

20 January 2014

QRC's submission on
Aurizon Network's
Response to Industry

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Part 1 - Introduction

The Queensland Resources Council (**QRC**) is described in Item 1 of the Executive Summary of its submission in relation to UT4 dated 10 October 2013 (**Main Submission**).

This submission (**New Submission**) is provided by the QRC in response to Aurizon Network's Response to Industry Submissions dated 29 November 2013 (**Response to Industry**). The QRC's New Submission is presented in the same order as Aurizon Network's Response to Industry. The QRC has (largely) only commented on matters raised in Aurizon Network's Response to Industry. Except where expressly stated in this New Submission, the QRC's Main Submission (including Mark-Ups) stands. This New Submission should be read in conjunction with the QRC's Main Submission.

The QRC notes that Aurizon Network has responded to only parts of the QRC's Main Submission. A list of some issues that Aurizon Network has not responded to is set out in Annexure E. This list is by no means exhaustive.

The QRC notes that Aurizon Network has indicated in its Response to Industry that it intends to change the drafting of some provisions of UT4. With the exception of a partial update of Part 8, that drafting has not been provided. Aurizon Network's Response to Industry is also prepared at a high level. It is therefore difficult for the QRC to meaningfully assess a number of Aurizon Network's comments. Industry are concerned as to how balanced Aurizon Network's drafting will be (for example, a principle may be reflected but its application may be subject to the exercise of numerous discretions by Aurizon Network).

Aurizon Network has not indicated when it will provide the amendments it has foreshadowed it would be willing to make to UT4. If Aurizon Network intend to provide that drafting before publication by the Queensland Competition Authority (**QCA**) of a draft decision on UT4, the QRC asks that the QRC be entitled to provide a submission on Aurizon Network's drafting. The QRC's preference is that the QCA does not delay a draft decision in order to receive Aurizon Network's drafting.

Unless otherwise expressly stated in this New Submission, it should be noted that acceptance by the QRC of a change proposed by Aurizon Network in its Response to Industry does not mean that the QRC withdraws its proposed drafting or submissions. We understand that this may create complexity for the QCA. If it would be helpful for the QRC's submissions to be presented in a different format (for example, a mark-up of the UT4 changes originally proposed by the QRC), please let us know.

The QRC recommends that the QCA reject UT4 for the reasons set out in the QRC's Main Submission and this New Submission. In rejecting UT4, the QRC recommends that the QCA provide drafting for the undertaking that the QCA would approve (rather than describing in principle how the drafting should be amended).

A glossary of terms used in this New Submission is set out at the back of this document.

The QRC confirms that this New Submission does not contain confidential information and may be made public.

Part 2 - Overview and response to key points

1 Overview

Aurizon Network has indicated its willingness to modify parts of UT4. The QRC is appreciative of Aurizon Network's Response to Industry and its willingness to change parts of UT4.

UT4 is however a very one-sided document. It was, as has previously been noted, submitted without consultation with industry. Changes made from UT3 only benefited Aurizon Network.

While there has been a willingness to move on some matters, industry's core issues have not been addressed. There remains a significant number of material issues between Aurizon Network and industry. These issues are set out in this New Submission and the Main Submission. While reluctant to produce a summary of issues, examples include:

- **WACC:** Aurizon Network has not proposed any change to the WACC. The QRC supports the consultation process currently being undertaken by the QCA. Aurizon Network has indicated that it will respond substantively to cost of capital issues as part of the current QCA consultation process. The QRC therefore requests the opportunity to consider and respond to any further material submitted by Aurizon Network.
- **Ringfencing:** There is a lack of confidence in the current ringfencing regime and even more so with the proposed UT4 regime. On this issue, the QRC feels that Aurizon Network has attempted to create a technical argument (which the QRC has been forced to address in this New Submission) while disregarding the core issue of conflicts raised by industry.
- **No integration of the capital planning and expansion processes:** There remains inadequate 'links' between stages in the capital planning and expansion process. For example, there is no relationship between long term planning (through the Network Development Plan (**NDP**)) with the expansion process, making the NDP a document with limited practical value. Similarly, there is no requirement for Aurizon Network to use the published System Operating Assumptions or the results of a capacity review in its expansion activities.
- **Expansion process:** Annexure C sets out the QRC's comments on Part 8, and Annexure D, the QRC's mark-up of Part 8. Industry suggests that Part 8 should codify the expansion process. The QRC objects to a number of aspects of Aurizon Network's proposed expansion process which are inconsistent with the principle of codification. Aurizon Network has suggested that there should be a legitimate business interest proviso. If Aurizon Network wishes to propose additional protections to protect its legitimate business interests, it should propose specific matters. Further, Aurizon Network should not be able to agree

arrangements outside of the expansion process framework which may adversely affect another access seeker (for example, providing an access seeker that enters into an agreement outside of the expansion process framework with priority over other access seekers).

- **Expansion funding:** A meaningful suite of expansion funding obligations is needed. Aurizon Network considers SUFA to be a genuine alternative to Aurizon Network funding. With substantial amendment, SUFA will be an alternative for a limited number of projects and for a limited number of access seekers. Aurizon Network has suggested that a funding obligation and regulatory oversight of access conditions is without precedent. The QRC considers that there is precedent for these matters (e.g. DBCT, the WA Railway Access Code and Aurizon Network's UT3). Further, the expansion funding issue (and regulatory oversight of Access Conditions) is of greater importance in the case of Aurizon Network due to Aurizon Network's unwillingness to invest in significant investments on regulated terms. Other regulated service providers have not demonstrated a similar reluctance.
- **Maintenance:** Aurizon Network considers that the linking of condition based assessments of the network to the determination of the RAB presents an *"unreasonable and unacceptable level of risk"*. In the QRC's view, there needs to be some mechanism which ensures that Aurizon Network adequately maintains the network, at least to the standard which has been funded by the cost allowances recovered through tariffs. The condition based assessment with potential RAB adjustment is one means of achieving this. The QRC is willing to consider alternative approaches.

In regard to the quantum of maintenance cost allowances provided for under UT4, the QRC has indicated in its Main Submission that a significant amount of work is required in this area. The QRC will provide its comments on maintenance costs after the publication of the QCA's maintenance cost information.

- **Operating costs:** The comments made by the QRC in respect of operating costs in its Main Submission stand. The QRC considers it unhelpful to provide further submissions on operating costs until the QCA publishes its operating costs information.
- **Access agreements:** In its Main Submission, the QRC proposed that the standard access agreements be modified to ensure that Aurizon Network is accountable for its services. Aurizon Network is unwilling to address industry's concerns in this respect.
- **Capacity determination:** The QRC suggests that the determination of capacity should be more independent, transparent and disputable. Aurizon Network does not appear supportive of this.

2 Response to key proposed changes (Section 1(e) of AN's Response to Industry)

In its Response to Industry, Aurizon Network provided an outline of its key points and a summary of its key proposed changes to UT4. The QRC's response to these items is summarised in the following table:

RESPONSE TO KEY PROPOSED CHANGES

Topic	AN's Proposed Change	QRC Response
Scope	<p>Aurizon Network will re-draft the provisions in relation to electricity supply to make clear that while EC is not a regulated service, access to the electric infrastructure is included in the regulated service and that Aurizon Network is seeking only to recover, via the EC rate, those costs relevant to <i>on-selling</i> electricity.</p>	<p>The changes proposed by Aurizon Network in relation to electricity are cosmetic only. Aurizon Network has not addressed the scoping issues raised by the QRC in its Main Submission.</p> <p>The QRC's position in relation to the scoping issues raised by Aurizon Network in its Response to Industry is outlined in Section 1 of Part 4 and in Annexure A.</p> <p>Annexure E provides a summary of the scoping issues that Aurizon Network did not respond to in its Response to Industry.</p>
Non discrimination	<p>Aurizon Network will make amendments to the 2013 DAU to provide further confidence to third parties in the integrity of the regulatory framework, particularly in relation to its non-discrimination obligations.</p>	<p>The changes proposed by Aurizon Network in its Response to Industry do not address the substance of industry's concerns regarding the non-discrimination obligations in UT4.</p> <p>The QRC's position in relation to the non-discrimination issues raised by Aurizon Network in its Response to Industry is provided in Section 3 of Part 4.</p>
Ringfencing	<p>In response to industry feedback, Aurizon Network will make a number of further improvements to the ringfencing regime that clarify drafting, address the functional structure and are consistent with best practice.</p>	<p>The "<i>further improvements</i>" proposed by Aurizon Network to the UT4 ringfencing regime are inadequate. Aurizon Network has disregarded the core issue of conflicts raised by industry.</p> <p>The QRC's position in relation to the ringfencing issues raised by Aurizon Network in its Response to Industry is outlined in Section 4 of Part 4 and Annexure A.</p>

RESPONSE TO KEY PROPOSED CHANGES

Topic	AN's Proposed Change	QRC Response
Dispute resolution	<p>Amendments to Part 11 will be made to put beyond doubt that Aurizon Network does not intend to restrict access to dispute resolution, or the role of the QCA.</p>	<p>The QRC appreciates Aurizon Network's commitment to broadening the application of the dispute resolution provisions. The QRC suggests that further changes are required in Part 8 to ensure the value of the dispute resolution framework is not undermined.</p> <p>The QRC's position in relation to the dispute resolution issues raised by Aurizon Network in its Response to Industry is set out in Section 5 of Part 4 and in Annexure A.</p> <p>Aurizon Network has failed to respond to a number of proposals raised by the QRC in its Main Submission in relation to the UT4 dispute resolution framework, a summary of which is provided in Annexure E.</p>
Expansion process and pricing	<p>A new draft of the expansion process, reflecting more than six months of discussions with the QRC, is attached to this submission (Annexure C).</p> <p>Aurizon Network will accept the inclusion of the QRC's preferred principles for the pricing of network expansion capacity in the undertaking.</p> <p>Aurizon Network will continue to explore options with the QRC over the coming months.</p>	<p>The QRC acknowledges that Aurizon Network has accepted the principles of a number of changes which the QRC proposed to Part 8.</p> <p>The QRC's position in relation to the expansion process issues raised by Aurizon Network in its Response to Industry is set out in Section 6 of Part 4 and in Annexure A. Annexure C provides a summary of the key changes made in Aurizon Network's revised draft and includes the QRC's response to those key changes. The QRC has also developed a mark-up of the revised draft which is attached to this New Submission at Annexure D.</p>

