



# Queensland Rail's 2023 Draft Access Undertaking:

New Hope submission

2 February 2024

<b>1</b>	<b>Introduction</b>	<b>3</b>
	1.1 New Hope	3
	1.2 The 2023 DAU	3
<b>2</b>	<b>Structure of NHG Submission</b>	<b>4</b>
<b>3</b>	<b>Overview of NHG Submission</b>	<b>4</b>
	3.1 Overview	4
	3.2 Concerns in relation to reference tariffs	5
	3.3 Concerns in relation to 2023 DAU and SAA wording	5
<b>4</b>	<b>Regulatory framework and powers of the QCA</b>	<b>6</b>
<b>5</b>	<b>West Moreton System Reference Tariffs</b>	<b>7</b>
	5.1 Overview	7
	5.2 Coal volume forecasts	7
	5.3 Asset base roll forward – DAU2 opening asset base	8
	5.4 Allocation to coal services of common network asset base	8
	5.5 Allocation of maintenance and operating costs	8
	5.6 WACC	8
	5.7 Capex, maintenance and operating costs: Overview	8
	5.8 Capital Expenditure	9
	5.9 Maintenance expenditure	10
	5.10 Operational expenditure	11
	5.11 Depreciation	12
	5.12 Two-part tariff	13
	5.13 Discount for Private Infrastructure	13
	5.14 Inflation	14
<b>6</b>	<b>WACC</b>	<b>14</b>
	6.1 Summary of NHG WACC submission	14
	6.2 Cost of debt uplift is no longer justified	15
	6.3 Asset and equity beta should be brought into line with other regulated businesses	17
	6.4 Market parameters should reflect the QCA’s orthodox methods	20
	6.5 Top-down assessment	21
<b>7</b>	<b>Metropolitan System reference tariffs</b>	<b>23</b>
<b>8</b>	<b>Access Undertaking Drafting</b>	<b>23</b>
	8.1 Approach	23
	8.2 Independent Capacity Assessment	24
	8.3 Loss capitalisation	24
	8.4 Volume Trigger for Review of Reference Tariff	25
	8.5 Renewal rights	26
	8.6 Approval of capital expenditure	26
	8.7 Capital expenditure true-up	26
	8.8 Other comments on QR’s proposed amendments to the Access Undertaking	27
<b>9</b>	<b>Standard Access Agreement</b>	<b>29</b>
<b>10</b>	<b>Conclusion</b>	<b>31</b>
	<b>Schedule 1 - Response to QCA “Topics for Stakeholder Comments”</b>	<b>32</b>
	<b>Schedule 2 - NHG Proposed Drafting Changes to Schedules D and E</b>	<b>33</b>

# 1 Introduction

Thank you for the opportunity to provide this submission on behalf of New Hope Group (**NHG**) in response to the Queensland Competition Authority's (**QCA**) request for submissions on Queensland Rail's (**QR**) proposed draft access undertaking to commence from 1 July 2025 (the **2023 DAU**).

## 1.1 New Hope

NHG is a majority Australian owned and operated diversified energy company which has been proudly operating for more than 60 years. NHG has business interests and operations spanning coal mining, exploration, port operation, oil, agriculture and innovative technologies.

NHG currently has two open cut coal mines, one in the Darling Downs and one in the Hunter Valley. These are New Acland, north of Oakey in Queensland, and Bengalla, west of Newcastle in New South Wales. The Company also has three previous operations that are currently undergoing rehabilitation in the West Moreton region - Jeebropilly, New Oakleigh and Chuwar.

NHG's principal interest in QR's network is in respect of its mining operations which utilise the West Moreton system and the Metropolitan system to access the Queensland Bulk Handling coal terminal at the Port of Brisbane (with those parts of the QR network shown in Figure 1 below).

**Figure 1: West Moreton / Metropolitan network and coal supply chain**



Given NHG's portfolio of coal projects, a key consideration when making investment decisions and allocating capital for NHG is the existence of regulatory arrangements which promote efficient supply chain performance and provide reasonable and predictable charges for use of infrastructure.

## 1.2 The 2023 DAU

NHG supports the relatively incremental approach to changes proposed by QR in respect of the wording of the 2023 DAU and related standard access agreement (**SAA**). That has allowed this submission to focus on primarily on those issues of concern in the amendments. However, NHG

also considers that reforms are necessary in the number of areas, primarily to ensure that contracted capacity can be delivered in the high-demand environment which is forecast during the AU3 period, that appropriate adjustments can be made when volumes or capital expenditures vary significantly from expectations, and to ensure that the prudence and efficiency of the major capital expenditure program proposed by QR is thoroughly tested before commitments to expenditure are made.

In regard to tariffs, we consider that the substantial increases proposed by QR are both unaffordable and unjustified. NHG considers that existing West Moreton tariffs are set at a level which risks making the businesses of current and future users of the system economically unviable, despite those tariffs being referred to by QR as the 'affordable' tariff. We do not consider that any increase in those tariffs is sustainable. We have strong concerns about the substantial increases which are proposed, and about what may happen to tariffs if any forecast tonnage is lost. We therefore consider that AU3 should retain the concept of a capped affordable tariff, with loss capitalisation applying to any revenue difference arising from the application of the cap.

In terms of the building block elements proposed by QR, we note that some elements of QR's approach are consistent with the approach to developing individual building blocks for AU2. However, NHG is concerned that:

- (a) Proposed maintenance and operating costs appear excessive and have not been adequately justified as being prudent and efficient.
- (b) The very large proposed capital expenditure program has not been adequately justified.
- (c) The proposed acceleration of depreciation has not been adequately explained.
- (d) The proposed WACC uplift is not appropriate in the context of the changes to QR's risk profile since the time of the previous undertaking.

## **2 Structure of NHG Submission**

The NHG submission addresses each of the components of the 2023 DAU as follows:

- (a) Section 3: Overview of NHG's submission;
- (b) Section 4: Discussion of the regulatory framework and role of the QCA;
- (c) Section 5: Discussion of West Moreton reference tariffs and the building block components which lead to the proposed tariff;
- (d) Section 6: Detailed discussion of the proposed WACC;
- (e) Section 7: Comment on proposed metropolitan tariff;
- (f) Section 8: Discussion of 2023 DAU drafting;
- (g) Section 9: Comments on Standard Access Agreement;
- (h) Section 10: Conclusion.

## **3 Overview of NHG Submission**

### **3.1 Overview**

Having considered the 2023 DAU and QR Submission, NHG considers that it is not appropriate for the QCA to approve the 2023 DAU under section 138(2) of the *Queensland Competition Authority Act 1997* (the **QCA Act**) for the reasons set out in this submission.

In particular, in respect of each of those matters, it fails to give sufficient weight to the following matters:

- (a) the object of Part 5 of the QCA Act, particularly regarding the efficient operation of and use of significant infrastructure;
- (b) the public interest;
- (c) the interests of persons who may seek access to the service;
- (d) the pricing principles in section 168A QCA Act, particularly in relation to the return on investment being commensurate with the regulatory and commercial risks involved.

Accordingly, NHG requests that the QCA makes a decision to refuse to approve QR's 2023 DAU and sets out the ways in which the 2023 DAU should be amended, in accordance with section 140 of the QCA Act. This submission provides NHG's suggestions as to what it considers those amendments should address.

### **3.2 Concerns in relation to reference tariffs**

NHG's principal concerns with the 2023 DAU relate to the proposed West Moreton system reference tariffs.

In particular, the reference tariffs proposed are:

- (a) unsustainable and economically unviable for QR's coal customers; and
- (b) based on building block components which include:
  - An excessive risk adjustment within WACC.
  - An acceleration of depreciation to reduce QR's risk without consideration of the impact of that change when assessing WACC and without adequate explanation of the impacts of the change.
  - Capital, operating and maintenance costs which are well in excess of previous allowances, with insufficient justification having been provided for the increases.

### **3.3 Concerns in relation to 2023 DAU and SAA wording**

NHG acknowledges that QR's has sought only incremental changes to the drafting of AU2, and NHG supports this approach. However, we do have concerns with some of the proposed changes, discussed in Section 8.

We also consider that additional drafting is required in AU3 to:

- (a) Provide for independent assessment of the capacity of the network. This is required to ensure that contracted capacity can be delivered and also to confirm that proposed capital expenditure is necessary and will deliver the expected capacity benefits.
- (b) Encourage QR to conduct thorough analysis of each major capital project, including by undertaking meaningful engagement with customers, so that the prudence and efficiency of each element of the major capital expenditure program proposed by QR is well tested ahead of the commitment of funds.
- (c) Allow tariff adjustments during the term, if actual capital expenditure varies from the capital indicator (up or down) by a material amount.
- (d) Provide for a review of reference tariffs if, following a review triggered under QR's proposed clause 3.2 of Schedule D (expected volumes below 7.5mt), volumes subsequently recover by a material amount.

#### **4 Regulatory framework and powers of the QCA**

NHG made extensive submissions to the QCA in previous processes in connection with the regulatory framework which applies to the QCA's consideration of a draft access undertaking.

In summary (and consistent with the QCA's findings and conclusions during the AU1 and AU2 consideration process):

- (a) the QCA has a wide discretion when determining whether it is appropriate to approve an undertaking;
- (b) that discretion of the QCA is only limited by:
  - (i) the requirement to approve an undertaking which it considers 'appropriate' after it has 'had regard to' each of the factors set out in section 138(2) of the QCA Act;
  - (ii) the requirement to consult, invite and take into account submissions received (and otherwise provide natural justice more generally); and
  - (iii) the QCA not having a right to refuse to approve a draft access undertaking only because the QCA considers a 'minor and inconsequential' amendment should be made to a particular part of the undertaking;
- (c) no single factor listed in section 138(2) QCA Act is a 'cornerstone requirement', or a dominant or paramount factor that is required to be given greater weight;
- (d) the QCA has the power to approve an undertaking which is inconsistent with a pricing principle in section 168A QCA Act if it would be appropriate to do so, having regard to all of the section 138(2) QCA Act factors; and
- (e) the QCA is not bound to follow any particular regulatory precedent and, while the QCA may often follow such precedent, the QCA must not follow a precedent if to do so would result in the approval of an undertaking which is not appropriate having regard to the factors set out in section 138(2) QCA Act.

## 5 West Moreton System Reference Tariffs

### 5.1 Overview

QR is seeking substantial and unsustainable tariff increases, despite forecasting a strong increase in volumes which would be expected to spread fixed costs and result in reduced tariffs.

