IPART Independent Pricing and Regulatory Tribunal | NSW

TAHE's compliance with the NSW Rail Access Undertaking – 2023-24

Draft Report

March 2025

Transport »

Acknowledgment of Country

IPART acknowledges the Traditional Custodians of the lands where we work and live. We pay respect to Elders both past and present.

We recognise the unique cultural and spiritual relationship and celebrate the contributions of First Nations peoples.

Tribunal Members

The Tribunal members for this review are:

Carmel Donnelly PSM, Chair
Jonathan Coppel
Sharon Henrick
Dr Darryl Biggar

Enquiries regarding this document should be directed to a staff member:
Gerard O'Dea (02) 9290 8495

Invitation for submissions

IPART invites comment on this document and encourages all interested parties to provide submissions addressing the matters discussed.

Submissions are due by Monday, 14 April 2025

We prefer to receive them electronically via our online submission form.

You can also send comments by mail to:

Rail access compliance, TAHE FY24
Independent Pricing and Regulatory Tribunal
PO Box K35 Haymarket Post Shop, Sydney NSW 1240

If you require assistance to make a submission (for example, if you would like to make a verbal submission) please contact one of the staff members listed above.

Late submissions may not be accepted at the discretion of the Tribunal. Our normal practice is to make submissions publicly available on our website as soon as possible after the closing date for submissions. If you wish to view copies of submissions but do not have access to the website, you can make alternative arrangements by telephoning one of the staff members listed above.

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The Independent Pricing and Regulatory Tribunal

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Contents

Overview of our assessment of TAHE's compliance

The NSW Rail Access Undertaking ('the Undertaking') provides for third-party access to certain parts of the NSW rail network. One of its functions is to limit the amount of revenue that rail owners can charge these third-party businesses to use the network. Rail owners cannot receive more revenue than the economic costs of providing the service. This requirement, known as 'the ceiling test', is intended to ensure that monopoly track owners provide prices and conditions of access to existing and future access seekers on reasonable terms.

IPART is required to assess the Transport Asset Holding Entity's (TAHE) annual compliance with the ceiling test. This compliance assessment relates to the 2023-24 financial year for TAHE's networks (shown in Figure 1 and Figure 2). We note that TAHE has become the Transport Asset Manager (TAM) subsequent to the end of the FY24 year.

This is our third assessment of TAHE's passenger network. Prior to the 2020-21 review, we did not apply the ceiling test to the metropolitan passenger network. Metropolitan passenger operations involved transfer payments between above-rail and below-rail departments of a single vertically integrated operation without any access contracts. On 1 July 2020, RailCorp became TAHE (a State-Owned Corporation). Passenger train operators now pay access fees for using TAHE's passenger network, and the NSW RAU now applies to these transactions.

We have also completed a detailed assessment of TAHE's Hunter Valley Coal Network against the ceiling test and a high-level assessment of TAHE's other freight networks.

In addition to the ceiling test, rail owners must meet the 'floor test', which requires them to charge every access seeker fees that recover their direct costs of using the network.

The floor test is intended to ensure efficient rail owners can recover the avoidable costs of providing access to a third-party access seeker. It protects against a cross-subsidy to one access seeker from other access seekers and taxpayers. While IPART does not have a formal role assessing the floor test, we have considered whether this requirement has been met.

1.1 Summary of our draft decisions

1.1.1 Metropolitan Passenger Network

Our draft decision is that TAHE has complied with the ceiling test for the Metropolitan Passenger Network. Its access revenue was less than 40%[1] of its full economic costs using the depreciated optimised replacement cost (DORC) asset valuation methodology required by the Undertaking.[a] We also consider that the floor test has been met.

1.1.2 Hunter Valley Coal Network

Our draft decision is that TAHE has not complied with the ceiling test in the Undertaking for its Hunter Valley Coal Network for the 2023-24 compliance year. Across all access seekers, TAHE recovered 122.6% of its costs of serving the combined coal and freight group of access seekers on the network. This was an over-recovery of around $1.84 million in 2023-24.[b]

TAHE's cumulative over-recovery was $7.12 million as at 30 June 2023.[2] TAHE's over-recovery of $1.84 million in 2023-24 has increased this cumulative balance to $8.96 million as at 30 June 2024.

We note however that the Unders and Overs Policy approved in May 2024 has taken effect from 1 July 2024 and we are advised that the overs account balance should fall by over $4 million in each of the 2024-25 and 2024-26 financial years through lower access prices to coal access users. Therefore TAHE has advised that the reduced access prices should result in reducing the over recovery by the end of FY26, approximately.[c]

1.1.3 Other TAHE Networks

Our draft decision is that TAHE has complied with the ceiling test for these 3 networks: the Country Rail Network, the Northern Sydney Freight Corridor and the Metropolitan Freight Network. The access revenue for these networks is less than TAHE's total of operating and maintenance costs and therefore the inclusion of capital costs would only increase the level of under-recovery of full economic costs (FEC).

