



AUSTRALIAN RAIL TRACK CORPORATION LTD

2011 CAPITAL CONSULTATION

HUNTER VALLEY COAL NETWORK

April 2012

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ATTACHMENTS

1. 2011-2020 HUNTER VALLEY CORRIDOR CAPACITY STRATEGY CONSULTATION DOCUMENT
2. 2011 CAPITAL WORKS PROJECT DETAIL AND DISPOSAL TREATMENT

1. Introduction

Australian Rail Track Corporation (“ARTC”) commenced a lease of certain parts of the NSW Rail Network (including the Hunter Valley Coal Network) on 5 September 2004. Under this lease, on 1 July 2011 ARTC committed to operating under the Hunter Valley Access Undertaking 2011 (“HVAU”) approved by the Australian Competition and Consumer Commission (“ACCC”).

In accordance with the Undertaking¹, ARTC must submit to the ACCC by 30 April each year in respect of the calendar year completed on 31 December of the previous year:

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

ARTC is responsible for meeting all obligations under the HVAU for the half calendar year July – December 2011 (“Compliance Period”).

In determining whether ARTC has complied with HVAU in relation to the RAB and RAB Floor Limit roll forward, the ACCC may have regard to the activities undertaken by ARTC as part of the capital expenditure consultation process described in the Undertaking². This document is provided to ACCC for the purpose of supporting those aspects of the ARTC’s conduct of the RAB and RAB Floor Limit roll forward, including:

- a detailed description of the capital consultation process undertaken in the Compliance Period and an explanation of how it met the requirements of the Undertaking;
- evidence of any Access Holders’ endorsement of any proposed capital expenditure, where relevant;
- the name, address, contact details (including email address) of stakeholders considered by Owners to be Access Holders (noting which of those are Access Holders) and other parties consulted regarding compliance matters.

¹ SCHEDULE G - Annual Compliance Assessment -information provision and timing

² 4.10 Annual ACCC compliance assessment

2. Capital Consultation Process

2.1. Compliance Scope

In accordance with section 9.2 of the HVAU; ARTC is obliged to convene and conduct regular monthly meetings of the Rail Capacity Group (RCG). The formal transition of the Rail Infrastructure Group (RIG) to this position is progressing with stakeholders involved in detailed discussions on the group's charter and confidentiality deed. Until the RCG is formally in place ARTC has continued the regular industry forum of the RIG to ensure Access Holders, prospective Access Holders and other industry stakeholders are provided a suitable forum in which to have input to, identify, prioritise and evaluate future network investments and refine the capital works programme.

To achieve this objective, ARTC has a consultation process that incorporates the following:

- the Rail Infrastructure Owner's (ARTC) planning approach, including the trade-off between routine maintenance and major periodic maintenance and capital expenditure;
- identification of the proposed capital investment needs for the forthcoming year and forecast capital expenditure for the following ten years;
- explanation of the inputs to and outcomes of the evaluation undertaken for the proposed capital expenditure for the forthcoming year;
- provision of an assessment of the impact of the proposed capital expenditure on the Regulatory Asset Base ("RAB");
- identification of the projects that will be funded or partly funded by capital contributions; and
- establishment of a process for Access Holders' input.

In determining whether ARTC has complied with the HVAU in relation to the RAB and RAB Floor Limit roll forward, the ACCC may have regard to submissions from users to the capital consultation process. However, ACCC will not have regard to any submission that is in direct conflict to the outcomes of the consultation process³.

ARTC recognises that the scope of compliance in 2011 relates to both capital works commissioned in 2011 and incorporated in the RAB and RAB Floor Limit roll forward in addition to consultation in relation to ARTC's investment in the Hunter Valley Coal Network to be commissioned in during the Compliance Period and in future years.

³ 4.10 (d)(iii) *Annual ACCC compliance assessment*

2.2. Industry Approach to Capital Consultation

2.2.1. Overview

Since taking responsibility for the NSW Hunter Valley Network in September 2004, ARTC has maintained its approach to consult all industry stakeholders with an interest in the movement of coal on the Hunter Valley rail network (the "Network"), and every effort to provide a comprehensive understanding of, and have input into, ARTC's overall strategy for the Network has occurred. This strategy was detailed in the document entitled *2011-2020 Hunter Valley Corridor Strategy Consultation Document* (refer to Attachment 1), which was released for consultation on 11th April 2011.

