DECISION NOTICE (DRAFT)

ANNUAL REVIEW OF REFERENCE TARIFFS

26 May 2021

The Queensland Competition Authority is minded to approve Aurizon Network's proposed variations to its volume forecast, maintenance and capital indicators, tax allowance and consequential adjustments to its 2021–22 allowable revenues and reference tariffs. The reasons for our intended decision are set out in this notice, in accordance with Aurizon Network's 2017 access undertaking. We invite stakeholders to provide additional submissions by **Thursday, 10 June 2021**.

Schedule F of Aurizon Network's 2017 access undertaking (2017 AU) provides a mechanism for Aurizon Network to adjust its reference tariffs prior to the beginning of each financial year. In accordance with clause 5.1(a)(ii)(B)[1], Aurizon Network must submit a reference tariff variation to the QCA by 28 February each year, encompassing variations to the tariff components outlined in clause 4.1(a). This allows Aurizon Network to update the system allowable revenues and reference tariffs (cl. 4.1(b)(vii)), to reflect the actual or updated changes in defined factors that impact reference tariffs.

Aurizon Network's proposal

On 26 February 2021, Aurizon Network submitted its proposed reference tariffs and allowable revenues for 2021–22 for our approval.[2] It proposed adjustments to volumes, allowable revenues and reference tariffs for each coal system. These adjustments are based on schedule F provisions that allow for:

- adjusting for any under- or over-recovery of revenues (revenue cap) (cl. 4.1(a)(i))
- the difference between approved **capital expenditures** and the capital indicator in previous years (cl. 4.1(a)(ii)).
- updating **volume forecasts**—used to determine reference tariffs (cl. 4.1(b)(i))
- the **maintenance and capital indicator** for each coal system to reflect the approved maintenance and renewals strategies and budgets (cls. 4.1(b)(v) and 4.1(b)(vi)), or Aurizon Network's proposed maintenance and capital indicators where approval has not been received
- updating the **tax allowance** to reflect the changes proposed to revenues (cl. 4.1(b)(vii)(F))
- incorporating approved forecast independent expert (**IE**) pass-through costs (cl. 4.1(b)(viii))
- updating **electric infrastructure** and **electric energy** charges to reflect the latest forecast of transmission and energy costs (cls. 4.1(c)(ii) and 2.2(a)).

[1] References to specific clauses in this notice are to schedule F of the 2017 AU, unless otherwise stated.
[2] Aurizon Network, *Annual Review of Reference Tariff—FY2022*, February 2021 (Aurizon Network proposal).

Aurizon Network subsequently amended this submission on 18 March 2021, to account for pricing updates from electric distribution transmission entities, which it received after its original submission.[3] It reflected these pricing updates in the electric traction and electric energy charges, and the allowable revenues and reference tariffs for the Blackwater and Goonyella systems.

Aurizon Network provided the methods, data and assumptions it used to determine the proposed variations to support its initial proposal and subsequent amendment.

Stakeholder comments

We published details of Aurizon Network's proposed reference tariff variation and invited comments from stakeholders regarding the proposed variation.

We received six submissions, from Aurizon Coal, Bravus Mining, Glencore, QCoal, Queensland Resources Council (QRC) and Rio Tinto. We considered all stakeholder comments.

Stakeholders were particularly concerned about the allocation of renewals costs for the Newlands system and potential impacts of privately funded infrastructure expenditure associated with a new train service on the Newlands system tariffs.

We provided these submissions to Aurizon Network, who submitted a response to the stakeholders' concerns, included those mentioned above.[4]

We are providing stakeholders a final opportunity to provide submissions to inform our decision on this review of reference tariffs for 2021–22. While stakeholders may comment on any part of our decision, we would like to draw particular attention to our present views and intended approach for the allocation of renewals costs in the Newlands system.

Assessment

We have assessed Aurizon Network's proposal in accordance with the requirement for the annual review of reference tariffs (cl. 4.1). This includes having regard to whether the revised volume forecasts are reasonable (with no errors made); the submitted maintenance and capital indicators are consistent with the approved indicators; the revised tax allowance has been calculated correctly; and no errors have been made in adjustments to allowable revenues or reference tariffs.

Volume forecasts

Aurizon Network has proposed updated 2021–22 volumes forecasts for the Central Queensland coal network (CQCN) and associated gross tonne kilometre (gtk) forecasts that we presently consider are reasonable, having regard to the information available at the time of submission.

