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8 May 2014

Mr Matthew Schroder
General Manager
Fuel, Transport and Prices Oversight Branch
Australian Competition and Consumer Commission
GPO Box 520
Melbourne Vic 3001

(By email: transport@accc.gov.au)

Dear Mr Schroder

**Consultation - ARTC's Proposed Variation to the Hunter Valley Rail Network Access Undertaking to include Gap to Turrawan Segments (Revision 24 March 2014)**

Idemitsu Australia Resources Pty Ltd (**Idemitsu**) welcomes the opportunity to provide the following submission in regards to the Consultation Letter issued (15 April 2014) by the Australian Competition and Consumer Commission (**ACCC**), in relation to the revised Australian Rail Track Corporation (**ARTC**) application to vary the Hunter Valley Rail Network Access (**HVAU**) to include Gap to Turrawan Segments (**Revised Variation**).

Idemitsu is an active coal producer located in both the Hunter Valley and the Gunnedah Basin, utilising the current Hunter Valley Rail Network (**Network**). As part of Idemitsu's logistics operation from its Boggabri Mine located in the Gunnedah Basin, coal is transported by rail originating in the Gap to Turrawan segment to the port of Newcastle.

Idemitsu has previously provided submissions in response to the ACCC's Consultation Paper (23 July 2013) and Position Paper (12 December 2013). Subsequently, ARTC has withdrawn its Initial Variation application (20 January 2014) to include Gap to Turrawan Segments in the HVAU Network (**Initial Variation**) and has submitted a Revised Variation (24 March 2014).

Idemitsu has had the opportunity to consider the Revised Variation:

## 1. Effective Date

Idemitsu acknowledges the intent of the Initial Variation was to obtain ACCC approval prior to 31 December 2013 to enable an effective date of 1 January 2014, obviously this has not occurred. In the Revised Variation, ARTC has proposed a retrospective effective date of 1 January 2014 for a variety of benefits. These include:

(a) alignment of obligations under the HVAU with respect to pricing, performance reporting, annual compliance assessment and Access Holder calendar year entitlements;

(b) reduction in the regulatory burden on ARTC in relation to the annual compliance assessment, RAB and RAB Floor Limit calculations and RAB roll forward;

(c) implementation and application of loss capitalisation for the calendar year;

(d) more efficient unders and overs accounting for the complete calendar year rather than part year apportionments; and

(e) simpler application of the system wide true up test and the annual TOP Rebate reconciliation which are based upon a calendar year.

In the Position Paper, the ACCC advised ARTC needed to consider the transition period from 1 January 2014 until the subsequent effective date (subject to ACCC approval). ARTC have considered this transition by performing various HVAU obligations with the assumption the ACCC would approve the extension to Pricing Zone 3, such as 2014 pricing.

Idemitsu acknowledges the benefits outlined by ARTC above and has no objection to a retrospective effective date of 1 January 2014.

## 2. Asset Valuation

It has been acknowledged throughout the ACCC consultations, the extension of Pricing Zone 3 to include the Gap to Turrawan segment was not ascribed a regulatory asset value under the NSW Rail Access Undertaking (**NSWRAU**) and as such Section 4.4(a) (iii) of the HVAU is applicable and a depreciated optimised replacement cost (**DORC**) method of valuing assets should be applied to establish the initial Regulated Asset Base (**RAB**).

After a considerable consultation process between ARTC, the ACCC and Gunnedah Basin coal producers, a number of concerns and issues were identified in the DORC valuation of the segment as at 1 January 2013. After further consultation with the ACCC and Gunnedah Basin coal producers, amendments have been made to the DORC valuation in the Revised Variation to establish the initial RAB, the proposed revised initial RAB value as at 1 January 2013 is $323.37 million.

