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16 November 2022

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

Dear Ms Bains

Aurizon Network's electric energy charge DAAU—final decision

The Queensland Competition Authority (QCA) approved Aurizon Network's electric energy charge (EC) draft amending access undertaking (the EC DAAU) on 16 November 2022, having regard to the information Aurizon Network provided, stakeholders' comments the QCA received in response and the relevant provisions in the QCA Act.

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

Should your staff have any specific queries on the attached paper, please direct these in the first instance to Pag Arao-Arao on 3222 0560, or by email pag.arao-arao@qca.org.au.

Yours sincerely



Charles Millstead
Chief Executive Officer

cc: *Dan Kearney, Head of Finance and Regulation*
Jon Windle, Network Regulation Manager

DECISION NOTICE

AURIZON NETWORK'S ELECTRIC ENERGY CHARGE DAAU—FINAL DECISION

16 November 2022

The Queensland Competition Authority approved Aurizon Network's electric energy charge DAAU, under section 142(2) of the *Queensland Competition Authority Act 1997*.

Background

Aurizon Network supplies electricity to electric traction train operators through its overhead distribution network on the Goonyella and Blackwater systems. Aurizon Network procures electricity through a supply agreement with an electricity retailer and recovers the cost of providing this service through the electric energy charge (EC) component of reference tariffs. The 2017 access undertaking (UT5) provides a mechanism for the true-up of any over- or under-recovery of electric traction energy costs.

On 8 June 2022, Aurizon Network proposed to increase the 2022–23 EC tariff components of the Blackwater and Goonyella reference tariffs from \$1.11 to \$2.82 per eGTK'000, through a draft amending access undertaking (the EC DAAU).¹ On 12 August 2022, Aurizon Network provided additional information to support its claim—in response to issues raised by stakeholders and our request for additional information.²

Statutory obligations

Under the *Queensland Competition Authority Act 1997* (QCA Act), Aurizon Network can submit a voluntary DAAU to amend the approved access undertaking (s. 142(1)).

We are required to consider the DAAU and either approve, or refuse to approve, the DAAU (s. 142(2)), having regard to the matters mentioned in s. 138(2) and the conditions set out in the QCA Act, including that the DAAU has been published and submissions have been sought and considered (s. 143).

¹ Aurizon Network, *Draft Amending Access Undertaking—Electric Energy Charge for Financial Year (FY) 2023*, June 2022 (supporting submission).

² Aurizon Network, *Response to Stakeholder Submission—Electric Energy Charge Draft Amending Access Undertaking*, August 2022 (response to stakeholders).

Aurizon Network's proposal

The EC DAAU seeks to increase the 2022–23 EC tariff components to reflect updated forecasts of electric energy costs for 2022–23 that have regard to the current volatility in the electricity market and recent pricing recommendations from Aurizon Network's electricity market expert Edge2020.³

The EC tariff included within the EC DAAU represents the projected costs of procuring electricity from the national electricity market (NEM) for 2022–23, based on the prevailing forward prices in Q2 2022. The adjusted energy cost claimed for 2022–23 is \$175.7 million.

Aurizon Network said the proposed energy costs reflect the competitive market price for the supply of electricity, which comprises consumption and supply charges, a market charge, any fixed services and metering charges set by the retailer, environmental compliance charges, and a variable connection charge set by the Australian Energy Regulator.⁴

Table 1 Proposed EC—energy cost breakdown

	<i>\$ million</i>	<i>\$ per eGTK'000[^]</i>
Consumption and supply	157.9	2.53
Variable connection charge	4.5	0.07
Environmental compliance	13.3	0.21
Total	175.7	2.82

[^] forecast of 62,359,945 eGTK'000 for 2022–23.

Source: Aurizon Network supporting submission, pp. 3–4.

