that they require for the GAPE additional tonnes, and at the same time, pay for electric infrastructure that they do not require, of which can be used by existing electric trains on the Goonyella system. Aurizon Network has not made a case as to why this should be allowed.

At the same time, Aurizon Network has not proposed that GAPE train services contribute to the existing Goonyella and Newlands systems' common costs (see Section 2.4 for further detail). This is at odds with current arrangements where a mine pays the incremental costs of its spur line, but then makes a contribution to the common costs on the system it uses to get to the port.

Taken together, it is not clear that any significant effects come from this arrangement at this time. For instance:

(a) the extent of impact of the electrification costs associated with the passing loops on the GAPE tariff is:

  (i) not certain at this time − it does not form part of the 2011-12 capital expenditure claim currently placed before the Authority;

  (ii) not expected to be significant − given it would presumably be some portion of the forecast $63 million that Aurizon Network has set out in its GAPE submission and which it has received regulatory pre-approval of scope (p. 13);

(b) the extent of any contribution to common costs made by GAPE users would likely:

  (i) have a negligible impact on reducing the tariffs of existing Goonyella and Newlands users − given that the amount is calculated on tonnages, and GAPE tonnages have been low; and

  (ii) have a greater impact on GAPE users given the tariff is already relatively high.

As such, it is not clear that any benefit would be obtained by GAPE users or existing Goonyella and Newlands users by applying an alternative pricing approach at this time (although the Authority notes that it has not, to date, rigorously tested alternative approaches).

Therefore, the Authority considers that the cost allocation approach for calculating the GAPE tariff is acceptable and suits the current circumstances by:

(a) deferring a full cost tariff until the tonnages ramp up, such as key cost components in the GAPE tariff costs (e.g. depreciation); and

(b) excluding other cost components that would make the tariff even higher, including a contribution Goonyella and Newlands systems' common costs.

Accordingly, the Authority's draft decision accepts that this approach is, on balance, reasonable in this instance. This, however, does not imply the Authority's acceptance of such approaches to allocating capital costs or common cost contributions in the future.

2.3 Operating and Maintenance Costs

Aurizon Network's proposed reference tariff recovers operating and maintenance expenditure associated with the GAPE infrastructure.

With regard to the proposed maintenance costs, and as noted in Chapter 1, Aurizon Network significantly reduced its claim between its September 2012 GAPE DAAU and April 2013 GAPE

DAAU. It kept the maintenance claim the same in the June 2013 DAAU. These costs, along with its proposed operating costs, are discussed below.

2.3.1 Aurizon Network's Proposal

Aurizon Network's June 2013 DAAU proposed the following *operating costs* for the GAPE infrastructure:

(a) $4.56 million in 2011-12 made up of:

  (i) $0.77 million for the NML; and

  (ii) $1.91 million and $1.87 million on the Goonyella and Newlands systems respectively; and

(b) $6.57 million in 2012-13 made up of:

  (i) $1.18 million for the NML; and

  (ii) $2.53 million and $2.88 million and on the Goonyella and Newlands systems respectively.

The Authority notes that Aurizon Network's proposed operating costs mainly relate to new staff required to plan, control, manage and administer the new and enhanced infrastructure. In addition, the proposed operating costs include a risk premium allowance consistent with that applied to train services in the CQCR.

Aurizon Network's June 2013 DAAU proposed the following *maintenance costs* for the GAPE infrastructure:

(a) $0.5 million in 2011-12 made up of :

  (i) $0.08 million for the NML;

  (ii) $0.33 million and $0.10 million for additional maintenance required on the Goonyella and Newlands systems respectively;

(b) $2.85 million in 2012-13 made up of:

  (i) $0.48 million for the NML; and

  (ii) $1.79 million and $0.58 million additional maintenance required on the Goonyella and Newlands systems respectively.

Aurizon Network based its maintenance cost estimates mainly on:

(a) estimates of 'actual' maintenance activities related to preventative and inspection works that have taken place on the NML; and

(b) additional GAPE traffic (in gtk) operating in the Newlands and Goonyella systems.

2.3.2 Stakeholders' comments

In terms of operating costs, stakeholders commented on the reasonableness of the risk premium allowance proposed as part of Aurizon Network's proposed operating costs.

In terms of maintenance costs, most stakeholders considered that Aurizon Network's revised (lower) proposed maintenance costs were appropriate given the tonnes railed to date over the GAPE infrastructure were low.

