

Queensland Rail Limited

Board Directive: Financial Framework

1. FINANCIAL MANAGEMENT

- 1.1 The Chief Financial Officer shall:
 - 1.1.1 prepare management and performance reports for each Queensland Rail Limited Board meeting, which are indicative of measures, controls and performance achieved in meeting Queensland Rail Limited Group's financial objectives. These reports will note any non-compliance with this Board Directive and provide a brief comment on any action required to remedy the non-compliance.
 - 1.1.2 ensure Queensland Rail Limited Group's statutory financial reporting obligations are met.
- 1.2 The Chief Financial Officer shall manage financial operational risk by establishing:
 - 1.2.1 roles, responsibilities and authority for those staff involved in financial processes;
 - 1.2.2 adequate segregation of duties among staff to minimise the risk of error or fraud and enhance the detection thereof;
 - 1.2.3 restrictions on access to Queensland Rail Limited's Financial Risk Management Systems;
 - 1.2.4 appropriate processes for assessing counterparty trade-related credit risk, including determining whether third party guarantees or securities are required; and by
 - 1.2.5 ensuring audits are undertaken at regular intervals, the timing of which will be determined via risk assessments, to verify risks have been diligently identified, evaluated and controlled.

2. BALANCE SHEET MANAGEMENT

- 2.1 Establishment of Subsidiary Companies & Joint Ventures
 - 2.1.1 The establishment of a subsidiary company or joint venture ("entity") is subject to Queensland Rail Limited Board and shareholding Minister approval.
 - 2.1.2 Submissions to the Queensland Rail Limited Board seeking approval to establish a new entity must include a recommendation from Queensland Rail Limited's Corporate Counsel and Chief Financial Officer. The submission will, at a minimum, include:
 - 2.1.2.1 a business case for establishing the entity and the associated investment;
 - 2.1.2.2 capital structure and weighted average cost of capital;

This Board Directive applies to Queensland Rail Limited and its subsidiary companies

- 2.1.2.3 funding arrangements;
- 2.1.2.4 governance arrangements;
- 2.1.2.5 a recommendation on the provision of a Queensland Rail Limited parent guarantee (limited to Queensland Rail Limited's equity interest); and
- 2.1.2.6 a comprehensive risk analysis.

2.2 Capital Structure

- 2.2.1 The Chief Financial Officer will recommend a capital structure to the Queensland Rail Limited Board that reflects the target mix of debt and equity to be used to fund operations.
- 2.2.2 The nominated target gearing is:
$$\frac{45\% (+/- 5\%) \quad \textit{debt}}{\textit{debt} + \textit{equity}}$$
- 2.2.3 Capital structure shall be reviewed annually.
- 2.2.4 Target capital structures are to be calculated for each of Queensland Rail Limited Group's businesses for the purpose of determining a cost of capital for each.

2.3 Dividend Payout Ratio

Subject to shareholder requirements, Queensland Rail Limited's dividend payout ratio (percentage of after tax profit) will be determined based upon commercial considerations and reviewed annually.

2.4 Evaluation and approval of Investments

- 2.4.1 Queensland Rail Limited Group has an Investment Framework to:
 - 2.4.1.1 focus Queensland Rail Limited Group on making commercial decisions and achieving sustainable financial performance;
 - 2.4.1.2 ensure Queensland Rail Limited Group's capital allocation is optimal for the corporation;
 - 2.4.1.3 provide a centralised/independent review process for investments on behalf of the corporation;
 - 2.4.1.4 provide strategic oversight for Queensland Rail Limited Group's investments and ensure all business cases are financially sound; and
 - 2.4.1.5 ensure business groups are accountable to deliver projects as proposed in business cases.
- 2.4.2 The Investment Framework applies to the review and endorsement of all investment proposals, that exceed business delegation limits where applicable, in the following categories:
 - 2.4.2.1 capital expenditure;
 - 2.4.2.2 operating expenditure (including expenditure contracts);
 - 2.4.2.3 all mergers, acquisitions and divestments;

This Board Directive applies to Queensland Rail Limited and its subsidiary companies

