



Economic Regulation Authority

Draft determination of Arc Infrastructure depreciated optimised replacement costs and depreciation schedule

Overview

26 March 2026

Acknowledgement of Country

At the ERA we value our cultural diversity and respect the traditional custodians of the land and waters on which we live and work.

We acknowledge their continuing connection to culture and community, their traditions and stories. We commit to listening, continuously improving our performance and building a brighter future together.

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Invitation to make submissions

Submissions are due by 4:00 pm WST, Wednesday, 13 May 2026

The ERA invites comment on this paper and encourages all interested parties to provide comment on the matters discussed in this paper and any other issues or concerns not already raised in this paper.

We would prefer to receive your comments via our online submission form <https://www.erawa.com.au/consultation>

You can also send comments through:

Email: publicsubmissions@erawa.com.au

Post: Level 4, Albert Facey House, 469 Wellington Street, Perth WA 6000

Please note that submissions provided electronically do not need to be provided separately in hard copy.

All submissions will be made available on our website unless arrangements are made in advance between the author and the ERA. This is because it is preferable that all submissions be publicly available to facilitate an informed and transparent consultative process. Parties wishing to submit confidential information are requested to contact us at info@erawa.com.au.

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1. Executive summary

The Economic Regulation Authority is currently considering whether to approve or otherwise determine the depreciated optimised replacement costs of route sections comprising Arc Infrastructure's freight rail network in Western Australia's South-West, and to approve or otherwise determine the depreciation schedule to be applied when updating the regulatory asset base.

This process is governed by the *Railways (Access) Code 2000*. This draft decision sets out our reasoning and seeks further information from interested parties to inform our final determinations.

The depreciated optimised replacement cost (DORC) of a route section approved or determined by the regulator is the initial regulatory asset base of the route section.¹ The regulatory asset base is the foundation of the assessment of capital costs for a route section which, when added to assessments of operating and other costs, forms the total costs applying to negotiations for an access seeker to access that route.

In this draft decision, we highlight where data may be missing or inadequate and provide pointers for further information by way of public comments in submissions, or the provision of more complete data by Arc.

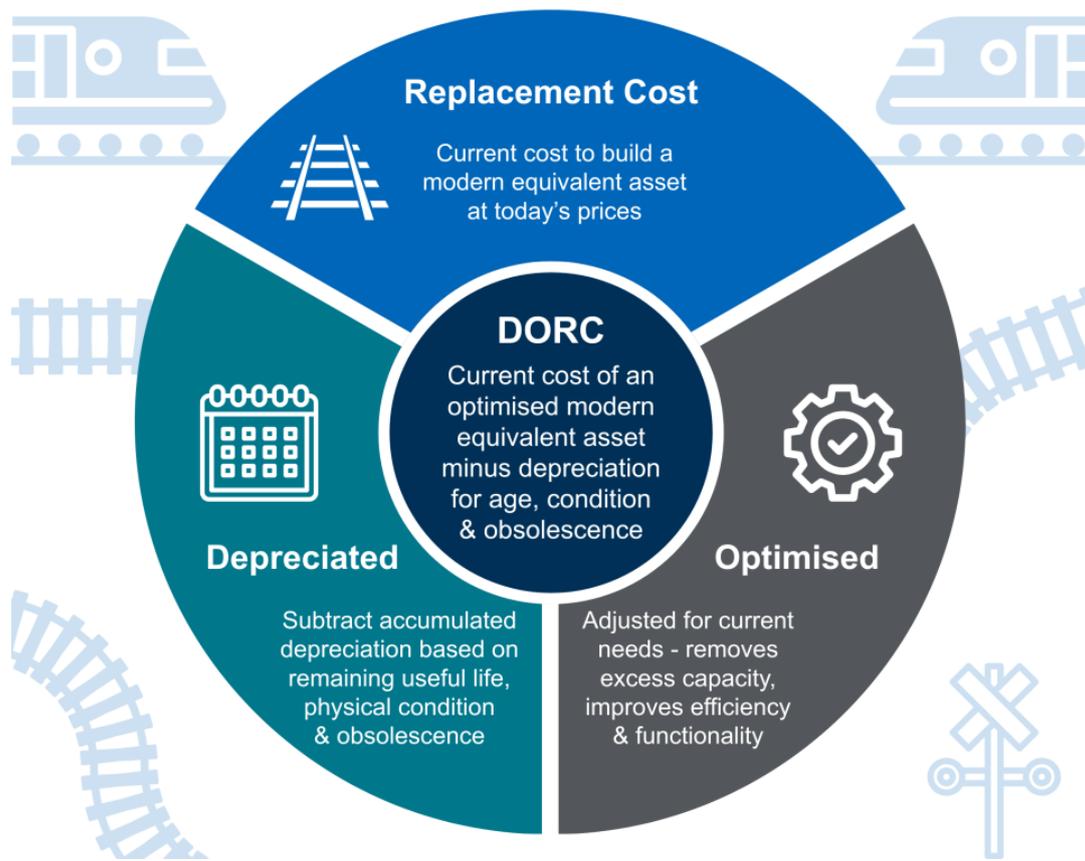
The draft determination of the depreciation schedule has been made consistent with the ERA's determinations of DORC. The determination applies straight-line depreciation based on the remaining economic lives of asset classes by route section. This draft decision also includes the ERA's determination of Arc's depreciation schedule.

The Code requires that a determination be made of DORC for each route section nominated in the railway owner's costing principles.

Depreciated optimised replacement cost

DORC is a measure of the current cost of replacing the assets required to provide the level of service that meets actual and reasonably projected demand. It is a regulatory measure of the compensation due to the service provider in consideration of its investments in the assets that provide the service.

¹ The *Railways Access Code (2000)* does not define DORC as an acronym for the term depreciated optimised replacement cost.

Figure 1: Depreciated optimised replacement cost

Arc's statement of depreciated optimised replacement costs

Section 47J of the Code requires that the railway owner submit (1) a statement setting out determinations of DORC for each relevant route section and (2) supporting material demonstrating the basis of each determination.

Arc did not provide supporting material by route section.² All analysis was presented by groups of routes. The supporting material did not list asset populations, geographic loadings, or any data specific to the route sections listed in Arc's Costing Principles, as required by the Code.

Arc did not initially provide a model as part of its supporting material. Arc has subsequently provided, on request, a copy of its model that was used to generate its report. The model contains engineering and commercial data for 1,784 track sections (subdivisions of routes) but does not provide results by the route sections required for this assessment.

The ERA has constructed its own (public) model that shows its draft determinations of DORC by relevant route section.

Submissions received and common themes

Following publication of Arc's proposal, we received submissions from Karara Mining, Aurizon, Pacific National, Co-operative Bulk Handling (CBH), the Association of Mining and Exploration Companies, and the Chamber of Commerce and Industry of Western Australia.

