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Dr Malcolm Roberts
Chairman
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14 June 2013

Dear Dr Roberts,

QCA's proposed alternative SAAs and consequential amendments

Aurizon welcomes the opportunity to provide a further submission on the QCA's proposed Alternative Standard Access Agreements (**SAAs**) and the consequential amendments to Aurizon Network's 2010 Access Undertaking (**2010AU**).

Aurizon has consistently supported the development of alternative (or split) standard agreements. It is desirable that the standard, 'safe harbour' contracts provide access seekers with a range of fallback options, so that operators are able to negotiate service offerings in the above rail market that are of commercial value to end users. It is equally important that operators, end users and Aurizon Network are able to depart from the SAAs where they voluntarily agree to do so through commercial negotiations.

Aurizon has previously provided two submissions to the QCA on Aurizon Network's original proposal; one in September 2011 and the other on the QCA's Draft Decision in October 2012. As made clear in the October 2012 submission, Aurizon is supportive of the QCA's assessment criteria, and agrees that it is appropriate to ensure consistency between the existing standard agreements and the approved alternative form.

1. Overview

With one material exception, Aurizon is generally supportive of the QCA's final decision, and of the QCA's proposed alternative SAAs.

The material exception is the inclusion of the new clause 4.5.3 (d) of the 2010AU that states:

> *"Aurizon Network must not enter a TOA Access Agreement that relates to utilising Access Rights contracted under more than one EU Access Agreement"*.

The effect of this clause is to mandate the structure for some classes of access agreements. If approved, cl 4.5.3(d) will prevent operators from negotiating with end users and Aurizon Network for any alternative contract structure from that approved by the QCA, as to do so would result in Aurizon Network breaching its access undertaking.

The rationale in the final decision for this clause is as follows:[1]

(a) mandating a contract structure is important to give parties certainty and create a transparent standard suite of arrangements available to commence negotiations;

(b) each EUAA being linked to separate TOAs is important to transparently remove cross-default risk, while continuing to retain other benefits, such as pooling and having the ability to suit TOAs to individual end user requirements; and

(c) that the Authority is not convinced that the contracting structure will be highly administrative and costly as the original TOA can be replicated in subsequent TOAs.

Aurizon believes that a mandatory contract structure is inconsistent with the purpose of the SAAs and possibly with the QCA Act itself. SAAs are intended to apply only where Aurizon Network and access seekers fail to reach an agreement, consistent with the 'negotiate-arbitrate' model. The inclusion therefore of a mandatory contracting structure is, in Aurizon's view, inappropriately restrictive, appears to exceed the QCA's powers under the legislation, and will materially impact on the commercial flexibility of operators to manage risk and ultimately compete through the provision of different service offerings.

In particular, Aurizon believes that the inclusion of clause 4.5.3(d) in the 2010AU:

a) may be contradictory to the provisions of the QCA Act, in particular those clauses that give effect to the negotiate-arbitrate model;

b) has not been demonstrated as compliant with s 138(2) of the QCA Act, particularly, s 138(2)(a) – the objects of Part 5 of the QCA Act, access to services;

c) is contrary to the provisions in cl 5.2(n)(iii) of the 2010AU, namely that any consequential amendments to the undertaking do not alter the scope and nature of the undertaking;

d) is contrary to the QCA's stated assessment criteria, namely that the only amendments are to give effect to the split form of agreements; and

e) did not give reasonable and due consideration to the issues raised by Aurizon in response to the Draft Decision.

Each of these points are discussed further below.

2. Contrary to the negotiate-arbitrate model

There is a question as to whether the QCA has a statutory power to compel access seekers to accept a mandatory contract structure, other than in limited circumstances (e.g. to preclude a contravention of s 125 – the prohibition on preventing or hindering access).

In particular, it is notable that:

- s 99 provides a statutory obligation on access providers (and corresponding right for access seekers) to *negotiate* access agreements; and

- s 101 provides a statutory obligation on access providers (and corresponding right for access seekers) to make reasonable efforts to satisfy the reasonable requirements of access seekers.

[1] Queensland Competition Authority, Final Decision Aurizon Network Alternative Standard Access Agreements, April 2013, page 11.

The effect of cl 4.5.3(d) is contrary to these provisions, in that it will remove Aurizon Network's obligation (and undermine the corresponding right of the access seeker) to negotiate an access agreement that reasonably reflects the requirements of an access seeker. In particular, if approved, cl 4.5.3(d) will prevent Aurizon Network from complying with s 101 where an access seeker reasonably requires one TOA agreement for multiple end user access rights, and Aurizon Network has no reasonable basis to refuse.

