

File Ref: 1414380

28 May 2020

Mr Jon Windle
Manager—Regulation
Aurizon Network
GPO Box 456
Brisbane Qld 4001

Dear Mr Windle

Aurizon Network's 2018–19 capital expenditure claim

I wish to advise that the Queensland Competition Authority has approved Aurizon Network's 2018–19 capital expenditure claim (as amended 30 April 2020). The total expenditure approved to be included into Aurizon Network's regulatory asset base is \$126,786,466 (including interest during construction).

The basis of our decision is set out in the attached decision notice, in accordance with schedule E, clause 2.3(c) of the 2017 access undertaking. This letter and decision notice will be published on the QCA website for stakeholders' information.

If you have any questions about this decision notice, please contact Pag Arao-Arao on 07 3222 0555.

Yours sincerely



Charles Millstead
Chief Executive Officer

DECISION NOTICE

AURIZON NETWORK'S 2018–19 CAPITAL EXPENDITURE CLAIM

28 May 2020

The Queensland Competition Authority accepts Aurizon Network's 2018–19 capital expenditure claim (as amended 30 April 2020). We have set out our reasons in this decision, in accordance with schedule E, clause 2.3(d)(i) of the 2017 access undertaking.

Aurizon Network's 2018–19 capital expenditure claim

We conduct an annual assessment of the prudence and efficiency of Aurizon Network's capital expenditure, to determine if it should be included in the regulatory asset base (RAB) for the CQCN. In determining the prudence and efficiency of capital expenditure, we have regard to the **scope of works, standard of works and cost** (sch. E, cl. 2.2(b) of the 2017 access undertaking).

Aurizon Network submitted its 2018–19 capital expenditure claim on 25 October 2019. It subsequently amended the claim on 22 November 2019, 19 December 2019¹ and 30 April 2020². The final claim encompassed 46 projects, totalling \$126 million excluding interest during construction (IDC).³

Engineering consultant's assessment

We engaged Flagstaff to provide engineering advice on the prudence and efficiency of Aurizon Network's capital expenditure claim (in accordance with cl. 2.2(h)). A sample of projects was selected to be assessed against the criteria in schedule E of the 2017 access undertaking. The sample comprised 15 projects, representing approximately 80 per cent of the claim at that time.⁴

Flagstaff assessed and reported on the projects based on a site visit to the Blackwater and Goonyella systems and a desktop review of information provided by Aurizon Network.

Flagstaff found most projects in the sample to be prudent and efficient, except for the following three projects, where it recommended adjustments to reduce the claim:

¹ Aurizon Network, *FY19 Capital Expenditure - Amendment*, letter to the QCA, 19 December 2019.

² Aurizon Network, *Response to Draft Decision FY2019 Capital Expenditure Claim*, letter to the QCA, 30 April 2020 (Aurizon Network April 2020 amended claim).

³ Aurizon Network April 2020 amended claim.

⁴ QCA, *December amended sample list*, stakeholder notice, February 2020.

- (1) IV.00449 Bridge Ballast Renewal Package 1⁵
- (2) IV.00360 Network Asset Management System Tranche 2⁶
- (3) IV.00476 Track Renewal Package 1.⁷

Flagstaff also advised that two projects should be delayed from the 2018–19 claim, based on a high-level assessment of the projects:

- (1) IV.00470 Corridor Security Package 1⁸
- (2) IV.00503 Power Systems Renewal Package 1⁹

While we have had regard to the advice provided, we have not fully adopted Flagstaff's views, recommendations or analysis. Rather, we have used this advice as one input to our overall assessment.

Stakeholder consultation

We provided stakeholders with opportunities to make submissions on Aurizon Network's initial claim and on Flagstaff's assessment of prudence and efficiency. We received a submission from Aurizon Network, in response to Flagstaff's assessment.¹⁰

Aurizon Network also responded to a draft of our decision (consistent with cl. 2.3(d)(ii)), revising its claim relating to an outstanding project that we were inclined not to approve.¹¹

Table 1 Aurizon Network's response to Flagstaff's assessment

<i>Project</i>	<i>Summary response</i>
IV.00449 Bridge Ballast Renewal Package	Aurizon Network agreed . It said it has withdrawn \$58,050 from project costs and will seek QCA approval of these costs upon commissioning. ¹²
IV.00360 Network Asset Management System Tranche 2	Aurizon Network disagreed . It considered this expenditure relates solely to post-commissioning costs associated with already approved works. ¹³
IV.00476 Track Renewal Package 1	Aurizon Network disagreed . It provided an updated cost breakdown to Flagstaff after the report was finalised, which Aurizon Network claimed, addressed concerns raised. ¹⁴
IV.00470 Corridor Security Package 1	Aurizon Network disagreed . It considered the amount reflects Aurizon Network internally approved budget, and it

⁵ Flagstaff, *Aurizon Central Queensland Coal Network Capital Expenditure Review FY 19*, February 2020, pp. 10, 75–83 (Flagstaff report).

