

AUSTRALIAN RAIL TRACK CORPORATION LTD

NATIONAL COMPETITION POLICY REVIEW (NCPR)

ARTC SUBMISSION



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1 KEY POINTS

ARTC has reviewed the Issues Paper (**Issues Paper**) released by the panel conducting the National Competition Review (**Review Panel**) as well as several submissions made to the Review Panel by key participants in the rail industry including Aurizon Holdings Limited (**Aurizon**) and Asciano, and a key participant in the coal industry served by rail, Glencore. ARTC has also reviewed the Draft Report released by the Review Panel (**Draft Report**).

ARTC has identified a number of areas raised in the Issues Paper and relevant stakeholder submissions, as well as the views of the Review Panel expressed in the Draft Report to which it will respond in this submission. Key points arising from ARTC's submission are prescribed below.

KEY POINTS

The scope and impact of economic regulation in rail ...

1. - Economic regulation should be applied consistently across the national rail network. This is not to say that uniform regulation in the form of access regimes or undertakings should apply in all circumstances. There should be differentiation between access regimes based on the access providers' market and industry position.
2. - Consistent rail regulation will not be achievable, if administered by several jurisdictional regulators due to the significant discretion provided to the regulator. ARTC supports the establishment of a national access and pricing regulator, and would welcome consideration by governments of national coverage of all rail networks in Australia. The costs and benefits associated with the establishment of a separate national rail regulator could then be determined.
3. - In order to achieve competitive neutrality in the provision of rail and road services in a number of interstate and regional transport markets, it is important for both transport modes to access relevant infrastructure on the same basis. There is merit in having a single national road (or even land transport) regulator, but there would need to be support from the states for the implementation of national regulation of both modes.
4. - ARTC's experience to date with the application of economic regulation in rail indicates:
 - a. - Regulatory practice to date has focused more-so on delivering efficient service and now the focus needs to be re-balanced towards the need and incentives to renew assets and invest for capacity enhancement.
 - b. - Regulatory arrangements in rail are becoming increasingly complex resulting in greater development and compliance costs for industry.
 - c. - The development of long term regulatory instruments has not provided ARTC with the expected certainty needed for investment where views of the regulator can change during the term.
 - d. - Rail networks often are dedicated broader supply chains and using a regulatory instrument applicable to one element of a broader supply chain is not necessarily the best means to pursue wider supply chain efficiency and coordination objectives, and may increase regulatory complexity and risk.

Rail industry structure ...

1. - ARTC welcomes the Review Panel's draft finding that rail reform has been successful and submits that vertical separation is the most appropriate model to promote competition and drive efficiency gains in the freight logistics sector
2. - Structural separation has been successful at promoting competition on the interstate network, since the reforms of the 1990's there has been around 25 operators enter the market, three have exited and 15 have been consolidated into four main operators. In terms of infrastructure, ARTC's \$2.5 billion investment program has provided a significantly enhanced asset for above rail operators, allowing them to harness the economics of longer and heavier trains. Reliability on the interstate network increased by 15% in 2013 alone.
3. - Considering the scope of operation and importance of the Hunter Valley coal chain to the Australian economy, ARTC submits that vertical separation should be maintained in the Hunter Valley. Efficiency improvements are being achieved through a highly competitive market for rail services provided by four rail haulage operators servicing 35 mines in the Hunter Valley.
4. - ARTC acknowledges that under-investment on grain branch lines is an issue across all jurisdictions and competitive structures. The quality and capability of the infrastructure is a major impediment to the efficiency of rail operations across all jurisdictions. The limited investment in grain branch lines is due to the economic reality that there is limited potential to earn a commercial return on investment, rather than structural impediments.

Delivering road/rail competitive neutrality ...

1. - It is encouraging that the Review Panel has considered the breadth of views and articulated the core issue of the road pricing reform debate; that more effective institutional arrangements coupled with a cost reflective road pricing regime are needed to promote an efficient mix of road and rail transport
2. - ARTC urges the Review Panel to strengthen Draft Recommendation 3 in the final report by including a recommendation on the accelerated introduction of heavy vehicle road pricing reform as a matter of priority for Government.
3. - As an interim measure, and to accelerate introduction, pricing reform should apply to articulated vehicles on the National Highway and State Arterial road network.

2 BACKGROUND

ARTC currently operates the interstate rail network between Brisbane and Kalgoorlie connecting to ports in Sydney, Melbourne and Adelaide (but excluding metropolitan passenger commuter networks and that part of the interstate rail network between Sydney and Newcastle). ARTC also manages the Hunter Valley coal network to Newcastle ports, as well as several parts of regional rail networks in NSW and Victoria.

In the last year or two, ARTC commenced management of the Sydney metropolitan freight network (**MFN**) connecting the interstate rail network to Port Botany, and opened for operations its \$1bn 36km Southern Sydney Freight Line (**SSFL**) between Macarthur in southern Sydney to Sefton Park permitting, for the first time, the operation of freight trains into Sydney from the south and free of the Sydney metropolitan commuter network. This new dedicated line will go a long way to alleviating a major bottleneck on the interstate freight rail network and will more than triple the capacity of this important rail corridor. Importantly, it will complement work now underway upgrading the rail corridor through the City's northern suburbs to Newcastle and the line to Port Botany, as well as support the development of the new intermodal terminal in Sydney proposed to be built at Moorebank.

Since the mid-2000's, ARTC has invested heavily in both the interstate and Hunter Valley rail networks. On the interstate network ARTC has invested around \$X.Xbn (including the SSFL) primarily aimed at improving rail's competitiveness on its north-south interstate rail corridor (between Melbourne and Brisbane) against strong road transport competition. Further detail in relation to this investment and outcomes is provided at section 5 of this submission.

On the Hunter Valley coal network ARTC has invested around \$1.5 billion over the last 10 years and expects to invest another \$0.5bn over the next 5 years. These investments have resulted in increased coal chain capacity from 75 million tonnes per annum (mTpa) in 2004-05 to 166mTpa in 2014 and 207mTpa expected in 2010.

ARTC also has an agreement in place with the owners of that part of the interstate network in WA that provides for consistency in conditions of key elements of access and operations for interstate services between Kalgoorlie, Perth and the Port of Kwinana.

Almost all parts of the interstate rail network managed by ARTC are now covered by a voluntary access undertaking (ARTC Interstate Access Undertaking (**IAU**)) accepted by the Australian Competition and Consumer Commission (**ACCC**) in 2008. ARTC is currently working towards extending coverage of this access undertaking to include those parts that have recently come under ARTC control including:

- NSW/Queensland Border to Acacia Ridge in Brisbane; and
- MFN in Sydney.

The interstate rail network in WA and the important rail freight line connecting Brisbane to far north Queensland continues to be covered by the rail access regimes administered by state based regulators in those states respectively. As significant interstate rail freight travels on these parts of the national rail network, the application of commercial and regulatory frameworks in these jurisdictions can have a significant impact on interstate freight markets and ARTC business.

ARTC's Hunter Valley coal network connecting coal mines in the Hunter Valley and Gunnedah coal basins to the port of Newcastle is covered by ARTC's voluntary access undertaking (ARTC Hunter Valley Coal Network Access Undertaking (**HVAU**)) accepted by the ACCC in 2011. The HVAU replaced the previous coverage of the NSW rail access undertaking and introduced a new framework for commercial and operational arrangements in the Hunter Valley intended to provide greater certainty for present and future access to the rail network and promote future investment in rail and complementary coal chain capacity to underpin substantial growth in demand for export coal through Newcastle in the foreseeable future. Further detail into the development of this voluntary access undertaking will be provided later in this submission.

Remaining parts of the ARTC network in regional NSW and Victoria, and the line connecting Sydney and Newcastle remain covered by rail access regimes administered by regulators in those States respectively.

ARTC, and its shareholders, have long held an objective to achieve greater consistency of regulation of rail networks in Australia generally and, in particular, on the interstate rail network. This should not be taken to mean uniform regulation across rail networks where ARTC recognises that the different commercial and operating frameworks of rail networks require different regulatory treatments and greater flexibility in arrangements (referred to later in this submission), but consistent arrangements where network users have greater certainty as to how they will be treated so as to instil confidence in using and investing in the rail network and complementary parts of relevant supply chains.