Aurizon Network said amendments are required to recover additional costs and to avoid a significant under-recovery in 2022–23 through the EC tariffs in 2023–24.⁵

While Aurizon Network accepted that this is a material increase in electric energy costs, it considered that the increase reflected the unprecedented and unforeseen movements in spot and contract prices, and ongoing volatility and disruption within the electricity market.⁶ This included lower coal-fired plant availability in the NEM from planned and unplanned outages across various states;⁷ increased periods in which higher-cost generation (gas and hydro) set the spot price in Queensland; and events such as flooding in the Hunter Valley and the Russian invasion of Ukraine.

Aurizon Network said that it has diligently undertaken a procurement process to purchase electricity in the interests of its customers and in line with the broader pricing expectations of other market participants at that time. Aurizon Network said it appears that many market participants did not foresee the material increase in contract prices that would eventuate in 2022.⁸ Aurizon Network said this suggests market participants either

³ Aurizon Network, supporting submission, p. 1.

⁴ Aurizon Network, supporting submission, pp. 3–4.

⁵ Aurizon Network, supporting submission; response to stakeholders.

⁶ Aurizon Network, response to stakeholders, pp. 12–19.

⁷ This includes at the Callide and Gladstone plants in Queensland.

⁸ The material increase in contract prices has resulted in significant financial impacts for tier 3 retailers, who have exited the market and led to tier 1 and tier 2 retailers being directed by the AER to take on impacted customers through retailer of last resort obligations. Other large electricity retailers are also experiencing significant financial costs and losses associated with price increases, including sophisticated market participants such as Energy Australia and Origin Energy.

expected the supply constraints to ease, or they maintained large unhedged positions and responded accordingly once further market disruptions became evident (noting around 73 per cent of trading activity between January and June 2022 occurred after 15 May 2022).⁹ Accordingly, Aurizon Network said that we should only have regard to the information available to Aurizon Network at the time decisions were made, and not speculate on what different decisions might have been made if future events or information had been known at the time.¹⁰

Aurizon Network was concerned that if the EC DAAU is not approved, it would have to assume risks for which it is not compensated and would be forced to supply electricity on terms that are not reasonable and commercial. It would also lead to further cost increases associated with the annual true-up mechanism and could have a negative compounding effect on the recovery of the efficient costs of supplying electricity.¹¹

Stakeholders' response

We provided stakeholders with two opportunities to comment—in response to Aurizon Network's proposal and in response to our draft decision. The Queensland Resources Council (QRC) provided responses at both stages.¹²

The QRC strongly objected to this proposal, noting the large cost increase will have a significant impact on users. Further, it considered that the increase has been driven, at least in part, by Aurizon Network's apparent mismanagement of the procurement process. This includes Aurizon Network failing to:

- establish or fill an 'electrical specialist role' despite being aware of the importance of such a role and being provided with funding to support it
- demonstrate to customers that it followed expert advice
- enter a new retail contract within a reasonable period ahead of 2022–23
- act to manage the risk of further increases while negotiating its retail contract
- inform its customers of its unhedged position or discuss the risks this posed in the context of a volatile electricity market.¹³

Accordingly, the QRC considered that a portion of the proposed increase should not be included in the EC allowance nor be included in the true-up provided for in UT5.¹⁴

We provided Aurizon Network with an opportunity to respond to the QRC's initial submission. Aurizon Network did not respond to the draft decision.

Draft decision

On 21 September 2022, we released our draft decision proposing to approve the EC DAAU, under section 142(2) of the QCA Act. The draft decision was made, among other things, on the basis that we were satisfied that:

- the EC tariff component was constructed so that the costs of electricity are passed to customers—with Aurizon Network filling the role of on-seller of electricity 'at cost'

⁹ Aurizon Network, response to stakeholders, pp. 19–20.

¹⁰ Aurizon Network, response to stakeholders, p. 23.

¹¹ Aurizon Network, response to stakeholders, pp. 21–22.

¹² QRC, sub. 1, 2.

¹³ QRC, sub. 1, pp. 3–6, sub. 2, p. 1.

¹⁴ QRC, sub. 1, p. 6.

