

11 March 2009

Mr James Cox
Chief Executive & Full Time Member
Independent Pricing And Regulatory Tribunal
PO Box Q290, QVB Post Office NSW 1230

By email: ipart@ipart.nsw.gov.au

Dear Mr Cox,

ANNUAL COMPLIANCE REVIEW UNDER THE NSW RAIL ACCESS UNDERTAKING - 2007/08

Asciano welcomes the opportunity to provide comments on RailCorp's and ARTC's compliance with the NSW Rail Access Undertaking ("Undertaking"). This submission contains no information over which Asciano wishes to claim confidentiality and IPART may make this submission publicly available.

RailCorp

Asciano is comfortable with RailCorp's approach set out in their revised submission to IPART. We agree with RailCorp that it has complied with the Undertaking and appreciate the improved information provided by RailCorp in its submission.

ARTC

Asciano has reviewed ARTC 2007/08 Submission and was also given a briefing by ARTC on its submission. Whilst the detail available to Asciano is at a high level, we are comfortable with the ARTC's approach. However, given the lack of detailed information available to Asciano, we urge IPART to undergo a thorough review of each of the building block components. Although ARTC has provided a plausible high level explanation for the increases, we urge IPART to pay particular attention to the increases in network control & corporate overheads and maintenance costs.

Of the three specific issues raised by IPART, Asciano is comfortable with Ulan and Wilpinjong being included in the constrained network and also with the inclusion of the \$20.1m of commissioned capex in the RAB. However, Asciano does have concerns with the third issue raised by IPART, namely the treatment of the Wollar and Mangoola crossing loops financing costs.

ARTC first raised the concept of including costs relating to Wollar and Mangoola into the RAB at the Rail Infrastructure Group (RIG) meeting on 3rd July 2008. On 11th July RIG submissions were distributed by ARTC to Pacific National and Queensland Rail seeking endorsement for \$15.42m to be added to the RAB, representing the construction costs incurred during 2007/08 for Wollar and Mangoola loops. There were further discussions at the August RIG meeting, however the matter then went silent until October. On 8th October 2008 ARTC distributed a revised RIG submission to Pacific National and Queensland Rail which sought \$1.125m, an amount equivalent to a 7.3% return on the costs incurred during 2007/08 (\$15.42m) and for this amount to be treated as part of the Unders & Overs process.

Throughout this consultation period Asciano was seeking to understand the rationale behind ARTC's proposals. It was not immediately evident that a rescheduling decision, with preference

given to other loops at Willow Tree and Ardglen, caused Wollar and Mangoola loops not to be commissioned on schedule. As late as March 2008 ARTC were forecasting all loops concerned to be commissioned within the 2007/08 financial year. By 30th June 2008 only one of the four loops – Willow Tree – had been commissioned. Asciano's view is that the delay in the construction of Wollar and Mangoola loops was a result of ARTC not completing works associated with CTC on the Ulan line rather than reprioritising the commissioning of loops on another line.

In October 2008 Asciano sought the views of the Hunter Rail Access Task Force (HRATF) which has members from all Hunter Valley coal producers. In late November the HRATF responded to Asciano expressing in principle concerns with the proposal and requested Asciano seek further information from ARTC. In a letter from Asciano to ARTC dated 1st December 2008 (attached as annex) further clarification and information on the details of the proposal was requested, in line with the issues raised by the HRATF. Asciano suggested to ARTC that they provide all stakeholders with a full detailed paper that adequately clarified the proposal in a concise way. Asciano's letter of 1st December was tabled by ARTC and discussed at the RIG meeting on 4th December and ARTC committed to Asciano to provide a response. To date no response has been provided by ARTC.

ARTC did not advise Asciano of their new proposal prior to the IPART submission becoming a public document. Although ARTC's claim is now based on six months return the information provided does not fully explain the move from \$1.125m for 12 months to \$0.74m for 6 months.

