

File Ref: 1482902

15 December 2022

Ms Pam Bains
Group Executive Network
Aurizon Network Pty Ltd
GPO Box 456
Brisbane Qld 4001

Dear Ms Bains

Aurizon Network 2021–22 revenue adjustment

The Queensland Competition Authority (QCA) has determined that, with the exception of the WACC adjustment, Aurizon Network has appropriately calculated all the revenue adjustments proposed on 4 November 2022.

The QCA's review of the revenue adjustment is summarised in the attached decision notice. The notice includes a brief overview of the basis of our assessment and our main findings.

The QCA does not accept Aurizon Network's view that the WACC uplift is to apply from 12 November 2021. Rather, it considers that the uplift will apply from 14 March 2022, in accordance with the requirements set out in UT5.

On that basis, the QCA requires Aurizon Network to amend and resubmit its proposal, with the amended uplift date, within 30 days, in accordance with clause 4.3(s)(ii) of schedule F of UT5.

Although the QCA would not ordinarily publish decisions where we are refusing to approve proposed revenue adjustments, in this instance, it considers that publication is appropriate because of the disagreement that exists around the date the uplift applied under UT5 and, in particular, on the meaning of the term 'report date'. This issue is also relevant in other UT5 compliance matters currently under QCA consideration. As such, the QCA intends to publish this decision on 20 December 2022, so that stakeholders can be informed of the QCA's position on the construction of the term.

I am happy to discuss any question you may have on this or any other matters. Should your staff have any specific queries on the attached paper, please direct them in the first instance to Pag Arao-Arao on 07 3222 0560, or by email at pag.arao-arao@qca.org.au.

Yours sincerely



Charles Millstead
Chief Executive Officer

cc: *Jon Windle, Network Regulation Manager, Aurizon Network*

DECISION NOTICE

AURIZON NETWORK'S 2021–22 REVENUE ADJUSTMENT AMOUNTS

15 December 2022

The Queensland Competition Authority (QCA) has refused to approve Aurizon Network's proposed 2021–22 revenue adjustment amount of \$44.6 million.

We are satisfied that Aurizon Network has calculated the adjustment amounts in accordance with clause 4.3 of schedule F to Aurizon Network's 2017 access undertaking (UT5), with the exception of the proposed WACC adjustment. We require that the WACC adjustment be calculated on the basis that the approved WACC increased (from 5.9% to 6.3%) on 14 March 2022.

We require Aurizon Network to resubmit its 2021–22 revenue adjustment proposal, with the WACC adjustment based on the amended uplift date, within 30 days.

Each year Aurizon Network submits a proposal to refund or recoup any over- or under-recovery of its allowable revenues. The proposed adjustments are the difference between Aurizon Network's maximum allowable revenue (MAR) plus any allowable adjustments (collectively termed the adjusted allowable revenue (AAR)), and the total actual revenue (TAR) collected in that year from the approved AT2–AT5 reference tariffs.

Revenue adjustment amounts for 2021–22

On 4 November 2022, Aurizon Network submitted¹ its revenue adjustment proposal for a net recovery of \$44.6 million for the 2021–22 financial year (see Table 1 for system-specific over- and under-recoveries).

¹ UT5 requires that Aurizon Network submit its yearly revenue adjustment amounts by 31 October—but also provides for the QCA to grant an extension of time, upon written request, should the extension be reasonable or necessary (sch. F, cl. 4.3 (m), (o)). The QCA agreed to a four-day extension for Aurizon Network to provide its 2021–22 revenue adjustment amounts (to 4 November 2022).

Table 1 Revenue adjustment amounts 2021–22 (\$ million)

System	AT2–4 (non-electric)	AT5 (electric)	Total
Blackwater	17.7	(0.6)	17.1
Goonyella	0.6	11.1	11.7
Moura	2.9	–	2.9
Newlands	1.3	–	1.3
GAPE	11.6	–	11.6
Total	34.2	10.5	44.6

Note: Numbers may not sum due to rounding. Negative values indicate an over-recovery, and thus a refund.

Source: Aurizon Network, FY2022 Revenue Adjustment – Explanatory Memorandum, November 2022, p. 3.

Revenue adjustment assessment process

UT5 (sch. F, cl. 4.3) sets out a process for assessing Aurizon Network's proposed revenue adjustment.

