Queensland Competition Authority

Draft decision

April 2023 GAPE and Newlands pricing DAAU

August 2023

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SUBMISSIONS

Closing date for submissions: 29 September 2023

This document represents the Queensland Competition Authority's preliminary views and is subject to revision. Public involvement is an important element of the decision-making processes of the QCA. Therefore, submissions are invited from interested parties concerning its assessment of the April 2023 GAPE and Newlands pricing DAAU. The QCA will take account of all submissions received within the stated timeframes.

Submissions, comments or inquiries regarding this paper should be directed to:

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Tel (07) 3222 0555
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Confidentiality

In the interests of transparency and to promote informed discussion and consultation, the QCA intends to make all submissions publicly available. However, if a person making a submission believes that information in the submission is confidential, that person should claim confidentiality in respect of the document (or the relevant part of the document) at the time the submission is given to the QCA and state the basis for the confidentiality claim.

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Claims for confidentiality should be clearly noted on the front page of the submission. The relevant sections of the submission should also be marked as confidential, so that the remainder of the document can be made publicly available. It would also be appreciated if two versions of the submission (i.e. a complete version and another excising confidential information) could be provided.

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DRAFT DECISION

On 6 April 2023, Aurizon Network submitted its April 2023 GAPE and Newlands pricing draft amending access undertaking (April 2023 DAAU). The April 2023 DAAU proposed a range of amendments to the 2017 access undertaking (UT5) in seeking to address ongoing issues arising from the Goonyella to Abbot Point expansion (GAPE) project and change the application of private incremental costs (PIC) discounts.

Our draft decision is to refuse to approve the April 2023 DAAU, having regard to the statutory criteria and stakeholder submissions we received.

We consider that Aurizon Network's proposal provides a foundation for resolving issues that have impacted parties over an extended period. We see merit in key aspects of Aurizon Network's proposal, including:

- the causation-based approach to allocating asset replacement and renewals expenditure in the shared rail corridor[1] between the Newlands and GAPE systems
- Aurizon Network recovering revenue associated with the deferred Newlands system infrastructure enhancement (NSIE) capital through the inclusion of an amount equal to the value of $81.4 million (at 1 July 2023) in the Newlands pricing regulatory asset base (RAB). We consider that this reflects the value of the NSIE, had it been included in the Newlands pricing RAB at the earliest reasonable opportunity
- the principle of narrowing the application PIC discounts to achieve the intended objective of recognising PIC amounts when determining access charges.

However, we consider that the April 2023 DAAU as proposed does not promote efficient use of the central Queensland coal network (CQCN), nor does it appropriately balance the interests of Aurizon Network, access seekers and access holders.

The April 2023 DAAU provides for the continued deferment of NSIE capital equal to the value of $26.7 million (at 1 July 2023), without justification, where existing commercial arrangements may dampen incentives that exist under the regulatory framework for Aurizon Network to recover deferred revenue at the earliest possible opportunity.

Further, amendments are proposed that could impact an access holder's ability to rail up to contract volumes in the current environment, where an existing capacity deficit (ECD) has been identified on the combined GAPE and Newlands system.

Finally, as proposed, we consider that narrowing the application of PIC discounts[2] will result in retrospective changes to discounts for previously approved PIC amounts,[3] in the absence of a change in circumstances. Such retrospective changes increase uncertainty for future access seekers as to the level of access charges that will be applied, where investment in private infrastructure to connect to the CQCN is required.

Our assessment of the April 2023 DAAU, including the way in which we consider the DAAU should be amended, is set out in detail throughout this draft decision.

[1] Between Newlands Junction and the Port of Abbot Point.
[2] By amending the definition of private infrastructure.
[3] Including the discount applied for Bravus.

Next steps

This draft decision is intended to give stakeholders an insight into our views on the April 2023 DAAU before we finalise our position.[4]

We invite written submissions by 29 September 2023. All submissions made by this date will be taken into consideration.

The way we apply the statutory assessment criteria, and our thinking, may change, in response to stakeholder submissions.

[4] This paper is not a draft version of a final decision, and it has no force of itself. There should be no expectation that these views and recommendations will prevail to the end of the decision-making process.

1 BACKGROUND

On 6 April 2023, Aurizon Network submitted its April 2023 DAAU under s. 142 of the *Queensland Competition Authority Act 1997* (QCA Act).

The April 2023 DAAU deals with a range of matters, including:

- ongoing issues arising from the GAPE project (Box 1)—in particular:
  - the allocation of asset replacement and renewals expenditure on the shared rail corridor—to date, asset replacement and renewal expenditure in the shared rail corridor has been predominantly recovered from Newlands users through the reference tariff,[5] despite GAPE users also railing through the corridor
  - the treatment of NSIE capital, which has remained deferred under the regulatory framework
- pricing arrangements to determine reference tariffs in the Newlands system and the transfer of access rights between the GAPE and Newlands systems
- the application of PIC discounts in determining access charges.

The circumstances under which the April 2023 DAAU was submitted are relevant when considering the proposed amendments. These circumstances include the:

- existence of commercial arrangements for capacity created by the GAPE project
- identification of an ECD on the combined Newlands and GAPE system[6]
- commencement of a new user on the Newlands system, whose PIC application was approved by us in December 2022.[7]

The April 2023 DAAU was also developed and submitted after regulatory processes were completed previously that dealt with allocation issues arising from the GAPE project.[8]

Aurizon Network stated it had prepared the April 2023 DAAU having regard to amendments that it considered best satisfied the statutory criteria. The proposed amendments are set out in detail in our assessment (chapter 2).

