Consultation Paper

Australian Rail Track Corporation's compliance with the financial model in the Hunter Valley Coal Network Access Undertaking for 2018

February 2021

Submission are due by: **Wednesday**, **24 March 2021**

Foreword

The Australian Competition and Consumer Commission (**ACCC**) is conducting a public consultation as part of its assessment of the Australian Rail Track Corporation's (**ARTC**) compliance for the 2018 calendar year with the Hunter Valley Coal Network Access Undertaking (**HVAU**). The ACCC is seeking submissions from interested parties with respect to ARTC's submission.

Under the HVAU, ARTC is required to submit documentation to the ACCC for an annual assessment of its compliance with the HVAU financial model.

Questions for stakeholders are set out in **section 3** of this consultation paper. However, comments are welcome on any aspect of ARTC's submission.

The ACCC's intention is that there will be a single round of consultation before the ACCC makes a final determination in relation to ARTC's compliance in 2018. However, the ACCC may consult further with industry if it considers there is a need to do so, having regard to the submissions made in response to this consultation paper and any additional issues identified in ARTC's compliance submission.

Submissions are due by **Wednesday**, **24 March 2021** and should be addressed to:

Mr Matthew Schroder
General Manager
Infrastructure & Transport – Access & Pricing Branch
Australian Competition and Consumer Commission
Email: transport@accc.gov.au

Confidentiality

Unless a submission, or part of a submission, is marked confidential, it will be published on the ACCC's website and may be made available to any person or organisation upon request. Sections of submissions that are claimed to be confidential should be clearly identified. The ACCC will consider each claim of confidentiality on a case by case basis. If the ACCC refuses a request for confidentiality, the submitting party will be given the opportunity to withdraw the submission in whole or in part.

For further information about the collection, use and disclosure of information provided to the ACCC, please refer to the relevant publication available on the ACCC's website.[1]

Further Information

ARTC's submission for 2018 compliance and other relevant information, such as the applicable HVAU, are available on the ACCC's website.[2] Public submissions made during the current process will also be published on the ACCC's website. If you have any queries about matters raised in this document, please contact:

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1 Available at http://www.accc.gov.au/publications/accc-aer-information-policy-collection-and-disclosure-of-information

2 Available at https://www.accc.gov.au/regulated-infrastructure/rail/artc-hunter-valley-annual-compliance/annual-compliance-assessment-2018

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Executive Summary

ARTC has submitted compliance documentation for 2018 to the ACCC for assessment pursuant to the HVAU.

The HVAU financial model allows ARTC to recover revenue equivalent to its efficient costs in each calendar year for the Constrained Network (currently comprising rail Segments in Pricing Zones (**Zones**) 1 and 2). The financial model also allows ARTC to capitalise revenue shortfalls for the unconstrained part of the network (i.e. Zone 3) into the regulatory value of its assets for recovery in future years.

ARTC submitted that it had a $30.7 million under-recovery of revenue for the Constrained Network in 2018, which is to be paid back by Zone 1 and 2 Access Holders. ARTC also submitted that 'loss capitalisation' continued to apply in Zone 3 and that the net balance of losses capitalised into the Zone 3 asset base as at the end of 2018 is $61.5 million, an increase of $1.4 million over the year.

For 2018, ARTC submitted that total net capital expenditure was $55.7 million, including $40.6 million for the Constrained Network and $15.0 million for Zone 3 (Table 1)[3]. Only a small amount ($0.1 million) related to major capital expenditure. Nearly all the expenditure related to minor (corridor) capital expenditure.

ARTC also submitted that its operating expenditure was $127.9 million for the Constrained Network and $61.5 million for Zone 3 (Table 3). A key component of operating expenditure is infrastructure maintenance costs, which were $105.3 million in 2018 ($62.8 million for the Constrained Network and $42.5 million for Zone 3 (Table 3). Compared to 2017, this represents an overall increase in maintenance costs of 5.6 per cent (an increase of 8.0 per cent for the Constrained Network and an increase of 2.4 per cent for Zone 3).

ARTC's 2018 compliance documentation is available on the ACCC's website.[4]

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[3] Totals may not add due to rounding.

[4] Available at https://www.accc.gov.au/regulated-infrastructure/rail/artc-hunter-valley-annual-compliance/annual-compliance-assessment-2018

1. Introduction

ARTC is an Australian Government-owned corporation that was established in 1998 and provides a single point of contact for parties seeking to operate trains on the Interstate Network across Australia and the Hunter Valley Rail Network in New South Wales. ARTC is vertically separated, providing 'below-rail' services (such as the rail track infrastructure) but not 'above-rail' services (such as haulage).

The Hunter Valley Coal Chain is the largest coal export operation in the world. It consists of about 40 coal mines owned by around 20 coal producers and four above-rail operators transporting coal to three coal terminals. A key component of the Hunter Valley Coal Chain is ARTC's Hunter Valley Rail Network, which is used to transport coal from the Hunter Valley to the Port of Newcastle. The Hunter Valley Rail Network is also used for coal transport to power stations, non-coal traffic, including general and bulk freight (such as grain) and passenger services.

ARTC has a natural monopoly over this below-rail infrastructure that forms the Hunter Valley Rail Network. ARTC's monopoly position creates the possibility for it to charge monopoly prices, operate inefficiently and undertake inefficient investment.