- the proposed EC tariff component is reasonable—it reflects the expected cost of electricity, given the forward (market) prices pertaining in the NEM at the time the contract was entered into, and has been calculated correctly
- there is insufficient evidence that Aurizon Network acted imprudently or without regard to its customers' electricity requirements in managing the procurement of electricity for its customers (particularly given the unexpected and unprecedented volatility in the NEM during the relevant period)
- it is in the interests of users to approve the DAAU at this time, rather than wait for a potentially very large true-up at the end of 2022–23.

Our assessment and final decision

We have approved the EC DAAU. We consider the proposed amendments are consistent with the legitimate business interests of Aurizon Network and its customers (s. 138(2)(b), (e)). It also supports the efficient operation and use of Aurizon Network's infrastructure in the Central Queensland coal network (CQCN) (s. 138(2)(a)) and is consistent with the pricing principles of Part 5 of the QCA Act (ss. 138(2)(g), 168A).

In particular, we are satisfied that:

- the EC tariff component was constructed with the intent that the costs of electricity were passed to customers
- the proposed EC tariff component is reasonable
- there is insufficient evidence to demonstrate that Aurizon Network acted imprudently or without regard to its customers' electricity requirements
- it is in the interests of users to approve the DAAU at this time.

The cost treatment of the electricity energy charge for Aurizon Network is not dissimilar to approaches in other jurisdictions. For example, in respect of the Sydney desalination plant (SDP), IPART's 2017 determination¹⁵ provides for losses (or gains) on the sale of surplus energy when the SDP is in shutdown or in restart mode to be passed through to customers (outside of a core band of plus or minus five per cent). Similarly, an adjustment mechanism to carry over gains and losses associated with surplus electricity and Renewable Energy Certificates (RECs) is provided for in the new (2022) terms of reference for IPART's current review of SDP's prices.¹⁶

Status of electricity cost recovery arrangements

Aurizon Network is not obliged to sell electricity to rail operators under UT5. However, when it supplies a related operator with electricity, it cannot refuse to also do so to other access seekers or access holders.¹⁷ Aurizon Network said that by supplying electricity, it allows operators to avoid the administration and compliance burden of the alternative option—which would involve Aurizon Network registering as a distribution network service provider (DNSP) and operators installing metering equipment and purchasing their own electricity.¹⁸

Aurizon Network stressed that it is not an electricity retailer but rather an on-seller of electricity based on the competitive rates prevailing in the NEM. This means that all risk management activities are undertaken by the retailer under the terms of the supply agreement.¹⁹

¹⁵ IPART, Final Report 2017, pp. 68–69.

¹⁶ K Andrews, Terms of Reference SDP for IPART 2022

¹⁷ UT5, cl. 2.6(a).

¹⁸ Aurizon Network, response to stakeholders, p. 3.

¹⁹ Aurizon Network, response to stakeholders, p. 3.

We acknowledge that in past approval processes and via true-up mechanisms the cost of the electricity was passed to customers—with Aurizon Network filling the role of an on-seller of electricity 'at cost'. In this regard, we note that in assessing Aurizon Network's 2017 DAU we maintained that:

In practice this mechanism means that these costs are passed through at cost, with any difference between forecast and actual costs reconciled through an ex post adjustment to the EC component.²⁰

We are satisfied that the proposed change to the EC tariff component has been correctly calculated. We also maintain that the proposed change to the EC tariff component is reasonable.

While the contract price Aurizon Network has agreed to for Q3 2022 is very high (in comparison to previous prices), it properly reflected the forward (market) prices in the NEM at the time the contract was entered into.

We still consider there is insufficient evidence for us to be satisfied that Aurizon Network acted imprudently in undertaking its electricity supply procurement process—there was unexpected and unprecedented volatility in the NEM in 2022, and the timing for finalising and signing the supply agreement was similar to the 2017 process. As the processes followed in 2022 were like those followed in 2017, when it appears that Aurizon Network also did not undertake any separate hedging activity, it is not clear why users would have expected such hedging activity to occur in the lead-up to finalising and signing the new supply agreement.