QR is seeking a West Moreton System tariff which, at \$32.63/000gtk in FY26, is 31% higher than the current tariff (“one-part” equivalent) of \$24.90/000gtk. It is important to note that the current (AU2) reference tariffs have been set below the Ceiling Reference Tariff because the Ceiling Reference Tariff was considered unaffordable for customers. QR has not explained how it has determined that a 31% increase above the “affordable” tariff will not adversely impact on the utilisation of the network. In NHG’s view, there is no increase on the current tariff which could be considered “affordable”, because the existing tariff has been set at a level which risks reducing utilisation of the network by making the business of one or more of its customers unviable. There is also a risk that some of the volume may transfer to road.

**[Paragraph redacted.]**

NHG understands that the higher forecast volumes will bring higher costs, however, our experience in other networks has been that increasing volumes results in economies of scale and reduced tariffs, rather than substantial increases. These figures should ring clear warning bells about what is proposed.

The proposed reference tariffs are both:

- (a) unsustainable and economically unviable, in terms of impacts on QR’s customers, because tariffs are substantially higher than the current tariffs which have been determined to sit at the limit of affordability; and
- (b) unjustified, based on analysis of the individual building blocks which contribute to the ~**[Redacted]** increase in claimed revenue.

NHG suggest that:

- (a) each element of the building block methodology should be thoroughly reviewed and, in our opinion, reduced; and
- (b) if the resulting tariff is not an affordable tariff (with the current tariffs providing a reasonable guide as to the limit of affordability), then tariffs must be limited to the affordable level.

### 5.2 Coal volume forecasts

QR has advised that the proposed West Moreton reference tariffs are based on a forecast of 9.6 million tonnes per annum (mtpa). We understand that these forecasts were developed by QR, taking into account a range of information, not limited to information provided by the miners.

NHG has no objection to the adoption of the forecast of 9.6mtpa if revenue allowances are established at reasonable levels.

However, for the reasons discussed throughout section 5, we consider that QR’s proposal to increase its revenues by ~**[Redacted]** is clearly inappropriate. The impact of this revenue claim is partly masked by adopting a volume estimate which is at the upper end of a likely range, as will

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<sup>1</sup> Information provided to NHG by QR

become clear if volume forecasts are not achieved and QR seeks to amend the undertaking through the proposed review mechanism.

### **5.3 Asset base roll forward – DAU2 opening asset base**

NHG accepts the standard roll-forward methodology for establishing the opening asset base, and relies on the QCA to verify that the amounts of capital expenditure, depreciation and indexation applied are consistent with the QCA's usual methodologies.

### **5.4 Allocation to coal services of common network asset base**

NHG accepts continuation of the allocation methodology which was approved for AU2.

### **5.5 Allocation of maintenance and operating costs**

NHG accepts continuation of the allocation methodology which was approved for AU2.

### **5.6 WACC**

NHG considers that the WACC proposed by QR is excessive. NHG supports the adoption of approaches to setting the WACC which are consistent with those adopted for AU2. Those approaches were, and must continue to be, based on a consideration of the risks to which QR is exposed. Section 6 discusses why NHG considers that the proposed WACC does not reflect QR's proposed risk profile, and is therefore not appropriate.

### **5.7 Capex, maintenance and operating costs: Overview**

NHG has a number of concerns with QR's proposal, which apply to the proposed capital expenditure program (discussed further in section 5.8), the proposed maintenance cost allowances (discussed further in section 5.9) and proposed operating costs (section 5.10).

These concerns include:

#### **(a) Lack of information**

The information provided by QR (some of which is redacted) is not sufficient to allow NHG or other stakeholders to provide meaningful comments regarding the prudence of the proposed costs. Stakeholders will therefore be heavily reliant on the QCA's assessment of prudence. At this stage, NHG considers there is a real question as to whether, given the level of information provided, stakeholders have been provided with procedural fairness in respect of QR's various cost proposals.

NHG provided an information request to QR on 13<sup>th</sup> December, and met with QR on 19<sup>th</sup> December. Information responding to some of the questions has since been received, but this does not include any additional information relating to the proposed capital expenditure, maintenance costs or operating costs. QR advised, at the meeting of December 13<sup>th</sup>, that much of the information could only be provided following execution of a confidentiality agreement. QR provided a draft agreement on 18<sup>th</sup> January, which included terms which NHG (and its employees in their individual capacity) could not accept. A revised draft has been provided to QR.

#### **(b) Limited meaningful review**

The AECOM review of proposed capital and maintenance costs appears unduly narrow in its scope, with limited projects considered, numerous assumptions made and significant limitations noted. These issues raise serious questions about the utility of AECOM's findings, and the extent to which the findings provide any evidentiary value about the prudence or efficiency of QR's proposed costs.

#### **(c) Excessive costs**



The proposed capital and maintenance programs are proposed to be significantly higher than those applying under AU2, increasing by 127% and 50% respectively, without adequate justification.

## 5.8 Capital Expenditure

### (a) NHG comments

QR's proposed capital program (\$347m) is 127% higher than that approved for AU2 (\$153m). It is reasonable to expect that some of this increase is attributable to supporting the increased volumes during the 2023 DAU period, however, the high-level information provided by QR does not allow stakeholders to appropriately assess the reasonableness of the capital program. Based on the information provided, NHG makes the following comments:

- (i) **Capital approval process:** NHG is concerned that QR may view the approval of the capital indicator as evidence of the prudence and efficiency of the capex program. Our understanding is that the capital indicator is relevant only as a placeholder number for the purposes of developing reference tariffs and does not in any way imply any 'pre-approval' of the scope, standard or efficiency of the projects. If this is not the case (i.e. if approval of the capital indicator implies support for the projects), we ask that the QCA clarifies the position. Meaningful consultation and, in our view, pre-approval of major capex by customers or the QCA (see our proposal in Section 8.6 and drafting in Schedule 2) is necessary to ensure that robust business cases are prepared for these projects. To date there has been no consultation with stakeholders on the projects proposed.
- (ii) **Supporting business cases:** Each capex project should be supported by a thorough business case. QR's Submission fails to provide this supporting evidence. NHG notes the QCA's views published in Section 2 of the QCA's Guideline on Climate change related spending of September 2023. This guideline sets out the QCA's expectations of the inclusions in a robust business case to support assessment of climate change related expenditure, including key requirements for demonstrated need, customer consultation, options considerations and efficient costs. This approach is not limited to climate change related expenditure and would apply equally to other forms of capex, including the West Moreton capital program. While NHG has requested QR to provide the business cases, it is concerned that these business cases will not have adequately addressed each of the expected inclusions described above. NHG considers that business cases must establish the need for these projects, must demonstrate that the options chosen are the best of all available options, and must demonstrate procurement and delivery processes which will result in efficient costs.
- (iii) **Prudence:** The significant capital program should be considered against the backdrop of the life expectancy of the coal mines and proposed accelerated depreciation to ensure that the scope and design life is fit for purpose. The design life of assets such as bridges, tunnels, culverts and earthworks are 50-100 years, which significantly exceeds the mine lives of the coal mines themselves. Alternative design of such assets should be considered with the aim of potentially reducing capital costs.

### (b) AECOM peer review: Capital Expenditure

The AECOM peer review report in Attachment 4 of QR's submission is provided by QR as justification for the prudence of its proposed capital expenditure. NHG notes that substantial elements of this report are redacted and we are unable to provide detailed commentary until such time as an unredacted version is provided. There are numerous parts of that AECOM report which should cause the QCA to question the evidential value of the review and its conclusions.

By way of some select examples:

- (i) AECOM's review assessed projects based on scope, standard and cost. For scope and standards, very few of the projects assessed were identified as having a high level of quality and range of supporting documentation and required a level of professional judgement to support the recommendation. For the cost category, all of the projects assessed were determined as having low documentary evidence and required professional judgement to support the recommendation. On this basis, NHG queries if all the capital projects have been studied to a reasonable level of confidence, including the cost estimates, to enable the QCA to form a view on the capital program.
- (ii) Due to the significant redactions, we are unable to determine which specific projects and values have been assessed. This is particularly relevant for the trackwork segment, which comprises 65% of the overall capital program, with 5 out of 8 projects assessed. NHG expects that additional projects should be reviewed for this discipline given its substantive contribution to the overall capital program.
- (iii) AECOM's review was a desktop assessment.<sup>2</sup> There is clearly a danger in this case that AECOM's assessment on the need for projects and on the selection of projects from among alternatives (if these were provided) were strongly influenced by the information provided by QR.

All of that, together with the limited sample of projects included, means that the AECOM report is hardly conclusive in aspects of prudence of cost or scope of QR's proposed capital expenditure.

Accordingly, and particularly in the context of the capital expenditure having a very high impact on the tariff and the potential for a material change in volume, NHG considers that it is warranted for the QCA to obtain separate impartial technical advice so as to reach an independent and informed view on the prudence of the proposed capital expenditure for the purposes of the capital indicator, while putting in place robust pre-approval processes for each material element of the program.

## **5.9 Maintenance expenditure**

### **(a) NHG comments**

QR's proposed maintenance cost of \$172.5m (\$FY26) is more than 50% higher than the current maintenance allowance despite the extensive capital program being proposed. As with the capital program, the limited high-level information provided by QR does not allow stakeholders to appropriately assess the reasonableness of the maintenance program. Based on the information provided, NHG makes the following comments:

- (i) Allocation methodology: QR proposes a continuation of the fixed/variable allocation methodology applying under AU1 and AU2, per section 2.10.6 of the QR Submission. NHG requests the QCA to consider the alignment of QR's actual allocations with the prior categories identified under AU2.

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<sup>2</sup> AECOM report provided as Attachment 3 to QR's submission, Executive Summary

- (ii) Volume impacts: NHG suggests that operating expenditure allowances should be revisited for material changes in volume which may occur over the AU3 period. This approach would mitigate QR over-recovering maintenance expenditure costs in the event of volume reductions. Determination of an approach to adjusting the allowance (such as a fixed/variable portion) as part of the DAU approval process would assist.
- (iii) Prudence: Currently there is little information upon which stakeholders can base any consideration of the prudence of the maintenance plan and the alternatives that have been considered by QR. Information as to how the maintenance plan is aligned to prior years, interaction of the planned maintenance outages compared to the Master Train Plan and deliverability of capacity over the period is required to assist in this process.
- (iv) Capital program savings: QR proposes a record capital program. NHG has a concern that the maintenance savings reflected in QR's Submission (section 5 of Attachment 6) are based on high level notional percentages and assumptions to determine the avoided maintenance costs. NHG is unable to provide a view on the appropriateness of these assumptions and resulting calculations. For stakeholders to adequately assess the trade-offs between maintenance and capital, it would be expected that an option of continued maintenance would be included as part of a robust business case for capital expenditure.