- 2.4.2.4 revenue contracts for rail haulage and external contracts;
 - 2.4.2.5 a 10% change in the financial outcome of an approved strategy;
 - 2.4.2.6 all joint ventures, partnerships, alliances or similar arrangements;
 - 2.4.2.7 investments in other entities, including loans to customers; and
 - 2.4.2.8 all business proposals (binding and non-binding) that involve the potential for a major expenditure commitment (e.g. tenders, risk sharing agreements and production sharing agreements).
- 2.4.4 The Chief Financial Officer and/or Chief Executive Officer will subsequently make a formal decision on each business case.
- 2.4.5 All business cases above the Chief Executive Officer delegation limits will require Board approval.
- 2.4.6 Queensland Rail Limited Group shall undertake the financial evaluation of projects on a net present value basis using an appropriate discount rate. The discount rate used will equate to the appropriate hurdle rate for the business unless the Chief Financial Officer has determined that a project specific discount rate, established with regard to the unique risk characteristics of the project, should apply. These rates are to be reviewed annually (in accordance with Queensland Rail Limited's WACC methodology as determined by the Chief Financial Officer) and approved by the Queensland Rail Limited Board.
- 2.4.7 Any overseas investments (excluding consulting services) shall be approved by the Queensland Rail Limited Board before seeking approval of the shareholding Ministers.
- 2.4.8 For all approved investments exceeding \$20 million, written notification must be provided to the shareholding Ministers.
- 2.4.9 All investment proposals which exceed \$100 million must be approved by the Queensland Rail Limited Board before seeking approval of the shareholding Ministers.

3. TREASURY RISK MANAGEMENT

3.1 Risk Appetite

Queensland Rail Limited's risk appetite is risk averse indicating a preference for minimising uncertainty, low volatility and eliminating downside risk where appropriate.

3.2 Objectives

- 3.2.1 To minimise the impact of interest rate volatility on the Profit & Loss Statement.
- 3.2.2 To minimise the impact of foreign currency and commodity price movements on the Profit & Loss Statement through monitoring and effective mitigation of exposures.
- 3.2.3 To minimise the impact of foreign currency and commodity price movements on the Balance Sheet through identification and mitigation of capital expenditure related exposures.

This Board Directive applies to Queensland Rail Limited and its subsidiary companies

3.2.4 To support business units to minimise the impact of foreign currency and commodity price movements on capital expenditure and operating expenses where appropriate.

3.3 Centralised Approach

Treasury risk management activities will be undertaken by Queensland Rail Limited Group's central treasury division following the framework determined and maintained by the Chief Financial Officer.

3.4 Financial Credit Risk

No financial transaction will be entered into that will result in a credit exposure for the Queensland Rail Limited Group to a counterparty, other than Queensland Treasury Corporation, that exceeds:

3.4.1 5% of the shareholders' funds of Queensland Rail Limited Group as shown in its most recent published annual report;

3.4.2 the term indicated, with reference to the long-term rating of the counterparty, in the table below.

Standards & Poor's (or equivalent) rating	Maximum Term
AAA	Up to 10 years
AA+	Up to 10 years
AA	Up to 10 years
AA-	Up to 5 years
A+	Up to 3 years
A	Up to 3 years
A-1	Up to 1 year

3.4.3 In addition to counterparties that comply with the above requirements, the Queensland Rail Limited Board has approved two other counterparties that may be used.

These are:

Counterparty	Rating	% of Shareholder s' Funds	Maximum Term
BP Oil International Ltd.	Not rated	3.0%	Up to 1 year
HSBC Malaysia	BB+	\$5 million	Up to 2 years

3.4.4 Counterparties for Cross Border Leases are exempt from Queensland Rail Limited Group's credit limits. Entering into a new cross border lease transaction requires Queensland Rail Limited Board approval.

This Board Directive applies to Queensland Rail Limited and its subsidiary companies

- 3.4.5 The balance sheet of the parent of the counterparty may be substituted for that of the counterparty for the purposes of establishing a credit term, only where the counterparty is the beneficiary of an unconditional parent guarantee and the Chief Financial Officer deems the form of the guarantee satisfactory.

