AURIZON

Professor Roy Green
Queensland Competition Authority
Level 27
145 Ann Street
BRISBANE QLD 4000

17 March 2017

Dear Roy

Aurizon Network Pty Ltd (Aurizon Network) - The 2017 Draft Access Undertaking (UT5) – Update relating to the consultation period for collaborative stakeholder submissions

Aurizon Network welcomes the opportunity to provide the Queensland Competition Authority (QCA) with an update outlining the progress made during the consultation period for collaborative stakeholder submissions, in accordance with the QCA's Statement of Regulatory Intent applying to UT5.

Aurizon Network continues to recognise the significant investment by industry in the ongoing regulatory process, and is encouraged by the level of interaction and engagement.

Since submission of UT5, Aurizon Network has actively engaged with stakeholders through various forums including individual customer meetings, industry working groups and provision of information to stakeholders. This engagement has led to positive outcomes which are detailed within this submission.

The purpose of this submission is for Aurizon Network to respond to a number of issues raised in stakeholder submissions where it is appropriate to do so at this stage of the regulatory process. This submission:

- Outlines the policy positions that have been agreed with stakeholders;
- Provides further information to assist stakeholders; and
- Highlights and clarifies a number of incorrect statements within stakeholder submissions.

Aurizon Network will continue to work with both the QCA and stakeholders to seek a timely and appropriate resolution to UT5.

Yours sincerely

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Aurizon Network Submission
2017 Draft Access Undertaking

Submission following collaboration with Stakeholders

Prepared by Aurizon Network
17 March 2017

Executive Summary

As part of the Queensland Competition Authority's (**QCA**) Compulsory Undertaking process outlined in their Statement of Regulatory Intent, stakeholders including industry associations, above rail operators and coal producers **(Stakeholders)** were required to formally provide their initial submissions on Aurizon Network's 2017 Draft Access Undertaking (**UT5**) on 17 February 2017.

The purpose of this document is for Aurizon Network to provide a report back to the QCA following the collaborative consultation period. This submission:

- Outlines the policy positions that have been agreed with Stakeholders;
- Provides further information to assist Stakeholders; and
- Highlights and clarifies a number of incorrect statements within Stakeholder submissions

This submission has been structured to align with the individual chapters of Aurizon Network's UT5 submission dated 30 November 2017 (**UT5 Submission**). This submission only seeks to address issues that were, by their nature, appropriate to deal with during the collaborative consultation period. That is, issues where it appeared that there was scope for reaching consensus. As such, this submission does not address all issues raised by Stakeholders in their initial submissions, nor does it provide a detailed response to individual matters raised. Aurizon Network will respond to issues raised in the initial submissions as part of the consultation conducted with respect to the QCA's draft decision.

Aurizon Network has worked with Stakeholders during the defined Collaboration Period (17 February to 17 March 2017) to provide further information to address matters raised within Stakeholder submissions and also to work with Stakeholders to reach agreed positions on a number of policy matters. Aurizon Network appreciates the opportunity provided in the Statement of Regulatory Intent to complete this period of collaboration.

Aurizon Network remains focussed on the timely and efficient delivery of UT5, whilst ensuring that it generates revenue commensurate with the regulatory and commercial risks involved in our business. To support these objectives, Aurizon Network has undertaken a thorough engagement process since our UT5 Submission:

- 30 November 2016 - Correspondence sent directly to Stakeholders outlining policy and system based pricing;
- 1 December 2016 onwards – Meetings with individual producers and operators to outline the contents of the submission and gather initial feedback;
- 12 December 2016 – Presentation to the QRC's Rail Working Group to outline the UT5 Submission and hear Stakeholder feedback directly
- January 2017 – Ongoing negotiations on policy matters with Stakeholders, aiming to establish agreed positions;
- January to February 2017 – Responses to information requests from Access Holders, to assist them with their response to the UT5 Submission; and
- 17 February to 17 March – Detailed engagement with Stakeholders to reach agreed drafting on policy items which were amenable to the collaboration process

Aurizon Network will continue its engagement with the QCA to provide further context to our submission and respond to detailed information requests.

As a result of its engagement with the Queensland Resources Council (**QRC**), Pacific National (**PN**) and Aurizon Operations (**AO**), Aurizon Network has reached agreed drafting on the following matters:

Table 1 – Agreed Drafting

Item	Brief Description
Relinquishments associated with increased payloads	Process to facilitate low cost relinquishment of paths where excess paths result from increase payloads.
Transfers	Simplified drafting. No fee for transfers under 2 years.
Access Conditions	Immaterial matters and non-coal carrying train service agreements excluded from the QCA approval process.
Supply Chain coordination	Drafting as per Aurizon Network's 30 November 2016 submission.
System Capacity Assessment	New annual assessment of System Capacity for information purposes only.
Standard Rail Connection Agreement	Aurizon Network required to conduct a review of the SRCA during the UT5 period.
RAB – treatment of disposals	Aurizon Network agrees to QRC proposed drafting in relation to clause 1.1(c)(i) of Schedule E
Disputes – minor clarification to clause 11.1.1(b) only)	Clarification to ensure disputes in relation to non-coal carrying train service agreements are covered.

A detailed description of this agreed drafting is set out in section 3, with the specific terms of the agreed drafting for each of the draft UT5 Access Undertaking, draft UT5 Standard Access Agreement and draft UT5 Standard Train Operations Deed provided in Appendix 1

The remainder of this Executive Summary provides the key points for each of the parts of this submission.

Inflation

Having misaligned inflation rates within the regulatory models is inconsistent with the nominal debt contract in place. In addition, ensuring an entity has an accurate forecast inflation rate is important as it affects the timing of cash flows. The QRC's view of the Australian Energy Regulator's recent decision does not take into consideration the requirements to comply with the National Electricity Rule's Post Tax Revenue Model requirements.

Forecast Volumes

Stakeholders agreed with Aurizon Network that the UT5 volume forecast will be reviewed by the QCA's appointed consultant.

Regulated Asset Base

The approval of new assets into the Regulated Asset Base (**RAB**) follows a detailed prudency assessment for each project. As part of that process, the QCA publishes information on their assessment of the capital spend for all Stakeholders to review. The last step in the inclusion of capital in the RAB sees further system based information being published through the RAB roll-forward mechanism.

Capital Indicator

Aurizon Network has provided more detail regarding the forward looking scope of the capital indicator. Specifically, there is additional information that has been provided that outlines how the scope is set for the forthcoming year, along with the planned scope for Financial Year (**FY**) 2018.

Maintenance Cost

On 13 March 2017, Aurizon Network presented a maintenance symposium to industry on matters that were raised within their submissions and address the requirements of clause 10.3.1 of the 2016 Access Undertaking. Specifically, this presentation aimed to provide more information to outline the efficient costs and more detailed information relating to historical spend and maintenance performance.

Operating Expenditure

Within Aurizon Network's UT5 Submission, information on the treatment of escalation factors such as Wage Price Index were articulated and displayed graphically. In addition to this information, greater information relating to the major projects and the regulation functions within Aurizon Network has been provided to outline the rationale for including those costs.

Weighted Average Cost of Capital

Aurizon Network has previously provided information to justify the rationale for not rolling forward the Weighted Average Cost of Capital (**WACC**) and retaining UT4 parameters. Within the UT5 Submission, detailed analysis and information relating to the risk assessment of Aurizon Network was provided. Reviewing Stakeholders comparable submissions from the Hunter Valley Coal Network (**HVCN**) regulatory regime where they highlighted that the CQCN is a riskier asset yet have supported a WACC 1.2% higher in the HVCN, highlighting Stakeholders conflicting and opportunistic view on risk and return.

Depreciation

All Stakeholders agreed to the approach for retaining the current depreciation arrangements from UT4

Reference tariffs

The QCA is aware of the confidential Wiggins Island Rail Project (**WIRP**) deed arrangements and the protections that it does and does not afford to Aurizon Network. The WIRP deed does not fully protect Aurizon Network for deferral or optimisation risk as the QRC suggests. In addition, all existing users of the Blackwater system are benefiting from the WIRP infrastructure being within the RAB due to socialised pricing.

Other Issues

Aurizon Network will continue to collaborate with Stakeholders on AT5 and will aim to submit a Draft Amending Access Undertaking (**DAAU**) by 31 July 2017 or sooner if a workable solution through collaboration is achieved.

Aurizon Network also agrees with the Dalrymple Bay Coal Chain Coordinator (**DCCC**) proposal to address Take-or-Pay pooling arrangements as part of a future DAAU.

1. Introduction

As outlined in the Aurizon Network Submission 2017 Draft Access Undertaking, coal producers have responded to subdued metallurgical and thermal coal price conditions by seeking productivity gains. Despite this unit cost reduction, there were periods since the approval of UT3 (primarily Q4 2015 to Q2 2016), where up to a quarter of Australian metallurgical coal export volume was understood to have operated at a negative cash margin. As a result of price pressure, some mines became insolvent during the UT4 period; Aurizon Network continues to monitor the situation with these mines and customers.

Relief in the form of higher coal prices was provided in the second half of 2016 where the implementation of policy in China impacting domestic coal production resulted in the primarily self-sufficient nation turning to the seaborne market to meet coal demand. This drove scarcity and a resulting increase in seaborne prices. Following on from a relaxation of the domestic supply-side constraints in China, both the metallurgical coal price and thermal coal price have retreated from the levels witnessed in late 2016, trading at around US$165/t and US$80/t respectively in March 2017.

Aurizon Network notes the submission made by the QRC and also shares the view put forward of the relative strength of Australia metallurgical and thermal coal supply, typically measured by cost position. However, Aurizon Network challenges the use of a metallurgical coal margin chart[1] and a thermal cost curve[2] as a balanced representation of difficult trading conditions experienced by Australian coal producers in recent times. In particular, the view put forward by the QRC that with only very rare exceptions all Australian coal mines remained cash margin profitable[3].