[5] Expenditure is allocated to the relevant coal system in which the asset financially resides.
[6] Related information is available on the QCA website at *Capacity assessment*.
[7] QCA, *Private incremental cost Carmichael rail loop and connecting infrastructure*, decision notice, December 2022.
[8] We initially published a guidance paper in September 2021, which encouraged Aurizon Network and affected stakeholders to work collaboratively to develop an agreed solution to the concerns being raised. Following this, Aurizon Network submitted its initial GAPE and Newlands pricing DAAU in September 2022, which was a package of amendments it considered most capable of acceptance by stakeholders. This DAAU was withdrawn following the publication of our preliminary considerations which set out our view that it is not appropriate to make amendments to UT5 that intend to resolve outcomes arising under previously accepted commercial arrangements, in the absence of consensus.

The proposed amendments have consequential impacts on the allowable revenues and reference tariffs applicable to the Newlands and GAPE systems.[9] Aurizon Network proposed that these amendments apply from 1 July 2023, with no retrospectivity.[10]

Box 1: History of the GAPE project

The GAPE project connected the Newlands and Goonyella systems through the construction of the Northern Missing Link (NML). Infrastructure enhancements were also required to the existing Newlands and Goonyella systems.

Following completion of the GAPE project, the rail corridor between the Newlands Junction and the Port of Abbot Point has been utilised by:

- Newlands users, including:
  - legacy Newlands users, whose mines were operational or committed prior to negotiation of the GAPE project and connected directly to the existing Newlands system
  - Newlands to Abbot Point expansion (NAPE) users, who sought access as part of the GAPE project and connected directly to the existing Newlands system
  - post-GAPE Newlands users, who sought access following completion of the GAPE project and connected to the existing Newlands system through the unregulated Carmichael Rail Network
- GAPE users, who sought access as part of the GAPE project and connected to the existing Newlands system through the NML.

The capacity created by the GAPE project is subject to commercial arrangements[11] that were negotiated by Aurizon Network, GAPE and NAPE users outside of the regulatory framework. These arrangements provided the commercial underwriting and commitments necessary to facilitate investment in the GAPE project.

A new coal system—the GAPE system—was established under the regulatory framework for pricing and revenue cap purposes in 2013. The associated reference tariff recovers expansion costs related to the NML and Goonyella infrastructure enhancements from GAPE users, along with an allocation of NSIE expenditure based on the relative proportion of total contracted paths across GAPE and NAPE users.[12]

Stakeholder views

Aurizon Network stated that consensus agreement was unattainable on the matters dealt with in the April 2023 DAAU.[13]

[9] The April 2023 DAAU also includes amendments to Blackwater, Goonyella and Moura tariffs and allowable revenues. However, these amendments reflect the QCA's decision on Aurizon Network's reset Schedule F preliminary values. See QCA, *Aurizon Network's reset Schedule F preliminary values*, decision, May 2023. Amendments to the QCA levy and IE fee across all systems are the result of Aurizon Network's proposed contract-volume-based pricing in the Newlands system, which is discussed in section 2.3.

[10] Aurizon Network, sub. 1, p. 7.

[11] The Newlands to Abbot Point expansion deeds (NAPE deeds) and the Goonyella to Abbot Point expansion deeds (GAPE deeds).

[12] The remaining allocation of NSIE expenditure has been deferred.

[13] Aurizon Network, sub. 1, pp. 3–4.

We published the April 2023 DAAU for comment and received 4 stakeholder submissions, from Bravus, Glencore, QCoal and Rio Tinto.

We also received an additional submission from Aurizon Network, which responded to stakeholder submissions.

There was some support for Aurizon Network's April 2023 DAAU—Rio Tinto supported the DAAU as a package, while all stakeholders[14] supported Aurizon Network's proposed approach to dealing with the ongoing issue of allocating asset replacement and renewals expenditure on the shared rail corridor.

However, there were a range of concerns with other aspects of the April 2023 DAAU. Stakeholders emphasised the need for our involvement in resolving matters within the April 2023 DAAU[15] that have impacted parties for an extended period of time.[16]

[14] Meaning those stakeholders who provided written submissions.
[15] See, for example, Glencore, sub. 3, p. 1; QCoal, sub. 4, p. 2; Rio Tinto, sub. 5, p. 1.
[16] Rio Tinto, sub. 5, p. 1.

2 ASSESSMENT OF THE DAAU

We are required to consider the April 2023 DAAU and either approve or refuse to approve it[17]—having regard to the matters in s. 138(2) and other conditions in the QCA Act, including that the DAAU has been published and submissions have been sought and considered.[18]

If we refuse to approve the DAAU, we must provide our reasons and views on the amendments we require, in order for it to be appropriate for us to approve the DAAU.[19]

Our draft decision is to refuse to approve the April 2023 DAAU. Our assessment is set out below.

2.1 Allocation of asset replacement and renewal expenditure on the shared rail corridor

Aurizon Network proposed a causation-based approach to allocating future asset replacement and renewal expenditure in the shared rail corridor. This approach identifies expenditure that is variable with use and allocates it between the Newlands and GAPE systems according to relative use of the shared rail corridor.[20]

Our assessment

We consider that Aurizon Network's proposed approach to allocating future asset replacement and renewals expenditure is appropriate.

The causation-based approach recognises that utilisation contributes to the physical degradation of assets and the need for assets to be replaced/renewed. Accordingly, we consider that a causation-based approach will produce reference tariffs that reflect the incremental costs of providing access to the shared rail corridor,[21] thereby providing cost-reflective price signals and promoting economically efficient outcomes.

Stakeholders supported Aurizon Network's approach.[22]

To identify expenditure that is variable with use, Aurizon Network assigned variable allocators to each of its asset categories.[23, 24] These allocators signify how much utilisation contributes to the degradation of the asset.

