

File Ref: 1390314

24 October 2019

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

Dear Mr Windle

**Aurizon Network's 2017–18 capital expenditure claim—decision**

The Queensland Competition Authority has approved most of Aurizon Network's 2017–18 capital expenditure claim, as amended on 16 November 2018, in accordance with schedule E, clause 2.3(c) of the 2017 access undertaking. The total expenditure approved to be included into Aurizon Network's regulatory asset base is \$212,553,214 (including interest during construction or IDC).

The QCA refused to approve part of the claim, valued at \$231,216 (including IDC). The basis of our decision is set out in the attached decision notice, in accordance with schedule E, clause 2.3(e) of the 2017 access undertaking.

This letter and decision notice will be published on the QCA website for stakeholders' information.

If you have any questions, please contact Amar Doshi on 07 3222 0534 or [amar.doshi@qca.org.au](mailto:amar.doshi@qca.org.au).

Yours sincerely



Charles Millstead  
Chief Executive Officer

## DECISION NOTICE

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### AURIZON NETWORK'S 2017–18 CAPITAL EXPENDITURE CLAIM

24 October 2019

The Queensland Competition Authority refused to approve part of Aurizon Network's 2017–18 capital expenditure claim, as amended on 16 November 2018, for inclusion into its regulatory asset base. We have set out our reasons in this decision notice, in accordance with schedule E, clause 2.3(e) of the 2017 access undertaking.

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#### Regulatory process

We conduct an annual assessment of the prudence and efficiency of Aurizon Network's capital expenditure claim to determine if it should be included in the regulatory asset base (RAB) for the central Queensland coal network. Aurizon Network submitted its annual capital expenditure claim report on 31 October 2018, under the 2016 access undertaking (UT4). UT4 was replaced by the approved 2017 access undertaking (UT5) and transitional arrangements provide for the assessment of this capital expenditure claim to be progressed under UT5 (cl. 12.4(a)).

In determining the prudence and efficiency of capital expenditure, we have regard to the **scope of works, standard of works** and **cost** (sch. E, cl. 2.2(b) of UT5).<sup>1</sup>

During the assessment process, we gave Aurizon Network a draft of our decision, outlining reasons for considering to refuse to approve part of its 2017–18 capital expenditure claim (cl. 2.3(d)(i)).

The following steps and timelines were followed:

| <i>Date</i>       | <i>Action</i>   |
|-------------------|---|
| 20 September 2018 | We published our assessment approach for the 2017–18 capital expenditure claim                              |
| 31 October 2018   | Aurizon Network submitted its 2017–18 capital expenditure claim   |
| 16 November 2018  | Aurizon Network amended its claim   |
| 19 November 2018  | We published Aurizon Network's submissions and our project sample list, and invited stakeholder submissions |
| 3 December 2018   | The submissions period closed—we received one submission  |
| 14 February 2019  | We published an amended project sample list   |

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<sup>1</sup> All clause references hereafter refer to schedule E of UT5, unless otherwise stipulated.

| <i>Date</i>       | <i>Action</i>   |
|-------------------|---|
| 21 February 2019  | Assessment of the claim transitioned to the approved 2017 access undertaking        |
| 27 May 2019       | We published our consultant's assessment report and invited stakeholder submissions |
| 24 June 2019      | The submissions period closed—we received one submission                            |
| 15 August 2019    | We provided Aurizon Network a draft of our decision                                 |
| 12 September 2019 | Aurizon Network responded to the draft of our decision                              |
| 24 October 2019   | We made our decision not to approve part of the claim                               |

In addition to this letter and decision notice, we published the following documents on our [website](#):

- Aurizon Network's amended 2017–18 capital expenditure claim and accompanying letter
- our amended project sample list
- the stakeholder submissions received on 3 December 2019 and 24 June 2019
- our consultant's assessment report and notices of advice
- Aurizon Network's response to the draft of our decision.

### [Aurizon Network's 2017–18 capital expenditure claim and amendments](#)

Aurizon Network's 2017–18 capital expenditure claim, as amended on 16 November 2018, encompassed 58 projects that totalled approximately \$213 million (including interest during construction or IDC).<sup>2</sup>

### [Engineering consultant's assessment](#)

We engaged AECOM to provide engineering advice on the prudence and efficiency of Aurizon Network's 2017–18 capital expenditure claim (in accordance with cl. 2.2(g)). A sample of projects was selected to be assessed against the criteria in Schedule E of UT5. The sample list comprised of 27 projects representing approximately 84 per cent of the claim.