Of further note, it is unclear which element of s 137[2] would support the QCA's inclusion in the access undertaking of a provision that prevents Aurizon Network and an access seeker from commercially (and voluntarily) agreeing a certain contract structure. The final decision itself does not identify the provision on which the QCA relies.

In the certification of the Queensland Rail Access Regime[3], it was noted by the National Competition Council that clauses 6(4)(a)-(c) of the Competition Principles Agreement *"requires that an effective access regime allows parties to try to reach mutually beneficial agreements through commercial agreement"*[4] and *"seek to ensure regulatory measures can provide an incentive to reach commercially agreed outcomes but also required that an effective regime provides a means for dealing with situations where access providers and access seekers are unable to reach agreement"*[5].

As part of the certification process, ss 99, 100, 101, and 112 of the QCA Act were described as the key legislative provisions giving effect to a negotiate - arbitrate model together with clause 5.1(d) of the 2010AU which acknowledges *"that the standard access agreement approved by the QCA applies 'unless otherwise agreed between QR Network and the Access Seeker"*[6].

3. Compliance with the objects clause

The final decision does not substantiate that a mandatory contracting structure promotes the object of the QCA Act, as required under s 138(2)(a). In particular, the final decision does not demonstrate that mandating that operators accept a certain contracting structure will promote competition in upstream and downstream markets.

In giving consideration to the competition effects, the final decision refers only to the ability of the alternate standard access agreements to *"give end users greater flexibility in managing their access rights*" and thereby increase competition in both the above – rail market and the overall competitiveness of the Queensland coal industry[7]. Aurizon agrees with the QCA that the ability for end users to contract under the form of the split agreements promotes above rail competition. However, a short note that split agreements will promote competition is not a reasonable basis for concluding that a mandatory contracting structure promotes competition.

In its September 2011 and October 2012 submissions, Aurizon argued that the regulatory arrangements should seek to provide the flexibility for end users, operators and Aurizon Network to commercially negotiate access arrangements. In particular, it was noted that the contracting framework must be sufficiently flexible to ensure that above rail operators are able to create value for end users by service differentiation and innovation.[8]

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2 Section 137 of the QCA Act outlines the contents of access undertakings

3 National Competition Council, Queensland Rail Access Regime Application for certification under s 44M of the Trade Practices Act 1974, Draft Recommendation, 14 September 2010, page 31.

4 National Competition Council, Queensland Rail Access Regime Application for certification under s 44M of the Trade Practices Act 1974, Draft Recommendation, 14 September 2010, page 30, clause 5.33

5 National Competition Council, Queensland Rail Access Regime Application for certification under s 44M of the Trade Practices Act 1974, Draft Recommendation, 14 September 2010, page 30, clause 5.33

6 National Competition Council, Queensland Rail Access Regime Application for certification under s 44M of the Trade Practices Act 1974, Draft Recommendation, 14 September 2010, page 31, clause 5.41, the NCC referred to the similar provision in both UT2 and UT3.

7 Final Decision, page 6

8 QR National, Submission on Draft Decision on QR Network's proposed Alternate Standard Access Agreement, 30 October 2012, page 7.

For example, the issue that the final decision cites as problematic (cross default risk under a single TOA), is in fact an issue that can be managed by competition – not by a mandatory contracting structure. As noted in Aurizon's earlier submission, the amalgamation of a number of end user access rights in one TOA actually reduces the risk to the end user that the access rights will be terminated[9], thereby allowing operators to leverage scale and scope economies.

This element of service differentiation is an essential component of a competitive (and dynamically efficient) market. By prohibiting this sort of innovation, a mandatory contracting structure seems more likely to lessen competition than promote it.

4. The QCA's compliance with its powers under the 2010AU

In determining the assessment criteria in relation to the alternate SAAs, the QCA has noted the requirement for any amendments to the undertaking to comply with cl 5.2(n) of the 2010AU, in particular, cl 5.2(n)(iii), namely that any consequential amendments to the undertaking required by the alternate SAAs do not alter the scope and nature of the undertaking[10].