We consider Aurizon Network has incentives to ensure it procures electricity in an efficient manner:

- As the Aurizon Group is vertically integrated, there may be adverse financial implications for Aurizon Network's related operator if electricity is priced inefficiently.
- Under the procurement process, electricity is procured to meet the demand of both the CQCN and the Aurizon Group's broader Queensland business—so the Aurizon Group is subject to the same price risks as Aurizon Network's customers.
- In recent years, Aurizon Network has undertaken significant investment in the CQCN electric infrastructure—and is therefore incentivised to act to improve the competitiveness of electric traction in the CQCN.²¹

The QRC has indicated in its response submission to the draft decision, however, that it considers these incentives to be weak.²² Our further comments on these matters are as follows:

- The QRC said that the impact of electricity costs on Aurizon Network's related operator is likely to be limited, as these costs are generally a pass-through to customers under haulage agreements. While this may be true in many cases, Aurizon Network has indicated it is conscious that the on-selling of electricity is a fuel cost to above rail operators and it makes no assumptions regarding the extent to which those costs are passed on to end users associated with the use of electric traction or form part of the rail operators' cost base. Further, Aurizon Network pointed to a number of initiatives and actions it has pursued in recent years to lower electricity costs on behalf of customers, which it said shows the strength of the incentives.
- The QRC also said that the electricity demand of the Aurizon Group's broader Queensland business is small compared to that of the CQCN, meaning the impact on those operations is limited. While we accept that the electricity demand of Aurizon's broader Queensland business may be relatively small in comparison to the entire CQCN, to the extent that the procurement of electricity for both occurs as part of a single exercise, we still consider that the incentive for Aurizon to conduct the exercise prudently remains a valid consideration.

²⁰ QCA, *Aurizon Network's 2017 draft access undertaking*, draft decision, December 2017, p. 247; QCA, *Aurizon Network's 2017 draft access undertaking*, decision, December 2018, p. 184.

²¹ Aurizon Network, response to stakeholders, pp. 3–4.

²² QRC, sub. 2, p. 2.

- The QRC said that Aurizon Network's incentive to maintain the competitiveness of electric traction in the CQCN has been significantly reduced by the electric traction DAAU that was approved by the QCA in 2019.²³ We accept that the approval of the electric traction DAAU has provided Aurizon Network with an additional level of protection against potential asset stranding risk for its electric infrastructure, but we note that this DAAU was predicated on a 'socialisation of costs as a last resort' approach, with an expectation that Aurizon Network and operators would likely explore alternative measures prior to socialisation being triggered. Thus, we consider there are still reasonable incentives for Aurizon Network to continue to seek to maintain the competitiveness of its electric infrastructure.

Aurizon Network has indicated that, with regard to its electricity supply procurement, all risk management activities are undertaken by the retailer under the terms of the supply agreement. It said that it has no direct exposure to the wholesale cost of electricity.²⁴ We consider this is not surprising for an entity for which participation in wholesale energy markets is not a core or specialist part of its business (as would be the case with, for example, an electricity retailer).

Given the existing UT5 arrangements, it appears that Aurizon Network is neither exposed to, nor compensated for, pricing risk associated with electricity supply to its customers. In particular, the true-up provisions that apply act as a pass-through, allocating the risk of cost variations to access holders. In addition, Aurizon Network's rate of return (agreed with users, proposed, and approved as part of the UT5 DAAU process) was based on industry's own assessment of the commercial and regulatory risks under the proposed UT5 DAAU arrangements, as well as the benefits and costs that these provisions are expected to provide.

In both our draft and final decisions on Aurizon Network's 2017 DAU, we noted that moving to progressive purchasing will expose Aurizon Network's customers to significant short-term price risk²⁵, which must be managed effectively—but were mindful that Aurizon Network had consulted with its users who endorsed the proposed approach at that time.²⁶

Aurizon Network's expert consultant (Edge2020) appears to have been central to the procurement processes related to the new supply agreement. In its initial submission, the QRC acknowledged that the electricity market is complex, as is the task of managing risk within the market. It said that it is for this reason that customers encouraged Aurizon Network to engage Edge2020 as an expert adviser on electricity procurement in 2016.²⁷

Aurizon Network's procurement process

While the QRC accepted that Aurizon Network is allowed to recover the efficient costs of supply, it was concerned that the proposed increase in costs were the result of Aurizon Network's apparent mismanagement of the procurement process:

Customers do not understand how, under a prudent implementation of the approved progressive procurement approach, Aurizon Network could have been in a position of being totally uncontracted and unhedged shortly before the commencement of FY23. We consider this outcome to be imprudent, having regard to the circumstances.²⁸

²³ QRC, sub. 2, p. 2-3.