² *Railways (Access) Code 2000, 47J(1)(b)(ii).*

Collectively, stakeholders noted that Arc had not provided sufficient data to enable meaningful comment on some elements of the valuations.

They also disagreed with Arc's position that the network contained no contributed assets, which are assets paid for by third parties or contributed in-kind. Stakeholders provided a number of examples where assets had been funded by third parties, including the State Government.

Some stakeholders also raised the possible acquisition of the Arc network by the Western Australian Government in January 2025.³ This issue has not formed part of the ERA's considerations for this draft decision.

ERA assessments which vary from Arc's statements

The ERA's assessments differ from Arc's statements in a number of areas, including:

- Arc provided determinations for routes that are not listed in its Costing Principles. The ERA has not included determinations for those route sections in this draft decision.
- Arc did not provide support material for all of its determinations. In particular, Arc provided support material for two categories of CBH spurs only (narrow gauge and standard gauge), despite there being 88 separate CBH routes listed in its Costing Principles. The ERA has made its determinations for all required route sections, by disaggregating asset data in Arc's model and recompiling it for the applicable route sections.
- The ERA has removed a greater number of non-operational assets through its optimisation process.
- The ERA has made allowance for higher capital contributions, where Arc proposed zero capital contributions.
- The ERA has not accepted Arc's funding cost calculations and has recalculated funding costs.
- The ERA has revised the depreciation methodology to better reflect the remaining life of the existing assets.
- The ERA has accelerated depreciation on some routes based on analysis of demand on the rail network. Arc did not include any accelerated depreciation amounts in its determinations.

ERA's determinations of Arc's DORCs

The ERA's assessment of Arc's statement of DORCs and depreciation includes consideration of the requirements of the Code, Arc's Costing Principles, the advice received from the ERA's technical consultant and stakeholder submissions.

The draft decision of the ERA is not to approve Arc's statement of its DORCs. The ERA has determined DORCs for all required routes. These are shown in the attachment ERA's *Draft Decision – Arc DORC Determination by Route*.

³ Government of Western Australia media statement, 25 January 2025, 'Cook Government to enter negotiations to secure control of the freight rail network, ([online](#)) [accessed 29 January 2026].

It is not possible to compare the ERA determinations for all routes with the determinations provided by Arc in its statement, as Arc did not provide determinations for all required route sections.⁴ ERA's draft determinations of DORCs provides a comparison between the ERA's determinations and Arc's determinations for only those routes where a direct comparison is available.

However, it is possible to compare the determinations aggregated to the whole-of-network level.

A comparison of the determinations at the aggregate network level is shown below.

Table 1: Comparison of Arc and ERA network-level aggregation of DORCs (\$ billion)

	Arc statement	ERA draft determination	Difference
Asset category: Construction replacement costs			
Right of way	2.3	1.6	-31%
Civil structures	0.8	0.6	-21%
Track	12.1	10.8	-11%
Signals and Communications	4.3	2.1	-50%
Buildings and Miscellaneous	0.3	0.3	+5%
Construction replacement costs - all routes	19.9	15.5	-22%
Railway owner's costs (ERA)		3.0	
Total Construction Replacement Cost (ERA only)		18.5	
Optimisation	-2.8	-2.3	-19%
Railway owner's costs (Arc)	3.6		
Optimised Total Construction Replacement Cost	20.9	16.2	-22%
Contributed Assets	0	-1.5	
Funding Costs	9.1	2.1	-77%
Depreciation	-14.8	-9.1	-38%
Aggregate of DORCs for all routes	15.3	7.7	-50%

⁴ Comparison of ERA and Arc determinations by Network Group will not account for variations in route lengths associated with the aggregation of sections into Network Groups by Arc. These are minor variations, amounting to approximately 13 kilometres across the network.

The main difference in construction replacement cost assessments is in the costing of track and signalling and communication.

Arc's statement is \$7.6 billion or 98 per cent higher than the ERA's assessment of the DORCs across all routes.

ERA's draft decision on Arc's depreciation schedule

The draft decision of the ERA is not to approve Arc's statement of its depreciation schedule as it does not align with the ERA's assessment of Arc's initial regulatory asset base.

The ERA has determined an applicable depreciation schedule which is consistent with its draft determinations of Arc's DORCs. The draft determination on the depreciation schedule is detailed in the attached model *ERA's draft determination of depreciation schedule*.

2. Draft decision

The draft decision of the ERA is not to approve Arc's determinations of DORCs for its route sections nor to approve Arc's statement of its depreciation schedule, and to make our own determinations.

A summary of the ERA's considerations in making its determinations is provided in this overview.

The detailed reasons for the ERA's decision are set out in the attachments outlined below, which together form the ERA's draft decision.⁵

- **Overview (this document)**
- ERA's draft determinations of Arc depreciated optimised replacement costs by route section
- ERA's draft determinations of Arc depreciated optimised replacement costs (model)
- ERA's draft determinations of Arc depreciation schedule (model)
- Attachment 1: Information used by the ERA
- Attachment 2: Total construction replacement costs
- Attachment 3: Optimisation
- Attachment 4: Capital contributions
- Attachment 5: Funding cost during construction
- Attachment 6: Depreciation
- Attachment 7: DORC summary
- Attachment 8: Depreciation schedules

The ERA invites submissions on this draft decision. The closing date for submissions is 5 May 2026. Before making its final determinations, the ERA will consider any submissions received on this draft decision, and any additional information provided by Arc.

The ERA expects to publish the final decision in October 2026.

⁵ This document and its attachments are available on the [ERA website](#).

3. Introduction

3.1 ERA regulatory role

The ERA administers the *Western Australian Railways (Access) Act 1998* and *Railways (Access) Code 2000*.⁶ Schedule 1 to the Code lists routes comprising four railway networks to which the Code applies, including the south-west regional freight network.

Arc owns the lease on the south-west regional freight network, covering all routes listed as Standard, Narrow, and Dual Gauge in Schedule 1 to the Code. Arc is the railway owner in respect of those routes.

3.1.1 Railway owner requirements

Arc is required to determine, for each route section of an applicable part of the railways network, the DORC of applicable railway infrastructure associated with the route section, and to submit to the ERA a statement setting out each of those determinations and supporting material demonstrating the basis of each determination.^{7,8}

Arc is also required to submit a statement of the depreciation schedule to be applied when determining updated regulatory asset base values.⁹

Arc must determine the DORCs and depreciation schedule in accordance with the costing principles for the time being approved or determined by the regulator.^{10,11} The ERA approved Arc's Costing Principles prior to Arc submitting its statements.¹²

The Costing Principles incorporate the rules and practices that Arc must apply and follow when determining the DORCs of applicable railway infrastructure.

3.1.2 The ERA's role

The ERA must either approve Arc's determinations of DORC or make its own determinations.

