

revenue cap arrangements that have been implemented, including for DBCT.

- Where variations in tonnage are expected by QR to be outside the 2% proposed by the QRC, there is little or no incentive to increase (or reverse a deterioration in) system performance or volumes. As indicated at Section 3.2.2 above, the variation in tonnage relative to the System Forecasts for 2006/07 and 2008/09 is expected to be well above 2%. Accordingly, the volume incentive would provide QR with little or no Below Rail incentive to improve either performance or volumes in these years.
- QR would still be exposed to some degree of forecasting risk associated with UT3 and subsequent Undertakings. QR considers this risk to be asymmetric, as end customers will be incentivised to promote a set of QCA endorsed forecasts which over-estimates the level of tonnage such that the expected outcome is an under-recovery (of which the first 2% would be absorbed by QR).
- QR's development of its proposals, particularly with respect to the relief for Take or Pay and Relinquishment Fees, has been on the principle that the costs of any proposal are shared amongst Access Holders via the revenue cap. The volume incentive is inconsistent with this principle, where an under-recovery is within the 2% threshold the incremental cost of these proposals is effectively supported by QR.

With respect to QR Cause the following matters are relevant:

- An adjustment for QR Cause is inconsistent with the principle of a revenue cap, being that all of QR's allowable revenue should be recovered from Access Holders. In addition, QR Cause is effectively a downside (and therefore asymmetric) element of volume risk for which QR receives no compensation through Reference Tariffs.
- QR is not aware of a similar provision having been included in other revenue cap arrangements.
- The Standard Access Agreement already provides contractual remedies for an Access Holder against QR for any loss or damage arising from either:
 - A wilful default of the Access Agreement; or
 - Any deliberate or negligent act or omission by QR.

In view of the above, a 2% volume increment modelled on the DBCT arrangements is a reasonable compromise to the QRC's proposal for a volume incentive. In addition, the proposal is consistent with the principles of a revenue cap form of regulation and does not place QR in a position more favourable than the proposals accepted by the QCA in respect of DBCT.

In this regard, QR notes the QCA's comments on its own proposal for a volume incentive at p.105 of its April 2005 Final Decision in respect of DBCT's draft access undertaking:

"This proposed flexibility to the revenue cap mechanism should increase incentives to obtain efficiency improvements while retaining the characteristics of moving the

majority of the volume risk to the users, and providing DBCT Management with a level of revenue security with regard to any capital expenditure undertaken.”

Whilst QR rejects the QRC's position as set out in its position document, it does understand the QRC's concern regarding the lack of a clear, simple and transparent mechanism to incentivise Below Rail performance. However, whilst the intention of the QRC proposal is to expose QR to performance risk, its effect in this case is to expose QR to a greater degree of volume risk.

In this regard, QR would be pleased to work with the QRC to review a range of alternative mechanisms for rewarding QR performance as part of the development of UT3.

7.3 UNDERS-AND-OVERS MECHANISM

7.3.1 QR's proposal

QR proposes that 100% of the over or under-recovery of System Allowable Revenue, adjusted for any volume increment, in a financial year be subsequently returned or recouped, through adjustments to the relevant Reference Tariff components for each of the Central Queensland coal systems.

The value of the under and overs adjustment would be determined following the end of each financial year. The adjustment would be calculated as follows:

- Adjustment to AT_{2-4} = Total Actual Revenue for AT_{2-4} for each system (Total Actual Revenue) inclusive of relevant Take or Pay amounts, Relinquishment Fees and transfer fees (less any reductions related to these fee types)

LESS allowable revenue for AT_{2-4} (System Allowable Revenue)

- Adjustment to AT_5 = Total Actual Revenue for AT_5 for each of the Goonyella and Blackwater systems

LESS System Allowable Revenue for AT_5

With respect to the adjustment to AT_{2-4} , Total Actual Revenue would be determined by reference to the Year in which the relevant Take or Pay amounts Relinquishment Fee and transfer fee is recovered and any reduction is made. For example, if a reduction is made to a Relinquishment Fee resulting in a refund payable in a subsequent Year, then the refund will be a deduction incorporated in Total Actual Revenue for the subsequent Year.

