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Mr David Marchant
Chief Executive Officer
Australian Rail Track Corporation
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Contact Aaron Murray
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David

Dear Mr ~~Marchant~~

REVIEW OF ARTC'S COMPLIANCE WITH THE NSW RAIL ACCESS UNDERTAKING ("UNDERTAKING") FOR 2007/08

On 13 February 2009, ARTC submitted its annual compliance report for 2007/08 to IPART. In March 2009, IPART released ARTC's report for stakeholder comment. Both Asciano and QR National Coal provided written submissions to IPART. These submissions raise a number of issues which IPART needs to consider further in assessing ARTC's compliance with the NSW Rail Access Undertaking (Undertaking) for 2007/08.

Asciano requested IPART to review each of the building block components but pay particular attention to the changes in network control, corporate overheads and maintenance costs.

IPART notes that ARTC's maintenance costs and corporate overheads increased by 45 per cent and 43 per cent respectively in 2007/08. ARTC attributed the increases to the inclusion of the Ulan line in the constrained group in 2007/08 and to a lesser extent the inclusion of flood rectification costs of \$1.81m in maintenance costs.

However, a preliminary analysis undertaken by IPART indicates that the increases in maintenance and corporate overhead costs were still significant even after taking into account the 22 per cent increase in throughput of the constrained group in 2007/08. IPART requests ARTC to provide additional information and an explanation of the drivers of these increases in corporate overheads and maintenance costs. IPART also requests ARTC to confirm whether any changes were made to the allocation of expenditure to these cost categories in 2007/08. Please confirm whether the 2007/08 cost allocations are the same as those which were reviewed by IPART as part of the 2004/05 compliance review.

IPART notes that the decrease in network control costs is likely to have been the result of the completion of the Train Control Consolidation project. Therefore, IPART is not requesting any additional information on network control costs.

Asciano recommends that IPART rejects ARTC's proposed approach to recovering the financing costs associated with the new crossing loops at Mangoola and Wollar on the grounds that the proposal does not conform to the requirements of the Undertaking and that it is inconsistent with ARTC's approved Unders and Overs Account Policy. Asciano claims that there is no precedent for ARTC's proposed approach. They note that ARTC's compliance report states that it is accepted practice to include financing costs associated with approved capital expenditure in the regulated cost base. Asciano agrees with this and notes that financing costs are normally capitalised into the asset base or alternatively some components of financing costs may be incorporated into the debt margin.

I understand members of IPART's Secretariat and staff from ARTC discussed this issue on 9 June 2009. Members of the Secretariat explained that it was IPART's normal practice to allow any interest during construction to be included in the value of capital expenditure projects when they are rolled into the regulatory asset base. Staff from ARTC indicated that they would be amenable to treating financing costs consistent with IPART's normal practice.

Consistent with these discussions, IPART seeks confirmation that ARTC is willing to amend its 2007/08 proposal and remove the financing costs associated with the crossing loops at Mangoola and Wollar from its operating costs for 2007/08 and include any incurred financing costs associated with these capital projects in its capital expenditure for 2008/09. This would require ARTC to provide amended calculations of its ceiling test and Under and Overs result to IPART for 2007/08.

QR National Coal has requested ARTC to provide it on a confidential basis with a breakdown of the Unders and Overs account by load point and customers for 2007/08 and previous years. IPART would appreciate ARTC's advice on whether it is feasible to provide a breakdown of the Overs and Unders account for 2007/08 and previous years on a confidential basis as requested by QR National Coal.

If you have any questions or wish to discuss any aspect of this letter, please contact Mr Aaron Murray on 9290 8440.

Yours sincerely



James Cox
Chief Executive Officer and Full Time Member