RESPONSE TO KEY PROPOSED CHANGES

Topic	AN's Proposed Change	QRC Response
Negotiation framework	Aurizon Network will implement a number of changes to the negotiation process, as suggested by industry.	<p>The QRC acknowledges that Aurizon Network has agreed to a number of the QRC's proposed amendments to the negotiation framework. However, Aurizon Network has left a number of other proposals unanswered.</p> <p>The QRC's position in relation to the negotiation framework issues raised by Aurizon Network in its Response to Industry is outlined in Section 7 of Part 4 and in Annexure A.</p> <p>Annexure E provides a summary of the negotiation framework issues that Aurizon Network failed to respond to in its Response to Industry.</p>
Demonstration of supply chain capacity	Aurizon Network will review the drafting of the provisions relating to the demonstration of supply chain capacity to ensure that the evidence required reflects what would reasonably be required at the relevant stages of the application and negotiation process.	The QRC appreciates Aurizon Network's willingness to undertake a review of the UT4 drafting in relation to the demonstration of supply chain capacity. The QRC's proposal for the amendment of these provisions is set out in Section 8 of Part 4. The QRC's position in relation to the supply chain capacity issues raised by Aurizon Network in its Response to Industry is provided in Annexure A.
Allocation of available capacity	Amendments to Part 7 will be made to clarify the mechanism for which scarce capacity is allocated. This includes refinements to the criteria to be used.	<p>The QRC considers that the allocation of capacity needs to be more transparent and objective. Although the QRC appreciates Aurizon Network's willingness to amend Part 7, Aurizon Network's proposed amendments have been described at a high level with no specificity or clarity. The QRC's response to Aurizon Network's proposed changes is set out in Section 9 of Part 4 and in Annexure A.</p> <p>As outlined in Annexure E, Aurizon Network has also failed to respond to a number of the QRC's proposed changes to Part 7, including its amendments to the renewal and transfer of access rights regime.</p>

RESPONSE TO KEY PROPOSED CHANGES

Topic	AN's Proposed Change	QRC Response
<p>Flexible management of access rights</p>	<p>Aurizon Network will include a proposal for short term capacity swapping, which will improve the flexible allocation of capacity and promote efficient use of the infrastructure.</p> <p>The mechanism must ensure that no other access holder is made worse off by the swap.</p>	<p>The QRC is pleased with Aurizon Network's willingness to develop a short term capacity swap mechanism. However, the QRC considers that the concept of no party being "<i>worse off</i>" requires further refinement.</p> <p>The QRC does not support the inclusion of an operator capping ToP regime in UT4. The QRC raised a number of concerns with respect to operator capping in its Main Submission which have not been addressed by Aurizon Network.</p> <p>The QRC's response to Aurizon Network's proposed key features of the short term capacity swap mechanism and further comments in relation operator capping are detailed in Section 10 of Part 4 and in Annexure A.</p>
<p>Performance and reporting</p>	<p>Aurizon Network is committed to improved transparency in reporting and information provision.</p> <p>It will examine the provision of information on performance against contract to individual access holders on a quarterly basis. It is also examining the performance metrics that are included in the contracts and has been consulting with industry on this.</p> <p>Aurizon Network will also continue to undertake periodic condition-based assessments in the interests of accountability and improved transparency, provided the outcomes are not linked to the RAB value and the costs of the assessment can be recovered via Reference Tariffs.</p>	<p>Aurizon Network has only responded to a narrow subset of the issues raised by the QRC in its Main Submission in relation to performance and reporting. The QRC's responses to the issues raised by Aurizon Network in its Response to Industry are provided in Section 11 of Part 4 and in Annexure A.</p> <p>Annexure E provides a summary of the performance and reporting issues that Aurizon Network failed to respond to in its Response to Industry.</p>

RESPONSE TO KEY PROPOSED CHANGES

Topic	AN's Proposed Change	QRC Response
Compliance and audit	Aurizon Network has proposed amendments in response to industry feedback and has agreed to reinstate the QCA's ability to approve the auditor. It will also include an obligation regarding the nomination of a compliance officer and the responsibilities they will have in ensuring that Aurizon Network complies with its obligations under the undertaking. Aurizon Network has also agreed to provide a public version of the audit report in the most recent audit plan.	<p>The QRC appreciates Aurizon Network's preparedness to reinstate the QCA's ability to approve the auditor for compliance audits. Unfortunately, beyond this proposed change, Aurizon Network has showed little willingness to make changes to the auditing framework.</p> <p>The QRC's response to Aurizon Network's proposed changes in relation to compliance and audit is provided in Section 12 of Part 4 and in Annexure A.</p> <p>Annexure E provides a summary of the compliance and audit issues that Aurizon Network failed to respond to in its Response to Industry.</p>

Part 3 - Response to AN's "Key Themes"

This section responds to the "*key themes in submissions*" section of Aurizon Network's Response to Industry. The "*key themes*" presented are Aurizon Network's interpretation of key themes. They are, in the QRC's view, not representative of industry's key themes.

1 **The competitiveness of Queensland coal (Section 3.1 of AN's Response to Industry)**

Aurizon Network noted the current state of the commodity cycle and suggested that below rail charges represent a "*very small contributor to costs*". Aurizon Network also suggested that the view of industry is that Aurizon Network should align "*its tariffs to complement the cyclical nature of the commodities market*".

The suggestion that below rail charges are a "very small contributor to costs" is inaccurate and irrelevant. It is also an unsettling view given the urgent need for all participants in the industry to work towards improving the competitiveness of the Australian export coal industry.

It is not the QRC's view that Aurizon Network should adjust its tariffs to reflect the commodity cycle. The QRC's point is simply that the industry is moving out of a super cycle phase, in which expansions will, generally speaking, be less prevalent than over the last 5 years. Provided that Aurizon Network's costs are efficient, industry's position is not that Aurizon Network should reduce its tariffs so as to share in the burden of the downward part of the commodity cycle, but rather, that there are practical steps that should be taken to consider the prudence of expenditure. For example, is all of the planned capex really necessary? Are there maintenance practices which were put in place to cater for the pressures of the expansion phase which could be reviewed to reduce costs? These measures are not about taking returns away, but rather are about Aurizon Network considering the prudence and need for expenditure in a changed environment.

2 **Winding back protections in the regulatory framework (Section 3.2 of AN's Response to Industry)**

Aurizon Network recognised the concerns raised by industry in relation to the re-writing of UT3. Aurizon Network noted that, in its view, such a re-write was necessary because UT3 was the result of "*bolt-ons*" since UT1. The QRC agrees with this position, however, the QRC has a number of concerns regarding the re-writing of UT3, including that:

- industry was not consulted before Aurizon Network's submission of UT4;

- due to the number of incomplete items in UT3, industry felt that while UT3 was clearly not perfect, it was known to all parties and that a period of stability was attractive; and
- all of the proposed changes to UT3 benefited Aurizon Network. In a number of cases, the changes were significant.

Aurizon Network also highlighted industry's concern about the removal of both the funding obligation and oversight of access conditions by the QCA. Aurizon Network suggested that these provisions "*remain the only known examples of such provisions in any third party access regime in Australia.*" This statement is both incorrect and misleading. The QRC notes that:

- the DBCT access undertaking includes an obligation on DBCT Management to expand the terminal and to fund such an expansion at the WACC (see clause 12.5 of the DBCT access undertaking);
- the Railways Access Code of Western Australia (which applies to TPI and Brookfield Rail) requires the rail infrastructure owner to undertake and fund expansions; and
- in UT3, Aurizon Network voluntarily proposed a funding obligation.

Most importantly however, Aurizon Network's comments ignore the issue underlying the need for a funding obligation and the need for regulatory oversight of access conditions. The issue is that, unlike most regulated entities, Aurizon Network is not willing to fund significant expansions on regulatory terms. The experience of industry is that unchecked, and without an alternative, Aurizon Network will fully exploit its monopoly position. Conversely, for example, a funding obligation and regulatory oversight of access conditions has not been relevant to the ARTC access undertaking because ARTC have funded at the regulated WACC.

Lastly, Aurizon Network has included some analysis showing how, over time, the undertaking has expanded in size and (impliedly) so has regulatory oversight. The QRC has a number of comments on this:

- first, it is a matter of quality and not quantity. The DBCT access undertaking is much shorter, yet it was submitted to the QCA with the support of industry;
- second, the privatisation of the rail infrastructure necessitated a change in regulation in any event; and
- third, UT3 appears shorter because it did not include the full suite of standard access agreements, connection agreement or SUFA. It should also be pointed out that a large number of pages are for SUFA – 8 complex agreements designed by Aurizon Network.

3 Negotiate-arbitrate model (Section 3.3 of AN's Response to Industry)

Aurizon Network objected to the suggestion that UT4 is a move to light handed regulation and suggested that the QCA had a significant oversight role under

UT4. There are a number of aspects of UT4 where this is not the case. The concerns raised by industry result from a number of elements of UT4, including:

- no regulatory oversight of access conditions;
- a greater emphasis on “*commercial terms*” and agreements being reached outside the terms of the undertaking;
- the attempt to limit the discretion of the QCA in its determination of disputes by defining and restricting the matters which must be taken into account to favour the interests of Aurizon Network over the interests of stakeholders and public interest considerations;
- greater discretions for Aurizon Network (which discretions are not capable of dispute or are practically not capable of dispute); and
- no regulatory oversight of capacity analysis.

In response to the significant difficulties experienced in the telecommunications industry with the “*negotiate-arbitrate*” model (as referred to by the QRC and other industry stakeholders in submissions), Aurizon Network argue that the relevant legislative changes made to that regime do not operate “*in such a way as to remove ‘negotiate-arbitrate’*”. This is incorrect. Indeed, the right for the ACCC to arbitrate disputes under access agreements has been entirely removed from Part IXC of the CCA. In its place, the ACCC has been given a power to set access terms upfront through access determinations¹ and, in the event of issues later becoming apparent, the ACCC may also issue ‘binding rules of conduct’ (**BRoC**)² which directly bind Telstra.

4 The impact of privatisation (Section 3.4 of AN’s Response to Industry)

Aurizon Network suggested that privatisation of the Aurizon Group has benefited industry because it now has a focus on efficiency, growth and maximising performance.

Industry agree that for unregulated businesses (such as Aurizon’s above rail business) there is a strong efficiency and cost saving incentive. However, for a monopoly with a revenue cap, there is little incentive to be efficient or save costs. The incentive for a monopoly with a revenue cap is to increase the asset base, and obtain above regulatory returns.

Industry’s experience of the Aurizon Group following privatization has been:

- a desire to participate in all parts of the supply chain;
- a greater focus on leveraging the integrated model and therefore tension on ringfencing and similar;

¹ CCA, section 152BC.

² CCA, section 152BD.

- a view that Aurizon Network will only invest in significant expansions at above regulatory returns;
- significantly higher corporate overheads; and
- a greater focus on increasing profits.

5 AN's influence over the development path (Section 3.5 of AN's Response to Industry)

Aurizon Network said that it has *“been suggested that Aurizon Network is seeking to control the outcome of the entire development path”*. Aurizon Network's response seeks to provide reassurance that *“Aurizon Network has never sought to exercise any degree of undue influence over the timing of developments and is hopeful that a redrafted Part 8 will put this commitment beyond question”*.

