

SUBMISSION TO THE QUEENSLAND COMPETITION AUTHORITY

**SUBMISSION IN RESPONSE TO THE
QCA DRAFT DECISION ON UT4.2**

APRIL 2015

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1. Executive summary

Anglo American Coal Australia (**Anglo American**) welcomes this opportunity to provide a submission on the Queensland Competition Authority's (**QCA**) Draft Decision in response to Aurizon Network Pty Limited's (**Aurizon Network**) 2014 Draft Access Undertaking (**UT4.2**). Anglo American has provided the QCA with a number of submissions throughout the UT4 decision process and it notes that this submission is intended to build on the comments that it has already made in those previous submissions, as well as address specific issues raised by the QCA in the Draft Decision.

Anglo American agrees with the statement made by the QCA that "the 2014 DAU provides Aurizon Network with an inappropriate level of discretion over the setting of access charges and reduces the accountability and transparency."¹ Anglo American, along with a number of other stakeholders, has expressed this opinion on a number of occasions from the beginning of the UT4 process.

Anglo American fully supports the QCA's comments that, while UT3 should and has provided a relevant benchmark for the assessment of the reasonableness of UT4, it is not a "model regime" to attempt to replicate, nor does it appropriately reflect the state of play in the current Queensland coal market.² As such, Anglo American agrees with the QCA that while the terms of UT3 are referable, they should really form a base requirement for the creation of UT4.

Anglo American also supports the QCA's attempts to ensure that the ringfencing and non-discrimination principles in UT4 are effective and flexible for protecting against conflicts and inappropriate advantage created in favour of the Aurizon Group's interests. Specifically, Anglo American agrees with the QCA that:

Aurizon Network should be prohibited from leveraging its unique position as the sole operator of the CQCN to provide its related parties (including any related operator) a commercial advantage over their respective competitors...³

Anglo American submits that this also includes ensuring that Aurizon Network is not able to use its monopoly position to influence non-contestable or marginally competitive markets that it provides services into. If these markets are not also protected as a result of the scope of the Access Undertaking, it will reduce the effectiveness of the existing regulation and allow Aurizon Network the opportunity to engage in monopoly activities even though it is a regulated entity in its operation of, and provision of access to, the Central Queensland Coal

¹ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 361.

² Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 20.

³ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 356.

Network (CQCN). Anglo American believes that this would be contrary to the theory and purpose behind natural monopoly regulation.

Anglo American notes that the Queensland Resources Council (QRC) has also made extensive submissions at all stages of the UT4.2 process. Anglo American has had the opportunity to review the comments made by the QRC and, other than the express comments made in this submission, Anglo American generally supports the comments made by the QRC on behalf of industry.

2. Part 2: Intent and scope

2.1 Introduction

Anglo American has previously raised major concerns in relation to the drafting of Part 2 on the intent and scope of UT4. Anglo American acknowledges that Aurizon Network has made some attempt to address stakeholders' concerns between UT4 and UT4.2, however, the Draft Decision has highlighted the major aspects that remain inappropriate. As such, Anglo American supports the Draft Decision in relation to:

- (a) recommendations 3.1(a)-(c) and (e)-(g) without further comment; and
- (b) recommendation 3.1(d), with the further comment that in light of the Aurizon Group's recent diversification of its interests, these protections against the abuse of Aurizon Network's natural monopoly position in favour of its related entities in upstream and downstream markets are essential to ensuring that the Access Undertaking actually promotes the public interest, including the public interest in having competition in markets (whether or not in Australia) as required by section 138(2)(d) of the QCA Act.

2.2 Electricity supply and sale

Anglo American has previously raised concerns in relation to the provisions relating to the supply and sale of electricity in UT4 and UT4.2. After considering the Draft Decision, including recommendation 3.3, Anglo American remains of the view that the supply of electricity should be covered by UT4.

For users of the CQCN, there is simply no other way to procure electricity supply than through Aurizon Network. Clause 2.4(a) should provide that UT4 must be consistently applied to all Access Holders in addition to those entities identified in the QCA Draft Decision. An example of where this may be important would be that UT4 should be consistently applied to different Access Holders in respect of the application of the contested train path matrix. This is particularly so if a coal producer enters into an Access Agreement in its own name and becomes an "Access Holder" in its own right. Should a coal producer

decide to enter into an Access Agreement in its own name in respect of a small amount of capacity (for example, 3 mtpa) it will be difficult, if not impossible, to obtain electricity supply on reasonable terms and conditions. Even if the coal producer obtains supply, the lack of economies of scale will mean that coal producer will pay significantly more for its electricity supply and this may affect the competitiveness of the end user. Any matter that affects the competitiveness of the coal producer in these circumstances will constitute a disincentive to enter the alternative form of Access Agreement, that is, an Access Agreement in its own name.

The declaration in section 250 of the QCA Act clearly includes electric assets and Aurizon Network is entitled to recover the costs of those assets. Anglo American submits that it is inconsistent with the declaration of the CQCN to require regulation of all aspects of the natural monopoly facility, and yet to permit Aurizon Network to charge monopoly prices for a service which is an essential component of that natural monopoly. Anglo American submits that only regulating some aspects of Aurizon Network's monopoly leaves users subject to the very monopoly rent behaviour that the Access Undertaking is designed to protect, against especially where that provision could be used to discriminate in favour of an Aurizon Network-related entity.

In instances where Aurizon Network, by virtue of its position as a natural monopolist, can control or impact upon services associated to the provision of below rail access which are not contestable, or at best are weakly contestable, it is important for the Access Undertaking to regulate those services as well. This generally includes services that Aurizon Network does not permit a third party to operate, or otherwise services that it is so inefficient or uneconomic to obtain from an independent third party, meaning that Aurizon Network is the only viable option for a price. The alternative is that Aurizon Network has incentive to exploit those associated services for anti-competitive prices (realistically, to price only marginally below the price at which it is competitive for independent third parties to enter the market meaning that it will discourage those third parties from doing so) so as to continue to earn monopoly rent even though the main service is appropriately regulated. This allows Aurizon Network to undermine the entire purpose of natural monopoly regulation. Anglo American submits that the sale and supply of electricity is just one of these services that should be regulated by virtue of Aurizon Network's monopoly position, otherwise it will risk Aurizon Network having the scope to abuse its significant market position.

Anglo American reiterates its earlier submission on this point that Aurizon Network should be required (as it is not an electricity retailer) to provide the supply and sale of electricity to users on a cost pass through basis. This meets Aurizon Network's legitimate business interests

under the QCA Act (as it will not suffer any losses in relation to the supply or sale of electricity) and also ensures the legitimacy of the Access Undertaking, as Aurizon Network does not have the opportunity to extract monopoly prices from users for what should really be a small element of its services. Anglo American also notes that the QRC has made a similar suggestion in its submission on the QCA Draft Decision, specifically that Aurizon Network should be required to commit to supply electricity.

Anglo American strongly supports recommendation 3.4 for the inclusion of specific dispute resolution provisions to govern disputes related to the supply and sale of electricity.

2.3 "Associated Services"

Anglo American remains of the view that UT4 should include a definition of "Associated Services" in UT4. The services that Anglo American believes should be covered as "Associated Services" include:

- (a) RIM and train control for spurlines;
- (b) level and other crossings;
- (c) land leases (leasing corridor land and land owned or leased by Aurizon Network);
- (d) design, scope and standard reviews (for example, where Aurizon Network requires infrastructure to comply with minimum standards);
- (e) rail and related infrastructure relocation;
- (f) Transfer Facilities Licences (**TFLs**); and
- (g) sale and supply of electricity (as discussed in section 2.2 above).

In particular, Anglo American remains of the view that the majority of these services are not contestable (or only very weakly contestable).

By way of example Anglo American has had occasion to deal with Aurizon Network's projects team from time to time in relation to operations or activities located near parts of the CQCN rail infrastructure. Although this team is part of Aurizon Network, payment at set rates for their time and project management services, including any contractors, is an Aurizon Network requirement. If these services are provided by employees of Aurizon Network, then Anglo American believes that their employment costs have already been paid for through the Reference Tariffs. If they are not employees of Aurizon Network, then Anglo American notes that the services that they provide, while not claimed by Aurizon Network as directly referable to the provision of Access, are non-contestable as they must be carried out by

Aurizon Network employees or contractors due to the impact on the CQCN. In this instance, therefore, Anglo American notes that these "project" services are not contestable and should be regulated under the Access Undertaking to ensure at the very least that Aurizon Network is not adding a margin and double recovering in providing these services. In any instance where the "projects" team fees are billed for Access-Related Services, these fees should be accounted for as part of the revenue cap and in relation to overheads to ensure that Aurizon Network is accounting for such revenue clearly related to operation of the CQCN.

In relation to rail relocation (as raised by the QCA), Anglo American does not agree that it is possible for competition in relation to the relocation of any section of mainline track or related infrastructure (such as transformers) either temporarily or permanently. There is no possibility (nor would it be appropriate) for another party to be able to coordinate the removal and relocation of mainline track, other than with Aurizon Network providing its consent. Anglo American also believes that a service fee for relocation of mainline track falls within the scope of section 250 of the QCA Act, as the mainline track is part of a coal system within the meaning of section 250(3)(a). At the very least, it is below rail infrastructure that is "directly or indirectly connected to a [coal system] and owned or leased by the owner or lessee of the coal system" within the meaning of section 250(3)(b). Also, such works should be subject to similar scope and prudence reviews as Expansions to ensure the project and related costs are prudent.

Anglo American notes the view of the QCA that regulation of Private Infrastructure falls outside of section 250 of the QCA Act. Anglo American, however, believes that Private Infrastructure falls within the scope of section 250 because:

- (a) balloon loops and spurlines have always fallen within the scope of the Access Undertakings and been subject to regulation and Aurizon Network should not be allowed to engage in the practice in UT4 of forcing users to give Aurizon Network unregulated revenue by pretending they have options for Short Private Infrastructure. The preferred alternative is that balloon loops and spurlines are treated as part of the CQCN and separately funded by the coal producer through Access Conditions or the User Funding Regime; and
- (b) Short Private Infrastructure where the coal producer effectively must use Aurizon Network to construct the Private Infrastructure and use Aurizon Network for RIM and train control services is effectively leased to Aurizon Network and clearly falls within section 250 of the QCA Act.

Anglo American also has concerns around the cost and provision of rail grinding and track laying services. It is Anglo American's understanding that these services are provided by Aurizon Operations and not Aurizon Network. Anglo American believes that these services are essential to the operation and maintenance of the CQCN and that there should be full transparency around how these services are contracted and conducted, particularly if they are truly contestable, in which case competitive rates should be achievable from parties other than a related entity.

While Anglo American notes that it (and the QRC) raised the concept of "Associated Services" (which was not included in UT3), this was specifically in response to Aurizon Network's UT4 drafting regarding the extremely narrow scope of "Core Access-related Functions". Anglo American notes that the QCA has made amendments to clause 3.5 of UT4.2 to address the issue of scope, however, Anglo American does not believe that these amendments have addressed the issue that a number of services inextricably linked with the provision of Below Rail Services still remain outside the scope of the Access Undertaking.