The revenue cap adjustment would be applied to the Reference Tariffs calculations for the second financial year following the subject year. For example, for the first financial year (2006/07), the value of the adjustments (being the under or over recovery) for each system's AT_{2-4} and the Electric Tariff (AT_5) would be added to (or subtracted from) the allowable revenues underlying the AT_{2-5} Reference Tariffs for the 2008/09 financial year commencing 1 July 2008.

The dates at which the revised Reference Tariffs would take effect would be consistent with the revision dates for quarterly inflation adjustments (i.e. 1 July each year).

For the 2007/08 financial year, the adjustments would be made against the allowable revenues underlying AT₂₋₄ and AT₅ for the 2009/10 financial year and so on for subsequent financial years.

An allowance for the funding of the net total of the adjustments - at QR's Discount Rate, or weighted average cost of capital - would be added to (or subtracted from) any adjustment. The allowance would be assessed over 2 years, being the period between the end of the financial year and the last date the revised Reference Tariffs take effect.

The Proposed Schedule F Amendment reflects QR's proposal via the following:

- Subclause 5.2 of Part A, which defines AT₂₋₄, System Allowable Revenue and Total Actual Revenue; and
- Subclause 3B.1 and 3B.3 of Part B, which details how the revenue cap adjustment is determined and reflected in a variation to Reference Tariffs.

7.3.2 Commentary

Some of QR's access charge revenue is paid to QR net of rebate payments. For the purposes of the revenue cap adjustment calculations, these payments will be adjusted against access charge revenue (i.e. system Total Actual Revenue is determined on a gross basis).

Further comments on the effect of the Proposed Schedule F Amendment on rebate payments are provided at Section 7.5 below.

QR has proposed that the process adopted for amending the Reference Tariffs is substantially that set out in Subclause 3.3 of Part A.

7.3.3 QRC's position

Other than the amount of the over or under-recovery which would be subsequently returned or recouped, which is discussed at Section 7.2 above, QR's proposals for the unders and overs mechanism are consistent with QR's understanding of the QRC's position document.

7.4 MINOR CONSEQUENTIAL AMENDMENTS

Other consequential amendments are minor and are summarised below.

- A number of numbering changes have been made to Schedule F to reflect the addition of various Subclauses. These changes are reflected in the marked-up document at Attachment B.
- A number of formatting changes have been made to Schedule F to improve consistency in the presentation of Parts A, B and C. These changes are not reflected in the marked-up document at Attachment B.

7.5 POSSIBLE FUTURE CONSEQUENTIAL AMENDMENTS

Subclause 6.5.2 states that in certain circumstances, QR may require an Access Seeker to agree to Access Conditions before being granted Access Rights, to the

extent that this is reasonably required in order to mitigate QR's exposure to the financial risks associated with providing access.

The subclause then provides for the payment of rebates in certain circumstances as follows:

“If an Access Condition results in QR earning revenue from the Access Seeker's Access that is in addition to the ongoing Access Charge (e.g. an upfront contribution or Access Facilitation Charge), QR will:

- (i) negotiate an agreement separate from the Access Agreement with the party who agreed to pay such additional revenue (or their nominee Access Seeker) which will provide for payment of a rebate to that party or their nominee, where the rebate is equivalent to the amount provided in the Access Charge for a cost component to the extent that this component is separately funded through the additional revenue (e.g. depreciation and the non-diversifiable component of the return on any relevant additional Rail Infrastructure, or modification of existing Rail Infrastructure)*”

QR has entered into a number of rebate arrangements with end customers. An unintended consequence of the revenue cap arrangements is that modifications to the rebate calculation methodology in each rebate arrangement may be required to ensure that effect can be given to the intent of the Proposed Schedule F Amendment.

The Proposed Schedule F Amendment assumes that these modifications can be made either in accordance with the terms of each rebate arrangement or as a separate agreement with each of the end customers. However, if it transpires that modifications are unable to be made or agreed then QR will consider submitting a voluntary draft amending undertaking to take effect prior to 30 June 2007.