⁶ Flagstaff report, pp. 10, 125–126.

⁷ Flagstaff report, pp. 10, 57–66.

⁸ Flagstaff report, pp. 34–35.

⁹ Flagstaff report, p. 36.

¹⁰ Aurizon Network, *FY2019 Capital Expenditure Submission*, submission letter to the QCA, March 2020, p. 4 (Aurizon Network response).

¹¹ Aurizon Network's April 2020 amended claim.

¹² Aurizon Network response, p. 4; Aurizon Network April 2020 amended claim, p. 1.

¹³ Aurizon Network response, pp. 9–10.

¹⁴ Aurizon Network response, p. 3.

<i>Project</i>	<i>Summary response</i>
	only claims commissioned values as at 30 June annually in its capex claims. ¹⁵
IV.00503 Power Systems Renewal Package 1	Aurizon Network disagreed . It said this claim relates to the costs incurred for an individual job and assets that were deemed necessary for execution in 2019, and part of an overall multi-year asset renewal programs. ¹⁶

QCA assessment and decision

We approve Aurizon Network's 2018–19 capital expenditure claim, as amended on 30 April 2020.

All of the projects assessed meet the criteria for prudence and efficiency for inclusion in the RAB. Overall, the total amount we are approving will provide approximately \$126 million (excluding IDC) to be included in the RAB. The related projects are listed in **Attachment 1**.

While Flagstaff also recommended adjustments to other projects, we do not require that these adjustments be made.

- Flagstaff recommended delaying amounts incurred for the IV.00470 corridor security and IV.00503 power systems renewal projects (\$1.38 million and \$0.84 million, respectively), on the basis of a high-level review. Flagstaff said it is too early in terms of completed work in a program of works to include either in a capital expenditure claim. However, we are satisfied that Aurizon Network has completed these projects according to the standards and overall scope of large rolling renewals, recognising the timing of commissioning in relation to the overall amounts claimed.
- Flagstaff recommended rejecting the entire amount claimed for IV.00360 network asset management system tranche 2 (being \$0.38 million). While Flagstaff saw the merit in the project, it was unable to assess the prudence and efficiency of costs incurred to date, as only estimated costs were provided for this project. However, we are satisfied that Aurizon Network has completed this project according to the standards and overall scope consistent with rolling renewals and that the costs now being claimed relate to post-commissioning amounts.
- Flagstaff recommended reducing the amount claimed for IV.00476 Track Renewal Package 1 (by \$1.02 million), given conflicting and incomplete cost information.¹⁷ In response, Aurizon Network said that the original cost breakdown contained 'administrative errors' that incorrectly allocated all indirect costs to two jobs—specifically, the 'bad order sidings'—rather than apportioning costs across all activities within the Track Renewal Package. The effect of this was that the bad order siding costs appeared to be materially higher.

We note Flagstaff generally found the costs reasonable in terms of scale, nature and complexity.¹⁸

We have also assessed the updated cost breakdown supplied to address these inconsistencies.¹⁹ We note Aurizon Network showed amounts for each system's share of indirect costs, separately identified the direct costs of each element²⁰, reflected the year to date expenditure, and showed the value of commissioned assets as at 30 June 2019, apportioned at a system level.

¹⁵ Aurizon Network response, pp. 5–6.

¹⁶ Aurizon Network response, pp. 7–9.

¹⁷ Flagstaff report, p. 64.

¹⁸ Flagstaff report, p. 64.

¹⁹ Aurizon Network response, p. 3.

²⁰ Aurizon Network response, Appendix C.

References

Aurizon Network, *FY19 Capital Expenditure - Amendment*, letter to the QCA, 19 December 2019.

Flagstaff Consulting Group, *Aurizon Central Queensland Coal Network capital Expenditure Review FY19*, report for the QCA, February 2020 (Flagstaff report).

QCA, *December amended sample list*, stakeholder notice, February 2020.