In assessing Arc's determinations, the ERA must consider Arc's compliance with its Costing Principles and must also have regard to the objective of the *Railways (Access) Act 1998* and the factors the Act requires the regulator to have regard to when making its determinations under the Code.

⁶ The Code was amended in 2023 to require a depreciated optimised replacement cost valuation of assets

⁷ A route is defined in Part 1 of the Code as meaning "those parts of the railways network and associated infrastructure to which this Code applies, and includes part of a route". A route section is defined in Part 1 of the Code as meaning "the sections of the railways network into which the network is divided for management and costing purposes". The terms route and route section are used interchangeably in the Code.

⁸ Section 47J of the *Railways (Access) Code 2000*.

⁹ Section 47K of the *Railways (Access) Code 2000*

¹⁰ Subsection 47J(1)(a) of the *Railways (Access) Code 2000*.

¹¹ Section 47H of the *Railways (Access) Code 2000*.

¹² Dated 30 May 2024 [Arc Costings Principles](#)

The Act objective is:¹³

The main object of this Act is to establish a rail access regime that encourages the efficient use of, and investment in, railway facilities by facilitating a contestable market for rail operations.

In performing functions under the Act or the Code, the ERA is to take into account:¹⁴

- the railway owner's legitimate business interests and investment in railway infrastructure;
- the railway owner's costs of providing access, including any costs of extending or expanding the railway infrastructure, but not including costs associated with losses arising from increased competition in upstream or downstream markets;
- the economic value to the railway owner of any additional investment that a person seeking access or the railway owner has agreed to undertake;
- the interests of all persons holding contracts for the use of the railway infrastructure;
- firm and binding contractual obligations of the railway owner and any other person already using the railway infrastructure;
- the operational and technical requirements necessary for the safe and reliable use of the railway infrastructure;
- the economically efficient use of the railway infrastructure; and
- the benefit to the public from having competitive markets.

3.2 Depreciated optimised replacement cost

DORC is a measure of the current cost of replacing the assets required to provide the level of service that meets actual and reasonably projected demand. It is a regulatory measure of the compensation due to the service provider in consideration of its investments in the assets that provide the service.

The DORC does not compensate the railway owner for over-investing, or for imprudent investments. The DORC also does not compensate the railway owner for changes in the market that impact the demand for its services.

DORC is determined through a staged assessment process, as detailed in Figure 2.

Figure 2: Depreciated optimised replacement cost flow chart



It is necessary to assess and estimate each of the components shown in Figure 1 to make a determination of DORC:

¹³ *Railways (Access Act) 1998*, section 2A.

¹⁴ *Railways (Access Act) 1998*, section 20(4).

- **Total construction replacement cost:** Total construction replacement cost is equal to the direct cost of procurement and construction plus all contractor's on-costs and railway owner's costs.
- **Optimisation:** The optimised asset configuration is the asset configuration that has the capacity to meet actual and reasonably projected demand, constructed at the least cost and within the constraints of the existing railway corridor. The optimised asset is arrived at by:
 - Assessing capacity of the replacement asset against existing asset capacity.
 - Identifying redundant assets, including those in excess of that required to meet forecasts of service demand.
- **Contributed capital:** Contributed capital is capital from a third-party entity used to fully or partially fund the construction of a railway infrastructure asset. Contributed capital is excluded from the asset base.
- **Funding costs:** Funding costs constitute the opportunity cost of the capital required to construct the network. This recognises the debt and equity funding that a business needs to take out to finance required expenditure over the construction period. To ensure that funding costs incurred during construction can be recovered, these costs are capitalised within the asset's initial value.
- **Depreciation:** Depreciation is the accumulated loss of value due to physical deterioration, or functional or economic obsolescence over the asset's life. Depreciation is subtracted from the optimised replacement cost to reflect the remaining useful life, and value, of the asset.
- **DORC:** The DORC of the assets is derived from the combination of these components.

The ERA's draft decision sets out our consideration of each of the above components – summarised in this overview, and in more detail in each relevant attachment.

3.3 Process for determining depreciated optimised replacement costs and depreciation schedules

Milestones for the making of the ERA's determinations are shown in Table 2.

Table 2: Milestones for making of the ERA's determinations of depreciated optimised replacement cost and depreciation schedules

Milestone	Description	Date
Pre-lodgement consultation	Stakeholders' views and queries about the process ahead of Arc's submission of its statements	May 2025
Arc submission of its statement of DORCs and statement of depreciation schedules	The statement of DORCs provides Arc's determinations of the realistic least cost that would be incurred in replacing routes comprising the rail network. The statement of depreciation schedule provides a framework for the depreciation of each component of the railway owner's asset base and for updates to the regulatory asset base	June 2025
Stakeholder submissions on Arc statements	Stakeholders' views and queries about Arc's statements	August 2025
ERA's draft decision	The ERA's draft determinations of DORCs for Arc's routes and corresponding depreciation schedules	March 2026
Stakeholder submissions on draft decision	Stakeholders' views and queries about the ERA's draft decision	May 2026
ERA's final decision	The ERA's final determinations of DORCs for Arc's routes and corresponding depreciation schedules	October 2026

3.4 Information used by the ERA

3.4.1 Arc statements

On 16 June 2025, the ERA published Arc's statements and called for public submissions. We published:

- Statement of Arc's determinations of DORC for each route section¹⁵
- Supporting material – Level of service demand forecast statement¹⁶
- Supporting material – Applicable Railway Infrastructure DORC Final Report (prepared by GHD)
- Statement of the depreciation schedule.

Arc's statements did not address all of the route sections nominated in its 2024 Costing Principles and provided determinations relating to some additional route sections not nominated in its Costing Principles.

¹⁵ Arc Infrastructure, Depreciated Optimised Replacement Cost List, 13 June 2025.

¹⁶ Arc Infrastructure, Level of service demand forecast statement, 6 June 2025.

The ERA has created a model, based on the model developed by our consultant RP Infrastructure (RPI), which reflects the route section listing in Arc's Costing Principles, by including those routes with zero asset values, and not including routes that were not nominated in the Costing Principles.

A detailed description of these adjustments to route sections is shown in *Attachment 1: Information used by the ERA*.

3.4.2 Consultant

To assist the review of Arc's statements, the ERA engaged RPI, to:

- Review the asset specification quantity and unit pricing elements of Arc's statement.
- Assess Arc's asset depreciation schedule.
- Evaluate and respond to public submissions.
- Provide advice to the ERA on the assessment of DORC outcomes for each route section.
- RPI requested further supporting material from Arc to assist in its assessment. Arc provided some of this information on request, and further information was requested by the ERA under legislative provisions enabling us to require that Arc provide this information.

We published the further information provided by Arc on the ERA website on 11 July and 17 July 2025. A detailed description of the requests for additional information is shown in *Attachment 1: Information used by the ERA*.

RPI has provided a report to inform the ERA's draft determination. This report is published together with this draft determination.