**(b) AECOM peer review: Maintenance**

The AECOM peer review report in Attachment 7 of QR's submission is provided by QR as justification for the prudence of its proposed maintenance allowance. NHG notes that substantial elements of this report are redacted and is unable to provide specific detailed commentary until such time as an unredacted version is provided by QR. Yet there are numerous parts of that AECOM report which should cause the QCA to question the evidential value of the review.

NHG notes that QR asked AECOM to undertake the peer review *"based on an assessment of whether the current maintenance practices demonstrate prudence (the necessity of the maintenance activities) and efficiency (the optimal delivery of those maintenance activities) as an indicator of whether the proposed costs for the DAU3 period align with these factors."*<sup>3</sup> The approach of assessing current maintenance practices to determine the alignment of future maintenance costs is not appropriate in the context of the significant variance in scope and maintenance cost resulting from increased volumes and also the proposed capital program. NHG submits that a more valid peer review should be undertaken based on a bottom-up approach to determine the appropriateness of the maintenance tasks being proposed.

NHG supports the QCA obtaining separate impartial technical advice so as to reach an independent and informed view on the prudence of the proposed maintenance costs.

**5.10 Operational expenditure**

Section 2.11 of DAU3 explanatory document provided with the QR Submission outlines QR's build-up of operating expenditure. QR proposes operating expenditure of \$85.3m (FY26\$), some 89% higher in real terms than under AU2. The main driver associated with this increase appears to be related to QR's varied approach to forecasting operating costs. The approach is disputed by NHG at a number of levels:

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<sup>3</sup> p. ii AECOM West Moreton Line - Review of Queensland Rail's DAU3 West Moreton Maintenance Submission

- (a) QR claims that AU2 has underestimated long-term costs and despite falling volumes, actual operating costs have remained reasonably consistent. NHG queries the efficiency of QR's operating expenditure in this regard, as it would be reasonably expected that reductions would be evident based on the relatively small coal volumes in recent years.
- (b) QR adopts FY22 as the efficient base year for forecasting future operating expenses. Insufficient justification is provided by QR to demonstrate that FY22 is an appropriate year and that such expenditure incurred is efficient.
- (c) Corporate overhead costs increase 87% from FY22 and network business costs increase 68% from FY22, which is significantly above inflation. There is no detail provided by QR to substantiate this increase nor demonstrate that such expenditure is efficient. If increases are linked to increasing coal volumes, then we would question the consistency of a methodology which treats costs as fixed when coal volumes decline, and variable when they increase.
- (d) Sections of supporting data are redacted, therefore limiting stakeholders' ability to assess certain expenditure elements.

NHG encourages the QCA to thoroughly assess QR's operating expenditure claim and associated methodology. NHG contends that operating expenditure allowances should be revisited for material changes in volume and proposes that a fixed/variable allowance is considered to cater for volume changes over the AU3 period. This approach would mitigate QR over-recovering operating expenditure costs in the event of volume reductions.

## 5.11 Depreciation

NHG understands QR's desire to reduce asset stranding risks by accelerating depreciation, but notes that this reduction in risk is not reflected in QR's WACC proposal (see section 6). The information disclosed by QR is not sufficient for NHG to form any views regarding the equity of QR's proposals, particularly in regard to the proposed additional acceleration of depreciation for new capex, however, we do question:

- QR's assertion that the increase in depreciation charges is 'affordable'. The HoustonKemp analysis of affordability<sup>4</sup> appears to be confined to the increase in depreciation charges, with no regard to the overall increase in proposed tariffs, which we consider unaffordable. NHG cannot comment on the HoustonKemp modelling due to redactions. We note that HoustonKemp values the Wilkie Creek mine, currently under administration, at \$330 million.
- QR's claim that the shortening of the life of new capex ensures that the remaining mines post-2034 will pay only for the service which they are still using. We would expect that the upgrades proposed by QR will continue to be of value to the remaining mines for as long as they continue to operate, through, for example, reduced maintenance costs and operating flexibility created by spare capacity.
- Whether it is appropriate that both existing and new assets be fully depreciated with zero residual value by June 2044 when non-coal use of the system may continue, given that the relevant assets will have remaining lives of up to ~85 years at that time. Continued use of the system past 2044 will, if QR's proposal is accepted, represent a double-recovery and windfall for QR or a 'free ride' for the relevant users of the system.

Given the limited information currently available to NHG on this issue, we rely on the QCA to consider the issue and provide information on which NHG can meaningfully comment in later

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<sup>4</sup> Houston Kemp report for QR "Regulatory Treatment of coal related assets", Section 5

processes.

## 5.12 Two-part tariff

We note that QR has proposed to continue the existing practice of recovering costs via a two-part tariff. NHG disagrees with this approach, which results in NHG's New Acland mine paying higher tariffs per gtk than other mines. We estimate that a blended tariff of around \$32/000gtk represents approximately \$38.50/000gtk for New Acland, and \$27.21/000gtk for Cameby Downs, a premium for New Acland of around 40%. We consider that the vast majority of QR's costs will vary with distance travelled (i.e. the length of the portion of the network which is used). The AT2 tariff, which recovers 50% of QR's revenue, does not vary with distance. Unless 50% of QR's costs are unrelated to distance, which is clearly not a credible estimate, the AT2 tariff is not cost-reflective and therefore represents a subsidy in favour of the more distant mines. We understand that the concept of the 'distance taper' has been applied in a number of networks, including the Central Queensland Coal Network. In other cases, such as ARTC Hunter Valley network, charges for the use of each zone are entirely reflective of the distance travelled (i.e. there is no 'per path' or 'per tonne' element).

If the two-part tariff is to be maintained in its current form, we request that the QCA confirms that Cameby Downs and Wilkie Creek will be each be contributing sufficient revenue to cover at least the full incremental costs of these services, taking into account:

- (i) the revenue contribution (based on the two-part tariff, if this is to be approved);
- (ii) the portion of the RAB attributable to the sections West of Jondaryan.
- (iii) a share of the RAB between Rosewood and Jondaryan, to the extent that expenditure within this section could have been avoided in the absence of services originating at Cameby Downs and Wilkie Creek (including any projects undertaken to facilitate the original entry of these mines);
- (iv) maintenance costs West of Jondaryan.
- (v) an allocation of operating costs; and
- (vi) variable maintenance costs between Rosewood and Jondaryan, attributable to the services from Cameby Downs and Wilkie Creek.

## 5.13 Discount for Private Infrastructure

To comply with an approval condition for the New Acland Stage 3 Project, NHG must construct a spur and balloon loop to the mine site. The spur and balloon loop will be funded by NHG and the cost will not be included within the RAB. Our understanding is that the cost of the Columboola spur and balloon loop is included within QR's RAB (we note that QR states that "coal only sidings/balloon loop" has a RAB value of \$14.5m as at 1 July 2020)<sup>5</sup>. This creates an inequitable outcome in which:

- Tariffs paid by NHG are increased by the inclusion of the Columboola spur and balloon loop in the RAB.
- NHG is solely responsible for the cost of its spur and balloon loop.

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<sup>5</sup> QR submission, Section 2.5.1.

We anticipate that this problem extends to maintenance costs (i.e. Columboola spur and balloon maintenance costs forming part of QR's maintenance claim, while maintenance of the New Acland balloon loop will be funded by NHG).

The QCA has considered this issue in the context of the Central Queensland Coal Network, where the identical problem existed. Older balloon loops are included in the RAB, and newer loops have been funded by individual mines. In that case, a discount for Private Incremental Costs was introduced into the undertaking to address what would otherwise be an inequitable outcome.

We suggest that a similar concept should apply within QR's undertaking. This could be modelled on the Aurizon Network approach, or a simpler approach could be developed. For example, NHG could receive a discount calculated by reference to the impact which the return on and of capital for the Columboola loop, plus maintenance if relevant, has on NHG's access charges. This would then put the access charges of New Acland and Cameby on a consistent basis: with neither mine bearing the costs of the other mine's spur or balloon loop.

We anticipate that the issue raised above also applies to costs associated with the Wilkie Creek siding (i.e. that it is included in the RAB).

#### **5.14 Inflation**

We rely on the QCA to confirm that QR's approach to estimating inflation is consistent with QCA's preferred methodologies.

### **6 WACC**

#### **6.1 Summary of NHG WACC submission**

QR proposes to adopt the same approach to estimating the weighted average cost of capital (WACC) as for AU2, updated for relevant market data and outcomes from the QCA's Rate of Return Review.

NHG considers that, for some WACC parameters, it is appropriate to maintain a consistent approach. In particular, market parameters such as the risk-free rate, market risk premium and gamma should continue to be estimated using orthodox methods as identified by the QCA in its Rate of Return Review.

However, the firm-specific parameters and adjustments adopted in AU2 require reassessment, in light of changes in the risk environment for AU3. Changes to the customer and contract profile on the West Moreton System mean that QR will face a lower degree of systematic risk. To the extent that longer-term stranding risk does remain, it is largely addressed through other elements of the undertaking proposal, particularly QR's proposed approach to depreciation.

These changes to the risk environment mean that the cost of debt uplift allowed for AU2 is no longer justified. This uplift was allowed by the QCA specifically to address short-term uncertainty around approvals for the New Acland Stage 3 mine development. Since this time, New Acland Stage 3 has been granted a mining lease and associated water licence and commenced mining operations in May 2023. While the decision to grant the associated water licence has been challenged in Land Court proceedings, it is anticipated that these proceedings will be completed in the current calendar year. Accordingly the previous uncertainty in relation to the project no longer exists, and therefore the uplift should be removed for the purposes of AU3.

The asset and equity beta should also be reduced to reflect changes in QR's customer profile and its proposed changes to the regulatory arrangements to address longer-term stranding risk. NHG proposes that the asset beta be more closely aligned with the estimated beta for regulated energy

and water businesses, given that QR will now have a risk profile that is more similar to these other regulated businesses.

With these adjustments to the QR proposal, the overall WACC would be 6.16%. NHG considers that this would be more reasonable and reflective of the regulatory and commercial risks involved in the provision of below-rail services on the West Moreton System.

## 6.2 Cost of debt uplift is no longer justified

QR has proposed maintaining the cost of debt uplift that was allowed by the QCA in AU2. The uplift is calculated as the difference between a US BBB-rated corporate bond and a US BB-rated bond – a difference of 150 basis points. In proposing to maintain this uplift, QR claims that it:<sup>6</sup>

*...still faces the same volume uncertainty on the West Moreton line that it faced in AU2, and so there remains a need for an uplift to the benchmark bottom-up WACC. For example, contracts will require resigning during AU3's term.*

NHG acknowledges that, at the time of the AU2 Decision, there were several factors warranting a departure from the QCA's standard methodologies and risk assumptions for the benchmark efficient firm. These included both short-term uncertainty and long-term risk factors that were not addressed through other risk protection mechanisms in AU2.