The proposed system forecasts are based on 2019–20 actual volumes, adjusted:

- in proportion to each train service's share (origin–destination pair) of the 'adjusted contract' in each respective coal system, and excluding any contracted train service that had not railed in 2019–20 or 2020–21
- to reflect anticipated new hauls and contract renewals currently under negotiation.[5]

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[3] Aurizon Network*, FY2022 Annual review of Reference Tariffs—Variation of electric connection and transmission charges and Electric Energy Charge,* March 2021 (Aurizon Network amendment).

[4] Aurizon Network, *Response to stakeholder submission on the FY2022 Annual Review of Reference Tariffs Proposal*, April 2021 (Aurizon Network response).

[5] Aurizon Network proposal, p. 11.

This reduces volume forecasts from current approved amounts across the CQCN and in all systems (Table 1).

Table 1 Volume forecasts, 2021–22

System	***Approved (mt)***	***Proposed (mt)***	***Variance (mt)***
Blackwater	70.2	62.6	(7.6)
Goonyella	131.7	117.7	(14.0)
Moura	17.3	13.6	(3.7)
Newlands	13.2	14.1	(0.9)
GAPE	18.9	18.8	(0.0)
Total	**251.3**	**226.9**	**(24.4)**

We note the inherent difficulty in predicting volumes when there is market uncertainty. However, given the ongoing shortfall in volumes observed since the UT5 decision, it seems likely that current approved volume forecasts do not reflect prevailing market conditions and a reduction in forecast volumes is reasonable. Moreover, Aurizon Network's approach draws from actual volumes, existing contracts and expectations—and is aligned with the volumes assumed in the development of the 2021–22 final draft maintenance and renewals strategy and budget.[6]

We acknowledge that using more recent information (including more recent railing data or user forecasts of their future railings) could provide greater forecast accuracy.[7]

The QRC encouraged miners to provide feedback, on a confidential basis, to assist in this assessment. However, only some miners provided information (making the information incomplete) and this was received well after the due date for submissions. We have therefore not sought to incorporate this information to determine new forecasts in this decision. In any case, stakeholders would be aware that actual volumes will be taken into account in the annual ex post revenue adjustment process. We encourage Aurizon Network and stakeholders to work together (having regard to confidentiality requirements) to develop an approach to determining volume forecasts (including agreeing on possible updates as more information becomes available) for future assessments.

Capital expenditure

The 2017 AU allows for an adjustment to reconcile the difference between the approved capital expenditure and the capital indicator for the year in which that relevant capital expenditure was incurred (cl. 4.1(a)(ii), and calculated in accordance with sch. E, cl. 5(b)[8]).

In July 2020, we approved Aurizon Network's 2018–19 capital expenditure of $126.8 million[9] and the subsequent roll-forward of that amount into the regulatory asset base (RAB) ($123.3 million).[10] Subsequently, Aurizon Network updated its financial models for the approved 2018–19 capital expenditures and applied the roll-forward mechanism. This reflected the relevant adjustments in allowable revenues by applying the approved discount rate accrued. The 2018–19 roll-forward impacts allowable revenues for 2021–22, adding $20.4 million for non-electric

[6] Aurizon Network proposal, p. 9.

[7] Aurizon Network proposal, p. 10, Aurizon Network response, p. 2; QRC, pp. 1–2.

[8] The clause refers to allowable revenue adjustments resulting from capital expenditure reconciliation.

[9] QCA, *Aurizon Network's 2018–19 capital expenditure claim*, decision, May 2020.

[10] QCA, *Aurizon Network's 2018–19 RAB roll-forward*, final decision, July 2020. The $126.8 million capital expenditure approved (end-of-year values including interest during construction or IDC) is rolled forward into the RAB at $123.3 million (start-of-year value).

assets and $3.4 million for electric assets. We presently consider that allowable revenues attributable to the 2018–19 capital expenditure have been appropriately included into the RAB and accounted for in this application.

In February 2021, we approved Aurizon Network’s 2019–20[11] capital expenditure claim of $238.2 million. Aurizon Network updated its financial models to reflect the approved capital expenditure for 2019–20 and calculated corresponding indicative allowable revenue adjustments, on the basis of a preliminary[12] RAB roll-forward.[13] Aurizon Network subsequently submitted its 2019–20 RAB roll-forward in March 2021, which we then approved in April 2021.[14] Aurizon Network's proposal showed that allowable revenue for 2021–22 from the 2019–20 RAB roll-forward process added $0.7 million for non-electric and $0.5 million for electric assets. The methodology used was consistent with our capital expenditure and RAB roll-forward approvals in 2021. We presently consider Aurizon Network's proposal accurately reflects these RAB adjustments.