We will approve an application if we are reasonably satisfied that the adjustment amount is calculated in accordance with clause 4.3 (sch. F, cl. 4.3(r)). The approved revenue amounts then adjust the second-year's system allowable revenues and corresponding AT2–AT5 reference tariffs (sch. F, cl. 4.4).

If we are not reasonably satisfied that the revenue adjustment amount is calculated in accordance with clause 4.3, we must refuse to approve it. In that case, we must then issue a notice to Aurizon Network, explaining our reasons for the refusal and the way Aurizon Network is required to amend its proposal for resubmission (sch. F, cl. 4.3(s)(ii)).

We have closely checked Aurizon Network's application and supporting models² against all available information (both publicly available and confidentially provided), to determine whether the calculations in this revenue adjustment process have been performed in accordance with UT5.

Stakeholder consultation

We invited stakeholder submissions on Aurizon Network's 2021–22 revenue adjustment proposal and received a submission from the Queensland Resources Council (QRC).³

Total actual revenues and adjustments

The TAR represents the collected revenues made up of the system reference tariffs—including cross-system AT2–AT5 tariffs (sch. F, cl. 4.3(d)–(k)), billed to access holders on all railed volumes in the financial year, any take or pay amounts payable, and any transfer and relinquishment fees received.

Aurizon Network submitted detailed monthly data to demonstrate the calculation of the TAR.

² Aurizon Network provided models for take or pay, WACC adjustment, rebate adjustment, transfers, electricity connection cost adjustments, and the revenue cap adjustment calculations.

³ The QRC's submission is available on our [website](#).

Take or pay, relinquishment or transfer fees, and cross-system revenues

Aurizon Network provided billing information on how it calculated the take or pay revenues under its access contracts.

Take or pay amounts were triggered in the Goonyella and Moura systems in 2021–22, with the take or pay recovering the full amount of AT2–AT4 shortfall. Take or pay was not triggered in the Blackwater, Newlands and GAPE systems (where actual volumes exceeded system forecasts, when adjusted for Aurizon Network cause and force majeure cancellations).

Transfer fees were collected in the Goonyella and GAPE⁴ systems and included in the relevant TAR.⁵ The transfer fees received, total cross-system proceeds and take or pay revenues for 2021–22 were \$63.7 million, comprising \$57.1 million from non-electric customers and \$6.6 million from electric customers.

We are satisfied that:

- the take or pay revenues were accurately estimated on the basis that railings within a nominated month, for the purposes of annual and variable take or pay, were consistently treated
- adjustments for Aurizon Network cause and force majeure events were appropriately attributed, and the methodology in the relevant access undertakings were applied correctly.

We confirm that Aurizon Network has correctly calculated the take or pay revenues that applied for agreements signed during each undertaking period (sch. F, cl. 4.3(d)(ii)).

Total actual revenues

Aurizon Network submitted TAR of \$942.6 million for 2021–22, including all take or pay and cross-system traffic revenues received (see Table 2).

⁴ The repayment of the GAPE transfer fee amount relates to the AT3 tariff and will be included in 2023–24 reference tariffs.

⁵ Aurizon Network noted that the GAPE transfer fee amount relates to the AT3 tariff (that relates to specific Goonyella system enhancements paid by GAPE access holders). Aurizon Network requested that the QCA approves the repayment of this transfer fee within AT3 in the 2023–24 reference tariffs.

Table 2 Total actual revenues 2021–22 (including take or pay and cross-system revenues) (\$ million)

<i>System</i>	<i>AT2–AT4 (non-electric)</i>	<i>AT5 (electric)</i>	<i>Total</i>
Blackwater	332.1	74.7	406.8
Goonyella	277.3	59.6	336.9
Moura	51.9	–	51.9
Newlands	33.2	–	33.2
GAPE	113.7	–	113.7
Total	808.3	134.3	942.6

Note: Numbers may not sum due to rounding.

Source: Aurizon Network, FY2022 Revenue Adjustment – Explanatory Memorandum, November 2022, p. 13.

We are satisfied that Aurizon Network calculated its system and cross-system tariff revenues in accordance with the 2021–22 annual review of reference tariffs⁶ and the current approved undertaking.