However the circumstances in which the QCA will be making its decision for AU3 are markedly different – the short-term uncertainty present at the time of the AU2 Decision have been substantially addressed, while longer term risk factors have been addressed through other elements of QR's proposal (particularly the proposed approach to depreciation). The cost of debt uplift is therefore no longer justified.

### The basis for the cost of debt uplift in AU2

In its AU2 Decision the QCA identified two specific sources of risk that it was seeking to address:

- short-term uncertainty due to uncertainty around New Hope's New Acland Stage 3 mine approval; and
- longer-term stranding risk.

The QCA indicated that its cost of debt uplift was specifically to address the short-term uncertainty – it was not intended to address longer-term stranding risk. The QCA explained the basis for the uplift as follows:<sup>7</sup>

*The ongoing uncertainty regarding New Hope's New Acland Stage 3 mine approval highlights the short-term volume risk that West Moreton coal is exposed to. If New Hope does not receive approval, there will be a significant short-term drop in coal volumes railed. While we have approved the use of limited-life loss capitalisation, and Queensland Rail has indicated that the medium- to long-term outlook remains positive, there is no guarantee that third-party investments will be made to restore the volume of coal railed to its recent higher levels. If higher volumes on the West Moreton system fail to materialise, a limited life loss capitalisation account is not an effective means of recovering revenue.*

*In response to short-term uncertainty West Moreton coal faces, we have provided West Moreton coal with an uplift to its estimated debt risk premium that in our view is sufficient; however we do not think that it accounts for West Moreton coal's longer-term stranding risk.*

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<sup>6</sup> QR submission, p 24.

<sup>7</sup> AU2 Decision, p 49.

In considering the appropriate quantum of uplift, the QCA noted in particular the low volumes that were forecast for AU2 and the potential for this to impact credit metrics.<sup>8</sup>

Contrary to what QR now submits, the uplift was not designed to address general volume uncertainty or recontracting risk – an uplift is not necessary to address these general risk factors that affect most infrastructure businesses. Rather, the uplift was directed at a very specific and short-term issue affecting AU2.

In relation to longer-term risks the QCA noted:<sup>9</sup>

*Stranding risk need not be compensated for within the WACC, provided that the underlying regulatory framework or adjustments to the firm's cash flows adequately account for this risk...*

*We consider that an appropriate accelerated depreciation profile would likely be sufficient to address the longer-term stranding risks that West Moreton coal faces. Alongside our adjustment to the debt risk premium to reflect short-term uncertainty, we consider that we have had appropriate regard to the risks West Moreton coal is exposed to.*

QR has now proposed an accelerated depreciation profile for AU3, to address this longer-term stranding risk. While not relevant to how the cost of debt uplift was justified in AU2, NHG considers this protection from longer-term stranding risk is relevant to the QCA's consideration of other elements of the AU3 WACC, particularly the asset / equity beta (discussed below).

#### The temporary cost of debt uplift should now be removed

The short-term uncertainty referred to in the AU2 Decision no longer exists. At the time of the AU2 decision, approvals had not been received for the New Acland Stage 3 project. As noted by QR, NHG has now obtained all final approvals to develop and operate the mine.<sup>10</sup> First railings occurred in October 2023.

To the extent that there is any remaining risk around thirdparty challenges to approvals for the New Acland Stage 3 project, these should not be reflected in the AU3 WACC. There is only one outstanding legal challenge (relating to a water licence) which is expected to be resolved prior to commencement of AU3. In any event, if there were to be any successful challenges to NHG's approvals which led to the project not proceeding, this would trigger a right for QR to review reference tariffs and submit a draft amending undertaking to the QCA under cl 3.2 of Schedule D. Given this mechanism to review reference tariffs in the event of material decline in contracted volumes (which would be triggered if the New Acland Stage 3 project did not proceed), it would not be appropriate to account for this in the WACC for AU3.

The temporary uplift that was allowed in AU2 to account for this short-term uncertainty should therefore be removed. With much higher volumes forecast for AU3, it is appropriate to revert to the QCA's standard methodology for estimating the cost of debt, based on benchmark rates for corporate bonds with a BBB rating.

As explained below, removal of the uplift is also necessary to ensure that the overall WACC is reasonable in light of prevailing market conditions and QR's exposure to systematic risk.

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<sup>8</sup> AU2 Decision, pp 43-45.

<sup>9</sup> AU2 Decision, pp 49-50.

<sup>10</sup> QR submission, p 12.



### 6.3 Asset and equity beta should be brought into line with other regulated businesses

QR proposes an equity beta that is unchanged from AU2 (equity beta of 0.71). The asset beta is then 'back-solved' from this AU2 equity beta value (asset beta of 0.48).<sup>11</sup>

The resulting value for the asset beta is approximately midway between the median asset beta values for:<sup>12</sup>

- a large set of regulated energy and water businesses (a sample of 39 businesses, with a median 10-year asset beta of 0.38, as estimated by HoustonKemp); and
- a very small set of toll road businesses (a sample of just four businesses, with a median 10-year asset beta of 0.58, as estimated by HoustonKemp).

The QR / HoustonKemp approach gives equal weight to the median value for the large energy / water set and the very small toll road set. Across the combined sample, each estimate for a toll road business is effectively given ten times the weight that is given to an energy / water business (due to the energy / water sample being roughly ten times as large).

Neither QR's submission nor the supporting HoustonKemp report provide any substantive justification for this proposal. It is not explained why toll roads are appropriate comparators for the purposes of estimating the AU3 asset / equity beta – or why such a small sample of these businesses should be given the same weight as a much larger set of energy / water businesses.

Since the QCA determined the asset and equity beta for AU2, there have been several important developments:

- first, there have been changes to QR's customer and demand profile, impacting its systematic risk exposure – notably, QR is now forecasting much higher contracted volumes across a broader customer base;
- second, additional risk protection mechanisms have been proposed in AU3 – notably an accelerated depreciation profile to address stranding risk;
- third, the QCA has reviewed and updated its framework for assessment of the asset / equity beta in its Rate of Return Review; and
- finally, the sample of toll road businesses available for beta estimation has become even smaller.<sup>13</sup>

Applying the QCA's framework from the Rate of Return Review and having regard to changes in QR's systematic risk exposure, NHG considers that an equity beta of 0.71 is no longer justified. NHG considers that QR's asset beta should be more closely aligned with the estimated beta for regulated energy / water businesses. If toll roads are to be given any role in the beta estimation, each of the available toll road businesses should be given no more weight than each energy / water business.

#### Systematic risk factors

In the Rate of Return Review, the QCA identified the following general factors that will influence systematic risk:<sup>14</sup>

- customer characteristics, and the responsiveness (or elasticity) of customer demand to changes in domestic economic conditions;

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<sup>11</sup> HoustonKemp, Queensland Rail's Weighted Average Cost of Capital, 16 August 2023, p 9; QR submission, p 19.

<sup>12</sup> HoustonKemp, Queensland Rail's Weighted Average Cost of Capital, 16 August 2023, p 8.

<sup>13</sup> The QCA's sample of toll road businesses has shrunk from four to three, as a result of the delisting of Atlantia Spa.

<sup>14</sup> QCA, Rate of Return Review: Final Report, section 6.5.2.

- revenue protection mechanisms available to the firm, including contractual mechanisms (e.g. take-or-pay) and/or regulatory arrangements (e.g. a revenue cap and/or true-up);
- growth / diversification options; and
- operating leverage.

QR is compared to regulated energy / water businesses and toll roads on each of these factors in the table below. On most factors, QR is much more similar to regulated energy / water businesses than toll roads. In particular, due to the availability of revenue protection mechanisms and the nature of customer demand, QR (like most regulated utility businesses) has relatively limited exposure to fluctuations in domestic economic conditions. Coal volumes and rail access revenues on the West Moreton System (in common with Central Queensland and the Hunter Valley) have shown little or no correlation with the state of the Australian economy.

Factor <sup>15</sup>	Degree of alignment between QR and regulated energy / water businesses	Degree of alignment between QR and toll roads
<p><b>Customer characteristics</b></p> <p>A customer base with relatively inelastic demand for a product or service will be likely to contribute to lower systematic risk.</p> <p>If the service or product is exported, then this will generally limit the level of systematic risk exposure.</p>	<p>Demand for QR below-rail services and energy / water network services are similarly inelastic to changes in domestic economic conditions. For energy / water network services, this is due to the essential nature of these utility services. In the case of QR's West Moreton System, this is because it is largely used to serve commodity export markets.</p>	<p>Demand for toll roads is likely to be much more elastic to changes in economic conditions, compared to demand on QR's West Moreton System. Toll road usage is likely to increase in times of high economic activity and decline in times of weaker activity (e.g. due to less commuter traffic and road freight).</p>
<p><b>Revenue protection mechanisms</b></p> <p>Contracting arrangements allow a firm to maintain a stable revenue profile, even in the midst of a sustained economic shock. Regulatory mechanisms may also stabilise revenue in instances where actual demand deviates from forecast.</p>	<p>Revenue protection mechanisms apply to QR and energy / water network businesses. In the case of QR, these are take-or-pay contracts, typically including relinquishment fees for termination. In the case of energy / water network businesses, similar protection is provided by regulated revenue cap mechanisms (with adjustment for unders / overs).</p>	<p>Toll roads typically do not have similar revenue protection mechanisms. Toll revenue is received on a per-use basis, rather than under take-or-pay contracts. Toll roads in Australia are also not protected by regulated revenue cap mechanisms.</p>
<p><b>Growth options</b></p> <p>Growth options (ability to expand service territory or product range) can have an impact on the systematic risk of a business, particularly when the growth option has a different risk profile to the firm's regulated activities</p>	<p>Growth options are similarly limited for QR and regulated energy / water network businesses – in part due to regulatory constraints (e.g. ringfencing rules and licence constraints).</p>	<p>Toll road operators are likely to have more options for growth – particularly through territorial expansion.</p>
<p><b>Operating leverage and pricing structure</b></p> <p>Firms that have a high level of operating leverage (high proportion of operating costs that are fixed) will find it difficult to cut costs in the event of an economic downturn, in response to a potential reduction in demand from customers.</p>	<p>Regulated energy / water network businesses will have varying degrees of operating leverage. If anything, QR's operating leverage may be lower than some of these businesses, as demonstrated by the variability of operating costs between AU2 and AU3, in response to increased volumes.</p>	<p>Toll roads are likely to have very high operating leverage – toll road operating costs will be largely invariant to traffic volumes.</p> <p>By contrast, QR's operating costs appear to vary with volumes. QR's operating expenditure proposed for AU3 is 89 per cent higher per annum in real terms than the annual operating expenditure allowance</p>

<sup>15</sup> QCA, Rate of Return Review: Final Report, p 67.