²⁴ Aurizon Network, response to stakeholders, pp. 3, 5.

²⁵ In contrast, procuring energy through a traditional fixed-price retail contract typically provides reasonable price stability, insulating customers from potentially significant short-term price volatility in the wholesale electricity market.

²⁶ QCA, *Aurizon Network's 2017 draft access undertaking*, draft decision, December 2017, pp. 248–249; QCA, *Aurizon Network's 2017 draft access undertaking*, decision, December 2018, p. 186.

²⁷ QRC, sub. 1, p. 4.

²⁸ QRC, sub. 1, p. 3.

Having reviewed Aurizon Network's management of this activity, we consider that while there are some opportunities for Aurizon Network to improve its processes in the future, there is no clear evidence that Aurizon Network acted imprudently in undertaking the procurement process.

Progressive procurement process

Aurizon Network said it had adopted a progressive procurement strategy—that is, purchasing quarterly energy blocks based on forecast load²⁹—thereby providing it with an opportunity to monitor electricity price movements and opportunistically lock in the prices for its electricity requirement in smaller blocks.³⁰ Progressive procurement, according to Aurizon Network, provides the lowest cost, as the frequency in actively managing it increases the pricing decision points (because it is purchasing electricity in shorter-term 'blocks'). This means that while the prices regularly adjust as market prices move, the impact of any short-term volatility does not persist over the term of the contract.³¹ Aurizon Network said that over the previous four years, its energy procurement has been close to the average forward price of the energy market.³² Our analysis of data from previous years showed that, present circumstances exempted, the progressive procurement process had produced relatively stable energy costs.

We note that Aurizon Network has sought to implement the previously approved procurement approach.³³ In the draft decision, we noted that we had previously flagged that the move to a progressive purchasing approach could expose Aurizon Network's customers to significant short-term pricing risk that needs to be managed effectively. In its response to the draft decision, the QRC acknowledged that such short-term pricing risk 'must be managed effectively'³⁴ (the QRC's emphasis). In pointing out the importance of effective management of the risk in our earlier decisions, we were highlighting the need for all parties to be involved in such risk management planning and activities (i.e. Aurizon Network and also its customers). In this regard, we again encourage Aurizon Network and its customers to engage in early and fulsome consultation about the best way to jointly manage these risks in future, in the interests of all parties.

Hedging position

Aurizon Network said that as it procures electricity through an electricity retailer, it has no direct commodity exposure to the wholesale cost of electricity.³⁵

Aurizon Network accepted that the observed purchasing outcomes are less favourable than those that might have been obtained, with the benefit of hindsight, if hedging had occurred before the extreme price increases were observed. However, it noted that a decision for it to hedge in an already uncertain and volatile environment (where prices were equally likely to have decreased) would also expose its customers to possible hedging losses.³⁶

Additionally, Aurizon Network said that using financial derivatives would require a detailed engagement with customers and their endorsements to assume those risks. Aurizon Network sees this customer endorsement as better occurring via a more detailed consultation process on the procurement strategy.³⁷

We consider that if Aurizon Network unilaterally hedged its position, without prior consultation and agreement of its customers, it would have undermined the agreed undertaking process.

²⁹ Aurizon Network, response to stakeholders, p. 32.

³⁰ Aurizon Network, response to stakeholders, p. 6.

³¹ Aurizon Network, response to stakeholders, p. 7.

³² Aurizon Network, response to stakeholders, p. 32.

³³ QCA, *Aurizon Network's 2017 draft access undertaking*, draft decision, December 2017, pp. 248–249; QCA, *Aurizon Network's 2017 draft access undertaking*, decision, December 2018, p. 186.