AECOM assessed and reported on the projects based on a desktop review of information provided by Aurizon Network, and in-person interviews with key Aurizon Network staff where documentation did not provide sufficient clarity and where deemed necessary.<sup>3</sup> AECOM also reviewed additional information provided by Aurizon Network in response to AECOM's published report<sup>4</sup> and subsequently, in response to a draft of our decision.<sup>5</sup>

AECOM found most projects in the sample to be prudent and efficient<sup>6</sup>, except for the following two projects, where it recommended adjustments to reduce the claim:

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<sup>2</sup> Aurizon Network, *Capital Expenditure FY18—Amendment*, letter to the QCA, 16 November 2018; Aurizon Network, *FY18 Capital Expenditure Report - Amended*, November 2018 (Aurizon Network report).

<sup>3</sup> AECOM, report for the QCA, *Assessment of Aurizon Network's 2017–18 Capital Expenditure Claim*, May 2019 (AECOM report).

<sup>4</sup> AECOM, notice of advice, *Aurizon Network's 2017–18 capital expenditure claim*, July 2019 (AECOM July notice).

<sup>5</sup> AECOM, notice of advice, *Aurizon Network's 2017–18 capital expenditure claim*, October 2019 (AECOM October notice).

<sup>6</sup> AECOM report, p. 59.



- (1) IV.00323 Track Upgrade FY18<sup>7</sup>
- (2) IV.00343 Level Crossings Renewal Program FY18<sup>8</sup>.

## Stakeholder consultation

We provided stakeholders two opportunities to make submissions and received a total of two submissions, from:

- Pacific National, who commented on Aurizon Network's proposal and the QCA's project sample list (November–December 2018)
- Aurizon Network, who addressed matters raised in AECOM's assessment report and provided additional information to substantiate its claim (May–June 2019).<sup>9</sup>

Aurizon Network also responded to the draft of our decision (consistent with cl. 2.3(d)(ii)), attaching further documentation in relation to one of the outstanding projects that we were inclined not to approve.<sup>10</sup>

## QCA assessment and decision

We approve Aurizon Network's 2017–18 capital expenditure claim, as amended on 16 November 2018, except for the adjustments discussed below. The majority of the projects assessed meet the criteria for prudence and efficiency for inclusion in the RAB. However, on the information currently before us, two identified projects do not meet the criteria in their entirety, so corresponding adjustments to the expenditure for these projects are required.

This will provide for approximately \$211 million (excluding IDC)<sup>11</sup> to be included in the RAB. The related projects are listed in **Attachment 1**.

### Required adjustments

#### *IV.00323 Track Upgrade FY18*

We refuse to approve part of Aurizon Network's claim for IV.00323 Track Upgrade FY18 valued at \$59,400, to reflect rerailings at one location being imprudent in scope of works.

Aurizon Network's track upgrade is a coordinated program of renewing the track structure, maximising the efficiency of construction by combining rerail and sleeper renewals, where both are approaching end of life.<sup>12</sup> On this basis, Aurizon Network upgraded the rail in the Coppabella-Broadlea Section to mitigate 'a potential derailment risk as a result of damaged fist clip sleepers and fatigued rail.'<sup>13</sup> AECOM found the replacement of sleepers prudent in scope but stated that Aurizon Network 'identified that the rail has a remain life of 50% without any further supporting information' and therefore, maintained 'that the rail replacement at this location is not considered prudent.'<sup>14</sup>

We consider the replacement of fatigued rail before the end of its service life may promote economically efficient operation of, use of or investment in the rail infrastructure in terms of reducing future costs or improving capability of existing assets (cl. 2.2(b)(i)(E)). However, we are unable to assess the reliability of the decisions in relation to

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<sup>7</sup> AECOM report, pp. 40–42; AECOM July notice, pp. 7–9; AECOM October notice, p. 12.

<sup>8</sup> AECOM report, pp. 44–45; AECOM July notice, pp. 10–11; AECOM October notice, p. 13.

<sup>9</sup> Aurizon Network, submission to the QCA, *Aurizon Network's 2017–18 capital expenditure claim*, June 2019 (Aurizon Network submission).

<sup>10</sup> Aurizon Network, *Aurizon Network Pty Ltd (Aurizon Network)—FY18 Capital Expenditure Submission*, letter to the QCA, 12 September 2019.