2.4 Incentive mechanism

Anglo American notes that the QCA has inserted the concept of an incentive mechanism in clause 2.8. Anglo American has previously made extensive submissions against the concept of an incentive mechanism. Anglo American continues to object to the concept.

Anglo American does not object solely to the current drafting of the incentive mechanism, but rather to the concept as a whole. Anglo American understands that throughout the various undertaking evolutions provided by Aurizon Network there has been a move from price based regulation, to revenue cap regulation; subsequently followed by a shift from Aurizon Network holding some level of risk to Aurizon Network holding minimal risk.

Anglo American does not believe that the concept of an incentive mechanism is appropriately applied to Aurizon Network's current form of regulation. If the QCA believes that an incentive mechanism is appropriate for ensuring that Aurizon Network is incentivised to increase and maintain throughput, Anglo American believes that the QCA should consider the form of regulation applied to the CQCN, rather than an artificially applied incentive mechanism. Anglo American believes that the incentive created by price cap regulation is a truer and more appropriate form of incentive regulation and the QCA might consider this for UT5, rather than forcing an artificial created incentive mechanism which is inappropriate.

If the QCA remains of the view that an incentive mechanism is appropriate, Aurizon Network must not be entitled to an incentive to deliver contracted volume.

2.5 Drafting issues

Anglo American also raises a number of drafting issues to assist in ensuring consistency and clarity in the terms of UT4, as follows:

- (a) clauses 2.2(g), (h) and (i) should all be replicated in the substantive obligations in UT4. Clause 2.2 as an objects clause can only be used to assist in interpretation of substantial clauses where there is an ambiguity, however, it contains important provisions which require enforceability;
- (b) clause 2.2(h)(i) refers to an objective of UT4 being that all transactions between Aurizon Network and Related Operators in relation to Access are conducted on an arms-length basis. Anglo American believes that this clause should refer to "Related Operators, Related Competitors and Third Parties". For example, it should be an objective of UT4 that Aurizon Network cannot enter into a Transfer Facilities Licence with a related coal mine on terms other than on an arms-length basis and but only for:
 - (i) performance above contracted tonnes; and/or
 - (ii) avoiding capex by adopting proposed solutions to deliver capacity without capex;
- (c) clause 2.4(a) should extend to "Access Holders" and "Train Operators". UT4 should be consistently applied to all Access Holders and Train Operators. For example, a coal producer who decides to become an Access Holder should be treated consistently with other Access Holders in the application of the contested train path matrix. Clause 2.4(b) is insufficient to deal with this as proving unfair differentiation is too high a bar. It would be appropriate to make this obligation subject to either the QCA Act, UT4 or the relevant Access Agreement expressly providing for inconsistent treatment.

Attachment A sets out other minor drafting considerations.

3. Part 3: Ringfencing obligations

3.1 General

Anglo American supports the QCA's Draft Decision in relation to the amendments to the Aurizon Network ringfencing obligations. With the expansion and diversification of the Aurizon Group business into new areas, including into related rail haulage, mining and port areas, Anglo American believes that the ringfencing requirements are important for user and investor confidence in the regulation, as well as the protection of competitive industries that are upstream and downstream of Aurizon Network's monopoly position in the supply chain.

Aside from the issue of the regulation of "Associated Services" (discussed in relation to "Part 2 Intent and Scope" because of the treatment of this issue by the QCA), Anglo American believes that the QCA has adequately addressed its concerns in relation to Aurizon Network's weakening of the ringfencing obligations.

3.2 Issues raised by Aurizon Network's information request - "Confidential Information"

Anglo American supports the QCA's definition of Confidential Information. Due to Aurizon Network's unique position in the supply chain, it will have access to extensive confidential material that is commercially sensitive to mine operators, train operators and port facilities. Anglo American notes that because of its high level of vertical integration with businesses in these other levels of the supply chain, it is essential that the protections around Confidential Information received by Aurizon Network be as strict as possible.

Anglo American notes that sub-paragraph (g) of the definition of Confidential Information allows the holder of the Confidential Information to make a judgment call as to when "the disclosure of the information by the recipient would no longer be expected to affect the commercial affairs of the owner of the information". Anglo American submits that this introduces an unnecessary subjectivity into the definition. Rather, this sub-paragraph should allow disclosure only "where the owner of the information has notified the recipient in writing that the owner no longer considers that disclosure of the information will affect its commercial affairs". This ensures that there is no error of judgment by the recipient and also provides it with certainty in its disclosure of information obligations.

However, Anglo American is concerned about the use by Aurizon Network of disclaimer clauses and confidentiality clauses on a broad range of documents (for example, general presentations). This information should be able to be provided to the QCA for the purposes of the QCA discharging its statutory duties. Anglo American believes that UT4 should address this issue, either by:

- (a) an exemption to the definition of Confidential Information for information provided to the QCA and an obligation not to make agreement or representations inconsistent with the provision; or
- (b) the incorporation of a clause in UT4 specifically allowing parties to provide information to the QCA even where the information is subject to a confidentiality obligation, as long as the information is treated confidentially by the QCA. This could be similar to the waiver contained in clauses 3.19(b) and (c) of the QCA Draft Decision.

Anglo American prefers the second option, but considers the first option to be workable.

Finally, Anglo American notes that Aurizon Network has raised a question in its information request to the QCA (**Aurizon Network Information Request**)⁴ regarding confidential information that it obtains outside its role of providing access. Anglo American supports the QCA's response as Anglo American similarly is not aware of any instance where Aurizon Network would be receiving confidential information that falls outside its role of Below Rail Services (unless as part of the allegedly contestable services discussed above). Anglo American cannot make any further comment until Aurizon Network responds on this point and, therefore, Anglo American assumes that an opportunity will be provided to comment on this issue if Aurizon Network submits evidence of situations where it receives Confidential Information outside of its role to provide Below Rail Services.

3.3 High-Risk Personnel

Anglo American believes that the list of High-Risk Personnel should include all executive managers of Aurizon Network (including all Executive Vice- Presidents and Vice-Presidents). Anglo American believes that this should best be expressed as defining High-Risk Personnel to include "all Executive Vice-Presidents and Vice-Presidents of Aurizon Network, as well as anyone else involved in the executive or management teams of Aurizon Network."

While Anglo American notes that there have been very few instances where any stakeholder has suggested that there has been a breach of the ringfencing provisions within the Aurizon Group of companies, Anglo American notes that it is extremely difficult for stakeholders to have any oversight of evidencing such a claim. Because of this, Anglo American believes that the QCA should have a clearly expressed audit right to investigate the businesses of the Aurizon Group in any instance where there is a suggested breach of the ringfencing provisions which users can provide sufficient information to create doubt of a breach. The ringfencing provisions are some of the most important drafting for protecting competitive markets from the natural monopoly owned and operated by Aurizon Network and Anglo American believes that it is essential for the stakeholders to be able to rely on the QCA to have sufficient ability to investigate the actions of the Aurizon Group in any instance where competition in a relevant market might be impacted by a breach of the ringfencing provisions.

3.4 Line diagrams

Anglo American completely supports the QCA's Draft Decision to reinstate the provisions relating to the line diagrams showing above-rail and below-rail division of assets within the Aurizon Group. Anglo American believes that this is essential for ensuring that the correct assets are accounted for by the Aurizon Group, particularly in respect of what is to be paid for

⁴ Aurizon Network, *Request for Information on the QCA's Draft Decisions* (3 March 2015).

by Access Holders as part of regulated access to the CQC and what is being used by other parts of the Aurizon Group.

Anglo American also believes that the QCA should require that the RAB that Aurizon Network earns its revenue from is in line with the final line diagrams submitted for UT4. Anglo American believes that this should be subject to independent audit of the assets used to calculate the RAB in light of the finalised line diagrams submitted the commencement of UT4. As Aurizon Network's RAB will have been calculated from these asset divisions, Anglo American does not believe that this is a large task and should be completed by an independent third party assessor appointed by the QCA and provided with sufficient information by Aurizon Network to complete and provide to the QCA an accurate assessment within six months of the commencement of UT4. Anglo American believes that this process should be repeated prior to commencement of each undertaking period when the MAR is calculated and reviewed by the third party assessor with updated information provided by Aurizon Network to ensure that any amendments to the line diagrams are reflected in the RAB calculations. As this information will be used to determine the RAB and therefore appropriate revenue, Anglo American does not see this annual process as an expensive or time consuming process.

3.5 Drafting issue

Anglo American also believes that clause 3.6(a) should prohibit Below Rail Services being undertaken by a "Related Operator" or a "Related Competitor".

4. Part 5: Access Agreements

Anglo American broadly supports the QCA's Draft Decision to simplify and streamline the Access Agreements. Anglo American notes that the majority of changes made by the QCA are sustainable and address real problems with the draft UT4 Access Agreements as submitted by Aurizon Network. In particular, Anglo American notes that the QCA's amendments address a number of concerns that Anglo American raised in relation to discrepancies between Train Operator-held Access Rights and End User-held Access Rights. Anglo American supports the QCA amending the Access Agreements in order to ensure that users are free to determine the most appropriate manner of holding and dealing with Access Rights.

In saying that, Anglo American notes that there are a number of outstanding issues raised by the redrafted Access Agreements. Anglo American believes that these issues, which have also been raised by the QRC, must be addressed in the QCA's final decision on UT4 or there may be significant flaws in the approved Access Undertaking processes.

Anglo American notes that the Access Agreement still contains a focus on (weekly) fixed scheduling and monthly entitlement. As Anglo American has previously noted, such rigid scheduling restrictions are detrimental where flexibility is required in order to maximise supply chain efficiency and the delivery of supply chain capacity is to be achieved. Anglo American submits, as it has in its Northern Bowen Basin System Rules submission that this focus on fixed scheduling, is particularly unfavourable to users (especially those reliant upon cargo assembly port capacity) by ignoring the related requirements for cargo assembly raiiling.

An ability to flex by + / - 10% in any given calendar month with the entitlement used being counted to overall annual contracted capacity would give users flexibility in railings to meet annual port entitlements and catch up or surge as required. Provided spare capacity is available on any given day, this would enable users to utilise each others' unused capacity when not peaking at the same time and have it count towards their contracted entitlement, rather than rely on "ad hoc" pathing (which is paid for as consumed) and still be exposed to full Take or Pay top up liability if the system trigger test is not achieved.

5. Part 6: Pricing principles

5.1 General Observations on the Draft Decision

Anglo American believes that many aspects of the Draft Decision have sought to adopt an equitable and more appropriate form of regulation than that proposed by Aurizon Network in UT4.2, especially in relation to pricing and the pricing principles.

In particular, Anglo American supports (without any further comments) the QCA's position in relation to recommendation 16.1, to ensure that Aurizon Network includes more practical and appropriate price discrimination protections due to the Aurizon Group's constantly expanding and diversifying interests. Anglo American notes that this issue has also been supported by the majority of other stakeholders.