³⁴ QRC, sub. 2, p. 2.

³⁵ Aurizon Network, response to stakeholders, p. 5.

³⁶ Aurizon Network, response to stakeholders, p. 11.

³⁷ Aurizon Network, response to stakeholders, p. 5.

We note the QRC said the draft decision 'discusses and dismisses an extreme version'³⁸ of a hedging option—namely, that Aurizon Network could have unilaterally hedged its position, without prior consultation and agreement of its customers. We maintain the draft decision position, but we accept there were other options that could have potentially been available to Aurizon Network, including consulting more fulsomely with customers with a view to seeking to agree on a more proactive strategy. That said, the timeline of activities described by Aurizon Network in its response submission to users indicates that the underlying market environment and level of volatility was evolving rapidly—suggesting that reaching any agreement with users on a detailed proposed hedging strategy in a timely manner may not have been easy to do.

It is not clear whether it would be prudent and efficient for Aurizon Network, an entity that is not normally actively engaged in wholesale energy markets, to undertake large-scale proactive hedging activities. Aurizon Network is not an energy trading company and is unlikely to be equipped, or financed, to take on such functions. In any event, Aurizon Network's customers are sophisticated entities that have substantial knowledge of energy markets and certainly of movements in thermal coal prices and may be able to undertake risk minimisation activities themselves. Moreover, users' exposure to thermal coal prices may operate as a natural 'hedge' in circumstances where movements in coal prices are a major driver of wholesale electricity costs.

That said, we consider there is scope for greater consultation between Aurizon Network and stakeholders to proactively investigate opportunities to improve processes in electricity procurement (see Consultation section below).

Renewable energy requirement

Aurizon Network said that its consultation with customers indicated that the customers were supportive of the proposal to source a greater proportion of electric energy from renewable sources. Aurizon Network added that this would have the benefit of reducing customers' scope 3 emissions (emissions in their supply chains).³⁹

Aurizon Network suggested that the change in approach towards renewable energy required a new supply agreement to be negotiated.⁴⁰ However, the QRC pointed out that given the existing supply agreement was expiring anyway, the need for a new one was known, and was not caused by any change in approach towards renewable energy.⁴¹

Our assessment of Aurizon Network's procurement process indicates that the increased renewable energy requirement may have caused some minor delays in negotiating and finalising the new Electricity Supply Agreement (ESA). However, it was not the major reason why the supply agreement was not agreed to earlier. We also note that the renewable energy component in the new supply agreement represents 25 per cent of Aurizon Network's electricity purchasing. As a consequence, we have not placed significant weight on the renewable energy requirement in our analysis of Aurizon Network's procurement process.

Timing of contract

The QRC was concerned that Aurizon Network had failed to enter a new retail contract within a reasonable period ahead of 2022–23, because Aurizon Network either commenced the process too late or failed to put adequate resources into concluding the negotiations.⁴²

Aurizon Network said that it had taken undertaken a complex, multi-supplier and multi-product market process for its new electricity supplier that included:

³⁸ QRC, sub. 2, p. 3.

³⁹ Aurizon Network, supporting submission, p. 1.

⁴⁰ Aurizon Network, supporting submission, p. 1.

⁴¹ QRC, sub. 1, p. 4.

⁴² QRC, sub. 1, pp. 4, 6–7.

- a competitive tender process—whereby Aurizon Network undertook market sounding (including engaging with suppliers on a renewable energy source option), requested and evaluated proposals (with cost, product structure and flexibility given majority weighting as part of the process), and negotiated and awarded the contract⁴³
- staff engagement—where Aurizon Network staff were heavily involved in the procurement process and ongoing management of the relationship with expert consultants^{44,45}
- ongoing customer consultation—where Aurizon Network provided updates on progress, although this was largely focused on options to incorporate renewable energy into the portfolio (see above).⁴⁶