[17] QCA Act, s. 142(2).
[18] QCA Act, s. 143.
[19] QCA Act, s. 142(3).
[20] The step-by-step process proposed by Aurizon Network is set out in its submission (Aurizon Network, sub. 1, p. 8). Further detail is also provided in Aurizon Network's initial GAPE and Newlands pricing DAAU (Aurizon Network, *GAPE and Newlands pricing draft amending access undertaking*, September 2022, pp. 30–33).
[21] This is consistent with the pricing principles in UT5. Clause 6.6.2 of UT5 states that access charges should be set at no less than the level that will recover the expected incremental cost of providing access to the user and no more than the level that will recover the expected standalone cost of providing access to the user.
[22] Bravus, sub. 2, p. 15; Glencore, sub. 3, p. 1; QCoal, sub. 4, p. 4.
[23] See Aurizon Network, sub. 1, appendix A. Aurizon Network clarified it would apply higher-level asset category allocators to determine the capital indicator, given the exact composition of assets and expenditure is unknown at this stage. We consider that this approach is reasonable where the detailed asset category allocators (outlined in appendix A of Aurizon Network's submission) are to be applied in Aurizon Network's ex post capital expenditure claim, which is submitted to us for approval.
[24] Costs that are not identified as being variable with use will be allocated to the coal system in which the replaced asset currently resides.

We consider that Aurizon Network's approach for determining the variable allocators is pragmatic and the allocators themselves are reasonable, on the basis that they reflect:

- consideration of allocators applied in other jurisdictions—Aurizon Network's variable allocators are based on an assessment of incremental costs for the Hunter Valley Coal Network (HVCN), conducted by WIK Consulting for the Australian Competition and Consumer Commission (ACCC). This assessment reflects an independent expert's view on a rail network with features similar to the CQCN
- Aurizon Network's own engineering judgement—where WIK Consulting's assessment did not provide a comparator or Aurizon Network's engineers formed views that differ from WIK Consulting's assessment, Aurizon Network justified the allocators to be applied, including through the identification of differences between the two rail networks and the assessment task at hand.

We will continue to publish the annually approved RAB roll-forward on our website and do not consider that amendments requiring further transparency are necessary at this time, as suggested by Glencore.[25] Rather, we remain of the view that our continued role in approving the annual RAB roll-forward should provide confidence that the RAB will be appropriately maintained.[26] Aurizon Network's supporting submission to the April 2023 DAAU clearly sets out the approach to be adopted for allocating future asset replacement and renewals expenditure, which, as discussed above, we consider is appropriate to approve.[27] We have checked the application of this approach as part of our assessment.

We consider it is appropriate that amendments to UT5 reflect the application of forecast gross tonne kilometres (gtks) as a reasonable metric for assessing usage of the shared rail corridor.[28]

2.2 Treatment of deferred Newlands system infrastructure enhancements

Aurizon Network proposed to recover revenue associated with the deferred Newlands system infrastructure enhancement (NSIE) capital through the Newlands reference tariff. It proposed to do this by including an amount equal to the value of $81.4 million (at 1 July 2023) for the deferred NSIE capital into the Newlands pricing RAB using a staged approach:[29]

- including an initial amount of $46.2 million from 1 July 2023
- including a subsequent amount of $32.7 million from 1 July 2024.

Based on its view that the full value of the deferred NSIE capital is $156 million (at 1 July 2023), Aurizon Network also proposed to deal with the residual value of the deferred NSIE capital by:

- continuing to defer $26.7 million (at 1 July 2023) of the deferred NSIE capital

[25] Glencore, sub. 3, pp. 3–4.
[26] QCA, *GAPE and Newlands pricing DAAU*, preliminary considerations, December 2022, p. 12.
[27] We note that the proposed amendments to Schedule F, clause 1.3(c) currently state that the methodology to be applied is that set out in the April 2023 GAPE Newlands Pricing DAAU. However, we consider that the amendments should clarify that it is the methodology set out in Aurizon Network's *supporting submission* to the April 2023 GAPE Newlands Pricing DAAU, given the DAAU itself does not set out a methodology.
[28] This is consistent with the intent of Aurizon Network's proposal. Glencore found that the current drafting of Schedule F, 4.1(b)(vii)(G) does not align with the intended approach (Glencore, sub. 3, p. 4). We consider that even where contract-volume-based pricing is applied in the Newlands system, using forecast gtks is appropriate for the purpose of allocating future asset replacement and renewal expenditure. This will ensure a consistent metric is applied across the GAPE and Newlands systems when assessing relative use of the shared rail corridor.
[29] Aurizon Network, sub. 1, pp. 10–14.

- voluntarily excluding $47.9 million (at 1 July 2023) of the deferred NSIE capital from its RAB models.[30]

Our assessment

We are minded to accept the inclusion of an amount up to the value of $81.4 million (at 1 July 2023) for the deferred NSIE capital in the Newlands pricing RAB.

We see merit in Aurizon Network's proposed approach to socialise the deferred NSIE capital across the Newlands system, in that it accounts for the benefits received by all Newlands users and reflects the level of service provided to users. We understand that all Newlands users utilise and benefit from the NSIE,[31] such that there is no differentiation in the service offering or level of service between GAPE, NAPE and Newlands users[32]. The NSIE increased the:

- capacity of the Newlands system by increasing the number of train paths
- capability of train services by increasing tonne axle load (TAL) from 20 to 26.5 TAL and lengthening existing passing loops.[33]

On balance, we consider that Aurizon Network's proposal to include an amount equal to the value of $81.4 million (at 1 July 2023) for the deferred NSIE capital in the Newlands pricing RAB is reasonable. We have verified that this amount is consistent with the value of the deferred NSIE capital, had it been included in the Newlands pricing RAB from the commencement of UT5.[34]

In forming this view, we consider it relevant to have regard to the way in which commercial arrangements may affect the risks and incentives encountered by parties under the regulatory framework. Not doing so could lead us to make regulatory decisions that would not be appropriate, having regard to the statutory criteria. This is especially relevant where there may be adverse implications for access seekers and access holders who were not party to those arrangements.