1.1. Hunter Valley Coal Network Access Undertaking

Access to ARTC's Hunter Valley Rail Network is currently regulated through the HVAU, which sets out the terms and conditions for Access seekers (both current and future). The ACCC accepted the 2011 HVAU submitted by ARTC under Part IIIA of the *Competition and Consumer Act 2010* (**the Act**). The Hunter Valley network was previously subject to the NSW Rail Access Undertaking and administered by the NSW Independent Pricing and Regulatory Tribunal.

The HVAU initially applied for a five year period, expiring on 30 June 2016. However, as a result of the most recent variation, the HVAU is currently set to expire on 31 December 2021. Appendix A sets out the various variations that have been approved by the ACCC.

The 29 June 2017 variation to the HVAU changed a number of provisions in the undertaking, including the rate of return and remaining mine life, and introduced Schedule I, which sets out amendments to ARTC's overhead cost allocation methodology (**June 2017 variation**).[5] The June 2017 variation is applicable to the 2018 annual compliance assessment.

Note that on 23 December 2020, ARTC submitted to the ACCC, for approval, a variation to the current HVAU. As at the time of writing, the ACCC is assessing this variation. For further information on this variation please visit the ACCC website.

More information on the HVAU and its variations and extensions can be found on the ACCC website: https://www.accc.gov.au/regulated-infrastructure/rail/artc-hunter-valley-access-undertaking.

Capitalised terms used in the remainder of this paper are terms that are defined in section 14.1 of the HVAU.

1.2. HVAU financial model and pricing principles

Section 4 of the HVAU regulates the amount of revenue that ARTC is entitled to recover from Access Holders for the Hunter Valley Rail Network. In particular the HVAU sets out a

5 The HVAU applicable for the 2018 annual compliance process is available at https://www.accc.gov.au/system/files/public-registers/other/1203007-1-June-Variation.pdf.

different methodology for the Constrained Network and Zone 3. Section 4.3 of the HVAU caps the maximum amount of revenue (**Ceiling Limit**) that ARTC is entitled to receive from Access Holders at the Full Economic Cost of providing services. Section 4.4 of the HVAU sets out how the Regulatory Asset Base (**RAB**) and RAB Floor Limit are rolled forward each year.

1.2.1. Constrained Network methodology

The RAB Floor Limit is a critical component for determining the Full Economic Cost for the Constrained Network. The Full Economic Cost of providing services is calculated using a ‘building block model’, which requires a regulatory valuation of assets. The initial regulatory value of assets is rolled forward each year to add prudent capital expenditure and deduct depreciation and disposals. This is known as the RAB Floor Limit in the HVAU (section 4.4(b)). The Full Economic Cost is the sum of the return on the RAB Floor Limit, depreciation and operating expenditure.

For the Constrained Network, the HVAU applies an ‘unders and overs’ accounting framework that enables ARTC to recover the Full Economic Cost of providing services in each compliance period (i.e. calendar year). If ARTC’s revenue for the Constrained Network is more than the Economic Cost in a given year, then ARTC is required to refund the ‘overs’ amount to Constrained Coal Customers (and vice versa).

1.2.2. Zone 3 methodology

For Zone 3 customers, the HVAU sets out a loss capitalisation model, where the RAB is compared to the RAB Floor Limit, when the RAB exceeds the RAB floor limit loss capitalisation continues to apply. Loss capitalisation was developed to encourage investment in new assets and to help Access Holders in Zone 3 who were unable to pay the full economic cost of the new part of the network. Loss capitalisation aggregated annual losses from early years of Zone 3 joining the network.

The RAB comprises the regulatory value of Zone 3 assets (RAB Floor Limit) and the accumulated losses incurred in Zone 3. It is rolled forward each year to include new capital expenditure, return on the RAB, expenditure less revenue.

Under the HVAU, once ARTC is able to recover the Economic Cost of Zone 3 (including the losses capitalised from previous years), it becomes part of the Constrained Network and the ‘unders and overs’ accounting framework (as per the Constrained Network, detailed above) would take effect.

1.3. ACCC compliance assessment

Section 4.10 of the HVAU provides for the ACCC to conduct an annual assessment to determine whether ARTC has complied with the HVAU financial model for the calendar year and True Up Test (**TUT**). In particular, the ACCC will:

- determine whether ARTC has correctly rolled forward the regulatory value of its assets (4.10(d)(i))
- determine whether ARTC has correctly reconciled revenues with the applicable ceiling limits and determine the allocation of any under or over recovery of revenue to Constrained Coal Customers (4.10(d)(ii))
- determine whether ARTC has undertaken prudent capital expenditure (including gained Rail Capacity Group (**RCG**) endorsement) (4.10(d)(iii))
- determine whether ARTC has incurred efficient operating expenditure (4.10(e))

- review the TUT final audit report and determined whether there are any amounts of underpayment or overpayment of rebates (4.10(f)(xi)).

ARTC submitted its 2018 annual compliance documentation to the ACCC on 23 December 2020. ARTC resubmitted some documents on 15 January 2021, correcting some mirror errors.

The key components of ARTC's submission are set out in section 2 of this consultation paper. ARTC's non-confidential (resubmitted) submission is available on the ACCC's website.[6] The relevant provisions of the HVAU relating to the annual compliance assessment are outlined in Appendix B of this consultation paper.

[6] Available at https://www.accc.gov.au/regulated-infrastructure/rail/artc-hunter-valley-annual-compliance/annual-compliance-assessment-2018.