As noted in the metallurgical coal chart reproduced by QRC, the metallurgical coal price assumption for Hard Coking Coal used was US$90/t. Although this spot price was reached in April 2016, for the preceding twelve months, the spot price did not breach this level, including the period from mid-October 2015 to mid-March 2016 where metallurgical coal traded at less than US$80/t. It is also noted that quarterly metallurgical coal contract price was less than US$90/t for the nine months to 30 June 2016. For thermal coal, the spot price identified in the August 2016 dated chart appears to be around US$68/t, a price level that had been seen in the previous 17 months

As such, the view put forward in the QRC submission does not appear to be a balanced representation of the difficult trading conditions experienced by Australian coal producers in recent times. Reference is made to the QRC State of the Sector Report (*Sector doing its best to keep its head above water*) from February 2016, where, through QRC-commissioned analysis by Wood Mackenzie, the report states

> *One-third of all our coal mines in Queensland are running at a loss – in other words they are not earning enough revenue to cover their cash costs. Breaking that down further, more than half of Queensland's thermal coal mines (producing coal for power generation) and one in four of our metallurgical coal mines (producing coal for steel making) are not covering their cash costs.*

As stated in the UT5 Submission, expenditure for coal exploration in Queensland has typically followed, albeit with a lag, the movement of the prevailing metallurgical price and more importantly, expectations of future price. Recent data including the month of December shows that the increase in coal prices seen in the second half of 2016 has not resulted in a significant increase in Queensland coal exploration spend. Such a response is not unexpected, given the volatility surrounding higher coal prices. This is best summarised by Mike Henry, BHP President Operations (Minerals Australia) in November 2016:

> *It's not going to be sustainable in the long term. The only question is when you see it balancing downwards. Is that next month, in two months, is it in six months? And for this reason, the prices were not causing BHP to pump more coal out of its low-cost mines to capture the huge margins on offer.*[4]

With UT4 operational, Aurizon Network has a stable regulatory base to continue to improve its performance and reliability by knowing its required scope and respective allowances. Ultimately this benefits the producers through the ability to meet their demand. Ongoing focus on key performance indicators include:

> a continuation of a lost time injury frequency rate of zero in the first half of FY2017;
> an ongoing focus to deliver the agreed plan, with first half performance to plan rate of 91.5%; and
> improving asset management leading to a 20% reduction in system closure hours[5].

Aurizon Network is well positioned to deliver on its Stakeholder requirements in volatile price and demand markets. Aurizon Network's reliability and efficient cost base must continue to allow coal producers in the Central Queensland

[1] Aurizon Network 20017 DAU QRC Submission, Volume 2: Pricing Submission, 17 February 2017, Figure 10, Page 26
[2] Aurizon Network 20017 DAU QRC Submission, Volume 2: Pricing Submission, 17 February 2017, Figure 11, Page 27
[3] Aurizon Network 20017 DAU QRC Submission, Volume 2: Pricing Submission, 17 February 2017, Page 27
[4] BHP says coal prices 'not sustainable', The Australian, 10 November 2016
[5] Half Year Results Analyst Presentation, Aurizon Holdings Limited, 13 February 2017, slide 7

Coal Network (**CQCN**) to meet current and future demand rapidly and efficiently in order to remain competitive in a global marketplace.

2. Chapter 2 – Legislative Framework

The topic of the legislative framework did not lend itself to collaboration and is not addressed in this submission.

3. Chapter 3 – Policy Positions

Agreed Policy drafting

In stakeholder's submissions, there was general support for limiting the scope of change from UT4. Since the UT5 submission, Aurizon Network has continued to progress upon its pre-lodgement engagement with both producers and operators to find common solutions to those policy positions, which are amenable to the collaboration process.

Aurizon Network has outlined below, a description of the drafting agreed with each of the QRC, Pacific National[6] and Aurizon Operations[7]. Where relevant, the specific terms of the agreed drafting is provided in Appendix 1. Aurizon Network's description of the agreed drafting is set out in Table 2 below.

Table 2 – Agreed Drafting

Item	Aurizon Network's Description of Agreed Drafting
Relinquishments	Agreed provisions to enable low cost access holder initiated relinquishment of paths, where excess paths result from access holder/operator initiatives to increase train payloads. Given industry and operator concerns in relation to Aurizon Network's proposal that Aurizon Network should be able, in appropriate circumstances, to initiate payload increases and associated relinquishments, Aurizon Network has agreed to drop this aspect of its proposal. Consequently, clause 12 of Aurizon Network's submission draft of the Standard Access Agreement dated 30 November 2016 (and associated definitions) has been deleted The relinquishment fee will be the present value of the AT2 component of TOP Charges that for the relinquished access rights would have been payable for the reminder of the term of those access rights.[8] Drafting has been included to ensure that where Access Holders notify Aurizon Network that they wish to amend their existing access agreements to incorporate these provisions, Aurizon Network will agree to such amendments. Agreed drafting is provided in Appendix 1 which includes a revised draft of the UT5 Standard Access Agreement, Standard Train Operations Deed and Clause 7.4.9 of the Access Undertaking).
Transfers	Agreed redrafting of the UT4 transfer provisions to improve clarity and workability. With one exception (relating to the transfer fee free period), the intent of this redrafting is not to change policy positions

[6] Pacific National has yet to complete its review all of the associated definition changes in Part 12 of the Undertaking, however it has indicated that it will provide its view on these items in in a timely manner.

[7] Aurizon Operations has indicated that it supports the agreed drafting in relation to relinquishments, transfer and access conditions, and that it has no comments to make in relation to the other matters.

[8] In light of broader industry agreement and QRC support of this approach, Aurizon Network notes BMA has not sought to maintain its alternate view on the relinquishment fee (per its February 2017 DAU submission).

Item	Aurizon Network's Description of Agreed Drafting
	approved in UT4, but to clarify drafting and improve workability so that transfer provisions are easier to understand and apply. Agreed that no transfer fee should apply to transfers for periods of 2 years or less. This aligns with the UT3 position, and the position under a number of UT1 and UT2 agreements that were varied by agreement between the parties following the QCA's in principle approval dated 16 February 2016 [9] relating to the adoption of the UT3 transfer fee free period within UT1 and UT2 agreements. Aurizon Network anticipates this measure will assist adoption and use by access holders of the UT5 transfer provisions, enabling access holders to take advantage of the UT5 expedited short term transfer process. Agreed drafting (clause 7.4.2 to clause 7.4.8) is provided in Appendix 1.
Access Conditions	Aurizon Network has agreed to adopt the QRC's proposed language with respect to Access Conditions (subject to two minor amendments discussed below). This will ensure that immaterial variations to standard access agreements do not require QCA pre-approval. Pre-approval will remain a requirement for other, more material variations. The first agreed minor amendment to the QRC's originally proposed language, is that non-coal carrying train service access agreements have been expressly excluded from the access conditions regime. The rationale for this exclusion is that the terms of the Standard Access Agreement relate specifically to coal-carrying services, such that access agreements for non-coal carrying train services will always vary from the Standard Access Agreement. This accords with our understanding of the original intent of the QCA's UT4 drafting and is supported by both non-coal carrying train service Access Holders (Aurizon Operations and Pacific National). The second agreed minor amendment to the QRC's original proposed drafting relates to the definition of Access Charge, so that an Access Charge only relates to an Access Agreement and not any other agreement or arrangement. This represents a reversion to the UT4 definition of Access Charge and to Aurizon Network's original UT5 proposal. Agreed drafting (clause 6.13 and the definitions of Access Charge and Access Conditions in Part 12) is provided in Appendix 1.
Supply Chain Coordination	Industry has agreed to support Aurizon Network's original drafting of the Supply Chain Coordination clauses (clause 7A.3). Agreed drafting is as set out in Aurizon Network's original UT5 submission dated 30 November 2016.
Supply Chain Capacity Review	Aurizon Network has agreed to undertake an annual assessment of system capacity (essentially, supply chain capacity) for each coal system. Aurizon Network has agreed to undertake this System Capacity Assessment on the basis that it will be for information purposes only for the benefit of Access Holders and Access Seekers (and their respective Customers and Train Operators), is not subject to expert review and will not result in any consequence for Aurizon Network in the event that a supply chain capacity deficit is identified in the System Capacity Assessment. Aurizon Network considers this position is appropriate given that Aurizon Network does not control elements of the supply chain other than its below rail infrastructure, and hence should not be penalised in the case of deficit which is outside its control. This measure is volunteered by Aurizon Network to provide clarity in relation to supply chain capacity, assist in identifying supply chain bottlenecks and promote industry discussion on how best to address these. Agreed drafting (new clause 7A.4.3) is provided in Appendix 1. Note the QRC originally proposed alternate drafting within 7A.4 to deal with System Capacity Assessments. Given the agreed position described, QRC has confirmed it no longer presses the balance of amendments it had sought to clause 7A.4 to the extent they relate to System Capacity Assessments.
Standard Rail Connection Agreement	The QRC has withdrawn its submission that the Standard Rail Connection Agreement should be reviewed as part of the UT5 approval process, in return for a commitment by Aurizon Network to review the SRCA by a date no later than 12 months following the approval of UT5.