Draft Decisions

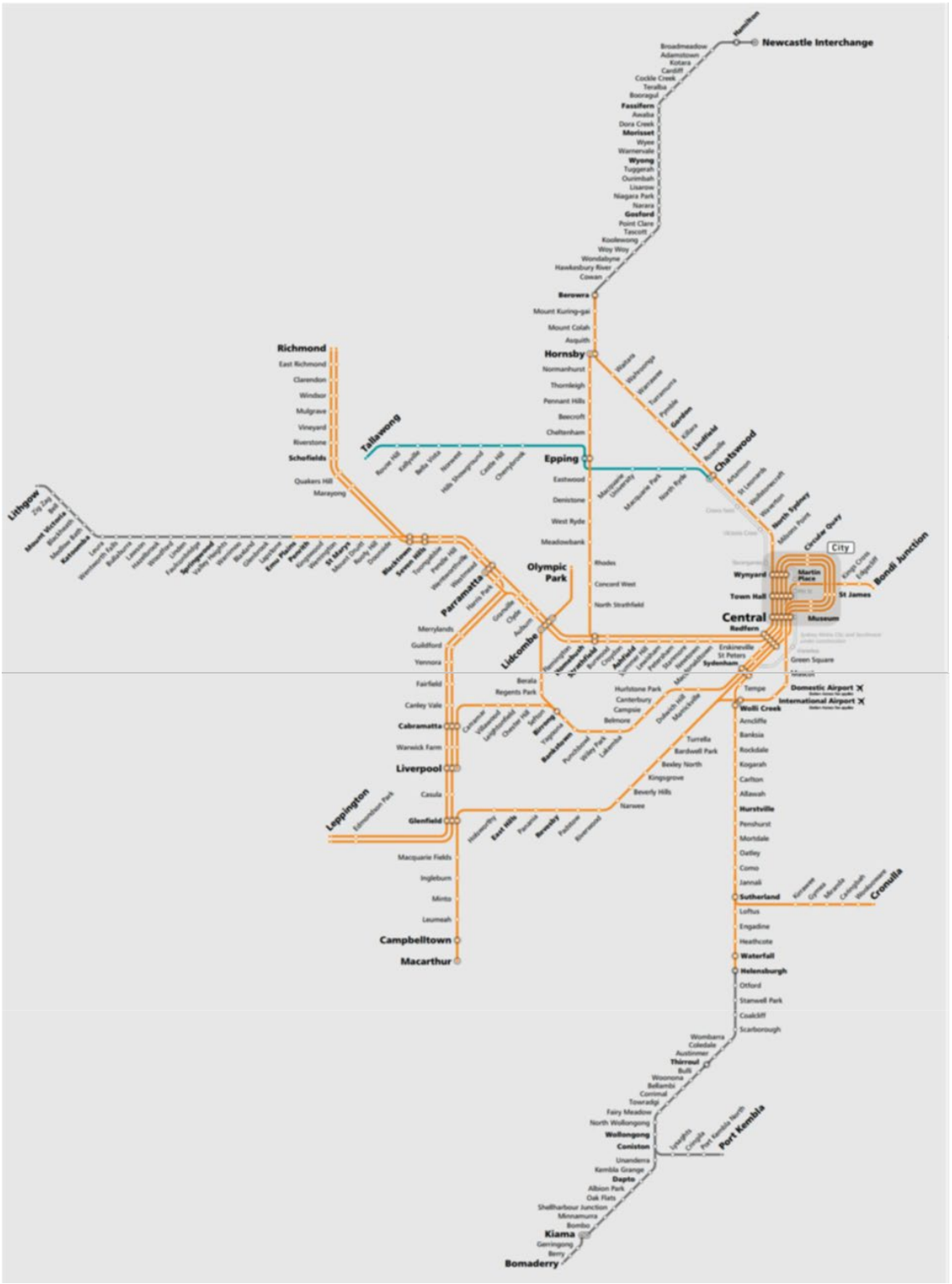
1. TAHE has complied with the ceiling test for its Metropolitan Passenger Network for 2023-24. 10

[a] Full economic cost is a defined term in Schedule 3 of the Undertaking. Full economic cost reflects in part TAHE's actual costs as well as regulated outcomes, such as rate of return that is determined by IPART.

[b] We also found that TAHE recovered 102.6% of it FEC of servicing coal only freight access users in 2023-24

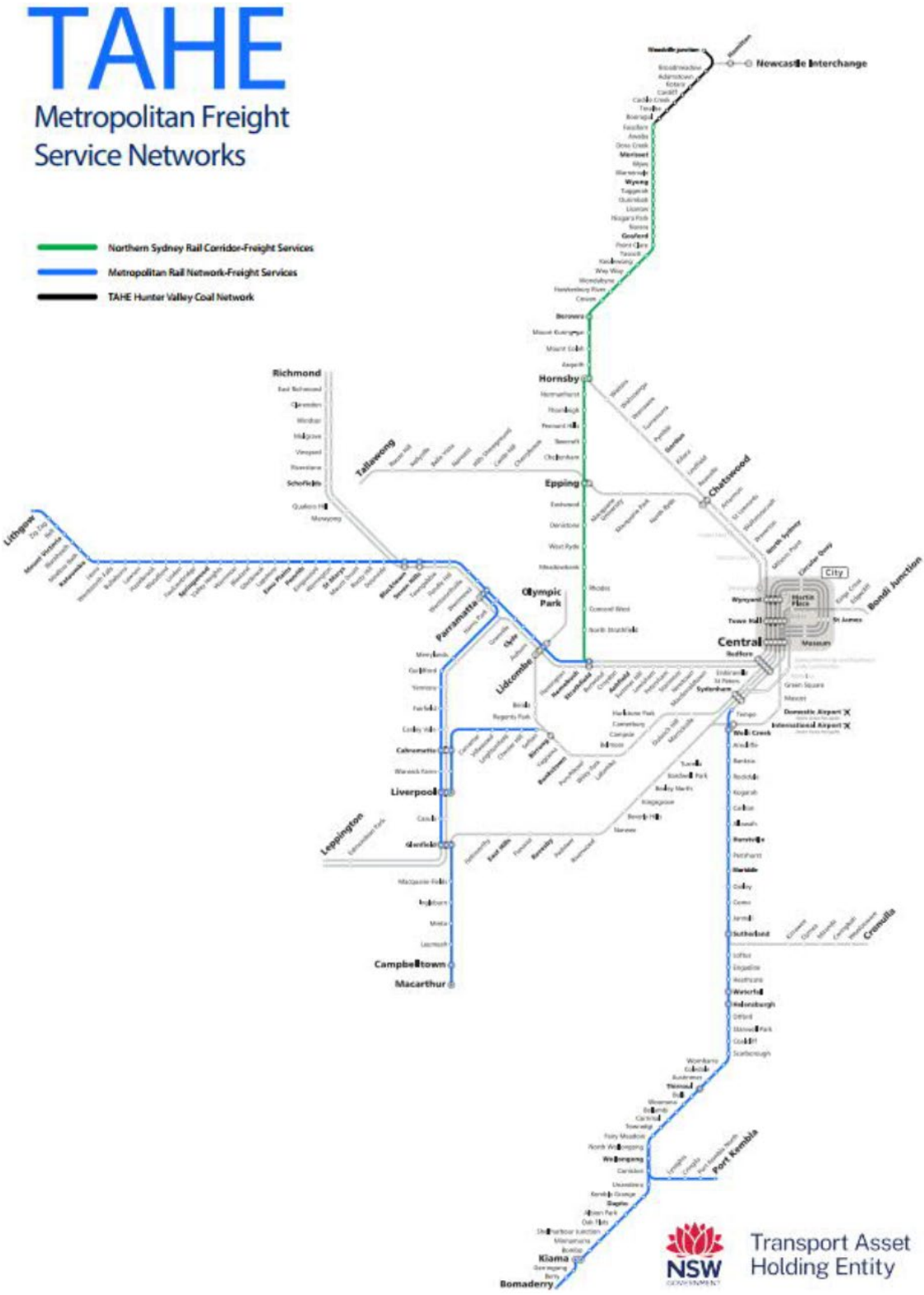
[c] This is based on correspondence with TAHE (TAM) and is discussed further in Section 3.4.1