2. Key areas for the 2018 compliance assessment

The ACCC has identified the following key areas as being relevant for 2018:

- unders and overs (section 2.1)
- prudency of capital expenditure (section 2.2)
- efficiency of operating expenditure (section 2.3)
- procurement (section 2.4)
- true-up test audit (section 2.5), and
- any other matters of interest to stakeholders.

2.1. Unders and overs

Section 4.10(d)(ii) of the HVAU requires the ACCC to determine whether ARTC has allocated the total 'unders and overs' amount to Access Holders in accordance with the HVAU.

ARTC submitted that the total under-recovery for the Constrained Group of Mines (i.e. Zone 1 and 2 customers) for 2018 was $30.7 million.[7] The proportion of this amount that is allocated to each Constrained Coal Customer in accordance with section 4.9 of the HVAU is based on:

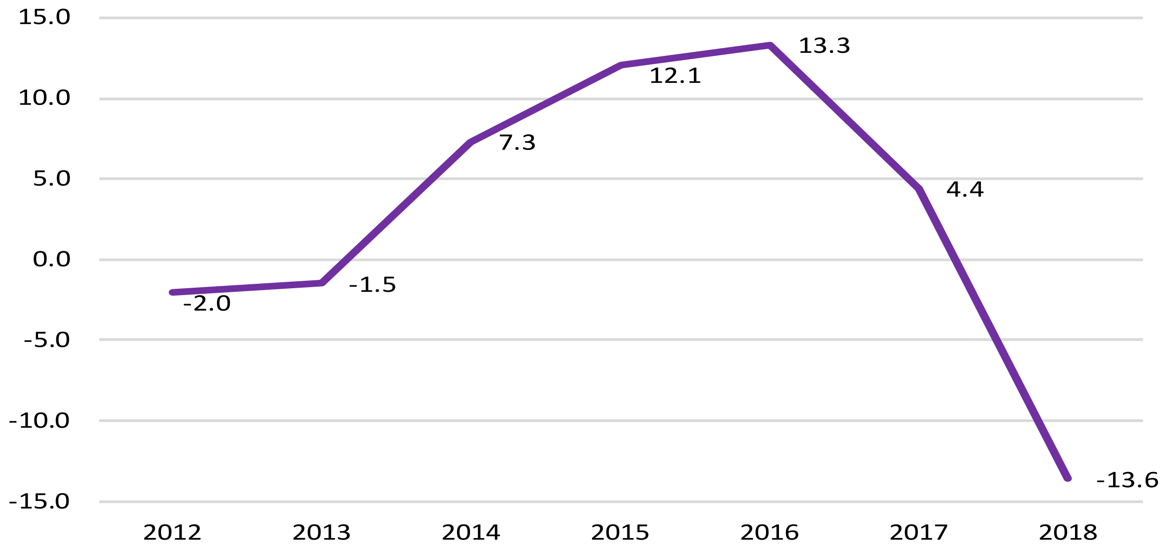
> *…the proportion of revenue paid for Access Rights over the Constrained Network by each Constrained Coal Customer, net of any rebate of the take or pay component of the Charges paid to that Constrained Coal Customer.*[8]

Figure 1 displays the 'unders and overs' amount as a percentage of total Access revenue for Zones 1 and 2.

[7] ARTC, *Hunter Valley Coal Network Access Undertaking – 2018 Compliance Assessment Submission*, 15 January 2021, p. 22.

[8] See section 4.9(b)(iii) of the HVAU.

Figure 1: Over (under) recovery amount as a percentage of total Access revenue (Zone 1 & 2)



In 2018, ARTC's under-recovered revenue as a percentage of Access revenue for the Constrained network was 13.6 per cent. This is the first time there has been under recovery since 2013. To comply with section 4.9(b)(ii) of the HVAU, ARTC provided confidential spreadsheets to the ACCC that set out the allocation of the total 'unders and overs' amount for 2018.

2.2. Prudency of capital expenditure

Sections 4.4(a) and (b) of the HVAU provide that net capital expenditure is defined as capital additions to the RAB and RAB Floor Limit, plus interest costs incurred during construction, less the written-down value of any disposals. The HVAU requires that, for capital expenditure to be included in the RAB and RAB Floor Limit, it must be incurred on a 'prudent' basis.

Section 4.10(d)(iii) of the HVAU explicitly provides that, if capital expenditure has been endorsed by the RCG in accordance with the consultation obligations set out in section 9 of the HVAU, then the ACCC will accept that capital expenditure as prudent for inclusion in the RAB and RAB Floor Limit. The RCG is a representative group made up of a range of stakeholders, including access holders and above-rail operators and the Hunter Valley Coal Chain Coordinator (**HVCCC**) (in a non-voting capacity).

Table 1 sets out ARTC's net capital expenditure for 2018, which was $55.7 million, including $40.6 million for the Constrained Network and $15.0 million for Zone 3.[9]

[9] Totals may not add due to rounding.

Table 1: Net capital expenditure, ($ million), 2018 ARTC Submission

Capital expenditure	Constrained Network	Zone 3	Total[10]
Major	0.1	0.0	0.1
Minor (Corridor Capital)	51.2	16.6	67.8
Interest during construction	0.4	0.0	0.4
Disposal value reduction	(11.1)	(1.6)	(12.7)
Net capital expenditure	40.6	15.0	55.7

Note: Totals may not add due to rounding.

