

Second Submission in response to QR's AU3 Access
Undertaking

14 March 2024



1 Introduction

This submission is provided in relation to Queensland Rail's (**QR**) 2025 draft access undertaking (**DAU3**) on behalf of Yancoal Australia Limited (**Yancoal**) in its capacity as operator of the Cameby Downs mine, located on QR's West Moreton rail network.

Yancoal thanks the QCA for the opportunity to comment on the issues raised by the other initial stakeholder submissions provided in respect of DAU3.

Yancoal's key concerns continue to relate to the proposed West Moreton network reference tariff, and notes that the stakeholder submissions, particularly of New Hope and Aurizon Operations, clearly demonstrate those concerns are widely held.

Yancoal's most critical concerns remain that:

- (a) however it is calculated, a tariff of the level sought by QR is unaffordable to coal producers and is very likely to result in a permanent loss of rail volumes that makes the West Moreton system unsustainable; and
- (b) even leaving aside that affordability issue, Yancoal has concerns about inappropriate 'building blocks' being used to calculate the revenue requirement from which the proposed reference tariff is derived.

2 Executive Summary

Yancoal continues to consider that the QCA should refuse to approve DAU3 as submitted, principally on the basis of the inappropriately high West Moreton network reference tariff proposed.

Both major users (New Hope and Yancoal) and the sole rail operator for the West Moreton system have:

- (a) raised the same concerns regarding the affordability of the reference tariffs proposed and the unsustainable future of the line if that was permitted to be charged; and
- (b) opposed material elements of the building blocks to derive the 'revenue requirement' underlying QR's proposed reference tariffs (including the asset beta, 'top down' WACC uplift, and capital expenditure, operation and maintenance costs).

Yancoal considers it is clear that the future of the West Moreton system depends on a more affordability based approach to pricing that corrects those issues.

In respect of non-pricing issues, Yancoal notes that, again, the major users and sole rail operator are aligned that the key issues are improving the rigour of capacity assessment and increasing the robustness of prudency assessment during the undertaking term. Yancoal considers that those issues also need to be addressed in order for DAU3 to be appropriate to approve, particularly in the context of the outages being caused by interaction with the passenger system (and related projects like Cross River Rail) and the intensive capital expenditure program QR is proposing.

3 West Moreton Reference Tariff Issues

3.1 Commonality of concerns

Yancoal notes that many of the key issues and concerns it raised in relation to the West Moreton tariff, have also been raised by the other users of the system (as per the New Hope and Yancoal submission) including:

- (a) the need to set tariffs having regard to tariff affordability – given that an unaffordable tariff may lead to premature closure of mines and be unsustainable;¹
- (b) that the proposed tariffs are unaffordable and economically unviable for West Moreton coal producers;²
- (c) that thermal coal prices are forecast to return to lower levels than those experienced during AU2³ (which Yancoal submits means that QR's reference to higher coal prices as part of the justification for the major tariff increased should be rejected);
- (d) that thermal coal volumes are forecast to remain stable over the medium term⁴ (which Yancoal submits suggests a lower assessment of volume risk than QR has sought to assert);
- (e) the incompatibility in the rationales provided by QR – in claiming substantial capital expenditure on long life assets is prudent and efficient, while simultaneously seeking risk mitigations like accelerated depreciation and uplifts as compensation for volume risk;⁵
- (f) the disingenuity of seeking to allocate fixed costs to coal services based on 97 paths of capacity being available for coal users, only to now claim that record capital expenditure is required to actually provide that same level of capacity;⁶
- (g) that where QR introduces new regulatory mitigants to stranding and volume risk, like the accelerated depreciation profile and volume trigger, it is, contrary to its claims not facing the same volume uncertainty as in AU2, removing any justification for the 'top-down' uplift;⁷
- (h) top-down normalised comparisons to the WACC for the most likely comparator businesses do not provide a justification for any uplift;⁸
- (i) depending how the balance of the Loss Capitalisation Account is recovered, the tariffs stated by QR could be increased further;⁹
- (j) the insufficient level of disclosure provided in relation to proposed expenditure in order to be able to assess prudence;¹⁰
- (k) the lack of a clear business case or demonstrated need for major capital expenditure projects, with any substantiating capacity modelling/analysis demonstrating the requirement to invest in such projects to actually achieve the forecast tonnage;¹¹
- (l) scepticism around the significant increase to the maintenance costs given the extensive capital expenditure/asset replacement program;¹²

¹ Aurizon Operations Submission, 56-61; New Hope Submission, 7.