3.4.3 Submissions from stakeholders

The ERA invited public submissions, with a closing date of 14 July 2025, allowing 20 business days. Following the publication of two rounds of supporting material received from Arc, the closing date for public submissions was extended by a further 20 business days to 11 August 2025.

We received seven public submissions:

- Karara Mining Limited (two submissions)
- Association of Mining and Exploration Companies
- CBH
- Aurizon
- Pacific National
- Chamber of Commerce and Industry Western Australia

Further details of consultation with stakeholders is provided in *Attachment 1: Information used by the ERA*.

4. List of questions from the draft determination

The ERA is seeking stakeholder feedback on Arc's determinations and asks questions of stakeholders.

We invite comment on this draft decision and encourage all interested parties to provide comment on the matters discussed or any other relevant issues not raised in this draft decision.

Table 3 details the questions the ERA has raised throughout the draft decision.

Table 3: List of questions for consultation

#	Question
2.1	Do stakeholders have accurate information relating to the location of access roads, where they exist?
2.2	Do stakeholders have a view as to whether access roads are formed up as a necessary precursor to some earthworks elements, to enable those earthworks to proceed?
3.1	Do stakeholders have data or relevant information relating to the capacity usage of the 33.6km of loops which Arc proposed to optimise from its asset base?
4.1	What is the appropriate allocation of funding to routes for the PTA/WestNet Rail agreement (2010)?
4.2	What is the appropriate allocation of funding to routes for the Passing Loops Koolyanobbing to Kalgoorlie capital contribution?
4.3	What is the source or purpose of funding in Arc's annual report for items classified as capital works in progress?
5.1	Is it possible for a commissioning schedule to be applied which incorporates a specific schedule of projects released to customers (and if so, how), or is the more general commissioning approach as applied in the draft decision appropriate?
6.1	The ERA is seeking any information that stakeholders may be able to provide regarding depreciation in terms of the remaining economic life of assets or routes that can assist the ERA for its final determination.
6.2	Is the proposed use of accelerated depreciation for select routes appropriate? If so, which routes should be subject to accelerated depreciation and why?
6.3	Are there any routes which are subject to current operational limitations that are not currently identified in this draft decision? If so, which routes are they and what supporting evidence exists to support such identification?
6.4	What is the appropriate treatment for assets identified as non-depreciable, perpetual for the purposes of the DORC statement?
6.5	What information exists regarding the condition of access roads that are not currently identified in this draft decision? If there are access roads with impaired operational conditions, where are they and what supporting evidence exists to support such identification?
6.6	What information exists regarding the condition of rail assets that are not currently identified in this draft decision?

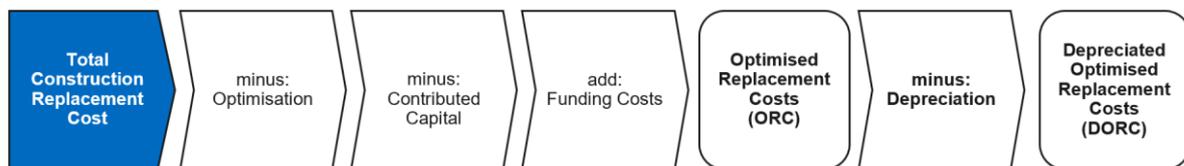
#	Question
6.7	What information exists regarding the condition of ballast assets that are not currently identified in this draft decision?
6.8	Do you support the ERA's draft depreciation approach? If not, what alternative approach/s could be adopted instead and why?
6.9	Are there any other relevant depreciation matters that should be considered by the ERA for the final determination?
8.1	What is an appropriate format for the Depreciation Schedule to take? Do you support the single asset group per route or route and asset group level, noting that it has impacts on both the presentation of the schedule and the depreciation profile?
8.2	Are there any other relevant Depreciation Schedule matters that should be considered by the ERA?

5. Considerations in the draft decision

The ERA's determinations of DORC for each route section are detailed separately in the attachment *ERA's determinations of depreciated optimised replacement costs*.

A summary of the key matters addressed in, and reasons for, the ERA's draft decision is provided here. This summary is not intended to be a comprehensive statement of the ERA's considerations. The ERA's detailed reasons are set out in the attachments, which together with this Overview comprise the ERA's draft decision.

5.1 Total construction replacement cost



The determination of a DORC for a route requires an assessment of the total construction replacement cost for the route. The total construction replacement cost is an assessment of the delivery and installation cost of an asset, prior to consideration of its utilisation or its financing.

Arc's Costing Principles provide that the asset replacement cost in its initial regulatory asset base will be calculated as the lowest current cost to replace the railway infrastructure with a modern equivalent asset. The term modern equivalent asset is not defined in the Code but is commonly regarded as a contemporary asset that serves the same purpose to the asset that is being valued.

Arc's Costing Principles state that the scope of the modern equivalent asset will meet the closest comparable service standard to the existing asset.

Arc's Costing Principles also provide that the asset replacement cost will be based on costs typical for efficient entities developing assets at scale, considering variations relating to geography and local factors at each route section. The Costing Principles provide that asset replacement costs would include:

- material and construction costs
- design development, project and construction management costs.

Material and construction costs are generally referred to as construction replacement costs. Design project and construction management costs are referred to as railway owner's costs. Together, these two components comprise total construction replacement costs.

Arc did not provide a total construction replacement cost of assets on this basis (that is, inclusive of railway owners costs). In its model, Arc applied railway owner's costs after optimisation.¹⁷

¹⁷ Arc's Costing Principles are not clear on this matter. RPI has advised that it is proper practice to apply railway owner's costs prior to optimisation.

Arc provided construction replacement costs only at a network group level, and not at a route level. Arc's report showed construction replacement costs aggregated into 14 geographic network groups.¹⁸

The ERA has provided an assessment of construction replacement costs for each required route. This assessment has required an aggregation of asset populations provided by Arc on a track section basis in its model, in order to assemble a complete and correct population of assets for each route section nominated in Arc's Costing Principles. The ERA has not relied on any automated aggregation of track section asset data in Arc's model and has manually aggregated track section data into the appropriate route sections. We have assessed total construction replacement costs by adding railway owner's costs to the construction replacement cost for each route.

As Arc did not provide construction replacement costs or total construction replacement costs by route section, it is not possible to provide a comparison of the Arc and ERA assessments of costs on this basis.

The ERA's assessment of construction replacement costs by asset class is shown below, aggregated across all route sections for which determinations of DORC must be made. The table shows a comparison with Arc's assessment of construction replacement costs by asset class on a network-wide basis. The Arc network-wide costs are derived by summing the costs shown in Arc's statement, which are shown on a network group basis.