Factor <sup>15</sup>	Degree of alignment between QR and regulated energy / water businesses	Degree of alignment between QR and toll roads
		included in AU2, due to coal volume increases on the West Moreton System. <sup>16</sup>

### The appropriate asset and equity beta for AU3

For reasons outlined above, NHG considers that the most relevant comparator businesses for setting the AU3 asset beta are regulated energy and water businesses. QR is similar to these businesses on each of the risk factors identified by the QCA in its Rate of Return Review.

HoustonKemp estimates the median 10-year asset beta for the QCA's energy / water business set to be **0.38**. NHG considers that this represents an appropriate benchmark for the AU3 asset beta.

Given lower systematic risk exposure in AU3, it is no longer appropriate to give equal weight to asset beta estimates from a small set of toll road businesses. If toll roads are to be given any role in the beta estimation, each of the available toll road businesses should be given no more weight than each energy / water business in overall sample.

### **6.4 Market parameters should reflect the QCA's orthodox methods**

NHG notes that the QCA has reviewed its methodologies for estimating market parameters in considerable detail in the Rate of Return Review. NHG would support the QCA applying these orthodox and well-tested methodologies in determining the WACC for AU3.

In this submission, NHG adopts the QCA's position on the market risk premium (**MRP**), gamma and debt-raising costs. NHG also supports use of the QCA's standard methodologies for estimating time-variant parameters.

NHG notes that QR's proposal includes 'indicative' estimates for time-variant parameters (risk-free rate and cost of debt), noting that these will be updated closer to the time of the AU2 decision.<sup>17</sup> QR's proposal does not indicate whether or how averaging periods have been selected for determining final parameter values. However NHG expects that this would be done well in advance of the averaging period commencing, in accordance with the process set out in the Rate of Return Final Report.<sup>18</sup> For the purposes of this submission, NHG has adopted the indicative values for these time-variant parameters.

In relation to the cost of debt, NHG notes that QR has not proposed a mechanism for updating revenue requirements within the AU3 period to reflect annual updates to the trailing average. In the Rate of Return Review, the QCA noted that annual update mechanisms should be considered on a case-by-case basis.<sup>19</sup> If QR proposes a mechanism for updating revenue allowances within the AU3 period, NHG will consider and address this in further submissions.

<sup>16</sup> QR submission, p 46.

<sup>17</sup> HoustonKemp, Queensland Rail's Weighted Average Cost of Capital, 16 August 2023, pp 5, 9-10.

<sup>18</sup> QCA, Rate of Return Review: Final Report, p 85.

<sup>19</sup> QCA, Rate of Return Review: Final Report, p 47.

## 6.5 Top-down assessment

### A reasonable rate of return for AU3

NHG's position on the appropriate rate of return for AU3 is set out in the table below, compared to the QR proposal. For reasons explained above, NHG proposes to remove the cost of debt uplift and reduce the asset beta to align with more comparable regulated energy / water businesses.

Parameter	QR proposal	NHG position
Risk-free rate	3.37%*	3.37%*
Gearing	40%	40%
Market risk premium	6.50%	6.50%
Asset beta	0.48	0.38
Equity beta <sup>20</sup>	0.71	0.55
Cost of equity	8.02%	6.97%
Debt beta	0.12	0.12
Benchmark credit rating	BBB	BBB
Cost of debt (including debt financing costs)	4.95%*	4.95%*
Cost of debt uplift	1.50%	-
Corporate tax rate	30%	30%
Gamma	0.484	0.484
<b>WACC</b>	<b>7.39%</b>	<b>6.16%</b>

\* Indicative values for the risk-free rate and cost of debt, as estimated by HoustonKemp. NHG understands these will be updated in the QCA's final decision.

### Comparison with other infrastructure businesses

NHG has undertaken a high-level review of its position and the QR proposal against normalised WACC values for a selection of Australian regulated infrastructure businesses. The sample includes regulated energy and water businesses (given their similar risk profiles), rail network businesses (to the extent that these have regulated WACCs) and the national broadband network (**NBN**).

A relatively simple form of normalisation has been applied, involving:

- application of time variant parameters (risk-free rate and cost of debt) from QR's proposal (these are substituted for the relevant time-variant parameters in each regulatory determination);
- use of gearing, asset beta and MRP assumptions as per the relevant regulatory determination. Where an asset beta value is not stated, this is calculated by de-levering the stated equity beta; and
- levering each asset beta based on QR's gearing of 40%, applying the Brealey-Myers levering formula set out in the Rate of Return Final Report.

<sup>20</sup> Equity beta is calculated based on the proposed asset beta, debt beta of 0.12 and gearing of 40%, applying the Brealey-Myers levering formula set out in the Rate of Return Final Report (p 79).

NHG notes that there are limitations to this comparison, particularly in relation to the rail and NBN benchmarks:

- For the Hunter Valley Coal Network, the ACCC's most recent decision does not provide a view on the appropriate WACC parameters. Rather, the WACC for this network reflects a negotiated outcome – with the main user group supporting this as part of a broader package of commitments from the network operator, ARTC.<sup>21</sup> Moreover, this negotiated WACC is expressed on a pre-tax basis and cannot be normalised because individual parameters are not specified – a comparable post-tax WACC would be lower.
- Similarly, the WACC for NBN was accepted by the ACCC as part of a broader package of commitments, notwithstanding some reservations regarding the WACC estimate. The ACCC identified some deficiencies in NBN's WACC methodology, particularly its selection of comparator businesses. The ACCC nonetheless accepted the NBN proposal because the WACC was unlikely to have a material impact in the initial regulatory period, noting that it would be more closely reviewed in future periods.<sup>22</sup>
- The WA rail networks each have very different risk profiles. NHG considers that at least Arc Infrastructure and Pilbara Infrastructure are not comparable with the West Moreton System, in terms of their exposure to systematic risk. This is reflected in the fact that the beta values for these networks are benchmarked against North American railroads, which the QCA considers are not appropriate comparators for the QR West Moreton System. The QCA has previously noted that North American railroads will have higher systematic risk exposure, because they operate in an environment where underlying demand is responsive to the state of the economy, with limited mechanisms to buffer revenues in the event of an economic shock.<sup>23</sup>

Given these limitations of the rail and NBN benchmarks, the most reliable and relevant comparators are the regulated energy and water businesses.

The comparison of normalised WACC values is set out in **Figure 1**. It can be seen that the NHG adjusted WACC of 6.16% sits comfortably within the range of normalised values, and slightly above most of the energy and water business comparators. The QR proposal sits at the top of the range, with only the non-comparable WA networks having higher values.

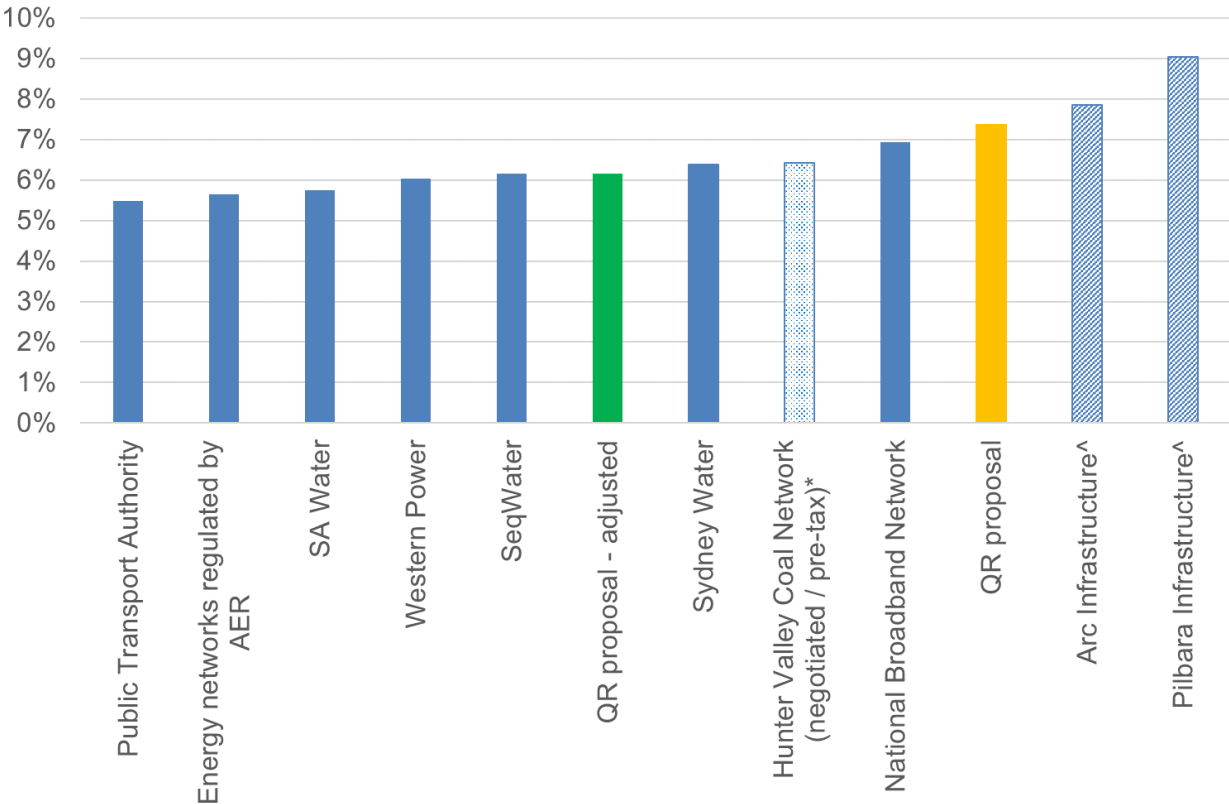
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<sup>21</sup> ACCC, Final Decision: Australian Rail Track Corporation's March 2021 variation to the Hunter Valley Coal Network Access Undertaking, 2 June 2021

<sup>22</sup> ACCC, Proposed variation to the NBN Co Special Access Undertaking: Final Decision, October 2023, p 32.

<sup>23</sup> QCA, Draft Decision: Queensland Rail's 2020 Draft Access Undertaking, April 2019, p 28 and Appendix A.