[9] Available on the QCA's website at http://www.qca.org.au/Rail/Aurizon/Intro-to-Aurizon/2010-Access-Undertaking/Aurizon-s-2010-AU-Ongoing-Compliance/Transfer-Fees/In-Progress/UT2-Transfer-Fees

Item	Aurizon Network's Description of Agreed Drafting
	Agreed drafting (new clause 9.2) is provided in Appendix 1.
RAB	Aurizon Network agrees to the QRC's proposed drafting change to clause 1.1(c)(i) of Schedule E which relates to the appropriate treatment of disposals from the RAB. (See QRC drafting submitted on 17 February 2017) Aurizon Network notes that the QRC has supported Aurizon Network's proposed drafting in clause 1.2(b)(i), 1.2(b)(ii) and 1.2(b)(iii) of Schedule E which relates to RAB optimisation. (See relevant clauses of QRC's drafting submitted on 17 February 2017) For clarity, Aurizon Network does not agree with the QRC's proposed new clause 1.2(b)(iv) to address the treatment of an Expansion related Capacity Shortfall within the RAB, for reasons outlined below.
Disputes – (minor clarification to clause 11.1.1(b) only)	Aurizon Network has agreed to a small revision to its original wording to ensure that non-coal carrying train service agreements are not inadvertently exempted from the dispute resolution provisions, because the dispute relates to a refusal by a party to vary the terms of a Standard Access Agreement. This is appropriate because the Standard Access Agreement relates to coal-carrying services, and must always be varied to accommodate non-coal carrying train services. Agreed drafting (clause 11.1.1(b)) is provided in Appendix 1.

Otherwise, Aurizon Network's position on policy items set out in its UT5 submission remains unchanged.

Other Policy Matters raised by Stakeholders

Although there was support for limiting the number of policy changes from UT4, some Stakeholders have commented on additional policy matters for QCA review. However, Aurizon Network considers these submissions have not set out a compelling case for change. These positions include:

Table 3 – Other policy matters

Matter	Stakeholder	Aurizon Network Position
Self-insurance – More prescriptive details outlining how events are funded using self-insurance	Anglo American	The Access Undertaking is clear about self-insurance and cost pass-through mechanisms.
Confidential Information (Ringfencing)	Anglo American and Pacific National	This part of the Access Undertaking was discussed at length during UT4 and new controls were mandated through that process. Prior to adopting additional change, appropriate time should be allowed to enable an informed assessment of these UT4 controls.
Form of Regulation	Anglo American	Outside the scope of an undertaking review
Review Event Process – Greater clarity on process	Anglo American	Aurizon Network will continue to seek to involve Stakeholders in the review event process, specifically on the period over which costs should be recovered. This is coupled with the QCA process of consultation and detailed engineering consultant review of review event claims. Aurizon Network agrees that it makes sense for the QCA to review the capital and operational expenditure claims associated with flood recovery at the same time (although the recovery method will differ) and will work with QCA staff to facilitate this approach (under existing Access Undertaking provisions) in respect of future flood related review events.

Matter	Stakeholder	Aurizon Network Position
Incentive Mechanism	Pacific National	The consideration of a KPI and a supporting incentive regime is appropriate. However a review of this needs to ensure that the correct KPIs are set, with appropriate incentives. This would be appropriate to include with the future pricing review.
Treatment of Capacity Shortfall within the RAB	QRC	Aurizon Network considers existing provisions within Schedule E (conditional pre-approval and ex-post approval of prudency and efficiency of Expansion capital for inclusion within the RAB) already deal appropriately with the situation where an Expansion does not deliver anticipated capacity.

4. The UT5 Maximum Allowable Revenue Proposal

The topic of the UT5 maximum allowable revenue proposal did not lend itself to collaboration and is not addressed in this submission.

5. Inflation

Stakeholder Issue - Different inflation rates is consistent with nominal debt financing

The QRC submits that the current approach of using different inflation rates in the regulatory models

> *"….links regulatory WACC determinations to financial markets where regulated businesses finance their activities using nominal debt and equity. Using a nominal WACC provides a regulated cash flow profile that better matches the servicing of nominal debt and equity."*

Aurizon Network Response

The misalignment of inflation rates used in the regulatory models is actually inconsistent with the nominal debt contract in place, as it delivers a target real cost of capital. This is explained in pages 114-116 of Aurizon Network's UT5 Submission and page 9-10 of the accompanying CEG report on inflation.

Stakeholder Issue - Implication of using forecast inflation in RAB roll-forward model

The QRC submits that

> "*If the QCA was minded to adopt a forecast of inflation for both the roll forward of the RAB and calculation of the ARR, there are two key implications:*
>
> a) *firstly, any methodology for forecasting the inflation rate will satisfy the NPV=0 principle – such that a decision to align the approaches to inflation should not in any way alter the QCA's existing approach to forecasting inflation; and*
>
> b) *secondly, if Aurizon Network's is genuine about being concerned about the systematic risk it faces due to differences in forecast and actual inflation, removing that risk should lead to an appropriate reduction in beta to reflect the elimination of that risk.*"

Aurizon Network Response

Even if the QCA accepts the proposal to use forecast inflation in the RAB roll-forward model, it is still important to have an accurate inflation forecast. This is because forecast inflation rate affects the timing of cash flows. Having adequate cash flows is important as Aurizon Network needs to distribute regular cash flows to both equity and debt holders, and also fund the sustaining/renewal capital expenditure.

The relationship between the proposed change in inflation used in the RAB roll-forward model and systematic risk is not plausible. For example, if equity investors prefer a real return, then the proposed change actually increases equity investor's risk. For systematic risk, it also depends on the relationship between the inflation movement and the market portfolio return. It is not a sound conclusion that by correcting the inflation rate inconsistency will reduce the systematic risk for Aurizon Network.

Stakeholder Issue - Long-term inflation forecast provides more stable cash flows

The QRC has provided the following statement in their submission:

> *"the inflation forecast simply becomes a cash flow deferment factor. By using a stable deferment factor across multiple regulatory periods, the QCA would provide stable and predictable cash flows."*

Aurizon Network Response

As explained in page 118 of Aurizon Network's UT5 Submission, breakeven inflation forecast is more likely to provide stable cash flows than the long-term forecast of 2.5%. As shown by CEG, breakeven inflation has a strong positive correlation with the nominal risk-free rate.[10] This means when the risk-free rate is high (resulting in a high WACC assuming other parameters are constant), breakeven inflation is likely to be high. As a result, the higher return on capital building block will be proportionately offset by a higher rate of inflation subtracted from the depreciation building block. Ultimately this approach smooths the Reference Tariffs over time.

Stakeholder Issue - Breakeven inflation forecast has been rejected by the AER in the AusNet Services Decision

QRC submits that breakeven inflation forecast has been rejected by the Australian Energy Regulator (**AER**) and that this decision highlights the flaws with the proposed approach.

Aurizon Network Response

Aurizon Network notes the decision to reject the breakeven inflation forecast by the AER. However, one of the important considerations of the AER, is the requirements of the post-tax revenue model (**PTRM**) under the National Electricity Rules (**NER**) which was outlined within the AER decision being:

> *"Moreover, the method for estimating expected inflation is defined in the post-tax revenue model (PTRM) and changing this should be done in accordance with distribution consultation procedures."*[11]

The AER therefore interprets the NER as limiting the ability of the AER to change the methodology for inflation for an individual regulated entity. The AER's position is that a change the inflation methodology requires a change to the PTRM, which is a standard approach for all entities in which the AER regulates.

This reasoning is further re-inforced by the determination of the Australian Competition Tribunal in respect of an application for review brought by South Australian Power Networks (**SAPN**), where the Tribunal found:

> *"For the reasons given, the Tribunal concludes that the PTRM is binding on SAPN and the AER such that AER cannot consider inflation outside the PTRM, as proposed by SAPN. Accordingly the Tribunal concludes that the AER did not make any error."*[12]

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[10] CEG, 2016 Best Estimate of Inflation: Revaluation and Revenue Indexation, pp. 26-28.
[11] AER, 2016, AusNet Services distribution determination final decision 2016-20, Attachment 3, p. 153.
[12] ACT, 2016, Application by SA Power Networks [2016] ACompT 11, para. 619.

The QCA, on the other hand, is not bound by the NER in the assessment of Aurizon Network's inflation proposal. Therefore, Aurizon Network does not consider the rejection of breakeven inflation forecast by the AER due to the requirement of the NER has any implications for the QCA's determination on Aurizon Network's proposed inflation forecast methodology.

A change in the way the rate of inflation was calculated was reinforced late last year by the Economic Regulation Authority of Western Australia (**ERAWA**), as part of the 2016 Rail Weighted Average Cost of Capital review[13], which saw them move away from the RBA mid-range forecast of 2.5% and adopt the breakeven inflation forecast.

6. Forecast Volumes

Aurizon Network continues to support the independent review by the QCA of the forecast tonnes.

7. Chapter 7 – Regulated Asset Base

Stakeholder Issue – Information on the build-up of the RAB

Anglo requested that there should be a "bottom up" build of RAB values by system so that users can see the detailed assets and other granular aspects, including asset write offs, etc making up the proposed RAB value in each system.

Aurizon Network Response

For clarity Figure 30 (page 155) in the UT5 Submission is only a forecast RAB. It contains approved capex until FY2015 and forecast spend for FY2016 and FY2017 respectively. The capital indicator estimates the capex for the UT5 period.

Aurizon Network believes that Stakeholders have sufficient visibility on what capital is included in the RAB under the existing regulatory processes which includes consultation relating to the capital approval process. Inclusion of assets into the RAB, follows the governance procedures outlined within Schedule E of UT4. The steps are as follows:

- Assets are included in the RAB only after the QCA has approved the capital expenditure through an ex post audit of the annual capital claim[14]
- The QCA appoints an independent consultant to perform this audit at a project and detailed transactions level.
- The consultant's analysis and findings are published and open for Stakeholder consultation.
- Following the consultation, the QCA makes a Final Decision on the claim. It should be noted that as part of this decision making process the QCA has in the past adjusted or rejected capital claimed by Aurizon Network for inclusion in the RAB.
- This is followed by the annual RAB roll-forward process. Where the approved capital project is included in the RAB .Each capital project is individually assessed and included in the RAB.

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[13] https://www.erawa.com.au/cproot/14527/2/Att%201%20Rail%20%20WACC%20Final%20Determination%20of%20WACC%202016%2061%20 2017.PDF

[14] While schedule F also details a pre-approval process including a detailed audit of prudency prior to project commencement. Recent times has not seen Aurizon Network seek pre-approval for capital projects.

- The RAB is reported at a system level. The RAB roll forward report is published on Aurizon Network's website following QCA approval. The QCA also publishes these reports upon approval on their website.