<sup>11</sup> All values in this section exclude IDC.

<sup>12</sup> Aurizon Network report, p. 15, AECOM report, p. 41.

<sup>13</sup> Aurizon Network submission, p. 11.

<sup>14</sup> AECOM July notice, p. 9.

scope of works being made in a prudent manner given the lack of relevant rail fatigue data to support the scope of rerailing works and as such, require corresponding adjustment to the claim for this project prior to inclusion into Aurizon Network's RAB.

#### *IV.00343 Level Crossings Renewal Program FY18*

We refuse to approve \$177,766 of Aurizon Network's total expenditure for IV.00343 Level Crossings Renewal Program FY18, to reflect design costs to be claimed in the future.

Aurizon Network stated it undertakes the majority of its capital renewal work 'on a continuous, rolling basis' and as such, 'it is highly likely that there will be situations where construction is performed in the financial year following the design.'<sup>15</sup> AECOM found one such instance where Aurizon Network included design costs for work to be commissioned in 2018–19 in the 2017–18 claim and recommended 'these costs should be deferred until the FY18/19 claim'<sup>16</sup>. Aurizon Network disagreed, stating that,

UT5 does not specifically define whether or not '*design costs*' alone are to be claimed in the year the expenditure [*sic*], however it would appear to be reasonable to include these costs within an overall project spend.<sup>17</sup>

Our view is that capital expenditure would be included in the RAB in response to the reporting of evidence of the commissioning of the associated asset, among other matters outlined in clause 1.3(a) (cl. 2.1(b)(i)). We do not regard the delivery of design work to represent the commissioning of an asset and instead, consider it appropriate to be claimed once the asset is commissioned.

#### Interest during construction

We assessed Aurizon Network's methodology for calculation of the IDC as appropriate and values accurately reported for the amended claim, accounting for the adjustments stated above. The IDC for each approved project of the 2017–18 capital expenditure claim is outlined in **Attachment 1**.

#### Recommendations

We recommend Aurizon Network make improvements to documentation of its decision-making and expenditure for capital projects. This pertains to AECOM:

- finding of a potential 'systemic issue related to processes and documentation related to discovery and use of non-compliant material [for formation renewals] that should be addressed'<sup>18</sup>, and
- depending heavily on its professional judgement, rather than Aurizon Network's documentation, in assessing the prudence and efficiency of the sample projects.<sup>19</sup>

We acknowledge Aurizon Network staff are in the process of implementing various improvements for the future capital expenditure review, and urge consideration to the matters identified in relation to documentation of project completion, cost and scope for renewal projects.

#### REFERENCES

Aurizon Network, letter to the QCA, *Capital Expenditure FY18—Amendment*, 16 November 2018.

— *FY18 Capital Expenditure Report - Amended*, November 2018 (Aurizon Network report).

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<sup>15</sup> Aurizon Network submission, p. 12.

<sup>16</sup> AECOM report, p. 45; AECOM July notice, pp. 10–11.

<sup>17</sup> Aurizon Network submission, p. 12.

<sup>18</sup> AECOM report, pp. 60–61.

<sup>19</sup> AECOM report, p. 61.

— submission to the QCA, *Aurizon Network's 2017–18 capital expenditure claim*, June 2019 (Aurizon Network submission).

— *Aurizon Network Pty Ltd (Aurizon Network)—FY18 Capital Expenditure Submission*, letter to the QCA, 12 September 2019.

AECOM, report for the QCA, *Assessment of Aurizon Network's 2017–18 Capital Expenditure Claim*, May 2019 (AECOM report).

— notice of advice, *Aurizon Network's 2017–18 capital expenditure claim*, July 2019, (AECOM July notice).

— notice of advice, *Aurizon Network's 2017–18 capital expenditure claim*, September 2019, (AECOM October notice).