Figure 2 shows ARTC's net capital expenditure from 2013 to 2018.

Figure 2: Net Capital Expenditure ($ million), 2013-2018

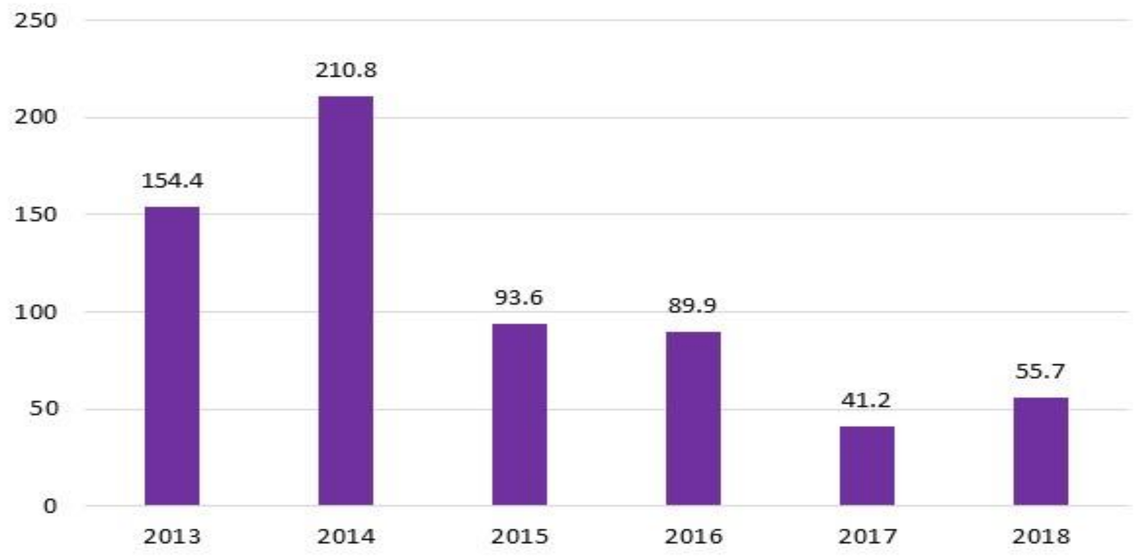
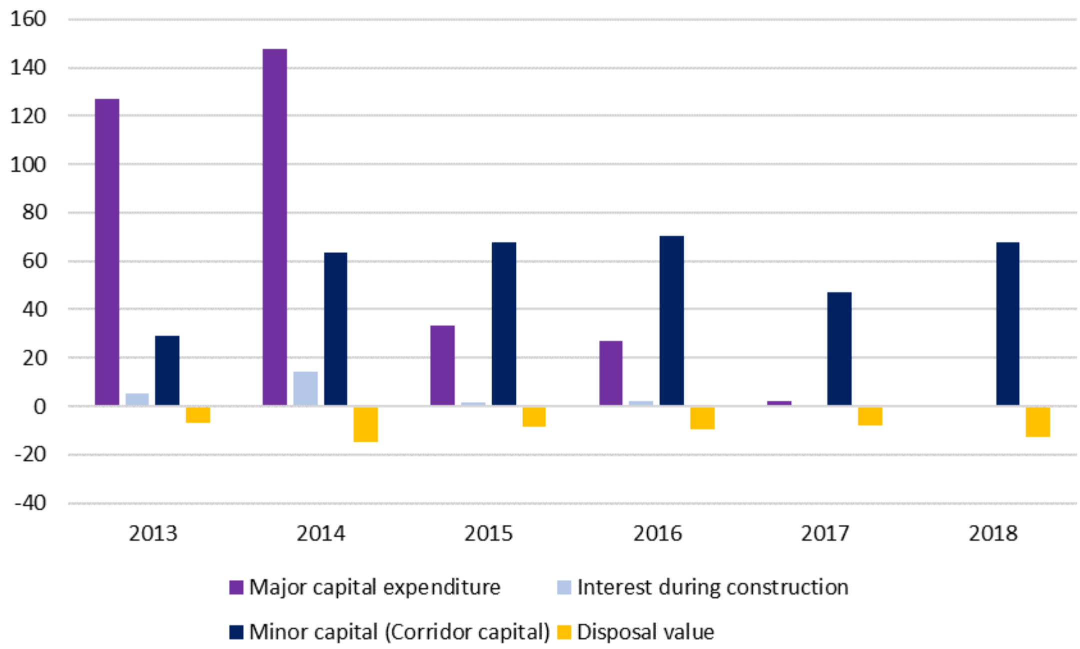


Figure 2 illustrates that while there was an increase in net capital expenditure from 2017 to 2018, expenditure in 2018 remains significantly below levels reported for 2013 to 2016.

Figure 3 displays each of the components of net capital expenditure over time.

10 ARTC, *Hunter Valley Coal Network Access Undertaking – 2018 Compliance Assessment Submission*, 15 January 2021, pp.11 and 14.

Figure 3: Net Capital Expenditure ($ million) by category, 2013-2018



In 2018, corridor capital expenditure increased by 43 per cent compared to 2017. Consistent with 2017, there was no major capital expenditure in 2018.

Major capital expenditure

ARTC submitted that there were no new major projects commissioned during 2018 and that post-commissioning costs were $0.1 million.[11] Table 2 outlines the major project capital expenditure that ARTC has included in the RAB Floor Limit for 2018.