On the interstate rail network, consistent regulatory and commercial arrangements have been developed over the last decade primarily through a combination of:

- increasing the extent of single management of the interstate network through lease of those parts of the interstate network in Victoria (1998), NSW (2004) and Queensland (2011); and
- establishing and maintaining goodwill and cooperative arrangements between jurisdictions at an operational level.

ARTC recognises that, in 2006, governments agreed, through the Competition and Infrastructure Reform Agreement (**CIRA**), to provide for more simple and consistent national economic regulation of nationally significant infrastructure, including railways. ARTC participated, with the ACCC, in the development of a proposal for a code that would apply to all rail networks that would govern central decision making in relation to the coverage and intensity of regulation applicable to rail networks as well as the application of a consistent set of principles for the development of access undertakings to rail networks. This proposal was considered by governments, but ARTC understands that relevant governments

elected to proceed with an alternative path to seek certification of existing state based regimes in order to satisfy CIRA requirements.

Further detail into this development will be provided later in this submission.

ARTC has actively participated in a number of previous reviews of competition arrangements and rail access regimes both nationally and on a state basis. Key relevant national reviews are the Productivity Commission reviews of the National Access Regime and related legislative arrangements including:

- the National Access Regime in 2001 and 2013; and
- National Competition Policy arrangements in 2004.

Three broad themes submitted by ARTC to these inquiries were:

- ARTC is of the view that there should be a single adjudicator with respect to regimes for access in Australia.
- ARTC is of the view that the differentiation of access regimes should be on the access providers' market and industry position.
- ARTC is of the view that Industry Codes should be able to be departed from by access providers as long as it can be demonstrated to the ACCC that the proposed regime satisfies the requirements of an access undertaking.

ARTC continues to broadly support these positions in the light of its more recent experiences in regulation of the national rail network. Further commentary and qualifications in this regard are provided in more specific issues addressed by ARTC later in this submission.

3 RELEVANT ISSUES RAISED IN THE NCPR ISSUES PAPER, DRAFT REPORT AND SUBMISSIONS

ARTC has reviewed the Issues Paper as well as several submissions made to the Review Panel by key participants in the rail industry including Aurizon and Asciano, and a key participant in the coal industry served by rail, Glencore. ARTC has also reviewed the Draft Report.

ARTC has identified a number of areas raised in the Issues Paper and relevant stakeholder submissions, as well as the views of the Review Panel expressed in the Draft Report to which it will respond in this submission as set out below and in subsequent sections of this submission. In particular, ARTC seeks to clarify and respond to views expressed in relation to both ARTC and the rail industry generally in the above submissions.

3.1 The scope and impact of economic regulation in rail

ARTC has noted the following questions raised in the Issues Paper relevant to the scope and impact of economic regulation in regulated industry sectors, including rail.

‘Are there unwarranted regulatory impediments to competition in any sector in Australia that should be removed or altered?’

‘Are competition-related institutions functioning effectively and promoting efficient outcomes for consumers and the maximum scope for industry participation?’

‘What is the experience of businesses in dealing with the ACCC, the Australian Competition Tribunal and other Federal regulatory bodies?’

‘What is the experience of businesses in dealing with state and territory regulators?’

ARTC has also identified a number of views relevant to the scope and impact of regulation in rail expressed by stakeholders as set out in Table 1 below.

Table 1: Relevant stakeholder views - The scope and impact of economic regulation in rail

Aurizon (p17)	<i>Economic regulation of some key enabling infrastructure has become complex, expensive and time-consuming. Many regimes have become disproportionately prescriptive or elaborate relative to the economic issues they are attempting to solve. As a result, clarity as to the objective of economic regulation appears to have diminished, with little sense of the best way to drive further productivity improvement.</i>
Aurizon (p22)	<i>There is no clear reasonableness standard in Australian regulation. The regulator is required to promote ‘effective competition in related markets’, without any benchmarks around what is ‘effective competition’ or when ‘effective competition’ has been achieved. This encourages a process of continual assessment against ‘perfect’ or theoretical benchmarks, rather than settling on a reasonable (albeit not necessarily perfect) outcome. As put by in 2005 by the then Prime Minister’s Export Infrastructure Taskforce: The manner in which regulators have approached their task has compounded the difficulties. A quest for ‘first best’ solutions, combined with a focus on removing monopoly rents, has distracted from what should be the regulatory task: which is not to determine whether what has been proposed by way of access conditions is optimal, but whether it is reasonable. The search for optimality and precision in regulatory decision making has not only made the regulatory</i>

	<i>process less predictable than it should be, but has also added greatly to regulatory delay, hindering investment in infrastructure used by export industries.¹</i>
Aurizon (p24)	<i>Another notable dynamic is that regulation has gone beyond that necessary to promote competition in dependent markets, and has begun to include elements of a broader industry policy. For example, in the rail sector, the regulators of bulk-supply chains have been called upon to develop planning frameworks for supply-chain expansions,² coordinate unregulated parts of integrated supply-chains to promote efficiency,³ and develop financial models for the direct sharing of the capital costs of expansions with mining companies.⁴ Likewise, the regulators of general purpose or mixed rail lines are required to consider issues relating to the interaction between urban passenger rail and freight services, the underlying poor economics of many state-owned networks,⁵ and the mixed commercial and social objectives of government-owned railways.⁶</i>
Aurizon (p28)	<i>Regulation has been effective at promoting productive and allocative efficiency in a number of downstream markets. Entry has occurred, and those entrants have driven lower prices and won market share from incumbents. However, regulation has been less effective at achieving dynamic competition – namely, encouraging dynamic service offerings in downstream markets, prompting the development of new facilities, promoting innovation, or contributing to major advancements in research or technology.⁶ In part, this is because regulation severely limits the ability of both regulated businesses and the users of regulated services to capture a return from innovation. This is linked to the reluctance of regulators to endorse efficient price discrimination, and the tendency of regulatory regimes to socialise the benefits of innovation by regulated businesses.</i>
Asciano (p8)	<i>In Asciano's opinion the light-full regulatory model dismissed by the Productivity Commission has merit.⁷ The Productivity Commission bases its opinion on the view that the regulatory costs of creating standard terms and conditions are too high (although this conclusion is based on assumption rather than actual facts). However, it would seem that the Productivity Commission is under estimating the number of access agreements that will have to be negotiated especially given this is a repeated game with in most cases multiple access seekers. For example, if you take the ARTC which has a standard access agreement as part of its ACCC approved undertaking. The ARTC provides access to multiple rail companies using this access agreement and given standard agreements run for between 5 and 10 years this agreement with minimal change has been utilised a number of times for the same access seeker. The cost of producing the standard access agreement in the first instance would be small in comparison with the cost to ARTC of multiple stand alone negotiations which ARTC would have to have had in the absence of the regulatory approved standard access agreement. It should be recognised that even if there is a standard access agreement in place, under the negotiate-arbitrate framework there remains an imbalance in the information held by both parties. Significantly, this information imbalance provides the infrastructure provider with an advantage in price negotiations and often results in costly and protracted access negotiations. As such, Asciano believes that the access framework and access outcomes should be improved by requirements for infrastructure providers to supply a reasonable level of cost information to facilitate even handed price negotiations. Asciano recognises that the Productivity Commission discusses this issue and concludes that there is no compelling evidence that poor information disclosure is a weakness in the access regime. However, the Productivity Commission does not take account of the relative economic efficiency of prices negotiated under asymmetrical information and are more focussed on process efficiency. A price based on transparent cost information available to both negotiating parties is more likely to be both efficient and non-discriminatory than a price negotiated when one party has incomplete information. A negotiation where both parties have substantially complete information is much more likely to result in a price outcome which approximates the outcome that could be expected in a competitive market.</i>
Asciano (p10)	<i>This multiplicity of regimes adds costs and complexity to rail access for no benefit, particularly as many of the access regulation functions are duplicated across states. Given this Asciano has advanced the concept of an industry specific national rail regime should be further considered. Asciano does not, nor indeed does the ARTC, advocate a one size fits all approach to rail regulation. For example you would not expect that the appropriate access regime in a government owned and operated regional grain network would be the same regime required to regulate a vertically integrated monopolist track provider such as Aurizon in Queensland. However, having a single national regulator would have a number of advantages:</i> <ul style="list-style-type: none"> <i>• Reduced duplication of effort – even with a number of tailored regimes (for example a regional network regime plus an interstate network regime) the number of regimes in operation would be significantly less than the current situation. In addition with one regulator making decision some key features of the</i>

¹ 'Exports and Infrastructure Taskforce, Australia's Export Infrastructure: Report to the Prime Minister, (May 2005), p.2.'