The QRC's objective in this area is to ensure that Aurizon Network cannot exercise inappropriate influence over the development path. Part 8 and the ring-fencing provisions are key to ensuring this outcome. Many of the concerns raised in relation to these areas arise from Aurizon Network's participation (or planned participation) in ports, above rail and connecting infrastructure, and from Aurizon Network's pursuit of above-regulated returns. The revised Part 8 does not fully address these concerns, for the reasons set out in Annexure C.

6 The case for changing UT3 (Section 3.6 of AN's Response to Industry)

The QRC accepts that it is Aurizon Network's prerogative to propose UT4. The draft of UT4 which has been put forward is very unbalanced. The QRC is concerned with the amount of power and discretion which is proposed to be left with Aurizon Network, as well as the shift in prices.

7 Accountability for compliance (Section 3.7 of AN's Response to Industry)

One of key themes in the QRC's Main Submission and in the submissions made by other industry members was the lack of transparency and accountability inherent in the UT4 framework. In its Response to Industry, Aurizon Network responded to this concern by commenting that *“all of the key accountability mechanisms from UT3 have been retained”* in UT4.

The QRC considers this comment to be misleading for a number of reasons:

- first, the comment proceeds on the false assumption that all accountability mechanisms in UT3 are workable and sustainable. This is not the case (e.g. ringfencing regime) and Aurizon Network has made this concession on a number of occasions (including in Section 3.6 of its Response to Industry);

- second, although Aurizon Network may have maintained the UT3 accountability mechanisms, it has often amended them in a way that has weakened their effectiveness (e.g. the reporting and auditing regime); and
- third, since the approval of UT3, the conflict risks created by the Aurizon Group's integrated model have been substantially heightened (the QRC has addressed this issue in depth in Section 4 of Part 4, below).

Accordingly, in the QRC's view, it is appropriate for UT4 to contain a significantly stronger compliance regime than what is currently proposed.

In Section 3.7 of its Response to Industry, Aurizon Network listed what it considered to be the key accountability mechanisms in UT4. The QRC's responses to the items listed by Aurizon Network are set out in Annexure F.

Part 4 - Response to key issue responses

1 Scope of UT4 (Section 4.1 of AN's Response to Industry)

As set out in its Main Submission, the QRC supports the broadening of the scope of UT4. Aurizon Network's Response to Industry addressed two key issues in this respect – the regulation of “*associated services*” and the supply of electricity. These issues are addressed below.

1.1 Associated Services

In its Main Submission, the QRC requested that UT4 include an obligation on Aurizon Network to perform certain services that the QRC considered to be directly associated with the provision of access under UT4. The QRC proposed an exhaustive definition of such “*associated services*” which included RIM and train control, level and other crossing services, land leases and design, scope and standard reviews. In its Response to Industry, Aurizon Network stated that “*the request for Aurizon Network to volunteer what are unregulated services into the regulatory regime cannot be accepted*”.

Aurizon Network also stated that “*Aurizon Network has consistently indicated in discussions with industry that it is happy to work with them on negotiating terms on which it provides all of its services.*” If this is the case, but Aurizon Network are not agreeable to including these services in the undertaking, where will this agreement live?

In addition to the arguments raised by the QRC in Part 2 of its Main Submission, the QRC notes that:

- the QRC does not accept that the “*associated services*” are unregulated services. Their exclusion from UT3 is not relevant given that the issue has not arisen previously. In the QRC's view, the scope of the declaration in relation to “*Access*” is drafted in broad terms (as reflected in section 250 of the QCA Act) and may feasibly include the “*associated services*”. The QRC is presently giving further consideration to this issue; and
- irrespective of the scope of the declaration, the QRC suggests that Aurizon Network should volunteer the “*associated services*” as part of UT4. Establishing a process in respect of the “*associated services*” in the undertaking will be efficient for all parties.

In its Main Submission, the QRC proposed a full framework for the provision of “*associated services*” which was not considered by Aurizon Network in its Response to Industry. The QRC would like to engage further with Aurizon Network and the QCA in relation to this framework.

1.2 Electricity Supply

The QRC requested the following amendments to the electricity supply regime under UT4 in its Main Submission:

- the reinstatement of an obligation on Aurizon Network to supply electricity to access holders on reasonable terms and conditions; and
- the reinstatement of a dispute resolution mechanism for disputes arising in respect of electricity supply.

These concepts were both included in UT3.

Aurizon Network's Response to Industry did not consider either of these issues and outlined only minor drafting amendments to improve clarity in relation to the recovery of costs.

The QRC does not agree with Aurizon Network that *"the UT3 commitment to sell electric energy for the operation of train services... has not fundamentally changed"* in UT4 and relies on its Main Submission in this respect.

2 Relationship between access agreements and UT4 (Section 4.2 of AN's Response to Industry)

In Section 4.2 of its Response to Industry, Aurizon Network provided some general commentary on its rationale for allocating obligations as between UT4 and the standard access agreements.

The QRC provides the following comments in response:

- the QRC generally supports the streamlining of UT4 and the standard access agreements and is in favour of the removal of duplication where appropriate;
- the QRC does not consider there to be a set of principles applicable to determining the proper allocation of subject matter as between UT4 and the standard access agreements. Whether an obligation should be included in UT4, the standard access agreements or both, requires case-by-case consideration;
- in relation to Aurizon Network's comments regarding its Part 3 (Ringfencing) obligations, the QRC considers UT4 to be particularly deficient in this respect. The QRC provided a re-draft of Part 3 in its Main Submission and supports the incorporation of a significantly more comprehensive conflicts protection regime in UT4; and
- in its Main Submission, the QRC provided a detailed Mark-Up of both UT4 and the AHAA. The QRC's Mark-Up of those documents currently reflects the QRC's position in relation to the allocation of obligations as between UT4 and the standard access agreements.

Under the QCA Act, terms incorporated into an undertaking are 'stronger' in effect than terms set out only in an access agreement. The scope of the QCA's investigation and enforcement powers are stronger in respect of an undertaking than an access agreement and the Court's powers to grant remedies are wider,

including scope for compensation orders. As Aurizon Network concedes (at page 19 of its Response to Industry), the QCA's role under access agreements is limited to approving the standard form of agreement and then ensuring that activities under the access agreements do not breach the high 'non-discrimination' threshold in section 104 of the QCA Act. At most, the QCA may play a role in arbitrating disputes – but even this is subject to the consent of Aurizon Network (a point conceded at page 23 of its Response to Industry). The role of the QCA in directly investigating and enforcing the terms of access agreements themselves is therefore weak and indirect, at best.

This is very different to the undertaking. The QCA has wide powers to investigate obligations under the undertaking, which are not available to access seekers. This is a critical factor in determining the 'balance' to be struck between the documents. Similarly, a breach of the access agreement is likely to sound only in damages (and will require the access seeker to establish loss, which will not always be straightforward in relation to issues such as non-discriminatory behaviour), whereas a breach of the undertaking (and therefore the Act) gives rise to a wider set of remedies.

An application in relation to a contravention of the undertaking can also be brought by any person who has been adversely affected, whereas an access dispute needs to be triggered by a party to the contract or the QCA (although others may be able to participate once it has commenced).

For these reasons, all key obligations of general application and importance to all of industry and/or for which the QCA is the appropriate body to investigate and enforce non-compliance (rather than just overseeing disputes) should be included in the undertaking and not only in access agreements.

The QRC notes that Aurizon Network intends to undertake a further review of this issue after receiving additional feedback from industry. The QRC will continue to engage with Aurizon Network on this issue and is willing to provide Aurizon Network with any reasonable assistance required.

3 Non-discrimination principles (Section 4.3 of AN's Response to Industry)

In its Response to Industry, Aurizon Network proposed three changes to the non-discrimination provisions in UT4. While the QRC appreciates Aurizon Network's attempt to compromise, the proposed changes do not address the nub of industry's concerns.

The first two changes proposed by Aurizon Network (the first and second dot points in Aurizon Network's Response to Industry) are simply a restatement of existing obligations.

The third dot point (extending the operation of the non-discrimination clause to the Aurizon Group's other upstream and downstream businesses) is meaningful.

It does not however go far enough – in particular, it should be extended so as to apply to the ringfencing provisions too.

The QRC considers that Aurizon Network should adopt some of the clauses proposed by the QRC in its Main Submission (see section 3.2 of the QRC’s Main Submission).

4 Ringfencing (Section 4.4 of AN’s submission)

In its Main Submission, the QRC proposed substantial amendments to the ringfencing provisions of UT4 (Part 3 of UT4).

While acknowledging the importance of “*a robust ringfencing regime*” for a vertically integrated business such as the Aurizon Group, Aurizon Network considered:

- that the QRC’s ringfencing provisions exceeded the legislative basis for ringfencing under the QCA Act and that such provisions could not be enforced on Aurizon Network;
- the QRC had not shown why the ringfencing regime proposed by Aurizon Network failed to meet the requirements of section 138 of the QCA Act; and
- the regime originally proposed by Aurizon Network in UT4 to be “*appropriate, clear and workable*”.

4.1 Why industry is so concerned with ringfencing

Industry is very concerned with the ringfencing provisions proposed by Aurizon Network for a number of reasons:

- first, the below rail service is the central component of each coal chain. Access to a multi-user port cannot be obtained without below rail capacity. Enjoyment of above rail capacity is dependent on below rail capacity. Despite the connection provisions of UT4, Aurizon Network exercises significant power over the connection of new unregulated infrastructure;
- second, industry has little confidence in the current or proposed ringfencing regime. It does not appear effective to control information or create a level playing field. At a macro and micro level there is little confidence that other relevant Aurizon Group activities (such as above rail, port and new rail infrastructure) will not be preferred or benefited;
- third, the current ringfencing provisions (i.e. UT3) and that proposed by Aurizon Network in UT4 are complex and difficult to apply. Under these regimes ringfencing is form over substance; and
- fourth, the Aurizon Group continually promotes the integrated nature of its business. The Aurizon Group has three “*strategic pillars to success*”.³ The second pillar is to “*operate, develop and integrate bulk supply*”.

³ Please see the Aurizon 2013 Annual Report.

chains".⁴ The third pillar is to "maximise the value of freight and logistics",⁵ including "terminal work" and "ports". The Aurizon Group's long term goal is to "operate highly efficient and integrated mine to port supply chains".⁶ The Aurizon Group's short term goal is to reduce the ratio of operating costs to sales revenue ("the drive to 75"⁷). Industry is concerned that the current and proposed ringfencing regime is inadequate to regulate activities of a privatised integrated business, whose goals are so tied to leveraging an integrated model.

4.2 Legislative basis for ringfencing

Aurizon Network has described the legislative basis for ringfencing in a narrow sense, as follows:

- "to not unfairly differentiate between access seekers"; or
- "to prevent or hinder a user's access to a declared service in specified circumstances".