**Figure 1: Normalised WACC values for selected infrastructure businesses**



\* WACC for the Hunter Valley Coal Network is a negotiated pre-tax value, and is therefore not directly comparable.

^ WACCs for Arc and Pilbara Infrastructure reflect different risk profiles, as reflected in the ERA's use of North American railroads for beta estimation.

**7 Metropolitan System reference tariffs**

NHG supports the continuation of the 'proxy' methodology for the development of the Metropolitan system reference tariffs.

Our understanding is that the QCA's intention, as set out on pages 173 and 174 of the June 2016 Decision, was that the AU2 Metropolitan tariff would reflect the AU1 tariff escalated by CPI, plus allowance for any coal-specific investment within the Metropolitan system (which QR has advised is nil). QR's proposal seems to reflect this approach.

**8 Access Undertaking Drafting**

**8.1 Approach**

NHG acknowledges that, consistent with its stated intention, QR's approach has been to only seek incremental changes from its current undertaking (AU2) on an exceptions basis.<sup>24</sup>

NHG has taken a similar approach. While AU2 is not perfect from NHG's perspective, NHG appreciates that the Queensland Competition Authority (QCA) has determined that it is appropriate. Accordingly, NHG has not sought to reargue every point that was the subject of submissions during the AU2 consideration process. Rather, it has focused its comments on:

<sup>24</sup> QR DAU3 Explanatory Document, 3.

- (a) QR's proposed amendments that it does not consider are appropriate or justified on an exceptions basis; and
- (b) incremental changes which it considers are appropriate and justified even on an exception basis.

## 8.2 Independent Capacity Assessment

QR's forecast volumes for the West Moreton system are at 9.6 mtpa for most of the AU3 term.<sup>25</sup>

QR has also proposed a significant capital expenditure program, which it submits is *'required to allow 9.6 mtpa to traverse the network by assisting to reduce operational risk, optimise maintenance costs and increase the confidence of the supply chain to deliver full coal railing demand'*.<sup>26</sup>

Yet QR has proposed no regulatory controls or protections for users to determine:

- The existing capacity of the system
- Whether the proposed capital expenditure projects will deliver 9.6mtpa of capacity.
- Whether the proposed projects are the most efficient for delivering the required capacity.

NHG submits that, given the magnitude of the capital expenditure that QR is proposing, it should be difficult for the QCA to be satisfied that such capital expenditure is prudent unless there is an independent assessment of these matters.

NHG notes that the QCA has considered such a system appropriate in the context of the Central Queensland Coal Network.

NHG submits that the need for such a system is actually more pressing in respect of West Moreton system as:

- (a) QR has less developed capacity modelling techniques relative to Aurizon Network;
- (b) the smaller number of producers utilising the West Moreton system mean that any shortfall of capacity impacts very significantly on individual producers (relative to the Aurizon Network system with a much larger volume of users such that the shortfall is likely to be spread more broadly); and
- (c) QR is proposing significant capital expenditure (and seeking material increases in reference tariffs) on the basis of delivering increased capacity.

According, NHG submits that drafting akin to that in clause 7A of Aurizon Network's UT5 should be introduced.

## 8.3 Loss capitalisation

It is extremely difficult to make informed submissions on QR's proposed amendments to this section (Schedule D, clause 8), where QR's submissions note that it is making separate submissions regarding the loss capitalisation volume trigger in AU2 and has not dealt with loss capitalisation recovery in AU3.<sup>27</sup>

However, on the limited information available, the partial deletion proposed by QR is not appropriate.

Either:

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<sup>25</sup> QR DAU3 Explanatory Document, 4.

<sup>26</sup> QR DAU3 Explanatory Document 26.

<sup>27</sup> QR DAU3 Explanatory Document, 55.



- (a) the entire loss capitalisation account will have been repaid during AU2 – such that the loss capitalisation provisions could be entirely deleted from DAU3; or
- (b) there is a remaining loss capitalisation account value to be recovered during the period of AU3 – such that that loss capitalisation provision should provide for the methodology of recovery provided for by the QCA.
- (c) In either case, seeking to partially retain the provisions as QR's drafted amendments propose is not appropriate.

We also note that the AU3 tariff may need to be set at an affordable level which is below a Ceiling Reference Tariff derived from the building block methodology (as discussed in Section 5.1). In this case, drafting will be required which is similar to AU2: allowing for additions to the balance of the Loss Capitalisation Account during the term.

NHG will provide substantive submissions on loss capitalisation following QR's AU2 submissions.

#### **8.4 Volume Trigger for Review of Reference Tariff**

The proposed new review mechanism (Schedule D, clause 3.2) is designed to immunise QR from changes in volume.

According to QR's submissions it is designed to trigger on the non-renewal of an access agreement.<sup>28</sup> However it is drafted more broadly to trigger on any reason for QR believing the annual contracted tonnages will fall below 7.5mtpa (such that it is also protects QR from any circumstances involving early termination).

In effect this transfers the volume risk of each producer onto the other producers rather than QR.

NHG notes that this provides a material reduction in QR's volume risk from the regulatory arrangements which exist under AU2, such that if this was to be accepted by the QCA as being appropriate, there should be a corresponding reduction in the asset beta. As a result it would clearly be inappropriate to simply adopt the equity beta from the AU2 decision as QR proposes to.

For further detailed submissions relevant to this point, please see section 6 of this submission.

If this clause was to be accepted, it is critical that the QCA is the final arbiter of the changes to the undertaking which are appropriate at the time. Given that the circumstances in which the trigger might apply are unknown, NHG would not support a clause where the adjustment to reference tariffs was simply a formulaic one where the existing revenue was simply socialised across the remaining tonnage (without consideration of matters like changes that should occur to capex and opex with the change in volume, affordability, loss capitalisation, and other matters going to appropriateness and efficiency in the changed circumstances). However, NHG considers that the current drafting would give the QCA sufficient ambit to consider appropriateness in that wholistic manner.

In the case where Schedule D, clause 3.2 has triggered and has resulted in amendments to the undertaking to reflect reduced volumes, we consider it critical that a further review should apply, if volumes subsequently recover to a level above the volumes which were forecast for the purposes of the review. Drafting suggestions for this additional review trigger are provided in Schedule 2 of this submission.

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<sup>28</sup> QR DAU3 Explanatory Document, 30.

## 8.5 Renewal rights

NHG acknowledges that the only change QR has made to the renewal provisions under section 2.10 is to limit renewal to only applying to access rights which were granted prior to the commencement date of AU3, which would not adversely impact on NHG.

However, NHG submits that, given the existing users will bear the burden of repaying the loss capitalisation and, if QR's proposals regarding accelerated depreciation are accepted, are likely to be providing QR with the vast majority of its return on and of capital, they should be granted stronger renewal rights than are provided for in AU2.

In particular, it is submitted that 2.10(c)(i) and (iii) should be deleted, such that existing users continue to have renewal rights irrespective of whether they have exercised such renewal rights before.

NHG considers such an approach is justified because:

- (a) where existing users have borne the economic burden of the continued operation of the network, they should have the ability to continue to have access for as long as is supported by their mine life (rather than having to make a one-off guess at remaining mine life at the point of renewal – which is the practical impact of the current AU2/DAU3 approach); and
- (b) it would be an inefficient outcome for an existing user's mine with remaining economic mine life to be replaced on the network by a new user's project, thereby effectively sterilising resources which can be extracted without significant new capital investment.

## 8.6 Approval of capital expenditure

Given the very significant capital expenditure program which is proposed by QR, and the lack of information on that program which is currently available, NHG considers that the undertaking should clarify the need for QR to:

- Consult meaningfully with customers before committing to significant projects, including by conducting a customer vote.
- Prepare robust business cases which demonstrate the need for projects and how a particular scope has been selected as the optimal method of addressing that need.
- Where customers do not support a proposed project, seek pre-approval from the QCA.

Our proposed drafting to address the above requirements is provided in Schedule 2.

## 8.7 Capital expenditure true-up

As was noted above, QR's proposed capital expenditure program is significant. We consider that there is a significant risk that actual expenditure will vary significantly (up or down) from the estimated costs. AU2 and DAU3 provide for a true-up of variances between forecast and actual capex over the term of the undertaking, with the true-up adjustment being spread over the term of the following undertaking (ending up to 10 years after the commencement of the term of AU3). We consider that, where variances between forecast and actual capex are material, an earlier true-up is appropriate, to avoid either QR or customers suffering cashflow impacts and potentially creating winners and losers within the customer group as relative volumes change. Our proposed drafting is provided in Schedule 2.

## 8.8 Other comments on QR's proposed amendments to the Access Undertaking

Clause	Issue / Concern	Comments / Proposed Amendments
2.6	Alternate Access Applications	<p>No substantive concerns. We agree with QR's assessment that the drafting changes do not substantively alter the application of the provision.</p> <p>For consistency with the change in terminology proposed, the remaining reference to 'Competing Access Seeker' in 2.6(c)(iv) should presumably be amended to 'Alternate Access Holder'</p>
2.9	Queuing	<p>No substantive concerns. We agree with QR's assessment that the drafting changes do not substantively alter the application of the provision.</p> <p>It is suggested the following minor amendments should be made:</p> <p>2.9.2(a) – 'tsk' should be amended to 'task'</p> <p>2.9.2(b) – 'collective' should be 'collectively'</p> <p>2.9.5(b)(vi) – delete 'comply'</p> <p>At least on the compare version reviewed, cross referencing needs to be updated to accommodate the changes made</p>
2.10	Renewals	See detailed submissions in section NHG of this submission above.
2.11.1	Access Rights granted under Access Agreements	No substantive concerns as this is the previous clause 2.9.1 moved but with the wording unchanged.
5.1.1	Quarterly report – timing and sign off	No substantive concerns with the delayed timing for production of the report or change in QR personnel responsible for sign-off
5.1.2	Quarterly report – content	<p>NHG is opposed to the proposed deletions of:</p> <ul style="list-style-type: none"> <li>the reporting requirements regarding the number of times a decision was made to deviate from a Daily Train Plan if it is reasonably necessary to do so to remedy, mitigate or avoid the operation of network congestion; and</li> <li>the reporting requirements on ad hoc possession start times, end times, number and duration.</li> </ul> <p>Where the network is anticipated to become more congested during the period of AU3 than it has previously been, it would seem reporting obligations of this nature are needed more than ever to provide transparency as to whether QR is actually able to provide the capacity which has been contracted and which has been used as the basis for QR's significant capex, or is not delivering the capacity due to possessions and variations.</p> <p>It is not obvious to NHG that ad hoc possessions only have a minor effect on delays as QR suggests.</p> <p>The only circumstance in which NHG would consider that such a KPI may not be necessary is if an independent capacity assessment was undertaken and reported upon as is required under the Aurizon Access Undertaking (UT5). As</p>

