



Submission to Queensland Competition Authority

Submission on Aurizon Network's 2013 Review Event

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1 Executive summary

Anglo American Metallurgical Coal Pty Ltd (**Anglo American**) welcomes this opportunity to present its views to the Queensland Competition Authority (**QCA**) on Aurizon Network Pty Ltd's (**Aurizon Network**) 2013 Review Event.

In summary:

- (a) the quantum of costs for the repair of the Moura System seems high and in light of the findings of Sinclair Knight Mertz (**SKM**) in respect of the anomalies surrounding a claim for \$1,453,716, Anglo American is concerned that the costs may not be for 'incremental costs' as required by Aurizon Network's Access Undertaking 2010 (**UT3**);
- (b) before making a decision on the 2013 Review Event, the QCA should be entirely satisfied that Aurizon Network has thoroughly exhausted all avenues of insurance claims;
- (c) Anglo American agrees with the report by SKM that the amount of \$2,301,270 should be excluded from the claim as it relates to ordinary labour which should be covered by the UT3 maintenance allowance;
- (d) although previously accepted by the QCA, Anglo American does not believe that Aurizon Network should obtain a margin of 5.75% on labour costs as costs recovered for a Review Event should be on a cost pass-through basis;
- (e) to the extent that the network has returned to full usage and the event occurred more than 6 months ago, Anglo American queries whether the costs are true 'incremental costs' as required under Schedule F, clause 2.2.7. In any event, Anglo American agrees with SKM that the future claims should not be allowed on the basis that they have not been incurred and should not be accepted under a Review Event which is based on a cost recovery model; and
- (f) to the extent that works undertaken, or to be undertaken, as a result of the Review Event would have otherwise been undertaken by Aurizon Network as planned maintenance activities, Aurizon Network has already been compensated under the regulatory regime and should not be allowed to 'double-dip' by recovering these costs from the Review Event.

2 Quantum of costs for the Moura System

Aurizon Network has claimed a total of \$17.1 million of costs in respect of the Moura System. This is \$11.2 million higher than the repair costs for the 2012 Review Event, which seems like a relatively high difference.

Anglo American requests the QCA to ensure that the costs are 'incremental costs' as required by UT3. In particular, Anglo American notes that SKM found that \$1,453,716 was claimed by Aurizon Network in respect of some additional sites which did not appear in the list shared with SKM during the site visit on 19 and 20 February 2013. This included the Stirrat site which was approximately \$1.2 million of that amount. SKM noted that the Moura System was open to traffic on 6 February 2013 but the additional sites did not appear on the list of affected sites until 7 March 2013. SKM noted this anomaly but did not specifically form a conclusion.

Anglo American is concerned that the \$1,453,716 in respect of the additional sites including the Stirrat site may not be 'incremental costs' as required by UT3 and requests that the QCA:

- (a) confirm with SKM whether they undertook a site visit of the Stirrat site and other additional sites and determined that the repairs were necessary because of the flood event; and

- (b) seek confirmation from Aurizon Network (for example, by way of photographs) that the damage done was caused by the 2013 Review Event.

3 Further evidence of insurance claims

Anglo American is not convinced that Aurizon Network has provided enough information about its insurance claims in order to assure the QCA and users that it has been properly utilising the risk premium that it receives as part of Reference Tariffs for the purpose of insuring the Central Queensland Coal Network (**CQCN**). As the coal producers have no visibility in respect of the insurance policies or the claims that Aurizon Network has made, Anglo American submits that before making a decision on approving the 2013 Review Event, the QCA should be entirely satisfied that Aurizon Network has thoroughly exhausted all avenues of insurance claims.

4 Labour costs

SKM found that \$2,301,270 should be excluded from the claim as it relates to ordinary labour which should be covered by the UT3 maintenance allowance (however, Anglo American notes that it is not sure whether this amount relates to all systems and, if so, what proportion relates to the Moura System).

Anglo American submits that there is no need for Aurizon Network to receive an additional margin on labour costs associated with repair of the CQCN. The concept of a cost pass-through to users is to absorb the entire actual cost of the repairs and repair work. It is, therefore, illogical that Aurizon Network should receive a margin greater than the actual outlaid costs (indexed for inflation and interest) of the repairs and in this instance the repair works.

Anglo American notes that the use of a margin on labour costs was approved by the QCA during the 2012 Review Event, however, does not agree that this provides precedent for including a margin on labour costs in the 2013 Review Event. The margin on labour costs appears to be associated with reimbursing internal Aurizon Network staff for work done during the flooding in 2013 and Anglo American seriously questions why users of the CQCN should be required to reimburse Aurizon Network at a 5.75% margin for work undertaken by its own staff, including the senior management of Aurizon Network.

Anglo American submits that the situation where the QCA should approve costs for a cost pass-through event is where actual, specified and proven costs have been evidenced by Aurizon Network rather than providing a 5.75% bonus without any way of satisfying the QCA or users that this is an accurate, appropriate or prudently incurred charge.