Figure 1 TAHE's Metropolitan Passenger Network



Source: TAHE, 2023-24 access pricing compliance submission to IPART, October 2024 p 54.

Figure 2 TAHE's Metropolitan Freight Network



Source: TAHE, 2023-24 access pricing compliance submission to IPART, October 2024 p12.

Metropolitan Passenger Network

TAHE's Metropolitan Passenger Network is used by Sydney and NSW Trains to provide passenger operations. It consists of the metropolitan rail network but excludes the new metro lines (turquoise lines in Figure 1 above). Sydney Trains operates suburban services entirely within the passenger network. NSW Trains uses the network to operate intercity and regional services that may have an origin or destination outside of the Metropolitan Passenger Network. Sydney Trains is responsible for maintenance and train control activities on the Metropolitan Passenger Network.[3,d]

2.1 How we assessed compliance

Clause 5 of Schedule 3 of the Undertaking requires TAHE to provide an annual compliance statement to IPART demonstrating its compliance with the ceiling test, including the asset valuation roll forward principles. For the Metropolitan Passenger Network, this test requires TAHE to not earn more than the full economic cost of providing access to the network for Sydney and NSW Trains.

IPART is required to assess this information to determine if TAHE has complied with these requirements.

We consider that an assessment of the ceiling test on a standalone basis requires estimating costs for a hypothetical network that is purpose-built and optimised for that group of access seekers. The actual costs of the existing infrastructure are not relevant unless they are efficient for a group of access seekers. For example, any extra costs that are driven by freight trains must be excluded from the ceiling test for passenger access seekers. Similarly, passenger train costs must be excluded when assessing the hypothetical freight networks.

TAHE has conducted the ceiling test using the depreciated optimised replacement cost (DORC) methodology as required by the Undertaking.[4]

Although we do not have a formal compliance role in relation to the 'floor test', we also considered whether this test has been met.

2.2 Assessment of the ceiling test

TAHE has calculated the full economic cost of the Metropolitan Passenger Network on a standalone basis for the passenger operators (Table 1). Our draft decision is that it meets the ceiling test.

[d] NSW Trains also paid a fee to Sydney Trains for the provision of maintenance and train control expenditure. See TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024 p24.

In calculating the costs of providing access, TAHE has included some expenditure by other entities. This reflects that some activities necessary for access are undertaken by other parties and incurred on TAHE's behalf. Accounting for these costs provides a holistic assessment of the cost of providing access to the passenger network.

Table 1 TAHE's ceiling test for the Metropolitan Passenger Network 2023-24 ($m)

	TAHE's estimates		
Activity	**Sydney Trains**	**NSW Trains**	**All passenger access seekers**
Variable operating costs	11.6	4.8	16.4
Variable maintenance costs	52.4	19.1	71.5
Total direct costs	64.0	23.9	87.9
Train control costs	126.5	126.5	126.5
Fixed maintenance cost	689.6	689.6	689.6
Fixed operating costs	91.2	91.2	91.2
Full incremental costs	n/a	n/a	816.2
Depreciation	786.5	786.5	786.5
Return on RAB	1229.9	1229.9	1229.9
Tax allowance	348.1	348.1	348.1
Full economic costs	**3,335.9**	**3,295.8**	**3,359.8**
Access revenue paid to TAHE	267.1	89.0	356.4
In-kind contributions[e]	672.4	223.7	896.1
Total access revenue and in-kind contributions	**939.5**	**312.7**	**1,252.5**
Total access revenue and in-kind contributions less full economic costs	-2.396.4	-2,983.1	-2107.3
Recovery Rate	**28.2%**	**9.5%**	**37.3%**

Source: TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p30 and IPART analysis.

[e] In-kind contributions by Sydney Trains mainly consist of labour and materials used for maintenance and train control activities undertaken by Sydney Trains on TAHE's behalf that are not directly billed to TAHE but instead off-set against Sydney Trains access charges. These aggregated costs are derived from the individual inputs to Sydney Trains accounting system

TAHE's ceiling calculation differs from our standard ceiling calculation in one respect. TAHE treats major periodic maintenance as capital expenditure, adding it to the Regulatory Asset Base (RAB) and applying depreciation to it. In contrast, IPART's standard approach is to calculate a life-cycle average level of major periodic maintenance for asset replacement and to include that levelized charge as a maintenance expense. In practice, these two approaches yield very similar values for the ceiling, so we consider TAHE's choices to be reasonable for the purpose of calculating a ceiling for the metropolitan passenger network.

2.2.1 Variable operating costs

TAHE has assumed that the proportion of its operating costs that vary with network usage is 10%.[5] It arrived at this percentage by first considering the proportion of its operating costs that related to its regulated assets.[f] TAHE then considered what proportion varied with usage and the driver of the costs.[g] The remainder of the operating expenditure has been treated as a fixed cost.