2.3.3 Authority's Analysis and Draft Decision

The Authority has assessed the reasonableness of Aurizon Network's proposed operating and maintenance costs.

In doing so, the Authority has had regard to advice from its technical consultant (B&H Strategic Services Pty Ltd), which also advised the Authority on its earlier assessments of the reasonableness of the operating and maintenance costs of Aurizon Network for the 2010 undertaking.

The Authority has reviewed the 'risk premium' amount included in the proposed operating costs − this relates to the self-insurance cost allowance approved in the 2010 undertaking and which is recovered by all train services in the CQCR via the approved 2010 undertaking operating costs.

The Authority accepts Aurizon Network's approach of basing the GAPE operating cost estimates on data previously assessed by the Authority as part of the approval of the 2010 undertaking, including the risk premium amount. The assessment of the 2010 undertaking's operating costs used bottom-up and benchmark comparisons. In this regard, the Authority notes B&H Strategic Service's view that:

> *The estimates for Operations Costs were soundly based as they are sourced from comparable operations cost data…this is a reasonable approach as the various components of Operating Costs were identified and benchmarked (B&H Strategic Services Report: 2,16)*

The maintenance cost estimates resubmitted by Aurizon Network in April 2013 comprise about 15% to 20% of the original estimates submitted in September 2012. On this, the Authority notes that B&H Strategic Services was of the view that:

> *These estimates fall within a reasonable range for new infrastructure costs and are therefore consistent with reasonable costs (B&H Strategic ServicesReport:2)*

The Authority accepts Aurizon Network's revised approach to forming its maintenance cost estimates and considers it reasonable that the estimates reflect the low actual volumes railed to date and the amount of maintenance activities required as a result.

Accordingly, the Authority's draft decision is to approve Aurizon Network's proposed GAPE operating and maintenance costs for 2011-12 and 2012-13.

2.4 No Common Cost Contribution

2.4.1 Aurizon Network's Proposal

Given the proposed GAPE reference tariff is significantly higher than the reference tariffs in other systems, Aurizon Network has not proposed that GAPE train services pay a contribution to common costs of other systems for the 2010 undertaking period.

2.4.2 Stakeholders' comments

Stakeholders had mixed views on this approach. For instance, Asciano noted that GAPE pricing should be based on a contribution to common costs (Asciano, sub no. 2: 5). The QRC disagreed with Asciano's view − particularly noting that, if the cost of expansion increases the reference tariff in an existing system, then a new reference tariff should apply to the expansion such that existing tariffs are not increased (meaning a zero contribution to common costs would be acceptable) (QRC, sub no. 6: 3-4).

2.4.3 Authority's Analysis and Draft Decision

In considering this matter, the Authority has reviewed Aurizon Network's proposal and stakeholders' comments.

Akin to the current arrangements in the 2010 undertaking for new mines or cross system services, the Authority would normally consider it reasonable for GAPE train services to make a contribution to a system's common costs when utilising it. The additional tonnages over that system can then at least contribute to the overall system costs, thereby reducing the access charges somewhat for existing users.

However, having regard to this, the Authority considers it reasonable, in this instance that GAPE customers only pay their incremental system costs and not make a contribution towards Goonyella and Newlands systems' common costs (also discussed above in section 2.2.3). As it stands, the GAPE tariff is the highest in the CQCR. Making such a contribution would increase the cost burden on GAPE customers, and is unlikely to make a noticeable reduction to the existing Goonyella and Newlands access charges given the low contracted tonnages that GAPE services rail until the end of 2013.

In making this decision, the Authority notes that pricing arrangements concerning all coal systems are currently being considered by the Authority as part of its assessment of Aurizon Network's 2013 DAU. Therefore, the Authority will make a thorough assessment on all aspects of future pricing, for GAPE and other train services, as part of its consideration of that application.

3 ASSESSMENT OF THE GAPE DAAU AMENDMENTS

The GAPE DAAU proposed a number of amendments to the undertaking, including:

(a) creating a new GAPE coal system;

(b) introducing a GAPE reference tariff of $9.48/nt to take effect from 1 January 2012 till 30 June 2012;

(c) a GAPE reference tariff of $9.63/nt applicable in 2012-13;

(d) GAPE revenue cap and volumes estimates; and

(e) a transitional tariff of $6.80/nt applicable in 2013-14.