² 'For example, both ARTC and Aurizon Network have been required to develop industry models which regulate how the network service provider engages not only with direct users (rail operators) of the service but also with other non-regulated infrastructure and service providers, in relation to how expansions of rail networks will be planned, negotiated and executed.'

³ 'For example, ARTC has been required by the ACCC to implement a pricing mechanism to actively coerce investment by other parts of the supply chain in order to achieve a theoretically optimal supply chain configuration, as opposed to pricing to reflect utilisation of the facility being regulated and allowing competition and aligned incentives to identify market based solutions.'

⁴ 'For example, Aurizon Network was required under its 2010 Access Undertaking to submit to the QCA a standard user funding model. ARTC is also required to make user-funding available to coal mines in the Hunter Valley.'

⁵ 'These typically involve regional freight networks. For example, IPART recently reviewed access charges for grain services on the NSW country network.'

⁶ 'Coulbuck, D, Ivaldi, M and McCullough G (2013) 'Static-Dynamic Efficiency Trade-off in an Open Access Policy: Application to the US Rail Freight Industry', Working Paper, note that 'to sustain innovation, and thus support dynamic efficiency, investment requires a rate of return which can be obtained through above-marginal cost pricing over time and this leads to a degree of allocative inefficiency. Indeed, some prospects of profits are necessary to motivate firms to make costly investment'. In an open access model, the regulated service provider may not have sufficient financial incentives to take risks and an access seeker may see its innovations quickly replicated and returns dissipated through competitive pricing.'

⁷ 'Productivity Commission, National Access Regime, Productivity Commission Inquiry Report, October 2013, p124'

	<p>regime would be common across networks. For example the approach to calculating the cost of capital or the approach to liabilities and indemnities which can currently vary significantly via jurisdiction, would be common. Having a single regulator would significantly reduce the regulatory resources required, saving both industry and Government significant resources. This proposal is consistent with the current Government's priority to reduce unnecessary red tape and cost.</p> <ul style="list-style-type: none"> • Increased specialisation – some regulators only deal with rail access issues intermittently, usually at the time an access undertaking comes up for renewal. Access undertakings are typically reviewed on a 5 or 10 year cycle. Thus it is difficult for these regulators to retain in house knowledge on rail issues. A national rail regulator with dedicated specialised rail staff would more likely to have the appropriate expertise and as such be more likely to come to efficient decisions. • Regulatory capture and independence – the potential for regulatory capture will be reduced with a national regulator. Where a state based regulator, part of the state government bureaucracy, regulates a private company which is a significant contributor to state finances or even a state government owned entity, the commitment to independence and efficient regulatory decision making may be tested. These close relationships would be more arms length with a national regulator. • Improved regulatory certainty – having a single regulator which as noted above would allow specialisation and also would implement decision consistently across networks would increase regulatory certainty compared with the status quo of multiple regulators and multiple access undertaking. The increase in regulatory certainty would reduce investment risk and all other things being equal expect to encourage more efficient investment decisions. • Co-ordination benefits – having a single regulator approve technical rail documents such as network rules will increase consistency between network owners thereby reducing operators' costs. For example, rules regarding rolling stock approval or possession planning would likely become more consistent thereby reducing co-ordination and regulatory compliance costs of dealing with multiple regimes. <p>Asciano believe that there would be significant benefits to having a single rail regulator and that the Productivity Commission's rejection of the concept was based on too narrow a view of the benefits which we believe would be significant.'</p>
Glencore (p2)	We believe there may be some efficiencies in a move from State based regulation to a single Federal regulator. In Glencore's view, such a move should be accompanied by the reform of the NAR.
Glencore (p8)	Glencore would suggest that an important constraint on the "negotiate-arbitrate" model should be to prevent an infrastructure owner favouring an access seeker willing to accept a negotiated outcome over another access seeker which relies on the regulated access seeking process. In particular, we suggest that one solution to the problem of forcing infrastructure investment is to permit "user funding" of infrastructure, and if that is the case then specifically discrimination between user funded expansions and infrastructure owner funded expansions should not be permitted.
Glencore (p9)	<p>Glencore is of the view that access undertakings can have a useful part to play in the regulation of access to infrastructure. However, there are difficulties with a voluntary access undertaking regime. By placing the drafting of the access undertaking in the hands of the infrastructure owner, a voluntary access undertaking regime creates considerable difficulties both for users and regulators who seek to influence the terms of the access undertaking. The asymmetry created by the fact that the infrastructure owner can seek amendment of the access undertaking at any time means that it is unwise for users to consent to lengthy access undertaking periods, because there can be no guarantee that the infrastructure owner would not seek to revisit the terms of the access undertaking prior to the end of the undertaking period if the terms of the access undertaking prove to be adverse to the infrastructure owner. On the other hand, the users of the infrastructure and seekers of access to the infrastructure have no ability to trigger a review of the terms of the access undertaking. Shorter undertaking periods lead to considerable costs caused by constant review of access undertakings.</p> <p>Glencore believes that mandatory access undertakings are one approach which could be used where appropriate to help address these difficulties.</p>

ARTC has also reviewed the Draft Report and has identified a number of views expressed by the Review Panel in relation to issues raised in the Issues Paper and in relevant stakeholder submissions to which it will respond in this submission as set out below and in subsequent sections of this submission.

ARTC has also identified a number of views expressed by the Review Panel in the Draft Report relevant to the scope and impact of economic regulation in rail as set out in Table 2 below.

Table 2: Draft Report views – The scope and impact of economic regulation in rail