Table 4: Construction replacement cost by asset class (\$ million)

Asset class	Sub-assets	Arc proposal	ERA
Right of Way	Clearing & grubbing, Cuttings/embankments, Formation, Access roads	2,287	1,591
Civil Structures	Bridges, Tunnels, Culverts, Level Crossings	840	630
Track	Ballast, Sleepers, Rail, Turnouts	12,103	10,824
Signals and Communications	Fibre Optic, Signalling and Control Systems, Control Centre Assets, Communication, Radio Masts	4,309	2,146
Buildings and Miscellaneous	Buildings (Control Centres, Maintenance Facilities and Other Buildings), Control Centres, Depots, Maintenance facilities, Plant and Equipment, Walkways, Signage, Pedestrian Level Crossings	338	316
Total all assets		19,876	15,507

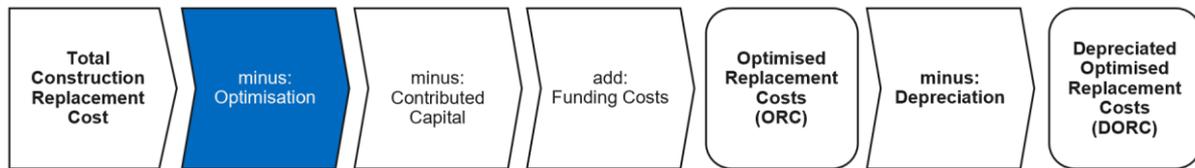
Source: Arc Infrastructure Applicable Railway Infrastructure DORC Final Report (GHD) Table 4.12, ERA analysis.

We assessed the aggregate of construction replacement costs across all routes as \$15,507 million. This is \$4,369 million lower than Arc's proposal of \$19,876 million.

¹⁸ Arc did not provide a rationale for providing results on this basis.

The ERA's assessment of total construction replacement cost for each route section is equal to the construction replacement cost for each route uplifted by 19.3 per cent for railway owner's costs.

5.2 Optimisation



The optimised asset configuration for a route is the asset configuration, constructed at least cost, that has the capacity to meet the actual and reasonably projected demand, within the physical constraints of the existing railway corridor.

The optimised asset configuration is established by adjusting the existing asset configuration as required to meet the actual and reasonably projected demand.

The goal of optimisation is to prevent the railway owner from recovering costs of an inefficient or overbuilt network. Optimisation ensures that costs reflect the costs facing an efficient new entrant.

Arc's Costing Principles state that the level of service associated with the actual and reasonable projected demand is defined in terms of maximum axle loads, maximum train speeds and maximum train lengths.

In its Costing Principles, Arc has undertaken to identify redundant assets, assess modern equivalent asset capability against existing capacity, assess the demand forecast to identify required changes, determine the value of optimisation and adjust the replacement cost by that value. The net present value of the difference between forecast operating cost of actual railway infrastructure and optimised infrastructure is also subtracted from the asset replacement cost.

In its Costing Principles, Arc has undertaken to provide a 10-year demand forecast based on 10 years of historical demand data. Arc has described demand in terms of maximum axle loads, train speeds and train lengths. Arc has defined demand as equal to the level of service and therefore has proposed that the current asset is required to be maintained at its present level of service to meet current and future demand. Arc has stated that optimisation of assets is not required on account of its assessment of current and projected future levels of demand.

Arc has nonetheless proposed some optimisation associated with an alternative lower-cost procurement strategy. This strategy would involve Arc providing ballast, sleepers, rail, turnouts, plant and equipment directly from its own suppliers, and not from the contractor constructing the network. Under this strategy, contractor indirect costs may be reduced to a 5 per cent margin.

Arc proposed additional optimisation amounts which would result from the removal of some redundant passing loops and route sections. Arc did not propose any optimisation associated with closed, or non-operational routes.

Stakeholders disagreed with Arc's definition of demand and therefore its estimation of forecast demand. Stakeholders also submitted that non-operational routes should be removed during

optimisation. Submissions also noted it was unclear how the optimisation, identified at network group level by Arc, was applied to individual route sections.

The ERA's assessment of optimisation is based on the following factors:

- Level of service demand
- Optimisation due to alternative lower-cost procurement
- Optimisation of passing loops and redundant route sections
- Optimisation of non-operational route sections.

These are discussed below.

5.2.1 *Level of service demand*

Arc defined demand in terms of maximum axle loads, train speeds and train lengths. On this basis, Arc has claimed that there is no scope for optimisation on account of projected demand.

The ERA considers that Arc's approach conflates concepts of demand and capacity. The difference is that, while the capacity may be required in terms of track specifications, demand levels must be assessed on the basis of the actual freight task, for example on the basis of gross tonne kilometres (GTK).

In response to a request by the ERA, Arc provided GTK data. RPI's analysis of the GTK data supports Arc's position that demand factors do not substantiate a case for optimisation.

5.2.2 *Optimisation due to alternative lower-cost procurement*

The majority of Arc's proposed optimisation is due to savings from a proposed alternative procurement strategy, whereby Arc would procure track assets and plant assets directly (and at the same cost as indicated by the Tier 1 contractor), but would install those assets itself, or under a separate construction contract. In Arc's statement, the proposed optimisation savings have been allocated entirely to track assets, and the optimisation of plant and equipment assets is unclear.

Further, the calculation of Arc's optimisation savings associated with the reduction of contractor's margins to 5 per cent is not transparent and the resulting optimisation does not result in a reduction of 5 per cent.

The ERA does not accept Arc's proposed optimisation based on alternative procurement as the alternative procurement scenario is not consistent with the costings provided by a Tier 1 contractor for replacement of all network assets. In addition, the scenario may not be practically feasible as the entire network including plant and equipment is being replaced, and Arc would not have the necessary means to undertake this project internally.

Furthermore, consideration of an alternative procurement scenario is not appropriate in the context of optimisation, but rather is relevant as part of considering construction replacement costs.

Arc has stated that it may provide further information to show how alternative procurement may be reconciled with the conventional Tier 1 procurement costing adopted by the ERA. The ERA invites further stakeholder submissions in conjunction with any further information from Arc on this matter.

5.2.3 **Optimisation of passing loops and redundant route sections**

Arc has identified 2.8 km of redundant route sections and a total of 33.6km of loops that it claims may be optimised from the asset base on the basis of train lengths. Arc has proposed the removal of loops which are more than 300m shorter than the maximum train length and loops which exceed the maximum train length have been shortened to match the relevant maximum train length. Routes which have been identified as redundant due to no realistic prospect of re-entering into service have also been removed.

The ERA does not accept Arc's proposal on the optimisation of loops because maximum train lengths do not influence the use of loops by shorter trains. A loop may still be required for use by shorter trains even if it cannot accommodate the maximum train length.