Once capital is included via the RAB Roll forward, the RAB is maintained at a system level and not asset level. Aurizon Network provides detailed models to the QCA and its auditors to support the processes above. Any difference between the indicator and actual capex is trued-up via the capital carry-over mechanism.

Capturing and tracking data at asset level for the RAB is not possible without significant investment in systems and resources which would add limited value.

8. Chapter 8 – Capital indicator

Stakeholder Issue - Asset renewals and maintenance trade-off

The QRC suggests that Aurizon Network has not demonstrated the tradeoff between investing in greater asset renewals rather that higher maintenance costs.

Aurizon Network Response

The proposed asset renewals regime is risk and priority based, balancing network availability, capital requirements and resourcing constraints. Assets are primarily renewed as they reach or are past their useful lives effectively maintaining the status quo.

Whist the maintenance and other reactive intervention costs relating to the renewed assets are reduced, this is offset by increased costs elsewhere on the network as other asset conditions deteriorate and have to be maintained until they can be renewed in an efficient manner. Hence the overall condition of the network remains largely constant requiring a steady maintenance/ renewal regime and costs remain constant as outlined at the maintenance symposium on 13 March 2017 and contained within Appendix 2.

Stakeholder Issue – Level of information on the Capital Indicator

Both the QRC and Anglo American consider there is insufficient information for the QRC to be able to make any detailed informed assessment of the efficiency or prudency of the proposed capital indicator. The QRC stated it will rely on the QCA consultants.

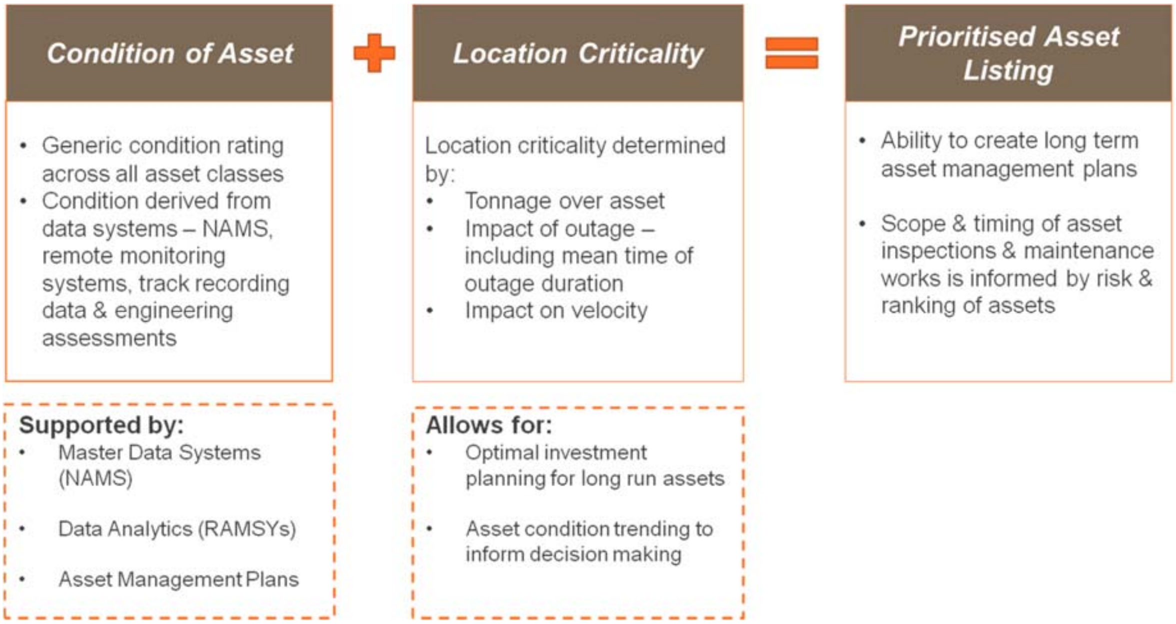
Anglo American went on to state that there is little information regarding the individual projects that make up the capital indicator.

Aurizon Network Response

Aurizon Network's capital indicator chapter was not detailed given the indicator is only a forecast of capital spend and actual capital is only included in the RAB subject to an ex-post assessment of prudency by the QCA.

Aurizon Network has a detailed framework to develop the scope for the capital indicator. This is detailed as below:

Figure 1 – Asset Based Management



The initial scope is then developed to a project level as part of the annual asset renewal program. Hence project level details on the capital indicator were not developed at the time of the UT5 Submission and were built at a broader program level scope which was provided in the submission.

Subsequent to the UT5 Submission, Aurizon Network has developed a more detailed renewals forecast for FY2018 which Aurizon Network presented to Stakeholders as part of Aurizon Network's Annual Maintenance symposium 13 March 2017. The scope is summarised in table 4.

Table 4 – FY18 Capital Renewal Plan

Blackwater $79.8m	Goonyella $94.4m	Moura $8.5m	Newlands $24.9m	System Wide $17.2m
• 22.1km rail renewal • 44.7km track upgrade • 3 Turnout renewals • 15,000 sleepers renewed • 5 structures renewed • 70km of Overhead minor component renewal • Power resilience upgrades at 13 sites	• 23.1km rail renewal • 30.2km track upgrade • 8 Turnout renewals • 7,400 sleepers renewed • 5 structures renewed • Level crossing upgrades at 8 sites • 73 km of Overhead minor component renewal • Location Case upgrades at 16 sites	• 2.3km rail renewal • 4.9km track upgrade • 1,051 sleepers renewed • 188m of bridge rollouts • Data coms upgrades at 21 sites	• 0.9km rail renewal • 2.1km track upgrade • 2 Turnout renewals • 1,896 sleepers renewed • 5 structures renewed • Data coms upgrades at 20 sites	• 0.9km rail renewal • 2.1km track upgrade • 2 Turnout renewals • 1,896 sleepers renewed • 5 structures renewed • Data coms upgrades at 20 sites

Stakeholder Issue - Capital Indicator to be endorsed by a 'Rail Capacity Group'

Anglo American believes the capital indicator should be presented and endorsed by a proposed 'Rail Capacity Group' or equivalent made up of the appropriate users of each system before consideration by the QCA.

Aurizon Network Response

Capital Expenditure is subject to a comprehensive ex-post audit and review by the QCA to assess prudency (in terms of scope, standard and costs) before inclusion in the RAB, as detailed in response to Chapter 7 above. The ex-post assessment process, means that Aurizon Network takes on the risk associated with the inclusion of the capital into the RAB.

If, at the end of a regulatory period there is a difference between the indicator and actual approved capex, it will be trued-up via the Capital Carry-over mechanism.

It is critical that an acceptable capital indicator is approved as part of the Draft Access Undertaking. This will allow tariffs to be set accurately and minimise any over/under recoveries through the use of the capital carry-over mechanism.

Aurizon Network presented to Stakeholders on the forecast renewal spend for FY2018 as part of Aurizon Network's Annual Maintenance Symposium on 13 March 2017. Aurizon Network believe this process already give Stakeholders an insight into Aurizon Network maintenance and renewals scope and plans.

As outlined within the UT5 submission on Page 155, there are significant engineering responsibilities tied to Aurizon Network personnel to ensure that it remains compliant with its Rail Infrastructure Manager accreditation. Aurizon Network's rail and safety framework is subject to regular audits and assessments to ensure it is compliant with the relevant obligations. As the entity that is responsible for compliance with these obligations and ensuring both the maintenance and capital program meet these requirements, seeking approval of these activities is difficult without allocating risk to those deciding parties. However, as part of its ongoing program of engagement with Stakeholders, Aurizon Network will be looking to provide greater ongoing transparency, to provide greater visibility of the task and any resulting impacts.

9. Chapter 9 – Maintenance Costs

Aurizon Network's maintenance position, including both scope and cost, remains as per its UT5 Submission. Aurizon Network is using this submission to provide Stakeholders with further information to assist with their review and understanding of the maintenance regime.

In addition, Aurizon Network provided a briefing to industry on 13 March 2017 as part of the annual Maintenance Symposium (in compliance with clause 10.3.1 of UT4). A copy of the presentation is included within Appendix 2.

Stakeholder Issue - Economic incentives to overstate maintenance scope

The QRC states that Aurizon Network has economic incentives to either overstate maintenance scope so that a higher MAR is recoverable or 'gold plate' or 'over-engineer' maintenance to reduce below rail risks, and Aurizon Operations' (AO) above rail risks and costs.

Aurizon Network Response

Aurizon Network believes that it plays a critical role in facilitating a reliable and efficient supply chain, which ultimately benefits coal producers and all rail operators in the CQCN.

Aurizon Network is not in a position where it can adjust its price for below rail access to take advantage of high market demand resulting from strong coal price. As a result, its focus is directed towards improving its core competencies, i.e. providing access to a robust and reliable coal rail network, which is fit for purpose. Aurizon

Network achieves this through an asset management regime which maximises the effective life of the network infrastructure while minimising whole of life costs.

Despite the variability in the spot and contract price for both metallurgical and thermal coal and the associated pressures on input costs, Aurizon Network's real unit costs of maintenance and asset renewal activities have remained relatively stable over time. This trend is illustrated by figure 2:

Figure 2 - Aurizon Network Asset Management Expenditure

Nevertheless, another critically important benefit to the supply chain is the demonstrable improvements in network performance that were outlined within Chapter 1 of Aurizon Network's UT5 submission[15].

Aurizon Network does not 'gold plate' the network infrastructure. To demonstrate to the QCA and Stakeholders that each coal system is maintained in a manner that is 'fit for purpose', a Condition Based Assessment (**CBA**) is undertaken during each regulatory period in compliance with clause 10.4.3 of UT4. The CBA assesses whether the network had 'deteriorated by more than would have been the case had good operating practice and prudent and effective maintenance and asset replacement policies and practices been pursued'.