Maintenance indicator allowance

The 2017 AU provides for adjustments to the maintenance indicators to reflect approved maintenance strategies and budgets (cl. 4.1(b)(v)), and in accordance with cl. 7A.11.3 of the 2017 AU).

Aurizon Network proposed maintenance indicator allowances consistent with its user-approved maintenance strategy and budgets[15] for the Moura, Blackwater, Goonyella and GAPE coal systems.[16] Aurizon Network based its Newlands maintenance indicator on its draft maintenance strategy and budget, pending QCA approval (Table 2).[17]

On 26 May 2021, we approved Aurizon Network's draft maintenance strategy and budget for the Newlands system as submitted.[18]

We are required to approve a proposed maintenance indicator allowance where it is consistent with an approved maintenance strategy and budget (cl. 7A.11.4(a)(ii) of the 2017 AU).

Accordingly, we intend to approve Aurizon Network's proposed maintenance indicator allowances.

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[11] QCA, *Aurizon Network's 2019–20 capital expenditure claim*, decision, February 2021.

[12] Aurizon Network's roll-forward application for 2019–20 was not submitted for our approval at the time it submitted its annual review of reference tariff proposal.

[13] Aurizon Network proposal, p. 14.

[14] QCA, A*urizon Network's 2019–20 RAB roll-forward*, final decision, April 2021. The $238.2 million capital expenditure approved (end-of-year values including IDC) is rolled forward into the RAB at $231.5 million (start-of-year value).

[15] Aurizon Network, *Aurizon Network Maintenance and Renewal Strategy and Budget*, 21 January 2021 (Aurizon Network MRSB).

[16] On 14 February 2021, the chair of the RIG advised that users had voted to approve the proposed maintenance strategies and budgets for all system except the Newlands system.

[17] Where users have not approved a maintenance strategy and budget for a system, Aurizon Network must submit the draft maintenance strategy and budget to the QCA for approval, and the QCA will determine whether activities and costs specified are prudent and efficient (cl. 7A.11.3 of the 2017 AU).

[18] QCA, *Aurizon Network's Newlands FY22 maintenance strategy and budget*, final decision, May 2021.

Table 2 Maintenance indicator allowance, by coal system

Coal system[a]	*Allowance ($m)*
Blackwater	65.0
Goonyella	61.1
Moura	12.4
Newlands[b]	3.8
GAPE[b]	8.8
Total	**151.1**

__a__ Includes ballast undercutting plant depreciation. __b__ Aurizon Network allocated the proposed Newlands/GAPE maintenance budget in proportion to GTK forecast for Newlands and GAPE train services.

Source: Aurizon Network proposal, p. 15; Aurizon Network MRSB, pp. 8, 35, 82, 124, 161, 192.

Capital indicator allowance

The 2017 AU provides for adjustments to the capital indicators to reflect approved renewals strategies and budgets (cl. 4.1(b)(vi), and in accordance with cl. 7A.11.3 of the 2017 AU).

Aurizon Network proposed capital indicator allowances that are consistent with its user-approved renewals strategy and budgets[19] for the Moura, Blackwater and Goonyella systems. Aurizon Network based its Newlands and GAPE capital indicators on the draft renewals strategies and budgets for the Newlands and GAPE systems, in accordance with their use as interim renewals strategies and budgets[20] (cl. 7A.11.3(m)(iii) of the 2017 AU) (see below) (Table 3).

Table 3 Capital indicator allowance

Coal system	*Allowance ($m)*
Blackwater	117.1
Goonyella	120.9
Moura	11.8
Newlands	25
GAPE	0.3
Total[a]	275.1

Source: Aurizon Network proposal, p. 17; Aurizon Network MRSB, pp. 9, 166.

We are required to approve a capital indicator allowance where it is consistent with an approved renewals strategy and budget (cl. 7A.11.4(c)(ii) of the 2017 AU).

Accordingly, we intend to approve Aurizon Network's proposed capital indicator allowances for the Moura, Blackwater and Goonyella systems.

[19] Aurizon Network, *Aurizon Network Maintenance and Renewal Strategy and Budget*, 21 January 2021.
[20] On the basis of its proposed cost allocation, that has not been accepted by Newlands system and GAPE users.