Aurizon Network has quoted section 137(1A) of the QCA Act as the primary basis for inclusion of a ringfencing regime in UT4. However, as noted by Aurizon Network, there are a number of provisions of the QCA Act that support a ringfencing regime. Section 137(1A) is only one such provision. Another key provision is section 137(2)(ea) of the QCA Act, which states that an access undertaking may include details of:

"(ea) arrangements to be made by the owner or operator to separate the owner's, or operator's, operations concerning the service from other operations of the owner or operator concerning another commercial activity;"

Section 137(2)(ea) creates a much broader foundation for a ringfencing regime than the description given in Aurizon Network's Response to Industry (see quote above). Section 137(2)(ea) contemplates separation of arrangements relating to the services from other aspects of Aurizon Network's business. Other provisions of section 137(2), including section 137(2)(b), (ba), (e) and (f) also support the need for the separation of the regulated service from other activities undertaken by related entities of Aurizon Network. The QRC contends that the QCA Act supports a much broader ringfencing regime than that described in Aurizon Network's Response to Industry (being confined to non-discrimination and hindering or preventing access). In particular, the QRC submits that the QCA Act supports a separation of aspects relating to the service (meaning all aspects of UT4, other than limited exceptions) from Aurizon Network's other operations and the activities of related entities so far as they are in a relevant Queensland

⁴ Ibid.

⁵ Ibid.

⁶ Ibid.

⁷ Ibid.

competitive market, such as above rail, ports and non-regulated railway infrastructure.

Aurizon Network's narrow characterisation of the legal basis for ringfencing also operates on the assumption that section 137 is an exhaustive statement of what an undertaking is to include. This is a false assumption. Section 137(1A) is a statement of what an undertaking must include. Section 137(2) identifies matters that an undertaking "may" include, which are examples only. Nothing in section 137 suggests that an undertaking cannot include other matters beyond those listed. There is a long line of case law which clearly indicates that the phrase "may include" is non-exhaustive. Provided the QCA applies section 138, the QCA has the power to reject an undertaking if it believes that that undertaking does not address a matter relating to a service which the QCA considers it should. This provision is not listed in section 137.

The generally understood meaning of ringfencing supports a view that ringfencing is about separation of the arrangement relating to the services from other competitive business (and not a more narrow concept). In its discussion paper on ringfencing, the AER stated:

"Ring-fencing is the identification and separation of the business activities, costs, revenues, and decision making of an integrated entity that are associated with a monopoly element, from those that are associated with providing services in a competitive market."

It is clear that ringfencing is about separation in a broader sense than is indicated by Aurizon Network. In the QRC's view, it is clear that there should be effective and absolute separation of matters relating to the regulated below rail services and arrangements relating to:

- ports in Queensland;
- above rail services in Queensland; and
- non-regulated rail infrastructure which may connect with the regulated service.

4.3 Separation of the business and the service

Aurizon Network has sought to characterise the QRC's ringfencing regime as a separation of the business and not the service. The QRC agrees with Aurizon Network that what is contemplated by the QCA Act is a separation of arrangements relating to the service and not a separation of the business (see in particular section 137(2)(ea)). However, effective separation of arrangements relating to the services from other activities, necessitates the separation of that part of the business from other business activities. Aurizon Network's arguments in relation to the separation of the "service" as opposed to the "business" do not cure the issues raised by industry or justify Aurizon Network's proposed inadequate ringfencing regime.

4.4 Aurizon Network’s proposed regime

The ringfencing regime proposed by Aurizon Network is substantially based on the ringfencing provisions of UT3. Aurizon Network suggested that amendments have been made to the UT3 provision because the UT3 version was “*unclear and overly complex, leading to a lack of certainty and practical application for both Aurizon Network and customers*”. The QRC agrees that the UT4 ringfencing provisions are clearer than the UT3 version. The QRC disagrees however that the complexity has now been removed and that the provisions are now practical and effective.

In the QRC’s view, the ringfencing provisions remain ineffective. This is compounded by the fact that since approval of UT3, the risks created by the Aurizon Group’s integrated model have been substantially heightened. The heightened concern with the nature of the Aurizon Group’s integrated business model are evident from the Aurizon Group’s stated business goals (which are summarised above at section 4.1). In the QRC’s opinion, the proposed ringfencing provisions are weak, whereas the commercial incentive offered by integration (above rail, ports and other rail infrastructure) are strong (and clearly fundamental to Aurizon Network’s short term and long term goals).

4.5 Aurizon Network’s response to industry’s proposed changes

The QRC’s response to each of Aurizon Network’s comments are listed below:

Aurizon Network comment	QRC response
Aurizon Network noted that obligations cannot be imposed on it that “ <i>are not supported by the legislation</i> ”.	The QRC considers that Aurizon Network have taken an overly restrictive and incorrect interpretation of the QCA Act and the intention of ringfencing. It is open to the QCA to impose a broader ringfence than proposed by Aurizon Network. In the QRC’s view, a broader and more effective ringfence is justified.
Aurizon Network suggested that stakeholders have failed to explain “ <i>why Aurizon Network’s drafting fails to meet the requirements of section 138</i> ” of the QCA Act.	The QRC disagrees that it is necessary for stakeholders to explain why Aurizon Network’s drafting fails to meet the requirements of section 138. The role of stakeholders is simply to provide its comment on whether they consider the ringfencing provisions are appropriate and effective. As is noted by Aurizon Network, ineffective ringfencing is a key theme in industry submissions. The depth of that sentiment is indicative of a lack of confidence in the current and proposed regime. In any event, the QRC’s explanation of why the ringfencing provisions fail to meet the

requirements of section 138 is set out above.

Aurizon Network noted that it is willing to make two concessions:

- making it clear that the purpose of Part 3 includes regulating the provision of access by Aurizon Network independently from other members of the Aurizon Group who compete in upstream or downstream markets; and
- a prohibition on short term secondments of employees in high risk competition area.

The QRC appreciates the compromise proposed by Aurizon Network. It is difficult to properly assess the proposed compromise without the drafting, but based on the principles described it seems like a small and inadequate compromise.

In relation to the first dot point, it is appreciated that the “*purpose*” of the ringfence will be clarified, but what industry is seeking is a meaningful and effective regime (not an adjustment to the purpose).

General statements of “*purpose*” of this kind, whilst helpful for interpreting the undertaking, are not capable of being directly investigated or enforced.

In relation to the second dot point, the continued crossover of people is symptomatic of a culture of non-compliance. The QRC considers it appropriate that all secondments be prohibited other than specific approved secondments.

Aurizon Network noted that it is willing to continue to discuss the ringfencing regime with industry.

The QRC appreciates Aurizon Network’s willingness to discuss the ringfencing regime. The QRC notes that in all discussions to date Aurizon Network has not indicated any willingness to materially move from the position it has put forward in UT4 on ringfencing.

5 Dispute resolution (Section 4.5 of AN’s Response to Industry)

In its Main Submission, the QRC proposed a number of amendments to Aurizon Network’s UT4 dispute resolution provisions. The QRC’s amendments were aimed at broadening the scope of the dispute resolution framework and improving various procedural elements of the framework.

In its Response to Industry, Aurizon Network acknowledged some but not all of industry’s concerns. This New Submission will only deal with the areas in which Aurizon Network has responded to the QRC’s proposal.

5.1 Application of the dispute resolution framework

In its Main Submission, the QRC was particularly concerned with the changes made in UT4 in relation to the general application of the dispute resolution framework. The QRC considered those changes to unnecessarily restrict the

application of Part 11. This was of particular concern to the QRC given dispute resolution is an integral component of the accountability of Aurizon Network to users, and it is imperative that users have the ability to refer a broad range of matters to dispute resolution.

In its Response to Industry, Aurizon Network acknowledged the importance of the dispute resolution mechanism. Aurizon Network has interpreted the concerns of the application of Part 11 to be a result of different interpretations of the drafting of Part 11, as opposed to being reflective of the true intention of Aurizon Network. Aurizon Network has committed to make "*minor clarifications to the drafting*" of Part 11 to "*put beyond doubt that Aurizon Network does not intend to restrict access to dispute resolution*". The QRC supports Aurizon Network's proposal, however, is unable to comment on the effectiveness of Aurizon Network's proposed "*minor clarifications*" until further drafting is provided. Nevertheless, the QRC considers this issue can be resolved as both the QRC and Aurizon Network are committed to developing a more robust dispute resolution framework.

5.2 Scope of the dispute resolution mechanism in Part 11 (Section 4.5.1 of AN's Response to Industry)

(a) Dispute resolution in relation to disputes arising under Part 8

In Part 8 of its Main Submission and in the QRC's Mark-Up of Part 8 of UT4, the QRC proposed a number of amendments to increase the application of dispute resolution for expansion related disputes. The QRC's proposal included an ability to refer matters throughout each phase of the expansion process to dispute resolution in order to achieve greater objectivity. The QRC considers that those changes are entirely appropriate given the impact which Aurizon Network's determination on access may have on access seekers.

Aurizon Network has acknowledged the QRC's concerns and has proposed to include a number of specific dispute resolution clauses in Part 8. However, in reviewing Aurizon Network's updated draft of Part 8, the QRC does not agree that Aurizon Network has made all necessary changes.

In particular, Aurizon Network has undermined dispute determinations made under Part 11 in relation to its obligations to fund, construct or permit expansions by providing that such determinations cannot be inconsistent with section 199 of the QCA Act. In effect, this means that dispute determinations made by the QCA or an expert must, for example, be consistent with Aurizon Network's "*legitimate business interests*". As discussed in Part 8 of the QRC's Main Submission, subjecting dispute determinations to broad and ambiguous tests such as "*legitimate business interests*" and "*commercial objectives*" undermines the recourse to an otherwise objective and independent dispute resolution process. Most importantly however, the "*legitimate business interest*" test conflicts with the detail and prescription agreed to in Part 8. The person adjudicating a dispute in respect of Part 8 should apply the provisions of Part 8, and not be subject to an overarching exception.

Aurizon Network has also failed to include a right to refer to dispute resolution any decision by it not to move to a feasibility study on the request of access seekers. As noted in Part 8 of the QRC's Main Submission, the QRC considers that the criteria to move between concept, pre-feasibility and feasibility studies is currently controlled by Aurizon Network. Access seekers need a right to dispute Aurizon Network's decision not to progress a project to the next study stage.

For these reasons, the QRC considers further changes are required to Part 8 in relation to the operation of the dispute resolution process set out in Part 11.

(b) Accessibility of dispute resolution to various parties

The QRC generally agrees with Aurizon Network's proposal to clarify when the dispute resolution mechanism and complaints handling process should be open to parties other than access seekers and train operators. The QRC will review the substance of these amendments once provided by Aurizon Network.