Table 2: Major Projects included in the RAB Floor Limit in 2018

Project Code	Project Name	Value ($)[12]
8667	Kooragang Arrival Roads Stage 2	60,251
6387	Hexham Relief Roads Stage 1	25,499
5255	Maitland to Minimbah Third Road (Farley to Branxton) and (Branxton to Whittingham)	43,449
Total		**129,199**

Note: Totals may not add due to rounding.

[11] ARTC, *Hunter Valley Coal Network Access Undertaking – Attachment 2 capital consultation*, 23 December 2020, p. 7.

[12] ARTC, *Hunter Valley Coal Network Access Undertaking – Attachment 2 capital consultation*, 23 December 2020, p. 9.

Minor capital expenditure

ARTC submitted that:

> *Corridor capital* (i.e. minor capital expenditure) *of $67.8m was commissioned during 2018.*[13]

ARTC has provided information on the RCG's endorsement of both major and minor capital expenditure to the ACCC on a confidential basis.

2.3. Efficiency of operating expenditure

Section 4.10(e) of the HVAU provides for the ACCC to assess the efficiency of ARTC's operating expenditure. Efficient costs and operating expenditure, in turn, inform the determination of the Full Economic Cost and the maximum amount of revenue that ARTC is entitled to receive. Section 2(c) of Schedule G of the HVAU requires ARTC to submit a detailed breakdown of the Full Economic Costs for the review period into standard operating cost line items, return and depreciation, as well as provide comparative values from the previous review period.

Table 3 sets out ARTC's 2018 operating expenditure by major operating expenditure components. ARTC's submission proposes operating expenditure of $127.9 million for the Constrained Network and $61.5 million for Zone 3.

Table 3: Operating expenditure, ($ million), 2018 ARTC submission

Operating expenditure	Constrained	Zone 3	Total[14]
Infrastructure maintenance costs	62.7	42.5	105.2
Net loss on disposals	9.2	1.5	10.7
Network control	11.6	4.2	15.8
Business unit management costs	25.9	8.3	34.2
Corporate overheads	18.4	5.0	23.4
Total operating expenditure	127.9	61.5	189.3

Note: Totals may not add due to rounding. The Total column refers to the sum of the two columns – not the whole network.

Figure 4 displays ARTC's historical operating expenditure for 2013 onwards.

13 ARTC, *Hunter Valley Coal Network Access Undertaking – Attachment 2 capital consultation*, 23 December 2020, p. 7.

14 ARTC, *Hunter Valley Coal Network Access Undertaking – 2018 Compliance Assessment Submission*, 15 January 2021, pp.11 & 22.

Figure 4: Total Operating Expenditure, ($ million), 2013-2018

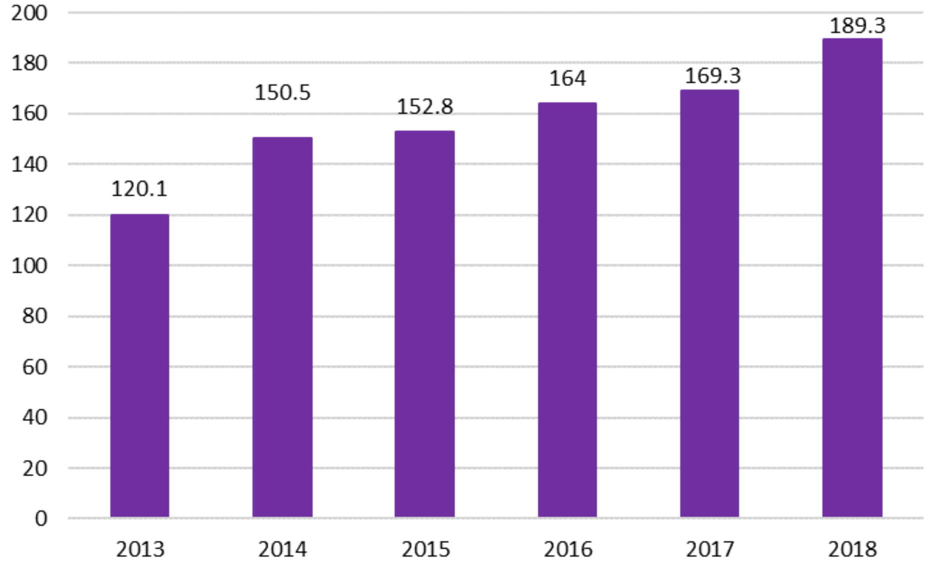


Figure 4 illustrates that ARTC's operating expenditures have steadily increased since 2013. Operating expenditure increased by 11.8 per cent in 2018 due to a 17.5 per cent increase for the Constrained Network[15] and 1.7 per cent increase for Zone 3.

Generally, changes in operating expenditure occur due to inflation and change in costs (i.e. labour, contractor costs), changes in volume, changes in level of performance of the network, changes in regulatory standards (e.g. safety, environment), age of infrastructure, weather conditions and improvements in efficiency due to technology changes, capital expenditure and management practices.

Figure 5 shows the six categories of ARTC's historical operating expenditure since 2013.

[15] ARTC, *Hunter Valley Coal Network Access Undertaking – 2018 Compliance Assessment Submission*, 15 January 2021, p. 22.