2.2.2 Variable maintenance

TAHE has included its variable maintenance, as required by the Undertaking.[6] TAHE has noted in its submission that the impact of COVID-19 created a maintenance backlog which is still being addressed. TAHE's submission shows that combined variable and fixed maintenance costs have risen by 44% from 2021-22 to 2023-24.[7]

2.2.3 Capitalised variable major periodic maintenance.

TAHE has excluded capitalised variable MPM from its variable maintenance cost figures. It has instead included this cost as part of capital expenditure. The capital expenditure increases the RAB and therefore leads to larger return on assets and depreciation building blocks in the ceiling. As noted above, we consider this is acceptable for the metropolitan passenger network ceiling test, even though this approach differs from our standard one.[8]

[f] Regulated assets refers to TAHE's rail networks, which are regulated by the NSW Rail Access Undertaking. TAHE also has assets that are not regulated by the Undertaking - mainly train stations and the property around them. See TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p51.

[g] Cost drivers considered by TAHE included trip length, carriage weighted trip length, gross tonne kilometres and service count. See TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p55.

2.2.4 Train control costs

TAHE has treated train control costs effectively as a fixed cost and has allocated the same charge to Sydney Trains, NSW Trains and combined passenger access seekers. The rationale being that the labour and expenses associated with train control are required for the provision of access regardless of the number of access seekers [9]. Notwithstanding the fixed nature of the control costs, TAHE have estimated the train control costs at $126.5 million based on the 2022-23 estimate indexed for inflation. We note that the data in Table 9 (of TAHE's submission) shows that Train Control Costs increased by only 3.4% between 2022-23 to 2023-24, compared to 10.0% for 2021-2 to 2022-23.[10]

TAHE's submission made it clear that train control costs are the responsibility of and are incurred by Sydney Trains. Therefore, they are outside TAHE's control.[11]

2.2.5 Capital costs

TAHE has calculated the RAB for 2023-24 in accordance with the principles in the Undertaking (Table 2). It has used a DORC valuation as the opening value for its passenger network. TAHE has then increased this value by CPI and added capital expenditure for the given year, less any depreciation and asset disposals. We have checked TAHE's asset roll-forward calculation and find it reasonable.

Table 2 Asset roll forward valuation for the Metropolitan Passenger Network ($ million)

Roll forward component	TAHE's estimates
Opening value 30 June 2023	22,362.7
Indexation	1,593.4
Capital expenditure	890.6
Additions	-
Depreciation	786.5
Disposals	10.7
Closing value 30 June 2024	24,049.5
Average RAB	23,206.1

Source: TAHE, Access Pricing Compliance Submission to IPART Financial Year 2023-2024, October 2023, p28 and IPART analysis.

Capital Expenditure

TAHE has incurred $890.6 million in capital expenditure in 2023-24 with the majority being spent on rail infrastructure and major periodic maintenance.[12] Approximately 57% of the capex was for improvements to rail network. Approximately 31% of the capital expenditure was on major periodic maintenance to extend the life of the existing assets.

We note that this level of capex is largely determined by, undertaken by, and therefore implicitly approved by TAHE's only customer on the metropolitan passenger network—Sydney Trains.

As discussed earlier we consider TAHE's treatment of major periodic maintenance as capital expenditure appropriate for determining the rate of return, depreciation, and size of the regulatory asset base. It is also appropriate for determining compliance with the ceiling test.

Our analysis shows that TAHE has rolled forward the regulatory asset base appropriately.

Depreciation

TAHE has included depreciation on all asset classes (excluding land) for the Metropolitan Passenger Network. It has calculated this figure over the estimated useful life of its assets on a straight-line basis, consistent with the requirements of the Undertaking.[13] TAHE has also depreciated new capital expenditure by half a year, as also required by the Undertaking.[14]

Return on RAB

TAHE has applied a 5.3% real post tax rate of return to the average of the opening and closing values of the RAB. This is the rate of return is set by IPART in our 5-yearly 2019-24 rate of return and remaining mine life review. TAHE states that it will apply the 4.9% real post tax rate of return IPART determined in our 2024-29 rate of return and mine life review for the 2024-25 compliance report.[15] We consider this the correct approach.

2.2.6 Tax allowance

TAHE has incorporated a tax allowance as required when using a real post-tax rate of return. It has estimated the tax allowance by applying the ratio of the real pre-tax rate and post-tax rate of returns from our 2019 rate of return determinations.[16] This tax allowance is 28.3%[h] of the return on assets. We consider that this is a reasonable method for calculating a tax allowance.

Final decision

1. TAHE has complied with the ceiling test for its Metropolitan Passenger Network for 2023-24.

2.3 Assessment of the floor test

Clause 1 of Schedule 3 of the Undertaking requires the access revenue from every access seeker to at least meet the direct cost imposed by that access seeker. This is known as the floor test.

[h] The pre-tax real WACC is 6.8%. The post-tax real WACC is 5.3%. The tax allowance is (6.8-5.3)/5.3=28.3%

As noted above, direct costs are the efficient, forward-looking costs which vary with the usage of a single operator.[17]

We consider the floor test has been met by TAHE for both Sydney Trains and NSW Trains (see Table 4).

As discussed earlier, not all of the costs of providing access are incurred by TAHE. Namely, Sydney Trains carries out maintenance and train control for the Metropolitan Passenger Network at no cost to TAHE under current arrangements.[18] TAHE treats this as an "in-kind" contribution. To conduct the floor test, all the costs of the network that vary with usage, including those funded through in-kind contribution by Sydney Trains and NSW Trains, should be captured in direct costs. TAHE has revised its approach this year and has included the non-TAHE incurred operating and maintenance costs in its compliance submission.

2.3.1 Variable TAHE operating expenditure

TAHE allocated variable operating expenditure based on aggregate trip length of each operator. This resulted in a 69% allocation to Sydney Trains and a 31% allocation to NSW Trains. We consider this approach reasonable.[19]

2.3.2 Variable major periodic maintenance

TAHE allocated variable major period maintenance based on gross tonne kilometres. TAHE considers that variable major periodic maintenance is driven by the number and weight of the trips. This resulted in a 73% allocation to Sydney Trains and a 27% allocation to NSW Trains.[20] We consider this approach reasonable.