5.3 Dispute resolution under access agreements (Section 4.5.2 of AN's Response to Industry)

The QRC appreciates Aurizon Network's further explanation of the dispute resolution process under the standard access agreements. The QRC has proposed to expand the circumstances in which a party can refer a matter to dispute resolution under the standard access agreements as reflected in the QRC's Mark-Up of the AHAA. The QRC is otherwise agreeable to Aurizon Network's understanding of the QCA's involvement in resolving disputes under the standard access agreements.

5.4 Compliance with the ringfencing framework (Section 4.5.3 of AN's Response to Industry)

The QRC agrees that the proper place for the ringfencing obligations is in UT4 itself rather than in the standard access agreements. Despite this, the QRC considers that the ringfencing obligations proposed by Aurizon Network are insufficient.

The QRC has addressed the issue of non-compliance with ringfencing obligations in Part 3 of the QRC's Main Submission, as well as the re-draft of Part 3 which accompanied the Main Submission.

6 Expansions (Section 4.6 of AN's Response to Industry)

6.1 Expansion process

Aurizon Network's Response to Industry included a partial re-draft of Part 8 of UT4. The QRC acknowledges that Aurizon Network has accepted the principles of a number of changes which the QRC had proposed to Part 8. It should be recognised however that the original draft expansion process included in UT4 was very one-sided. The extent of change proposed by Aurizon Network is therefore not indicative of a balanced document. Like a large part of UT4, it is a movement from an ambit position.

This New Submission includes the QRC's Mark-Up of Aurizon Network's partially revised Part 8 drafting (please see Annexure D). Industry have also prepared a table describing the changes that it believes are necessary to Aurizon Network's proposed new Part 8 – this is set out in Annexure C.

The QRC responds to the six dot points included in Aurizon Network's Response to Industry as follows:

Aurizon Network comment	QRC response
<p>Aurizon Network proposed that its obligations in Part 8 be subject to a legitimate business interest test.</p>	<p>The QRC considers this to be inappropriate. Part 8 sets out a detailed process in relation to expansions. Aurizon Network's legitimate business interests should be protected through specific provisions and not a general or blanket provision as proposed. Making the detailed provisions of Part 8 subject to a vague general catch-all undermines the purpose of a detailed process.</p> <p>In a similar vein, the QRC notes that Aurizon Network has retained the provision which enables Aurizon Network to agree an arrangement with an access seeker outside of the process provided for in Part 8. The process in Part 8 ensures everyone is treated fairly. It also ensures that Aurizon Network's monopoly power is kept in check. If Aurizon Network can agree a process outside of Part 8 there is scope for Aurizon Network to utilise its monopoly position. It would also undermine the objective criteria set out in the Part 8 process.</p>
<p>Aurizon Network wants to have the option to fund prefeasibility and feasibility studies.</p>	<p>The QRC considers that the right approach is for only access seekers or its customers to fund prefeasibility and feasibility studies. There are two reasons for this approach:</p> <ul style="list-style-type: none"> • first, it ensures that only those access seekers / customers that genuinely require capacity participate in the project. Historically, some access seekers have participated in study projects to retain an option and to show progress for their project. This adversely impacts those access seekers who also genuinely require capacity, as projects are unrealistically scoped; and • secondly, where Aurizon Network can fund prefeasibility and feasibility studies, it is able

to progress projects without the involvement of customers / access seekers and outside of the processes provided for in Part 8.

Access seekers chosen to fund a study are selected through a clear process with specified criteria.

Subject to the QRC's comments on the drafting outlined later in this New Submission, the QRC supports the principles of this dot point.

Aurizon Network proposed that Aurizon Network must consult with access seekers and agree on scope.

Subject to the QRC's comments on the drafting, the QRC support this principle.

Aurizon Network proposed that the scope of expansions will be agreed through consultation, agreement and/or resolution of user funding schedules or standard access agreements.

The QRC's view is that the scope of work for all expansions (whether user funded or not) should be agreed and failing agreement determined by an expert. Aurizon Network have proposed that only the scope for user funded projects requires the agreement of the access seeker.

After entry into the first SUFA agreement, Aurizon Network proposed to review the SUFA suit.

If following such a review Aurizon Network do not propose any changes to the SUFA suite, it should make a submission to the QCA explaining why changes are not necessary.

6.2 Expansion funding

Aurizon Network has removed the \$300m expansion funding commitment that was included in UT3 and has erroneously suggested that no other regulated infrastructure owner has a mandatory funding obligation. The QCA will be aware that DBCT Management has an obligation to fund expansions of the DBCT. Whilst ARTC do not have a funding obligation, the ARTC readily fund the regulated WACC without any difficulty.

Aurizon Network noted that there is a *“fundamental distinction between facilitating or enabling expansions of the network (which remains Aurizon Network's core responsibility) and who bears the costs of those expansions”*. This statement is misleading. The need for some form of funding obligation arises because absent SUFA there is no ability to effect an expansion of the network. The only party that can effect an expansion of the network is the Aurizon Group. As is discussed in the QRC's SUFA submission, SUFA (if it can be fixed) will only be suitable for a very small percentage of projects. The Aurizon Group has publicly and privately disclosed its intention to only undertake major expansions at a premium to what the regulator has approved. Aurizon Network have a commercial interest to ensure that only it can effect expansions of the network. If an effective mechanism could be found for others to feasibly fund expansions

there would be competition for expansion funding and no need for a funding obligation. Aurizon Network cannot have it both ways – blocking the ability for others to fund and no funding obligation.

Finally, Aurizon Network noted that it hopes that a negotiated solution can be achieved in the short term. The QRC shares this wish, but industry's experience on this issue and SUFA does not give cause for optimism.

6.3 Expansion pricing principles

The QRC's comments on the expansion pricing principles are set out in the QRC's Main Submission. Those submissions stand.

The QRC notes Aurizon Network's acceptance of the QRC's principles and willingness to continue to work with the QRC on the expansion pricing principles. Discussions on this issue to date have been productive and the QRC is hopeful that the agreed principles can be developed into agreed drafting. The issue (and required drafting) is necessarily complex. Given the complexity and the progress currently being made, we would suggest that (for this issue only), the QCA, in any draft decision, provides guidance on the principles which the QCA would support, rather than seek to prepare detailed drafting.

6.4 Expansion process is not integrated with capital planning (i.e. Network Development Plan)

The QRC reiterates concerns it and other stakeholders have previously raised about the need to have an integrated 'end to end' capital planning and expansion process.

It is critical that there are clear links between the NDP process and both the expansions and capital pre-approval processes. This will allow the industry to have confidence that it can predict with reasonable accuracy how Aurizon Network will provide for capacity growth over the medium to long term. Industry should not be 'surprised' (as it has been in the past) by the scope or nature of new capital or expansion projects or those for which pre-approval has been sought. Aurizon Network should therefore be required to be transparent and detailed about various capacity options for developing its network.

The changes proposed by Aurizon Network in its partial draft of Part 8 currently do not address this issue. For example:

- **There is no link between the Network Development Plan or the capacity review process and the expansion process.** Aurizon Network should be required to develop expansion planning in accordance with the project pipeline and capacity planning set out in the NDP, or explain to industry why it is not doing so and the benefits of any alternative. Without this clear link, the NDP is of little or no value.
- **There is no link between the Network Development Plan and the capital pre-approval/customer voting process.** Aurizon Network should not be able to seek capital pre-approval for projects which have

not previously been disclosed in the NDP to the industry, unless separate approval is sought from the QCA.

- **Aurizon Network is under no obligation to use its published system operating assumptions or capacity review results as the principle input for expansion planning (i.e. as an input in concept studies).** This significantly limits the value of both the NDP and system operating assumptions and limits the extent to which they can be relied upon by the industry.

7 Negotiation framework (Section 4.7 of AN's Response to Industry)

In its Main Submission, the QRC proposed a number of improvements to the negotiation framework in UT4. The QRC's proposed amendments were aimed at strengthening the negotiation framework in an attempt to ensure an objective and transparent process.

In its Response to Industry, Aurizon Network agreed to a number of the QRC's proposals, however, left other proposals unanswered. Aurizon Network's proposed changes are discussed as follows:

- Aurizon Network has agreed to include a mandatory requirement for it to notify an access seeker if their access application is incomplete. The QRC supports this change and considers this amendment will allow for the expeditious and efficient completion of access applications to allow for the negotiation of access rights in a timely manner;
- Aurizon Network has agreed to place "*reasonable limitations*" on the additional information it may request from an access seeker in relation to an access application. The QRC appreciates Aurizon Network's preparedness to consider restricting the additional information that may be sought but is unable to comment on the substance of this proposal until such "*reasonable limitations*" are defined;
- the QRC appreciates Aurizon Network's agreement to provide reasons for the suspension of access negotiations;
- Aurizon Network has agreed to consider circumstances in which an access seeker should be permitted to review and revise its access application. The QRC appreciates Aurizon Network's preparedness to consider "*possible exceptions*" to the prohibition on reviewing and revising an access application, however, the QRC is unable to assess Aurizon Network's proposal unless and until more information is provided. The QRC considers an access seeker should be permitted to vary its access application before and after the provision of an indicative access proposal, as well as during the negotiation period. Finalising an access agreement takes some time, and during that time, planning progress will often cause information contained in an access application to become obsolete. Allowing an access seeker to revise its access application will remove unnecessary delay and ensure Aurizon Network is made aware of the most current information available. However, the QRC also understand that certain revisions (such as a significant change in load point, or a substantial increase in the required train

paths) effectively represents a different access application rather than a revision;

- Aurizon Network has agreed to include a new obligation for it to provide information on expansions in an indicative access proposal where relevant. Aurizon Network has also agreed to include more information on how an access charge has been determined under an indicative access proposal. The QRC appreciates Aurizon Network's willingness to make these changes and considers this will provide greater transparency and assist access seekers with mine and project planning;
- the QRC appreciates Aurizon Network's agreement to allow an access seeker a mutual right to suspend the negotiation process where access is dependent on an expansion or customer specific branch line; and
- the QRC proposed a number of changes aimed at improving the objectivity of various criteria applying to Aurizon Network's decision making powers under Part 4. In response, Aurizon Network has shown a willingness to develop more objective grounds for its decisions. The QRC is unable to comment on the effectiveness of Aurizon Network's proposed changes until Aurizon Network communicates how it intends to achieve more objectivity.

Despite the above, there are a number of key amendments proposed by the QRC which remain unanswered by Aurizon Network or otherwise remain in disagreement between the parties. These issues are set out in Part 4 of the QRC's Main Submission, as well as the corresponding Mark-Up of Part 4. Further discussion can also be found in the QRC's response to Annexure A set out in Annexure A of this document. Examples of issues not addressed are listed in Annexure E and include:

- the QRC's proposal to expand the provisions dealing with a train operator entering into a train operations agreement so that those provisions more broadly encompass rail haulage operators contracting under a standard access agreement (operator);
- the QRC's proposal to expressly acknowledge that a rail haulage operator may only apply for access, or hold access rights, where this is done for a specified customer (and with the support of the customer); and
- the QRC's proposal to improve the definition of "*Customer*".