Figure 5: Operating Expenditure ($ million), by category, 2013-2018

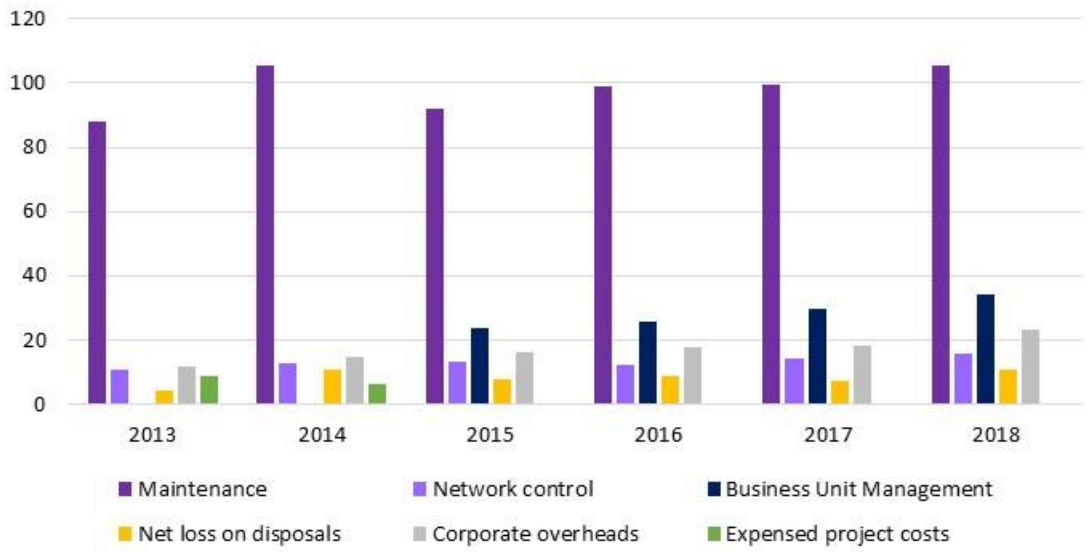


Figure 5 illustrates the magnitude of maintenance expenditure on total operating expenditure and the steady increase in business unit costs and corporate overheads.

The methodology for cost allocation was changed with the introduction of Schedule I from 1 July 2017. Schedule I sets out the methodology for allocating non-segment costs, such as network control, business unit management and corporate overheads. For comparison purposes, ARTC has reported two values for 2017; actual and restated. The restated value is as if Schedule I had applied for all of 2017, enabling a like for like comparison between 2017 and 2018.

Maintenance costs

The operating expenditure used to calculate Economic costs (and presented in Table 3 and Figure 4) were calculated *after* allocating incremental maintenance to the non-coal traffics.[16]

In contrast, ARTC provided a more detailed explanation of operating costs in Attachment 1, including a breakdown of maintenance costs by activity. The costs in Attachment 1 'reflect the underlying maintenance costs for each activity *before* allocating a share of incremental maintenance to the non-coal traffics'[17]. The following maintenance cost information is taken from Attachment 1.

ARTC's proposed 2018 maintenance costs is $114.4 million,[18] of which $70.4 million[19] relates to the Constrained Network and $44.0 million[20] relates to Zone 3. Compared to 2017, this represents an overall increase of 2.3 per cent[21] (i.e. an increase of 5.4 per cent for the Constrained Network and a decrease of 2.3 per cent for Zone 3).[22]

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16 Due to this difference, total maintenance costs in 2018 are $114.4 million in Attachment 1 compared with $105.2 million in the main submission.

17 ARTC, *Hunter Valley Coal Network Access Undertaking – 2018 Annual Compliance Assessment – Attachment 1: Hunter Valley Network Operating Costs*, 15 January 2021, p. 6.

18 Ibid, p. 7.

19 Ibid, pp. 8-9.

20 Ibid, p. 10.

21 Ibid, p. 7.

22 Ibid, p. 10.

ARTC provided details on the top ten maintenance activities by value for the Network and each of the Zones.

Ballast cleaning was the largest maintenance activity in 2018, and it increased by 13.5 per cent.[23] ARTC noted that in 2018 ballast cleaning was undertaken only in Zone 3.

Rail grinding was the second largest maintenance activity in 2018. Rail grinding expenditure in 2018 increased by 6.0 per cent.[24]

Business unit management costs

Business unit management costs were introduced in 2015 due to a corporate restructure, covering costs previously included in maintenance costs. This expense is now the second highest expense and has increased each year. It increased by $4.4 million in 2018.[25]

Business unit management costs comprise Hunter Valley direct costs and encompasses four functions:

- Hunter Valley Customer Service and Operations
- Hunter Valley Asset Delivery, including the Provisioning Centres
- Hunter Valley Asset Development
- Hunter Valley Management and Support.

Corporate overhead

Corporate overheads are general costs shared across the organisation and include the following expenditure: executive, finance, people, corporate services and safety, and strategy. Corporate overhead increased by $5.1 million (28 per cent) in 2018.[26]

2.4. Procurement

ARTC implemented a new procurement strategy in April 2018. Regarding the new procurement strategy, ARTC stated:

> *The updated manual documented refreshed guidelines for the engagement of suppliers, established a Procurement Threshold Matrix which set out delegations and approval pathways based on anticipated contract values, and set a renewed standard for articulating and demonstrating value for money throughout the procurement process. In addition to the manual, a suite of process maps and reference guides were developed to assist with the implementation and detailed personnel training was undertaken throughout the year to embed the new processes across the business.*[27]

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23 Ibid, p. 7.