Cost allocation concerns—Newlands system and GAPE

Aurizon Network's proposed capital indicator allocates the asset replacement and renewal expenditure for the shared rail corridor in the Newlands system to Newlands users via the system reference tariff, without any allocation to GAPE users. According to Aurizon Network, this expenditure is 'progressively transitioning the price of the legacy 20 [tonne axle load or] TAL system to the more efficient 26 TAL cost of service delivery over a long period of time'.[21]

Some stakeholders submitted that Newlands users should not bear the full cost of asset renewals and upgrade of prevailing assets. These stakeholders stated that these costs are attributable to the traffic originating from the GAPE system.[22] Bravus Mining and Glencore suggested GAPE users should contribute to paying these costs through the GAPE system tariffs.[23]

On balance, taking account of the information provided, we presently consider Aurizon Network's proposal to allocate the asset renewal costs in the Newlands system to Newlands users is appropriate for this reference tariff review. We have considered all the views presented by Aurizon Network and stakeholders in their submissions and presently consider that:

- the upgrade of 20 TAL Newlands assets to 26 TAL as part of the GAPE project in 2012 was considered incremental to GAPE users and was included in the GAPE RAB, which GAPE tariffs are currently based on
- non-GAPE users in Newlands have utilised and benefitted from the upgrade of assets to accommodate 26 TAL services—particularly through the avoidance of longer-term costs to maintain the less productive 20 TAL assets—such that the ongoing renewals of upgraded assets and the upgrade of the remaining 20 TAL assets are not incremental to GAPE users
- it is appropriate for the ongoing costs to be reflective of the 26 TAL asset base rather than a 20 TAL asset base, given the former is the only reference service offered in the Newlands system[24]
- prevailing (pre-GAPE) and new users in the Newlands system would have sufficient information that ongoing renewals would include the progressive upgrade of 20 TAL assets to reflect the reference service of 26 TAL.

Our assessment is based on current information provided by all parties. However, we recognise the complexity of this matter and that new information may support adopting an alternative cost allocation approach. We maintain that, ideally, Aurizon Network and affected Newlands and GAPE users would reach an agreed approach. Accordingly, we continue to encourage Aurizon Network to work collaboratively with affected stakeholders, should they request, to develop an agreed alternative approach that could be adopted in the future. To assist with this, we intend to develop a preliminary position paper to provide a framework for Aurizon Network and users to facilitate reaching an agreed approach to the allocation of renewal expenditure in the Newlands system.

New coal carrying service in the Newlands system

Aurizon Network identified a new coal carrying train service for the Newlands system due to commence in FY22. It stated this new service is 'expected to incur material capital expenditure costs on private infrastructure' which

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[21] Aurizon Network proposal, p. 21.

[22] Glencore, submission to the QCA, *Annual Review of Reference Tariff—FY2022* (Glencore submission), Appendix I, pp. 2–4; QCoal, submission to the QCA, *Annual Review of Reference Tariff—FY2022* (QCoal submission), pp. 2–3; QRC, submission to the QCA, *Annual Review of Reference Tariff—FY2022* (QRC submission), pp. 3–7.

[23] Bravus, submission to the QCA, *Annual Review of Reference Tariff—FY2022* (Bravus submission), p. 7; Glencore submission, Appendix I, p. 1.

[24] Aurizon Network, *Newlands System Information Pack—Version 7*, March 2017, p. 9.

would, if approved by the QCA under the private incremental costs (PIC) provisions (cl. 6.3.2 of the 2017 AU), result in:

- the new coal carrying train service paying an access charge which comprises only the minimum revenue contribution
- corresponding material increases in the AT3 and AT4 tariffs for Newlands users (by approximately 35 per cent) (cl. 6.3.1(c) of the 2017 AU).[25]

However, Aurizon Network has set the approved PIC amount at zero for its 2021–22 review.[26] This is consistent with requirements that the PIC be set at zero unless and until the QCA approves the relevant PIC amounts (cl. 6.3.2(e)(ii) of the 2017 AU).

Stakeholders expressed concerns about applying the existing PIC provisions to the new coal service, given the large scale of the project, the potential for the infrastructure to also be used by other customers and the materiality of the projected increase to the system tariffs.[27] We presently consider these matters are beyond the scope of this assessment—but nevertheless encourage Aurizon Network to consult with stakeholders to address concerns about impacts on system tariffs from PIC approvals.