Aurizon Network, *FY2019 Capital Expenditure Submission*, submission letter to the QCA, March 2020 (Aurizon Network response).

Aurizon Network, *Response to Draft Decision FY2019 Capital Expenditure Claim*, letter to the QCA, April 2020 (Aurizon Network April 2020 amended claim).

ATTACHMENT 1: APPROVED 2018–19 CAPITAL EXPENDITURE CLAIM

Project Number	Project Name	Asset Type	Claimable Expenditure (\$, excl. IDC)
IV.00425	Rail Renewal Program Package 1	Asset Renewals	26,572,373
IV.00446	Structures Renewal Package 1	Asset Renewals	15,465,451
IV.00476	Track Renewal Package 1	Asset Renewals	15,193,594
IV.00461	Turnout Renewal Package 1	Asset Renewals	14,053,345
IV.00452	Formation Renewal Package 1	Asset Renewals	9,851,560
IV.00449	Bridge Ballast Renewal Package 1*	Asset Renewals	8,509,462
IV.00455	Control Systems Renewal Package 1	Asset Renewals	6,875,112
IV.00473	Sleeper Renewal Package 1	Asset Renewals	6,317,874
IV.00458	Level Crossing Renewal Package 1	Asset Renewals	4,048,374
IV.00049	Radio System Replacement	Asset Renewals	3,609,098
IV.00437	Callide Infrastructure Upgrade	Sustaining Other	2,298,631
IV.00470	Corridor Security Package 1	Asset Renewals	1,381,137
IV.00555	FY19 Minerva Infrastructure Upgrade	Sustaining Other	1,379,635
IV.00399	2017 Cyclone Debbie Rectification	Asset Renewals	1,156,299
IV.00329	Structures Renewal FY18	Asset Renewals	926,232
IV.00004	Traction Fault Locator Renewal	Asset Renewals	881,498
IV.00376	FY18 Access Points	Asset Renewals	843,497
IV.00503	Power Systems Renewal Package 1	Asset Renewals	835,307
IV.00346	Package 1 FY18 Control Systems Renewal	Asset Renewals	815,826
IV.00283	Traction SCADA System	Asset Renewals	811,715
IV.00364	Turnout Renewal FY18	Asset Renewals	696,543
A.04313	Gauge Face Lubrication Asset Renewal	Asset Renewals	564,946
IV.00334	Bridge Ballast Renewal Program FY18	Asset Renewals	493,610
IV.00467	Access Roads Package 1	Asset Renewals	478,621

<i>Project Number</i>	<i>Project Name</i>	<i>Asset Type</i>	<i>Claimable Expenditure (\$, excl. IDC)</i>
IV.00374	CQ Access Roads FY18	Asset Renewals	337,699
IV.00321	Sleeper Renewal Program FY18	Asset Renewals	336,966
IV.00344	Formation Renewal FY18	Asset Renewals	330,989
IV.00360	Network Asset Mgt System Tranche 2	Transformation	323,399
IV.00343	Level Crossings Renewal Program FY18	Asset Renewals	311,435
IV.00322	Rail Renewal FY18	Asset Renewals	210,734
IV.00154	FY17 Autotransformer Renewal Project	Asset Renewals	185,545
IV.00145	Track Upgrade FY17	Asset Renewals	154,769
A.01731	WIRP1: DINGO TO BLUFF DUPLICATION	Growth	108,391
A.04599	Havilah Culverts Upgrade	Growth	73,476
IV.00495	Coppabella Walkways Relocation	Sustaining Other	59,417
A.02976	WIRP1: North Coast Line	Growth	47,818
IV.00184	Network Capacity Model	Growth	30,469
IV.00040	Train Detection Renewal Program	Asset Renewals	14,961
A.03686	WIRP1: MOURA SYSTEM UPGRADE	Growth	7,189
IV.00261	Telecommunications Infrastructure Renewal	Asset Renewals	7,105
IV.00266	Transmission Renewal FY17	Asset Renewals	6,281
A.03735	WIRP1: Bauhinia NORTH Upgrade	Growth	1,194
IV.00177	Structures Renewal FY17	Asset Renewals	(16,709)
IV.00316	Access Points Renewal Program	Asset Renewals	(56,746)
IV.00384	OH Equipment Renewal FY18	Asset Renewals	(113,497)
IV.00144	Rail Renewal FY17	Asset Renewals	(117,009)
TOTAL			126,303,616

NOTE" *amount after adjustments