

16 OCT 2007

DATE RECEIVED



12 October 2007

Mr John Hall
Chief Executive Officer
Queensland Competition Authority
GPO Box 2257
Brisbane QLD 4001

Dear Mr Hall,

QR COAL SYSTEM MAINTENANCE COSTS – QCA DRAFT DECISION

The draft decision of the QCA with regard to QR's application to raise prices to cover substantial changes in its cost base represents a pragmatic solution to the continual problem of matching efficient costs to a changing environment. As such Asciano sees little advantage in further arguing the merits of QR's approach, nor whether QR should be required to accept more or less of the consequence of its previous estimates. However, this submission raises three matters that did not appear to be adequately addressed in the draft decision.

Reintroduction Of An "X" Factor To Price Escalation

In its approval of QR's 2006 Access Undertaking (UT2), the QCA approved indexation of prices based on the Consumer Price Index (CPI) and removed the allowance (the "X" factor) for productivity improvements under the previous Undertaking. The rationale for this was that QR's maintenance costs were fully efficient and therefore it was not appropriate to expect further gains and hence apply a continual allowance for improvement.

Whether or not one accepts the argument that the UT2 costs were not subject to on-going productivity improvements, given that the basis of the costs for the current decision are costs taken from the 2001 Undertaking (ie no longer based on the 2006 analysis), it would appear that the rationale for removing the "X" factor from the escalation equation is no longer consistent with the logic that applied to the revised base (ie an expectation of continual productivity improvement).

The QCA's expert consultant, GHD, also suggested that it is appropriate to reintroduce the "X" factor to represent productivity improvements from investment etc.

The draft decision notes the recommendation by GHD on p.10, but does not comment on it nor does it explain the reasons for not accepting that recommendation. It is therefore unclear whether the QCA has considered this issue in arriving at its decision. While the QCA is clearly not obligated to accept a recommendation by its own expert, a decision not to adopt a recommendation by that expert ought to be explained. If the QCA is of the view that it remains inappropriate to apply a discount to CPI for escalation, it would be helpful for the final report to document the reasoning behind this decision.

Implications For UT3

The draft decision rightly points out that the decision should not be taken as a precedent for the approval of the 2009 Undertaking (UT3). Asciano supports the QCA's approach that the decision should be based on finding a simple, pragmatic solution and that such a solution would be inappropriate to apply to the approval of a new undertaking.



However, the draft decision does not appear to address the QCA's expectations or approach with regard to the need to avoid any repetition of the problem of material error by QR either in the approval for UT3, nor during the currency of UT3. Clearly it is most unsatisfactory for the QCA and other stakeholders to engage in a comprehensive review process only to be afterwards faced with a situation such as has arisen under UT2. This results effectively in a fait accompli and places the QCA in a most difficult position. It also significantly undermines stakeholder confidence in the regulatory process.

Accordingly it would be entirely appropriate for the QCA to articulate in the final report clear guidelines for the approval process of UT3, including details of how the QCA intends to avoid a similar situation occurring and any remedial steps that the QCA would adopt should they be required.

Utility of Costing Manual

In its previous submission, Asciano (under the name of Pacific National) questioned the utility of the Costing Manual given the magnitude of the systematic accounting errors admitted by QR. If the methodology documented in the Costing Manual was incapable of highlighting such a significant error, there appears to be little value in the document as it stands. Asciano has long considered the Costing Manual to be of limited value and it was suggested that it has out-lived any usefulness that it might initially have had.

The draft decision does not address this issue nor does the initial QR submission provide any explanation as to why the Costing Manual methodology failed completely to highlight the error. It would be helpful for the QCA to address the continued need for the Costing Manual or otherwise in the final report. The removal of a redundant portion of the Undertaking in any amendment must be a positive step and Asciano requests the QCA to consider this issue.

Alternatively, if the QCA sees continued value in the Costing Manual, it would seem that the document requires a complete review, and an amended Undertaking should not be approved without such a review taking place. In its current form the Costing Manual is demonstrably incapable of providing any certainty that QR's reported costs do represent what the manual purports them to be.

Yours Sincerely,

A large black rectangular redaction box covering the signature of Dr Tim Kuypers.

Dr Tim Kuypers
General Manager Access & Regulation
Asciano