Aurizon Network also proposed a number of consequential amendments, including updating the CQCR definition to account for the new GAPE infrastructure.

The Authority has reviewed these amendments and believes that these are reasonably required to give effect to the proposed tariff.

Accordingly, the Authority's draft decision is to accept Aurizon Network's proposed reference tariff and consequential amendments.

3.1 GAPE System and Tariff

Schedule F of the 2010 undertaking sets out details for each of the Goonyella, Blackwater, Moura and Newlands systems, including:

(a) the characteristics of the system and the train services that use it, including specifying the reference train characteristics, the loading and unloading points of mines utilising the system;

(b) a reference tariff based on the approved revenue requirement, and a defined tariff structure that comprise:

    (i) cost-reflective tariff components that recover a proportion of the required revenue through:

        (1) a usage-based charge which reflects the incremental operating and maintenance costs, expressed on a per gross tonne kilometre basis (AT_1);

        (2) a capacity charge that covers the incremental cost to the network owner of the capacity, expressed per train path (AT_2); and

        (3) allocative components that equally recover the remainder of the required revenue through:

            (A) a per net tonne kilometre charge (AT_3); and

            (B) a per net tonne charge (AT_4).

The 2010 undertaking also contains pricing principles that describe the charging arrangements that will apply to train services that use the infrastructure of more than one coal system on their journey to the port (i.e. cross system pricing principles – in cl. 4, Part B of Schedule F).

In addition, the 2010 undertaking provides for Aurizon Network to propose, and the Authority to approve, reference tariffs for new coal carrying train services. A new train service must pay the higher of:

(a) its incremental costs plus a contribution to common costs at the rate specified in the 2010 undertaking; or

(b) the tariff of an existing coal system.

3.1.1 Aurizon Network's Proposal

Aurizon Network considered that the current undertaking arrangements did not adequately address the circumstances where a material amount of cross-system services apply (such as those which originate in Goonyella and arrive in Newlands).

Therefore, Aurizon Network proposed that the GAPE assets form a new coal system for the purpose of pricing.

As a consequence, Aurizon Network proposed to amend the 2010 undertaking to:

(a) include a new section containing the details of the GAPE system and train services, including the description of the reference train (cl. 9, Part B, Schedule F);

(b) explicitly exclude the GAPE train services from being subject to the cross system pricing principles (that are in cl. 4, Part B, Schedule F); and

(c) amend the CQCR definition to include GAPE train services and infrastructure (Part 12).

The GAPE reference tariff has been determined in accordance with the defined tariff structure set out in the 2010 undertaking (see Table 3.1).

Table 3.1 Aurizon Network's Proposed GAPE Tariff

Reference Tariff Component	*2011-12*	*2012-13*
AT1	$1.29	$1.33
AT2	$11,949.82	$12,248.57
AT3	$1.71	$1.75
AT4	$4.45	$4.56
AT1-4 average $/nt	**$9.48**	**$9.63**

Aurizon Network did not propose any change to the Goonyella and Newlands system tariffs.

Aurizon Network has sought to backdate the reference tariff to 1 January 2012. This corresponds to the date that contracted train service entitlements commenced.

3.1.2 Stakeholder Comments

Stakeholders were seeking clarity on whether the GAPE was intended to be a stand-alone system and, if so, a stand-alone system for all purposes or only the purposes of reference tariff pricing (Asciano, sub no 12: 6). Anglo American noted that the question of socialising or incremental pricing approaches should be assessed on a case-by-case basis (Anglo, sub no. 11:1).

QRC noted in this respect that:

> *Aurizon's proposal to establish the GAPE assets as a new system within the Central Queensland coal region for the purposes of pricing (rather than to include these assets within existing system) appears a reasonable approach to achieving certain pricing outcomes. (QRC, sub no 14: 2).*

3.1.3 Authority's Analysis and Draft Decision

In reviewing Aurizon Network's proposed tariff for the GAPE train services, the Authority was able to establish that:

(a) the proposed reference tariff will recoup the proposed GAPE system costs;

(b) the GAPE tariff has a structure consistent with other tariffs, including having a:

(i) set AT_1 and AT_2 tariff component; and

(ii) AT_3 and AT_4 tariff components calculated in a manner, consistent with other central Queensland coal reference tariffs, to recoup the remainder of the costs not recovered via the AT_1 and AT_2 tariffs.