		noted in section NHG of this submission above, NHG considers that would be appropriate in the circumstances.
6.3*	New declaration	No substantive concerns with this deletion given the period of the existing declaration made by the Treasurer in respect of the parts of the QR rail network that remain declared extends beyond the anticipated term of AU3
7	Definitions	<p>The revised definition of Network needs to be refined to reflect the fact that it needs to refer to infrastructure the use of which forms part of the declared service – otherwise the definition does not operate as intended in relation to more granular pieces of infrastructure. This requires changing 'the use of which is' to 'the use of which is, or forms part of,'</p> <p>The weighted average cost of capital referenced in the definition of WACC is considered inappropriately high. For further detailed submissions relevant to this point, please see section NHG of this submission.</p> <p>The definition “First Escalation Date” needs to be updated to 1 July 2025.</p>
Sch D, 3.1(e)	Reference tariff	The weighted average cost of capital referenced in the definition of WACC is considered inappropriately high. For further detailed submissions relevant to this point, please see section NHG of this submission.
Sch D, 3.2	Review of Reference Tariff	See detailed submissions in section NHG of this submission above.
Sch D, 4(f)	Ceiling Revenue Limit	<p>NHG opposes the proposed Ceiling Revenue Limits for the same reasons it opposes the proposed Reference Tariff which is based on those Ceiling Revenue Limits.</p> <p>For further detailed submissions relevant to this point, please see section NHG of this submission.</p>
Sch D, 8	Loss Capitalisation	See detailed submissions in section NHG of this submission above.
Sch F	Network Management Principles	<p>NHG opposes the deletion of the disputes regime which prevents a possession (other than an Emergency or Urgent Possession) proceeding if it is the subject of an unresolved bona fide dispute.</p> <p>While QR suggests it is unprecedented, it needs to be recognised that the West Moreton system is a unique system which currently has only three users, rather than the multi-user systems with numerous operators. It is also a system which has been beset by possessions in recent times, and where QR is proposing very significant capital expenditure, partly to remove the need for such possessions.</p> <p>If QR considers the dispute regime is preventing appropriate possessions proceedings or imposing additional cost, NHG suggests that that should instead be managed through shorter time frames for commencing disputes and a streamlined dispute process rather than removal of the dispute process.</p> <p>NHG does not oppose the other changes described in Schedule F.</p> <p>For completeness:</p> <ul style="list-style-type: none"> <li>in section 3(f) of this Schedule where the reference to 'Network Controller' was deleted it should presumably be replaced with Network</li> </ul>

		Control Officer as has occurred in other clauses; and <ul style="list-style-type: none"> <li>in section 3(i) of this Schedule the reference to "Network Controllers" should be deleted, as Network Control Officer has been added to replace it.</li> </ul>
Sch G	Operating Requirements Manual (ORM)	NHG defers to the views of operators on the on the changes to the ORM, particularly Aurizon Operations as the only current operator on the West Moreton system.  From the perspective of a coal producer / user of the QR access service there is not anything that is evidently problematic in the changes proposed to this schedule.

\* clause reference is to a clause in AU2 which has now been deleted

## 9 Standard Access Agreement

A robust SAA is essential to ensuring that access rights and the process for contracting those rights is sufficiently certain to promote an efficient and competitive system.

As noted by the QCA in previous decisions, the SAA facilitates the timely development of access agreements by providing 'a safe harbour' access agreement which the parties can adopt without the need for further negotiation, or which parties can use as a guide when negotiating alternative terms of access.

NHG commends the approach adopted by QR of making minimal amendments to the SAA given the rigorous and recent review conducted as part of previous processes. There are however concerns regarding the proposed SAA, discussed below:

Clause	Issue / Concern	Comments / Proposed Amendments
16.1(b)	More onerous insurance requirements for Operator's Associates, agents, consultants, contractors and subcontractors.  The concern for producers is that any more onerous insurance requirements might impose additional costs	NHG has no concerns with QR's rationale of seeking for such entities to contract their own insurance rather than the previous requirement to be covered by the Operator's insurance policy <sup>29</sup> (at least where it was problematic).  However, the proposed QR amendments appear to go further than that and extend the insurance requirement for such entities to types of insurance beyond that covered by the wording of the previous standard access agreement (which were just the insurances in paragraphs (iv) and (vi) rather than all policies referred to in clause 16).  NHG also suggests that it might be preferable for the Operator's insurance to be able to cover such entities were that is more economic or efficient (such that the obligation for such entities to obtain separate cover only

<sup>29</sup> QR DAU3 Explanatory Document, 66.

		<p>applies to the extent they are not covered by the Operator's insurance).</p> <p>While NHG considers that Aurizon Operations (as the entity closest to what these requirements may mean in practice should be requested to specifically provide submissions on this change), NHG's suggested amendments to the proposed clause 16.1(b) are:</p> <p><i>The Operator must ensure that, to the extent not covered in the public liability policy or other appropriate insurance policy of the Operator, each of the Operator's Associates, agents, consultants, contractors and their subcontractors take out and maintain insurance referred to in this clause 16.1(a)(iv) and (vi), to at least the coverage level specified in paragraph (iv) (as applicable) or otherwise reasonable sufficient to protect the interests of these Associates, agents, consultants, contractors and their subcontractors as the case may be).</i></p>
22.1	<p>Broadening of QR rights to assign</p> <p>The concern is that the proposed drafting permits assignments in inappropriate circumstances.</p>	<p>NHG has no concerns with QR's rationale of being able to assign an access agreement in circumstances where QR ceases to have a right to operate the network.<sup>30</sup></p> <p>However, the proposed QR amendments appear to go further than that. In particular the drafting proposed permits assignments in inappropriate circumstances (such as where the parts of the network for which operatorship have changed are not relevant to the access rights under the agreement or it is not actually certain that operatorship has changed).</p> <p>NHG's suggested amendments to the proposed clause 22.1(a) are:</p> <p><i>If Queensland Rail <del>will no longer have or expected to no longer have</del> a right to operate the Network or any part of the Network relevant to providing the Access Rights under this Agreement it may Assign all or part of its rights or obligations under this agreement corresponding to the parts of the Access Rights which Queensland Rail can no longer provide to an Assignee who:</i></p> <p><i>(i) will have the right to operate the relevant parts of the Network; and</i></p> <p><i>(ii) has the expertise, the financial resources and other relevant resources to enable it to provide the relevant Access Rights,</i></p> <p><i>without the prior consent of the other Parties, provided that Queensland Rail procures the Assignee to covenant by deed with the other</i></p>

<sup>30</sup> QR DAU3 Explanatory Document, 66

		<i>Parties to provide the Access Rights to the extent of the rights and obligations Assigned to the Assignee.</i>
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**10 Conclusion**

For the reasons set out in this submission, NHG consider that the 2023 DAU as submitted by QR is clearly not appropriate to approve where proper regard is had to the matters in section 138(2) QCA Act.

## Schedule 1 - Response to QCA “Topics for Stakeholder Comments”

	QCA Notice Topic	Section(s) in NHG Submission
1.	the negotiation framework and pricing rules, which establish the process and requirements for negotiating prices and other terms to access the declared service (DAU3, Parts 2 and 3)	No concerns
2.	changes to the provisions associated with mutually exclusive access applications (the ‘queuing mechanism’) (DAU3, clause 2.92)	No substantive concerns: see section 8.6
3.	the reporting regime, having regard to experience with the reporting prescribed in the 2020 undertaking (DAU3, Part 5)	Various concerns: section 8.6
4.	changes to Queensland Rail’s quarterly reporting deadlines and obligations (DAU3, clauses 5.1.1–5.1.2)	No substantive concerns: see section 8.6
5.	changes to the processes after a dispute on a planned possession or an ad hoc possession proposed by Queensland Rail (DAU3, Schedule F, clause 2.4)	Various concerns: section 8.6
6.	the West Moreton reference tariff approach, including: a. the proposed capital and maintenance programs and the associated allocation of volume risk to Queensland Rail, access holders and seekers (DAU3 explanatory document, sections 2.4 and 2.7) b. the proposal for accelerated depreciation and the extent to which the proposed rate of return is commensurate with the regulatory and commercial risks involved in providing the declared service (DAU3 explanatory document, sections 2.6 and 2.8) c. anticipated operating, maintenance, and capital costs that might result from changes in volumes (DAU3 explanatory document, sections 2.7, 2.10–2.11).	QR proposals are inappropriate and unaffordable: see Sections 5 and 6



## Schedule 2 - NHG Proposed Drafting Changes to Schedules D and E

*Amend clause 3.2 of Schedule D so that if the AU is amended following volume falling below the volume trigger, it is reviewed again if volumes return to above the volume trigger or there is otherwise a material increase in volume. This is important in order to be able to socialise the revenue requirement across the higher volume and thereby reduce the tariff payable*

### 3.2 Review of Reference Tariff

(a) If at any point Queensland Rail, based on its contracted volumes, reasonably believes the annual aggregate contracted coal tonnages for Tariff Train Services (excluding Ad Hoc Train Services and Additional Train Services as defined in the Standard Access Agreement) for a Year during the Term will:

(i) be below 7.5 million tonnes; or

(ii) where clause 3.2(a)(i) has previously applied, either return to being equal to or greater than 7.5 million tonnes or otherwise increase by more than 1 million tonnes from the forecast adopted when this clause 3.2 was last applied,

then Queensland Rail must undertake a review of the Reference Tariff and submit a draft amending access undertaking to the QCA setting out the outcomes of that review (including of any consultation with stakeholders) and Queensland Rail's proposed amendments

(b) For the purposes of **clause 3.2(a)**:

(i) a draft amending access undertaking submitted under clause 3.2(a) will be treated as if it were submitted in response to an initial amendment notice given by the QCA under the QCA Act; and

(ii) Queensland Rail and the QCA will act in accordance with the provisions of the QCA Act as though this were the case.

(c) Where an amendment to the Reference Tariff is given effect through an amendment to this Undertaking in accordance with this **clause 3.2** and the QCA Act, the QCA may determine that matter will be applicable or effective from a date prior to the QCA's approval of the relevant amendment. If the QCA makes such a determination, **clause 6** and any other provisions of this Undertaking relating to Adjustment Charges will apply, as applicable, in relation to the amendment to the Reference Tariff.