Amendments made to the initial DORC valuation in the Initial Variation include:

(a) removal of a number of rail assets which are not required for coal haulage;

(b) inclusion of an amount representing financing costs – interest during construction;

(c) reduction in the proposed mark-up to direct costs as a means of calculating indirect costs for signalling, ballast, rail and sleepers;

(d) inclusion of present value cost savings with respect to the operation and maintenance of a modern equivalent asset (optimised asset) – limited to specific assets;

(e) adjustments (net reduction) to the remaining useful life of bridges, signalling assets and adjusting for the mix of timber and steel sleepers;

(f) reduction to the remaining lives of the relevant assets planned to be replaced as a result of the imminent 30 tonne axle load investment program; and

(g) correction of several modelling errors underpinning the DORC valuation, which will provide a net increase to the DORC.

Furthermore, the initial RAB value for the Gap to Turrawan segment will be divided into relevant Additional Segments defined in the Revised Variation:

| Additional Segment | DORC Valuation (1 Jan 2013) |
|---|---|
| Gap to Watermark | $82.10M |
| Watermark to Gunnedah | $95.41M |
| Gunnedah to Boggabri | $87.38M |
| Boggabri to Turrawan | $58.48M |
| **Total** | **$323.37M** |

Idemitsu acknowledges the DORC valuation contained in the Revised Variation has complied with the prescribed process in the HVAU.

The Initial and Revised Variations both consider the determination of initial RAB value for the Gap to Turrawan segment as at 1 January 2013 and rolled forward in accordance with the NSWRAU to establish an opening RAB value for 1 January 2014, which is consistent with previous approaches by ARTC and endorsed by the ACCC. Idemitsu understands the workings for the initial RAB roll forward were provided to the ACCC on a confidential basis. Idemitsu would welcome the transparency of these workings as part of the 2014 Annual Compliance Assessment.

## 3. Access Charges

ARTC have advised when determining the Initial Indicative Access Charges for the 2014 calendar year for extended Pricing Zone 3, they have considered and complied with the pricing objective of Section 4.13 and the annual process outlined in Section 4.20 of the HVAU. The Initial Indicative Access Charge for the 2014 calendar year is:

| Extended Pricing Zone 3 | Non Top $/kgtkm (ex GST) | TOP $/kgtkm (ex GST) |
|---|---|---|
| Initial Indicative Service 1 | 1.496 | 9.635 |

Idemitsu understands the above access charge was determined based on the assumption the extended Pricing Zone 3 (including the initial RAB value) would be approved by the ACCC prior to 31 December 2013 and effective 1 January 2014 and using the DORC valuation in the Initial Variation ($325.4 million), the Revised Variation is $323.37 million. Despite the lower DORC valuation in the Revised Variation, Idemitsu understands there will be no change to the Initial Indicative Access Charges above, due to ARTC exercising their discretion regarding setting access charges (not recovering full Economic Cost). The above Initial Indicative Access Charge, for both DORC valuations in the Initial and Revised Variations are priced below ceiling and any shortfall will be recovered through loss capitalisation.

## 4. Capitalised Loss Transparency

Idemitsu supports the concept of improved transparency regarding charges Access Holders in the extended Pricing Zone 3 are likely to face in the future by ARTC providing an estimate of likely losses to be capitalised to the Access Holder during the annual pricing process. ARTC are proposing to provide Access Holders with opening and closing RAB estimates for the relevant year. In addition, Idemitsu requests ARTC as part of this transparency to provide Pricing Zone 3 Access Holders a component breakdown of the RAB movement by dollar amount (i.e. loss capitalisation, capital expenditure, operating costs, rate of return and revenue). This will require some additional drafting amendments in section 4.20(d) of the HVAU.

Furthermore, the loss capitalisation amount should be clearly defined in the annual compliance assessment for the extended Pricing Zone 3.

## 5. Amendments

ARTC in the Revised Variation have proposed a number of amendments to both the HVAU and the Indicative Access Holder Agreement, these amendments appear reasonable and reflect the introduction of the Gap to Turrawan segment.

In conclusion, Idemitsu considers it appropriate to extend the current Pricing Zone 3 to include the Gap to Turrawan segments as part of the Network contained in the HVAU.

Idemitsu would like to thank the ACCC for its consideration on these matters and if further discussion is required please do not hesitate to contact Mr Craig Forster (Ph +61 7 3222 5623).

Yours sincerely

Lee Gordon
General Manager Marketing and Logistics