This consultative process continues to provide ARTC with significant insight and understanding of stakeholders' expectations of the rail infrastructure owner and has led to improved interaction between ARTC, Access Holders and prospective Access Holders along with a clearer and more precise methodology of dealing with project endorsement. Historically the consultative process has principally been facilitated through a number of industry forums attended by rail operators and coal producers, including:

- Rail Infrastructure Group ("RIG")
- Hunter Valley Coal Chain Coordinator Board and associated Sub-Committees

The purpose of each of these forums are discussed in more detail in Sections 2.2.2 to 2.2.5 below.

All capital expenditure on the Network is subject to one of the two consultative processes depending on the type, value and strategic significance of projects. For significant and strategic capital enhancement projects (e.g. Maitland to Minimbah 3rd Road project), consultation is undertaken through a number of strategic and operational forums with industry participants. Through this process, ARTC seeks input from Access Holders to ensure that the overall *Hunter Valley Corridor Capacity Strategy* reflects industry requirements.

In relation to less significant asset replacement or minor operational improvements projects, ARTC is of the view that consultation through a single, operational forum is most appropriate. The RIG is currently such a forum. This process ensures a disproportionate amount of industry resources is not consumed when seeking endorsement of asset replacement or minor operations capital works.

It should be noted that during the Compliance Period, the RIG consisted of similar industry representation to that contemplated for the RCG and consultation was carried out during the Compliance Period on a basis similar to that contemplated for the RCG under the HVAU.

At either level of consultation, industry endorsement is necessary before ARTC will proceed to project implementation phase and formal endorsement for the value of the project to be added to the RAB occurs at the RIG which in due course will transition to RCG.

This consultation process is designed to provide maximum opportunity to work with Access Holders to identify and prioritise network investment and to refine capital work programs.

2.2.2. Rail Infrastructure Group

The RIG comprises a senior executive representative from major rail operators hauling coal on the network (QR National), four large coal producers (Rio Tinto, Whitehaven, BHP, Xstrata) and one representative from the smaller producers (Bloomfield Coal), ARTC is represented by personnel from Asset Management, Operations and, as necessary, by representatives from the project delivery and strategic group.

This RIG meets each month and has a standing agenda that covers:

- asset replacement and minor capital works on the Network
- major capital investment on the Network
- strategic proposals necessary to meet coal industry forecast in the coming five (5) year horizon and beyond..

The RIG deals with the detail of major investment proposals. ARTC provides detailed and extensive project submissions to the RIG for their review and inputs. At each of the monthly meetings, considerable discussion has focussed on identifying not only the projects required to deliver enhanced capacity but assessment of whether the projects were the right projects and the priority of delivery to meet demand or service the industry need operationally.

In addition, the RIG is currently the forum for consultation on & endorsement of all minor capital investment that is not included in the *Hunter Valley Corridor Capacity Strategy*. Expenditure of a minor capital nature is presented for review and approved annually by the Rail Infrastructure Group in advance of the work being undertaken⁴.

ARTC does not 'trade off' expenditures; rather ARTC uses a professional and standardised approach for classification of maintenance and capital expenditures. It uses the internal ARTC definitions and classifications of reactive corrective routine maintenance, major periodic maintenance and capital

⁴ The only exception to this is when for either safety or urgent operational needs, an expenditure of a capital nature is necessary. The details of such expenditure are advised to the RIG (No such events occurred in H2 2011)

expenditure, which is made clear to the RIG. However, when there is not a clear treatment, the issue is brought to the RIG for consultation and guidance.

ARTC acknowledges the contribution the producers can make through direct consultation however concludes that it is inefficient and impractical for ARTC to consult with every individual coal producers on the specifics of each investment. As such, ARTC relies on the small producer representative (currently Bloomfield Coal) to take back any relevant information pertaining to infrastructure investment that their constituents may have an interest in, in order to ensure the successful and timely delivery of all projects. ARTC understands that this approach is acceptable to the coal industry.