Anglo American also wishes to address a number of elements of the building block methodology that Aurizon Network has contested from the QCA's Draft MAR Decision, including:

- (a) Aurizon Network's proposal to increase *operating costs* by \$54.8 million over the UT4 period from the level outlined in the QCA Draft MAR Decision;
- (b) Aurizon Network's proposal to increase *maintenance costs* by \$55.8 million over the UT4 period from the level outlined in the QCA Draft MAR Decision; and

- (c) Aurizon Network's proposal to maintain a utilisation rate of 0.25 for *gamma*, despite the clear evidence that this is not a realistic figure to apply to the Aurizon Network business.

In relation to the risk free rate, Anglo American strongly agrees with a term of five years as proposed by the QCA. This matches the term of the regulatory period and allows it to be updated in line with the Access Undertaking. In particular, Anglo American disagrees with using the 10 year Commonwealth bond rate as that figure incorporates a level of long term risk which Aurizon Network is not forced to bear (as its risk free rate is actually re-estimated every five years or shorter depending on the time for the approval of the Access Undertaking). Beyond a renewal of Aurizon Network's risk free rate, it also has a complete renegotiation of the terms of its regulation every five years, effectively meaning that Aurizon Network's risk is renegotiated on this timeframe. Anglo American supports the use of the five year Access Undertaking period for the term of the risk free rate.

While Anglo American believes that Aurizon Network's reply submission has not provided any evidence to support any deviation from the QCA's position in the Draft MAR Decision on the other building block elements (specifically risk free rate and *gamma*), Anglo American reiterates its position as it relates to the QCA Draft MAR Decision on these aspects.

Because of these factors, Anglo American sees no reason for the QCA to alter its Draft MAR Decision in favour of Aurizon Network's response submission. Aurizon Network claims that the QCA Draft MAR Decision will not provide sufficient revenue flow or incentive to invest in the CQCN, however, Anglo American submits that the QCA's Draft MAR Decision provides above adequate returns for a regulated business with a reliable cash flow and low capacity volatility (through assurance mechanisms such as revenue cap regulation and Take or Pay contracts). As such, Anglo American submits that the QCA should reject Aurizon Network's further comments in its response in relation to both the WACC and the Maximum Allowable Revenue.

5.2 Market Risk Premium

Anglo American continues to reiterate its comments that the current Market Risk Premium (**MRP**) calculation is too high, and (as previously submitted by Anglo American and the QRC) is correctly estimated at around 6.0% (in line with the recent decisions of other regulators). The QCA Draft Decision altered the previous MRP of 6.0% to a slightly higher estimation of

6.5%.⁵ Anglo American believes that this estimation is inappropriately high as it does not believe that there is any evidence supporting the change from the previous MRP of 6.0%.

5.3 The Access Conditions regime

Anglo American supports the Draft Decision in relation to ensuring that non-standard agreements or negotiations which transfer risk away from Aurizon Network should be subject to some level of QCA oversight. Specifically, Anglo American supports recommendation 16.2 that:

- (a) the UT3 Access Condition regime be included and expanded to ensure equal operation to all users; and
- (b) Aurizon Network be required to provide a copy of any non-standard agreement to the QCA within a given timeframe.

Anglo American agrees with the QCA that this increased level of transparency is likely to ensure that Aurizon Network does not obtain any benefit from potential double-dipping where it has agreed protections or returns outside the sphere of the regulation. While Anglo American recognises Aurizon Network's right to make agreements outside the regulation, it believes that it is vitally important that these agreements are considered in relation to their impact on Aurizon Network's MAR and the obligations imposed on any other stakeholders.

5.4 Use of the DORC methodology rather than RAB

Anglo American supports the Draft Decision on recommendation 16.4 regarding use of the RAB value over a DORC methodology. Specifically, Anglo American agrees that a DORC valuation of the CQCN is likely to lead to inaccurate valuation of the assets, resulting in an over or under recovery for Aurizon Network and impacting on both its finances and those of its users. As such, Anglo American does not believe that DORC valuing is appropriate for regulated monopoly assets where sunk costs and regulation are significant aspects of the business operation and produce outcomes that are not in line with the objects of Part 5 of the QCA Act.

Anglo American has never fully supported the use of the DORC valuation for determining the asset value of the CQCN. As Anglo American's economic expert, Economic Insights, noted in its report during the UT3 process, the DORC methodology "based on some strict theoretical assumptions and, in practice, allows considerable discretion in arriving at an asset value for

⁵ Queensland Competition Authority, *Draft Decision: Aurizon Network 2014 Draft Access Undertaking - Maximum Allowable Revenue*, September 2014, 237.

regulated networks."⁶ This is based in part on the fact that "it provides for discretion, arbitrary valuations and divergences of views in the valuation of network assets",⁷ all effects that could drastically alter the tariffs and charges implemented on the network (and impact on its efficiency or economy). It is this discretion (provided to the natural monopolist, while the rest of the regulation attempts to remove discretion from the hands of the monopolist) that Anglo American does not believe is appropriate, especially when a RAB value can provide an extremely accurate estimation of the true value of an asset and so reduce the risk of extreme under- or over-recovery.

Anglo American agrees with the QCA that using the detailed RAB figures (namely, the indexed, depreciated historic cost) available from the many years of regulating the CQCN is likely to produce a much more accurate estimation of the real value of the assets. Because of this, Anglo American supports the Draft Decision recommendation 16.4.

5.5 Expansion pricing framework

Anglo American generally agrees with the QCA that an Expansion pricing framework could add certainty and predictability to the Expansion regime, making it easier to operate and fund.

Anglo American understands that the QCA's suggested decision-making process in relation to the socialisation of Expansion costs is as described in the flowchart in Figure 1:

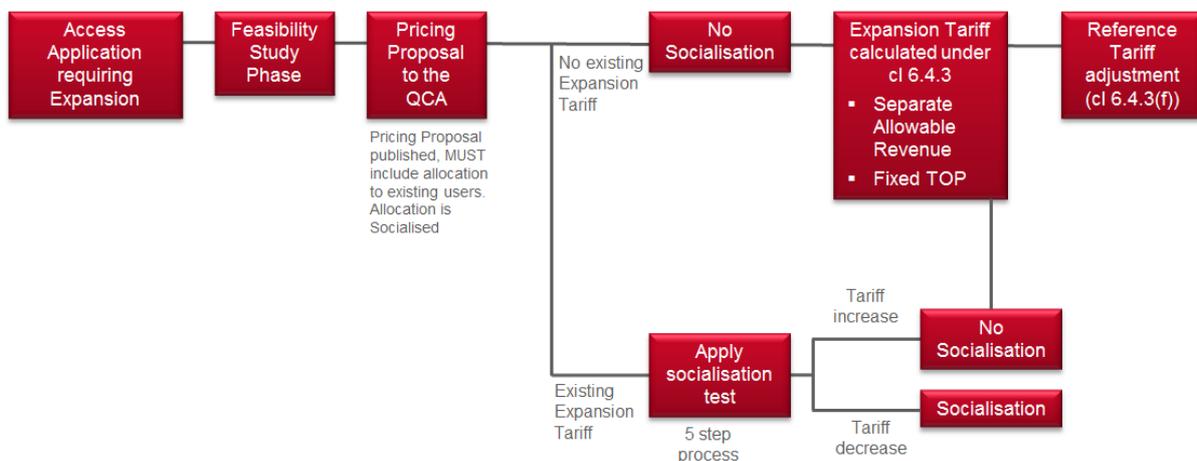


Figure 1: Anglo American understanding of the Expansion pricing process

As such, Anglo American generally supports the concept for inclusion of an Expansion pricing framework with some suggested amendments. Specifically, Anglo American agrees that:

⁶ Economic Insights, *Cost of Capital, Stranded Asset Risk and Socialisation of Costs for QR Network: Report prepared for Anglo American Metallurgical Coal Pty Ltd* (12 February 2010) 21.

⁷ Economic Insights, *Cost of Capital, Stranded Asset Risk and Socialisation of Costs for QR Network: Report prepared for Anglo American Metallurgical Coal Pty Ltd* (12 February 2010) 22.

- (a) Expansion users should bear the incremental costs of the Expansion where those costs increase the Reference Tariffs of existing Access Holders if the Expansion costs were to be "socialised". The nature of the coal mining industry is that Access Seekers are required to make decisions and investments based on long term contracts and costs. Where an Expansion alters those long term costs, for example increasing Reference Tariffs, this is likely to impact those long term investments and any uncertainty created by that could impact adversely on the market as a whole, through decreasing investments or investment potential. Further, Anglo American does not believe that existing Access Holders and users should be required to take cross default risk of potential competitors with a different risk profile and potentially unsustainable returns putting those additional future volumes, which may ordinarily be socialised, also at risk. Where an Expansion has the effect of decreasing existing Reference Tariffs, however, Anglo American acknowledges that it would create an economic welfare loss to continue to apply two separate tariffs (the QCA has described this as an "averaging down / incremental up" approach, which Anglo American generally supports under a "user pays" to hold capacity regime).⁸ As such, Anglo American agrees with the QCA that Expansion users should bear the costs associated with an Expansion, but only in the event that that Expansion adds no capacity benefits to existing users and would cause an increase in existing Reference Tariffs;
- (b) where existing Access Holders obtain a material benefit from an Expansion, the cost of the Expansion related to that benefit might be appropriately socialised across all Access Holders (both new and existing). Anglo American supports the QCA's comments that the price of Access should be reflective of the service provided to users and that in any instance where that service has been materially improved, users might be required to pay for that improvement. Anglo American uses the phrase "might" as it submits that these improvements should still be subject to efficiency and prudence tests, including a reliable user voting process. Anglo American supports the QCA's suggestion that it is Aurizon Network (and the Expansion users) that should bear the onus of proving that there has been a clear and definable benefit to existing Access Holders, and also that those existing Access Holders should be given the opportunity to review (by way of audit) and make comments on the benefits that they might be receiving; and
- (c) the approach should be considered in each of the circumstances on a "case-by-case" basis once these issues are properly understood by all stakeholders.

⁸ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 369.

However, Anglo American has some outstanding concerns regarding the Reference Tariff adjustment process contained in clause 6.4.3(f) of the QCA's Draft Decision on UT4.2. While Anglo American has generally expressed its support for the QCA Expansion pricing process, it is difficult to fully endorse the proposed system without understanding how the Reference Tariff adjustment process is actually going to be implemented (eg, whether the expected revenue from the Expansion Tariff be taken into account when calculating the Reference Tariff for existing users and the revenue pooled to determine the System Allowable Revenue).

Otherwise, to the extent that it is consistent Anglo American generally supports the QRC's suggested Expansion Pricing principles approach to socialisation proposed under UT4 given the risks are manageable and it provides a simpler approach with the implications more readily understood.