We also compared TAHE's variable major periodic maintenance costs for the 3 years provided with our own estimates based on a gross tonnes per km basis and found them to be reasonable.

For 2023-24 TAHE has reported that there were 15.87 billion gross tonne-kilometres (gtk) for passenger trains on the Metropolitan Passenger Network. Using TAHE's estimate of $87.9 million for direct costs for the MPN implies an average direct cost rate of $5.54 per '000 gtk. [i]

Table 3 sets out TAHE's estimate of direct costs in millions of dollars per year. We have concluded that TAHE's estimate of variable operating cost and variable maintenance cost for the Transport cluster are reasonable.

[i] Gross tonne km come from the confidential submission tab I10. Direct costs from Table 3. and IPART calculations.

Table 3 Direct costs for the Metropolitan Passenger Network ($ m)

	TAHE's estimates		
	Sydney Trains	**NSW Trains**	**All passenger access seekers**
Transport cluster basis			
Variable operating costs	11.6	4.8	16.4
Variable maintenance expenditure	52.4	19.1	71.5
Total Direct costs	**64.0**	**23.9**	**87.9**

Source: TAHE, Access Pricing Compliance Submission to IPART Financial Year 2023-2024, October 2024, p30

2.3.3 All transport cluster direct costs must be included.

For this draft decision we propose to include an allocation of all transport cluster direct costs in the floor test not just TAHE's own directly incurred costs.

1. Sydney Trains has undertaken $672.4 million in in-kind works for TAHE in 2023-24 and NSW Trains has contributed $223.7 million in fees to Sydney Trains for the work they undertook. These represent the bulk of the resource costs incurred to provide access. It is these resource costs and not simply TAHE's costs to administer the access contracts that represent the avoidable cost if rail access were not provided.
2. Ignoring resource costs incurred by parties other than TAHE to provide access might also raise competitive neutrality concerns of a type that the floor test is designed to prevent. If these resource costs are not reflected, then the direct costs on the MPN would be undervalued and possibly lead to a situation where a private operator was subsidised by the other access users who make in-kind contributions.[j]

Failure to include all the network direct costs could lead to other access seekers being charged less than the actual direct costs they impose on the MPN without failing the floor test. This would see Sydney Trains and NSW Trains[k] subsidising those access seekers.

2.3.4 Sydney Trains and NSW Trains floor test

Table 4 below shows the TAHE floor test for Sydney Trains and NSW Trains.

This is the upper bound of the floor test and shows that the floor test is passed for Sydney Trains and NSW Trains individually and also for all access sectors combined.

[j] While the number of private trains using the MPN is relatively small it is nonetheless important to have the principles properly applied to create a level playing field for competition.

[k] Ultimately then NSW taxpayers.

Table 4 Floor test for the Metropolitan Passenger Network ($ m)

	TAHE's estimates		
	Sydney Trains	**NSW Trains**	**All passenger access seekers**
Transport cluster basis			
Access revenue paid to TAHE	267.1	89.0	356.4
In-kind contributions	672.4	223.7	896.1
Total access revenue and in-kind contributions	**939.5**	**312.7**	**1252.5**
Total Direct costs	**64.0**	**23.9**	**87.9**
Access revenue less direct costs	**875.5**	**288.8**	**1164.6**

Note: Access revenue for all passenger access seekers includes $0.3 m from other passenger access seekers who use the passenger network, such as heritage passenger operators.
Source TAHE, Access Pricing Compliance Submission to IPART Financial Year 2023-2024, October 2024, p30 and IPART analysis

Table 4 shows that access revenue exceeds TAHE's estimate of direct cost more than 13 times over.

Our draft decision is that TAHE's access prices for metropolitan passenger services passes the direct cost floor test.

Hunter Valley Coal Network

3.1 How we assessed compliance

We have assessed TAHE's compliance with the ceiling test for its Hunter Valley Coal Network. We:

- Considered whether TAHE had performed the test for all relevant access seekers or groups of access seekers.
- Considered whether TAHE had correctly calculated the full economic costs of the Hunter Valley Coal Network on a standalone basis for each of those groups. This included testing whether TAHE had complied with the asset roll forward requirements in the Undertaking. We compared TAHE's calculations against our own assessment of costs.
- Compared access revenues received by TAHE, with our calculations of full economic costs for each group.

Our draft decision is that TAHE has failed the ceiling test for coal access seekers alone because this combined revenue exceeds the relevant full economic costs. Consequently, TAHE has also failed the ceiling test for combined coal and general freight access users.

3.2 Relevant access seekers

TAHE submitted ceiling tests conducted on 3 different groups of access seekers:

1. combined coal and general freight
2. coal
3. general freight.

We find the 3 groups proposed by TAHE are appropriate.

Both coal and general freight access seekers need to use the same assets. This means the full economic cost is similar for each group, differing only by the extent that direct costs (i.e. variable costs) are different.

3.3 Assessment of the ceiling test

The ceiling test requires that every group of access seekers pays no more than the full economic cost of the network assets that they use. In the present context, that means that we need to examine three groups: all coal trains, all non-coal freight trains, and all freight trains including coal. There is substantial overlap between the assets and costs that support each of these groups. This is why the combined ceiling test is not just the sum of the coal and non-coal cost recoveries.

TAHE calculated the full economic costs for each group of access seekers on a standalone basis (Table 5), consistent with the Undertaking and our 2020-21 decision. Specifically, it has excluded any extra costs that are driven by other access seekers (namely passenger trains).