In the FY2012 CBA, Evans & Peck found that the CQCN generally performed well and was maintained in a manner consistent with the targets for lagging indicators, leading indicators and operational key performance indicators. The FY2016 CBA is being completed, with the results due to be published within the coming months.

In addition, Aurizon Network regularly monitors and reports against the Overall Track Condition Index (**OTCI**) which is provided within the Quarterly Performance Report (clause 10.3.4 of UT4) and annually within the Maintenance Cost Report and accompanying presentation (clause 10.3.2 of UT4). For each system OTCI has remained within the required bounds in support of the Evans and Peck Condition Base Assessment.

Stakeholder Issue – Level of detailed information

Stakeholders including the QRC, Anglo American and QCoal, have expressed concerns over a lack of detailed information in relation to Aurizon Network's UT5 maintenance cost proposal.

[15] The Maintenance symposium presentation included within appendix 2, also contains performance data on slide 6.

Aurizon Network Response

As outlined in its UT5 Submission (p.153), Aurizon Network's maintenance scope is developed using a detailed bottom up process for each coal system.

In the UT5 Submission, Aurizon Network outlined that it has not sought to fundamentally change the process by which the approved maintenance scope and costs from UT4 were developed. As Stakeholders have pointed out, the UT4 process was detailed and provided multiple decision and numerous responses. The UT4 documentation provides a large quantum of information detailing the nature of how maintenance is scope, planned and executed. This was again contained within Chapter 9 of the UT5 submission.

In drafting its UT5 Submission, Aurizon Network sought to present its maintenance cost proposal in a way which clearly identified the variances from the QCA's UT4 Final Decision in the hope that it would improve readability and avoid the unnecessarily duplication of volumes of material provided as part of the previous regulatory process.

Furthermore, Aurizon Network recognises the pivotal role played by the QCA (and its consultants) in assessing the efficiency of both the scope and cost of the maintenance proposal for the UT5 regulatory period. . This is particularly so given Stakeholders logically have different priorities in relation to the management of different sections of the network. Aurizon Network has provided detailed information to the QCA is actively working with QCA staff as part of a Request for Information (**RFI**) process.

Aurizon Network acknowledges the concerns raised by producers and will take this feedback into consideration when preparing future regulatory submissions.

Additional information of performance to scope and UT4 allowance.

Aurizon Network has provided additional detail below to help them review Aurizon Network maintenance performance, including the:

- UT4 approved scope;
- UT4 approved cost; and
- Actual performance against both scope and cost for the UT4 regulatory period to date.

Information relating to the proposed scope and costs for the term of UT5, are contained within Chapter 9 of the UT5 Submission, which Stakeholder can use for comparison purposes. Please note that this data is presented at a CQCN wide level and has already been provided to the QCA.

Figure 3 – Ballast Undercutting Information

UT4 FINAL DECISION

SCOPE	FY2014	FY2015	FY2016	FY2017	TOTAL
Mainline Undercutting (km)	118	129	133	140	**520**
Turnouts (number)	41	40.3	40.3	40.3	**162**
Variance between 140km and approved scope		*11*	*7*		*18*

**QCA Final Decision provided turnout scope of 121 over final 3 years of UT4, and 140km per annum of mainli

UT4 SCOPE DELIVERED	FY2014	FY2015	FY2016	Scope Variance (FY14-FY16)
Mainline (km) - Linear	118	124	123	**(15)**
Mainline (km) - Volumetric	0	152	133	**23**
Turnouts (number)	41	48	58	**25**

*** Linear scope assumes uniform ballast depth of 300mm*

UT4 ALLOWANCE ($m)	FY2014	FY2015	FY2016	FY2017	TOTAL
QCA Final Decision - Real $FY2012	52.2	58.0	59.3	62.4	**231.9**
QCA Final Decision - Nominal	54.6	61.6	64.5	69.6	**250.3**

UT4 ACTUAL COSTS ($m)	FY2014	FY2015	FY2016
Ballast Undercutting	54.6	61.7	73.6
Variance to allowance Under / (Over)	(0.0)	(0.1)	(9.1)

Figure 4 – Rail Grinding scope, delivery and costs

UT4 FINAL DECISION

SCOPE	FY2014	FY2015	FY2016	FY2017	TOTAL
Mainline (km)	2,574	3,605	4,009	4,138	**14,326**
Turnouts (number)	546	666.0	813.0	780.0	**2,805**

UT4 SCOPE DELIVERED	FY2014	FY2015	FY2016	Scope Variance (FY14-FY16)
Mainline (km)	2,569	3,601	3,931	**(87)**
Turnouts (number)	537	628	783	**(77)**

UT4 ALLOWANCE ($m)	FY2014	FY2015	FY2016	FY2017	TOTAL
QCA Final Decision - Real $FY2012	13.4	13.7	12.9	12.7	**52.7**
QCA Final Decision - Nominal	14.1	14.6	14.0	14.2	**56.9**

UT4 ACTUAL COSTS ($m)	FY2014	FY2015	FY2016
RailGrinding	14.6	17.4	18.2
Variance to allowance Under / (Over)	(0.6)	(2.8)	(4.2)

Figure 5 – Resurfacing scope, delivery and costs

UT4 FINAL DECISION

SCOPE	FY2014	FY2015	FY2016	FY2017	TOTAL
Mainline (km)	1,881	2,093	2,227	2,376	**8,577**
Turnouts (number)	336	371	394	419	**1,520**

UT4 SCOPE DELIVERED	FY2014	FY2015	FY2016	Scope Variance (FY14-FY16)
Mainline (km)	1,882	2,146	2,356	**183**
Turnouts (number)	398	392	428	**117**

UT4 ALLOWANCE ($m)	FY2014	FY2015	FY2016	FY2017	TOTAL
QCA Final Decision - Real $FY2012	19.2	19.0	18.4	20.8	**77.5**
QCA Final Decision - Nominal	20.1	20.3	20.0	23.3	**83.7**

UT4 ACTUAL COSTS ($m)	FY2014	FY2015	FY2016
Resurfacing	19.1	21.2	21.7
Variance to allowance Under / (Over)	1.0	(0.9)	(1.6)

Stakeholder Issue - New mechanised maintenance assets

The QRC raised concerns relating to the level of information or evidence to support the procurement of the new mechanised machinery to ensure that it produces the productivity initiatives and that is correctly reflected in the maintenance costs allowance.

Aurizon Network Response

The new machinery within the Aurizon Network fleet includes tampers, a ballast undercutter and ballast spoil wagons. All of the replaced machinery was at either end of life or would be past it at the time new machinery could be commissioned. The new machinery was also purchased to allow Aurizon Network's to be able to deliver its contracted tonnes.

Stakeholder Issue - Maintaining built capacity

Anglo American states that it is inappropriate for Aurizon Network to maintain built capacity particularly where (forecast) volumes are considerably less with no clearly defined targets to reduce fixed costs.

Aurizon Network’s response

When Aurizon Network refers to the requirement to maintain built capacity, it is referring to the fact that the physical quantity of infrastructure within the CQCN was constructed to deliver a level of contracted capacity that was assessed through the Access Seeker and expansion process. Aurizon Network must maintain that infrastructure, and ensure that it is fit for purpose, in order to meet its commercial obligations to its Stakeholders.

For clarity, the scope of UT5 maintenance activities is essentially a product of three types of maintenance activities. These include:

- periodic interventions (for example, scheduled patrol inspection of heavy haul track every 192 hours, and annual engineering inspections);
- volumetric interventions (for example, grinding tight radius curves every 10 million gross tonnes); and
- unplanned corrective activities.

The scope of:

- volumetric interventions is directly linked to the forecast volumes proposed for the regulatory period or data driven activities, and accordingly, will be adjusted as the volume forecasts are refined through the regulatory process; whereas
- unplanned corrective activities are forecast after careful consideration of historical trends and asset renewal activities.

It should therefore be reiterated that the scope of such maintenance activities is not set assuming that contracted volumes will rail during the UT5 regulatory period.

The scope of periodic interventions, however, is directly linked to the quantum and characteristics of physical infrastructure within the CQCN and is therefore independent of volume. Such interventions (such as the inspection regime) are necessary to ensure the ongoing safe operation of rail infrastructure, which in addition to the substantial contact forces which exist at the rail-wheel interface is subject to extreme geographic and climatic conditions.

Stakeholder Issue - Financial benefits of preventative maintenance approach

Fitzroy Australia Resources raised concerns in relation to seeing benefits of Aurizon Network transitioning to a preventative maintenance approach.

Aurizon Network Response

Aurizon Network’s asset management regime seeks to proactively manage the rate of asset degradation, and by doing so, maximise the effective life of the network infrastructure, while creating a broader benefit of minimising whole of life costs. The impacts of the preventative regime have specifically flowed through to the UT5 revenue proposal in two forms:

- Expected scope of unplanned corrective activities, which is set with regard to historical trends and asset renewal activities; and
- Reduction in the proposed self-insurance premiums, due to downward trends of low severity derailments as result of Aurizon Network’s emphasis on preventative maintenance activities and the rail restressing program; further noting that the self-insurance costs form part of the operating cost proposal for UT5.

In addition, it should also be noted that a preventative maintenance approach, which encompasses a number of innovative work practices that Aurizon Network has implemented in the asset management space, also improves network reliability and availability. This creates a clear financial benefit to producers where below rail cancellations are avoided, which can been seen through the improvements in Aurizon Network performance indicators.

Stakeholder Issue - Inconsistencies in the submission.

The QRC notes that tables 27 and 28 under mechanised ballast undercutting list identical scopes for FY2018 and FY2019, and again for FY2020 and FY2021, yet the costs increase in real terms.

Aurizon Network Response

For clarity, the cost uplift in FY2019 and FY2021 are attributable to the forecast cost of additional GPR runs, which will be used to refine the scope of the ballast undercutting program, identify condition trends and better target areas in which ballast undercutting is required.

Stakeholder Issue - Maintenance task inherently linked to the RAB.