In relation to the treatment of Common Costs Anglo American believes two approaches should apply. First, in cases where the Expansion would create a lower Expansion Tariff than the existing Reference Tariff and the QCA is proposing to equalise the Tariffs through an adjustment to Common Costs, Anglo American believes that the Expansion should be effectively socialised into the existing Reference Tariff thereby eliminating the Common Cost adjustment issue. Secondly in cases where the Expansion provides a new and higher Tariff than existing Reference Tariffs, Anglo American believes that it is appropriate to require a portion of Common Costs (those relating to various fixed services provided by Aurizon Network for train control and other Aurizon Network operations as used by the expanding user) to also be recouped in the new Expansion Tariff. It is appropriate for users of services to make a contribution to those services which are a normal part of accessing the Network. Anglo American submits that the true test of whether the Expansion Tariff for a particular mine haul is able to accommodate a portion of Common Cost is whether that Expansion Tariff is actually higher on a dollar per net tonne basis than the Reference Tariff of an existing user with the longest haul and adjusting for differences in train characteristics. Anglo American is particularly concerned that there is no information or guidance on how the QCA intends to build up AT1-5 for an Expansion Tariff, and on current reading it is unclear whether expanding users will contribute to mainline track costs that existing users are required to pay.

Anglo American also agrees with the QRC submission in relation to the pricing of post-Expansion Access Seekers, with the exception that these proposed arrangements would only apply to Expansions by users within that same Rail System and not to expansion works resulting from cross System users (eg, GAPE).

5.6 Use of Australian utility businesses to benchmark risk for equity beta

Anglo American notes that in its Draft MAR Decision, the QCA has used a number of different entities to benchmark the equity beta figure. Anglo American agrees with the QRC and Aurizon Network that Australian toll roads are unlikely to be relevant to the Aurizon Network business due to the completely different risk profile of those businesses.

Anglo American notes that the QRC has suggested that the QCA should only consider water and electricity utility entities because they are the only businesses exposed to substantially similar systematic risks as Aurizon Network. While Anglo American agrees that these businesses exhibit the most similar characteristics to the Aurizon Network risk profile, Anglo American submits that it is important for the QCA to continue to ensure that it considers the Aurizon Network business in light of its broader risk profile (rather than just attempting to apply a framework risk profile from other businesses).

Anglo American makes this comment because, while Australian utility entities may have similar risk profiles to Aurizon Network, in many instances Australian utility entities actually bear increased risk on elements of their business than Aurizon Network does. In particular, Australian utility entities bear risk because of the manner that their profits link to the volume delivered and required by users. While Aurizon Network has some volume risk (arising purely from inconsistency between forecast and railed tonnages), as stakeholders have said on a number of occasions Aurizon Network does not bear any volume risk while protected by long-term (generally at least 10 year) Take or Pay agreements and the its revenue cap (meaning that even the risk it bears regarding forecasting errors is corrected by a regulatory true up every year).

Aurizon Network has attempted to justify its high equity beta by benchmarking its business against that of US Class 1 railroads. Aurizon Network has attempted to justify the inclusion of these US Class 1 railroad businesses for a number of reasons that Anglo American does not find persuasive. For example, Aurizon Network's reply submission attempts to cast doubt on the QCA's finding that US Class 1 railroads tend to have significantly shorter contract terms, increasing the risk of fluctuations and volatility (as these contracts are negotiated far more frequently than the long-term 10 year contracts that Aurizon Network signs). Anglo American continues to support the QCA's empirical evidence on this point as it notes that Aurizon Network has not presented any information in its reply submission to suggest otherwise. Further, Aurizon Network has suggested in its reply submission that because of the relatively stable percentage of the total coal transported figures held by US Class 1 railroads, they must possess some level of market power (and, similar to Aurizon Network's monopoly position,

not be subject to effective competition).⁹ Anglo American believes that this argument is flawed - in simple economic terms, the outcome of tough competition is a Nash equilibrium where competing firms maintain production and market share without ever having monopoly market power. Although an extreme example, it exposes the flaws in Aurizon Network's argument. As such, Anglo American does not believe that US Class 1 railroads provide an appropriately analogous benchmark for reviewing Aurizon Network's equity beta.

Because of these issues, Anglo American believes that Aurizon Network's equity beta (rather than being partially informed by the models applied to high risk businesses such as toll roads) should actually reflect the fact that it operates one of the lowest risk business models in the country, and its equity beta should be set using Australian utility entities as an upper bound, not as an average benchmark.

Anglo American also notes the figures presented by the QRC in its recent submission in relation to Aurizon Network's equity risk premium. Anglo American notes that there is a considerable difference in the systematic risk that Aurizon Network faces (as discussed previously, it is close to or is zero) and that Aurizon Network's equity risk premium (and, therefore, its overall rate of return) should be reduced to reflect a midpoint between the other regulated businesses that the QRC outlined. While the QCA has estimated an equity risk premium rate of 5.2%, Anglo American believes that the appropriate equity risk premium figure is in a range of 4.0-4.5% as Aurizon Network's risk sits just below that of the utilities networks that the AER regulates. Anglo American does not see any reason or empirical evidence supporting the QCA's Draft MAR Decision to set an equity risk premium of 5.2% and supports the QCA reducing this figure for the Final Decision in order to reflect the true risk borne by Aurizon Network.

5.7 Estimation of gamma

While Anglo American supports the QCA's Draft MAR Decision to increase the gamma figure from that suggested by Aurizon Network, Anglo American submits that there is still reason to increase the figure further because of the low utilisation rate that the QCA has relied on.

Specifically, Anglo American notes that Aurizon Network's reply submission attempted to detract from the reasoning of the QCA on this point, primarily by stating that there is no regulatory precedent for a gamma figure as high as 0.47. Anglo American contends that this is because there are extremely few (and possibly no) regulated entities with similar characteristics for the use and distribution of imputation credits as Aurizon Network.

⁹ Aurizon Network, *2014 Draft Access Undertaking: Aurizon Network Response to Queensland Competition Authority's Draft Decision on Maximum Allowable Revenue* (December 2014) 202-3.

Aurizon Network is a highly diversified business with interests at almost all levels of the supply chain (including mines, rail, rollingstock and ports), across a number of different commodities and in both regulated and unregulated businesses. Anglo American believes that this gives Aurizon Network the potential to obtain a much higher distribution and utilisation of imputation credits, the outcome of which is a significantly higher gamma. Relying on regulatory precedent from decisions by regulators in other States and in relation to businesses that do not resemble Aurizon Network's would only result in an incorrect gamma assumption (like Aurizon Network's 0.25 suggestion) and Anglo American continues to support the QCA's Draft MAR Decision to recalculate gamma based on its own assessment of the criteria.

5.8 Significant increases in operating costs

Reliance on the "stand-alone" business model

One major flaw that Anglo American has already commented on in relation to Aurizon Network's operating cost modelling (including the operating cost modelling prepared by its independent consultant Ernst & Young) is the benchmarking against a "stand-alone business of a similar size and in a similar industry." Aurizon Network's continued reliance on the position of a "stand-alone" business simply ignores the reality of its position as one entity within an extremely broad and diverse group of companies with significant shared corporate and back-end services (even though the Aurizon Network business should be appropriately ringfenced from its related entities).

Anglo American acknowledges that an integrated structure does provide certain benefits for the organisations involved in the structure. One of these benefits is increased efficiency, including economies of scale and overhead costs. Importantly, this increased efficiency means that while overheads and operating costs are significant to the entire organisation, it is noted that the cost to each entity in the organisation is reduced from what it would be if the company operated as a stand-alone business. This is a central driver behind integration, and importantly vertical integration, of business units.

As such, Anglo American believes that Aurizon Network is completely incorrect to continue to benchmark itself as a stand-alone business, ignoring the significant efficiencies and cost benefits that it receives as part of the broader Aurizon Group. Anglo American supports the QCA Draft MAR Decision and believes that Aurizon Network has not provided any clear evidence to convince the QCA that it should deviate from its previous position to increase operating costs based on the benchmarking of costs relevant to Aurizon Network as a standalone business.

Forecast Wage Price Index

Anglo American notes that Aurizon Network's reply submission raised strong objections to the QCA's use of the Forecast Wage Price Index (**WPI**) rather than the BIS Shrapnel AWOTE methodology that Aurizon Network proposed.

While Anglo American notes the main points of Aurizon Network's objections to the QCA's reliance on the WPI rather than the AWOTE model, Anglo American submits that Aurizon Network has missed an important aspect of the QCA's Draft MAR Decision. Specifically, while the QCA stated that "the skill base of a company's workforce is a business choice for the owners",¹⁰ it went on to acknowledge that with a company's choice to increase the skill component of its workforce then it will also receive time and efficiency benefits: ie, "if a company chooses to pay for a higher skilled workforce, then it will get the associated productivity benefit of that decision... it seems counterintuitive that the allowance should be increasing (due to an increase in the AWOTE) in the wake of improved labour productivity."¹¹

Aurizon Network has a number of incentive methods for increasing its productivity, including a number of proposed incentive mechanisms under UT4. Further, if Aurizon Network is truly focused on obtaining productivity incentives, Anglo American believes that it should consider the benefits of the price cap form of regulation which is designed specifically to increase the incentives for a regulated entity; an outline and analysis of this form of incentive regulation was considered by the QCA in its recent pricing principles and form of regulation review. Anglo American does not believe that it is appropriate to be transferring the role of incentive mechanisms on to the escalation of Aurizon Network's employment costs.

Further, Anglo American understands that when the WPI and AWOTE are directly compared over a date range (viewed dynamically, rather than focused on a static point), the WPI is favoured for its ability to more accurately measure true fluctuations in employment costs. Because of its increased accuracy, as well as the ability to predict increases over the term of the regulatory period, Anglo American continues to support the QCA's reliance on the WPI model rather than the AWOTE as suggested by Aurizon Network. There should be no change to this aspect of the QCA's Draft MAR Decision.

Anglo American also notes Aurizon Network states in benchmarking that it is likely to have higher costs than the Hunter Valley Coal Network, in part because of the role of the HVCCC.

¹⁰ Queensland Competition Authority, *Draft Decision: Aurizon Network 2014 Draft Access Undertaking - Maximum Allowable Revenue*, September 2014, 58; quoted in Aurizon Network, *2014 Draft Access Undertaking: Aurizon Network Response to Queensland Competition Authority's Draft Decision on Maximum Allowable Revenue*, December 2014, 47.

¹¹ Queensland Competition Authority, *Draft Decision: Aurizon Network 2014 Draft Access Undertaking - Maximum Allowable Revenue*, September 2014, 59.

Aurizon Network should not benefit from claimed increases in its costs in circumstances where independent centralised coal chain co-ordination can provide better efficiencies and related revenue increases as well as reduced overall unit costs by delivering improved network utilisation.

Costs for the preparation of the 2018 Draft Access Undertaking (UT5)

Anglo American supports the QCA's Draft MAR Decision in its significant reduction in allowed costs for the preparation of UT5. While Anglo American has engaged in the extensive submission and negotiation process in UT4, it notes that Aurizon Network has had little incentive to truncate or streamline the process as it has not borne the vast majority of the costs. Not only has industry (both through the QCA and through the preparation of their own advisor's reports) experienced significant costs from the extended UT4 process, through Reference Tariffs users have also supported the extensive reports, submissions and proposals made by Aurizon Network. Anglo American understands that users are required to bear some of the cost of the regulatory burden imposed on a regulated business, however, Anglo American does not believe that it is appropriate to assign such a large portion of costs (which are essentially the outline of the Aurizon Group's commercial interests in its infrastructure business) to the participants on the other side of that commercial negotiation. Further, Anglo American supports the QCA's Draft MAR Decision that because of the immense overhaul of the regulatory arrangements and Access Undertaking in the UT4 process, there should not be the requirement for such a high level of consultation and renegotiation when UT5 negotiations are shortly due to commence.