² Aurizon Operations Submission 56-57; New Hope Submission, 4, 7 and 12.

³ Aurizon Operations Submission, 59.

⁴ Aurizon Operations Submission, 60.

⁵ Aurizon Operations Submission, 56, New Hope Submission, 9.

⁶ Aurizon Operations Submission, 71-72.

⁷ Aurizon Operations Submission, 55-56 and 77; New Hope Submission, 14-16, 25.

⁸ New Hope Submission, 23.

⁹ Aurizon Operations Submission, 55; New Hope Submissions, 24-25.

¹⁰ Aurizon Operations Submission, 72; New Hope Submission, 8, 11, 12.

¹¹ New Hope Submission, 9.

¹² New Hope Submission, 10-11.

- (m) concern that costs were asserted by QR to be largely fixed when coal volume was at its lowest during the AU2 term and as a result costs were allocated on the 97 paths 'available' for coal services, and yet now significant increases in costs are asserted to be required to provide the return to those volumes anticipated¹³. As the Aurizon Operations Submission notes, if significant new capital costs are required, then the AU2 capacity available for coal services was overstated and coal users bore (either directly or through the loss capitalisation account) a disproportionate share of costs such that consideration should be given to a deduction from the loss capitalisation account for the over-recovery by QR¹⁴;
- (n) QR being required to publish a transparent roll-forward of the proposed revenue and building block components across the regulatory period.¹⁵ Yancoal submits that is clearly appropriate so that the QCA has the appropriate information to assess affordability);¹⁶
- (o) inappropriateness of fully depreciating to zero assets which will continue to have physical lives as likely use (at least for non-coal purposes) under QR's accelerated depreciation proposal;¹⁷
- (p) the concern that the high level of overhead and other operating expenditure is driven by the Metropolitan system / passenger service and infrastructure enhancements for them (i.e. Cross River Rail) – such that those costs should not be allocated to coal services;¹⁸
- (q) the need for a bottom-up independent review of material costs;¹⁹ and
- (r) that the WACC should be closer to the WACC of regulated energy and water businesses, which have a more similar risk profile to QR's West Moreton access.²⁰

That should be strong evidence for the QCA that these concerns are real and genuinely and commonly held by the users of the West Moreton network.

3.2 Affordability

Yancoal submits that in considering the affordability issues raised across multiple submissions, the QCA should take into account that:

- (a) the QR proposed tariffs are a very significant increase on the pricing levels that were considered by the QCA to be affordable during the AU2 undertaking process;
- (b) while the AU2 West Moreton reference tariff was ultimately set above the affordability level that Yancoal advocated for, Cameby Downs (and given it was the only producing mine, the West Moreton system) was effectively saved by unanticipated high thermal coal prices as a result of unforeseen trade issues and geopolitical events;
- (c) by contrast thermal coal prices are now declining towards long term pricing levels – such that it would not be appropriate to assume that even the same rail tariffs are realistically affordable;
- (d) at the pricing levels QR is now proposing, there are material risks of mine's ceasing production at the next expiry of their access agreement (when they can exit without triggering a material take or pay liability), compounding the affordability issues for any

¹³ New Hope Submission, 12.

¹⁴ Aurizon Operations Submission, 71-72.

¹⁵ Aurizon Operations Submission, 77

¹⁶ Aurizon Operations Submission, 77-78.

¹⁷ New Hope Submission, 12.

¹⁸ Aurizon Operations Submission, 76; New Hope Submission, 10.

¹⁹ Aurizon Operations Submission, 77; New Hope Submission, 10.