Nevertheless, the proposed GAPE tariff of $9.63/nt will be the highest tariff in central Queensland. The key drivers of the relatively high proposed GAPE tariff are the recovery of the capital expenditure from GAPE customers only and the low ramp-up tonnes.

In these circumstances, the Authority considers it reasonable that a separate GAPE system and tariff be developed. This tariff is largely based on the incremental costs of the GAPE infrastructure, and avoids the sharing of GAPE costs with other users that do not use or benefit from the GAPE infrastructure. Such an approach is consistent with the Authority's current view on how best to price for capital expansions in rail and ports[4].

Given the range of alternatives and the length of time remaining for the GAPE tariff to apply, the Authority considers that the reference tariff proposed by Aurizon Network is reasonable.

As far as the commencement date for the proposed new tariff is concerned, the provisions of the 2010 undertaking allow Aurizon Network to backdate the proposed tariff to the commencement of the relevant train services. Given this, the Authority accepts the proposed commencement date of 1 January 2012.

3.2 GAPE Revenue Cap and Volume Estimates

Schedule F of the 2010 undertaking sets out details for each of the Goonyella, Blackwater, Moura and Newlands systems, including:

(a) the revenue Aurizon Network is allowed to recover (system allowable revenue); and

(b) the volumes used to calculate it.

3.2.1 Aurizon Network Proposal

Based on the introduction of the GAPE as a new coal system and the commencement of the GAPE train service, the GAPE DAAU includes a proposal to include the GAPE systems:

(a) system allowable revenues of: $17.5 million in 2011-12 and $91.7 million in 2012-13; and

(b) volume forecasts of:

(i) in 2011-12 – 2.0 mtpa (or 1,294,098 gross tonne kilometres ('000 gtks)); and

(ii) in 2012-13 – 10.4 mtpa (or 6,288,019 ('000 gtks)).

[4] See the Authority's discussion paper on *Capacity Expansion and Access Pricing for Rail and Ports* (April 2013) at http://www.qca.org.au/cross-industry/PricingPapers/.

With regard to the volumes, Aurizon Network said that it converted contracted train path entitlements into nominal net tonne forecasts and noted that the volumes fell short of the contracted volumes at full utilisation – as such, the remainder of the regulatory period covered by the 2010 undertaking is considered to be part of the 'ramp-up' period.

3.2.2 Stakeholder Comments

Stakeholders commented that the volume forecasts adopted by Aurizon Network for GAPE appeared high and were considerably more than what is actually expected to be railed (QRC, sub no. 14: 7).

3.2.3 Authority's Analysis and Draft Decision

The Authority has reviewed Aurizon Network's proposed allowable revenues and was able to verify that they are based on the GAPE costs (discussed in Chapter 2).

The forecast volumes proposed by Aurizon Network are significantly lower than the capacity associated with GAPE infrastructure, reflecting the fact that mines are ramping up production and train services in this early period following the commissioning of the GAPE infrastructure. Indeed, this is not unexpected and the volume forecasts are based on the contracted volumes associated with GAPE train services. Therefore, the Authority considers that Aurizon Network's forecasts are reasonable under these circumstances.

It is noted that the actual volumes railed in the GAPE system in 2011-12 and 2012-13 were significantly lower than the forecast. For instance, using the January to March 2013 quarter actual railings as a guide[5], one may expect tonnes in the area of around 3.1 mtpa in 2012-13 (i.e. 0.8 mtpa extrapolated for the remaining quarters in the year). As such, using contracted volumes to calculate the reference tariffs is likely to result in Aurizon Network being worse off in the short term. However, these revenues will eventually be recouped via the revenue cap unders- and overs- mechanism.

Accordingly, the Authority proposes to accept the GAPE system allowable revenues and volumes as set out in the June 2013 GAPE DAAU.

3.3 Consequential Amendments

Aurizon Network has made a number of consequential amendments to parts of the 2010 undertaking to account for the inclusion of GAPE system within the CQCR and for the operation of GAPE train services.

The Authority has reviewed these proposed amendments and believes that they are reasonable and necessary to give effect to the GAPE reference tariff. For example, the June 2013 GAPE DAAU proposed:

(a) that GAPE traffics not be subject to the rules governing cross-system pricing; and

(b) to include a definition for the GAPE system in the CQCR (which now includes GAPE) and, for consistency, include definitions for each of the other coal systems.