Anglo American also believes that this is inappropriate as, although Aurizon Network has allocated all of the costs of preparation of the Access Undertaking (and, indeed, all of its legal costs) to the regulated aspects of its business activities, it is also engaged in a certain range of unregulated activities (as noted by the QCA's Draft Decision where it has considered a number of services provided by Aurizon Network in contestable markets). Throughout the UT4 process, Aurizon Network has also attempted to increase the scope of its involvement in unregulated activities (or more appropriately described as an attempt to decrease what the Access Undertaking declares as regulated activities). Due to this, Anglo American does not believe that it is appropriate for Aurizon Network to allocate 100% of its legal costs to users of the regulated business, as there is a significant risk that not all of those costs are in fact attributable to regulated activities, or to addressing the burden of administration that regulation places on Aurizon Network.

Risk and insurance

Anglo American and other industry stakeholders have previously commented on the complete lack of clarity in the application of Aurizon Network's self-insurance, cost pass-through and insurance premium costs (this has been a recent issue in relation to the cost pass-through of flood events impacting on the CQCN). As such, Anglo American welcomes the QCA's Draft MAR Decision in relation to risk and insurance (including that it is no longer appropriate to recover costs through increases to Reference Tariffs).

While Aurizon Network has accepted the QCA Draft MAR Decision's treatment of its self-insurance approach, Anglo American does not. Anglo American does not believe that there is sufficient clarity or structure around Aurizon Network's self insurance charges, including not specifying whether "self insurance" is meant to apply as an offset or payments into a sinking fund, who would manage that fund, and the criteria that must be met before the offset fund is utilised.

Anglo American, therefore, supports the Draft MAR Decision to the extent that it creates more robust reporting requirements around the figures held as self-insurance costs. By reviewing Aurizon Network's previous submissions and materials, it would appear that there is potentially an undisclosed amount of money remaining in Aurizon Network's self-insurance fund from UT3 and, to the extent that this is being used as an offset fund, Anglo American believes that Aurizon Network should be made to disclose the funds that it has received for the purpose of self-insurance and the use that it puts those funds to, if any.

Branding

Anglo American has previously raised concerns regarding Aurizon Network's claim for "Branding" costs. Anglo American supports the QCA Draft MAR Decision that users should not be required to bear the commercial costs of Aurizon Network's business branding activities, especially where some of those costs have been diverted to pay for the branding and advertising of the Aurizon Group as a whole. This gives unfair subsidies to the non-monopoly arms of the business and Anglo American does not believe that this is an appropriate cost to be regulated under the Access Undertaking. In its reply submission, Aurizon Network has already admitted that some of the costs that it claimed as "Branding" under UT3 included advertising, artwork, brochures and signage - all of which is of benefit to the broader (and unregulated) aspects of the Aurizon Group.

Anglo American does not wholly understand Aurizon Network's arguments on this point in its reply submission.¹² Aurizon Network has claimed that "Branding" costs include:

- (a) printing of material for awareness campaigns. Anglo American fully supports Aurizon Network's work in running awareness campaigns for the safety of the public, however, Anglo American does not believe that this is a cost that is entirely attributable to the regulated aspects of the network business. This is a cost that the Aurizon Group (with its varied investments across the above rail transport haulage and supply chain such as depots) should also be involved in, and Anglo American does not support it being completely passed through to regulated users of the Aurizon Network business only. For example, operators such as Pacific National are also engaged in specific social awareness campaigns but are not entitled to a regulated pass through of costs;¹³
- (b) induction material for new staff. Anglo American notes that Aurizon Network is also provided with a significant portion of funds that are to be directed toward employment and associated services. Anglo American does not understand why there are separate costs under the "Branding" heading which are addressed toward the training of new staff, where those costs (including safety training and awareness induction programs) are all also covered under the specific employment costs allocation that Aurizon Network receives in the MAR; and
- (c) costs related to the UT4 submission documents. As discussed elsewhere in this submission, Anglo American notes that Aurizon Network already receives extensive funding from users for the preparation of the Access Undertaking. Where Aurizon Network is already receiving funds related to the preparation of the next round of regulation, Anglo American is not convinced that Aurizon Network requires separate funding under its "Branding" heading which also relates to the preparation of the Access Undertaking submission. Again, Anglo American is concerned that this is an example of attempted double recovery for Aurizon Network and does not believe that this reasoning justifies its excessive "Branding" allowance.

As such, Anglo American continues to support the QCA Draft MAR Decision in relation to "Branding" after considering and discounting the reasoning put forward by Aurizon Network in its reply submission, mainly due to the extensive double-recovery that Anglo American believes that Aurizon Network's "Branding" costs are likely to result in.

¹² See mainly Aurizon Network, *2014 Draft Access Undertaking: Aurizon Network Response to Queensland Competition Authority's Draft Decision on Maximum Allowable Revenue*, December 2014, 77.

¹³ See examples of Pacific National activities such as Asciano, *Pacific National marks Rail Safety Week with school education campaign*, 13 August 2013; and Asciano, *Pacific National drivers visit local schools with safety message*, 12 August 2014.

Audit and condition-based assessment

Please note that Anglo American has also considered this issue separately in section 9.2 in relation to its interaction with the reporting provisions of UT4.2.

Anglo American understands that Aurizon Network has made claims for the costs incurred during its condition based assessment process. As the condition based assessment process was required under UT3, Anglo American does not object to the theory behind including the cost of the condition based assessment in the MAR. Anglo American understands that the burdens placed on a regulated infrastructure owner by that regulation are appropriate to pass-through to users of that infrastructure.

Under UT3, Aurizon Network was required to undertake two stages of condition based assessment, specifically:

- (a) immediately upon the commencement of UT3 in order to determine the asset condition at the start of the regulatory period; and
- (b) at the end of UT3 in order to determine the final asset condition and to ensure that Aurizon Network had maintained its assets to the standard required under the Access Undertaking.

The purpose of this process was to ensure that there were both opening and closing asset condition benchmarks. Anglo American notes that this is not precisely how the condition based assessment process has in fact proceeded.

Aurizon Network's requirement to complete a condition based assessment process at the commencement of the UT3 period was not fulfilled until August 2013, and relied on data collected during the 2011-2012 financial period. This did not fulfil the requirement to ensure that both the QCA and industry were provided with a full analysis of the asset quality at the commencement of UT3 (rather, it was received after the submission of the 2013 Draft Access Undertaking in what should have been the start of the UT4 period).

Further, Anglo American is not aware that Aurizon Network has completed a final condition based assessment report considering the final asset condition of the CQCN at the conclusion of the UT3 period. This means that Aurizon Network has failed to fulfil the goal actually set by the regulation to create a benchmark asset condition at both the start and the end of the regulatory period. The QCA Draft MAR Decision notes that "the initial purpose of the Evans

& Peck study was to establish a baseline condition of the CQCN, which could then be tracked over time through subsequent assessment."¹⁴ This has not been achieved.

Because of this failure to comply with the requirements of UT3, Anglo American questions why Aurizon Network is actually entitled to the return of any of these claimed costs. Rather than providing an accurate spread of data across the period (and a dynamic view of the asset condition), the single report has only provided a static point in time view of the asset quality. This has not achieved the goal of the UT3 requirement because Aurizon Network failed to comply with the regulation and Anglo American does not believe that users should be required to return those costs to Aurizon Network.

5.9 Significant increase in maintenance costs

Aurizon Network's reply submission focuses on the fact that the QCA should adopt the Aurizon Network-generated proposed maintenance allowance. While Anglo American understands that the initial figures considered by the 2013 and 2014 Draft Access Undertaking submissions will need to be revised for the purposes of finalising UT4, it does not agree that the proposals made by the QCA's independent consultants should be rejected (as suggested by Aurizon Network). Rather, Anglo American believes that the views of the independent consultants are to be preferred (being impartial) and are likely to reflect a reasonable balancing of Aurizon Network's (and the broader Aurizon Group's) commercial interests with a focus on increased efficiency and cost-awareness.

As such, Anglo American continues to generally support the independent reports submitted by SKM and Energy Economics.

Ballast replacement and maintenance costs

Anglo American notes that Aurizon Network has argued that its ballast repair and maintenance costs should be reincluded. Anglo American supports the QCA's analysis that drove the MAR Draft Decision to remove these costs, including the empirical evidence that the QCA collected that Aurizon Network's costs in this area are high when compared to similar operators.

Anglo American continues to support the QCA's Draft MAR Decision to remove the ballast repair and maintenance costs and does not believe that Aurizon Network has provided sufficient evidence that these are reasonably and prudently incurred costs that should be included in its MAR.

¹⁴ Queensland Competition Authority, *Draft Decision: Aurizon Network 2014 Draft Access Undertaking - Maximum Allowable Revenue*, September 2014, 98.

6. Part 7A: Baseline Capacity

6.1 General

Anglo American strongly supports the QCA's inclusion of a new Part 7A in relation to information provision on the Baseline Capacity of the CQCN. Anglo American has previously made extensive submissions in relation to the lack of transparency for stakeholders around the true capacity of the CQCN (rather than simply the uncontracted capacity) and how this has led to inefficiencies in the supply chain, including meaning that stakeholders have very little oversight of when the CQCN actually requires Expansions versus potentially cheaper operational or scheduling changes. Because of this, Anglo American believes that increased transparency regarding the Baseline Capacity of the CQCN ought to increase the efficiency of the supply chain, and ought to reduce unnecessary expenditure in areas that do not require major infrastructure investment.

Anglo American supports the QCA's drafting in relation to the Baseline Capacity review and the Baseline Capacity Assessment Report. Importantly, Anglo American believes that whatever amendments the QCA makes to this clause, the QCA ensures that clause 7A.4.1(i) remains so that both the QCA and stakeholders get an unredacted version of the Baseline Capacity Assessment Report.

Anglo American also strongly supports the QCA's development of clause 7A.2.3 in relation to the making of initial System Rules. The System Rules decision and consultation process has been extensive throughout UT3, and Anglo American notes that it remains a deferred outcome of UT3 that Aurizon Network is yet to rectify. As such, Anglo American welcomes the QCA's Draft Decision to require the submission of Draft System Rules within two months of the approval date.

Anglo American notes that the Aurizon Network Information Request also contains a number of questions relating to specific clauses within this Part 7A. Anglo American has reviewed both the Aurizon Network Information Request and the QCA responses in light of the QCA mark-up of UT4.2 and the Draft Decision. After doing so, Anglo American wishes to broadly support all of the comments made by the QCA in response to the Aurizon Network Information Request, except for point 6 which is discussed further at section 6.2 of this submission.

6.2 Below Rail Capacity vs Baseline Capacity vs Supply Chain Capacity

Anglo American notes that Aurizon Network raised an issue in relation to the interpretation of these three definitions in the Aurizon Network Information Request.