Table 5 Ceiling test for the Hunter Valley Coal Network ($)

	2022-23 (from IPART's 2022-23 decision)	2023-24 (from TAHE's submission)
All access seekers (combined coal and freight)		
Maintenance costs	5,153,369	5,354,916
Network control costs	645,463	673,430
Corporate and system overheads	533,493	554,608
Depreciation	700,565	729,596
Return on assets	662,852	661,451
Tax allowance	187,600	187,203
Full economic cost	7,883,341	8,161,204
Access revenue	9,051,440	10,003,794
Cost over-recovery	1,168,099	1,842,589
Coal		
Maintenance costs	4,757,416	4,947,486
Network control costs	645,463	673,430
Corporate and system overheads	497,065	517,124
Depreciation	700,565	729,596
Return on assets	662,852	661,451
Tax allowance	187,600	187,203
Full economic cost	7,450,960	7,716,290
Access revenue	7,213,916	7,916,497
Cost over-recovery	-237,044	200,207
General Freight		
Maintenance costs	4,639,270	4,834,608
Network control costs	645,463	673,430
Corporate and system overheads	486,195	506,740
Depreciation	700,565	729,596
Return on assets	662,852	661,451
Tax allowance	187,600	187,203
Full economic cost	7,321,944	7,593,028
Access revenue	1,837,524	2,087,296
Cost over-recovery	-5,484,420	-5,505,732

Source: 2022-23 final decision, TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p.36.

3.3.1 Maintenance costs

TAHE has applied the same general approach that we used in our 2021-22 decision. It used the benchmarking data provided by SNC Lavalin to determine the benchmark fixed maintenance costs (per km of track) and variable costs (per thousand gross tonne kilometres (gtk)).[l][21]

TAHE has escalated its maintenance cost estimates using CPI[22], rather than the maintenance cost index (MCI) as proposed in our 2020-21 decision.[m] This leads to lower maintenance costs, as CPI is lower than MCI. TAHE acknowledge in their submission that CPI is a conservative estimate of maintenance cost inflation.[23]

3.3.2 Network control costs

TAHE has escalated last year's network control costs accepted by IPART using CPI. TAHE has adopted this approach on the basis that network control costs are fixed and do not vary by the number of access seekers or volume of freight[24]. We consider that this approach is reasonable.

3.3.3 Corporate and system overheads

TAHE has again used IPART's 2020-21 estimate of an efficient level of corporate and system overheads equal to 9.2% of the sum of maintenance and network control. This is derived from industry benchmarking we commissioned in 2009-10.[25] This 'mark-up' approach is generally accepted industry practice. We would not expect the percentage of costs allocated for corporate and system overheads to increase over time for an efficient firm.

TAHE has noted that there is a slight difference in corporate and system overheads between coal and general freight access seekers. It states that this reflects the difference in direct (variable maintenance) costs relating to each group of access seekers.[26] We consider that this approach is reasonable.

3.3.4 Capital costs

TAHE has calculated the RAB for 2023-24 according to the roll forward principles in the Undertaking (Table 6). It must use the RAB in the prior year plus the CPI increase on that prior RAB. TAHE must then add capital expenditure in the given year, less depreciation, and any asset disposals in the given year.

TAHE has correctly adopted the asset life from our 2019-2024 asset mine life determination and applied depreciation on a straight-line basis.

[l] RailCorp contracted SNC Lavalin to estimate efficient costs for the 2015-16 to 2017-18 compliance assessments.

[m] MCI measures the change in price of standard inputs used in maintenance, for example fuel costs and metal products. It may more accurately reflect the change in maintenance costs than CPI as it does not include goods that are not relevant to maintenance (e.g. grocery prices and the cost of residential rental).

It has also applied the correct rate of return of 5.3%[27] from our 2019-2024 determination to the average of the opening and closing values of the RAB. The rate of return is set by IPART in our 5-yearly review.[n]

Table 6 TAHE's asset roll forward valuation for combined coal and general freight access seekers ($)

	2022-23	2023-24
Opening RAB	12,610,166	12,403,124
Opening RAB x CPI	493,522	883,773
Add Capex	0	0
Add Additions	0	0
Less Depreciation	700,565	729,596
Less Disposals	0	0
Closing RAB	12,403,124	12,480,213

Note: The figures for 2022-23 are from our 2022-23 final decision.
Source: TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024*, October 2024, Table 14, p.35.

3.3.5 Tax allowance

TAHE has estimated the tax allowance by applying the ratio of the real pre-tax rate and post-tax rate of returns from our 2014 and 2019 rate of return determinations.[28] [o] We consider that this is an appropriate method for calculating the tax allowance.

Draft decisions

2. TAHE has not complied with the ceiling test for its Hunter Valley Coal Network for 2023-24.

3. TAHE has complied with the asset valuation roll forward principles in the NSW Rail Access Undertaking for its Hunter Valley Coal Network for 2023-24.

[n] The interested reader will note that IPART released its 2024-29 Rate of Return and Remaining Mine Life Determination in September 2024. The RoR was determined to be 4.9% real post tax. The 4.9% RoR takes effect from 1 July 2024. This compliance report is for the period 1 July 2023 to 30 June 2024. Therefore the 2019-24 determined rate of return of 5.3% still applies to this compliance report.

[o] The pre-tax real WACC is 6.8%. The post-tax real WACC is 5.3%. The tax allowance is (6.8-5.3)/5.3=28.3%

3.4 TAHE's unders and overs account

When the Undertaking was established, it was recognised that it may be impractical to set access prices in a way that would avoid over-recovery of full economic costs in every year. This is because prices must be set with only an estimate of the tonnage for the coming year. Prices set with an expectation of low tonnage will generate too much revenue if tonnage turns out to be higher than expected (and vice versa).

To adjust for these under or over-recoveries of the ceiling revenue, the Undertaking provides for an unders and overs account. The expectation is that the net balance of this account would remain close to zero, even though it might fluctuate from time to time.

We must have regard to the operation of the unders and overs account as part of our compliance reviews.

3.4.1 The unders and overs account balance

Our finding is that the unders and overs account balance is $8.96 million as at 30 June 2024.

Table 7 IPART findings on unders and overs account ($)

	All access seekers (combined coal and freight)	Coal	General Freight
Balance at 30 June 2022	5,975,088		
2022-23 revenue minus costs	1,168,099	-237,044	-5,484,420
2022-23 cost recovery percentage	114.8%	96.8%	25.1%
Balance as at 30 June 2023	7,115,334		
2023-24 revenue minus costs	1,842,589	200,207	-5,505,732
2023-24 cost recovery percentage	**122.6%**	**102.6%**	**27.5%**
Balance as at 30 June 2024	**8,957,923**		

Source: TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024 and IPART analysis.