In this instance, we consider that existing commercial arrangements may dampen the incentives under the regulatory framework for Aurizon Network to recover deferred revenue at the earliest possible opportunity.[35]

We consider Aurizon Network is incentivised under the regulatory framework (and in the absence of commercial arrangements) to recover deferred revenue at the earliest possible opportunity. The deferment of capital is used to address initial periods of uncertainty around volumes in a way that allows Aurizon Network to recover the full costs of an expansion. Aurizon Network does not incur windfall gains or losses from a delay to the recovery of deferred revenue.[36] Rather, any

[30] This amount will be removed from Aurizon Network's roll-forward models and will not be included in the Newlands pricing RAB, which is used to set access charges.

[31] Benefits have previously been identified as part of our annual review of reference tariffs, particularly in relation to the avoidance of longer-term costs to maintain the less productive 20 TAL assets. See QCA, *Annual review of reference tariffs 2021–22*, decision notice, 22 June 2021, p. 6.

[32] In this case, legacy and post-GAPE Newlands users.

[33] Aurizon Network, *GAPE and Newlands Pricing Draft Amending Access Undertaking*, 2 September 2022, p. 7.

[34] In other words, the $81.4 million amount corresponds to the deferred capital component of the NSIE being depreciated from 1 July 2017, with foregone returns capitalised until this date.

[35] Under the terms of the GAPE deed, Aurizon Network may recover revenue associated with the deferred NSIE capital. Where Aurizon Network is able to recover the full value of the NSIE amount (including the capitalisation of foregone returns) under the regulatory framework, these commercial arrangements may provide for Aurizon Network to benefit from additional revenue, the longer the NSIE amounts are deferred.

[36] The application of the revenue deferral mechanism is consistent with the principle of financial capital maintenance, which refers to the requirement that the present value of expected capital charges for an asset over its economic

delay to the recovery of deferred revenue may act to increase Aurizon Network's exposure to the risk of not recovering the full amount of deferred revenue. Indeed, Aurizon Network has identified such risks as part of past regulatory proposals to include deferred capital amounts into the RAB.[37]

Therefore, we consider it appropriate to include an amount for the deferred NSIE capital in the Newlands pricing RAB that corresponds to the value of the NSIE, had it been included in the RAB from the earliest reasonable opportunity.

From the information available, we consider the commencement of UT5 (1 July 2017) represents the earliest reasonable opportunity for Aurizon Network to have sought to recover revenue associated with the deferred NSIE capital, under the regulatory framework.

Aurizon Network submitted that the commencement of UT5 represented the earliest practical date the deferred NSIE capital could have been reflected in the Newlands system reference tariff.[38]

We understand that the NAPE user had started railing by the commencement date of UT5.[39]

We also note that the deferral of the NSIE capital was approved as part of the 2016 access undertaking (UT4) in October 2016. Our final decision on Aurizon Network's 2014 DAU outlined that we would assess a NAPE reference tariff proposal if the NAPE train services commenced.[40] We consider that our assessment of Aurizon Network's 2017 DAU (which was submitted in November 2016) represented a practical period for consultation on a proposed treatment of the deferred NSIE.

Staged approach to including the NSIE amount

We consider it reasonable to stage the inclusion of the amount relating to the deferred NSIE capital in the Newlands pricing RAB—with Aurizon Network spreading the amount across two years. Importantly, the total amount being proposed by Aurizon Network for inclusion in the Newlands pricing RAB is equal to the value of $81.4 million (at 1 July 2023).

In support of this approach, Aurizon Network acknowledged customer concerns regarding the subsequent increase in the allowable revenue without a corresponding increase in deliverable network capacity.[41] Aurizon Network said that the staged approach means the percentage increase in the Newlands system asset values used for pricing purposes is not expected to exceed the percentage increase in system capacity provided by the installation of remote control signalling (an approved transitional arrangement).

While we consider the staged approach reasonable, we do not consider it necessary for the inclusion of the NSIE amount to be delayed until additional works are undertaken to increase

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life should be equal to the initial asset value. Within a regulatory context, this means that investors of a regulated firm can expect to recover the opportunity cost of their capital and the nominal value of their initial investment over the life of the asset.

[37] For instance, see Aurizon Network, *Submission on the 2017 Draft Access Undertaking (UT5)*, 30 November 2016, p. 129.

[38] Aurizon Network, sub. 1, pp. 10–11.

[39] Insofar that there was some uncertainty as to the extent that the NAPE user was railing and the pricing arrangements that would be applied to recover revenue associated with the deferred NSIE, we would expect this to reinforce the incentives for Aurizon Network (under the regulatory framework) to seek to recover this amount from the relevant parties at this time.

[40] QCA, *Aurizon Network 2014 draft access undertaking, Volume III—Pricing & tariffs*, final decision, April 2016, p. 124.

[41] Aurizon Network, sub. 1, p. 11.

deliverable network capacity, or until the ECD has been reduced.[42] Concerns regarding the existing capacity deficit in the Newlands system are best dealt with through the related processes, as provided in UT5.

Residual value of the deferred NSIE capital

From the information available, we do not consider it appropriate for Aurizon Network to continue to defer NSIE capital equal to the value of $26.7 million (at 1 July 2023).

Aurizon Network acknowledged that continued deferral of residual NSIE capital would increase regulatory and commercial uncertainty, while also noting that a true and full assessment of differences between regulatory and commercial asset values can only be considered at the expiry of commercial arrangements.[43]

Reflecting its views that the full value of the deferred NSIE capital is $156 million at 1 July 2023, Aurizon Network proposed to continue to defer $26.7 million (at 1 July 2023) of the NSIE capital.[44] Aurizon Network stated that the allocation of this amount (between Newlands and GAPE systems) would be determined at a later date.[45]

In general, we consider it is appropriate for Aurizon Network to recover an amount equal to the full value of the deferred revenue, including the capitalisation of foregone returns, to compensate Aurizon Network for any such deferral.