Competition laws and regulations that are clear, predictable,	<p>Australians expect consumers to be dealt with fairly and on reasonable terms, and businesses to refrain from conduct that damages the competitive process (and ultimately consumers). They expect laws to be clear, predictable and reliable and administered by regulators (and applied by the judicial system) without fear or favour. Our competition law must ensure that market participants, big and small, can compete in a way that allows the most efficient and responsive players to thrive.</p> <p>These principles are particularly important where market participants differ in their capacity or financial</p>
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and reliable	<p>means to engage with the legal or regulatory process. Difficulty in accessing justice in matters of competition policy or consumer protection can undermine broader confidence in our regulatory institutions.</p> <p>There is a natural tension between designing specific laws and regulations to deal with problems that emerge at a point in time and building in flexibility to cope with changing market circumstances as they arise. Laws that are less predictable in their immediate application may nevertheless prove more reliable over time as they are adapted through the judicial process to encompass novel developments.</p> <p>This is especially relevant when new technologies are rapidly altering market conditions faced by businesses and consumers. The more tightly specified our laws, the more likely they are to lag behind developments in markets and possibly act against the long-term interests of consumers.</p> <p>A competition policy that is fit for purpose should enshrine competition law that is sufficiently general in its design to accommodate evolving ways of doing business or engaging with consumers, but sufficiently reliable and predictable in its application so as not to discourage innovation and entrepreneurship.(p20)</p> <p>This reflects the object of the law to protect the welfare of Australians. There is no sound reason for Australian law to regulate conduct affecting competition in overseas markets.</p> <p>That should not mean, though, that the CCA ignores the forces of competition that arise outside Australia but which affect Australian markets. Today, more than ever, Australian consumers are able to use the internet to browse for and purchase goods and services from overseas suppliers. While the objective of the CCA is to protect and promote competition in Australian markets, frequently the sources of competition in Australian markets are global.(p39)</p>
Price Discrimination	<p>Price discrimination is the practice of charging different prices for the same or similar goods or services, where the price difference does not reflect differences in the cost of supply. Examples of price discrimination include student, seniors and family discounts, 'early bird specials', and may include discounts for bulk purchases and group buying.</p> <p>The effects of price discrimination will depend on the particular circumstances of the market. Pricing according to consumer willingness to pay can result in more consumers being able to obtain the good or service than if a common price were charged. In these circumstances price discrimination can make goods or services more accessible and can enhance consumer choice.</p> <p>Nonetheless, awareness of price discrimination can irritate consumers who find themselves unable to purchase goods at the same price that others can.(p212)</p> <p>Supporters of a price discrimination provision often argue that it would improve the ability of small businesses to compete, and allow them to be more responsive to consumer needs because it would remove the capacity of larger firms to price their product below the level charged by local, smaller retailers.⁸285 However, restricting pricing flexibility can be harmful to competition and thereby harm consumers.</p> <p>Price discrimination should only be unlawful where it substantially lessens competition. The Panel agrees with the conclusions of previous reviews that anti-competitive price discrimination is best addressed under section 46. The Panel's proposal for the reform of section 46 should also assist the identification and prohibition of such conduct.(p213)</p>
Industry Codes	<p>Codes of conduct play an important role under the CCA by providing for a flexible regulatory framework to set norms of behaviour, and are generally applied to relationships between businesses within a particular industry.</p> <p>The Panel has heard of codes that are perceived to be lacking in meaningful enforcement sanctions and the capacity for public enforcement.</p> <p>The introduction of civil penalties and infringement notices for breaches of codes strengthens the CCA enforcement options.</p> <p>Having these options available for CCA codes is a significant development. Any new CCA codes could consider whether they should apply penalties for non-compliance.(p220)</p>
National Access Regime - Scope	<p>The National Access Regime in Part IIIA of the CCA was originally established to enable third-party access to identified bottleneck infrastructure where it was apparent that economic efficiency would be enhanced by promoting competition in markets that were dependent upon access to that infrastructure.</p> <p>The bottleneck infrastructure cited by the Hilmer Review is now subject to a range of access regimes. Those regimes appear to be achieving the original policy goals identified by the Hilmer Review. Today, Part IIIA has only a limited role in the regulation of that bottleneck infrastructure.</p> <p>The question that arises today is: what are the infrastructure facilities for which access regulation will be required under Part IIIA in the future? Unless it is possible to identify those facilities or categories of facilities, it is difficult to reach a conclusion that the regulatory burden and costs imposed by Part IIIA on Australian businesses are outweighed by economic benefits, or that the benefits can only be achieved through the Part IIIA framework.</p> <p>The recent PC inquiry concluded that the Regime is likely to generate net benefits to the community, but that its scope should be confined to ensure its use is limited to the exceptional cases where the benefits arising from increased competition in dependent markets are likely to outweigh the costs of regulated third-party access.</p> <p>The Panel agrees that the scope of the Regime should be confined because of the potential costs of regulation.</p> <p>The Panel invites further comment on:</p> <ul style="list-style-type: none"> • the categories of infrastructure to which Part IIIA might be applied in the future, particularly in the mining sector, and the costs and benefits that would arise from access regulation of that infrastructure; or • whether Part IIIA should be confined in its scope to the categories of bottleneck infrastructure cited by the Hilmer Review.
Declaration	<p>The declaration criteria in Part IIIA should be targeted to ensure that third-party access is only mandated where it is in the public interest. To that end: • criterion (a) should require that access on reasonable terms</p>

⁸ 'See generally submissions to the Senate Economics Committee, Inquiry into the Trade Practices Amendment (Guaranteed Lowest Prices — Blacktown Amendment) Bill 2009.'

	<p>and conditions through declaration promote a material increase in competition in a dependent market; • criterion (b) should require that it be uneconomical for anyone (other than the service provider) to develop another facility to provide the service; and • criterion (f) should require that access on reasonable terms and conditions through declaration promote the public interest. The Competition Principles Agreement should be updated to reflect the revised declaration criteria.(p273)</p>
National Competition Council	<p>The NCC, which oversaw the NCP, now has a considerably diminished role. It has been put to the Panel that the NCC no longer has the capacity to provide leadership in this domain. Draft Recommendation 46 proposes that the remaining functions of the NCC, associated with the National Access Regime, be transferred to a new national access and pricing regulator. The NCC could then be dissolved.(p283)</p> <p>Including the NCC's functions under the National Access Regime and the National Gas Law within the access and pricing regulator would allow the NCC to be dissolved.(p296)</p>
Australian Council for Competition Policy	<p>The Panel believes that reinvigorating competition policy reform requires leadership from an institution specifically constituted for the purpose and therefore proposes establishing the Australian Council for Competition Policy (ACCP) with a mandate to provide leadership and drive implementation of the evolving competition policy agenda. The establishment of governance arrangements to implement reforms must be undertaken in the context of Australia's federal structure.</p> <p>The Panel sees advocacy for competition as a central function of the ACCP, and that it should act as an independent assessor of progress on reform.</p> <p>The effectiveness of the ACCP could be strengthened by assigning it a market studies function which would create a convenient, consistent, effective and independent way for governments to seek advice and recommendations on recurrent and emerging competition policy issues.</p> <p>The competition policy environment is not static. New technologies can raise new issues and resolve older ones. The Panel considers that governments would benefit from an annual analysis of developments in the competition policy environment, which could be undertaken by the ACCP.</p> <p>There is a case to be made that the benefits of reform, including any fiscal dividend, should be commensurate with the reform effort made. The differing revenue bases of the Commonwealth and the States and Territories mean that revenue may not flow in proportion to reform effort.</p> <p>The PC should be tasked to undertake a study of reforms agreed to by the Commonwealth and state and territory governments to estimate their effect on revenue in each jurisdiction. The ACCP could then assess whether reforms had been undertaken to a sufficient standard to warrant compensation payments. That assessment would be based on actual implementation of reforms, not on the basis of undertaking reviews or other processes.(p287)</p>
Role of the ACCC	<p>The Panel considers that the ACCC should continue to combine competition and consumer regulation. There are synergies from having the competition and consumer functions within the one regulator. For example, fair trading issues may raise concerns about misuse of market power, unconscionable conduct or unfair contract terms. Having one regulator overseeing all of these functions allows the different courses of action to be considered simultaneously. It also encourages the building of expertise. We recognise that with these synergies come tensions, and note that the ACCC should continue to carefully balance its competition-related regulatory tasks with its consumer protection role.(p290)</p>
National Regulation	<p>A multiplicity of regulators can also be administratively costly, and lead to gaps and overlaps in regulatory responsibility. Business may have to engage with more than one regulator.</p> <p>The Panel notes these concerns but believes that States and Territories should continue to have responsibility for those sectors with which they are, by geography and institutional arrangements, better placed to deal.(p295)</p> <p>The Panel supports a continuing role for state and territory economic regulators. However, a move to national regulation as circumstances permit should be encouraged, including, for example, in the case of water.(p297)</p>
Single access and pricing regulator	<p>The Panel considers that access and pricing regulatory functions would be best performed by a single national independent agency. The benefits of a single national independent agency include:</p> <ul style="list-style-type: none"> • a single agency will have the scale of activities that enables it to acquire broad expertise and experience across a range of industries, and acquire and retain staff who have that expertise; • a single agency regulating a range of infrastructure industries reduces the risk of capture (the agency losing necessary independence from the regulated industry); and • a single agency will reduce the costs associated with multiple regulators and regulatory frameworks and promote consistency in regulatory approaches.(p296) <p>The Panel sees benefit in focusing the ACCC on its competition and consumer functions and separating out its access and pricing functions into a separate, dedicated regulator. Amalgamating all price regulatory functions into a single body will sharpen focus and strengthen analytical capacity in this important area of regulation.(p295)</p> <p>The Panel proposes the creation of a separate access and pricing regulator to oversee all industries currently regulated by the Commonwealth.</p> <p>The following regulatory functions would be transferred from the ACCC and the NCC and be undertaken within the national access and pricing regulator:</p> <ul style="list-style-type: none"> • the powers given to the NCC and the ACCC under the National Access Regime; • the powers given to the NCC under the National Gas Law; • the functions undertaken by the Australian Energy Regulator under the National Electricity Law and the National Gas Law; • the telecommunications access and pricing functions of the ACCC; and • price regulation and related advisory roles under the Water Act 2007 (Cth). <p>The national access and pricing regulator should be established with a view to it gaining further functions as</p>

	<p>other sectors are transferred to national regimes.(p297)</p> <p>The Panel notes concerns⁹ expressed by the PC about a single body undertaking these functions but does not foresee any conflict in a single regulator performing both functions and anticipates there may be benefits. Under the current telecommunications access regime (in Part XIC of the CCA), the ACCC performs both the declaration and arbitration functions.(p297)</p>
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ARTC provides its views in relation to the scope and impact of economic regulation in rail and relevant stakeholder views in section 4 of this submission.