Based on the information provided, Aurizon Network commenced the process earlier than its previous process. However, Aurizon Network said it still took more time than first anticipated to renew its supply agreement. It said that the additional time was required to investigate alternative energy procurement options and to negotiate terms and conditions that promote the longer-term interests of its customers over the full duration of the new supply agreement.⁴⁷

While several factors appear to have had a significant impact on the timing for the renewal of the supply agreement (as compared to the previous process), we consider these reflect the complexity of the task being undertaken in a period of business disruptions and restrictions, volatile market conditions, and material differences in contract terms that had to be negotiated. In addition, in setting an operating cost allowance, we set an overall allowance in order to provide the business with the incentive to manage its affairs within this amount. In the draft decision, we specifically noted that we do not prescribe how Aurizon Network manages its own business.

In response to the draft decision, the QRC said that while it understands the regulatory arrangements allow Aurizon Network to seek and obtain operating cost allowances, then keep the savings if costs can be lowered or avoided,⁴⁸ Aurizon Network's decisions to do so should not be without consequence. It added that, in cases where Aurizon Network's decisions to cut operating costs result in inefficient outcomes, then Aurizon Network's recovery of resulting costs should be limited to efficient costs. This view does not take account of the forward-looking nature of the regulatory framework, whereby operating cost allowances are set in advance based on forecasts, not actual costs. We reiterate our view that it is not the role of the QCA to specify how Aurizon Network should operate its business on a day-to-day basis. That is not to say that individual elements of operating cost allowances should not be revisited at the time that regulatory resets are undertaken.

Use of external advice

Aurizon Network said it engaged and relied on external expert advice, provided by Edge2020, in undertaking the procurement process, selecting the successful tenderer, and negotiating and agreeing the terms and conditions of supply. This included price terms, where it relied on the expert advice of the consultants. Edge2020 has been advising Aurizon Network since 2017, following the suggestion by industry.⁴⁹

Our examination of Aurizon Network's submission and supporting documentation showed that Edge2020's updates and Aurizon Network's processes were broadly aligned. The main cause of protracted delays occurred as Aurizon Network attempted to negotiate more favourable pricing arrangements, following Edge2020's advice, up

⁴³ Aurizon Network, response to stakeholders, pp. 8–10.

⁴⁴ While Aurizon Network intended to recruit an in-house energy procurement specialist, this proved to be unsuccessful, and the role was ultimately filled with a general procurement specialist.

⁴⁵ Aurizon Network, response to stakeholders, p. 7.

⁴⁶ Aurizon Network, response to stakeholders, pp. 10–11.

⁴⁷ Aurizon Network, response to stakeholders, pp. 2, 8.

⁴⁸ QRC, sub. 2, p. 3.

⁴⁹ Aurizon Network, response to stakeholders, p. 5.

until February 2022.⁵⁰ In response to the QRC's comment regarding Edge2020's advice on recommendations on when to 'lock in' the price of 'blocks' of future demand, our examination has also not evidenced any misalignment between the advice and Aurizon Network's processes.

Consultation with stakeholders

We also reviewed the nature and effectiveness of communication between Aurizon Network and its stakeholders. While there were some opportunities to improve communication, which may have resulted in better outcomes, we do not consider the issues identified are sufficient in themselves for us to reject Aurizon Network's proposal.

Aurizon Network appears to have provided updates and consulted with customers, formally and informally, throughout the process of the new supply agreement. However, it is clear that the focus of this consultation was on incorporating renewable energy into the portfolio (and not on broader considerations) and that the nature of consultation was limited, given perceived confidentiality constraints.

We consider there is scope for process improvements that provide for better stakeholder engagement and awareness that may have delivered more customer-centric outcomes, in view of the increasing volatility being observed in the energy market. This includes:

- the timing and frequency of future interactions. Given the time Aurizon Network spent investigating its energy purchasing strategy, there appears to be some opportunity for it to better keep stakeholders abreast of developments at each key stage in the process (subject to confidentiality restrictions and requirements). Providing for detailed consultation only after best and final offers have been received does not appear to maximise the opportunities for engagement with customers
- the scope of engagement. There appears to be some scope for providing more opportunity for users to understand the various options, and associated risks, that were available in the market. While we do not question the expertise of Edge2020, ultimately these purchases are paid for by users, and as such, users should have the opportunity to provide input into these decisions (subject to confidentiality restrictions and requirements)
- the focus of information provided. It appears that engagement focused on options for renewable energy purchases and the potential additional costs of each option. We consider the consultation process would have been more effective if a similar amount of information was provided for the entire energy purchase portfolio. While Aurizon Network stated that there were issues of confidentiality around purchases, it demonstrated its capability to provide useful indicative figures for renewable purchases without violating confidentiality.