However, it is our view that Aurizon Network has not provided sufficient justification as to why it would be reasonable for it to recover deferred revenue under the regulatory framework beyond that associated with including a value of $81.4 million into the Newlands pricing RAB. As outlined above, we consider it appropriate for Aurizon Network to include an amount for the deferred NSIE capital into the Newlands pricing RAB consistent with the value of the deferred NSIE capital had it been included from the commencement of UT5.

We have concerns with the proposed approach, as it contributes to uncertainty under the regulatory framework.[46] We also do not consider it the role of the regulatory framework to resolve outcomes under commercial arrangements.[47]

Concerns raised by stakeholders

A number of stakeholders did not agree with including an amount for the deferred NSIE capital in the Newlands pricing RAB above $46.9 million (at 1 July 2023)[48]—the amount Aurizon Network proposed to include in the Newlands pricing RAB, as part of its initial GAPE and Newlands pricing DAAU.[49]

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[42] Glencore requested that any additional NSIE amount only be included in the pricing RAB once the independent expert has determined that the installation of remote control signalling has been effective in reducing the ECD as proposed (Glencore sub. 3, p. 2).
[43] Aurizon Network, sub.1, p. 13.
[44] While voluntarily excluding the remaining $47.9 million (at 1 July 2023) from its RAB models.
[45] Aurizon Network, sub. 1, pp. 12–15.
[46] Where our view is that the commencement of UT5 represented a reasonable time for Aurizon Network to have sought to recover revenue associated with the deferred NSIE capital.
[47] Doing so could harm certainty and predictability, both in relation to commercial arrangements and the regulatory framework. See QCA, *GAPE and Newlands pricing DAAU*, preliminary considerations, December 2022, p. 5.
[48] Glencore, sub. 3, p. 1; QCoal, sub. 4, pp. 1–2. Similarly, Bravus did not support including an amount above the depreciated historical cost of the NSIE (Bravus, sub. 2, pp. 5–6).
[49] Aurizon Network, *GAPE and Newlands Pricing Draft Amending Access Undertaking*, 2 September 2022.

Stakeholders expressed concern that Aurizon Network could use the commercial arrangements to 'double recover' costs.[50] QCoal submitted that the inclusion of $46.9 million had stakeholder support, with Aurizon Network previously stating that it determined this amount having regard to how these costs are accounted for in commercial arrangements.[51] Glencore also raised concerns that Aurizon Network was using the lack of transparency around the non-regulatory agreements to extract greater value from customers via the interaction of regulatory and commercial arrangements.[52]

In our preliminary considerations on the initial GAPE and Newlands pricing DAAU, we stated that where there was agreement between Aurizon Network and stakeholders on the appropriate amount to include in the Newlands pricing RAB for the deferred NSIE capital, we would take this into consideration. Our position remains the same.

We do not consider that including an amount beyond $46.9 million in the Newlands pricing RAB would lead to a double recovery of revenue under the regulatory framework. The NSIE capital has remained deferred and has not been accounted for in the Newlands or GAPE systems reference tariffs. To the extent Aurizon Network has recovered revenue through commercial arrangements, this is a matter that falls outside the scope of the regulatory framework. We do not consider it is appropriate to give weight to the potential outcomes occurring under commercially negotiated arrangements, as doing so could harm certainty and predictability, both in relation to commercial arrangements and the regulatory framework.

Bravus submitted that Aurizon Network’s proposal fails to allocate deferred NSIE amounts to stakeholders against the benefits enjoyed since 2012. Bravus stated that the earliest practical date that the NAPE deed should have triggered was 2014 when the NAPE expansion mine commenced railing. It considered that commercial drivers led to the NAPE deed not being triggered in 2014, and these drivers were outside of the scope of the regulatory framework.[53]

We acknowledge that mining operations at the NAPE expansion mine may have begun before UT5 commenced. However, as outlined above, we consider the commencement of UT5 (1 July 2017) represents the earliest reasonable opportunity for Aurizon Network to have sought to recover the deferred revenue associated with the NSIE, under the regulatory framework.

As part of our approval of UT4, we considered it was appropriate that revenue associated with the NSIE be deferred until such time as there was more certainty regarding the commencement of NAPE train services. We understand that there was still considerable uncertainty surrounding the relevant volumes being railed by the NAPE user at that time. Furthermore, our approval of UT4 considered that any proposal to recover the deferred NSIE from all Newlands users would need to go through stakeholder consultation.[54]

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[50] QCoal, sub. 4, p. 2; Glencore, sub. 3, p. 1; Rio Tinto, sub. 5, p. 1. Specifically, QCoal and Glencore did not consider it appropriate for Aurizon Network to be compensated for the deferred NSIE amounts from Newlands system customers, where Aurizon Network has recovered these costs from GAPE customers and there is no associated cost to Aurizon Network as a result of the deferral.

[51] QCoal, sub. 4, p. 1. Glencore also said the $46.9 million amount was endorsed by customers (Glencore, sub. 3, p. 1).

[52] Glencore, sub. 3, p. 1.

[53] Bravus, sub. 2, pp. 5–6.

[54] QCA, *Aurizon Network 2014 draft access undertaking, Volume III—Pricing & tariffs*, final decision, April 2016, p. 124.

2.3 Contract-volume-based pricing in the Newlands system

Aurizon Network proposed to apply contract-volume-based pricing in the Newlands system, meaning reference tariffs would be determined using contract volumes. The contract volumes applied in the April 2023 DAAU were adjusted down for 'Aurizon Network cause'.[55]

Complementing its proposal to apply contract-volume-based pricing, Aurizon Network proposed to provide Newlands users with the opportunity to relinquish excess access rights without incurring a fee.[56]

Separately, Aurizon Network also proposed to remove barriers within the regulatory framework that prevent GAPE access rights being transferred to Newlands users.[57]

Our assessment

We generally consider there is merit in contract-volume-based pricing where users are able to manage their contract volumes. However, given current circumstances, we are minded to retain the current pricing arrangements in the Newlands system at this time.