24 Ibid, p. 7.

25 Ibid, p. 19.

26 ARTC, *Hunter Valley Coal Network Access Undertaking – 2018 Annual Compliance Assessment – Attachment 1: Hunter Valley Network Operating Costs*, 15 January 2021, p. 21.

27 ARTC, *Hunter Valley Coal Network Access Undertaking – 2018 Compliance Assessment Submission*, 15 January 2021, p. 7

2.5. True-up Test audit

For 2018 RSM Australia (**RSM**) has audited ARTC's compliance with the system TUT obligations under Schedule 2 of the Indicative Access Holder Agreement annexed to the HVAU. The TUT determines whether ARTC is liable for any rebates to users for ARTC's failure to deliver contracted path usages.

The final audit report concluded that ARTC had complied, in all material respects, with Schedule 2 of the Access Holder Agreements under the HVAU for the year ended 31 December 2018[28] and ARTC is not liable to pay any rebates to users.

RSM found two minor compliance risk issues:

- publication of January, July and August 2018 TUT monthly reports was not on time, and
- errors in total path usage in relation to maintenance and non-coal customers.

These errors were deemed non-material and did not result in any shortfalls by ARTC. Additional details about the TUT results can be found in RSM's audit report.[29]

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[28] RSM Australia, *Australian Rail Track Corporation – Hunter Valley Access Undertaking – System Wide True Up Test Audit – Reasonable Assurance Engagement Report*, April 2019, p. 6.

[29] Available at: https://www.accc.gov.au/regulated-infrastructure/rail/artc-hunter-valley-annual-compliance/annual-compliance-assessment-2018.

3. Questions

The ACCC welcomes stakeholder views on any aspect of ARTC's 2018 compliance submission. In particular, the ACCC seeks any stakeholders comments about:

Unders and overs

1) The amount of under-recovered revenue.

Capital expenditure

2) ARTC's compliance with the HVAU regarding:

   (a) the cost of major capital projects to be rolled into the regulatory value of assets for 2018.

   (b) the level of capital expenditure in relation to minor capital projects and the costs of those projects to be rolled into the regulatory value of assets for 2018.

3) The process conducted by ARTC in relation to consultation with, and endorsement of, capital expenditure by the RCG.

Operating expenditure

4) Whether the operating expenditure incurred by ARTC during the 2018 compliance period was incurred in an efficient manner (as defined in section 14 of the HVAU), including ARTC's infrastructure maintenance, business unit management, corporate overhead and network control costs, as well as its loss on disposals.

Procurement

5) Whether stakeholders have any issues regarding the new procurement strategy.

True-up Test audit

6) ARTC's application of the TUT for 2018 or the findings / conclusion set out in the audit report prepared by RSM.

Appendix A: HVAU variations since 2011

This appendix outlines the key parameters in the original 2011 HVAU, followed by the key changes affecting annual compliance in subsequent variations to the HVAU.[30]

Version 1. Original undertaking, accepted by ACCC 29 June 2011

- Term of 5 years commencing 1 July 2011
- Average remaining mine life (**RML**) is set at 22 years as at 1 July 2010
- Real pre-tax rate of return (**RoR**) is set at 9.10 per cent
- Nominal pre-tax RoR is set at 11.83 per cent.

Version 2. Variation accepted by ACCC 17 October 2012

- Implemented the Initial Indicative Service and associated Initial Indicative Access Charges.

Version 3. Variation accepted by ACCC 25 June 2014

- New segments from Gap to Turrawan included (retrospective to 1 January 2014).

Version 4. Variation accepted by ACCC 22 June 2016

- Extended 2011 HVAU by six months - 'Extension period' is from 1 July 2016 to 31 December 2016
- Real pre-tax RoR is 6.74 per cent and nominal RoR 8.50 per cent for the Extension Period.
  - ➢ This RoR was superseded by a lower RoR from 1 July 2016 to 31 December 2016 set in the variation accepted 29 June 2017, although prices charged during the extension period reflected the 6.74 per cent RoR;
- Allowed ACCC to conduct a reconciliation to effectively backdate any difference between the rate of return ultimately approved by the ACCC for the new access undertaking and the specified rate of return for the extension period.

Version 5. Variation accepted by ACCC 23 November 2016

- Extended HVAU by 6 months to 30 June 2017 while the next access undertaking was being finalised
- Amended the transitional arrangements relating to the True Up Test, compliance assessment and pricing for the entire extension period from 1 July 2016 to 30 June 2017
- Applied the same interim RoR and RML as per the first six month extension. ARTC also proposed to maintain the access charges that applied to the first six month extension.

Version 6. Variation accepted by ACCC 29 June 2017

- Extended 2011 HVAU until 31 December 2021

[30] See https://www.accc.gov.au/regulated-infrastructure/rail/artc-hunter-valley-access-undertaking - Past projects.