Volumes

Aurizon Network's TAR is based on amounts billed against each customer's actual railings achieved in that period (see Table 3). All coal systems recorded actual railings that were lower than the system forecast.

Table 3 Forecast and actual volumes 2021–22 (million net tonnes)

<i>System</i>	<i>Approved forecasts</i>	<i>Actual tonnages</i>	<i>Variance (%)</i>
Blackwater	62.6	58.3	–7%
Goonyella	117.7	105.6	–10%
Moura	13.6	12.0	–12%
Newlands	14.1	13.9	–1%
GAPE	18.8	16.8	–11%
Total	226.9	206.5	–9%

Source: Aurizon Network, FY21 Revenue Adjustment Amounts – Explanatory Memorandum, November 2022, p. 7.

The gross tonne kilometres and net tonnes submitted by Aurizon Network were reconciled to performance reporting data on its customer portal and Aurizon Network's 2021–22 report on full-year results.

System allowable revenues and adjustments

Annual system allowable revenues represent the approved amounts Aurizon Network is set to recover in each year during the term of its approved undertaking. Each system's allowable revenues are published in schedule F of UT5.

Under the revenue adjustment process (sch. F, cl. 4.3(c)), Aurizon Network can submit adjustments to the annual allowable revenues. Aurizon Network's 2021–22 proposal outlined its claim for the following cost adjustments to the allowable revenue (under sch. F, cl. 4.3(c)).

⁶ QCA, [Annual review of reference tariffs](#), decision notice, 28 May 2020.

WACC adjustment

The WACC adjustment accounts for the difference between the actual approved WACC and the approved WACC that was used to determine the relevant reference tariff for the year (UT5, sch. F, cl. 4.3 (c)(i)).

The approved WACC used in determining 2021–22 reference tariffs was 6.3%. This assumed that the ‘report date’, which triggers the increase of the approved WACC (from 5.9% to 6.3%)⁷, would occur by 1 July 2021.⁸ However, as this did not occur, an adjustment is required to reflect that the approved WACC remained at 5.9% for part of the year.

Aurizon Network proposed a net return to access holders of \$9.3 million, on the basis that the report date occurred on 12 November 2021. This was when Aurizon Network provided its preliminary response to the independent expert’s Initial Capacity Assessment Report (ICAR). On that basis, Aurizon Network has calculated a net return to access holders of \$9.3 million, to account for the difference in the approved WACC applied (see Table 4 for system-specific adjustments).

Table 4 WACC adjustment by system (\$ million)

<i>System</i>	<i>AT2–AT4 WACC adjustment</i>	<i>AT5 WACC adjustment</i>	<i>Total</i>
Blackwater	(3.6)	(0.6)	(4.2)
Goonyella	(2.5)	(0.4)	(2.9)
Moura	(0.5)	–	(0.5)
Newlands	(0.4)	–	(0.4)
GAPE	(1.3)	–	(1.3)
Total	(8.3)	(1.0)	(9.3)

Note: Numbers may not sum due to rounding.

Source: Aurizon Network, FY2022 Revenue Adjustment – Explanatory Memorandum, November 2022, p. 10.

We do not accept that Aurizon Network’s provision of its preliminary response to the ICAR (on 12 November 2021) meets the definition of the report date (Box 1), given the natural and ordinary meaning of the language of its definition used in its context and having regard to its purpose and consequences. Instead, we consider that definition refers to the detailed report Aurizon Network subsequently provided (on 14 March 2022), in accordance with the requirements of clause 7A.5(a)(iii) of UT5.

⁷ See the definition of the approved WACC (UT5, Part 12).

⁸ Aurizon Network, *FY2022 Revenue Adjustment – Explanatory Memorandum*, November 2022, p. 10.