Current pricing arrangements use forecast volumes to determine reference tariffs, where the forecast volumes reflect expected demand over a given period. Contract-volume-based pricing on the other hand uses contract entitlements held by users to determine the reference tariff. In some cases, these contract entitlements may be in excess of expected demand.

The allocation of costs under contract-volume-based pricing makes users more accountable for their contract volumes, which may improve price signals to users regarding the extent to which they value their consumption of contracted capacity. Where users are able to manage their contract volumes, this may result in a more efficient allocation of system capacity. We note that Aurizon Network proposed fee-free relinquishments, which would assist users in managing contract volumes.[58]

However, an ECD has been identified on the combined GAPE and Newlands system through the relevant UT5 processes, such that contract volumes may be above deliverable network capacity. Furthermore, the April 2023 DAAU does not modify the current take-or-pay arrangements regarding the revenue cap.

A number of stakeholders identified concerns relating to a user's ability to manage their contract volumes in the current environment (where an ECD remains), which they considered would increase the risk of users not being able to rail up to contracted levels.[59]

In this regard, we note:

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[55] The adjustment was considered necessary to ensure expected access revenue from access charges and take-or-pay would equate to the system allowable revenue (Aurizon Network, sub. 1, pp. 19–23).

[56] Subject to it being notified within a specified period of time. Aurizon Network also proposed that the relinquished access rights be available to access seekers, conditional on the ECD in the Newlands and GAPE systems being resolved (Aurizon Network, sub. 1, pp. 23–24).

[57] Currently, the GAPE reference train service criteria (in schedule F cl. 11.1(a) of UT5) requires GAPE reference train services to operate in the GAPE system, which comprises the northern missing link (NML). The NML is not utilised by Newlands train services. Aurizon Network noted the proposed amendments were necessary, but not on their own sufficient, for GAPE access rights to be transferred to Newlands users, where there may be constraints under commercial arrangements (Aurizon Network, sub. 1, p. 26).

[58] To the extent users have signed up to commercial arrangements that prevent them from participating in relinquishment processes as suggested by QCoal, this is an outcome under commercial arrangements and should be dealt with through the relevant arrangements (QCoal, sub. 4, p. 3).

[59] Glencore, sub. 3, pp. 2–3; QCoal, sub. 4, pp. 3–4.

- the GAPE and Newlands train services are scheduled and operated together, with both utilising the shared rail corridor between the Newlands Junction and the Port of Abbot Point. Where contract-volume-based pricing is only applied in the Newlands system, this could provide different incentives across the two systems to retain 'buffer capacity'[60]—Newlands users will have a financial incentive to relinquish 'buffer capacity', while GAPE users are more likely to maintain 'buffer capacity'
- where there are contested train paths, UT5 establishes the principles for prioritising/allocating capacity among access holders. Amongst other things, these principles give priority to users who are 'more behind' on contract volumes.

Bravus also considered that contract volumes are not a plausible predictor of current or future railings and raised concerns with the associated relinquishment process, which could increase access charges for remaining access holders.[61]

Following stakeholder concerns, Aurizon Network submitted it was agnostic as to the use of contract volumes or forecast demand as the basis for setting the Newlands reference tariffs and would accept a decision that rejected this aspect of the April 2023 DAAU.[62]

On balance, given the concerns raised by stakeholders, we are minded to retain the current pricing arrangements in the Newlands system at this time, which apply forecast volumes to determine reference tariffs. We note that a shift to contract-volume-based pricing would typically involve broader changes to the take-or-pay arrangements.[63]

The current forecast volumes used to establish reference tariffs in the Newlands System have been established with the benefit of stakeholder feedback on proposed railings for each of their respective origin–destination pairings. We consider using forecast volumes to determine reference tariffs will also minimise revenue cap adjustments in future years.

Where contract-volume-based pricing is not applied, we do not consider that fee-free relinquishments are necessary for Newlands users to manage contract volumes.[64] To the extent that stakeholders consider fee-free relinquishments an appropriate mechanism to reduce the ECD,[65] these matters should be dealt with through the relevant processes.[66]

GAPE reference train service criteria

We are minded to refuse to approve amendments providing for the transfer of GAPE access rights to Newlands users in the presence of an ECD.

Stakeholders generally supported the removal of barriers that prevent the transfer of GAPE access rights to Newlands users where this can improve efficiency.[67] Rio Tinto noted that GAPE

[60] Contract entitlements held above expected demand.
[61] Bravus, sub. 2, pp. 8–9.
[62] Subject to its proposed fee-free relinquishments also being rejected (Aurizon Network, sub. 6, p. 2).
[63] Aurizon Network and stakeholders have previously identified that a shift to contract-volume-based pricing would typically involve broader changes to the take-or-pay arrangements, with Aurizon Network stating that it would be taking on additional financial risks without such changes. See, for example, Aurizon Network, *GAPE and Newlands Pricing Draft Amending Access Undertaking*, 2 September 2022, p. 44; QRC, submission to the QCA, *Aurizon Network Draft Amending Access Undertaking – GAPE and Newlands Pricing*, 2 November 2022, p. 3.
[64] This position is also relevant for the GAPE system, where Rio Tinto has suggested fee-free relinquishments should also apply (Rio Tinto, sub. 5, p. 1).
[65] For example, QCoal, sub. 4, p. 4.
[66] See UT5, cl. 7A.5.
[67] QCoal, sub. 4, p. 4; Rio Tinto, sub. 5, p. 1; Bravus, sub. 2, p. 15.

reference train services had the contracted right to utilise the full length of the journey to Abbot Point and therefore reference train service should be transferable to any point along it.[68]

However, in the current environment, where an ECD has been identified on the combined GAPE and Newlands system, some stakeholders had concerns about the ability of Newlands users being able to rail up to contract volumes. QCoal submitted that until the ECD in the Newlands system is significantly reduced, or eliminated, Aurizon Network's proposal has the potential to further compromise opportunities for access holders to be able to utilise their contracted capacity.[69]

We note that the transfer of unused access rights to a Newlands user would enable such a user to obtain access rights beyond its current contract position. This may result in an increase in real demand in the Newlands system. In the current environment, where capacity is constrained, this could potentially impact how Newlands users' train services are prioritised—potentially impacting the ability of current system users to rail up to contract volumes.