3.2 Rail industry structure

ARTC has noted the following questions raised in the Issues Paper that may be relevant to the impact of the structure of regulated industry sectors on competition and efficiency in that sector, including rail.

‘Are there unwarranted regulatory impediments to competition in any sector in Australia that should be removed or altered?’

‘Is there a need for further competition-related reform in infrastructure sectors with a history of heavy government involvement (such as the water, energy and transport sectors)?’

‘What are the competition policy reform priorities in sectors such as utilities, transport and telecommunications?’

‘Should the recommendations in the Productivity Commission’s report on the National Access Regime be adopted? Are there other changes that could be made to improve competition in the relevant markets?’

ARTC has also identified a number of views relevant to the impact of the structure of regulated industry sectors on competition and efficiency in that sector expressed by stakeholders as set out in Table 3 below.

Table 3: Relevant stakeholder views – Rail industry structure

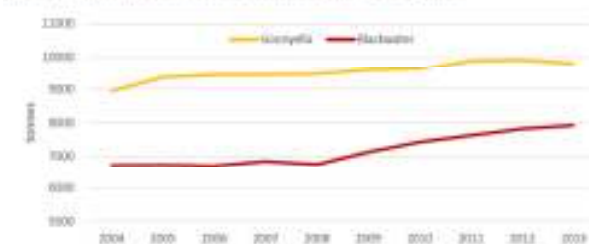
Aurizon (p10)	<p>Open access and separation has facilitated effective and sustainable competition in some rail freight markets. This is clearest in the coal supply-chains in Central Queensland and the Hunter Valley, where competition between rail operators is vigorous and entrenched.</p>
Aurizon (p11)	<p>However, in other markets, particularly non-coal general freight markets, open access has been less successful at promoting competition. In those markets, either no new entrants have appeared, or there are doubts about the sustainability of the limited competition which has emerged.</p> <p>Due to intense competition from road transport, contestable volumes on general rail freight networks are typically well below those needed to reach efficient scale. As a consequence, the scope for above-rail competition is very marginal.¹⁰</p> <p>General freight rail markets typically also rely on ongoing taxpayer support for the network infrastructure. Given budget constraints at all levels of Government, this must inevitably call into question the long-term economic sustainability of many of Australia’s rail networks.</p> <p>For example, in NSW, grain producers pay in access charges only 2% to 4% of the annual cost of maintaining the NSW grain network – i.e., more than 95% of the cost is paid directly by government.¹¹ The cost to NSW taxpayers of merely stabilising (but not improving) the NSW grain rail network is expected to be around \$1.5bn over the next ten years.¹² The interstate freight network that links Australia’s capital cities does not earn an economic return on capital¹³ – with the ARTC having impaired \$2.1bn worth of capital expenditure since 2005-06.</p>

⁹ ‘Productivity Commission 2013, National Access Regime, page 291’

¹⁰ ‘See, for example, Productivity Commission (2006) ‘Road and Rail Freight Infrastructure Pricing’, Canberra, p.314; and BITRE, Rail Infrastructure Pricing: Principles and Practice (2003). The OECD has described the scope for above-rail competition in rail markets as “modest”, see: OECD, Structural Reform in the Rail Industry, DAF/COMP(2005)46, p.47-48.’

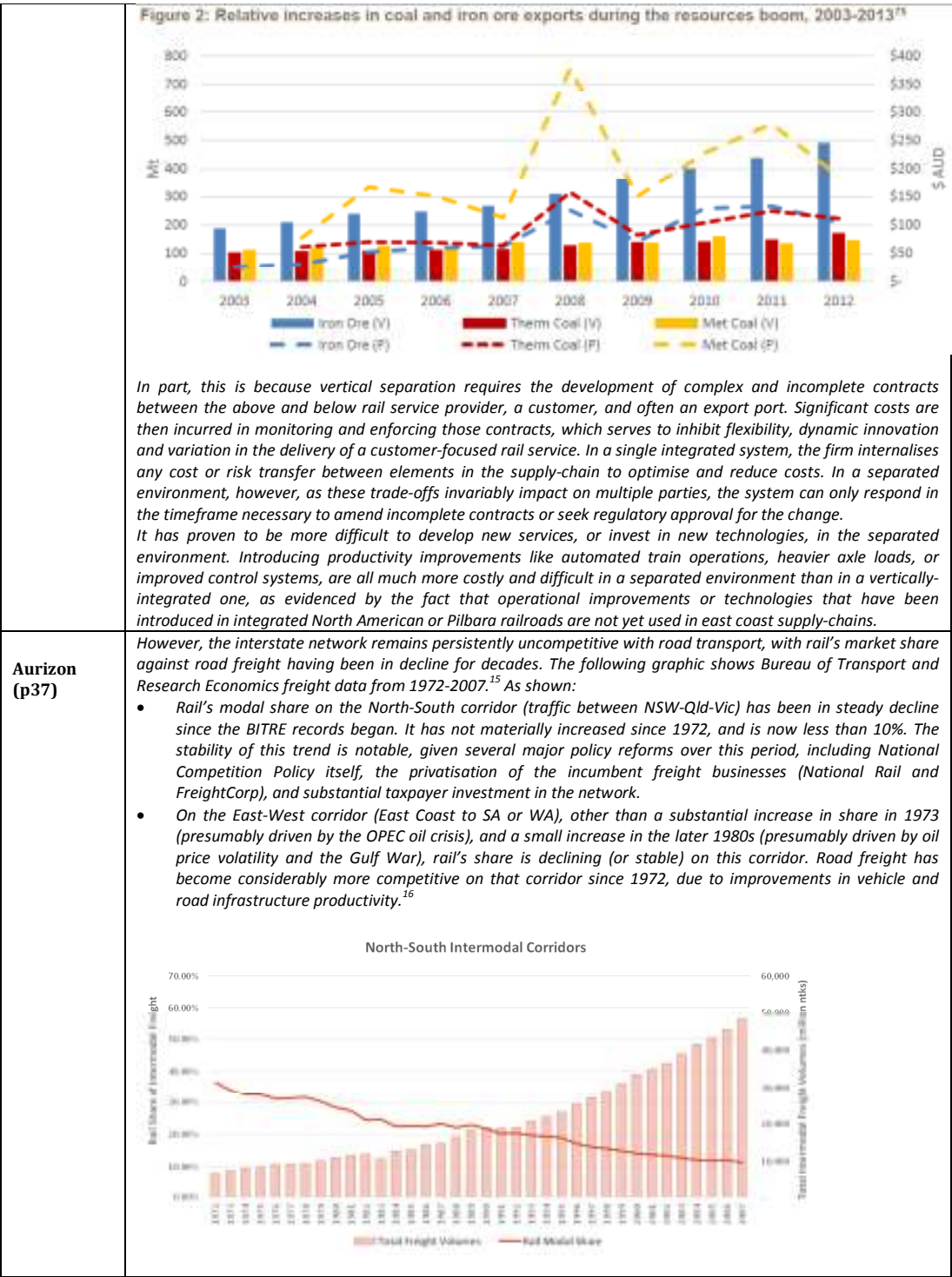
¹¹ ‘IPART, Review of Access pricing on the NSW grain line network, April 2012, p.6.’