Table 7 shows that the level of cost recovery from the general freight sector is 27.5%. However, the level of cost recovery from the coal sector is 102.6%. Moreover, the level of cost recovery from the combined sectors is 122.6%. TAHE has breached the ceiling test by $1.84 million in 2023-24. This has increased the Unders and Overs Account balance to $8.96 million as at 30 June 2024.

3.4.2 Development of the unders and overs account policy

When TAHE[p] succeeded RailCorp as the rail infrastructure owner in July 2020 they engaged in consultation and collaboration with rail access stakeholders and IPART to develop an Unders and Overs Account.

IPART approved TAHE's Unders and Overs Policy on 9 May 2024. The access prices for this compliance review for 2023-24 were published in May 2023 and took effect from 1 July 2023. That is 12 months before we the Policy took effect. 2023-24 prices were set to recover the Full Economic Cost of the HVCN. However volumes were considerably higher that expected and this led to an over recovery of $1.84 million for 2023-24 and the Overs Account balance rising to $8.96 million.

The price adjustments in the Policy designed to reduce the overs account balance took effect from 1 July 2024 for the 2024-25 financial year. The Policy aimed to return the Overs Account Balance to coal access users through lower prices in both 2024-25 and 2025-26 and then up to 20% of FEC in subsequent years.

[p] Noting that TAHE became the Transport Asset Manager (TAM) on 23 September 2024. https://www.kwm.com/au/en/insights/latest-thinking/transport-administration-amendment-act-2024-transforming-the-transport-asset-holding-entity.html

TAHE advise that coal access prices for 2024-25 are 59% lower than for 2023-24 and that access revenue overall is down 58% for the 7 months to January 2025 compared to the same 7 month period for 2023-24.[29]

All other things begin equal, TAHE is projecting to return $4.90 million to coal access users through lower access charges in 2024-25 and a further $4.37 million in 2025-26.[30]

Our draft decision is that TAHE is on track to return the Unders and Overs Account near to balance by 30 June 2026.

We note also that our recent review of mine life resulted in a significant shortening of the life. By shortening the mine life, we have effectively increased the permissible depreciation building block, which means that the ceiling is somewhat higher. If TAHE does not change prices, this would accelerate the return of past over-recovered money because a given level of revenue would represent lower (or even negative) economic profit.

We understand, though, that TAHE has cut prices by around 50%, so the combined effect of that and the higher ceiling should see the surplus returned faster.

Other TAHE Networks

Several segments of TAHE's network are accessed by freight trains to transport goods to domestic and export markets. They carry a diverse range of goods, including grain, cotton and containerised freight. The specific segments used are the:

- Country Regional Network
- Northern Sydney Rail Corridor
- Metropolitan Rail Network – freight.

These segments are treated as hypothetical standalone networks for the purposes of the Undertaking. This ensures freight operators are only charged the efficient cost of using the network (i.e. so that costs attributable to passenger trains are not passed on to freight trains).

4.1 How we assessed compliance

For the 2021-22 compliance assessment we assessed TAHE's compliance information under clause 5(f) of the Undertaking. Under this clause, IPART is not required to undertake a detailed compliance review where a rail infrastructure owner can demonstrate that access revenue for a sector is no more than 80% of the full economic cost for that sector.

Last year we conducted a more detailed review of the compliance with the ceiling test for the 3 network segments as it had been 5 years since our more detailed review. We were mindful however to minimise the regulatory burden and cost on TAHE where there was no material benefit to other stakeholders. Requiring TAHE to undertake a DORC study of the assets and prepare a detailed regulatory asset base and roll forward would be burdensome, unless necessary to determine the ceiling test result. Last year (2023-24) TAHE were able to show that access revenue was below the total operational and maintenance costs and therefore the addition of capital costs would only further increase the level of under-recovery of FECs in the 3 sectors.

4.2 Assessment of the ceiling tests

TAHE has provided us with the same level of information as last year.

Table 7, Table 9 Table 10 shows that the access revenue for each of the:

- Country Regional Network
- Northern Sydney Rail Corridor
- Metropolitan Rail Network – freight

is again below the total operational and maintenance costs for those individual segments. As mentioned above, the inclusion of capital costs would only further increase the under-recovery of the full economic costs.

Our draft decision is that we satisfied TAHE has complied with the ceiling test for the three respective segments and a capital cost review is unnecessary.

Table 8 Country Rail Network – Ceiling Test Compliance

	2021-22	2022-23	2023-24
Maintenance Costs	61,120,876	97,138,490	101,161,886
Network Control Costs	7,617,814	5,921,266	6,491,887
Corporate Systems and Overheads	10,702,798	6,163,297	8,577,454
Mobilisation payment (annualised)	4,861,65249	4,861,652	4,861,652
Total Operations and Maintenance (O&M)	84,303,140	114,084,707	121,092,879
Access Revenue	14,344,889	15,853,564	13,350,528
Access revenue less O&M	-69,958,251	-98,231,143	-107,742,351
Recovery rate for O&M	**17.0%**	**13.9%**	**11.0%**

Source: TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, Table 17, p42.

Table 9 Northern Sydney Rail Corridor – Ceiling Test Compliance

	2021-22	2022-23	2023-24
Maintenance costs	20,525,917	20,446,807	20,049,216
Network control costs	3,658,882	3,919,592	4,089,426
Corporate and system Overheads	2,225,001	2,241,709	2,220,755
Total O&M	26,409,800	26,608,107	26,359,397
Access revenue	22,204,663	23,394,296	24,961,707
Access revenue less O&M	-4,205,137	-3,213,811	-1,397,690
Indicative recovery rate	84.1%	87.9%	**94.7%**

Source: TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, Table 18, p43.