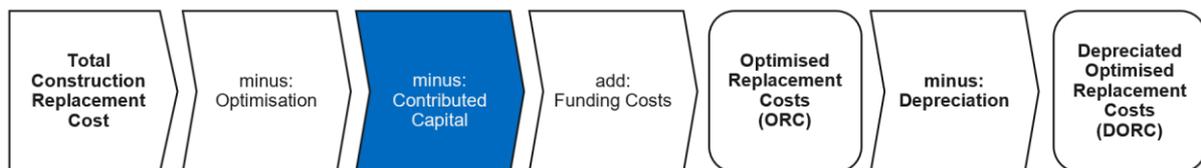
5.2.4 **Optimisation of non-operational route sections**

Arc has not optimised any non-operational route sections from its asset base, but rather has removed associated replacement values through depreciation.

The ERA has optimised out all non-operational routes on the basis that it is the most appropriate treatment for non-operational assets. The ERA has identified the route between Picton and Greenbushes as non-operational and has removed that route section from the asset base.

The ERA seeks stakeholder views on any optimisation of other non-operational route sections.

5.3 **Capital contributions**



Contributed capital is defined in the Code in section 47B as being railway infrastructure that has been funded wholly or in part by an entity other than the railway owner or its associate. This includes cash or in-kind contributions, undertaking work or paying for work, or making payments which fund the recovery of capital in relation to the railway infrastructure (these must not be payments of charges for access).

Arc's Costing Principles quote the Code and state that the railway owner will exclude any railway infrastructure that has been funded by contributed capital. It states that where another entity has funded the entirety or part of an asset, the replacement cost will be reduced in proportion to the percentage funded by that entity.

Arc stated in its submission that none of the assets included in the asset base are contributed assets and therefore it did not make any adjustment for contributed capital.

Stakeholder submissions provided examples of claimed contributed capital on the network. These examples include government contributions to the network, private contributions which have been claimed as confidential and private contributions in the public domain, all of which have been accepted by the ERA.

5.3.1 Contributed capital claimed in submissions

Stakeholders have provided detailed breakdowns of amounts claimed to have been paid as capital contributions.

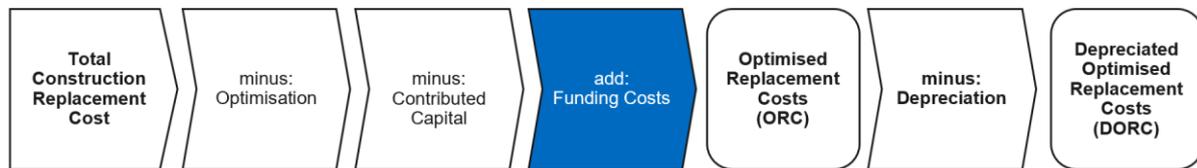
RPI provided a recommendation that any contributed capital amounts documented in the public domain should be accepted as capital contributions.¹⁹

The ERA has cross referenced the relevant amounts claimed by [REDACTED]. The ERA has also identified further government funding amounts in Arc's 2024 Annual Report, and these have been included as capital contributions.

The total amount of contributed capital accepted by the ERA across all route sections is approximately \$1.5 billion.

¹⁹ RP Infrastructure, *Initial Report (Review of Arc Infrastructure's Sections 47J and 47K submissions) FINAL*, 6 January 2026, pp. 38-9.

5.4 Funding cost during construction



Funding costs constitute the opportunity cost of the capital required to construct the network. This recognises the debt and equity funding that a business needs to finance required expenditure over the construction period.

Arc's Costing Principles regarding funding costs state that they are to be based on a weighted average cost of capital (WACC) determined by the ERA, where funding costs are capitalised during the construction development curve from start through to completion.

Arc calculated funding costs to be \$9.1 billion on an optimised replacement cost of \$20.9 billion, or 44 per cent of optimised replacement cost. Arc allocated funding costs to the underlying network assets, where they then inherit the economic life of those network assets.

All stakeholder submissions disagreed with Arc's amount and approach to funding costs during construction. On the funding cost amount, stakeholders questioned the quantum with respect to precedents and proportion of the financial capital compared with the physical capital. Stakeholders disagreed with the construction scope, duration and staging, stating that Arc's approaches appeared excessive. Additionally, some stakeholders questioned whether the weighted average cost of capital applied by Arc was appropriate given the regulatory task.

The ERA has considered Arc and stakeholder views and has formulated an estimation of funding costs based on the following factors.

5.4.1 *The appropriate form of the rate of return to apply for a depreciated optimised replacement cost exercise*

In its statement, Arc proposed a real pre-tax WACC based on the 2024 WACC determination of 7.46 per cent.

In the draft decision, the ERA applies a real post-tax WACC of 6.22 per cent, based on the ERA's 2024 WACC determination. As DORC values are calculated in 2024 real dollars, the 2024 WACC determination is appropriate as it reasonably matches with the real dollar base.

The use of a post-tax WACC for calculating funding costs results in a regulatory asset base that does not include a tax allowance. This leaves it open for negotiations to incorporate tax impacts as counterparties see fit. This also avoids the complexity of stakeholders attempting to unwind embedded tax payments in the regulatory asset base which would result from the use of a pre-tax approach. Tax expenses can then be transparently incorporated into standard building block costs for any future price setting.

The ERA considers that the use of a post-tax WACC avoids the risk of double counting tax in future price assessments. It also reflects the reality that tax payments are not incurred during the construction of the rail infrastructure.

5.4.2 The appropriate capital amount

In its statement, Arc applied the rate of return to its optimised construction replacement cost estimate of \$20.9 billion.

The ERA has applied the rate of return to the ERA's optimised replacement cost estimate of \$14.8 billion, which is a lower amount. The ERA's optimised replacement cost is lower due to changes in total construction replacement costs, lower due to higher optimisation amounts, and due to the deduction of capital contributions. Funding costs are not applied to capital that has been removed from the asset base from optimisation or from capital contributions.

5.4.3 The transaction costs for raising capital

Arc did not calculate transaction costs, except that debt transaction costs are implicitly incorporated in the 2024 WACC determinations as part of the overall cost of debt.

In the draft decision, the ERA includes transaction costs for equity finance. The 2024 WACC determination includes debt financing costs in the WACC, but equity raising costs are usually calculated separately to the WACC. For consistency, and to recognise that transaction costs are necessary to raise equity capital, equity raising costs are included in the draft decision.

5.4.4 The expenditure profile and duration of funding cost capitalisation to completion

Arc's proposal capitalised funding costs for 19 years, being the length of the construction period based on its consultant's monthly expenditure profile, where funding costs are capitalised from when they are incurred until network completion.

In its draft decision, the ERA capitalises funding costs for 11 years, in line with RPI's estimated construction period based on an annual expenditure profile where funding costs are capitalised in two stages to full completion. The ERA does not consider that economic efficiency and utilisation is promoted by assuming that the rail network can only earn revenue when the last expenditure dollar is spent (at full completion) and has, accordingly, adopted a draft position that commissioning occurs in two stages. This recognises that a prudent operator would seek to minimise funding costs.