Asciano's view since the concept was initially raised in July 2008 is that the proposal does not conform to the requirements of the Undertaking. Schedule 3 (through the definition of Capex_t in paragraph 3.1) of the Undertaking outlines the criteria for infrastructure additions to the RAB, which allows for ARTC's prudently incurred costs to be allowed for inclusion into the RAB in the year in which the infrastructure is commissioned. For convenience, the relevant parts of paragraph 3.1 are set out below:

"The Regulatory Asset Base shall be calculated in accordance with the following formula:

$$RAB_t = RAB_{t-1} + (RAB_{t-1} * CPI_t) + Add_t + Capex_t - Dep_t - Disp_t$$

Capex_t is: The actual Capital Expenditure for assets commissioned in relation to the Regulatory Asset Base for the year t, where that Capital Expenditure is incurred in accordance with the provisions of clause 3.3, less that portion of any Capital Contribution which is to recover Capital Expenditure."

ARTC's approach is also inconsistent with their Unders and Overs policy approved by IPART in August 2008. The policy did not suggest the inclusion of a return on funds expended on partially complete projects.

The rationale provided by ARTC for the proposal is that it is suffering a financial penalty due to the late commissioning of the loops and that this penalty is inequitable. Apart from anything else, this argument fails to recognise the substantial financial impact for Access Seekers and other Hunter Valley coal chain stakeholders arising as a result of the delay.

It is notable that there is no precedent for ARTC's approach. In its compliance submission (p 15), ARTC argues that it is accepted practice to include "financing costs associated with approved capital expenditure in the regulated cost base". Asciano agrees with this statement. Such financing costs are normally capitalised into the asset base and include interest and financing fees incurred, or alternatively some components of financing costs may be incorporated into the debt margin.¹ However, ARTC relies on this proposition to justify a

¹ Queensland Competition Authority, "Draft Decision QR's 2005 Draft Access Undertaking", July 2005 p 49 wherein the QCA expressly rejects QR's claim for the inclusion of debt/equity financing costs as operating costs.

completely different outcome. ARTC is seeking to immediately recover the amounts, rather than capitalising the cost, and without any explanation is substituting the return component as the amount claimed rather than the finance costs. It is also noted that ARTC has not indicated that it intends to forego any future claim for capitalisation of interest for these particular projects. As far as Asciano is able to determine, ARTC is seeking a return on an investment from its customers prior to those customers being able to use that facility to their advantage.

Also on page 15 of its submission to IPART, ARTC has indicated that it intends to continue to consult with Access Seekers on this matter and then "make appropriate adjustments to the regulated cost base". This seems a most peculiar statement in the circumstances:


- ARTC has submitted the 2007/08 Unders & Overs account to IPART for approval. The amount in question (the "financing charge") is still, according to ARTC, under consultation, and therefore it is inappropriate to seek regulatory approval when the matter is still being negotiated;
- ARTC's submission talks about adjusting the "regulated cost base", not the Unders & Overs account. It is unclear what the regulated cost base is, though this might possibly refer to ARTC's allowable expenses for the year. Even if this is the case, it is unclear precisely what ARTC is proposing as it would seem that any resulting adjustments to the Unders & Overs account would need to be approved by IPART. It is not a matter of unilateral adjustment for ARTC.

Given the foregoing, Asciano believes that the proposal should be rejected by IPART on the basis that:

- ARTC's proposal does not conform to the requirements of the Undertaking, Schedule 3, paragraph 3.1 for the calculation of capital expenditure for the 2007/08 year.
- ARTC has not prepared the Unders and Overs account in accordance with its own policy, that policy having been approved by IPART in August 2008;
- Despite both oral and written requests for further information, ARTC has failed to adequately demonstrate to stakeholders why its proposal should be supported, notwithstanding that it is contrary to the Undertaking;
- ARTC's argument that the delay to commissioning Wollar and Mangoola loops were as a result of a rescheduling decision to give priority to the commissioning of Willow Tree and Ardglen loops is inaccurate. At best, the explanation fails to mention other material reasons for the delay that are less supportive of ARTC's claim; and
- ARTC's position is that it is suffering an inequitable financial penalty due to the late commissioning of the loops is without merit. Contrary to suffering an inequity, ARTC is seeking to be paid by its customers for the making of an incomplete investment that its customers cannot use. The claim is without precedent.

We would be happy to provide further details on these views.

Yours sincerely



Dr Tim Kuypers
General Manager
Access & Regulation