In addition, further Industry Representatives (Pacific National , Freightliner & HVCCC) have been in attendance as observers during 2011, which has facilitated the consultation process for various projects.

In addition to the Industry Representatives in attendance at RIG meetings, ARTC recognises the importance of input from all coal producers, particularly at the strategic level. As part of the consultative process, ARTC seeks input from coal industry senior executives or their representatives at the following forums:

- Hunter Valley Coal Chain Coordinator Board and associated Sub-Committees

These forums also provide the opportunity for ARTC to keep all coal producers and stakeholders fully informed of the status of various projects, including delivery timelines and expected value of capacity enhancements.

2.2.3. Hunter Valley Coal Chain Coordinator

On 27 August 2009 the Hunter Valley Coal Chain Coordinator Limited (HVCCC) was incorporated as a new independent legal entity and formally replaced the HVCCLT (Hunter Valley Coal Chain Logistics Team) The membership of the HVCCC has been expanded to include all current Hunter Valley Coal Chain Producers as well as Service Providers.

ARTC is a member of the Hunter Valley Coal Chain Coordinator ("HVCCC").

The HVCCC's mission is to plan and co-ordinate the co-operative daily operation and long term capacity alignment of the Hunter Valley Coal Chain. Its strategic objectives include;

- To plan and schedule the movement of coal through the Hunter Valley Coal Chain in accordance with the agreed collective needs and contractual obligations of Producers and Service Providers
- To ensure minimum total logistics cost and maximised volumes through the provision of appropriate analysis and advice on capacity constraints (whether physical, operational or commercial) affecting the efficient operation of the Hunter Valley Coal Chain; and
- To advocate positions, on behalf of Producers and Service Providers, to other stakeholders and governments on issues relevant to the efficient operation of the Coal Chain in order to maximise opportunities for improved co-ordination and/or further expansion of the Coal Chain.

ARTC works very closely with the HVCCC in the delivery process of the major capital works as the impact of the works can be significant. The HVCCC assist with any modelling to determine benefit on a throughput basis and assessment on timing of projects to meet other coal chain expansion.

As an integral part of managing each project, ARTC undertakes a process review of effects on network throughput impacts and consults with the HVCCC on options to mitigate or reduce the impact wherever possible. HVCCC is also involved with ARTC in the coordination of works and track possession closedown.

Additionally, the board of the HVCCC consisting of senior executives from each member group meets each month to discuss coal industry requirements for expansion and other strategic development. ARTC provides this group with regular updates of project progress, cost and benefits associated with infrastructure investment.

In providing the HVCCC detail of ARTC's strategic investment intent, it allows a comprehensive understanding of the linkages of investment in the supply chain. ARTC considers the approach to include the HVCCC in this process a vital cog in the mechanism to ensure the investment fits cohesively with other coal chain development.

2.2.4. Contact Details of Stakeholders

As described in Section 2.2 above, ARTC has consulted widely within the coal industry, particularly through the various industry forums. Appendix 1 presents the contact details for industry stakeholders and parties consulted regarding compliance matters.

2.3. Development of the Hunter Valley Corridor Capacity Strategy

2.3.1. ARTC Approach

The development of the 2011-2020 *Hunter Valley Coal Corridor Capacity Strategy* involved:

- assessments of the capacity of the existing Hunter Valley rail network for transporting export coal to the Newcastle ports and domestic coal to Hunter Valley power stations
- update demand forecasts by obtaining revised industry forecasts and views
- comparisons of this capacity with anticipated demand, to identify existing and future likely constraints
- reviews of the options previously proposed to address these constraints
- where necessary, the development of additional or refined options, and
- the selection of preferred actions to address each of the identified constraints.

2.3.2. Strategy Development

ARTC has continued to review and develop changes where necessary to the *Hunter Valley Corridor Capacity Strategy*.