¹² ‘IPART, Review of Access pricing on the NSW grain line network, April 2012, p.1.’

	<i>The limited impact of above-rail competition in general freight markets, combined with the cost to government of maintaining the infrastructure, has led to the Productivity Commission recommending that open access be reconsidered in these markets.</i>																					
Aurizon (p14)	<p><i>Is there a compelling need to refocus competition policy on a consumer welfare standard, rather than pre-ordained ‘competitive’ market structures? In many Australian markets, not only in infrastructure but also more broadly, there has been a noticeable trend for governments and regulators to ‘lock in’ a certain market structure. Whether through access regulation, government ownership or antitrust – the effect is the same, namely, that many Australian businesses have become boxed within a certain function or structure. While that structure may be initially welfare enhancing, over time structural rigidity comes at a cost to growth, innovation and investment. There is a need to move away from this brand of structuralism and back to an economic standard, refocusing competition policy on overall community welfare and living standards achieved through quality of service, investment, innovation and improved efficiency.</i></p> <p><i>It is submitted that in the rail sector, this would mean removing the governmental barriers to vertical integration in the non-coal markets where above-rail competition is either non-existent, where the benefits of competition do not offset the coordination costs, or where competition unsustainably relies on perpetual government subsidy. In those markets, the Hilmer Committee’s ‘presumption’ that structural separation in infrastructure markets would promote efficiency has proved inaccurate – instead, there are indications that these markets have been locked into a cycle of declining productivity, inadequate investment, commercially unrenewable assets, and indefinite taxpayer subsidy.</i></p>																					
Aurizon (p30-31)	<p><i>In other rail networks, particularly the coal export supply-chains, productivity and efficiency gains have been realised from downstream competition, but future gains may be less likely under the prevailing market structure to the extent it impedes vertical coordination between supply-chain elements (e.g., the network, haulage providers and the export ports). With this objective in mind, significant efforts have been expended in recent years to partially replicate (in the open access context) the coordination benefits achieved by integrated supply-chains, with various different models adopted (e.g., system rules to govern the day-to-day operation of supply-chains and prices that incentivise behaviour that promotes supply-chain efficiency.</i></p> <p>.....</p> <p><i>Competitive entry has occurred in both the NSW and Queensland coal markets through investment in new haulage equipment and has been well supported by complimentary investment in network infrastructure. New entrants have obtained sufficient scale to invest in long-dated assets, like depots and maintenance facilities, suggesting that the competition is both enduring and intense. Productivity improvements in the operation of these railroads, promoted by competition as well as privatisation, has promoted longer trains and increased axle loads – and, hence, greater export volumes, and more productive rail systems. This is evident in the following graph of payload per train service in the two most significant coal systems in Central Queensland.</i></p> <p><i>Figure 2: Payload per train path in Queensland’s major coal systems¹³</i></p>  <table><caption>Estimated data for Figure 2: Payload per train path in Queensland's major coal systems</caption><thead><tr><th>Year</th><th>Wivenhoe (tonnes)</th><th>Blackwater (tonnes)</th></tr></thead><tbody><tr><td>2004</td><td>9,000</td><td>7,000</td></tr><tr><td>2005</td><td>9,500</td><td>7,000</td></tr><tr><td>2006</td><td>9,800</td><td>7,000</td></tr><tr><td>2007</td><td>10,000</td><td>7,000</td></tr><tr><td>2008</td><td>10,200</td><td>7,500</td></tr><tr><td>2009</td><td>10,500</td><td>8,500</td></tr></tbody></table>	Year	Wivenhoe (tonnes)	Blackwater (tonnes)	2004	9,000	7,000	2005	9,500	7,000	2006	9,800	7,000	2007	10,000	7,000	2008	10,200	7,500	2009	10,500	8,500
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Aurizon (p35)	<p><i>As shown in the following graph, the integrated supply-chains of the iron ore exporters in the Pilbara were able to capitalise on global demand much more rapidly than the coal industry on the east coast. At least in part, noting the different demand drivers for each commodity, this can be attributed to the relative ease with which an integrated supply-chain can respond to commodity price signals relative to a multi-user, open access, supply-chain.¹⁴</i></p>																					


¹³ 'This has been broadly acknowledged by the ARTC. For example, in 2006, the ARTC told the Productivity Commission that, even on the section of its network where it achieves the highest level of economic cost recovery (Dry Creek to Parkeston, near Kalgoorlie), prices would need to double to achieve full economic cost recovery'; ARTC, Submission to the Productivity Commission Inquiry on Road and Rail Freight Pricing (May 2006).'

¹⁴ 'See for example, the discussion in Fisher, B.S. and Rose, R. (2006), 'Export infrastructure and access: key issues and progress', Australian Commodities 13(2), 97.'



¹⁵ BITRE, Interstate freight in Australia: Report 120, April 2010.

¹⁶ The BITRE notes that roads share in 1972 (7%) was due to very low productivity, e.g. the highway was not sealed at the time.