The QRC notes that maintenance tasks are 'inherently linked' to the capital investments previously made and that this is not the same as being 'inherently linked to the RAB'.

Aurizon Network Response

Aurizon Network confirms that the intent of the 'inherently linked' statement was to make reference to the physical quantum of infrastructure within the RAB, rather than imply that the maintenance task was linked to the residual economic value of those assets.

As outlined in the UT5 Submission, and in this response, a component of the Aurizon Network's maintenance scope is set with reference to volumetric interventions. To the extent that network infrastructure is under-utilised (relative to contract), the scope of forecast volumetric interventions will be adjusted accordingly.

It should be noted however, that even new infrastructure will still require preventative maintenance, in accordance with periodic and volumetric triggers.

Stakeholder Issue - Allocation of costs associated with traction engineers.

The QRC suggests that Aurizon Network's costs associated with traction engineers may be partly attributable to Aurizon's unregulated above rail business. As a result, the QRC suggests that only a portion of their costs should be included in the maintenance allowance.

Aurizon Network Response

Aurizon Network confirms that its traction engineers are solely engaged to perform work on Aurizon Network assets. It would be inappropriate for any such cost allocation to be applied as doing so would not compensate Aurizon Network for its efficient costs incurred in providing these services to the CQCN.

10. Chapter 10 - Operating Expenditure

Aurizon Networks operating expenditure position remains as per its UT5 Submission. Aurizon Network is taking the opportunity to provide Stakeholders with further information to assist with their review and understanding of the Operational expenditure.

Stakeholder Issue - Labour cost escalation

The QRC questions how labour costs can be escalated using the Wage Price Index (**WPI**), when Aurizon Network states that it has made labour cost savings.

Aurizon Network Response

Aurizon Network's forecasting methodology is clearly outlined in its UT5 Submission in section 10 and detailed graphically in figure 62. All labour cost savings (and other adjustments for non-recurrent costs) are first deducted from the FY2015 base year, prior to the adjusted costs (in real terms) being applied to estimate the cost base for UT5.

By doing so, Aurizon Network confirms the reduction associated with the labour cost savings flows through to the UT5 proposal in full and is not eroded by the application of WPI.

Stakeholder Issue - Non-coal carrying train services allocation to network control centre

The QRC is concerned that the 2% allocation of network control costs results in an insufficient allocation to non-coal carrying train services.

Aurizon Network's response

The change of allocation from 9% to 2% increases Aurizon Network's base MAR by approximately $1.3 million per annum; an increase of approximately $0.005 per net tonne at the proposed volume forecast for FY2018.

Aurizon Network maintains that the costs associated with providing network control services to non-coal carrying trains is negligible. Aurizon Network provided additional information in support of the 2% allocation as part of its response to the QCA's MAR Draft Decision on UT4 (pg. 50) and notes that this information remains relevant in the context of assessing an appropriate non-coal carrying train service allocation of network control centre costs.

Stakeholder Issue - Business management costs

The QRC concerns relate primarily to the impact of revised cost allocations associated with the Major Projects Group, Network Regulation and the allocation of network finance and legal costs. In particular, whether this results in regulated business effectively cross-subsidizing any 'non-regulated' activities that Aurizon Network becomes involved with.

Aurizon Network Response

The Major Project group, within the Network Commercial team, provide support relating to the process for network development, planning, studies and expansions, which is within the definition of the Below Rail Service. They are also involved in the development of the Standard User Funding Agreement.

Within Part 3 of UT4, Aurizon Network must at all times employ a regulatory affairs advisor, compliance officer and not outsource any regulatory function to any other part of the Aurizon Group. These obligations, the extensive compliance program within the Access Undertaking and responding to complex Stakeholder and QCA requests regarding any future enhancements to the Access Undertaking, make any work outside of the scope of the Access Undertaking difficult for the Regulatory team. For this reason, 100% of the Network regulation costs are included within the Operational Allowance.

Aurizon Network's proposed treatment of network legal and finance costs for UT5 results in an average cost saving of $1.6 million per annum, relative to the QCA's UT4 Final Decision.

Stakeholder Issue - Corporate costs

The QRC has expressed concerns that it appears that corporate costs have only reduced because of the reclassification of Finance and Legal to business management costs.

Aurizon Network Response

This is not correct. There has been a reduction in the submitted cost allowances in almost all functional areas. This is illustrated in the table below.

Figure 6 – Corporate Costs

Split of Corporate overhead (Nominal $)	UT4 QCA FINAL DECISION 2013/14 $m	2014/15 $m	2015/16 $m	2016/17 $m	UT5 SUBMISSION 2017/18 $m	2018/19 $m	2019/20 $m	2020/21 $m
Finance	10.7	10.9	11.1	11.4	3.0	3.1	3.2	3.3
General Counsel and Company Secretary	5.8	5.9	6.1	6.2	1.5	1.5	1.6	1.6
Internal Audit and Enterprise Risk Management	1.5	1.5	1.6	1.6	1.2	1.2	1.2	1.3
Information Technology	19.0	19.3	19.8	20.3	18.0	18.3	18.6	18.9
Human Resources	5.0	5.1	5.2	5.4	3.7	3.8	3.9	4.1
Safety, Health and Environment	6.4	6.5	6.7	6.8	2.5	2.6	2.6	2.7
Enterprise Real Estate	6.2	6.3	6.4	6.6	14.8	15.4	15.8	16.0
Enterprise Procurement	1.4	1.4	1.5	1.5	1.7	1.7	1.8	1.8
Enterprise Strategy and Branding	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Managing Director/CEO	1.7	1.7	1.8	1.8	2.1	2.1	2.2	2.2
Non-benchmarked functions	1.3	1.3	1.4	1.4	0.6	0.7	0.7	0.7
Less corporate stretch target	-5.0	-5.1	-5.2	-5.3	0.0	0.0	0.0	0.0
Total Costs ($)	54.0	55.0	56.3	57.8	49.1	50.5	51.6	52.6
Network Finance					5.1	5.3	5.5	5.6
Network Legal					3.0	3.0	3.1	3.1
					57.2	58.8	60.1	61.4

Corporate overheads of the Aurizon Group have decreased since UT4 was submitted as the company continues to implement transformational changes. As noted in our UT5 Submission, the actual costs for FY15 have been adjusted to included targeted savings for FY16.

We also noted in the UT5 Submission that the use of direct costs as an allocation methodology implicitly includes efficiencies, as it results in a lower cost allocation than would otherwise be provided using the blended allocator methodology which was detailed within Chapter 10 of the UT5 Submission.

The increase in the cost allowance for Enterprise Real Estate was explained within Chapter 10 of our UT5 Submission. Costs relating to operational sites were not included in the UT4 approved cost allowance, as they were not included in the submitted costs. This was due to corporate cost allowance originally being submitted for maintenance and other all areas separately. This was overlooked when the allowances were combined by the QCA, with the result that Aurizon Network has been under-recovering in relation to operational sites during UT4. Costs in relation to these operational sites are genuine costs to the Network business, representing amounts that Aurizon Network incur as a stand-alone entity, where these facilities are not owned by it.

In relation to licence/lease costs paid to AO (where the properties are owned by a related party), the market rate was determined based on a desktop market rental advice performed by CBRE Valuations Pty Ltd. The licence agreement between AO and Aurizon Network for the use of the properties provides for the licence fee to align to these market rates, and this licence fee is paid from Aurizon Network to AO.

Stakeholder Issue - Risk and insurance

The QRC states that “there is nothing in the undertaking provisions which prevents Aurizon Network from seeking to use the cost pass through mechanisms for costs below…” the specified threshold.

Aurizon Network Response

The only mechanism to seek recover of additional costs is the review event mechanism contained within Schedule F of the Access Undertaking. There is a minimum threshold for cost, requiring incremental costs to exceed at least $1 million before a claim can be considered. There are also other triggers outlined in Schedule F, Clause 5.3 which prevent claims under the $1m threshold. If incremental costs are under $1m and meet the requirement of a Force Majeure Event, then it would be expected that these costs would be incurred by Aurizon Network as these are re-covered through the self-insurance process and costs built into the Reference Tariffs.

11. Weighted Average Cost of Capital

The topic of the WACC did not lend itself to collaboration and is not addressed in this submission. Aurizon Network responds to some high-level positions on the weighted average cost of capital noted in Stakeholder submissions below.

Stakeholder Issue - UT4 WACC Roll-over

The QRC, QCoal, Anglo American, Fitzroy Resources and BMA submission expressed a preference to roll over the UT4 WACC, with market sensitive parameters updated.

Aurizon Network's Response

Aurizon Network's revenue proposal for UT5 aims to reflect the inherent risks of operating within the CQCN, which it believes are higher than what the QCA has previously considered. These risks include:

> a relatively small number of customers, all exposed to a single asset class (coal);

> the volatile operating environment of the CQCN;

> the RAB is fragmented by system (Moura, Blackwater, Goonyella, Newlands and Goonyella to Abbot Point System) which results in an increased risk of asset stranding; and

> revenue deferrals which result in expansion capital being excluded from the RAB.

Specifically as it relates to the WACC methodology, Aurizon Network has undertaken a comprehensive review for a number of reasons, including:

> Aurizon Network disagrees with many aspects of the QCA's UT4 WACC decisions. For example, Aurizon Network considers the reference to utility firms understates the risk exposure of Aurizon Network;

> There has been dramatic change in the financial market between UT4 and UT5. In particular, the 10-year risk-free rate has dropped from over 4% to around 2% in June 2016. As submitted in Aurizon Network's 2017DAU, market risk premium is likely to increase as the risk-free rate falls (page 259-263). Therefore, continuing the UT4 WACC will not provide a sufficient return that is commensurate with Aurizon Network's risk. Aurizon Network also notes that the initial Maximum Allowable Revenue Draft Decision[16] and the WACC Market Parameter Decision[17] were made in 2014. As a result, it is appropriate to reconsider the WACC methodology for UT5 given the dramatic market changes during this period; and

> Coal market conditions have deteriorated further during UT4 and have led to a deterioration in mining company credit ratings and changes in ownership structures. As a result, Aurizon Network's counter party risk has increased.