While this suggests there is clearly some scope for improving its consultative efforts, we consider that Aurizon Network and its stakeholders are best placed to identify those areas which are a priority, including whether there are possible benefits from formalising arrangements within UT5.⁵¹ In that event, we would expect Aurizon Network to work collectively with affected users, should they request this, to develop an agreed approach to address their concerns.

Future consultation on procurement

Having considered stakeholder views we received in response to our draft decision, we have decided to approve Aurizon Network's EC DAAU.

⁵⁰ Aurizon Network, response to stakeholders, p. 10.

⁵¹ UT5 sets out a new process for engagement regarding the development of Aurizon Network's maintenance and renewals strategies and budgets (cl. 7A.11.3). It appears that these arrangements have resulted in significant and positive changes to the way in which these allowances have been set and managed—providing for greater customer involvement and improving the information provided.

However, this process has highlighted that stakeholders have serious concerns about how Aurizon Network manages electricity procurement and pricing—in particular, that Aurizon Network has not adequately consulted with its customers, nor taken their interests sufficiently into account, to their material detriment.

While Aurizon Network has not proposed any procedural changes to its electricity procurement processes as part of this DAAU, it has committed to:

- procure electricity diligently under the terms of its supply agreement, having regard to the advice of Edge2020, with the objective of obtaining favourable outcomes for customers
- engage with customers to provide further information on electricity price expectations for the remainder of the year⁵²
- submit a further DAAU for our approval to ensure that any realised cost reductions within 2022–23, including favourable downward movements in the spot market, are passed on to customers in a timely way.⁵³

Beyond these initiatives, it is our view that industry-led solutions and processes can lead to a more customer-centred approach to resolve outstanding matters. This is particularly relevant, as Aurizon Network and users developed UT5 with the view to achieving solutions that will deliver mutual benefits for all stakeholders.

On that basis, we encourage Aurizon Network to strengthen its efforts to pursue opportunities to proactively engage with users on this matter and improve both the quality and quantity of information provided.

We also note that, in its response to the draft decision, the QRC welcomed the QCA's comments regarding the need to improve customer consultation and input.⁵⁴ More specifically, the QRC said it will consider various options for improving customers' input into electricity procurement processes, including:

- improved consultation and input, which will require Aurizon Network to make genuine efforts to address confidentiality constraints
- requiring that key decisions (including the decision to lock in blocks of demand under the retail contract) proceed only with customer approval
- Aurizon Network facilitating the option for individual customers to procure their own electricity
- a full transfer of the management of this function to an independent party.

While the QCA has not considered in detail the pros and cons of these specific suggestions, we strongly encourage the QRC (and its members) and Aurizon Network to engage with each other on these matters and other potential measures that may lead to improved electricity procurement processes, and greater transparency regarding the conduct of these processes, in the future.

⁵² This includes Aurizon Network looking to provide relevant information to customers on the percentage of block/spot mix in comparison with the EC tariff in UT5 (if able to do so).

⁵³ Aurizon Network, supporting submission, p. 3; Aurizon Network, response to stakeholders, pp. 12–19.

⁵⁴ QRC, sub. 2, pp. 4–5.

Submissions

Aurizon Network, *Draft Amending Access Undertaking—Electric Energy Charge for Financial Year (FY) 2023*, June 2022 (supporting submission).

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Queensland Resources Council (QRC), *Aurizon Network Draft Amending Access Undertaking—Electric Energy Charge FY23*, July 2022 (sub. 1).

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