5.4.5 The economic life of the funding costs

In its statement, Arc attributed funding costs to the underlying network assets. In doing so, the funding costs inherited the economic life of those network assets instead of the 50 years stated in the Costing Principles.

The ERA has accepted Arc's approach. The ERA considers that funding costs are tied to the procurement and commissioning of specific assets which all have different economic lives, most of which are not close to the 50 years. The draft decision approach means that funding costs will have the same economic life and depreciation treatment of the related assets. This matching approach is likely to result in greater economic efficiency and utilisation than the approach in Arc's Costing Principles, as it avoids the situation where an asset may be fully depreciated but still have outstanding associated funding costs remaining in the asset base.

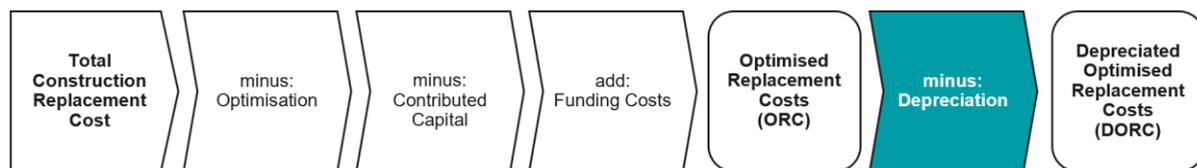
5.4.6 Draft decision

The ERA's draft decision is that funding costs of \$2.1 billion will be included as part of the optimised replacement costs. These funding costs will be attributed to the underlying network assets and will have the same economic life of those network assets.

The ERA seeks stakeholder views on options around the progressive commissioning schedule and how parts of the network could be brought into service sooner. This recognises that the rail network build would be progressively commissioned and likely better aligns with what a commercial operator would do and also works to minimise the total costs, inclusive of funding costs.

For the final determination, the ERA will undertake further work to understand how a commissioning schedule can align with individual customer routes. This will include consideration of the use of specific commissioning project schedules (schedule of projects released to customers) versus the use of general commissioning assumptions (commissioning when a percentage of the rail network is complete). We are inviting feedback from stakeholders to assist with this assessment.

5.5 Depreciation



Depreciation adjusts the hypothetical new-build cost represented by the optimised replacement cost (ORC) to reflect the asset's current economic value. Depreciation accounts for the asset's age, condition, and remaining useful life, representing the portion of the asset base consumed through wear and tear. The reduction of the optimised replacement cost by depreciation forms the determination of the DORC.

Arc's Costing Principles regarding depreciation provide guidance on determining economic lives, with the consideration of both the asset's current physical condition and the forecast rate of asset consumption. Arc has to compare the economic life of an asset to the Standard Design Life and reduce the asset's optimised replacement cost accordingly.

For example, a rail asset with an optimised replacement cost of \$100 million may have a standard design life of 50 years when it is new and a remaining economic life of 10 years. That is, the asset has been used for 40 years. This means that 80 per cent of the asset's economic use has been consumed (the depreciation rate). The depreciation rate multiplied by the ORC equals \$80 million (the depreciation amount).

Arc's statement included depreciation of \$14.8 billion, which amounted to around 49 per cent of Arc's estimated optimised replacement cost of \$30.1 billion. This depreciation amount is largely comprised of track (55 per cent) and signalling and control assets (34 per cent). Arc's approach involved analysing each asset category and assessing depreciation based on available asset life information. For assets with missing information, Arc used an average condition from assets that had condition data available. Arc did not depreciate certain assets associated with land on the basis that they do not deteriorate and these assets are entered into the DORC at their full optimised replacement cost values. Arc proposed to use the straight-line depreciation method.

All stakeholder submissions disagreed with Arc's amount and approach to depreciation. All stakeholders considered that Arc's proposed depreciation was too low, which resulted in DORCs that were too high. Most stakeholders considered that Arc's provision of information for depreciation was inadequate. Some stakeholders provided detailed, asset specific criticisms and stated that Arc selectively applied the Costing Principles to its benefit. Most stakeholders questioned whether it was appropriate to treat assets with missing information in the manner proposed by Arc. Further, most stakeholders disagreed that land associated assets should be perpetual in nature and these assets should be depreciated. There was stakeholder support for the straight-line depreciation method.

The ERA accepted the majority of Arc's proposed depreciation methods across the asset categories, however, it recalculated depreciation on the basis of:

- the ERA's estimated ORC
- some adjustments to specific depreciation approaches
- asset specific changes
- the introduction of accelerated depreciation to route sections with material customer demand reductions.

The ERA's optimised replacement cost in this draft decision is \$16.9 billion, compared to Arc's \$30.1 billion.

The ERA's refinement to Arc's depreciation methodology includes changes to the default approach of a minimum of 10 per cent remaining life for assets with no condition information available. This modifies Arc's proposed approach which only applied the 10 per cent for assets where condition data does not exist, but commissioning date is known. The ERA notes that Arc's asset condition information was not complete and seeks further information from Arc.

The ERA includes accelerated or greater depreciation to routes where customer utilisation has materially declined along with a strong expectation that future route demand is terminal. This results in \$462 million of accelerated depreciation.

Arc's proposal has in part applied a 100 per cent depreciation rate to non-operational assets, while the ERA has instead not included non-operational assets in the ORC. This has necessitated adjustments in depreciation rates to maintain consistency.

Specific asset considerations of the ERA are outlined in the sections below.

5.5.1 *Right-of-way – Formation, earthworks, and clearing and grubbing*

In its statement, Arc has applied zero depreciation for formation, earthworks and clearing and grubbing assets with an optimised replacement cost of \$2.8 billion, along with zero depreciation in the depreciation schedule.

In the draft decision, the ERA also applies zero accumulated depreciation to the formation, earthworks, and clearing and grubbing assets.

5.5.2 Right-of-way – Access roads

Arc included depreciation of \$330.2 million, around 39 per cent of Arc's estimated optimised replacement cost of \$839.1 million.

The ERA accepts Arc's approach to depreciate access roads which results in a depreciation rate of around 39 per cent. However, the ERA's assessment of the construction costs of access road is zero which results in no depreciation being allocated.²⁰

5.5.3 Track – Rail

Arc's statement included depreciation of \$3.2 billion, around 38 per cent of Arc's estimated optimised replacement cost of \$8.3 billion.

The ERA reviewed Arc's rail life assessment and considers that it skews remaining asset life upwards. The ERA's draft decision has adjusted the allocations to reduce any skews to remaining life and results in a depreciation rate of around 47 per cent.

5.5.4 Track – Sleepers

Arc included depreciation of \$1.4 billion, around 46 per cent of Arc's estimated optimised replacement cost of \$3.1 billion. Arc's Costing Principles state that there are three sleeper types (concrete, steel and timber), where Arc estimated the remaining life of sleepers assuming that all sleepers are concrete.