Anglo American notes that the question in the Aurizon Network Information Request as well as the subsequent response by the QCA both refer to "Below Rail Capacity". Anglo American notes it is not a defined term in UT4.2.

Anglo American would also like to question the QCA's response to the Aurizon Network Information Request on this point because the QCA states that:

Baseline Capacity is in respect of the Below Rail Capacity once all relevant considerations have been taken into account. For example the Baseline Capacity should identify the number of TSEs in each coal system (defined as system paths in the Capricornia System Rules) that are aligned to a mine loading slot, a port unloading slot and take account of the dwells required to perform a train service on the path (eg train crewing).¹⁵

While Anglo American understands that a figure will need to be given for the Baseline Capacity of the CQCN and each of its various systems once a number of factors are taken into account, Anglo American also understood (and interpreted from the QCA Draft Decision and mark-up of UT4.2) that Baseline Capacity should include a figure outlining the absolute capacity of the CQCN without any deductions. Anglo American understands that this will be a purely objective figure of the "nameplate" capacity of the CQCN (including each System) without any maintenance reductions, contracted capacity or flexibility deducted from the figure. Anglo American believes that the QCA's response should make this clear, otherwise Anglo American and other users have previously noted that enough information for stakeholders has not been provided to make relevant determinations about the existing capacity and necessity of any prudent future Expansions of the CQCN.

As such Baseline Capacity is crucial to efficient use of current capacity and determining the needs for any future capacity particularly when matched with a robust voting process whether it be user- or Aurizon Network-funded (including shortfall) Expansions.

7. Part 7: Available Capacity Allocation and Management

7.1 General

Anglo American supports the QCA Draft Decision not to approve the provisions of Part 7 as submitted by Aurizon Network in UT4.2. In particular, Anglo American supports the QCA's Draft Decision to:

- (a) reinstate the queue mechanism for allocation of Available Capacity as Anglo American believes that this is the only truly equitable method (free from any bias or suggested bias) for the allocation of Capacity between competing Access Seekers;

¹⁵ Queensland Competition Authority, *Information Update: Aurizon Network 2014 Draft Access Undertaking (2014 DAU)* (23 March 2015) 4.

- (b) subsequently reinstate the capacity notification register and the committed capacity register;
- (c) move the provisions relating to force majeure back into the Access Undertaking from the Access Agreement (Anglo American's previous submissions have addressed a number of key concerns regarding provisions that have been moved from the Access Undertaking into the Access Agreement, and as such Anglo American has provided detailed arguments against removing these provisions from the Access Undertaking);
- (d) reinstate the preference treatment for Access Holders wishing to renew their existing Access Agreements on substantially the same basis and operational criteria (eg, origin / destination, TSEs). Anglo American believes that this increases regulatory certainty, as well as ensuring that mining companies and investors (who typically make these investments for extended periods of time) can in some way ensure the consistency required for such substantial and long-term investments. Anglo American understands that this includes a decision to reinstate the priority provisions for renewing Access Holders. However, if the access has previously been held for at least 10 years the renewing party should be able to renew for minimum five year periods to keep the "first rights" alive and align with existing "exit capability" commitments;
- (e) amend the UT4.2 provisions relating to renewing Access Holders to ensure that they are not required to undertake the entire negotiation process again. While Anglo American agrees with the QCA's Draft Decision that it would be preferable that some elements of Access Agreements are updated to reflect the provisions of the Access Undertaking in force at the time of the renewal,¹⁶ Anglo American is concerned that Aurizon Network will not be amenable to only renegotiating certain elements of the renewing Access Agreement. Further, Anglo American notes that the QCA has not specifically outlined exactly which elements of a renewing Access Agreement can be renegotiated: Anglo American believes that if the QCA wishes to enforce provisions that renewing Access Agreements can be renegotiated, it is necessary to provide a list of the only elements that can be renegotiated (or simply the provisions that are to be amended in line with whatever the appropriate Access Undertaking provisions at the time of renewal) otherwise it will be in Aurizon Network's interest to take a broad view and suggest that all elements are open for renegotiation;
- (f) again, while Anglo American is open to the "replacement mine concept", it acknowledges the comments of the QCA in the Draft Decision that Aurizon Network is yet to provide enough clarity and transparency around the replacement mine

¹⁶ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 227.

concept to properly analyse the effectiveness of these provisions. Until such time as Aurizon Network provides this clarity, Anglo American does not believe that the QCA can support the inclusion of the replacement mine concept;

- (g) reinstate the UT3 provisions relating to transfers and relinquishments until such time as the transfer mechanisms proposed by Aurizon Network (including the Short Term Transfer Mechanism proposal) can be properly understood, and Aurizon Network has provided enough transparency to ensure that the QCA and stakeholders understand what each of the transfer mechanisms is intended to achieve. Anglo American also wishes to express its agreement with the QCA in relation to:
 - (i) Draft Decision recommendation 11.8, that Aurizon Network be required to provide a transferring or relinquishing Access Holder with information regarding how a relinquishment / transfer fee is calculated and any assumptions relied on to calculate the relevant fee; and
 - (ii) Draft Decision recommendation 11.9, that the customer initiated transfer provisions in UT3 be reinstated. Anglo American believes that these provisions are an important mechanism to allow Access Holders to appropriately and easily deal with their Access Rights and Capacity allocation under an Access Agreement and that the customer initiated transfer process allows Access Holders to manage their Capacity without detrimentally impacting any other Access Holder, Access Seeker or Aurizon Network itself, therefore, Anglo American does not see any relevant objection to the provisions; and
- (h) resumption because of lack of supply chain rights or where Aurizon Network believes that a user is underutilising its Access Rights.

Anglo American also notes that it provided detailed commentary to the QCA in relation to Aurizon Network's proposed Short Term Transfer Mechanism. As neither the QCA nor Aurizon Network has made any further remarks or decisions in relation to the proposed Short Term Transfer Mechanism, Anglo American continues to support its earlier submission on this point.

7.2 Capacity queue

While Anglo American notes that the QCA has recommended reinstating the queuing mechanism (which Anglo American has already noted it supports), Anglo American does not believe that the QCA has adequately reintroduced all of the provisions relevant to reinstatement of the queue. Importantly, Anglo American believes that:

- (a) clause 4.6 (Anglo American notes that this is to do with negotiation, but believes that this issue is directly relevant to Available Capacity) should include a requirement that Aurizon Network's Indicative Access Proposal include a response regarding the position of the Access Seeker in the Capacity queue; and
- (b) further, in clause 4.10 Anglo American notes that there is no obligation on Aurizon Network to notify or discuss with an Access Seeker if they are going to be moved or removed from the Capacity queue. Anglo American believes that there should be a positive obligation on Aurizon Network to notify an Access Seeker of its intention to move it or remove it from the queue, as well as an obligation on Aurizon Network to allow the Access Seeker a defined period of time from receiving Aurizon Network's notice of intention to allow the Access Seeker to rectify any problems with its Access Application. As it currently stands, Anglo American notes that an Access Seeker may be removed from the queue without any notification.

8. Part 8: Expansions

8.1 General

As Anglo American's previous submission outlined a number of failings in Aurizon Network's proposed Expansion provisions for UT4.2, Anglo American broadly supports the QCA's Draft Decision in relation to Part 8. Specifically, Anglo American supports:

- (a) Draft Decision recommendation 12.1, that there should not be a separate definition of Aurizon Network's legitimate business interests for this Part 8;¹⁷
- (b) Draft Decision recommendation 12.2, that:
 - (i) any expression of interest process conducted by Aurizon Network should be excluded from the requirements to conduct a demand assessment due to the potential bias involved in such a process;
 - (ii) broadening the ability of the demand assessment to consider other supply chain options before Expansions (Anglo American believes that this will be supported by the Baseline Capacity Assessment process and any moves toward independent central coordination); and
 - (iii) restrict the areas that Aurizon Network's demand assessment can consider to rail-related issues, avoiding out-loading access at ports and information on the status of coal reserves or resources, both of which are protected by other

¹⁷ Anglo American specifically agrees with the QCA's comment that "there is no justification for the 2014 DAU to define further what constitutes Aurizon Network's legitimate business interests", see Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 254.

mechanisms within the Access Undertaking and are not appropriate matters to be decided on a subjective basis by Aurizon Network;

- (c) Draft Decision recommendation 12.3, to remove the concept of "commercial terms" and to reintroduce the Access Conditions regime with a requirement for acceptance by the QCA. Anglo American strongly believes that due to Aurizon Network's monopoly position in the supply chain, it is essential that any amendments to the approved regulatory restrictions are outlined, assessed and recorded by the regulator (the QCA);
- (d) Draft Decision recommendation 12.4, to review and amend the Study Funding Agreement. Anglo American has provided its own drafting amendments to Aurizon Network's UT4.2 Study Funding Agreement as **Attachment B** of this submission;
- (e) the Draft Decision insofar as it requires Aurizon Network to be responsible for the construction of Expansions. As Expansions will ultimately form part of the CQC and Aurizon Network's asset base, Anglo American considers it appropriate that Aurizon Network is involved in the construction process of any Expansion, except where the Access Undertaking provides otherwise (for example, where stakeholders have been involved in a step-in). Anglo American believes that this will mean that Aurizon Network will have direct control over the costs and timeframes involved with an Expansion and will be best placed to manage any risk that it bears through the Expansion construction process;
- (f) the Draft Decision relating to Aurizon Network's consideration of the pre-feasibility and feasibility studies in determining the target capacity to be achieved by an Expansion. Anglo American understands that estimating the target capacity required by an Expansion is not an exact science, however, believes that the central purpose of the studies process is to achieve as accurate an estimation of this figure as possible;
- (g) the Draft Decision relating to the assignment of study funding rights and provisional capacity, as long as the assignee meets the criteria that the initial holder of the rights was required to meet to participate in the study process. As long as this requirement is met (including requirements for the financial viability of the assignee), Anglo American does not see how an assignment of study rights will impact Aurizon Network or other Study Funders' risk profile in the relevant Expansion process, rather the assignment could in fact reduce the risk of losing a party from an Expansion process (and therefore mean that other Study Funders are not required to bear the loss

of a Study Funder). Anglo American has dealt with this concept in greater detail below; and

- (h) the Draft Decision requiring UT4.2 to include clear step-in rights, although Anglo American wishes to stress that step-in rights for stakeholders will only have the desired impact where that step-in involves all information obtained through the study process that is commercially able to be provided and any of Aurizon Network's estimations regarding capacity and costs to date, otherwise the engagement of the step-in process could result in unviable costs for Study Funders, meaning that the process is rarely (if ever) utilised (or even considered).

Further, Anglo American notes that it broadly supports the amendments suggested in the QRC's submission on the Draft Decision insofar as they relate to Expansion process provisions in the Access Undertaking.

Anglo American appreciates the effort and attention that the QCA has applied to the development of the Expansion principles in the Access Undertaking. While Anglo American is positive about the development of a workable SUFA solution within the next undertaking period, Anglo American agrees with the comments of the QCA that "This situation [an untested SUFA] provides Aurizon Network with market power which could incentivise monopolistic rent-seeking behaviour."¹⁸ Until such a time as a tested and workable SUFA is available, Anglo American could never support the removal of the regulation of Expansions from the Access Undertaking (even then, Anglo American believes that there should be some form of Expansion principles in the Access Undertaking for those factual scenarios that simply do not fit the SUFA model, or which require a regulated outcome).