²⁰ New Hope Submission, 14-15.

producers that remain through QR seeking to recover the same revenue over a much small production base;

- (e) there is a public interest in employment, royalties and the broader economic and community contribution West Moreton coal projects make, and passenger and grain services remaining affordable, all of which will cease to be the case if coal services cease or materially reduce; and
- (f) there are now hidden costs to producers which have arisen due to the extent of rail network outages caused by large infrastructure projects or events in the Brisbane Metro area (for example, Cross River Rail construction and Olympics). Additionally, it is not clear as to pathing that will remain accessible for West Moreton services through the Brisbane Metro rail network once those projects are completed and passenger rail traffic is increased as a result. To mitigate, Yancoal has had to contract additional haulage services (at greater cost) to be able to transport the same volume of product and is at greater risk of outages causing additional supply chain and stockpiling costs (such as storage, rehandle and demurrage costs).

3.3 Two part-tariff

Yancoal strongly disagrees with New Hope's criticism of the two-part tariff structure.²¹

The QCA has previously considered this tariff structure and considered it appropriate across multiple undertakings.

As the QCA noted in its final decision in respect of QR's 2020 draft access undertaking:²²

The distance taper aims to strike a balance between the user pays principle, revenue adequacy and fostering development along the West Moreton system. It recognises that mines closer to the Port of Brisbane (e.g. New Hope's New Acland mine) do not use infrastructure west of their haulage point—but consume capacity so that fewer paths are available to access seekers further west (e.g. Yancoal's Cameby Downs mine). This means supplying a train path with an origin closer to the port carries an inherent opportunity cost to Queensland Rail (which requires sufficient revenue to cover access to the entire system) and the distance taper provides for users closer to the port to pay a portion of that cost.

....

Our decision is that, while there is still an expectation that New Acland or another mine may contract for access on West Moreton during the term of the 2020 undertaking, it is appropriate to retain the distance taper approach in the pricing structure. When volumes are high, the distance taper helps balance the competing objectives of cost reflectivity and revenue adequacy by:

- *having miners closer to the port pay less for access than those further away, which is consistent with the user pays principle (ss. 138(2)(a), (e), (h))*
- *encouraging economic development by mitigating some of the cost disadvantage faced by mines further from the port (ss. 138(2)(d), (h))*

²¹ New Hope Submission, 13.

²² Queensland Competition Authority, *Decision – Queensland Rail 2020 draft access undertaking*, February 2020, 16-17

• *addressing in part the opportunity cost to Queensland Rail of selling a shorter path, which it might otherwise have been able to use for a more distant mine that provided more revenue (s. 138(2)(b)).*

The balance remains appropriate.

In addition Yancoal notes:

- (a) a change to the tariff structure of the type New Hope is proposing for Cameby Downs is unaffordable and will result in Cameby Downs losing significant amounts and ceasing operations, materially increasing the costs to be borne by remaining users;
- (b) the recent re-opening of the Wilkie Creek mine demonstrates that the distance taper has in fact played its part in encouraging economic development – adding volume to the line which should reduce the cost per tonne;
- (c) it is clearly inequitable and inappropriate that after years of Cameby Downs alone bearing the costs of the West Moreton system, upon New Hope's volumes returning it is willing to try to distort the allocation of costs in New Hope's favour; and
- (d) it appears from QR's submission that the vast bulk of the capital expenditure relates to the section west of Jondaryan in any case.

3.4 Private Infrastructure

Yancoal does not agree that the Columboola spur and loop being included in QR's regulatory asset base creates the inequitable outcome New Hope asserts or QR not funding the New Acland Stage 3 loop should result in a discount to New Hope's tariffs.²³

The development of the Columboola spur and loop infrastructure was effectively funded by Yancoal's payment obligations under an Access Facilitation Deed with QR. Yancoal is intended to receive rebate based on part of the regulated return QR derives from that funded asset (although the loss capitalisation has had the effect that no rebate has been payable during the period where loss capitalisation has applied).

The intent of those arrangements should not be overturned by unanticipated changes to the tariff structure. To do so now, creates windfall gains and losses where QR and Yancoal have made their funding and contracting decisions in respect of the Columboola loop, and New Hope has developed New Acland Stage 3 and contracted access, in both cases without any indication the treatment of private infrastructure would be altered as New Hope now seeks.