5 Anomalous differences between overtime costs on various systems

Anglo American acknowledges that Aurizon Network was required to work under tight time constraints in order to repair the damage to the CQCN for the benefit of the entire Queensland coal market. Anglo American acknowledges that Aurizon Network worked hard to repair the CQCN to a serviceable and safe state within a short time. Anglo American fully appreciates that this level of work involved some amount of overtime by Aurizon Network employees and contractors.

In saying that, Anglo American is concerned about the comparison of ordinary labour costs and overtime costs between the various systems listed in the 2013 Review Event claim by Aurizon Network. In particular, Anglo American notes that there is a significant difference between the proportion of overtime costs compared to ordinary costs on the Moura line as opposed to the Blackwater line.

As a ratio, Anglo American notes the following:

System	Ordinary Labour Costs	Overtime Labour Costs	Percentage of Total Cost
Blackwater	\$2,055,230	\$69,886	3.4%
Moura	\$461,738	\$88,078	19%

On a whole that is a total variance of 15.6% as proportion of the total costs of preparing the system. Anglo American notes that this variance appears to be extreme.

Anglo American submits that the QCA should not approve the 2013 Review Event without further evidence as to why overtime costs formed 19% of the total cost for repairing the Moura system, where the overtime costs for the Blackwater system was only 3.4%.

6 Future flood rectification works

Anglo American understands that Aurizon Network wishes to claim a considerable portion of the \$17.1 million as costs for future works that have not yet been undertaken. Aurizon Network explains that these estimated costs are 'for works that have been planned as part of the flood rectification works that will be delivered in the near future'.

This claim for future works by Aurizon Network amounts to \$4,251,000. As such, Aurizon Network is claiming 25% of the total 2013 Review Event for expenses that it has not yet incurred, an amount totalling almost $\frac{3}{4}$ of the entire 2012 Review Event. Anglo American submits that this is inappropriate.

Anglo American notes that SKM has recommended that these costs (which are \$932,000 on the Moura System) be excluded from this claim. Anglo American agrees with this and notes that the flooding occurred over 6 months ago and that full capacity coal rollingstock has been operating on the CQCN for almost 5 months. While Anglo American understands that some rectification works will continue past the recommencement of full services (eg, repairs to scours, culverts, pick up of materials and repairs to maintenance roadways), 25% of the costs in Aurizon Network's current claim are for future works. As such, Anglo American questions why such a large amount of the expenditure remains outstanding when the system appears to have already been returned to the level of service available before the flood.

Assumedly Aurizon Network has not allowed full-capacity full-speed rollingstock back on the CQCN without the network operating as normal and, therefore, it must be assumed that the vast majority of costs have been incurred to return the system to the standard it was prior to the January 2013 flooding.

Further, even if a large percentage of the costs remains to be paid in FY13/14, the Review Event process in UT3 operates on a cost pass through basis. Aurizon Network can recover all prudently incurred costs of repairs to the network, but only after those costs have been incurred. The 2013 Review Event application by Aurizon Network applies a vague prediction process in order to determine costs outstanding. If these costs are required to be passed-through to users, that pass-through should occur at the end of the next financial year when Aurizon Network has exact figures, not as a premature loan by users with no guarantee of recovery in the event of over-expenditure.

To the extent that the network has returned to full usage and the event occurred more than 6 months ago, Anglo American queries whether the costs are true 'incremental costs' as required under Schedule F, clause 2.2.7.

7 Potential for 'double-dipping'

Anglo American notes that part of the standard reference tariff that Aurizon Network receives from users is for planned maintenance activity. This covers all standard and expected maintenance works undertaken on the CQCN.

Anglo American notes that SKM has not specifically considered whether works that Aurizon Network has undertaken as part of the 2013 Review Event should have been covered as part of annual planned maintenance. Although Anglo American supports SKM's suggestion to exclude ordinary labour costs from the claim, the QCA should also be satisfied that maintenance undertaken and claimed would have occurred on the CQCN even without the Review Event.

Further, Anglo American is concerned that works undertaken and claimed as part of the 2013 Review Event might negate the need for planned maintenance works in the FY13/14 period. Anglo American submits that to the extent Aurizon Network would have undertaken maintenance works in the next period if they were not completed as part of the 2013 Review Event, the cost of those works should be excluded or deducted from the maintenance budget charged to users.

Another concern with costs attributable to the 2013 Review Event is the impact that these rectification works will have on Aurizon Network's renewals program. In instances where rail and track infrastructure was due to be renewed in the near future but has been replaced by virtue of the current flood works, the QCA should ensure that Aurizon Network only receives those costs once. Whether that is managed by deducting costs which soon would have been incurred for track replacement from the Review Event, or reducing the renewal margin in the Reference Tariff, the QCA must prevent Aurizon Network from securing double-recovery for the replacement cost of infrastructure which it already receives from users.

If costs overlap, Aurizon Network is essentially 'double-dipping' as it is already been compensated under the regulatory regime for maintenance while double recovering by virtue of the 2013 Review Event.