Mount Isa Line — Q&A

2017–18 Below Rail Financial Statements

What are the Below Rail Financial Statements?

Queensland Rail prepares an Annual Report and Financial Statements, as required by the *Financial Accountability Act 2009.* These Financial Statements detail the overall financial performance of Queensland Rail.

Queensland Rail's Access Undertaking 1 (AU1), which is approved by the Queensland Competition Authority (QCA), requires the preparation of Below Rail Financial Statements.

The Below Rail Financial Statements are a subset of Queensland Rail's Financial Statements. They allocate assets, costs, revenues and investments related only to Queensland Rail's below-rail services. The Below Rail Financial Statements excludes passenger stations and associated facilities as they are not required to enable the operation of freight train services.

Queensland Rail is required to prepare separate Below Rail Financial Statements for the West Moreton System, Mount Isa Line, North Coast Line and Metropolitan System.

What are the Below Rail Financial Statements used for?

The Below Rail Financial Statements are intended to provide interested stakeholders with information about the revenues and costs of providing the declared rail infrastructure services.

The Below Rail Financial Statements are based on the accounting performance of the business and are not used by the QCA for setting prices.

Is Queensland Rail earning monopoly returns on the Mount Isa Line? [1]

Queensland Rail's Below Rail Financial Statements show a 6.1% return on assets (ROA) in 2017–18. It is not correct to compare the ROA in the Below Rail Financial Statements for the Mount Isa Line with a regulated return that would be set by the QCA.

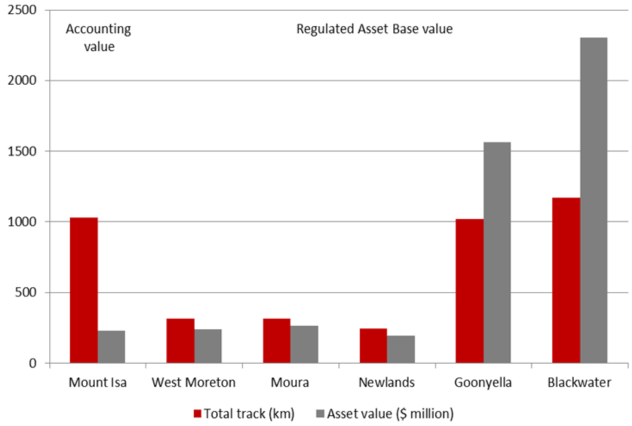
The perception of a high return on the Mount Isa Line assets arises because a comparison is being made to the accounting value of the Mount Isa Line assets — $267 million as at 30 June 2018— not a Regulated Asset Base (RAB) value.

The QCA has not assessed what the RAB value would be for the Mount Isa Line. However, as shown in Figure 1, the accounting value for the Mount Isa Line is lower than the RAB values for the West Moreton system and for Aurizon's Moura system — even though the track length is more than three times longer. The Mount Isa Line has a similar track length to Aurizon's Goonyella system, and while there are differences in the track standard, the RAB value for the Goonyella system is almost seven times higher than the Mount Isa Line's accounting valuation.

To make a like-for-like comparison between the return on the Mount Isa Line and the return from assets regulated by the QCA would require the Mount Isa assets to be valued in the same way. The modified Depreciated Optimised Replacement Cost (DORC) valuation for the Mount Isa Line (the methodology the QCA applied to the West Moreton RAB) was estimated at $1.343 billion as at 1 October 2016.

[1] A monopoly return is considered to occur where the revenue earned from declared infrastructure is above the return that a regulator would apply to a regulated asset. The QCA decided that the benchmark rate of return for the West Moreton assets for the AU1 period was 5.73% post tax nominal vanilla WACC (equivalent to 6.34% pre-tax WACC).

Figure 1: Asset values and track lengths — different valuation approaches as at 30 June 2017



Source: Queensland Rail Below Rail Financial Statements, West Moreton MAR, Aurizon UT5 Submission, system information packs

If Queensland Rail's assets for the Mount Isa Line were valued based on the DORC methodology, the revenue in 2017-18 was insufficient to cover the operating, maintenance and higher depreciation costs, so from a regulatory perspective was operated at a loss.

What does AU1 say about how access charges on the Mount Isa Line should be set?

AU1 requires Queensland Rail to set its access charges so that its expected access revenue

- at least covers the floor costs of providing the services and
- does not exceed the ceiling revenue.

System floor costs are considered to be the operating, maintenance and capital renewal costs of providing the service.

Ceiling revenue includes earning a commercial return on the assets used to provide the service, plus the depreciation of the asset.

How does Queensland Rail set prices on the Mount Isa Line?

Queensland Rail sets its access charges on the Mount Isa Line so that it at least covers the operating, maintenance and capital renewal costs of providing service (**system floor revenue**), taking into account the forecast volumes on the system.

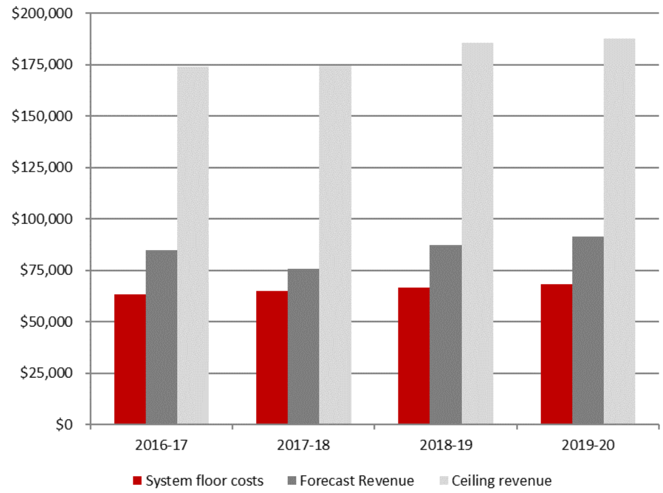
Queensland Rail does not receive government subsidies for the provision of infrastructure access services on the Mount Isa Line, so if it is not able to cover these costs, the service is not financially sustainable.

Access revenue is important to support the maintenance and asset renewal on the Mount Isa, so that rail remains a safe and reliable link in the North West Minerals Province export supply chain.

Further, as the rail transport is in direct competition with road transport for a number of the commodities hauled on the Mount Isa Line, particularly intermodal freight, Queensland Rail's objective is to set its access charges to ensure rail transport remains competitive with road transport.

Based on current volumes and prices on the Mount Isa Line, Queensland Rail's access charges recover less than half of the ceiling revenue and only marginally above the floor costs (Figure 2).

Figure 2: Estimated system floor costs, access revenue and ceiling revenue — Mount Isa Line 2016–17 to 2019–20 ($'000)



Source: Queensland Rail