Since taking up the lease of the NSW rail network in September 2004, ARTC has continued to gain a better understanding of the Network and the expectations of ARTC as a rail track owner. As a consequence of this and the supply of information relating to specific growth areas, several key changes in the now current version of the Network Improvement Strategy document have been made. Upon release of the 2011-2020 version, ARTC wrote to all coal producers in the constrained and non-constrained Network making them aware the document is available for public distribution.

The major changes to *2009-2018 version* of the strategy document (as previously outlined) included:

- Fully revised volume forecasts based on indicative contracted volumes & prospective volumes.
- Assumed that port capacity will accommodate producer volumes.
- Project timing adjusted as required.

To ensure it had the best possible understanding of forecast volumes, ARTC sourced forecast information from:

- All Producers
- QR National

- Pacific National
- HVCCC (on a line section basis)

The strategy has given the coal chain increased certainty with timeline delivery of the projects along with updated projected costs and as such offers options to resolve constraints and understand how coal producers can better manage their proposed course of action to increase coal throughput.

Consultation undertaken during the Compliance Period has been maintained from the previous year. ARTC has focussed on the critical aspects of delivering capacity on all areas of the Network for the next ten years and is confident the level of endorsement for the proposed investment program included in *2011-2020 & subsequent 2012-2021 version* of the Hunter Valley Corridor Improvement Strategy will be received.

ARTC will continue to monitor and review the strategy to ensure proposals for infrastructure change are developed ahead of demand. ARTC intends to update annual profiles of coal industry haulage demands to further develop future strategy requirements based on a rolling ten year horizon.

2.4. Project Consultation

2.4.1. Project Consultation Process

ARTC undertakes a comprehensive capital consultation process for all capital projects. There are generally three categories of capital projects:

- major capital capacity projects
- major asset renewal projects; and
- minor capital projects

The major capital capacity projects are those which are capacity enhancement projects that form part of the *Hunter Valley Corridor Capacity Strategy* described in Section 2.3 above, while the other projects are classified as either asset replacement or asset enhancement projects.

For major capital capacity projects, in accordance with Sections 9.3 – 9.7 of the 2011 HVAU, consultation and endorsement is performed in stages to ensure that stakeholders are fully informed before final endorsement for construct is provided. The rail operator representatives are provided with detailed analysis of key elements of each project stage and all major projects sign off endorsements includes details of:

- project aim
- timing – start / finish
- benefits and deliverables (e.g. capacity improvement, operational performance improvement, safety, cost savings)
- diagrams / document references
- cost and contingency to RAB and loss on disposal where applicable
- endorsement signatory.

For the major asset renewal or replacement projects, a submission detailing the projects objectives, options, financial and risk management aspects is provided for review and endorsement by RIG. This endorsement process is often iterative, and ARTC works closely with the stakeholders in providing all necessary information for evaluation.

For the minor capital projects, the programme of smaller projects is typically submitted collectively for consultation and endorsement to the RIG. This is consistent with historical practice and the requirement of Section 9.1(e)(ii) of the HVAU. Additionally for the minor capital projects where the classification between regulatory capital and maintenance is unclear, guidance is sought from the RIG.

2.4.2. Project Endorsement

Attachment 2 shows detail of project status for all projects (minor, major or asset renewal in nature).

This attachment presents:

- a) projects on the constrained network commissioned in H2 2011 and sought for RAB inclusion, together with disposals treatment
- b) projects on the constrained network but not completed in H2 2011 (i.e., WIP carried), including expenditure incurred to date.
- c) projects on the unconstrained network commissioned in H2 2011 and sought for RAB inclusion, together with disposals treatment
- d) projects on the unconstrained network, but not completed in H2 2011 (i.e., WIP carried forward), including expenditure incurred to date.

3 capital projects were completed and commissioned during the Compliance Period. ARTC is seeking to include the commissioned projects on the Network at a total value of \$54,297,909 to be added to the RAB and RAB Floor Limit via the roll forward mechanisms prescribed at Section 4.4 of the HVAU.

Asset disposals of \$ 1,412,613 (including net values) have been determined in relation to commissioned projects in 2011.