Aurizon considers that the inclusion of cl 4.5.3(d) has altered the nature of the 2010AU. In the 2010AU (and indeed, in the proposed 2013 Draft Access Undertaking), SAAs are simply the 'safety net' for commercial negotiations. It is beyond doubt that parties may, consistent with the QCA Act, commercially agree alternate positions that are different to those in the standard agreement.[11] Further, the pricing principles allow for price differentiation between services for a "specified commodity in a specified geographic area" due to differences in cost and risk (clause 6.1.2(b)).

Neither of these provisions are consistent with the proposed 4.5.3(d), which prevents the execution of an agreement substantially in the form of the alternate SAAs whilst also providing for multiple end user access rights in one TOA.

5. Compliance with the QCA assessment criteria

In assessing the arguments and information provided, it was noted in the final decision that *"it is appropriate to retain consistency between the existing SAAs and the proposed new SAAs as far as is possible"*[12] and that any changes to the risk profiles of the parties were *"necessary … to enable the split arrangement to operate effectively, flexibly and in a commercially balanced way"*[13]. The decision to mandate the contracting structure is contrary to the current provisions of the 2010AU which in practice allow for access holders to have one access agreement per rail haulage agreement or one access agreement for multiple rail haulage agreements.

6. Due consideration to matters raised in October 2012

In making its assessment to impose a contracting structure, the final decision states regard was had to the following considerations raised by Aurizon in earlier submissions:

(a) transparent removal of cross default risk;

(b) maintaining the ability to pool access rights;

(c) ensuring the ability to customise TOAs to individual end user requirements; and

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9 QR National, Submission on Draft Decision on QR Network's proposed Alternate Standard Access Agreement, 30 October 2012, page 12.

10 QR Network, QR Network's 2010 Access Undertaking, 1 October 2010, clause 5.2(n)(iii).

11 See, e.g. cl 5.1(d)

12 Queensland Competition Authority, Final Decision Aurizon Network Alternative Standard Access Agreements, April 2013, page 6

13 Queensland Competition Authority, Final Decision Aurizon Network Alternative Standard Access Agreements, April 2013, page 7

(d) administration and cost impacts of the mandated structure.

Aurizon acknowledges that the final decision provided a sufficient basis to demonstrate that the mandated structure would not impact on the ability to pool access rights.

However, the final decision does not demonstrate that reasonable regard was given to the remaining issues raised by Aurizon, other than expressing a view that a mandated structure would be transparent and certain, and that it did not believe administrative costs would be unduly burdensome.

It is concerning that sufficient regard does not appear to have been given to the broader issue of commercial negotiation of alternate arrangements, the benefits to end users and operators of commercial flexibility, practical alternatives to the cross default risk[14], and the benefits associated with the reduced risk of a material breach.[15] Moreover, Aurizon does not consider that the QCA's view that the administrative costs would not be unduly burdensome is reasonable; that multiple TOA contracts are substantially similar does not provide a reasonable basis for concluding that Aurizon should be required to bear the costs associated with administering multiple contracts as opposed to the costs associated with managing one TOA with multiple end user access rights.

7. Conclusion

Aurizon considers it essential that cl 4.5.3(d) is modified prior to the 2010AU being amended, in line with legislative requirements.

Aurizon believes this could be simply achieved by including in the TOA[16] a new subclause in the clause describing the interaction between the operational rights in the TOA and the access rights in the EUAA, mandating the contract structure as per the following :

- cl 7(a)(iii) Unless otherwise agreed with the End User, Aurizon Network and the Operator will not vary this Train Operations Agreement so that it utilises Access Rights contracted under more than one End User Access Agreement.

Critically, this will not undermine the benefits (or protections) otherwise afforded to industry by the alternate SAA. There is no suggestion that an end user should be required to accept a single, amalgamated TOA – it is entirely within the control of an end user as to the contracting arrangements that are of value to them. For example, where an end user is negotiating with two operators, if one operator is proposing to include the end user's access rights within an amalgamated TOA and the other operator is proposing to have only that end user's access rights in the TOA, it is the end user that is able to commercially determine the outcome.

For further information with regard to this submission please contact Rachel Martin, Senior Regulatory Strategist on (07) 3019 5476.

Yours faithfully,

[redacted]

Andrew MacDonald
Senior Vice President
Commercial and Marketing

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14 Refer discussion in section 2.1.1.3 (pp 11 and 12) of QR National's October 2012 submission

15 IBID

16 For clarity, the new clause would be included in the agreement which contains the recitals, operative provisions and access rights, rather than schedule A - the reference schedule or schedule B – the general conditions of contract.