																																																																																																																																									
Aurizon (p39)	<p>The fundamental economic problem for the interstate rail network is a lack of scale, which manifests as an inability to compete effectively with road transport. The introduction of above-rail competition has done little to resolve this issue, and has arguably worsened it by introducing the coordination costs associated with vertical separation, undermining the scale efficiency of above-rail operators.</p>																																																																																																																																								
Aurizon (p40)	<p>..., it is not surprising that the interstate network does not generate economic returns, and requires ongoing public subsidy to ensure its long-term economic and financial viability. This is in keeping with most of the non-coal railroads that remain owned by Australian governments.</p> <p>Since its formation, the ARTC has received substantial assistance from the Commonwealth, with the ARTC being supported by direct government grants and new equity issues, totalling approximately \$4.1bn since its creation, as well as:¹⁷</p> <ul style="list-style-type: none">• an implicit sovereign guarantee (ARTC has a AA2 credit rating from Moody's);• uncommercial capital expenditure (the ARTC has impaired \$1.2bn of capital investment in the last three years alone); and• the Government tolerating low or negative returns for a plainly uncommercial period of time, with Australian taxpayers never having obtained the benefit of a commercial rate of return. <p>A full record of the public support received by the ARTC is shown in the table below.</p> <p>Table 4: Public financial support for the ARTC, 1999-2013 ('000)</p> <table><tr><th></th><th>Establishment Payments</th><th>Australia Infrastructure Fund</th><th>Special Gov Grant (incl Interest)</th><th>Equity Injection</th><th>Government Grants Other</th><th>Dividends</th><th>Net Flows</th></tr><tr><td>1999</td><td>\$37,879</td><td></td><td></td><td></td><td></td><td>-\$2,000</td><td>\$35,879</td></tr><tr><td>2000</td><td></td><td>\$37,330</td><td></td><td></td><td></td><td>-\$2,000</td><td>\$35,330</td></tr><tr><td>2001</td><td></td><td>\$12,000</td><td></td><td></td><td></td><td>-\$8,750</td><td>\$3,340</td></tr><tr><td>2002</td><td></td><td>\$14,100</td><td></td><td></td><td></td><td>-\$5,725</td><td>\$8,375</td></tr><tr><td>2003</td><td></td><td>\$4,800</td><td></td><td></td><td></td><td>-\$2,000</td><td>\$2,800</td></tr><tr><td>2004</td><td></td><td></td><td>\$450,000</td><td>\$143,375</td><td></td><td>-\$5,990</td><td>\$586,385</td></tr><tr><td>2005</td><td></td><td>-\$1,881</td><td>\$33,000</td><td></td><td>\$20,527</td><td></td><td>\$151,866</td></tr><tr><td>2006</td><td></td><td></td><td>\$13,103</td><td></td><td>\$12,001</td><td></td><td>\$325,104</td></tr><tr><td>2007</td><td></td><td></td><td>\$45,084</td><td></td><td>\$14,484</td><td></td><td>\$60,568</td></tr><tr><td>2008</td><td></td><td></td><td></td><td></td><td>\$39,148</td><td></td><td>\$39,148</td></tr><tr><td>2009</td><td></td><td></td><td></td><td>\$422,000</td><td>\$155,605</td><td></td><td>\$577,605</td></tr><tr><td>2010</td><td></td><td></td><td></td><td>\$786,900</td><td>\$133,404</td><td></td><td>\$900,304</td></tr><tr><td>2011</td><td></td><td></td><td></td><td>\$559,200</td><td>\$88,701</td><td></td><td>\$648,901</td></tr><tr><td>2012</td><td></td><td></td><td></td><td>\$409,300</td><td>\$52,651</td><td></td><td>\$461,951</td></tr><tr><td>2013</td><td></td><td></td><td></td><td>\$211,700</td><td>\$42,385</td><td></td><td>\$254,085</td></tr><tr><td>Total</td><td></td><td></td><td></td><td></td><td></td><td></td><td>\$4,089,421</td></tr></table>		Establishment Payments	Australia Infrastructure Fund	Special Gov Grant (incl Interest)	Equity Injection	Government Grants Other	Dividends	Net Flows	1999	\$37,879					-\$2,000	\$35,879	2000		\$37,330				-\$2,000	\$35,330	2001		\$12,000				-\$8,750	\$3,340	2002		\$14,100				-\$5,725	\$8,375	2003		\$4,800				-\$2,000	\$2,800	2004			\$450,000	\$143,375		-\$5,990	\$586,385	2005		-\$1,881	\$33,000		\$20,527		\$151,866	2006			\$13,103		\$12,001		\$325,104	2007			\$45,084		\$14,484		\$60,568	2008					\$39,148		\$39,148	2009				\$422,000	\$155,605		\$577,605	2010				\$786,900	\$133,404		\$900,304	2011				\$559,200	\$88,701		\$648,901	2012				\$409,300	\$52,651		\$461,951	2013				\$211,700	\$42,385		\$254,085	Total							\$4,089,421
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Aurizon (p42)	<p>Aurizon submits that this raises significant questions as to the economic viability of the network, given the unwillingness of commercial investors to renew assets that do not generate sufficient revenue to cover the economic cost of their own replacement. It also raises significant questions as to the current road freight pricing arrangements...</p> <p>The access revenue generated by the interstate network would appear to only marginally cover costs (maintenance, other operating costs and depreciation). This raises a major fiscal policy question for the Commonwealth Budget, as there is a question as to whether the ARTC will be able to maintain sufficient free cash flow to fund investment and renewal activity without significant ongoing support.</p>																																																																																																																																								
Aurizon (p43)	<p>Separating the interstate network from the end markets for which it provides an input can also distort investment priorities, particularly when coupled with government ownership. Overcoming this information asymmetry requires a much deeper involvement in network planning of those directly exposed to end markets, together with optimisation of both above and below rail costs, which runs counter to the separation model.</p> <p>The result of separating the network from the commercial drivers of above-rail operators can be unpredictable capital planning, as evident in the following graph. This figure shows the disparity in the quantum of investment made by ARTC on the interstate network since 2006-07 compared to its initial projections of required capex submitted to the ACCC in 2007. As can be seen, the ARTC forecast \$1.5bn in capital spend, yet spent \$3.5bn. It is unclear why the forecast was so manifestly short of actual expenditure – though it likely was, at least in part, driven by changing government expenditure decisions. Nevertheless, it highlights the unpredictability of capital flows that are subject to changing government priorities.</p>																																																																																																																																								

¹⁷ Includes interest earnings on cash balances and excludes Country Regional Network (NSW) revenues.

	<p>Figure 11: Investment in the Interstate Rail Freight Network - Expectations and Reality¹⁸</p>
Aurizon (p44)	<p>For example, the following figure reproduces ARTC's volume projections in its 2007 North-South Corridor Strategic Investment Outline, which were used to justify most of the capital expenditure recorded in the preceding figure. Overlaid with those forecasts are actual freight volumes on the corridor. The figure shows that, contrary to increasing corridor volumes, the ARTC's investment has not resulted in any improvement in volumes – in fact, volumes were, on average, lower than the ARTC expected them to be had no investment occurred at all.</p> <p>Figure 13: North South Corridor volumes – ARTC's Strategic Forecast v estimated volumes¹⁹</p>
Aurizon (p51)	<p>Open access and competition policy has also diminished the incentives for rail operators to invest in rollingstock and associated infrastructure in the grain sector. The threat of loss of market share and the inability of a number of market participants to enter into long term supply agreements is not conducive to investment in dedicated asset, where there are also significant barriers to exit.</p> <p>Moreover, the structural separation of above and below rail has substantially increased the coordination problems associated with optimising costs and improving productivity.</p>
Aurizon (p51)	<p>Aurizon therefore believes that there is a clear imperative to revisit the question of combining above-rail and below-rail operations on the interstate network, and perhaps on the grain railroads. Aurizon considers that the enforced separation of the two, while perhaps once justified, is now flawed and counterproductive, imposing considerably greater costs than it does benefits.</p>
Aurizon (p54)	<p>Despite the ubiquity of separation, there is no demonstrated economic case for separating and regulating most non-coal railroads.</p>
Aurizon (p55)	<p>The truth of this seems to be borne out by the very limited entry of new interstate operators since the creation of the ARTC. Of note, the only major entry that has occurred did so in response to regulatory intervention to create a new entrant.¹⁸ Other than that instance, the 'market' remains dominated by the incumbent operator, which, as noted, had a large fleet initially acquired on its behalf by government.</p>
Aurizon (p61)	<p>Aurizon therefore submits that the Harper Review should consider whether:</p> <ul style="list-style-type: none"> • There are compelling indications that Hilmer-era structural separation of Australian long-haul and agricultural railroads has locked the freight rail industry into a cycle of declining productivity, inadequate investment, commercially unrenovable assets, and indefinite taxpayer subsidy. • There should therefore be a fundamental re-assessment of structural separation in the long-haul and agricultural rail freight sectors, with the aim of boosting incentives to invest in upgrading existing infrastructure and rolling stock, and ensuring the industry is commercially sustainable and competitive with road freight for the long-term. • Structural reform of railways is best achieved through market forces; i.e., the optimal structure of Australian railways should be brought about through commercial negotiation and market drivers, rather than by government design. • There is a need to re-evaluate the competition policy restrictions on structural reform in railways, particularly: <ul style="list-style-type: none"> ○ the ongoing application of access regulation to long-haul and agricultural railroads; ○ the preference of competition regulators to define narrow, functional markets in the freight transport sector, which makes industry consolidation difficult, despite the demonstrable importance of scale in railways and the overwhelming competitive constraint posed by road

¹⁸ 'In 2007, SCT Logistics began operating train services in its own right (prior to this its trains were operated by incumbent operators), having acquired 12 locomotives from Pacific National. Pacific National had been required to divest the locomotives to comply with an undertaking given to the ACCC as part of the Toll/Patrick merger.'