The credit limit and maximum term of exposure for Queensland Treasury Corporation shall be unlimited. Counterparty credit limits are also subject to the counterparty being domiciled in the following countries:

- Australia
- Canada
- People's Republic of China (Hong Kong)
- France
- Germany
- Ireland
- Japan
- Malaysia
- Netherlands
- New Zealand
- Singapore
- Sweden
- Switzerland
- United Kingdom
- United States of America

3.5 Interest Rate Risk

To mitigate the financial risk associated with movements in interest rates the following requirements apply:

- 3.5.1 Interest rate exposure will be managed with reference to average target benchmark durations for each debt pool with Queensland Treasury Corporation ("QTC"):
- 3.5.1.1 The benchmark duration of the two Queensland Rail Limited Network debt pools will match as far as practical the duration assumed in the below rail Transport Service Contract (TSC) and the Queensland Competition Authority (QCA) determination;
 - 3.5.1.2 The benchmark duration of the remaining QTC debt pool/s must remain as close as practical to 4.5 years.
- 3.5.2 The Chief Financial Officer is delegated authority to exercise a debt management range of +/- 1.0 years around the target benchmark duration of these facilities.
- 3.5.3 The target benchmark duration of each debt pool is to be regularly reviewed. Reviews are to occur at least once during each QCA regulatory cycle or TSC negotiation for the Queensland Rail Limited Network debt pools and every three years for remaining debt pools.
- 3.5.4 Individual debt pools may be established for subsidiary company funding.

3.6 Currency/Commodity Risk

The risk of movements in foreign currency purchases and the price of the commodities Queensland Rail Limited Group purchases through the normal course of business will be mitigated by:

This Board Directive applies to Queensland Rail Limited and its subsidiary companies

- 3.6.1 A centralised approach, therefore all related transactions will be undertaken by Queensland Rail Limited Group's central treasury division;
- 3.6.2 Those involved in contract negotiations promptly advising the Queensland Rail Limited Treasurer of all potential exposures that exceed AUD 1 million equivalent during the contract term; and
- 3.6.3 The Chief Financial Officer managing Queensland Rail Limited Group's currency and commodity hedging in accordance with the following limits:

Minimum Hedge %	Delegated Range %	Forecast Exposures
80% hedged	+ 20% i.e. (80% to 100%)	Up to 1 year
70% hedged	+ 30% i.e. (70% to 100%)	From 1 year up to 2 years
60% hedged	+ 40% i.e. (60% to 100%)	From 2 years up to 3 years

- 3.6.4 Speculative trading or trading for profit is prohibited.
- 3.6.5 Restricting Queensland Rail Limited Group's currency/commodity management to hedging underlying business created exposures.

3.7 Derivatives Risk

- 3.7.1 Derivative transactions may only be entered into for the purpose of hedging exposures that arise in the normal course of Queensland Rail Limited Group's business (e.g. foreign currency, commodity price and interest rate risk).
- 3.7.2 Approved derivative risk Instruments are:
- 3.7.2.1 foreign currency forward exchange contracts.
 - 3.7.2.2 foreign currency swap agreement.
 - 3.7.2.3 interest rate forward rate agreements.
 - 3.7.2.4 interest rate swap agreements.
 - 3.7.2.5 commodity swap contracts.
 - 3.7.2.6 interest rate option contract.

3.8 Treasury Operational Risk

The Chief Financial Officer will manage treasury operational risk by ensuring:

- 3.8.1 adequate segregation of duties among front, middle and back office staff to minimise the risk of error or fraud and enhance the detection thereof;
- 3.8.2 restrictions on access to the Treasury Risk Management System;
- 3.8.3 the preparation and maintenance of treasury procedures covering key operational aspects of treasury management;
- 3.8.4 front, middle and back office staff maintaining minimum competency standards;

This Board Directive applies to Queensland Rail Limited and its subsidiary companies

4. FUNDING

4.1 Centralised Approach

All procurement of funding, bank guarantees and cross border lease transactions and liquidity risk management will be undertaken by Queensland Rail Limited's central treasury division.