Box 1 The 'report date'

Under UT5, the term 'report date', when satisfied, triggers two main effects. First, if a report date occurs before 1 July 2023, it triggers a financial benefit for Aurizon Network, by increasing the approved WACC (from 5.9% to 6.3%). Second, it triggers potential liability for Aurizon Network under the capacity provisions of Part 7A of UT5, where Aurizon Network is held accountable for meeting the deliverable network capacity set by the independent expert—and will compensate customers for the effect of any shortfalls in the delivery of train service entitlements in specified circumstances

The term is defined in UT5 (Part 12) to mean:

The date on which the last of the following events has occurred:

- (a) *the Independent Expert has provided the Initial Capacity Assessment Report to Aurizon Network and the Chair of the Rail Industry Group; and*
- (b) ***Aurizon Network notifies the Chair of the Rail Industry Group of the proposed options for addressing any Existing Capacity Deficits identified in the Initial Capacity Assessment Report, provided that where the Initial Capacity Assessment Report does not identify any Existing Capacity Deficits, Aurizon Network will be deemed to have satisfied the notification requirement in this paragraph (b) on the date that the Initial Capacity Assessment Report has been provided in accordance with paragraph (a). (emphasis added)***

The independent expert issued the ICAR on 28 October 2021—identifying existing capacity deficits. On that basis, the issue to be determined is the date of the appropriate notification of the proposed options for addressing the identified capacity deficits to the chair of the Rail Industry Group (RIG).

In particular, we note that the definition:

- should not be construed in abstract, but should rather be considered having regard to the concepts and processes set out in UT5, particularly those in clause 7A.5
- uses the expression 'the proposed options for addressing' the capacity deficits—so is referring to:
 - a particular kind of notification having regard to the process set out in clause 7A.5 (not any notification, made at any time)
 - options that Aurizon Network is proposing, for addressing these capacity deficits (not merely options which could, or might, be proposed)
- requires that the proposed options be provided to the chair of the RIG—which is a requirement for the detailed report (but not the preliminary report).

On this, we note that the process outlined in Part 7A.5 provides that Aurizon Network's preliminary report will include its preliminary views on solutions to address the capacity deficits (with indicative timeframes)⁹—to assist with the subsequent consultation¹⁰ and possible agreement with users—and will accordingly be provisional and tentative in nature. It is only after consultation that Aurizon Network must set out proposed transitional

⁹ UT5, cl. 7A.5(a)(i)(B).

¹⁰ UT5, cl. 7A.5(a)(i)(A), (a)(ii).

arrangements that it considers would most effectively and efficiently address the capacity deficits¹¹—for the independent expert's review and recommendation, where agreement with users has not been reached.¹²

Beyond this, we note that linking an increase to the WACC to the delivery of the detailed report provides Aurizon Network with a financial incentive to progress its consultation and engagement with customers, with a view to expediting the process and ultimately putting transitional arrangements in place.¹³ By contrast, it is difficult to see the real need to provide Aurizon Network with an incentive to set out only its preliminary options (where these are likely to be provisional in any event). Indeed, if the WACC uplift was simply linked to providing a statement of proposed options, Aurizon Network would have an incentive to deliver the report before proper consultation had been undertaken and analysed, and so could potentially deliver a report that was of no particular use.¹⁴

Accordingly, we require that Aurizon Network calculate the WACC adjustment on the basis that the approved WACC increased (from 5.9% to 6.3%) on 14 March 2022.

Maintenance cost adjustment

The maintenance cost adjustment accounts for the difference between the approved maintenance indicator and actual maintenance costs for the year, where actual maintenance costs are lower.¹⁵

Overall, actual maintenance costs for 2021–22¹⁶ were higher than the maintenance indicator for 2021–22. Aurizon Network has calculated a net recovery from access holders of \$9 million (see Table 5 for system-specific adjustments).

¹¹ UT5, cl. 7A.5(a)(iii).

¹² UT5, cl. 7A.5(d).

¹³ At the same time, Aurizon Network's position is protected, by allowing it to obtain this incentive within a limited timeframe (i.e. 3 months after the ICAR was released). It is noted, however, that Aurizon Network took longer than that, agreeing to provide more time for additional consultation with stakeholder at stakeholders' request.

¹⁴ Aurizon Network would only have a limited disincentive to do so under the rebate provisions, as during this initial period a liability for rebates would only arise if there was a failure to maintain the capacity reported in the independent expert's initial capacity assessment.

¹⁵ UT5, sch. F, cl. 4.3 (c)(ii).

¹⁶ The QCA approved Aurizon Network's maintenance cost claim for 2021–22 on 16 November 2022.

