

## Chapter 14 - Contributed Assets

### KEY ASPECTS

**Evidence** - past contributions will only be recognised where recognition is justified by way of documentary evidence.

**Extent of recognition** - the amount of contribution that is recognised will be based on that documentary evidence.

## 14.1 Introduction

Since the 1960s, QR has required coal mine developers to make substantial capital contributions to the construction, augmentation and upgrading of rail facilities. In response to subsequent changes in the legal, financial and taxation environment, the approach adopted by the Queensland Government and QR in recognising and treating these contributions has involved a mix of arrangements which have evolved over time.

An examination of the implications of past user-funded capital contributions for asset pricing could therefore be considered in light of the historical background in which the contributions were made.

There is an argument that these users, having funded the initial capital for infrastructure to service a mine, should not be required to pay for those assets again by being required to pay rail freight charges that include a commercial return on assets that they have directly provided.

Alternatively, it may be argued that capital contributions represent past and irreversible cash flows, and as such ‘bygones should be bygones’. The possible recognition of past capital contributions, perhaps after many years, could potentially result in the rewriting of contracts that have already expired.

If past contributions are to be recognised, further issues arise concerning the quantification of the benefit that current mines should have recognised under the access arrangements. Establishing the method by which credits should be quantified raises a number of issues that refer back to the time at which the contributions were made.

## 14.2 Recognition of contributed assets

### *Background*

The QCA determined that past capital contributions should only be recognised where documentary evidence demonstrates that recognition beyond the existing haulage contract is justified. The extent of the recognition will be based on that evidence. In these instances, such contributions will be dealt with through respective rail haulage agreements.

### *Stakeholder views*

**QR** - will continue to honour any existing contractual obligations that it has, through its existing rail haulage contracts, in respect of past user funded capital contributions.

**FreightCorp** - recommends the QCA:

- modifies its position on the recognition of contributed assets in the calculation of access charges;
- requires QR to provide the details of the contributions, the remaining value and the methodology used to allocate the remaining value; and
- applies the remaining value of contributed assets to the reduction of access charges.

**QMC** - the Draft Decision’s treatment of contributed assets is methodologically deficient.

The Draft Decision not accounting for contributed assets in access charges is unfair to the companies who made the contributions and represents a substantial revenue windfall to QR. The unfairness of the QCA’s approach is emphasised by IPART’s decision to exclude coal rail formation assets from RIC’s asset base, on the grounds that these assets will not need to be replaced.

The Draft Decision proposes to include earthworks in QR's asset base even though the case for their exclusion is stronger than in NSW - because here the funds to construct these assets were contributed by the users - and despite the competitive disadvantage this would place on the Queensland industry. Not only will QR not have to replace its existing formation assets, it did not pay for them in the first place and, unless the proposed approach is changed, QR will now receive a windfall regulated return on these assets.

The QCA should reconsider its position on contributed assets in light of the NSW precedent and in the interest of fairness to the contributing companies.<sup>1</sup>

**Stanwell** - in establishing a pricing structure, it is essential that the QCA recognises the historical background to current arrangements and ensures the rights of users are protected.

Contributed assets were not taken into account in the QCA's assessment, because any adjustments will be made on a case-by-case basis upon the presentation of documentary evidence confirming the user's contribution. However, in practice, this might be somewhat unfair if confirmatory, direct *documentary* evidence never existed, or has long since disappeared since the facilities were constructed.

This issue is important, since in addition to equity concerns, it raises concerns about the likelihood of future investment in Queensland, and the 'rational expectations' of business in relation to the regulatory risk of future projects. As the Authority correctly points out, "Without confidence in the integrity of the process, market participants will not invest, nor will customers take the risk to contract with them".

**Queensland Government** – the QCA's Draft Decision leaves open the possibility for companies to seek an extension of credit for past capital contributions beyond the existing rail haulage contracts. This is because the QCA has determined past capital contributions will be recognised where a claimant can demonstrate, through documentary evidence (such as a letter), recognition beyond the existing rail haulage contract is justified. Where recognition is warranted, the QCA has specified the principles for quantifying the amount of the 'credit' to be given.

The Government's position on this issue is no recognition should be given for past capital contributions beyond the expiry of the current rail haulage agreements unless there is a demonstrated contractual right in the rail haulage agreements. Given the length of time between the date of the capital contribution and the expiry of current rail haulage agreements (between 2004 and 2010), the Government considers full recognition has already been given to companies for their past capital contributions.