8 Demonstration of supply chain capacity (Section 4.8 of AN's Response to Industry)

Aurizon Network has introduced a new information requirement in UT4 requiring the provision of information or evidence as to an access seeker's ability to fully utilise the requested access rights. An access seeker must provide information or evidence as to its ability to secure access to a port, existence of a rail haulage contract and other private infrastructure rights. This information is required during the application and negotiation process and is relevant to Aurizon Network's decision as to how to manage and allocate capacity.

In its Main Submission, the QRC outlined its concern in relation to the drafting of this requirement in various parts of UT4. In particular, Aurizon Network's proposed drafting fails to acknowledge that at the time an access application is made and during the negotiation period, it is unlikely an access seeker would actually hold the ancillary contractual rights which it is required to provide information or evidence about.

In its Response to Industry, Aurizon Network acknowledged these concerns and in particular, the *"interdependencies between the various components of the supply chain"*. Aurizon Network suggested the drafting reference to the *"likelihood"* of securing access rights reflects its intention not to impose obligations beyond that reasonably required. Nevertheless, Aurizon Network has proposed to review the drafting of UT4 and clarify the extent to which an access seeker is required to prove its supply chain rights.

The QRC is not convinced that the use of *"likelihood"* is alone sufficient to overcome these issues. The QRC appreciates Aurizon Network's willingness to undertake a review of the current drafting. The QRC proposes drafting amendments need to be made to more accurately capture Aurizon Network's intention not to impose unreasonable obligations on access seekers in relation to demonstrating supply chain capacity. An appropriate solution may include requiring an access seeker to provide evidence of a reasonable likelihood of obtaining the necessary ancillary contractual rights by the time the access rights are to commence. The QRC also considers that reference to whether an access seeker has sufficient facilities (including rollingstock etc.) should be removed. It is not Aurizon Network's place to scrutinise whether an access seeker (or a prudent and appropriately credentialed haulage provider) has sufficient facilities to enable the use of the relevant capacity in circumstances where an access seeker has provided evidence or information of a rail contract.

9 Allocation of existing capacity (Section 4.9 of AN's Response to Industry)

Under UT4, the queuing framework has been dismantled in favour of the use of capacity allocation criteria. The QRC generally agrees with this shift towards the use of capacity allocation criteria, however, disagrees with the discretion and subjectivity currently evident in the drafting of this criteria by Aurizon Network.

9.1 General requirements for capacity allocation

In its Main Submission, the QRC proposed a number of amendments to the drafting of the capacity allocation criteria as it relates to the requirement of an access seeker to demonstrate an ability to fully utilise the access rights requested. This issue is discussed by the QRC at Section 8 above.

9.2 Mutually exclusive access application criteria

The removal of the queuing framework has also resulted in the capacity allocation criteria being applied to resolve mutually exclusive access applications.

UT4 contemplates that where mutually exclusive access applications meet certain factors, or where none of the applications meet the relevant criteria, Aurizon Network will enter into negotiations with those access seekers who best meet Aurizon Network's "*legitimate business interests*". There are also a number of detailed objectives which Aurizon Network is entitled to consider in this context.

As provided in its Main Submission, the QRC disagrees with the discretion afforded to Aurizon Network in applying the relevant criteria, and in particular, disagrees with the inclusion of the following factors:

- Aurizon Network's legitimate business interests;
- highest marginal value; and
- revenue adequacy.

In its Response to Industry, Aurizon Network has agreed to remove the first two factors listed above, but retain revenue adequacy as a relevant consideration. The QRC appreciates Aurizon Network's willingness to compromise on this matter and agrees to retain revenue adequacy (as it is currently drafted in reference to the pricing principles under Part 6). Aurizon Network has also demonstrated a willingness to make the criteria exclusive, in accordance with the QRC's proposal. The QRC considers these changes will remove some of Aurizon Network's discretion, and ensure more transparency and objectivity in the decision making process. The QRC is however concerned with Aurizon Network's comment that it will "*consider whether any more matters are required to be listed*" in the criteria. For this reason, the QRC is unable to undertake a proper assessment of Aurizon Network's proposed changes to the capacity allocation criteria until Aurizon Network communicates any additional matters its requires to be included.

10 Flexibility in managing access rights (Section 4.10 of AN's Response to Industry)

Aurizon Network's Response to Industry addressed two key issues in relation to flexibility in managing access rights – short term capacity swaps and operator capping. These issues are addressed below.

10.1 Short term capacity swaps

The QRC is pleased with Aurizon Network's willingness to further explore and develop a short term capacity swap mechanism (**STCSM**) for inclusion in UT4.

Save for the following comments, the QRC agrees with the key features of the STCSM proposed by Aurizon Network in the body of its Response to Industry:

- the QRC does not consider that the STCSM should be implemented via the system rules. In the QRC's view, the existing system rules are inefficient and difficult to interpret;

- in the QRC's view, the STCSM must include a capacity analysis process to be effective; and
- the concept of no party being "*worse off*" will require further development. For example, if there is a transfer from a senior mining company to a junior, will Aurizon Network be considered to be "*worse off*"?

The QRC acknowledges that the principles outlined by Aurizon Network were only proposed as a starting point and that the matter is to be progressed in consultation with industry. The QRC is willing to engage further on this issue.

10.2 Operator capping

The QRC does not support the inclusion of an operator capping ToP regime in UT4. The QRC raised a number of concerns regarding Aurizon Network's UT4 operator capping proposal in its Main Submission which were not addressed by Aurizon Network in its Response to Industry. These concerns included that:

- there is a lack of clarity around how operators are to allocate savings amongst their customers;
- the regime is not equitable in that a particular customer may benefit from a ToP offset where the TSEs for one origin/destination are exceeded simply on the basis of a nomination, whereas other users of the system, and other customers of the same operator, may receive no benefit at all;
- the ability for operators to nominate ToP groupings as late as May in each year will likely result in groupings being more of an accounting fiction rather than an operational arrangement; and
- the flexibility afforded to end users to vary the nomination of path usages between operators may be reduced given the need for end users to request that TSEs form part of their operators' take or pay groupings.

In the QRC's view, a more practical way for access holders to manage ToP exposure is through the inclusion of a flexible short term capacity transfer mechanism (as discussed in Section 10.1, above). The QRC considers that such a framework is more likely to promote the efficient use of infrastructure and properly reward those customers who take steps to make their surplus capacity available to the system.

11 Performance and reporting (Section 4.11 of AN's Response to Industry)

In its Main Submission, the QRC proposed a number of key amendments to Aurizon Network's UT4 reporting obligations centered at improving transparency and accountability under UT4. The QRC's proposed amendments included:

- the reinstatement of the quarterly operational reporting regime contained in UT3;
- the reinstatement of the ability for the QCA to publically disclose "*Below Rail*" details of access agreements (subject to the exclusion of nominated confidential information) contained in UT3; and

- the inclusion of a requirement for the format of all reports required under UT4 to be approved by the QCA in advance.

In its Response to Industry, Aurizon Network acknowledged industry's concerns regarding the need for greater transparency and made a broad commitment to improve transparency in reporting and information provision. The substance of Aurizon Network's response however, focused only on the frequency of operational reporting as well as reporting on contractual performance and maintenance and asset conditioning. These issues are addressed below.

11.1 Quarterly operational performance reports

UT3 obliges Aurizon Network to provide quarterly operational reports. Aurizon Network has sought the relaxation of this obligation under UT4 to provide annual operational reports only.

(a) The consequences of public disclosure

Aurizon Network has expressed concern that *"in being required to publically disclose operational performance data each quarter, the information could mislead the market, unless the users of that information fully understand the broader context and the potential variations in throughput levels within the year"*. Aurizon Network has also stated that it does not consider the costs involved in preparing operational reports on a quarterly basis to be justified.

The QRC and Aurizon Network are in disagreement about the likely consequences of Aurizon Network being required to publically disclose operational data on a quarterly basis. In addition to the arguments raised by the QRC in its Main Submission, the QRC notes that:

- Aurizon Network has been publishing quarterly operational reports under UT3 since the listing of AHL and neither Aurizon Network nor AHL have ever faced allegations of breaches of the ASX listing rules or corporations law in respect of that information; and
- raw operational data in and of itself is very unlikely to be misleading. Aurizon Network is responsible for the form that operational data is released in. To the extent that Aurizon Network has concerns about *"context"* and *"potential variations in throughput levels"*, these issues can be explained within a report.

There are a wide variety of listed companies that publish directly, or through the relevant regulator, detailed operational information – both publicly and, in some cases, to the industry - without raising legal issues under the Corporations Law or ASX disclosure rules.

Accordingly, the QRC does not accept Aurizon Network's justification for the relaxation of operational reporting obligations. Subject to the QRC's comments below, the QRC seeks the reinstatement of the quarterly reporting obligations contained in UT3.

(b) Aurizon Network’s alternative proposal

In recognition of industry’s concerns regarding transparency, Aurizon Network has stated that “*it is willing to look at confidentially supplying information to individual access holders on a more frequent basis [than annually]*”.

The QRC appreciates Aurizon Network’s preparedness to explore a workable solution to this issue. The QRC is willing to engage on this issue and consider an alternative framework but requires a greater level of detail to assess Aurizon Network’s proposal. Regardless, the QRC believes that access holders should be capable of using any information provided confidentially by Aurizon Network in the same way as those access holders are currently able to use publically reported information.

11.2 Contractual performance

Aurizon Network has expressed an eagerness to develop more appropriate KPI reports to be included in the standard access agreements as a means of providing customers with better information at an individual level. The QRC supports this initiative and is willing to assist Aurizon Network with this endeavour.

11.3 Maintenance and asset condition reporting

Aurizon Network considers the linking of a condition based assessment to the opening RAB value to be an “*unreasonable and unacceptable level of regulatory risk*”. In lieu of deleting the provision of the asset condition report, Aurizon Network has offered to report on the condition of the network provided that such reports have no financial or other consequence on Aurizon Network.

Aurizon Network’s proposal is wholly unacceptable to industry. Any assessment of the condition of the network should be undertaken by an independent party (and not Aurizon Network or its contractors). Such a report is of no use if it has no consequence.

There needs to be a regime where Aurizon Network is accountable for the maintenance of the network. This extends to both determining the scope of maintenance activities and the performance of those maintenance activities. The QRC is open to considering alternative methods in consultation with Aurizon Network.

12 Compliance and audit (Section 4.12 of AN’s Response to Industry)

In its Main Submission, the QRC proposed a number of amendments to the UT4 auditing framework. These amendments were aimed principally at enhancing the information available to access holders to enable effective compliance monitoring and included:

- the inclusion of mandatory annual audits of Aurizon Network’s reporting and ringfencing obligations, and a separate ability for the QCA to require an audit of each of those obligations as required;
- the ability for Aurizon Network to recover its costs of undertaking a compliance audit to be subject to the QCA’s approval; and

- the reinstatement of the QCA’s involvement in the appointment of auditors.