Table 10 Metropolitan Rail Network/Freight - Ceiling Test Compliance

	2021-22	2022-23	2023-24
Maintenance costs	28,689,912	29,107,287	26,118,692
Network control costs	4,261,393	4,565,035	4,762,836
Corporate and system overheads	3,031,520	3,097,854	2,841,101
Total O&M	35,982,825	36,770,176	33,722,628
Access revenue	28,612,365	26,340,776	25,603,307
Access revenue less O&M	-7,370,460	-10,429,401	-8,119,322
Indicative recovery rate	79.5%	71.6%	**75.9%**

Source: TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, Table 19, p44-45.

Draft decision

4. TAHE has complied with the ceiling test for the Country Rail Network, the Northern Sydney Freight Corridor and the Metropolitan Freight Network for 2023-24.

Glossary

The following terms are defined in section 2.1 of schedule 3 to the NSW RAU (Pricing Principles).

Asset Valuation Roll Forward Principles means the provisions of clause 3 of this Schedule by which the Opening Regulatory Asset Base in any year is adjusted to derive the Closing Regulatory Asset Base in that year.

Closing Regulatory Asset Base means the value of the Regulatory Asset Base at the end of a financial year determined in accordance with clause 3 of this Schedule.

Capital Contribution means a direct payment other than by way of an access price or charge by any person in connection with Capital Expenditure or New Investment undertaken by the Rail Infrastructure Owner. Where a Capital Contribution is to be paid over a period of years, the value of the Capital Contribution may be represented as one figure calculated on a net present value basis.

Capital Expenditure means expenditure undertaken in order to increase the capacity, service quality or useful life of an asset but not including maintenance or operating expenditure.

Corridor Formation Assets means cuttings, embankments and tunnels (including lighting and ventilation).

Depreciation means depreciation of the Regulatory Asset Base, over the useful life of the Regulatory Assets calculated on a straight-line basis.

Depreciated Optimised Replacement Cost (DORC) is the replacement cost of an 'optimised system', less accumulated depreciation.

Direct Costs means efficient, forward-looking costs which vary with the usage of a single operator within a 12 month period, plus a levelised charge for variable MPM costs, but excluding Depreciation.

Full Incremental Costs means all costs which could be avoided if a Sector was removed from the system.

Full Economic Costs are Sector specific costs including a permitted Rate of Return and Depreciation and an allocation of non-Sector specific costs such as train control and overheads including a Rate of Return and Depreciation on non-Sector specific assets. All included items are to be assessed on a stand-alone basis.

Hunter Valley Coal Network means the group of Sectors located in the Hunter Valley utilised for the purpose of coal train movements as specified in Schedule 6.

Major Periodic Maintenance and/or MPM means planned maintenance expenditure on infrastructure assets at intervals of more than one year, including activities that renovate and refurbish the assets to achieve their predetermined service life and service level.

Opening Regulatory Asset Base means the value of the Regulatory Asset Base at the start of a financial year determined in accordance with clause 3 of this Schedule.

Rate of Return means a rate of return in percentage terms approved by IPART for a period of five years to be applied to the average of the Opening and Closing Regulatory Asset Base. The Rate of Return approved by IPART for the period from 1 July 1999 is 8.0 percent on a real, pre-tax basis.

Regulatory Assets means the facilities and associated assets used in the provision of Access to the NSW Rail Network and where the term is used in relation to a Sector or group of Sectors shall include the facilities and associated assets used in the provision of Access to that Sector or those Sectors and includes non-Sector Specific Assets.

Regulatory Asset Base means the capital value of the Regulatory Assets as determined in accordance with clause 3 of this Schedule and further:

(a) Shall be based on an initial valuation of the Regulatory Asset Base calculated using the depreciated optimised replacement cost methodology.

(b) Where applied in relation to a Sector or group of Sectors means the capital value of that Sector or group of Sectors determined in accordance with clause 3 of this Schedule and includes that portion of non-Sector specific assets allocated in accordance with the Rail Infrastructure Owner's asset allocation policy.

Routine Maintenance means inspections and unplanned minor maintenance carried out annually or at more frequent cycles and includes track inspection, track patrolling, replacing broken track components, corridor maintenance, fence maintenance and signal testing.

Unders and Overs Account means the account established by the Rail Infrastructure Owner pursuant to clause 4 of this Schedule.

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1 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p7.
2 IPART, Final Report – TAHE's compliance with the NSW Rail Access Undertaking – 2022-23, May 2024, p2 & p19.
3 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p25.
4 cl 2.1 of Schedule 3 of the NSW Rail Access Undertaking
5 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p24
6 cl 2.1 of Schedule 3 of the NSW Rail Access Undertaking.
7 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p26
8 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p27
9 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2022-2023,* October 2023, p34
10 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p26 Table 9
11 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p25
12 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p27 Table 10
13 cl 2.1 of Schedule 3 of the NSW Rail Access Undertaking.
14 cl 3.2 of Schedule 3 of the NSW Rail Access Undertaking.
15 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p27
16 Final Report – Review of rate of return and remaining mine life from 1 July 2019, July 2019.
17 cl 2.1 of Schedule 3 of the NSW Rail Access Undertaking.
18 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, pp33, 48-49&52.
19 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p55
20 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p55
21 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p33
22 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p33
23 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p33
24 TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p34

[25] IPART, *Compliance with the NSW Rail Access Undertaking RailCorp HVCN, 2009/10*, Final Report, August 2012, p 14. and Sapere Research Group, *A ceiling test protocol for RailCorp – prepared for IPART*, November 2011, p 12.
[26] TAHE, *Access Pricing Compliance Submission to IPART Financial Year 2023-2024,* October 2024, p34
[27] Final Report – Review of rate of return and remaining mine life from 1 July 2019, July 2019. p.6
[28] IPART, Final Report and Decisions - NSW Rail Access Undertaking - Review of the rate of return and remaining mine life - from 1 July 2014, July 2014 and IPART, Final Report – Review of rate of return and remaining mine life from 1 July 2019, July 2019.
[29] Email correspondence from TAHE (TAM) 12 February 2025 (D25/3709)
[30] Email correspondence from TAHE (TAM) 14 February 2025 (D25/3710)

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