Yancoal also draws the QCA's attention to the fact that the requirement for New Hope to build a new rail load out was, unlike the Aurizon Network example referenced by New Hope, not imposed by a decision by the rail infrastructure manager to cease funding mine-specific spurs and loop infrastructure, but rather a condition of its approvals that it develop a rail loop to address noise issues (associated with the use of a front loader at the previous loop).

It is inappropriate for a producer (New Hope) to be cross-subsidised by other users (i.e. Yancoal) paying a higher tariff to provide a discount for costs the first producer incurs in meeting the conditions of their regulatory approvals (which will differ between projects). This type of cross-subsidisation is not efficient or appropriate.

3.5 Aurizon Network submissions

Yancoal submits that the submission on West Moreton tariff matters received from Aurizon Network, which is not even a stakeholder in respect of the system, should be given very limited weight.

²³ New Hope Submission, 13-14.

That submission:

- (a) Is transparently self-serving in seeking to advance positions Aurizon Network considers will be to its benefit in respect of the next central Queensland coal network access undertaking; and
- (b) fails to meaningfully engage with the circumstances of the West Moreton system and what they may mean for the appropriate outcome of the undertaking.

4 Non-pricing issues

4.1 Capacity assessment and modelling

Both New Hope and Aurizon Operations have raised similar concerns to Yancoal in relation to the lack of transparency regarding system capacity.²⁴

Without clarity regarding system capacity, Yancoal submits that:

- (a) it is difficult to ascertain what capital expenditure is genuinely required to provide the contracted system capacity (and whether a particular capital expenditure project is the prudent and most efficient way to improve capacity); and
- (b) users are not able to rely on receiving their contracted system capacity (resulting in losses of sales and extra costs in respect of haulage and demurrage).

Yancoal supports each of:

- (c) the submissions from Aurizon regarding the need for QR to disclose key assumptions made in its network capacity analysis; and
- (d) the submissions from New Hope regarding an independent capacity assessment (as also put forward by Yancoal).

4.2 Capital expenditure during the undertaking term

Yancoal also supports each of

- (a) the submissions by New Hope regarding approval of capital expenditure during the term of the undertaking (as also put forward by Yancoal) – which Yancoal considers is of heightened importance in the current scenario where there are currently reasons to doubt QR's assessment as to what capital expenditure is prudent; and
- (b) the submissions and drafting proposed by New Hope in relation to a capital expenditure 'true-up' (as where a very extensive capital program is proposed resulting in materially higher tariffs, Yancoal agrees that an underspend should be passed through to users within the term to alleviate the financial pressure).

Where QR is seeking a very significant capital expenditure program it is difficult to see how it can be accepted as prudent given the current lack of transparency around system assumptions and modelled capacity, and the context of QR at the same time claiming there are significant volume risks which warrant accelerated depreciation,

5 Conclusion

For the reasons set out in its initial submission and in the further analysis above, Yancoal submits that the QCA should refuse to approve the DAU3 as submitted, principally on the basis of the inappropriately high West Moreton network reference tariff proposed.

Yancoal notes that both major users and the sole rail operator for the West Moreton system have:

²⁴ Aurizon Operations Submission, 61-64

- (a) all raised the same concerns regarding the affordability of the reference tariffs proposed and the unsustainable future of the line if that was permitted to be charged; and
- (b) opposed material elements of the building blocks to derive the 'revenue requirement' underlying QR's proposed reference tariffs (including the asset beta, 'top down' WACC uplift, and capital expenditure, operation and maintenance costs).

Yancoal considers it is clear that the future of the West Moreton system depends on a more affordability based approach to pricing being implemented for AU3.

In respect of non-pricing issues, Yancoal notes that again the major users and sole rail operator are aligned that the key issues are improving the rigour of capacity assessment and increasing the robustness of prudency assessment during the undertaking term. Yancoal considers that those issues also need to be addressed in order for DAU3 to be appropriate to approve, particularly in the context of the outages being caused by interaction with the passenger system and the intensive capital expenditure program QR is proposing.

As always, please do not hesitate to contact Mike Dodd of Yancoal Australia Limited on [REDACTED] [REDACTED] if you have any queries in relation to this submission.