In its Response to Industry, Aurizon Network agreed to amend UT4 to allow the QCA to annually approve an auditor to complete the necessary compliance audits. Beyond this however, Aurizon Network showed little willingness to make any meaningful changes to the UT4 auditing framework (see Annexure A – Part 10), instead opting to make a number of broad observations only. These observations are addressed below.

12.1 UT4 auditing framework

At a very high level, the QRC and Aurizon Network appear to be in agreement about the need to abridge the information imbalance that presently exists between Aurizon Network and industry participants. In this respect, Aurizon Network has noted (and the QRC endorses) that the audit regime is critical in *“ensuring accountability and engendering confidence in the integrity of the regulatory framework”*. Where the parties differ however, is on the type of auditing framework best suited to UT4.

(a) Number of audits

Aurizon Network continues to endorse what it describes as an *“efficient”* and *“flexible”* auditing framework – a framework which removes all ongoing obligations for annual audits contained in UT3 and under which audits are triggered only at the request of the QCA. In contrast, industry’s view is that, as a matter of course, auditing should occur no less than annually.

Although the parties have not discussed this issue in their dialogue to date, the QRC is hopeful that progress can be made with further consultation in light of Aurizon Network’s acknowledgement that it *“is indifferent to the number of audits that are conducted, provided it is compensated for the costs of undertaking them”*. We note in this respect that Aurizon Network did not address the QRC’s position in relation to cost recovery in its Response to Industry.

(b) Other framework observations

The QRC can only make general responses to the balance of Aurizon Network’s observations, as follows:

Aurizon Network comment	QRC response
Aurizon Network noted that it does not support specifying matters in UT4 that will be subject to audit.	The QRC is generally in agreement with this position given the requirement for the auditor and Aurizon Network to agree an audit plan with the QCA. However, the QRC does support the inclusion of specific drafting in relation to conflicts audits (see clause 10.8 or the QRC’s Mark-Up of Part 10 in its Main Submission).

Aurizon Network noted that it does not support the inclusion of a requirement in UT4 that each year's audit should assess whether the previous year's audit recommendations have been implemented.

The QRC agrees with this position.

Aurizon Network noted that it will redraft clause 10.4 of UT4 to impose further obligations in relation to Aurizon Network's compliance officer.

The QRC supports the inclusion of additional obligations on the compliance officer (including an obligation on the compliance officer to take all steps necessary to ensure Aurizon Network is able to meet the obligations imposed by UT4) and is willing to consider alternative drafting to clause 10.4.

The QRC will assess Aurizon Network's proposed amendments when the drafting foreshadowed by Aurizon Network is provided.

Aurizon Network noted its preference for the audit plan to require the publication of an audit, rather than UT4.

The QRC agrees with this position.

13 Train Service Types (Section 4.13 of AN's Response to Industry)

In Section 4.13 of its Response to Industry, Aurizon Network provided further information on its rationale for including a new definition of "*Train Service Type*" in UT4. The QRC notes Aurizon Network's explanation and has no comments on this issue.

Part 5 - Response to UT4 revenue proposal

1 Rate of return

The QRC's submissions in relation to the rates of return are set out in its separate WACC submission.

In relation to the cost of capital, the QRC seeks a consistent and predictable application of the methodology currently used by the QCA in its calculation of the rate of return under the CQCN access arrangements (being the methodology used for valuations undertaken both before and during the privatisation process). In the QRC's view, Aurizon Network is seeking to disrupt the consistent application of this methodology in an attempt to *increase* the rate of return at a point in the commodity cycle when such a change is likely to cause significant damage to industry. The QRC will further address this issue in responding to any further material filed by Aurizon Network on cost of capital issues.

2 Operating and maintenance expenditure

The concerns outlined by the QRC in its Main Submission in respect of operating and maintenance expenditure remain. Rather than replying to the comments made by Aurizon Network in its Response to Industry, the QRC will provide a submission after reviewing the QCA's operating cost information.

3 Ballast fouling from coal

The QRC provided an outline of its position in relation to coal fouling of ballast in Part 7 of its Pricing Submission. Aurizon Network has not responded to the QRC's position. Given ballast fouling is an important issue, the QRC considers it necessary to reaffirm its position on this issue.

The QRC has identified three main issues in relation to ballast fouling:

- Aurizon Network has proposed a \$43 million adjustment to the UT4 allowable revenue to recover the net costs associated with the impairment charges and ballast undercutting costs incurred under UT3;
- Aurizon Network has proposed that, going forward, the risk of ballast fouling should be borne by access holders; and
- Aurizon Network has not provided, either to the QCA or industry, a detailed asset management plan to address current and historical legacy issues associated with ballast fouling from coal.

3.1 Adjustment for ballast fouling under UT4

The QRC does not agree with Aurizon Network's proposal to make a \$43 million adjustment under UT4 on account of ballast fouling. In the QCA's 2010 Draft Decision on pricing, the QCA decided to reduce the RAB by \$107 million, which was derived as:

“...the difference, in net present value terms, between an efficient level of ballast maintenance and the amount QR Network will need to spend over the next 7 years in order to address concerns with the condition of the ballast in central Queensland.”

Ballast fouling from coal has been a long standing issue for industry. The QRC believes Aurizon Network has sufficient levers to implement activities necessary to manage ballast fouling, including through access agreements, land licences and access undertaking amendments.

The QRC supports the QCA’s previous decisions in relation to coal fouling. Excessively fouled ballast has been reviewed by the QCA during every undertaking process. It is clear through these processes that Aurizon Network is not obtaining the design life of its track structure due to coal contamination of the ballast. For example, in the Goonyella System, Aurizon Network only gets 5 years of life out of its ballast even though the design life is 10 years.

The QRC considers the QCA’s decision to remove extra ballast cleaning costs in UT3 to be reasonable. The QCA has previously indicated that it is prepared to reconsider this decision if Aurizon Network is able to provide a comprehensive ballast management plan which identifies efficient maintenance practices, as well as preventative and environmental mechanisms, to address both legacy and future coal contamination concerns. As the owner of the rail infrastructure, the QCA identified that Aurizon Network had a responsibility to all its customers to ensure that its ballast is not excessively fouled.

In its draft decision on UT3 in December 2009, the QCA stated:

“Ballast contamination has been an issue since at least the start of the 2001 undertaking. It appears that ballast contamination is an increasing problem in terms of traffic disruptions, environmental concerns and the costs of the maintenance program. The Authority has allowed for ballast cleaning at the level incurred per GTK by ARTC in the Hunter Valley but has given QR Network the opportunity to have the allowance increased if it is able to convince the Authority that its proposed approach is the most efficient available in a whole of system context.”

Aurizon Network has not submitted a coal contamination plan as part of its asset maintenance plan, despite the QCA’s UT3 decision. The QRC is concerned that this means that Aurizon Network does not currently have a ballast asset management plan. As an immediate priority, the QRC recommends the QCA again requests the development of a ballast asset management plan in order for it to assess whether the ballast maintenance practices and costs identified by Aurizon Network are the most efficient and effective to fix the ongoing operational and maintenance problems caused by coal contamination. The issue of whether or not there are legacy issues involved would also need to be addressed by Aurizon Network.

3.2 Responsibility to manage ballast fouling in the future

Looking forward, the QRC considers that the risk and responsibility in relation to ballast fouling properly lies with Aurizon Network. In the QRC's view, Aurizon Network has both the ability and responsibility to prevent, and efficiently remediate the effects of, ballast fouling on the central Queensland rail network.

As the owner of the rail network, Aurizon Network is well equipped to control many of the contributing factors to ballast fouling by developing appropriate systems to manage the risk of coal spillage. Whilst Aurizon Network does not itself directly cause coal spillage (in the sense that it does not physically load trains with coal), as the owner of the rail network, Aurizon Network has control of, and the ability to improve, factors which contribute to ballast fouling. For example, Aurizon Network could develop improved wagon loading practices through the Standard Access Agreements and implement procedures aimed at minimising coal loss under its transfer facilities licences which govern the use of train loading facilities built on its land. By employing measures such as these, Aurizon Network has the ability to actively minimise coal loss and thereby prevent the ballast fouling problem which now exists.⁸ Aurizon Network should be encouraged to develop and implement procedures that would minimise and manage coal spillage.

3.3 Plans to manage ballast fouling

Aurizon Network's submission in respect of UT4 includes a report from Evans and Peck in relation to coal fouling. The Evans and Peck report is not a report or proposal to manage coal fouling, but a report recommending a scope of work for a study to consider the coal fouling issue.

The QRC considers that it is not sufficient for UT4 to be approved only with a scope of work for a study in relation to ballast fouling. The QRC suggests that Aurizon Network with industry consultation should develop a well-considered plan to manage coal fouling and that plan should be submitted to the QCA for consideration.

⁸ The establishment of coal veneering stations at all train loadouts in central Queensland is a good example where preventative measures are being put in place to address the coal fouling concerns of industry.

Part 6 - Comments on AN's model

The QRC wishes to make a number of general comments in response to Aurizon Network's UT4 "Coal System Aggregate" Model (as published by the QCA in December 2013) (**AN Model**).

1 Depreciation

Aurizon Network's reference tariff model proposes a departure from the existing QCA approved depreciation methodology. Aurizon Network has stated that this departure will have only a "modest" revenue impact, increasing the total MAR by less than 1% over the term of UT4. The QRC has significant concerns with both the methodology proposed by Aurizon Network and Aurizon Network's assessment of its impact.

(a) Change in methodology

Aurizon Network has not provided any commercial justification for the shift away from the existing depreciation methodology. As the QCA will appreciate, the central Queensland mining reserves are long life reserves and extend well beyond the 25 years proposed by Aurizon Network. By Aurizon Network accelerating depreciation on its central Queensland assets, existing producers' logistics costs will be heightened, allowing future producers to enter the market with the benefit of a lower value asset base. Industry does not consider this to be an acceptable outcome.

(b) Impact of change

Given the brevity of the information published with the AN Model, the QRC has been unable to undertake its own assessment of the likely impact of Aurizon Network's depreciation proposal. The QRC requests that the QCA test Aurizon Network's model against the existing approved methodology and provide an assessment of the revenue impact for industry to consider.

2 Impact of changes to the modelling methodology

Aurizon Network has submitted separate revenue and pricing models to the QCA, with the revenue model based on the key assumptions reflected in the AER's Post Tax Revenue Model (**PTRM**).

The QRC wishes to make a number of general comments in relation to the approach taken by Aurizon Network.