Stakeholder Issue - QRC's Overall WACC Position

The QRC has proposed a WACC that is materially lower than Aurizon Network's proposal. The QRC analysis provides limited evidence to support its position and it does not align to the *Queensland Competition Authority Act 1997 (QLD)* requirements where Aurizon Network would earn a return commensurate with its commercial and regulatory risks.

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[16] Queensland Competition Authority, Draft Decision Aurizon Network 2014 Draft Access Undertaking – Maximum Allowable Revenue, 30 September 2014

[17] Queensland Competition Authority, Final decision Cost of Capital: market parameters, August 2014

Aurizon Network's Response

The coal producers have been opportunistic with their comments between regulated rail entities. The majority of members of the QRC are also users of the HVCN and are members of the Hunter Rail Access Task Force (**HRATF**). On 6 February 2017, the HRATF responded to the Australian Rail Track Corporation 2017 Draft Access Undertaking for HVCN and has considered a WACC of 6.29% (using June 2016 averaging period) as appropriate while the QRC, made up of similar members, has recommended a WACC that is some 1.20% lower, as illustrated in Table 5.[18]

Table 5. Comparison between QRC and HRATF WACC submission

	QRC Submission	HRATF Submission
Regulated Entity	Aurizon Network	ARTC
Regulator	QCA	ACCC
Averaging period	Adj.to June 2016	June 2016
Risk-free rate	1.62%	2.14%
Risk-free rate term	4 years	10 years
Gearing ratio	55%	52.5%
Asset Beta	0.42-0.45	0.55^
Equity Beta	0.7	0.94
Market risk premium	6.0-6.5%	6.0%
Debt risk premium (inc. transaction costs)	2.69%	2.80%
Gamma	0.47-0.5	0.45
Return on equity	**5.82%-6.17%**	**7.78%**
Return on debt	**4.31%**	**4.94%**
WACC	**4.98%-5.16%**	**6.29%**

^Asset beta has been derived from de-leveraging equity beta using QCA's preferred Conine formula

The lower WACC proposed by the QRC for Aurizon Network is difficult to reconcile with HRATF's, considering their view of different risk levels between the CQCN and the HVCN:

> "*Our view is that a careful analysis of risks faced by ARTC compared to other regulated rail service providers on the east coast of Australia strongly supports our position that ARTC's asset beta should be materially lower than the level observed for Aurizon and QR*"[19]

The reasons cited include:

> "…*Aurizon operates several different coal systems with limited cross system traffic, with each individual coal system having lower volumes and less diversification of users than the Hunter Valley.*

> *ARTC has rolling 10 year agreements, meaning that ARTC has volumes contracted for the next 10 years. Aurizon access agreements have a term of 10 years with a right to renew, meaning that for an individual user the total future volume contracted to Aurizon will decline each year until renewal*

[18] To facilitate the comparison, Aurizon Network has adjusted QRC submission to reflect June 2016 averaging. For simplicity, Aurizon Network has used Bloomberg BBB yield curve to update debt risk premium.

[19] HRATF, 2016, ARTC 2016 HVAU Submission, p. 28.

> *Aurizon faces the risk that the QCA may remove from its regulated asset base the value of infrastructure which is deemed no longer to be required. This is not a risk faced by ARTC* …"

HRATF's view was initially articulated in their submission on ARTC's 2016DAU. However, as indicated in HRATF's submission on ARTC's 2017DAU, its view remains unchanged, and the previous submission was attached to this newer submission.

HRATF is advised by Castalia Strategic Advisors (**Castalia**), who have the same view that CQCN is of higher risk than the HVCN. Castalia is also the consultant for QRC on their response submission to Aurizon Network's 2017DAU.

Aurizon Network agrees with HRATF and Castalia that the CQCN should be of higher risk, and that should be reflected in beta, than the HVCN due to the nature of the differences which include:

> Aurizon Network's RAB is fragmented with limited ability to socialise revenues. This is recognised by HRATF, but largely ignored by the QRC;

> As indicated in Aurizon Network's submission on DBCT's 2015DAU, the weighted average (by volume) remaining contract duration as at 1 July 2016 is 5.3 years.[20] Access Holders are seeking to renew contracts for shorter terms when existing access rights expire rather than renewing for a 10-year period.[21] This is in direct contrast to HVCN's 10-year evergreen contract;

> Aurizon Network's capital expenditure is subject to the QCA's ex-post assessment. If any of the capital costs is deemed not to be efficient, it will be excluded. This additional risk is not shared by utility firms or ARTC.

More importantly, additional non-regulated returns are not relevant to the comparison of WACCs between the two coal networks as the QCA and ACCC are determining a rate of return for the existing assets in place rather than a major expansion project. The risk of large scale green or brown field expansion projects are fundamentally different to those of an existing assets.

The reasons provided do not fit with the user's arguments in proposing a WACC that is greater than 1.2% lower than what they would accept in HVCN.

Stakeholder Issue - Aurizon Share Performance and UT4 WACC Decision

The QRC and its consultant, Castalia, argue that the WACC for the UT4 period was appropriate and the market responded through Aurizon's share price which was not adversely affected by the UT4 revenue decisions. Specifically, the QRC has provided in its submission a chart of Aurizon's comparative share performance tracked against the S&P/ASX50 and S&P/ASX200. Castalia has included a similar comparison between Aurizon share performance and the S&P/ASX100.

Aurizon Network Response

The QRC submission states that it

> *"….is not suggesting that Aurizon's share price can provide meaningful indications of the appropriateness of the QCA's decision"*,

however, a comparison is still included in the submission.

Aurizon Network asserts that the QRC is correct in their statement that the inclusion of such comparison is flawed for the following reasons:

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[20] Aurizon Network, 2016, Aurizon Network submission on DBCT 2015DAU Draft Decision, p. 1.

[21] Aurizon Network, 2016, 2017DAU, p. 255.

- Aurizon's share price performance is subject to many factors, both internal and external to our business, and discrete announcements by the QCA over a four-year period are unlikely to account for the majority of share price movements during the comparison period;
- The market generally incorporates new information in a timely manner which means any QCA decision announcement will only affect share movement for a short period of time after the announcement, rather than the whole comparison period; and
- More importantly, the comparison of Aurizon's past share performance against a benchmark does not reveal any information about the market's assessment of whether it is appropriate to roll over the UT4 WACC with only the market parameters updated

Stakeholder Issue - Credit Rating

QRC submits that its WACC proposal allows Aurizon Network to maintain BBB+ credit rating.

Aurizon Network's Response

The QRC did not provide any form of analysis or data to support its statement as to the maintenance of a BBB+ credit rating. Furthermore, Aurizon Network is unable to interpolate a scenario whereby the QRC's WACC proposal would enable it to maintain a BBB+ credit rating during the UT5 period.

By adopting the QRC's proposed WACC and performing an internal calculation that mirrors a credit rating agencies' assessment, this would result in Aurizon Network not meeting either S&P or Moody's credit metrics (with FFO/Debt materially lower than 13%). Importantly, this was completed without taking into account QRC's proposal to continue all of the WIRP deferrals. Aurizon Network also notes QRC's comment that it may be justified by the QCA to use 10-year risk-free rate if Aurizon Network is facing financeability issues which is the case according to QRC's proposal.[22]

Stakeholder Issue - Aurizon Network's Risk Exposure

The QRC has submitted that Aurizon Network is immune from coal price volatility due to various regulatory protections. Due to the position of Australian export coal, Aurizon Network is at minimum risk and therefore its most comparable firms are those energy and water utilities. However, the QRC in its submission has not provided any further evidence of this beyond the UT4 decisions.

Aurizon Network Response

For clarity, Aurizon Network does not perceive that it has the same degree of exposure to coal price as coal producers. This is why Aurizon Network has not submitted coal mining companies as comparable firms within its beta estimates and instead, considered a sample of US pipeline companies to be the most comparable. The QRC or its consultants, Castalia, have not provided convincing evidence on why these are not appropriate comparable companies to Aurizon Network. Castalia has been inconsistent in the reasoning. For example, Castalia has considered the variability of returns for Aurizon Network is mainly driven by the regulatory regime, while mainly citing industry specific differences of US pipeline companies when rejecting them as the most comparable firms, even when they share similar regulatory regime and have long-term take-or-pay contracts in place.

Aurizon Network is nevertheless exposed to the long-term risk associated with the Queensland coal industry. The reasoning is simple, if Queensland coal export is not viable in the long run, Aurizon Network will not be able to recover its sunk investment of the long-term infrastructure assets.

As highlighted in the UT5 Submission, there has been an increase in the level of coal market volatility. Although Queensland coal is currently well placed on the global cost curve, it does not eliminate the long-term demand risk. A legitimate example could see lower cost producers emerge in the other regions of the world.

[22] QRC, Aurizon Network's 2017DAU – QRC Submission, p. 16.

The seaborne coal market and hence the demand for Queensland coal is also heavily influenced by China's coal domestic production policies 24.4% or 40.46mnt of CQCN coal was exported to China in Calendar Year 16. For thermal coal, there has been a high level of uncertainty due to climate change and the policies that underpin that. This risk is exacerbated by the CQCN RAB fragmentation with some systems having nearly half of their volume being thermal coal and a limited number of remaining producers.[23]

In the short term, these risks may not translate directly into a variation in Aurizon Networks cash flows, but in the long term it certainly will. Importantly, investors include these risk factors in their valuation of both the required return and cash flows for Aurizon Network, and hence, the valuation of the firm. As a result, Aurizon Network is not immune from the long-term risk associated with Queensland export coal market.