In Chapter 2 of this draft decision, the Authority discussed, and accepted, the rationale for GAPE traffic to not contribute to Goonyella and Newlands systems' common costs. The Authority also has accepted the proposal that a separate GAPE system be developed. These proposed amendments to the 2010 undertaking simply seek to give effect to, and are consistent with,

[5] Information from Aurizon Network's published quarterly report on its website.

these principles. The Authority therefore considers these amendments to the 2010 undertaking appropriate.

In making this decision, the Authority notes that stakeholders had observed that the definition of the Goonyella to Abbot Point System is drafted so that there are overlaps with the definitions of the Goonyella and Newlands systems. This is unavoidable given the inter-related nature of the infrastructure and train operations across the three systems (e.g. a GAPE duplication in the Goonyella system will be used by both GAPE and Goonyella traffic). It will, however, be necessary for the Authority to ensure that, in assessing future tariff applications, this does not result in any double-counting of the costs of operating such infrastructure.

3.4 Transitional Tariff

As Aurizon Network's 2010 undertaking was due to terminate on 30 June 2013, Aurizon Network submitted a DAAU to the Authority to extend the terminating date to 30 June 2014. This DAAU was approved by the Authority on 31 May 2013.

Given the above, Aurizon Network has proposed a transitional reference tariff for the GAPE system (i.e. 2013-14). Aurizon Network said that the process for determining a transitional tariff for the GAPE system should be different from the other CQCR systems due to the anticipated ramp-up in volumes. As such, escalating all tariff components at CPI would likely result in over-recovery of revenue from customers. Accordingly, Aurizon Network has proposed to:

(a) escalate AT_1, AT_2 and AT_3 components by forecast CPI;

(b) adjust the AT_4 tariff downwards to reflect the increase in the GAPE system volumes;

(c) commence the GAPE assets' depreciation; and

(d) include the capital related to the one Newlands GAPE customer.

This results in a proposed reference tariff of around $6.80/nt for GAPE train services in 2013-14.

The Authority notes that the GAPE tariff is significantly lower than that proposed for 2011-12 and 2012-13. This is explained by the fact that, while Aurizon Network has included depreciation for the GAPE assets in the 2013-14 cost build-up (which increases costs), this effect is offset by Aurizon Network's higher forecast volumes.

Stakeholders requested the Authority to assess the reasonableness of the transitional volumes, which were forecasted to be 20.6 mtpa for 2013-14 and were based on the contracted tonnages. The Authority has not sought independent advice on the volume estimate, mainly because all aspects of the 2013-14 GAPE tariff will be reviewed as part of the Authority's assessment of the 2013 DAU. It will also be the subject of the same unders- and overs-mechanism that would apply to other coal tariffs in central Queensland. As a result, while a volume forecast that is too high may have an adverse impact on Aurizon Network's cash flows in 2013-14, this will be subsequently rectified in a Net Present Value (NPV) neutral manner.

The Authority therefore accepts that Aurizon Network's proposed approach to calculate the 2013-14 GAPE transitional reference tariff is reasonable and, for the most part, is consistent with the approach applied to the 2013-14 transitional tariffs for other coal systems in the CQCR.

APPENDIX A: SUBMISSIONS RECEIVED

Submissions on GAPE 2012 DAAU

(1) Anglo American (Anglo) (Nov 2012)

(2) Asciano (Nov 2012)

(3) BHP Billiton Mitsubishi Alliance (BMA) (Nov 2012)

(4) Middlemount Coal (Middlemount) (Nov 2012)

(5) QCoal (Nov 2012)

(6) Queensland Resources Council (QRC) (Nov 2012)

(7) Rio Tinto Coal Australia (RTCA) (Nov 2012)

(8) Vale (Nov 2012)

(9) Xstrata Coal (Xstrata) (Nov 2012)

Submissions on April 2013 GAPE DAAU

(10) Adani Mining (Adani) (May 2013)

(11) Anglo (May 2013)

(12) Asciano (May 2013)

(13) BMA (May 2013)

(14) QRC (May 2013)

(15) RTCA (May 2013)

Submissions on June 2013 GAPE DAAU

(16) Anglo (Jun 2013)

(17) Asciano (Jun 2013)

(18) BMA (Jun 2013)

(19) QRC (Jun 2013)

(20) Vale (Jun 2013)