Table 5 Maintenance cost adjustment by system, AT2–AT5 (\$ million)

<i>System</i>	<i>Maintenance indicator</i>	<i>Actual maintenance costs</i>	<i>Variance</i>	<i>Variable maintenance</i>	<i>Total maintenance adjustments</i>
Blackwater	65.0	66.2	1.2	1.7	2.9
Goonyella	61.1	62.5	1.4	2.3	3.7
Moura	12.4	12.2	(0.1)	0.7	0.6
Newlands	3.8	4.0	0.2	0.1	0.3
GAPE	8.8	9.2	0.5	1.0	1.5
Total	151.1	154.2	3.1	5.9	9.0

Note: Numbers may not sum due to rounding.

Source: Aurizon Network, FY2022 Revenue Adjustment – Explanatory Memorandum, November 2022, pp. 10–11.

We confirmed that actual maintenance costs are consistent with those included within the 2021–22 annual maintenance report, and the maintenance indicator is consistent with the values approved. Therefore, we are satisfied with Aurizon Network's claim under the maintenance cost adjustment.

Non-electric operating expenditure allowance

Commencing 1 July 2021, Aurizon Network calculates an adjustment to the component of allowable revenues relating to the recovery of non-electric operating expenditure allowance (NOEA)¹⁷. This adjustment to the NOEA is based on the difference between actual and the forecast consumer price index (CPI) in UT5.

Table 6 Non-electric operating expenditure allowance 2021–22 (\$ million)

<i>System</i>	<i>Non-electric operating expenditure allowance</i>	<i>NOEA adjustment</i>
Blackwater	53.9	2.7
Goonyella	12.9	0.6
Moura	58.8	2.9
Newlands	5.8	0.3
GAPE	3.6	0.2
Total	135.1	6.7

Note: Numbers may not sum due to rounding.

Source: Aurizon Network, FY2022 Revenue Adjustment – Explanatory Memorandum, November 2022, p. 11.

We have confirmed that both forecast and actual CPI used to calculate the NOEA adjustment amount are correctly applied as required in the undertaking, and that actual CPI corresponds to published information.¹⁸

¹⁷ UT5, sch. F, cl. 4.3(c)(iii).

¹⁸ Australian Bureau of Statistics, 'Tables 1 and 2. CPI: All Groups, Index Numbers and Percentage Changes' [time series spreadsheet], [Consumer Price Index](#), Australia, September quarter 2022, accessed 30 September 2022.

Electricity connection costs

The electricity connection cost adjustment accounts for the difference between forecast and actual costs incurred in connecting to an electric transmission or distribution network.¹⁹ This adjustment is only applicable to Aurizon Network's electrified systems.

Aurizon Network has calculated a net return to access holders of \$0.4 million. This is the difference between the amounts paid to Powerlink Queensland and Ergon Energy for the connection of Aurizon Network's electric infrastructure to their respective electricity networks and the forecast costs (used for determining the AT5 reference tariff components for 2021–22).

We consider these costs have been appropriately tracked, and invoices Aurizon Network supplied reflect actual costs incurred.

Rebates adjustment

To account for the difference between forecast and actual rebate payments made in 2021–22, Aurizon Network has calculated a net return to access holders of \$4.9 million (see Table 7 for system-specific rebates).

This adjustment is the difference between forecast and actual rebate payments made to access holders who have provided Aurizon Network with funds to underwrite capital investments (sch. F, cl. 4.3 (c)(viii) of UT5).

Table 7 Aurizon Network rebates by system totals (\$ million)

System	Total
Blackwater	(4.2)
Goonyella	(1.0)
Newlands	0.3
Total	4.9

Note: Numbers may not sum due to rounding. Negative values indicate an over-recovery.

Source: Aurizon Network, FY2022 Revenue Adjustment – Explanatory Memorandum, November 2022, p. 15.

Aurizon Network provided a detailed model of the rebate adjustments. We have verified these amounts and are satisfied with the adjustments made.

Decision

For the reasons discussed above, we consider Aurizon Network has appropriately calculated the revenue adjustment amounts, with the exception of the WACC adjustment. Our decision is to refuse to approve the total revenue adjustment amounts and to require Aurizon Network to amend and resubmit its proposal, within 30 days, with the amended uplift date (of 14 March 2022).

¹⁹ UT5, sch. F, cl. 4.3 (c)(iv).