Anglo American does note, however, that the QCA has not outlined support for mandatory funding obligations to be placed on Aurizon Network. Anglo American has consistently submitted that it considers mandatory funding obligations essential to ensuring that the efficiency and delivery of contracted capacity through the CQCN continues to improve. Anglo American continues to believe that because of its natural monopoly position, Aurizon Network's ability to engage in economic hold-up to the detriment of the capacity and efficiency of the CQCN, and subsequently Access Holders and the supply chain, must be constrained. Anglo American believes that this is most appropriately done by ensuring that Aurizon Network is required to expand the CQCN in certain specific and controlled situations, all of which were considered appropriate under UT3 and have proved an invaluable alternative to the ongoing lack of agreement on a workable SUFA. Anglo American continues to submit the comments made in its earlier submissions in the UT4 process regarding the

¹⁸ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 6.

reinclusion of Aurizon Network's mandatory expansion obligations. Anglo American also observes, however, that whether any expansion is user-funded or funded by Aurizon Network, ultimately it is a "user pays" system. As such the users should have the "final say" as to when and how Expansions take place through a robust modelling and voting process.

As such, Anglo American broadly supports the QCA's amendments to Part 8 dealing with Expansions.

8.2 Assignment of Study Funding Agreement

Anglo American notes that in its request for information to the QCA (dated 3 March 2015) Aurizon Network has requested clarification of the provisions surrounding the assignment of a Study Funding Agreement (**SFA**). Anglo American notes that the QCA's response (dated 23 March 2015) was unclear on this point and has requested further input from stakeholders.

Anglo American understands Aurizon Network's concern in relation to the assignment of a SFA insofar as that means that a new Feasibility Funder (please note that Anglo American has used this phrase broadly in this section to refer to any Potential Pre-feasibility Funder, Pre-feasibility Funder or Feasibility Funder) has been given rights which it has not been assessed under UT4.2 to be able to commit to. Anglo American agrees with Aurizon Network that it is not appropriate for a Feasibility Funder to have rights under a SFA (including a right to Provisional Capacity Allocation (**PCA**)) without some analysis of its ability to fulfil the requirements of the SFA or any subsequent Access Agreement.

In saying that, Anglo American believes that an assignment of the rights under a SFA should definitely include the assignment of any PCA that the relevant Feasibility Funder has contracted for, otherwise there will be very little incentive for users to assign SFAs and the QCA's insertion of a right to assign will be for no purpose. The assignment should be for a proportion of the PCA which is the same as the assignment of the Feasibility Funder's rights under the SFA; ie, if the SFA permits the contracting Feasibility Funder to 10 votes on how a Feasibility Study should be conducted and it wishes to assign 40% of its contracted PCA, then the assignment would also assign the rights of four of the 10 votes belonging to the original Feasibility Funder.

Anglo American submits that the concern relating to the appropriateness of the assignee Feasibility Funder could be allayed by:

- (a) ensuring that the assignee Feasibility Funder contracts with Aurizon Network on the same terms as the original Feasibility Funder (except for any necessary amendments for the change of entity);

- (b) require the PCA assigned for the purposes of a mine development, or for a customer with a mine development;
- (c) the assignee Feasibility Funder must accept and pay any costs required for Pre-feasibility Studies (clause 8.4), Feasibility Studies (clause 8.5) or Expansions (clause 8.9) as required; and
- (d) most importantly, that the assignee Feasibility Funder meets the criteria for determining who the relevant Access Seekers for a particular type of study are. For example, Anglo American notes that for Pre-Feasibility Studies the relevant criteria are contained in clause 8.4.2(c) and include:
 - (i) Access Seekers with Capacity Shortfall Applications in relation to the Capacity Shortfall in question (in this instance that would include where the assignee Pre-feasibility Funder was also receiving an assignment of rights under the Capacity Shortfall Application of the original Pre-feasibility Funder); and
 - (ii) satisfy the following requirements:
 - (A) relevant out-loading capacity (or chance of obtaining out-loading capacity);
 - (B) Exploration Permit, mine plan and diligent development;
 - (C) has provided a bank guarantee or has the ability to meet its funding obligations.

As long as the assignee Feasibility Funder meets these criteria, Anglo American does not see why an assignment of rights under a SFA, including the assignment of PCA, makes any impact to Aurizon Network's position.

8.3 The Expansion voting process

In addition to the observations above about Expansions, Anglo American is particularly conscious that previous voting processes have not been successful and have not necessarily involved all users whose throughput, Access Rights and Reference Tariffs were going to be impacted by the outcome of the voting process. In particular, Anglo American notes that the Goonyella to Abbot Point Expansion process is an instance where existing users encountered Capacity degradation or increased Reference Tariffs because of decisions made by the expanding users without the input of the existing users. Anglo American believes that this does not allow existing users the ability to protect Access Rights that they have made multi-

million dollar long-term investments on. Anglo American believes that any instance where an existing user faces some form of compression or price increase because of decisions that they had no involvement in is inappropriate. As such existing users should be entitled to vote and / or make submissions on any proposed Expansion in their system.

8.4 Existing Expansions

Anglo American notes that a number of decisions regarding Expansions (and their socialisation or inclusion in the RAB) remain outstanding from UT3, for example the WIRP or the Rolleston Expansions. Importantly, due to delays in the UT4 process, the claims were made during what should have been the UT4 period, and were made at a time when stakeholders have had limited resources to devote to their consideration due to the considerable time and funds that have been directed toward the negotiation of UT4. As such, Anglo American believes that the decisions and applications for these Expansions have now been left too long and it would be best to approach these decisions using whatever regulatory method is decided under UT4, rather than making a UT3 decision after the commencement of the next regulatory regime period, given that this is when the Expansions are to be paid for.

9. Part 10: Reporting

9.1 General

Anglo American broadly supports the QCA's amendments to Aurizon Network's reporting obligations contained in Part 10.

Anglo American does, however, suggest some amendments are necessary including:

- (a) Anglo American has previously made extensive submissions in relation to Aurizon Network's self-insurance requirements. Anglo American again stresses that if Aurizon Network wishes to continue self-insuring through payments made by users, it should be required to provide detailed information into how, where, when and why users' self-insurance costs have been spent; this is consistent with comments made by the QCA in the Draft Decision, including recommendation 5.2.¹⁹ Anglo American does not believe that Aurizon Network should be allowed to continue obtaining such high levels of self-insurance from users every year without properly accounting for where that money has been spent (or, if it has not been spent, where it is held and the amount being held), precisely which occurrences self-insurance funds are being spent on, and whether users or the QCA have preapproved spending self-insurance funds on those particular activities; and

¹⁹ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 105.

- (b) Anglo American believes that there are improvements that could be made to the maintenance and performance reporting requirements in the Access Undertaking. Anglo American notes that stakeholders receive relatively limited information regarding these processes, and a great deal of the little information that stakeholders do receive is heavily modified or redacted. Noting the need for confidentiality of information that is sensitive to each stakeholder, Anglo American does not believe that it is appropriate to restrict information beyond this when stakeholders are inevitably paying for throughput but not able to have visibility over the spending or usage of those funds. As such, Anglo American believes that transparent and informative maintenance and performance reporting requirements are necessary in UT4.2.

Anglo American agrees with the QCA's position in the Draft Decision that reporting is an extremely important aspect of UT4.2 as it is the method by which stakeholders receive valuable information regarding the performance and management of the CQCN and compliance by Aurizon Network with the Access Undertaking.²⁰ Without strict reporting requirements, including requirements for the public availability of information, Anglo American notes that users have very little oversight into these aspects of the Aurizon Network business. As such, Anglo American submits that strict and comprehensive reporting requirements are not only important, but rather are essential to the effective operation of natural monopoly regulation.

9.2 Condition based assessment of the CQCN

Under the provisions of UT3 Aurizon Network was required to undertake a complete network assessment in order to analyse the standard of maintenance and upkeep that Aurizon Network is applying to the CQCN. While Anglo American strongly supports the Draft Decision in relation to recommendation 5.6, it is concerned that Aurizon Network has previously failed to comply with a similar provision.

Anglo American notes that the final condition based assessment under UT3 is yet to be completed (and, judging by the progress of UT4 discussions, it is unlikely to ever be completed). Further, Anglo American notes that it was almost three years into the UT3 period before the first assessment was completed.

Anglo American does not believe that this has allowed the QCA or stakeholders to have any overview of the standard of the network at the time of the commencement of UT3, nor has it

²⁰ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 103.

allowed the QCA or stakeholders to be assured that Aurizon Network has maintained the CQCEN to the standard that is required (and paid for) under the Access Undertaking.

While inserting the provision requiring condition based assessment is appropriate, Anglo American believes that it is important to ensure that Aurizon Network complies with the provision.

Further, Anglo American submits that it is inappropriate for Aurizon Network to be required not to make these reports publicly available on its website, or on the QCA's website. In the interests of greater transparency, as has been promoted by many of the recommendations in the Draft Decision, Anglo American believes that it is essential for stakeholders and investors to see where the costs attributed to maintenance and asset renewal have been spent, and to ensure compliance with UT4.

Anglo American does not believe that Aurizon Network's failure to comply with this requirement of UT3 was adequately outlined in the Draft Decision. This is an essential assessment for the purposes of ensuring that Aurizon Network efficiently and economically maintains its assets. Without an analysis of the status of the assets at the beginning and the end of the regulatory period, the assessment process is completely undermined as to determining whether Aurizon Network has been complying with asset maintenance standards, or effectively utilising the maintenance funds provided by users.

Anglo American believes that the final UT4 approved by the QCA should include a provision requiring Aurizon Network to complete a maintenance assessment within six months of the commencement of UT4. There should also be a requirement for Aurizon Network to complete another maintenance assessment no more than six months prior to the expiry of UT4 and for any relevant subsequent regulatory periods where the maintenance allowance is included as part of the MAR.

10. Part 11: Dispute resolution

Anglo American notes that the QCA has done extensive work in the Draft Decision to ensure that UT4.2 incorporates appropriate dispute resolution mechanisms. Anglo American submits that the QCA's suggestions in recommendation 6.1 are correct and that the QCA should maintain these requirements for its final decision on UT4.2.

Importantly, Anglo American notes that the QCA has addressed its concerns regarding the scope of the dispute resolution provisions to ensure that all interested parties can participate in and institute dispute resolution proceedings. Anglo American has previously noted that there are a number of instances where current decisions may not involve users, however, the outcomes of those decisions can impact on the operation of those users' businesses or capacity

entitlements. Anglo American has previously experienced situations where it has been unable to intervene in dispute resolution proceedings despite the future impact on its activities because it has not been an "interested participant" for the purposes of the Access Undertaking.

11. Miscellaneous outstanding issues

11.1 Acting reasonably and in good faith

Anglo American has previously provided comments on Aurizon Network's various restrictions to act (and make decisions) reasonably, but not necessarily in good faith. Anglo American notes that the QCA has not taken the opportunity in the Draft Decision to rectify these issues.