- ARTC was not able to provide the exact disposal values of the projects they related to, for advanced endorsement by the RIG as the prospective values of any offset to the disposal value (arising from sale as scrap or transfer to inventory) for equipment that was to be replaced was not yet known.

2.4.3. Major Capital Projects

During the year, major capital enhancement projects at a total cost of \$50,450,982 were commissioned for which ARTC is seeking inclusion of the associated expenditure in the RAB and RAB Floor Limit roll forward for the Compliance Period.

The breakdown for each large capital project is;

• Koolbury Passing Loop	\$ 16,042,645
• Wilpinjong Passing Loop	\$ 16,830,533
• Bengalla Passing Loop	\$ 17,577,804

In addition ARTC commissioned minor capital enhancement/replacement projects at a total cost of \$6,987,636, which is also sought to be included in the RAB and RAB Floor Limit roll forward for the Compliance Period. A full summary of major and minor capital works and the associated cost breakdown is included at Attachment 2

2.5. Compliance with the Undertaking

ARTC considers that consultation undertaken as described in Sections 2.2 to 2.4 (above), provides comprehensive evidence that ARTC has complied with the relevant requirements of the HVAU.

ARTC has worked very closely with Access Holders, both rail operators and coal producers, in identifying and prioritising network investments and refining capital works programs. Through this extensive consultation process, Access Holders have provided input into the major capital enhancement projects that form part of the overall *Hunter Valley Corridor Capacity Strategy*. This strategy document identifies the proposed capital investment needs for the forthcoming year and includes forecasts of capital expenditure for the following ten years.

ARTC has spent considerable time in communicating each project with the RIG, and have been purposeful in advising the coal industry producers at Industry Communication Sessions and at senior executive level through the HVCCC board. As is required by the HVAU, ARTC has provided comprehensive detail of each project explaining the input to and outcomes expected for the forthcoming year(s).

This has included a process where all options are assessed by the internal ARTC investment committee who consider the viability of each proposed project before being passed forward for consideration and endorsement as capital expenditure to the RIG as an alternative to RCRM or MPM. For each project, ARTC has been consistent in the classification of works as either maintenance or capital expenditure. Importantly, where the classification is unclear, ARTC has consulted with the RIG.

ARTC has, through the consultative process, provided an assessment of the impact the proposed capital expenditure will have on the RAB and RAB Floor Limit for the forthcoming year.

ARTC also provides clarity in relation to projects which are intended to be partly or fully funded by capital contributions. There were no such projects in 2011.

3. Conclusion

The consultation activities that ARTC has engaged in has revolved around obtaining a comprehensive understanding of new coal mine development proposals and their timing of development where increased capacity is required on the Network. This information is reviewed against other industry information and ARTC seeks confirmation, where applicable, that its priority of project delivery matches other coal chain capacity deliverables.

During 2011, ARTC has found the level of co-operation and advice provided by rail operators, coal producers and the other services providers to be both informative and constructive in all aspects of managing and progressing with investment options. In particular, ARTC is satisfied it has well developed working relationships with the coal chain as a whole and looks forward to continuing the work started through the RCG forum.

The capital consultation process is constantly improving with experience, particularly at the RIG level. Improvements made throughout 2011 include continued enhanced formalisation of information provision & sign off, and importantly the inclusion into the RIG of industry representatives including coal producers.

ARTC considers the development of the *Hunter Valley Corridor Capacity Strategy* and the delivery of the identified projects to be an important commercial and mandatory requirement, and as such, ARTC is strongly committed to implementing each phase of the capacity plan in a timely manner.

ARTC is committed to the ongoing consultation through the various industry forums, including the RCG, and looks forward to a continued delivery of optimal rail network solutions in the Hunter Valley Coal Network.

Appendix 1 – Contact Details of Stakeholders

Deleted for privacy reasons

2011-2020 Hunter Valley Corridor Capacity Strategy Consultation

Document – 11April 2011

http://www.artc.com.au/library/news_2011-04-11.pdf

2011CAPITAL WORKS PROJECT DETAIL AND DISPOSAL TREATMENT