In this regard, utility firms are not comparable firms to Aurizon Network which is a view shared by rating agencies. In a recent credit rating report on Aurizon Network, Moody's has stated:

"Network's rating tolerance level is set a materially higher level than equivalently rated regulated electricity and gas utilities in order to reflect Network's ***intrinsically higher business risk****, a consequence of the higher volatility to which its key customers are exposed."*[24]

Similarly, Standard & Poor's has assessed regulated energy distribution businesses to have an 'excellent' business profile while Aurizon Network having a 'strong' (i.e., weaker than 'excellent') business risk profile. Therefore, Aurizon Network maintains its view that it is of higher risk than utility companies.

Stakeholder Issue - Relevance of deferrals to risk profile

The QRC considers that the WIRP revenue deferral is not a regulatory or commercial risk that should be compensated through WACC. Further, the QRC believe that the revenue deferral is not about the sharing of risk between users and Aurizon Network, but rather it is only amongst users. This is because:

> *"Aurizon Network, of course, is effectively kept net present value neutral due to the roll-forward to the capital on which a return is being deferred."*[25]

Moreover, the QRC suggests that the WIRP revenue deferral actually reduces Aurizon Network's risk as it is better than RAB optimisation. The QRC has stated:

> *"Aurizon Network has the benefit of a myriad of revenue protection mechanisms including:*
> *…*
> *8) limits on optimisation of the RAB (and the QCA's UT4 decision providing for deferral, which is net present value neutral for Aurizon Network, instead of optimisation)."*[26]

Aurizon Network Response

Aurizon Network disagrees with the QRC that WIRP revenue deferral is the sharing of risk among users. The WIRP revenue deferral effectively means Aurizon Network bears the risk of non-railing volume. It is contrary to the legitimate business interests of Aurizon Network and network investors, who are penalised for risks that are entirely outside of their control. Moreover, the WIRP revenue deferral will only be NPV neutral if there is no uncertainty around the recovery of deferred revenue. That is, one has to assume that there is perfect certainty that the current non-railing producers will start railing in the near future.

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[23] Aurizon Network, 2016, 2017DAU, Table 68 and Table 77.
[24] Moody's, 2017, Aurizon Network Pty Ltd Credit Rating, p. 3.
[25] QRC, Aurizon Network's 2017DAU – QRC Submission, p. 32.
[26] QRC, Aurizon Network's 2017DAU – QRC Submission, p. 30.

As discussed in Chapter 13, the additional risk from WIRP revenue deferral is not covered under the WIRP fee. As a result, this additional risk should be recognised in the WACC allowance as per the pricing principle contained in the QCA Act.

Lastly, Aurizon Network does not agree with the QRC that WIRP deferral reduces Aurizon Network's risk. Revenue deferral represents additional source of risk when compared to utility firms or HVCN.

Stakeholder Issue - Debt Risk Premium Term

The QRC considers that debt risk premium should be based on debt with a 5 year term to maturity.

Aurizon Network's Response

Aurizon Network notes that the QRC has submitted similar view during the UT4 process, and was rejected by the QCA.

The QCA concluded in its September 2014 Maximum Allowable Revenue (**MAR**) Draft Decision that

> *"We accept Incenta's benchmarking analysis and conclude that an efficient term of debt is 10 years. Incenta has also advised credit default swaps are not available to convert the debt premium component. As a consequence, we consider a 10-year term is reasonable in this instance."*[27]

Aurizon Network agrees with the QCA on this issue and considers that 10 years is the appropriate term for the estimation of debt risk premium.

Stakeholder Issue Cross-currency Swap Cost

QRC has submitted that

> *"Aurizon Network seeks to make much of the need for cross-currency swaps as a result of an asserted need for greater foreign bond issues. However, as noted above, the QCA has already appropriately resolved to use the high end of the domestic corporate bonds based estimate to practically make allowances for the extra costs of foreign bond issues. Accordingly the QRC submits that no specific allowance should be provided for cross-currency swaps."*

Aurizon Network Response

As submitted in page 278 of Aurizon Network's UT5 Submission:

> *"The QCA currently provides a benchmark allowance for debt raising costs of 0.108% and this assumption was applied to Aurizon Network in the UT4 Final Decision. The 0.108% allowance is derived with reference to domestic bond issues only. As pointed out by PwC in its report to the QCA, foreign bond issues attract 2.3 to 3.1 bps higher transaction costs."*

Therefore the QCA's UT4 Allowance for debt issuance costs is not a sufficient allowance for the efficient costs incurred on foreign bond issuances based on the PwC analysis prepared for the QCA.

More importantly, debt issuance costs and cross-currency swap costs are two distinct and unrelated costs. Debt issuance costs refer to the fees incurred in the debt issuance process, such as legal counsel fee, credit rating fee and investment bank charge. On the other hand, cross-currency swap costs are incurred in managing the exchange rate risk associated with foreign debt issue, and is a standard and efficient commercial practice. Therefore, Aurizon Network position remains consistent with that within the UT5 Submission.

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[27] QCA, Aurizon Network 2014 DAU MAR Draft Decision, p. 217.

12. Depreciation

Stakeholders supported the continuation of the current depreciation arrangements. Aurizon Network's position remains consistent with that within the UT5 Submission.

13. Chapter 13 – Reference Tariffs

Stakeholder Issue - WIRP Deed arrangements and Deferrals

The QRC in its response stated

> a) *"deferrals are net present value neutral for Aurizon Network – deferrals are about allocation of costs and risks as between users, not a risk to Aurizon Network; and*
>
> b) *Aurizon Network agreed to develop the WIRP infrastructure on the basis of access conditions in the WIRP Deed which most relevantly include:*
>
> > (1) *an additional return through the WIRP Fee for risks above that borne in relation to the existing network (which are compensated for through the regulated WACC); and*
> >
> > (2) *provision for recovery of the additional capital if the WIRP investment is ever subject to optimisation (such that it is misleading for Aurizon Network to suggest that deferrals represent a risk to recovery of the capital).*
>
> *In other words, Aurizon Network's risks from deferrals have been entirely compensated for by the WIRP Deed arrangements and it is not appropriate that those asserted risks to automatically result in such deferrals coming to an end."*[28]

Aurizon Network's Response

The WIRP Deeds are confidential as between Aurizon Network and the WIRP Customers. However, the QCA considered the WIRP Deeds during its approval of the WIRP Access Conditions, and will be aware that the WIRP Deeds do not fully protect Aurizon Network from deferral risk, or from all forms of optimisation risk, as asserted by the QRC.

Stakeholder Issue - Existing users and Deferrals

Anglo American questions the application of expansion pricing principles and continues to be of the view that existing users should not be required to take any cross default risk of access seekers (i.e. competitors). This cross default risk is realised when expansion project volume does not materialise.

Anglo American also state there is no clearly established basis for the relevant deferred revenue tonnes coming on line to support this.

Aurizon Network's Response

Aurizon Network has applied the same pricing principles as approved by the QCA in its Final Decision on WIRP. If the WIRP expansion didn't exist or existing users were priced independently of WIRP, existing users would pay a higher tariff, compared to the socialised tariff under UT5. Existing users benefit from the positive contribution WIRP railings make through the socialisation of WIRP costs.

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[28] Aurizon Network 2017DAU QRC Submission, volume 2 Pricing Submission, 17 February 2017, page 51

Aurizon Network notes that the QCA will review and approve the final volumes forecasts but can confirm that the Aurizon Network calculations do not include volumes for mines that are not currently railing to WICET.

Stakeholder Issue - Incremental costs for WIRP users

Anglo American suggests that a portion of Common Costs (for various fixed services provided by Aurizon Network for train control and other Aurizon Network operations to be used by the expanding user) should also be included in the new Expansion Tariff.

Aurizon Network's Response

Under the UT5 proposal, charges recovered from a majority of WIRP users are sufficient to meet all their incremental costs and through socialisation, WIRP users make a contribution to the common costs of the Blackwater system, benefiting existing Blackwater users.

14. Other Revenue matters

Stakeholder Issue - Addressing the issue of AT5

AO submission recommended:

> an obligation to complete an assessment on the form of regulation and pricing of the overhead power system and implement appropriate reforms no later than 31 December 2017;

> appropriate positive and negative incentives for narrow gauge locomotives in the Goonyella and Blackwater systems to prevent further decline in the electric utilisation, including a requirement for diesel services which are introduced after the date of the initial undertaking notice:

- to make a contribution to the overhead power system commensurate to the associated costs being transferred to existing operators of electric services; or
- to be subject to a reference train path multiplier which applies to the AT2, AT3 and AT4 tariff components.

Aurizon Network Response

Aurizon Network acknowledges the issues that the Aurizon Operations presents within its submission. Within its UT5 submission, Aurizon Network outlined the cost savings it has achieved that reduced ongoing electric traction costs and alleviate the cost pressures for users of electric traction within the CQCN.

In addition, Aurizon Network has already commenced a broader Stakeholder consultation process, with an aim of developing and submitting a DAAU to address the AT5 issue. Industry engagement on AT5 is critical to the success of any proposed solution, given its broad nature affecting both current and future stakeholders of the CQCN. Including the AT5 issue within UT5, would not allow sufficient time for Stakeholder collaboration to address the issue without impacting on the timely completion of UT5.

Aurizon Network is looking to develop the AT5 DAAU separately to the QCA's consideration of UT5. Aurizon Network will aim to submit the DAAU by 31 July 2017, however would look to submit earlier if a workable outcome with Stakeholders is achieved. Aurizon Network will look to keep the QCA informed of the AT5 DAAU development.

Stakeholder Issue – Take or Pay Pooling

PN and the DCCC raised issues with the current take-or-pay mechanisms.

To address the issue, the DCCC and PN submission did confirm that parties would be prepared to address the matter during the UT5 term, via a Draft Amending Access Undertaking.[29]

Aurizon Network Response

Aurizon Network agrees with the DCCC and PN submission that it should be reserved for a DAAU during the term of UT5.

[29] PN and DCCC Submission on take or pay pooling, 17 February 2017, pg. 5