*Amending clause 2 of Schedule E to require seeking customer acceptance for capital expenditure projects above a certain threshold value, to seek to provide greater transparency and rigour to the acceptance of capex than is possible based on the limited information QR has been willing to provide to date on its capital projects.*

## **Approval of capital expenditure**

### **2.1 Requirements for acceptance of capital expenditure into the Regulatory Asset Base**

- (a) The QCA will accept capital expenditure into a Regulatory Asset Base if that capital expenditure:
- (i) is or has been accepted by the West Moreton Users in accordance with **clause 2.3** (where a project will be considered as having been accepted if the project as delivered does not vary materially in scope, standard or cost from the project as accepted by West Moreton Users) or is or has been accepted by the QCA as:
    - (A) prudent in scope in accordance with **clause 3**;
    - (B) prudent in the standard of works in accordance with **clause 4**; and
    - (C) prudent in cost in accordance with **clause 5**; and

....

### **2.2 Assessing prudence of capital expenditure**

For the purposes of **clauses 3, 4 and 5**:

- (a) the QCA:
- (i) in assessing whether capital expenditure is prudent:
    - (A) ....
    - (B) must consider any non-acceptance by West Moreton Users of the relevant capital expenditure project and any reasoning provided by each West Moreton User for their vote for acceptance or non-acceptance; and
    - ~~(B)(C)~~ may, as it considers necessary...

### **2.3 Seeking customer acceptance of capital expenditure**

- (a) Queensland Rail must seek acceptance by the West Moreton Users under this **clause 2.3** for:
- (i) any capital expenditure project within the West Moreton System anticipated to cost \$[Note: NHG suggests a threshold of \$3-5m, but we note that the definition of a project will need to be addressed, to prevent disaggregation of expenditure which should be considered a single project into components] million or more (other than any capital expenditure incurred in response to an emergency) whether that cost is to be incurred in a single year, or over multiple years; or
  - (ii) any capital expenditure project that has previously been accepted by West Moreton Users under this **clause 2.3** which either:
    - (A) has undergone a material change to the scope, standard or costs; or
    - (B) is to be commenced more than 2 years after the date that capital expenditure project was previously accepted.

- (b) In order to seek acceptance by the West Moreton Users of a capital expenditure project, Queensland Rail must at least 3 months prior to any funds (other than study costs) being committed to a capital expenditure project of the type described in clause 2.3(a):
- (i) make available to West Moreton Users information on the relevant capital expenditure project which is material for assessing the prudence in the scope, standard of works and cost of the capital expenditure project, to a similar level of detail intended to be provided to the QCA when seeking acceptance of prudence (provided that Queensland Rail may require a West Moreton User to sign a confidentiality agreement on reasonable terms prior to providing it with any commercially sensitive information under this **clause 2.3**).
  - (ii) schedule a meeting with the West Moreton Users to discuss the capital expenditure project; and
- (c) Queensland Rail is permitted to seek acceptance of multiple capital expenditure projects at the same time (and combine the information provided and meeting held for the purposes of **clause 2.3(b)** for each project), but where that occurs each such capital expenditure project will be voted on separately.
- (d) During the Voting Period:
- (i) Queensland Rail must use reasonable endeavours to provide further information and engage in discussions with West Moreton Users where reasonably requested by a West Moreton User; and
  - (ii) each West Moreton User is to notify Queensland Rail of whether they accept or do not accept as prudent the capital expenditure project (and any failure to notify either such vote within the Voting Period, will result in that West Moreton User being deemed to have accepted the capital expenditure project as prudent).
- (e) If a West Moreton User votes:
- (i) to not accept a capital expenditure project as prudent, it must provide its reasons for the vote so that the QCA may understand its reasons;
  - (ii) to accept a capital expenditure project as prudent, it may, but is not required to, provide any reasons for its decision.
- (f) The capital expenditure project will be considered to be accepted as prudent by the West Moreton Users for the purposes of **clause 2.1(a)(i)** if it is approved or deemed approved by a majority by number of West Moreton Users which in aggregate also hold at least 60% of the votes.
- (g) On a vote occurring under this **clause 2.3**, each West Moreton User has the number of votes equal to the aggregate Train Paths they have contracted on the West Moreton System across the next 5 Years after the Year in which the vote is occurring, subject to also including any Train Paths that are reasonably likely to be renewed or reapplied for before their expiry.
- (h) Queensland Rail must notify each of the West Moreton Users of the results of the vote for each capital expenditure project within five (5) Business Days after Queensland Rail has determined those results.
- (i) A vote resulting in non-acceptance does not prevent Queensland Rail from:
- (i) proceeding with a capital expenditure project prior; and/or
  - (ii) seeking the QCA's acceptance of the same capital expenditure.
- (j) For the purposes of this clause:
- (i) **Voting Period** means:

- (A) the period specified by Queensland Rail when providing information to West Moreton Users seeking acceptance, which must be at least six weeks after the first information is given; or
- (B) such longer period as Queensland Rail and the West Moreton Users agree.
- (ii) **West Moreton Users** means each Access Holder that has contracted Access Rights on the West Moreton System, provided that where the Access Holder is an Operator the relevant Customer will be considered the West Moreton User not the Operator.

*Insert a new clause 7 of Schedule E (as per below) to provide for an annual reconciliation of capex and amend the previous clause 7 of Schedule E (Capital Expenditure Carryover Account) and replace it with the following – so that if there is a material underspend or overspend of capex, this results in a more proximate reduction in tariff rather than awaiting the end of the term. It is designed to be similar to clause 5 Schedule E of the Aurizon Network UT5 access undertaking, but with adjustments to customise it to the West Moreton / Metropolitan system context taking into account the existing wording of clause 7 of Schedule E.*

...

## **7 Capital Expenditure Reconciliation**

- (a) Queensland Rail will maintain registers in which it annually records all Approved Capital Expenditure for each Year (including identifying the relevant capital expenditure by project) in relation to the West Moreton System and Metropolitan System.
- (b) If at the end of any Year (other than the final two years of the Term), the total Approved Capital Expenditure for each year of the Undertaking to date (excluding any years in respect of which this clause 7(b) has previously been applied) differs from the total of the Capital Indicator for West Moreton System and Metropolitan System (as applicable) for the corresponding years, the Reference Tariffs for the Year which commences 12 months after the end of the relevant year for which the QCA approved the Approved Capital Expenditure under **clause 2.1** will be adjusted by an amount which reflects the change in 'Allowable Revenue' from which the Reference Tariffs have been calculated by the QCA in the Final Decision dated [\*\*] 2024 which includes:
  - (i) a return on capital component, calculated as the difference between the return on capital calculated based on the Capital Indicators for the relevant Years and the return on capital that should have applied based on the Approved Capital Expenditure for those same Years;
  - (ii) a depreciation component, calculated as the difference between the depreciation calculated based on the Capital Indicators for the relevant Years and the depreciation that should have applied for the Approved Capital Expenditure for the same Years; and
  - (iii) a tax depreciation component, calculated as the difference between the tax depreciation calculated based on the Capital Indicators for the relevant Years and the tax depreciation that should have applied for the Approved Capital Expenditure for the same Years,

with the total of those adjustments rolled forward to the Year in which the adjustments will be made at the WACC, and with those components, and the changes to the Reference Tariffs calculated using the modelling parameters and assumptions used to determine the Reference Tariffs by the QCA in the Final Decision dated [\*\*] 2024.

- (c) The adjustment process described in **clause 7(b)** of **Schedule E** will not apply if the difference between the total of the Capital Indicators and the Approved Capital Expenditures for the relevant Years is less than \$30m or if QR can reasonably demonstrate that this difference is likely to reduce to less than \$30m within 12 months.

- (d) For the avoidance of doubt, where **clause 7(b)** has been applied in respect of any Year, the Capital Indicators and total Approved Capital Expenditures in respect of any such Year will be excluded from any subsequent calculations of total Capital Indicators and total Approved Capital Expenditures under **clause 7(b) and Clause 8**.

## **78 Capital Expenditure Carryover Account**

- (a) ~~Queensland Rail will maintain registers in which it will annually record all Approved Capital Expenditure (including identifying the relevant capital expenditure by project) in relation to the West Moreton System and the Metropolitan System.~~
- (ba) If, at the end of ~~each~~ the last Year of the Term, there are any Years in which:
- (i) the Approved Capital Expenditure differs from the relevant Capital Indicator for West Moreton System or the Metropolitan System (as applicable); and
  - (ii) that Year was not the subject of an adjustment under **cause 7(b)** such that it is excluded for these purposes as provided for in **clause 7(d)**,

the difference will be entered in the Capital Expenditure Carryover Account. The balance recorded in the Capital Expenditure Carryover Account will be deemed as:

- (iii) an under recovery of revenue, where the Approved Capital Expenditure exceeds the relevant Capital Indicator; or
  - (iv) an over recovery of revenue, where the Approved Capital Expenditure is less than the relevant Capital Indicator.
- (c) The balance recorded in the Capital Expenditure Carryover Account will include:
- (i) a return on capital component, calculated as the difference between the return on capital assumed for the relevant Capital Indicator and the return on capital that should have applied for the Approved Capital Expenditure, accrued at the WACC;
  - (ii) a depreciation component, calculated as the difference between the depreciation assumed for the relevant Capital Indicator and the depreciation that should have applied for the Approved Capital Expenditure; and
  - (iii) a tax depreciation component, calculated as the difference between the tax depreciation assumed for the relevant Capital Indicator and the tax depreciation that should have applied for the Approved Capital Expenditure, and will be calculated using the modelling parameters and assumptions used to determine the relevant Reference Tariff
- (d) The balance in the Capital Expenditure Carryover Account at the end of each Year to which **clause 8(a)** applies will be rolled forward at the WACC.
- (e) The balance in the Capital Expenditure Carryover Account at the end of the Term will be taken into account when determining:
- (i) in relation to the West Moreton System, Reference Tariff; and
  - (ii) in relation to the Metropolitan System, the Reference Tariff input(s) relating to (in whole or part) the Regulatory Asset Base applicable to the Metropolitan System,

~~relevant to when setting Reference Tariffs in the next undertaking. on the basis of clearing the Capital Expenditure Carryover Account over the term of that next undertaking with the capital component described in **clause 8(a)** ~~7(b)~~ to be included in the Regulatory Asset Base and the cash flow components described in **clause 8(b)** ~~7(c)~~ to be taken into account in setting Reference Tariffs.~~ In the event there is no next undertaking and the Reference Tariff last applicable under this Undertaking was set at a level such that it would generate Expected Access Revenue equal

to the Approved Ceiling Revenue Limit, the portion of the balance in the Capital Expenditure Carryover Account described in **clause 8(b)**~~7(e)~~ will be recovered from, or returned to, Access Holders (as the case may be) in the form of a single payment following the Terminating Date