Other—Revenue cap, electric transmission and energy costs, independent expert and tax allowance

Revenue cap

Aurizon Network has proposed adjustments relating to our approval of its 2019–20 revenue adjustment proposal (revenue cap).[28]

We note these adjustments are permitted under cl. 4.1(a)(i) and presently consider that Aurizon Network has accurately calculated the adjustment amounts.

Electric transmission and energy costs

Aurizon Network proposed to pass through the latest pricing changes from its transmission network service providers (TNSPs) and electricity retailers to customers utilising its electric assets.

Electric transmission and connection charges are determined according to the regulatory framework and oversight by the Australian Energy Regulator. They are negotiated by Aurizon Network for customers using its electric assets (chargeable through the AT5 tariff). The EC tariff is set to recover the forecast costs relating to the consumption of electric energy.[29] Aurizon Network amended its original proposal to reflect the latest forecast electric transmission, connection and energy costs from the TNSPs and Clean Energy Regulator (cls. 2.2(a), 5.2(b)). The amended 2021–22 charges for use of electric infrastructure are lower than originally forecast in the 2017 AU.[30]

We presently consider it reasonable that Aurizon Network reflect the latest forecasts for the electric transmission costs and energy charges on the corresponding reference tariffs. We have verified this was done accurately in Aurizon Network's amended proposal.

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[25] Aurizon Network proposal, pp. 20–21.
[26] Aurizon Network proposal, p. 20, Aurizon Network response, pp. 3, 24.
[27] Aurizon Coal, p. 2; Glencore submission, pp. 1–2; QRC submission, pp. 9–10.
[28] QCA, *Aurizon Network's 2019–20 revenue adjustment amounts*, final decision, December 2020.
[29] Aurizon Network proposal, p. 19.
[30] Aurizon Network amendment, pp. 2–3.

Independent expert

Aurizon Network has proposed to pass through the forecast cost to operate CNCCo (the IE), adjusted to account for a forecast under-spend, and invoicing under-recovery during 2020–21.

We note this pass through is permitted under cl. 4.1(b)(viii) and presently consider that Aurizon Network has accurately calculated the amount.

Tax allowance

The tax allowance is a computation of Aurizon Network's post-tax revenue model. We presently consider that Aurizon Network has accurately calculated its tax allowance adjustment and it is appropriately reflected in the calculation of updated allowable revenues and reference tariffs for 2021–22.

System allowable revenues

We presently consider that the proposed updates satisfy cl. 5.5(h)(ii) of schedule F, which requires the inclusion of revised gtk forecasts and allowable revenues to the extent applicable to that reference tariff variation.

Table 4 System allowable revenues, 2021–22

System	*Non-electric allowable revenues ($m)*	*Electric allowable revenues ($m)*
Blackwater	352.2	74.8
Goonyella	277.2	71.0
Moura	51.9	
Newlands	34.1	
GAPE	124.9	
Total	**840.3**	**145.9**

2020–21 reference tariffs

We presently consider that Aurizon Network's updates to key variables are reflected in its financial models, supporting materials and in the corresponding changes to the reference tariffs for 2020–21.

Table 5 System reference tariffs, 2020–21 ($)

System	*AT1*	*AT2*	*AT3*	*AT4*	*AT5*	*EC*	*QCA levy*	*IE fee*
Blackwater	0.99	2,429.76	7.18	2.56	2.97	0.87	0.00327	0.01485
Goonyella	0.68	1,539.39	5.09	1.03	1.96	0.87	0.00327	0.01485
Moura	1.84	719.63	11.11	1.80	0.00	0.00	0.00327	0.01485
Newlands	1.91	325.41	8.78	1.11	0.00	0.00	0.00327	0.01485
GAPE	1.54	1,5106.30	1.24	1.91	0.00	0.00	0.00327	0.01485

References

Aurizon Network, *Aurizon Network, Newlands System Information Pack—Version 7*, March 2017.

—— *Aurizon Network Maintenance and Renewal Strategy and Budget*, 21 January 2021.

QCA, *Aurizon Network's 2018–19 capital expenditure claim*, decision, May 2020.

— *Aurizon Network's 2018–19 RAB roll-forward*, final decision, July 2020.

— *Aurizon Network's 2019–20 revenue adjustment amount*s, final decision, December 2020.

— *Aurizon Network's 2019–20 capital expenditure claim*, decision, February 2021.

— *Aurizon Network's 2019–20 RAB roll-forward*, final decision, April 2021.

— *Aurizon Network's Newlands FY22 maintenance strategy and budge*t, final decision, May 2021.