## ATTACHMENT 1: APPROVED 2017–18 CAPITAL EXPENDITURE

| <i>Project ID</i> | <i>Project name</i>                    | <i>Asset type</i>    | <i>Capital expenditure (\$, excl. IDC)</i> | <i>IDC (\$)</i> | <i>Capital expenditure (\$, inclu IDC)</i> |
|-------------------|--|----------------------|--|-----------------|--|
| IV.00323          | Track Upgrade FY18*                    | Track                | 23,389,982                                 | 35,379          | 23,425,361                                 |
| IV.00049          | Radio System Replacement               | Network Controls     | 23,351,894                                 | 547,207         | 23,899,101                                 |
| IV.00322          | Rail Renewal FY18                      | Rail                 | 21,468,545                                 | 84,167          | 21,552,712                                 |
| IV.00329          | Structures Renewal FY18                | Structures           | 15,054,900                                 | 77,616          | 15,132,516                                 |
| IV.00344          | Formation Renewal FY18                 | Formation / Ballast  | 12,236,291                                 | 107,636         | 12,343,927                                 |
| IV.00364          | Turnout Renewal FY18                   | Turnouts             | 11,500,392                                 | -89,629         | 11,410,762                                 |
| A.04599           | Havilah Culverts Upgrade               | Structures           | 8,719,163                                  | 249,917         | 8,969,080                                  |
| IV.00346          | Package 1 FY18 Control Systems Renewal | Network Controls     | 8,223,807                                  | -16,069         | 8,207,738                                  |
| IV.00347          | Package 2 FY18 Control Systems Renewal | Network Controls     | 8,035,389                                  | -103,596        | 7,931,793                                  |
| IV.00334          | Bridge Ballast Renewal Program FY18    | Formation / Ballast  | 7,272,262                                  | 35,831          | 7,308,093                                  |
| IV.00321          | Sleeper Renewal Program FY18           | Sleepers             | 6,747,175                                  | 57,937          | 6,805,013                                  |
| IV.00360          | Network Asset Mgt System Tranche 2     | Operational Systems  | 5,311,528                                  | 41,228          | 5,352,755                                  |
| IV.00343          | Level Crossings Renewal Program FY18*  | Level Crossings      | 5,244,232                                  | -9,981          | 5,234,250                                  |
| IV.00437          | Callide Infrastructure Upgrade         | Track                | 5,151,241                                  | -91,892         | 5,059,349                                  |
| IV.00145          | Track Upgrade FY17                     | Track                | 5,145,878                                  | 55,231          | 5,201,109                                  |
| IV.00399          | 2017 Cyclone Debbie Rectification      | Various              | 4,441,745                                  | 19,239          | 4,460,984                                  |
| OP.00161          | FY18 Minerva Renewals                  | Sleepers             | 3,813,799                                  | -4,953          | 3,808,847                                  |
| IV.00177          | Structures Renewal FY17                | Structures           | 3,618,047                                  | 16,517          | 3,634,564                                  |
| IV.00384          | OH Equipment Renewal FY18              | Distribution Network | 3,461,614                                  | 14,099          | 3,475,713                                  |
| IV.00270          | Ethernet to Corner SCADA Upgrade FY17  | Network Controls     | 3,022,135                                  | 116,639         | 3,138,774                                  |
| IV.00146          | Sleeper Renewal FY17                   | Sleepers             | 2,843,381                                  | 52,887          | 2,896,268                                  |
| IV.00168          | Turnout Renewal FY17                   | Turnouts             | 2,685,243                                  | 45,043          | 2,730,286                                  |
| IV.00294          | Goonyella Supersite FY17               | Network Controls     | 2,147,879                                  | 78,947          | 2,226,827                                  |