Further, while we consider there would typically be efficiency gains associated with the transfer of unused access rights to Newlands users, these efficiency gains are premised on the fact that Newlands users would be able to increase their railings overall, to account for capacity not being utilised by GAPE users. Where capacity is constrained, this may limit the extent to which any efficiency gains can be realised.

2.4 Application of PIC discounts

Aurizon Network proposed to amend the definition of private infrastructure so that it captures only rail transport infrastructure that does not form part of the declared service and is solely constructed to connect an access holder's or customer's loading facility to the CQCN.[70]

This proposed amendment has the effect of narrowing the application of PIC discounts provided to access holders and customers under UT5.[71] In particular, the PIC amount previously approved for Bravus[72] would no longer satisfy the requirements for consideration for a PIC discount under UT5. On that basis, Aurizon Network's reference tariff calculations do not apply a PIC discount to Bravus under the April 2023 DAAU.

Our assessment

UT5 provides for approved PIC amounts to be recognised in determining the access charge payable by train services operating on a private extension.[73] This is to ensure that end users are not commercially disadvantaged where they elect to privately construct and own mine-specific infrastructure, rather than having it constructed and owned by Aurizon Network.

To date, the provisions have been applied in the context of customer-specific network connections, spurs and balloon loops.

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[68] Rio Tinto, sub. 5, p. 1.

[69] QCoal, sub. 4, pp. 4.

[70] See Part 12 of Aurizon Network's April 2023 GAPE Newlands pricing DAAU.

[71] Under UT5 (cl. 6.3.2), the approval of a PIC amount is based on the QCA being satisfied that expenditure is for the prudent and efficient value of the assets that are used to provide train services over private infrastructure.

[72] On 15 December 2022, we approved a PIC amount of $44 million in respect of Bravus's Carmichael rail loop project and connecting infrastructure. At the time of approval, Bravus's PIC claim satisfied the requirements for consideration under the PIC provisions in UT5.

[73] Under UT5 (cls. 6.3.1 and 6.4.10), users of new train services using mine-specific infrastructure (that does not require an expansion) will pay the higher of the system reference tariff less a discount for any approved PIC and the minimum revenue contribution.

Aurizon Network said the intended objective of recognising PIC amounts when determining access charges was to promote competitive neutrality in the market for construction and ownership of mine-specific infrastructure. However, Aurizon Network considered the current definition of private infrastructure may lead to outcomes that are inconsistent with this intent.[74]

We consider that Aurizon Network's proposed amendment to the definition of private infrastructure achieves the intended objective of recognising PIC amounts and appropriately narrows the scope of private infrastructure that is applicable for a PIC discount. In particular, it:

- continues to provide for end users to not be commercially disadvantaged for electing to privately construct and own mine-specific infrastructure
- should prevent an end user from obtaining a commercial advantage over other system users from electing to privately construct and own mine-specific infrastructure[75]
- potentially limits the extent to which a PIC discount would be provided for a project where the nature and scale of that private infrastructure leads to a PIC amount that results in a significant redistribution of system costs.[76]

In principle, we consider proposed amendments to the definition of private infrastructure appropriate to narrow the application of PIC discounts. However, we note that the term private infrastructure is used more broadly throughout UT5. Accordingly, we must be satisfied that a change to the definition of private infrastructure does not lead to outcomes that are inappropriate, more broadly, and invite feedback on this matter. We also have concerns with retrospective impacts, discussed below.

Implications for previously approved PIC amounts

Under UT5, we approved the prudent and efficient value of PIC amounts associated with private infrastructure related to 2 projects—the Sojitz Meteor Downs South rail and train loading project and Bravus's Carmichael rail loop and connecting infrastructure.[77]

The application of the approved Bravus PIC amount was to take effect from 1 July 2023.[78]

Under Aurizon Network's April 2023 DAAU, the previously approved Bravus PIC amount would no longer satisfy the requirements for consideration for a PIC discount. In this regard, Aurizon Network submitted that the Carmichael rail infrastructure:

- has not been constructed solely to connect the loading facility for the Carmichael mine to the declared service—with the proposed amendment to the definition of private infrastructure, a PIC amount would not be applicable to the calculation of access charges for train services entering and exiting the declared service to access Carmichael rail infrastructure

[74] Aurizon Network raised concerns about having the PIC provisions also applying more broadly, including where the nature and scale of the project may result in significant adverse impacts for other access holders (Aurizon Network, sub. 1, pp. 29–31).

[75] For instance, providing a PIC discount for multi-user infrastructure may provide a commercial advantage to the relevant access seeker where it elects to privately construct and own mine-specific infrastructure and it is able to also recover a portion of the PIC from third parties accessing that private infrastructure.

[76] Whereas Aurizon Network has previously advised that the development and connection of a new coal mine would normally be expected to represent under 10% of the contracted system volume in large multi-user coal systems.

[77] Information on these assessments is available on our website at *Private incremental costs.*

[78] Aurizon Network, *2017 Access Undertaking—Updates to Reset Schedule F Preliminary Values*, February 2023, p. 25.

- has been developed as an open-access, multiuser railway, which is subject to an access policy approved by the State of Queensland.[79]

Bravus did not consider it appropriate for Aurizon Network to use the April 2023 DAAU process to reopen and retrospectively change an otherwise completed regulatory process. Bravus sought that the discount be applied in line with existing arrangements.[80]

We do not consider it appropriate to retrospectively change the application of PIC discounts for previously approved PIC amounts following an access holder's investment in private infrastructure, unless circumstances change such that the arrangements are providing benefits beyond those benefits originally intended.[81] Providing for retrospective changes to discounts will increase uncertainty for future access seekers as to the level of access charges that will be applied, where investment in private infrastructure to connect to the CQCN is required.