### ***QCA's analysis***

Most stakeholders have taken the view that original contributions should be recognised to the extent that these funds were not acknowledged under existing contracts. In particular, they considered that the DORC value of user-funded contributions should either be refunded or excised from QR's asset base for rate of return calculation purposes.

In the Draft Decision, the QCA indicated its reluctance to revisit past contracts. The Authority recognises the significance of the issue to the mining industry, and the very considerable financial contributions that were made by the industry to the development of the rail network. However, these past contracts were a reflection of government policy at the time, including royalty policy. Nonetheless, past contributions would be recognised where a user could point to documentary evidence regarding the recognition.

The QCA maintains the view that, beyond reductions to rail haulage charges during the term of the original agreement, any additional recognition must be supported by a documented commitment in which QR acknowledges any liability beyond that recognised in contracts. The alternative approach would be tantamount to changing the terms of contracts, many of which have already expired.

---

<sup>1</sup> In a confidential submission to the QCA, Curragh echoed these comments.

Concern was expressed that the QCA’s treatment of contributed assets could potentially increase the perception of regulatory risk and consequently jeopardise future investment in Queensland. On the contrary, the QCA considers that any attempt to revisit contracts and recognise contributions beyond explicit contractual arrangements would, if anything, send perverse signals to future developers and financiers and undermine confidence in the industry.

The regime that is established under the Undertaking explicitly makes provision for future capital contributions in access charges, for instance through an access charge ‘holiday’ or discount as indicated by the haulage contract. The QCA believes that this approach will engender confidence in the integrity and transparency of the access arrangements and promote investment in both the network and the Queensland coal mining industry.

#### ***QCA’s position***

**In assessing QR’s reference tariffs, the QCA has taken the following position on contributed assets:**

1. **elements of past capital contributions will not influence the process that establishes reference tariffs;**
2. **QR may have contractual obligations to honour past user-funded capital contributions, and these will be dealt with through the respective rail haulage agreements; and**
3. **past contributions should only be recognised where a claimant can demonstrate that recognition beyond the existing haulage contract is justified by way of documentary evidence presented, in which case specific adjustments would be made to access charges.**

### **14.3 Quantifying the extent of recognition of past contributions**

#### ***Background***

On establishing that credit beyond contractual recognition for past capital contributions is warranted, the QCA identified a number of issues that were relevant in relation to the quantification of the extent of that recognition.

One such issue concerned the treatment of above-rail contributions. The QCA considered that there should be no differential treatment between user-funded contributions for above and below-rail assets. Accordingly, to the extent recognition was warranted, the Authority determined that contributions for above-rail assets should be treated as if they were for below-rail assets.

#### ***Stakeholder views***

**QR** - agrees with the QCA’s recommendations in regard to QR having a continuing obligation to provide credits for past contributions, with the exception of the proposal that past contributions for above-rail assets should be deemed to be contributions for below-rail assets in assessing credits. Contributions should be split between above and below-rail services in the manner originally agreed between QR and the mines. However, this difference of opinion is not problematic as QR does not have any obligation to provide recognition to any mines specifically in relation to upfront contributions for above-rail assets.

***QCA's analysis***

QR was of the view that it had no obligation to provide recognition to any mines in relation to contributions for above-rail assets. However, the QCA maintains its position that, if credits for past contributions are to be applied, all of the recognition should be deemed to relate to below-rail assets.

The notion of separating recognition of below-rail from above-rail assets is incompatible with the creation of a competitive market for the services provided by these assets. This is because charges for above-rail services will be set by the market. Consequently, recognition of above-rail contributions in the way proposed by QR could effectively render them meaningless as the only relevant market rate would be the market rate for those services.

For instance, a significant barrier to entry for above-rail competitors could be inadvertently created if contributions for rollingstock are not recognised or only recognised if QR's rollingstock is used for haulage purposes. This is particularly the case where users have had little or no discretion over which assets their contributions funded. The QCA's approach assists in providing a more competitively neutral outcome in this regard.

***QCA's position***

**In assessing QR's reference tariffs, the QCA considers that where further recognition of past contribution is warranted:**

- 1. the approach applied in quantifying the extent of this recognition should be dependent upon the nature of this commitment that the mine is able to produce;**
- 2. the inclusion of recognition through adjustments to reference tariffs is the most effective means of ensuring equity between users;**
- 3. there should be no minimum threshold on the value of contributed assets to be included in the recognition;**
- 4. credits should be independent of the identity of the contributor;**
- 5. taxation effects should not be considered unless they are specifically identified in supporting documentary evidence; and**
- 6. all of the recognition should be deemed to relate to below-rail assets.**