Thursday, 6 March 2014

Dr Malcolm Roberts
Executive Chairman
Queensland Competition Authority
GPO Box 2257
Brisbane QLD 4001

By email: rail@qca.org.au

Dear Dr Roberts,

Asciano Submission on QCA Cost Consultant's Reports Regarding the Aurizon Network 2013 Draft Access Undertaking

Introduction
Asciano welcomes the opportunity to provide comments to the Queensland Competition Authority (QCA) on two consultant's reports which have recently been released by the QCA in relation to the QCA's continuing assessment of the Aurizon Network 2013 Draft Access Undertaking (DAU). The two reports assess the forecast operating, capital and maintenance costs and cost allocations which underpin the pricing proposed in the 2013 DAU.

The two reports are:

- a report by RSM Bird Cameron (RSMBC) which is a Financial Assessment of Operating Expenditure in the Aurizon Network 2013 DAU; and
- a report by Sinclair Knight Merz (SKM) which is an Engineering and Technical Assessment of Maintenance, Operating and Capital Expenditure in the Aurizon Network 2013 DAU

This submission contains comments on both the RSMBC and SKM reports.

Asciano has previously provided extensive comments to the QCA on the Aurizon Network 2013 DAU. This submission builds on these comments, particularly in relation to previous comments by Asciano relating to Aurizon's corporate cost allocation and the cost reflectivity of the Aurizon Network tariff structure.

This submission contains no confidential information and may be considered a public document.

Asciano Comments on the RSM Bird Cameron Report
Asciano has previously raised concerns with the QCA that the costs underpinning the 2013 DAU tariffs include a substantial increase in Aurizon Network's allocation of corporate costs.

The RSMBC report has found instances where Aurizon has inappropriately allocated costs by:

- allocating costs that should be attributed to its above rail activities to its corporate

cost pool from where they are partially allocated to Aurizon Network; and
- allocating costs using broad allocators when more targeted allocators are available;

Such cost misallocations have the affect of:

- increasing costs to all users of below rail services; and
- artificially reducing the costs of Aurizon Network's related party above rail operator, which then provides it with an advantage when competing with other above rail operators.

Thus such mis-allocations are not economically efficient and acts to discourage competition in the market for train operations.

These cost mis-allocations further reinforce the need for an updated Aurizon costing manual which is developed and implemented with a high degree of regulatory oversight. Aurizon has not sought to substantially amend their cost allocation manual since their separation from Queensland Rail and privatisation in 2010. Asciano strongly believes that the 2013 DAU should include requirement for Aurizon to meaningfully update their costing manual in such a manner that provides substantially more detail on Aurizon's cost allocation approach. Industry concerns regarding Aurizon Network's potential to favour their related above rail operator would be reduced if a thorough regulatory process resulted in a revised cost allocation manual approved by the QCA.

Asciano notes that the RSMBC report supports the use of direct costs as an allocator (including the use of direct costs in the blended allocator). Asciano broadly supports this approach although, as noted by RSMBC, the high percentage of electricity costs in the direct costs may need to be further investigated to ensure that the allocator is not being skewed.

Asciano Comments on the Sinclair Knight Merz Report
Asciano notes that the SKM report (page 5) states:

> *... Given the lack of available asset information on age, condition and remaining capability, SKM found the proposed forecast to be reasonable...*

Asciano has a concern that the lack of information indicated by SKM brings into question the validity of the SKM assessment. Asciano believes that any review of Aurizon Network costs should be based on detailed cost and asset information which ideally should be collected over a period of time at regular intervals using a consistent approach. Asciano notes that the 2010 Access Undertaking (Schedule A clause 5 (a)) requires an initial network condition assessment within 3 months of the commencement of the 2010 Access Undertaking and an end of period assessment 6 months prior to the terminating date. (This latter assessment was delivered in August 2013). Asciano believes that concerns regarding the detail, consistency and timeliness of Aurizon Network costs and asset information could be partially addressed by establishing a more structured annual cost reporting regime and network condition reporting regime for Aurizon Network. Such a regime should be able to utilise information collected in current Aurizon network internal processes.

Asciano also notes that SKM (page 5) are proposing that the proportion of costs allocated to the AT1 tariff component should be higher. Asciano broadly supports this reallocating of costs between tariff components.

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More broadly, Asciano notes that in industry forums Aurizon Network has proposed that they are looking to reduce the number of maintenance windows while increasing the length of time each maintenance window will be in force. Asciano is raising this potential change to maintenance operations in order to ensure that it is taken into account in both the SKM analysis and the QCA consideration of the Aurizon Network cost forecasts.

Conclusion

Asciano welcomes the opportunity to provide comments to the QCA on the RSMBC and SKM reports.

Asciano is concerned that the cost misallocations identified by the RSMBC report are not economically efficient and act to discourage competition in the market for train operations. Asciano believes that such misallocations could be substantially reduced if the 2013 DAU included a requirement for Aurizon to meaningfully update their costing manual such that it provides substantially more detail on Aurizon's cost allocation approach. Concerns regarding Aurizon Network's misallocation of costs would be reduced if a thorough regulatory process resulted in a revised cost allocation manual approved by the QCA.

Similarly Asciano believes that that concerns regarding the detail, consistency and timeliness of Aurizon Network costs could be partially addressed by establishing a more structured annual cost reporting regime and network condition reporting regime for Aurizon Network. Such a regime should be able to utilise information collected in current Aurizon network internal processes.

Feel free to contact Stuart Ronan on 02 8484 8056 to discuss this submission.

Yours faithfully,

Dr Tim Kuypers
General Manager Regulation

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