We note that Bravus's PIC claim qualified for consideration under the current UT5 provisions. Furthermore, it is not apparent that applying the PIC provisions in this circumstance has resulted in Bravus obtaining a commercial advantage over other system users from electing to privately construct and own the associated infrastructure. In this regard, we note:

- the approved Bravus PIC amount related to infrastructure that could typically be associated with mine-specific infrastructure—Bravus has not sought a PIC discount that considers costs associated with the broader Carmichael rail network[82]
- Bravus is the only access holder that is currently utilising the Carmichael rail infrastructure.

Separately, we do not consider a comparison with the GAPE reference tariff is a relevant consideration in determining whether a PIC discount should be applicable for Bravus's train services (see Box 2).

Accordingly, we do not consider that a retrospective change to the application of Bravus's PIC discount is justified at this time—we only consider it reasonable to retrospectively change the application of the Bravus PIC discount in circumstances where its application demonstrably results in Bravus obtaining commercial advantage over other system users from electing to privately construct and own mine-specific infrastructure.[83]

While we consider that the proposed amendments to the definition of private infrastructure are appropriate in principle, we are of the view that further amendments are required, so that the Bravus PIC discount can continue to be applied under the current circumstances.[84] We welcome further views on the way in which it may be appropriate to amend Aurizon Network's April 2023 DAAU to provide for this.

[79] Aurizon Network, sub. 1, pp. 30–31.
[80] Bravus, sub. 2, pp. 12–14.
[81] For instance, where a PIC discount results in an end user obtaining commercial advantage over other system users from electing to privately construct and own mine-specific infrastructure.
[82] QCA, *Private Incremental Cost—Carmichael rail loop and connecting infrastructure*, decision notice, 15 December 2022, p. 2.
[83] We acknowledge that circumstances may change in future, which could result in such a scenario.
[84] For instance, this may be realised through further amendments to how an approved PIC is separately defined under UT5.

Box 2: Consideration of the GAPE reference tariff in applying the PIC discount

Bravus's access charges are calculated with respect to the Newlands system reference tariff.[85]

UT5 clearly, and separately, defines the Newlands system and the GAPE system. Access charges for access rights in the Newlands system are calculated with respect to the Newlands system reference tariff. Thus, we consider that any PIC discount is to be considered with respect to the applicable reference tariff for the relevant train services.

Aurizon Network considered that regard should be had to the extent to which Bravus train services receive an effective discount through the application of the Newlands system reference tariff, in comparison to the GAPE reference tariff.[86] In this regard, Aurizon Network considered that:

- it can be inferred from clause 6.3.1(e) of UT5 that the Newlands system reference tariff and the GAPE system reference tariff apply in respect of access rights in the Newlands system, given that GAPE train services utilise the Newlands system. Thus, Aurizon Network submitted that services operating in the Newlands system are subject to the GAPE reference tariff
- if the GAPE reference tariff had been implemented as an expansion tariff[87], clause 6.3.1(e) of UT5 would have expressly required the access charges for new coal-carrying train services operating in the Newlands system to be calculated based on the GAPE reference tariff.[88]

Aurizon Network considered that determining an access charge with respect to the highest relevant reference tariff applicable to the operation of train services using the same rail infrastructure avoids discriminatory pricing effects.[89]

QCoal also considered that there is no differentiation in service offering between Newlands and GAPE services and that the PIC discount should apply to the higher GAPE reference tariff (on a $/ntk basis).[90]

The GAPE system was not established as an expansion tariff, but as an independent system with a separate reference tariff. Therefore, we do not consider that the application of clause 6.3.1 (e) is a relevant consideration as to whether a PIC discount should be applied to train services operating in the Newlands system.

We do not consider that the application of the PIC discount in this instance results in discriminatory pricing effects. The UT5 price differentiation provisions are applied with respect to the system reference tariffs, which result in different access charges being applied to users depending on specific coal system(s) they access. UT5 does not specifically limit price differentiation between users accessing different systems.

Bravus submitted that the application of the PIC discount only relates to the proportion of private infrastructure costs associated with its Newlands contracted capacity and not any proposed expansion tonnage through the GAPE system.[91]

[85] Bravus, sub. 2, p. 12.
[86] Aurizon Network, sub. 1, p. 28.
[87] As opposed to be being established as an independent revenue and pricing system to quarantine costs and risks from Newlands system users.
[88] Aurizon Network, sub. 1, pp. 27–28.
[89] Aurizon Network considered the application of a PIC discount to new coal carrying train services commencing after the completion of the NSIE would have a discriminatory price effect. (Aurizon Network, sub. 1, pp. 27–29).
[90] QCoal, sub. 4, p. 5.
[91] Bravus, sub. 2, p. 13.

SUBMISSIONS

We received the following submissions during our assessment of Aurizon Network's April 2023 GAPE and Newlands pricing DAAU, which are available on our website.[92] The submission numbers below are used in this draft decision for referencing purposes.

Stakeholder	Submission number	Submission	Date received
Aurizon Network	1	April 2023 GAPE Newlands pricing DAAU supporting submission	6 April 2023
	6	Additional submission on the April 2023 GAPE Newlands pricing DAAU	15 June 2023
Bravus	2	Submission on Aurizon Network's April 2023 GAPE Newlands pricing DAAU	25 May 2023
Glencore	3	Submission on Aurizon Network's April 2023 GAPE Newlands pricing DAAU	25 May 2023
QCoal	4	Submission on Aurizon Network's April 2023 GAPE Newlands pricing DAAU	25 May 2023
Rio Tinto	5	Submission on Aurizon Network's April 2023 GAPE Newlands pricing DAAU	24 May 2023

[92] QCA, *GAPE Newlands pricing DAAU*, QCA website, 2023.