| <i>Project ID</i> | <i>Project name</i>                       | <i>Asset type</i>    | <i>Capital expenditure (\$, excl. IDC)</i> | <i>IDC (\$)</i> | <i>Capital expenditure (\$, inclu IDC)</i> |
|-------------------|---|----------------------|--|-----------------|--|
| IV.00283          | Traction SCADA System                     | Network Controls     | 2,078,916                                  | 6,696           | 2,085,613                                  |
| IV.00144          | Rail Renewal FY17                         | Rail                 | 2,064,204                                  | 30,855          | 2,095,059                                  |
| IV.00004          | Traction Fault Locator Renewal            | Distribution Network | 1,985,507                                  | 100,503         | 2,086,010                                  |
| IV.00266          | Transmission Renewal FY17                 | Network Controls     | 1,926,012                                  | 54,099          | 1,980,111                                  |
| IV.00261          | Telecommunications Infrastructure Renewal | Telecommunication    | 1,875,684                                  | 34,899          | 1,910,583                                  |
| IV.00170          | Bridge Ballast Renewals FY17              | Formation / Ballast  | 1,284,390                                  | 24,080          | 1,308,470                                  |
| IV.00154          | FY17 Autotransformer Renewal Project      | Power Systems        | 1,437,366                                  | -15,781         | 1,421,585                                  |
| IV.00375          | Corridor Security & Fencing FY18          | Corridor Access      | 769,726                                    | -2,404          | 767,323                                    |
| IV.00032          | FY16 Turnout Renewal Program              | Turnouts             | 717,377                                    | 3,341           | 720,718                                    |
| A.01731           | WIRP1: Dingo to Bluff Duplication         | Track                | 550,225                                    | 363             | 550,588                                    |
| IV.00184          | Network Capacity Model                    | Network Controls     | 521,256                                    | 22,957          | 544,213                                    |
| IV.00169          | Formation Renewal FY17                    | Formation / Ballast  | 459,984                                    | 9,539           | 469,523                                    |
| IV.00040          | Train Detection Renewal Program           | Network Controls     | 360,580                                    | 244             | 360,825                                    |
| IV.00316          | Access Points Renewal Program             | Corridor Access      | 308,344                                    | 1,960           | 310,303                                    |
| A.04313           | Gauge Face Lubrication Asset Renewal      | Track                | 276,873                                    | -1,497          | 275,376                                    |
| IV.00271          | UTC and DTC Upgrade Program               | Signalling Equipment | 264,528                                    | 2,436           | 266,964                                    |
| IV.00267          | Asset Protection Equipment Replacement    | Signalling Equipment | 238,851                                    | 3,549           | 242,400                                    |
| IV.00171          | Level Crossings FY17                      | Level Crossings      | 214,462                                    | 5,111           | 219,573                                    |
| A.02976           | WIRP1: North Coast Line                   | Track                | 159,332                                    | -3,602          | 155,730                                    |
| IV.00005          | Blackwater Supersite                      | Network Controls     | 153,288                                    | 2,687           | 155,975                                    |
| A.02628           | Coal System: Coal Loss Management         | Environmental        | 125,187                                    | 2,266           | 127,453                                    |
| IV.00046          | Interlocking Renewal Program              | Signalling Equipment | 92,267                                     | 1,581           | 93,848                                     |



| <b>Project ID</b> | <b>Project name</b>                      | <b>Asset type</b>    | <b>Capital expenditure (\$, excl. IDC)</b> | <b>IDC (\$)</b>  | <b>Capital expenditure (\$, inclu IDC)</b> |
|-------------------|--|----------------------|--|------------------|--|
| IV.00359          | FY16 Goonyella Flood                     | Various              | 86,001                                     | 1,669            | 87,670                                     |
| A.03735           | WIRP1: Bauhinia NORTH Upgrade            | Track                | 64,434                                     | -1,503           | 62,931                                     |
| A.03686           | WIRP1: Moura System Upgrade              | Track                | 30,112                                     | -7               | 30,105                                     |
| A.04357           | NR Gladstone Yard Retaining Wall Upgrade | Structures           | 22,842                                     | 417              | 23,259                                     |
| A.01552           | WIRP1: Wiggins Balloon Loop              | Track                | 22,465                                     | -111             | 22,354                                     |
| IV.00260          | CQ Access Roads FY17                     | Corridor Access      | 14,561                                     | 334              | 14,895                                     |
| IV.00025          | NR Track Upgrade Program FY16            | Track                | 4,491                                      | 73               | 4,564                                      |
| IV.00257          | Minerva Renewals                         | Sleepers             | 1,107                                      | 26               | 1,133                                      |
| IV.00056          | Diagnostic Computer Renewal              | Signalling Equipment | -105                                       | -131             | -236                                       |
| A.01631           | WIRP1: Rocklands to Stanwell Duplication | Track                | -2,342                                     | 36               | -2,306                                     |
| IV.00024          | NR Vital Disabling Release               | Network Controls     | -2,585                                     | -52              | -2,637                                     |
| A.04321           | Central Coal UPS Upgrade Project         | Operational Systems  | -9,291                                     | -291             | -9,582                                     |
| IV.00262          | Power Resilience FY17                    | Power Systems        | -31,321                                    | -1,679           | -32,999                                    |
| <b>Total</b>      |  |                      | <b>210,951,251</b>                         | <b>1,601,963</b> | <b>212,553,214</b>                         |

*Note: The shaded projects were included in the amended project sample list assessed by AECOM. Projects marked with an asterisk (\*) reflect adjustments to the claim amount.*