Anglo American submits that because of Aurizon Network's monopoly position, it is essential that any discretionary judgment that is granted to Aurizon Network under UT4 needs to be qualified by a requirement to act "reasonably and in good faith". Anglo American notes that the two phrases imply very different legal tests when determining how Aurizon Network has acted, and Anglo American submits that it is important to include a good faith test requiring Aurizon Network to also consider the interests of users as well as itself when exercising its discretionary powers.

11.2 Central coordination

Anglo American notes that in the Draft Decision the QCA has expressed a strong preference for centralised coordination, specifically that:

In the absence of instituting a regime for effective coordination, it will be difficult to conclude that the 2014 DAU is consistent with the promotion of the efficient use of, operation of, and investment in infrastructure in the CQCN.²¹

Further, Anglo American notes that the QCA has specifically stated that "coal supply chain coordination is a necessary requirement for meeting the object of the third-party access regime in the QCA Act."²²

Anglo American supports the QCA's comments in relation to central coordination, however, believes that those comments should be qualified. Anglo American has long suggested that central coordination could improve the throughput and efficiency of the CQCN, as well as the delivery of contracted capacity by Aurizon Network and the various ports. Further, central coordination has the ability to achieve these goals by looking at other options for improved throughput without first focusing on significant capital investment options increasing the costs of related Expansions (which an Aurizon Network business may be more likely to), and rather

²¹ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 14.

²² Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 195.

streamlining and improving scheduling and other operational improvements to first deliver asset optimisation and then lower cost solutions. However, Anglo American believes it is completely inappropriate to subject supply chain stakeholders to central coordination by any particular participant that would be able to act in its own interests. Effective centralised coordination can only truly be achieved by an independently operated and governed central coordinator with throughput improvements and efficiencies as its unfettered objective.

Anglo American believes that the independence of the central coordinator is key to the success of any centralised coordination process and its objectives. Without this independence, stakeholders will quite rightly continually question whether a central coordinator is motivated by other reasons, including its own business interests. For these reasons, Anglo American believes that any suggestion that Aurizon Network, as part of a business group with an above rail operator, a port operator or a miner (or even a combination of these) should act as the coordinator is flawed and will not achieve the efficiency or productivity gains of an independent coordinator.

As such, in order for central coordination to truly deliver the objectives of third party access, it is essential for the central coordinator to be a trusted independent body with appropriate ringfencing and confidentiality obligations. While the QCA has expressed its strong preference for central coordination, Anglo American does not believe that it has expressed a preference for the independence of that central coordinator and Anglo American believes that this is a concern.

11.3 Focus on a broad range of incentives

Because of varied incentives and drivers for users' actions, Anglo American believes that it is vitally important for the QCA to ensure that its Final Decision adequately balances (and appropriately reflects the most important) incentives that drive users' actions.

Further, while Anglo American strongly supports the QCA's Draft Decision that the Access Undertaking should support efficient investment across the network, Anglo American believes that the most vital aspect of the Access Undertaking's operation is that it ensures efficient utilisation of the existing assets. The QCA noted this same point in its Draft Decision, stating that "effective use of existing capacity can defer the requirement for capacity expansions."²³ Anglo American strongly agrees with this point, however, currently questions whether there is truly effective use of existing capacity, primarily because of the existing inflexibility of Aurizon Network's capacity allocation, modelling and train path contracting and consumption. Only once there is efficient utilisation of the capacity of the existing assets

²³ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 347.

should the Access Undertaking then apply to ensure that there is also efficient investment in the expansion and development of the network.

Anglo American notes that this question is also integrated with the approval of the Short Term Capacity Trading Mechanism that the QCA has been considering. In its Draft Decision, the QCA states that "if users are to be made fully accountable for the use of their contracted capacity, then it may be necessary for there to be flexible trading mechanisms in place to allow users to efficiently manage risk."²⁴ Anglo American supports this finding, however, believes that it is essential for simple and expeditious trading mechanisms to operate to ensure that users can adequately trade their capacity. Further, Anglo American believes that before causing users to be "fully accountable for the use of their contracted capacity" (a concept that Anglo American believes users are already facing), it is essential to ensure that users are actually able to access and utilise their full range of contracted port and rail capacity. Anglo American has previously noted that one way of achieving railings much closer to contracted capacity is to ensure that users' have some flexibility around surge capacity, especially those with cargo assembly port capacity. Anglo American continues to believe that this suggestion would allow the system to have enough elasticity that it can increase railed tonnes over a period of months because of the ability to integrate with both mine and port scheduling, rather than applying the strict scheduling currently (and suggested to be) applied by Aurizon Network on the CQCN.

11.4 Take or Pay obligations

Anglo American acknowledges the reasoning behind Take or Pay requirements in Access Agreements, for investor confidence and long term asset viability, as well as for the incentive reasons outlined by the QCA in its Draft Decision, specifically to:²⁵

- (a) encourage consistent network use by above-rail operators, and in turn by mines, to achieve efficient use of infrastructure; and
- (b) discourage above rail operators and mines from systematically overestimating their capacity requirements.

While Anglo American understands that these are important incentives for mine and train operators, its believes that these incentives must be delicately balanced to ensure that they are not in fact operating to reduce the efficiency of the network, or of the coal supply chain. One particular example where Take or Pay achieves little or no incentive benefit is where users are unable to achieve their desired throughput and are forced to resort to over contracting in order

²⁴ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 346.

²⁵ Queensland Competition Authority, *Aurizon 2014 Draft Access Undertaking - Draft Decision* (January 2015) 340.

to ensure that they have adequate surge capacity for their planned output. Although Take or Pay would apply, and users would have to pay for excess unutilised capacity, some may see this as necessary in order to ensure adequate capacity is available when required. In this example the excess that the users pay above their actual required capacity, as well as any users that are restricted from accessing capacity because it is notionally contracted to another user, are both welfare losses to the whole supply chain.

11.5 Review Event process under UT4

Anglo American understands that the Review Event process is an important framework for protecting Aurizon Network from incurring significant losses where there have been major unforeseen natural disasters which have damaged contracted hauling or have actually severely damaged the CQCN infrastructure. Anglo American does not disagree with the theoretical concept behind the Review Event process.

Anglo American does, however, disagree with the use that the Review Event process is currently being (and Anglo American believes will continue to be) put to. Specifically, this is as an insurance mechanism to pass through claims at a regulated rate of return rather than simple escalation in the form of costs related to what are now relatively frequent flooding events in various systems. Anglo American directs the QCA to the 2013 and 2015 flood claim Review Events as examples.

Anglo American has, through consultation processes other than UT4, raised a number of concerns with how the Review Event framework is being applied. Anglo American is now raising a concern with the practical implications of having the Review Event process at all.

First, flood events are now relatively commonplace in a number of regions of rural and remote Queensland, particularly in a number of locations where CQCN railway is located. Stretches of railway have been damaged, some on repeated occasions, and have formed the basis of cost pass through claims to users made by Aurizon Network. Industry, Aurizon Network and the QCA have to accept that there will be more of these flooding events in the future.

Regardless of whether Aurizon Network does not have relevant insurance for high risk parts of the CQCN infrastructure, Anglo American believes that Aurizon Network should not be immediately able to recover the value of the repair in one lump sum from users. Rather, Anglo American submits that the costs of the repair and construction works should be attributed as replacement capital expenditure (or treated as part of its renewals program) in the CQCN (ie, as a replacement of parts of the existing infrastructure, which it essentially is) and these costs should be optimised into the RAB. Obviously, the value of the damaged or lost

assets should be removed from the RAB as these assets are no longer part of the CQCN, meaning that Aurizon Network will once again end up receiving a regulated rate of return (at the relevant WACC) on a RAB which is based on the actual current value of those assets. However, Aurizon Network will then receive that WACC on the repair construction costs over the period of the depreciation.

Further, as a number of systems within the CQCN are already heavily depreciated, Anglo American does not believe that Aurizon Network will stand to lose from removing the value of the damaged assets out of the RAB. This will not impact significantly, as Aurizon Network will actually stand to gain from the increased value of the RAB when the replacement construction costs are optimised.

In no instance does Anglo American believe that Aurizon Network should be entitled to a regulated rate of return in respect of pass through costs. Anglo American understands that there is regulatory precedent that takes this approach, however, Anglo American submits that this precedent does not align with regulatory theory, and therefore should be reversed.

11.6 Confidentiality requirements

Anglo American submits that there should be amendments to the Access Undertaking, or to the QCA Act, in relation to the provision of confidential documents to the QCA for its regulatory purposes. In particular, Anglo American believes that there should be provision in the Access Undertaking that allows documents to be provided to the QCA for it to exercise its regulatory functions even where those documents are subject to a commercial confidentiality restriction.

Anglo American believes that this is necessary for both Aurizon Network and stakeholders. Importantly, through the recent WIRP socialisation process, Anglo American has noted that a number of stakeholders possessed information that the QCA required in order to make a properly informed decision, however, were unable to present it to the QCA because of existing confidentiality restrictions.

Anglo American understands that it would be appropriate for any documents provided to the QCA under this power to remain confidential to the QCA, rather than a requirement to make the documents public. Anglo American does believe, however, that it is far better for there to be some level of confidentiality around the documents that the QCA bases its decision on, as opposed to the current situation where there is limited information available to the QCA and it is forced to rely on stakeholders or Aurizon Network submitting that certain representations were made, but being prevented from providing any evidence of those representations because of confidentiality restrictions.

Anglo American submits that the QCA's ability to make a fully informed decision in relation to the regulation that it has oversight of is of paramount importance and should be supported in every way possible by the Access Undertaking.

ATTACHMENT A

Other Minor Drafting Considerations

Part	Issue
Part 2: Intent and Scope	Clause 2.2(h)(ii)(C) should not constitute a separate paragraph but indented once to the left-hand margin.
	Clause 2.5(e) should not refer to a "standard access agreement" but to "an Access Agreement". Even if an access agreement executed before the Approval Date is not in the form of a standard access agreement, it should be grandfathered.
Part 3 - Ringfencing	Clause 3.19 has a paragraphing issue. There should be no paragraph 3.19(a)(iv) and the paragraph which is current numbered (iv) should be moved to be directly under the numbered paragraphs (i), (ii) and (iii).
Part 4 - Access Agreements	Clause 4.3(f) refers to clause 6(g) but maybe should refer to clause 6 (including all subclauses).
	Clause 4.4(b) should not be subject to confirmation under an Acknowledgement Notice. If Aurizon Network fails to issue such a notice a user may lost its position in a queue because the deeming will not operate unless a Notice is issued.
	Clause 4.5 - should remove the reference to "in good faith". Obligations on Aurizon Network in Part 4 only refer to "acting reasonably" and the obligation on users should not be higher.
Schedule D	Clause 3.5(b) provides that Aurizon Holding will be liable for any consequential loss suffered by "any party". The only "party" to the Deed is Aurizon Holdings. There is no definition of "party" in UT4. The clause should refer to "any person".

ATTACHMENT B
Draft Study Funding Agreement