4.2 Procurement of Funding

When procuring new funding, Queensland Rail Limited Group shall comply with the requirements of the Code of Practice for Government Owned Corporations Financial Arrangements, October 2004.

Specifically, Queensland Rail Limited shall:

- 4.2.1 ensure borrowings are within the approved State Borrowing Program (SBP) allocation;
- 4.2.2 review semi-annually the approved SBP allocation;
- 4.2.3 acknowledge that Queensland Rail Limited Group's obligations are not guaranteed by the State; and
- 4.2.4 include Queensland Treasury Corporation in any tender or quote for financial arrangements.

4.3 Bank Guarantees

The Queensland Rail Limited Treasurer is responsible for procuring guarantees and standby letters of credit from the most efficient provider for all businesses.

4.4 Leasing

- 4.4.1 No business will enter into a material lease or hire transaction (excluding real property leases), where the actual or expected term to maturity exceeds 12 months without the written approval of the Queensland Rail Limited Treasurer.
 - 4.4.2.1 Queensland Rail Limited Board approval is required to enter into a new cross border lease (CBL) transaction.

4.5 Liquidity Risk

The risk of an unforeseen event or counterparty reluctance in providing the required liquidity level will be mitigated by:

- 3.6.1 Generating and monitoring short-term and long-term cash flow forecasts to enable liquidity risk to be efficiently managed;
- 3.6.2 Maintaining short-term borrowing and investment facilities to manage the Queensland Rail Limited Group's working capital requirements;
- 3.6.3 Maintaining a centralised banking facility to meet the Queensland Rail Limited Group's banking requirements;
- 3.6.4 Establishing State Borrowing Program approvals to cover 110% of the anticipated annual borrowing requirement; and
- 3.6.5 Maintaining long-term borrowing facilities to meet the Queensland Rail Limited Group's ongoing funding requirements.

This Board Directive applies to Queensland Rail Limited and its subsidiary companies

5. TAX

5.1 Centralised Approach

Queensland Rail Limited requires a consistent approach on all material tax activities across the Queensland Rail Limited Group. Queensland Rail Limited's Tax Unit shall be informed of:

- 5.1.1 major capital investments, including mergers, acquisitions and divestments;
- 5.1.2 joint ventures, partnerships, alliances or similar arrangements;
- 5.1.3 all business proposals that involve the potential for a major expenditure commitment; and
- 5.1.4 tax compliance activities of the Queensland Rail Limited Group.

5.2 Tax Risk Management Approach

Queensland Rail Limited Group will undertake tax positions most favourable to Queensland Rail Limited in all circumstances where it is reasonably arguable to do so. In determining the position to be taken, the following should be considered:

- 5.2.1 The merit of the technical aspects of the issue;
- 5.2.2 The materiality of the issue;
- 5.2.3 The likely resources required to sustain any position taken; and
- 5.2.4 The corporate impact of taking a position that is disputed by the respective revenue authority.

6. DEFINITIONS

All terminology used within this document is in accordance with Queensland Rail Limited's Terminology and Definitions standard GEN/STD/1002/ADM. Except for the following:

“Financial credit risk” – includes credit exposures to counterparties with which Queensland Rail Limited Group has entered into financial transactions.

“Financial transaction” – is a transaction with a counterparty that creates a financial exposure for Queensland Rail Limited Group, but does not include operational exposures from carrying on the normal course of Queensland Rail Limited Group's business (e.g., contracts with suppliers to procure goods and customers to deliver a service). Financial transactions include but are not limited to: - Foreign Currency hedging transactions - Commodity hedging transactions - Interest Rate hedging transactions - Cross Border Lease exposures / defeasance assets - Leasing transactions (domestic) - Bank Investments and deposits - Acceptance of Bank guarantees / Letters of credit - Interest bearing loans and receivables

“Trading for profit (Speculative trading)” – is a form of portfolio management with the intention of profit making only, without reference to any of Queensland Rail Limited Group's underlying business exposures or intentionally exceed the underlying physical exposure. Trading for profit includes unreasonable frequent buying and selling of instruments over a short term timeframe.

This Board Directive applies to Queensland Rail Limited and its subsidiary companies