In its draft decision, the ERA has aligned the depreciation approach for timber sleepers with the standard design life of 15 years in the Costing Principles. This means that the remaining life for timber sleepers is reduced as the ERA's method allocates more assets into the minimum 10 per cent remaining useful life. In the draft decision, the depreciation rate for sleepers is around 69 per cent.

5.5.5 Track – Ballast

Arc included depreciation of \$126.3 million, around 9 per cent of Arc's estimated optimised replacement cost of \$1,472 million. Arc's approach for ballast diverges from the Costing Principles and appears to apply a useful life of 878 years.

In the draft decision, the ERA has aligned the depreciation approach for ballast with the standard design life of 50 years in the Costing Principles. Given the assumed commissioning dates, the remaining life for most ballast lies at the minimum 10 per cent remaining useful life instead of Arc's assumption that those ballast assets were mostly undepreciated. In the draft decision, the depreciation rate for ballast is around 74 per cent.

5.5.6 Draft decision

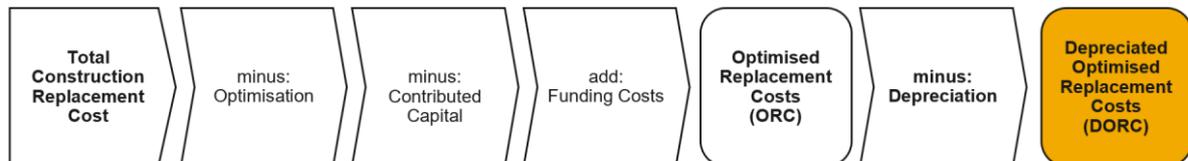
The draft decision applies a total depreciation amount of \$9.1 billion, which is around 54 per cent of the ERA's estimated optimised replacement cost. This amount is lower than Arc's proposed \$14.8 billion, being 42 per cent of Arc's proposed optimised replacement cost on a corrected basis – that is, excluding non-operational assets. While the ERA applies a lower

²⁰ The draft decision of the ERA is that there is insufficient evidence of the existence of access roads across the entire network to establish costs on a route section basis, and in reference to stakeholders' submissions that some access roads are made in formation work, that the costs of access road costs are adequately captured in formation costs.

dollar amount for depreciation than Arc, this is due to the ERA calculating a lower optimised replacement cost. The ERA applies a 13 percentage point higher depreciation rate than proposed by Arc.

The ERA seeks stakeholder feedback on its depreciation approach, including on specific asset classes and the application of accelerated depreciation on routes with material customer demand reductions. Further stakeholder feedback will help refine depreciation across assets and the rail network's different routes.

5.6 Depreciated optimised replacement cost



The ERA has not accepted Arc's proposed DORC value.

The ERA has made a draft determination for Arc's DORC of \$7.7 billion. This is a reduction of \$7.6 billion (or 50 per cent) compared to Arc's proposed value.

As Arc detailed its DORC values by network group, a presentational equivalent is provided in Table 5.

Table 5: Comparison of depreciated optimised replacement costs by network group

Network Group	DORC		Difference (%)
	Arc statement (\$ million)	ERA draft decision (\$ million)	
Metropolitan	461.8	330.1	-28.5%
Eastern Goldfields Railway	4,222.3	2,216.1	-47.5%
Midwest	1,088.7	312.4	-71.3%
Esperance Bulk Line	1,856.6	941.6	-49.3%
Leonora Bulk Line	828.9	435.6	-47.5%
South West Main	955.9	421.6	-55.9%
Collie	238.6	97.1	-59.3%
Midland Railway	1,369.7	684.0	-50.1%
Central	1,325.7	737.1	-44.4%
Great Southern Railway	1,713.6	929.3	-45.8%
Lakes	673.7	359.9	-46.6%
CBH Sidings	241.3	175.4	-27.3%
Sidings & Other	154.0	84.1	-45.4%
Non-Operational	162.2	0.0	-100.0%
Total	15,293.0	7,724.4	-49.5%

6. Depreciation schedule considerations

The forward depreciation schedule sets out the profile of annual depreciation of the initial regulatory asset bases, relying on the ERA's determination on Arc's initial regulatory asset bases and the remaining life of assets.

Arc provided simple depreciation schedules that provided annual percentages for depreciation for each year by route section and asset group. Arc did not calculate annual amounts of depreciation expenditures over time based on its proposed initial regulatory asset bases.

Arc's proposed depreciation schedules result in a weighted average remaining life of 25.2 years for the whole rail network. Arc's proposed initial regulatory asset bases and proposed depreciation schedules, implies network-wide depreciation payments of \$3.6 billion for the first five years, averaging around \$700 million each year. Over this five-year period, the proposed depreciation schedules would result in recovery of about a quarter (24 per cent) of its proposed initial regulatory asset bases.

Stakeholders submitted that Arc's proposed DORC valuation, which they considered excessive, would result in an inflated schedule of depreciation. Submissions considered that the DORC valuation needed to be corrected before meaningful comment could be provided on the depreciation schedule.

The ERA has recalculated the schedules on the basis of:

- The ERA's draft decision on the initial regulatory asset base resulting from the DORC valuation of \$7.7 billion.
- The assets' remaining life from the DORC valuation, which sets the period of time over which depreciation is recovered.
- A straight-line depreciation approach, which allocates the recovery of assets to equal annual amounts.
- Unlike Arc, the ERA includes no non-depreciating assets. Earthworks, cuttings and formation assets are depreciated over their standard design lives.

The ERA's draft decision is shown as the Depreciation Schedule Model.²¹

The ERA's determined depreciation schedules result in depreciation payments of \$2.3 billion (real 2024 dollars) over the first 5 years, averaging around \$460 million annually and would recover around 30 per cent of the ERA's initial regulatory asset base. Most of the initial regulatory base and therefore depreciation is in track and signalling and control systems.

Our analysis of the profile of annual capital charges over time shows that capital charges are significantly front-loaded.²² The return on capital and return of capital combines to result in high annual average capital charges of nearly \$1 billion (real 2024 dollars) for the first five years. With the full depreciation of signals, there is a material reduction in total capital charges from year seven onwards.

²¹ ERA's draft determinations of depreciation schedules (model).

²² Capital charges include a return of capital (depreciation) and a return on capital (rate of return of the regulatory asset base). These generally represent the biggest components of regulatory building block costs.

The ERA seeks stakeholder feedback on the merits of simplification of the depreciation schedules to apply one single asset group per route section.

The ERA has made a draft decision on the depreciation schedules informed by the ERA's draft decision on Arc's initial regulatory asset base. The depreciation schedules will be updated for the ERA's final decision.

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Appendix 3 Submissions received

Submissions from interested parties are listed below.

Submissions on Arc statement

AEMC

Aurizon

Co-operative Bulk Handling

Chamber of Commerce and Industry of Western Australia

Karara Mining

Pacific National