- For 2016 - a single annual compliance assessment but with a different RoR and RML to be applied in each half year:
  - 1 January 2016 to 30 June 2016 (2016H1): a pre-tax real RoR of 9.10 per cent (as in original 2011 HVAU) and RML of 16.5 years at 1 Jan 2016 [based on life of 22 years as at 1 July 2010]
  - 1 July 2016 to 31 December 2016 (2016H2) a pre-tax real RoR of 5.38 per cent, nominal pre-tax RoR of 7.91 per cent, and RML of 23 years at 1 July 2016
  - For 2017 and onwards, annual compliance assessments for each calendar year with a pre-tax real ROR of 5.38 per cent, nominal 7.91 per cent, and RML declining from 23 years at 1 July 2016;
- Reconciliation for 'backdating' period between 1 July 2016 and 30 June 2017:
  - the under and overs accounting process is used to reimburse Constrained Coal Customers for any over-recovery
  - one-off adjustment to revenue for unconstrained PZ3, to be offset against out-turn revenue;
- Updated the indicative access charges for the period 1 July 2017 to 31 December 2017 (2017H2), to reflect the proposed commercial parameters in the Application
- Revised corporate overhead cost methodology and allocators (Schedule I)
- Commencement date of 1 July 2017 (e.g. Schedule I cost allocators).

Version 7. September 2018 Variation - accepted by ACCC 29 Nov 2018

- Path based pricing - altered the structure of Access Charges to a new three-part tariff including two Take-or-Pay components based on contracted GTK (intended to recover Incremental Capital Costs) and Train Km (intended to recover Fixed Costs)
- Incremental cost methodology, including:
  - change to allocating Incremental Capital Costs on the basis of contracted capacity
  - new process for allocating capital costs as either Fixed and/or Incremental Capital Costs at Rail Capacity Group meetings;
- Dual ceiling limit – one for PZ1 and PZ2, and one for PZ3 when constrained
- Provided for ARTC to submit annual documentation by later of 30 April or four months after ACCC's previous determination:
  - also to apply retrospectively to 2016, 2017, 2018 assessments;
- Provisions commenced from 1 January 2019.

Appendix B: Annual compliance assessment provisions in the HVAU (Version 6)

Section 4.10 of the HVAU provides for the ACCC to conduct an annual compliance assessment to determine whether ARTC has complied with the access pricing principles under the HVAU. These provisions are set out below (capitalised terms are defined under section 14 of the HVAU).

a) ARTC will submit to the ACCC by 30 April each year in respect of the previous calendar year:[31]

   i. documentation detailing roll-forward of the RAB and the RAB Floor Limit, and comparisons between RAB and RAB Floor Limit;

   ii. where documentation in (i) above demonstrates that RAB is at or below RAB Floor Limit, documentation detailing calculations relevant to reconciliation of Access revenue with the applicable Ceiling Limit and calculation of any allocation of the total unders and overs amount; and

   iii. where documentation in (i) above demonstrates that RAB is above the RAB Floor Limit in Pricing Zone 3, documentation demonstrating that Indicative Access Charges, or Interim Indicative Access Charges, as applicable, satisfies the requirements in section 4.3(b).

b) The documentation submitted by ARTC to the ACCC will, unless otherwise agreed with the ACCC and having regard to the relevant circumstances applicable at the time, meet the information provision guidelines and the timeframes set out in Schedule G.

c) If the ACCC reasonably considers that it requires additional information, other than that provided by ARTC in accordance with Schedule G, in order to carry out its assessment under section 4.10(d), it may request this information from ARTC in accordance with section 3 of Schedule G and upon receipt of such a request ARTC will use reasonable endeavours to provide the information to the ACCC as soon as reasonably practicable.

d) The ACCC will determine whether ARTC has undertaken:

   i. roll-forward of the RAB and RAB Floor Limit in accordance with the Undertaking and, where the roll forward is not in accordance with the Undertaking, determine what closing RAB or RAB Floor Limit would be in accordance with the Undertaking;

   ii. when required, the calculations relevant to reconciliation of Access revenue with the applicable Ceiling Limit and calculation of any allocation of the total unders and overs amount in accordance with the Undertaking, and where the calculations are not in accordance with the Undertaking, determine what total unders and overs amount or allocation would be in accordance with the Undertaking having regard to the operation of its unders and overs account;

   iii. in determining whether ARTC has complied with the provisions of section 4.4 in rolling forward the RAB or the RAB Floor Limit, the ACCC may have regard to the submissions of relevant industry participants but if Capital Expenditure has been endorsed by the RCG in accordance with section 9, the ACCC will not consider whether that Capital Expenditure is Prudent;

[31] Section 4.10(a) was amended in the September 2018 variation to the HVAU to allow the submission by the later of 30 April each year and 4 months from the ACCC's final determination of the previous year's Compliance Assessment. This variation took effect from 1 January 2019. Section 4.10(h) of the HVAU notes that the varied section 4.10(a) applies for the 2018 compliance assessment.

iv. the ACCC will publish its findings on its website and/or circulate to Access Holders in relation to the matters for its determination; and

v. ARTC will revise the closing RAB and manage Constrained Coal Customer Accounts in accordance with any determination by the ACCC.

e) The ACCC will determine whether ARTC has incurred Efficient costs and Efficient operating expenditure in accordance with section 4.5(b), and determine the change (if any) to:

i. the total ‘unders and overs’ amount or allocation; and

ii. closing RAB in section 4.4(a),

that results from Economic Cost under section 4.5(a) only including Efficient costs and Efficient operating expenditure determined in accordance with section 4.5(b).

Section 4.10(f)(x) of the HVAU also provides that ARTC will provide the final written report of the True-Up Test, as prepared by the independent auditor, to the ACCC to review as part of the annual compliance assessment process under the HVAU.