(a) Rationale for change

Aurizon Network has justified its approach to the revenue model on the basis that it removes complexity from regulatory pricing. In the QRC's view, this comment is misleading because, in many instances:

- the suggested reduction in complexity arises from a non-modelling related factor instead of Aurizon Network's modelling approach. For

example, the reduction in complexity associated with both the iterative solving of the tax allowance and the requirement to solve for NPV over the regulatory period is attributable to the removal of tariff smoothing from UT4 rather than a shift in modelling;

- the change in model will have little to no effect on the net complexity experienced under the UT3 model. For example, the need to develop separate revenue sheets in the AER style model will dilute any benefit obtained from calculating tax as part of the 'raw' building block revenues; and
- Aurizon Network has erroneously considered issues to be modelling related only. For example, the issue raised by Aurizon Network in its UT4 explanatory material regarding the escalation of operating costs is an input control issue rather than a modelling issue.

(b) Intra-year cash flows

Aurizon Network has proposed that no intra-year discounting be applied under UT4. In its explanatory material to UT4, Aurizon Network highlighted a number of the economic flaws in the assumption of intra-year cash flows. The QRC notes the following in reply:

- the assumption of intra-year cash flow is an adjustment to the annual revenue requirement that is designed to reflect the difference in timing between the modelling of cash flow in excel (which assumes all payments are at the end of each year) and fact that Aurizon actually receives (and pays) its cash flows on a monthly basis. The assumption lowers Aurizon Network's annual revenue requirement to account for the benefit it receives from receiving this cash earlier than is accounted for in the discounting formulas;
- the QRC's preliminary modelling suggests that Aurizon Network's proposed change increases Aurizon Network's revenue by over 1.5% during the regulatory period (a point that is not made in Aurizon Network's submission). Given the size of Aurizon Network's asset base, this is a materially significant amount in both dollar and percentage terms;
- the AER chose not to include an intra-year cash flow adjustment so to make its model simpler and more transparent. However, in doing so, the AER noted that its consultants (AGC) had found that without an intra-year cash flow adjustment "working capital was not necessary and also that PTRM's timing assumptions tended to overcompensate service providers".⁹ The combination of an intra-year cash flow adjustment combined with a well specified working capital allowance was considered to be technically superior from a methodological perspective.
- The application of UT4 to a single entity (Aurizon Network) and Aurizon Network's relatively small number of major customers (relative to an energy company, for example) means that many of the criticisms of the use of an intra-year cash flow adjustment (and associated requirement for a working capital allowance) raised by Aurizon Network are not justified. The working capital allowance can be tailored to Aurizon

⁹ AER, Guidelines, models and schemes for electricity distribution network service providers, Issues Paper, November 2007

Network's cash flows and Aurizon Network's customers are better resourced to understand the complexities of the regulatory process than domestic consumers.

For the above reasons, the QRC considers that the assumption of intra-year cash flows should be retained in UT4.

(c) The need for further consultation

Although the QRC welcomes the introduction of a more open and transparent modelling structure, it does not consider it is necessary to adopt all elements of the AER's PTRM to achieve this. In the QRC's view, where changes to the modelling approach have a significant financial impact on Aurizon Network's net financial position, these changes need to be justified by more than the aim of achieving a less complex modelling structure. The QRC considers that further consultation between industry and the QRC on this issue is required.

3 Revenue Smoothing

Aurizon Network has proposed that revenue smoothing be adopted under UT4, seemingly on the basis that it is in customers' best interests. The QRC notes however that Aurizon Network has not consulted with industry regarding such an approach.

Given the range of the adjustment mechanisms included in UT4, the QRC does consider smoothing of any type (either revenue smoothing or tariff smoothing) to be necessary.

4 The need for further information

The QRC appreciates Aurizon Network's publication of a public version of the AN Model. The QRC notes however that the public version is a very high level summary of the model only and cannot be used for sensitivity testing of the tariffs (for example, by adjusting key inputs like the components of WACC or operating costs). In the QRC's view, disclosure of a more expansive model is required if Aurizon Network's goal of gaining industry's confidence in the modelling process is to be achieved.

The QRC understands that Aurizon Network has concerns about breaching its confidentiality obligations in disclosing any further modelling information. The QRC would like to work with Aurizon Network to resolve this issue (for example, by mutually appointing an independent third party (who would also be subject to confidentiality obligations) to assess the more detailed modelling material on industry's behalf).

Annexure A QRC's response to AN's Annexure A

Annexure B QRC's response to AN's Annexure B

Aurizon Network's Annexure B contains three separate tables:

- Table B.1 – Detail response – Standard Access Agreements;
- Table B.2 – Comparison of End User Access Agreement; and
- Table B.3 – Comparison of Train Operations Agreement.

The QRC's response to Table B.1 is below. However, as noted by the QRC in Part 1, Aurizon Network's Table B.1 only responds to a small portion of the QRC's Mark-Up of the AHAA (which was included in the QRC's Main Submission). To ensure meaningful progress can be made on the content of the standard access agreements, the QRC invites Aurizon Network to prepare a mark-up in response to the QRC's drafting. Unless expressly stated otherwise, nothing in the QRC's response to Table B.1 limits or changes the QRC's Mark-Up of the AHAA.

Tables B.2 and B.3 have been provided by Aurizon Network as an aide to identify (what Aurizon Network considers to be) the key changes to the UT3 End User Access Agreement and Train Operations Agreement. The QRC has not responded to these tables. In the QRC's view, the changes proposed by the QRC in relation to the AHHA should be applied (as relevant) to all UT4 standard access agreements (including the EUAA and TOA). To avoid duplication, the QRC has not prepared mark-ups of these documents. However, if the QCA would find mark-ups helpful, the QRC is happy to provide these documents as part of a supplementary submission.

Annexure C QRC's Response to AN's partial update of Part 8

Annexure D QRC's mark-up of Part 8

Annexure E Table of omissions

Aurizon Network has only responded to parts of the QRC's Main Submission. The following table provides a list of some of the QRC's proposals which Aurizon Network has not responded to. This list is by no means exhaustive and should be considered in conjunction with the remainder of this New Submission and the QRC's Main Submission including its Mark-Up.

Annexure F Response to AN’s list of accountability mechanisms

UT4 accountability mechanism	QRC response
The provision of separate below rail financial statements	The QRC agrees with the drafting proposed in UT4 (subject to some minor amendments) and has incorporated this obligation in its re-draft of Part 3 (see clause 3.9).
Protected Information Register	A more comprehensive coverage of protection against conflicts is required in UT4. The QRC has proposed a re-draft of Part 3 which contemplates the information register applying to a broader scope of confidential information.
Mandatory training requirements in relation to Protected Information obligations	<p>The mandatory training requirements imposed by UT4 are too narrow. Aurizon Network should be obliged to carry out:</p> <ul style="list-style-type: none"> • initial training for all Aurizon Group staff on the application of conflict protections under UT4; and • more detailed training sessions for Aurizon Network staff who perform Access-related Functions or have access to Confidential Information (as defined by the QRC). <p>These obligations are included in the QRC’s redraft of Part 3.</p>
Dispute resolution and complaints handing mechanism	The dispute resolution framework in UT4 has been unnecessarily restricted compared to UT3. The QRC understands Aurizon Network is jointly committed to broadening the

application of the dispute resolution provisions. Despite this, the QRC considers further changes are required in Part 8 to ensure the value of the dispute resolution framework as an accountability mechanism is not undermined.

Reporting, including compliance and breach reports

The obligation on Aurizon Network to provide quarterly operational performance reports in UT3 has been relaxed in UT4 to require annual reporting only. The quarterly reporting obligations in UT3 should be retained.

Disclosure of access agreements to the QCA

Although the obligation on Aurizon Network to provide details of the “Below Rail” aspects of an access agreement to the QCA has been retained, the QCA’s entitlement to publically publish such information under UT4 has been limited to circumstances where the QCA has obtained the prior written consent of the parties to the access agreement. The disclosure regime in UT3 provided a significant mechanism for providing access seekers and holders with confidence about non-discriminatory treatment by Aurizon Network and should be retained.

The provision of certifications by Aurizon Network’s Executive Officer

The QRC largely agrees with the framework proposed in UT4 however considers that Aurizon Network should be obliged to provide any expert advice relied upon by its Executive Officer in providing a certification required under UT4 if requested to do so by the QCA.

The ability for the QCA to request information

The QRC agrees with the drafting proposed in UT4.

The requirement to maintain a Compliance Officer

Aurizon Network has noted in its Response to Industry that it will redraft clause 10.4 of UT4 to impose further obligations in relation to Aurizon Network's compliance officer. The QRC supports the inclusion of additional obligations on the compliance officer (including an obligation to take all steps necessary to ensure Aurizon Network is able to meet the obligations imposed by UT4). The QRC will assess Aurizon Network's proposed amendments when the drafting foreshadowed by Aurizon Network is provided.

The ability for the QCA to audit Aurizon Network's compliance with any matter under UT4.

The UT4 auditing framework removes all ongoing obligations for annual audits contained in UT3. The QRC's view is that, as a matter of course, auditing should occur no less than annually. The QRC also supports the inclusion of a mandatory annual audit of the Aurizon Network's compliance with its ringfencing obligations.

The QCA's statutory powers

For clarity, the QRC considers it useful that the QCA's powers in relation to UT4 be expressly set out in the undertaking.

Glossary

Term	Meaning
ACCC	Australian Competition and Consumer Commission
AER	Australian Energy Regulator
AHAA	Access Holder Access Agreement – Coal
AHL	Aurizon Holdings Limited
AN Model	Aurizon Network's UT4 "Coal System Aggregate" Model (as published by the QCA in December 2013)
ARTC	Australian Rail Track Corporation
Aurizon Network / AN	Aurizon Network Pty Ltd
BRoC	Binding Rules of Conduct under the CCA
CCA	<i>Competition and Consumer Act 2010 (Cth)</i>
CQCN	Central Queensland Coal Network
DBCT	Dalrymple Bay Coal Terminal
EUAA	End User Access Agreement
industry	miners in the Queensland coal industry

Main Submission	the QRC's submission in relation to UT4 of 10 October 2013, including the Mark-Ups and Pricing Submission
Mark-Ups	the amendments to UT4 (including standard agreements) proposed by the QRC and included in the Main Submission
NDP	Network Development Plan as defined in UT4
New Submission	this submission made by the QRC dated 20 January 2014
Pricing Submission	the QRC's submissions on pricing under UT4 provided as part of its Main Submission
PTRM	AER's Post Tax Revenue Model
QCA	Queensland Competition Authority
QCA Act	<i>Queensland Competition Authority Act 1997</i> (Qld)
QRC	Queensland Resources Council
RAB	Regulatory Asset Base
Response to Industry	Aurizon Network's Response to Industry Submissions dated 29 November 2013
STCSM	Short term capacity swap mechanism
SUFA	Standard User Funding Agreement

TOA	Train Operations Agreement
ToP	Take or Pay
TSE	Train Service Entitlement
UT3	the 2010 rail access undertaking, as approved by the QCA (including amendments)
UT4	the 2013 draft access undertaking
WACC	Weighted Average Cost of Capital