	<p>competition; and,</p> <ul style="list-style-type: none"> the inflexibilities of government ownership limiting the scope for private-sector ownership, management or operation of rail networks.
Asciano (p7)	<p>During the Productivity Commission's review of the National Access Regime, Asciano made several submissions and attended a public hearing. In these submissions Asciano was advocating:</p> <ul style="list-style-type: none"> the continuation of an effective third party access regimes in Australia; strengthening access regimes by including provisions relating to information provision, vertical separation, ring fencing and anti-competitive discrimination; increasing powers for regulators to monitor, audit and enforce access provisions; and rationalising access regimes and in particular introducing consistency between state and Commonwealth access regimes.
Asciano (p19) (Queensland coal rail haulage)	<p>Aurizon are clearly positioning themselves to reduce the regulatory impact on their business and to exploit being a vertically integrated monopolist. The market positioning and approach of Aurizon, which is seeking to reduce regulatory impact and to exploit its vertically integrated monopoly position, makes having an effective non discriminatory regulatory regime significantly more important now than it has been in the past. Without appropriate regulation we have the potential to lose the economic benefits that competition in above rail haulage has produced. This benefit includes demonstrated improvements in price efficiency, system volume and service improvements.</p>
Asciano (p21)	<p>The ultimate way of preventing this discrimination from occurring is to not have vertically integrated monopolists. However, if that is not an option then in Asciano's opinion the regulatory regime should have as a minimum five key elements.</p> <ol style="list-style-type: none"> 1. Ring Fencing 2. Effective Non-Discrimination Provisions 3. Strong Regulator Enforcement Powers 4. Penalty Regime 5. Strong Compliance Program
Glencore (p2)	<p>Coal export infrastructure suffers from the economic problems caused by private ownership of "natural monopoly" infrastructure, particularly as previously State owned infrastructure moves into the private sector. The expected privatisation of further natural monopoly infrastructure will exacerbate these problems. Existing regulatory approaches have not been sufficient to prevent or resolve these problems.</p>
Glencore (p5)	<p>Glencore supports the user ownership model as it also addresses one key issue which arises from natural monopolies: the refusal of the owner to expand the capacity of the available infrastructure. User owners have an incentive to expand the infrastructure capacity which they own in order to service their own needs, and any problems in relation to the distribution of access to expansions between existing and new users are comparatively easy to address through the imposition of "common user" provisions which require all access seekers to be treated equally. The problem of discrimination between existing and new users is a much easier problem to address than the failure by a non-aligned infrastructure owner to invest in expanding the capacity of an infrastructure asset.</p>
Glencore (p6)	<p>While in principle we support privatisation, Glencore has experienced the consequences of privatisation across the East Coast of Australia in terms of infrastructure asset sales and the results are not mixed, they are almost always negative. In every instance of monopoly coal infrastructure being sold into private ownership in the last 15 years there has been an associated significant increase in the cost of access to use that infrastructure arising from both the imposition of higher access charges and/or the reallocation of risk back to the users of that infrastructure. These problems have arisen as a result of the failures of the regulatory regimes which have been imposed to fully deal with the problems which arise from natural monopoly infrastructure. The problems have arisen much more in Queensland than in New South Wales, since the rail track and port infrastructure in New South Wales currently remains user or Government owned. However, the privatisation of ARTC is likely to create similar challenges in New South Wales to those which have already faced Queensland.</p>

ARTC has identified a number of views expressed by the Review Panel in the Draft Report relevant to rail industry structure as set out in Table 4 below.

Table 4: Draft Report views – Rail Industry Structure

Structural Separation	<p>Structural separation was extensively pursued in rail. The main interstate freight network was brought together under the ownership of the Australian Rail Track Corporation, while above-rail freight operations have been privatised. Jurisdictions have access regimes in place for regional freight lines. While competition in above-rail services has emerged on some routes, on many others volumes have been too low to support competitive entry. Much of the rail freight sector faces strong competition from road transport. The major ports have also been reformed with port authorities now typically acting as landlords for competing service providers rather than directly providing services.(p118)</p>
Privatisation	<p>In rail, above-rail freight operations have been privatised as have many regional freight lines. However, the Australian Rail Track Corporation still remains a Commonwealth-owned corporation.</p>
Rail Reform	<p>In the rail sector, the NCP reforms focused on the structural separation of the interstate track network from above-rail operations, with the formation of the Australian Rail Track Corporation, along with the development of access regimes and regulatory bodies. Networks have been declared under the National Access Regime or equivalent State-based regimes. Open access was also applied sporadically to related rail assets such as bulk handling assets, intermodal terminals, coal ports and grain export facilities. At a national level, the objectives set by the original NCP have been largely met. The application of price controls and the oversight of regulators appear to have addressed concerns about possible monopoly pricing.</p>

	<p><i>Regulatory regimes have generally promoted competition and entry has occurred in some access-dependent markets.</i></p> <p><i>With the removal of regulation reserving certain freight tasks for rail under NCP, rail freight on the majority of routes now has to compete with road transport. Aurizon notes:</i></p> <p><i>The fundamental economic problem for the interstate rail network is a lack of scale, which manifests as an inability to compete effectively with road transport.</i></p> <p><i>While rail track may be considered a natural monopoly, intermodal competition can act as an effective constraint. This has reduced the need for heavy-handed regulation in the rail sector.</i></p> <p><i>Issues raised in submissions include the complexity of access issues, with some above-track operators having to contend with multiple access regimes to provide a single rail service, and that structural separation has been imposed in areas where above-rail competition has not and is unlikely to emerge.</i></p> <p><i>The Panel's view Rail reform has been relatively successful and proceeded at a reasonable pace. Many rail freight tasks face significant competition from road freight, which has made efficiency-enhancing reforms relatively palatable. Regulators and policymakers should be pragmatic about structural separation of railways, recognising that on some low-volume rail routes vertical integration may be preferable.(p133)</i></p>
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ARTC provides its views in relation to rail industry structure and relevant stakeholder views in section 4 of this submission.

3.3 Regulation of greenfields rail projects

ARTC has noted the following questions raised in the Issues Paper that may be relevant to the regulation of greenfields projects, including rail.

'Are there unwarranted regulatory impediments to competition in any sector in Australia that should be removed or altered?'

'Should the recommendations in the Productivity Commission's report on the National Access Regime be adopted? Are there other changes that could be made to improve competition in the relevant markets?'

ARTC has also identified a number of views relevant to the regulation of greenfields rail projects expressed by stakeholders as set out in Table 5 below.

Table 5: Relevant stakeholder views – Regulation of greenfields rail projects

Aurizon (p62)	<i>Continuing to expose greenfield projects to the risk of declaration after capital is sunk is an unnecessary risk to new investment. Instead, Aurizon believes that an effective, modern infrastructure policy would allow governments to conclusively determine what, if any, third party access arrangements should apply to greenfield projects before capital is sunk and, thus, reduce the cost of capital for new projects..</i>
Aurizon (p66)	<i>The potential for regulation to truncate investors' returns once capital is sunk, or to otherwise impact on the operation or management of an infrastructure asset such as to reduce the attractiveness of the investment, is well recognised and understood. Professor Allan Fels has recently described this as the "the long-term insidious effect of regulatory error on investment incentives".¹⁹</i> <i>To the extent that the risk discourages investment in otherwise economically efficient greenfield infrastructure, it is a cost to the economy and, thus, to the Australian community.</i>
Aurizon (p69)	<i>Underlying Aurizon's view that it is not necessary for declaration to apply to greenfield infrastructure, is the simple point that an effective, modern access policy would require definitive and irreversible regulatory arrangements (if any) to be put in place before capital is sunk. This will allow investors to make informed and certain investment decisions in relation to greenfield projects.</i>
Aurizon (p70)	<i>There are no effective mechanisms presently in the national competition policy framework that allow governments to determine and set access arrangements as part of project approval.</i> <i>Part IIIA²⁰ 168 currently contains two options for infrastructure providers and governments seeking to put a multi-user or access framework in place ahead of a greenfield project:</i> <ul style="list-style-type: none"> <i>• first, ineligibility rulings, also known as 'access holidays'; in effect a period of time in which an asset will be ineligible for regulation; and,</i>

¹⁹ 'Fels, A. 'The Merits Review Provisions in the Australian Energy Laws', Submission to the Review of the Limited Merits Review Regime, (2012).'¹

²⁰ 'Other legislation contains other mechanisms, which are not discussed at length here. Most such legislation has not been heavily used, if at all. For example, the Queensland Competition Authority Act 1997 provides a mechanism to obtain "rulings" prior to an applicant building a new greenfield project, but these have not been used (largely because of the difficulties associated with specifying the circumstances on which they become invalid). The National Gas Law contains mechanisms for international pipelines that regulate access, but prevent the regulator from imposing pricing regulation.'

	<ul style="list-style-type: none"> second, a government requiring a project proponent to lodge of a voluntary undertaking with the ACCC or a state competition regulator as a condition of project approval. <p><i>Neither option is particularly well suited to the task of promoting infrastructure development.</i></p>
Aurizon (p72)	<p><i>Aurizon submits that a new competition policy framework for greenfield infrastructure be developed. This framework would have two objects – first, to remove the risk of declaration after an asset is built, but secondly, to improve the ability of governments and businesses to put appropriate regulatory frameworks in place before it is built.</i></p>

Apart from broader reflections around the need for competition policy to promoter efficient investment in infrastructure and encourage innovation, ARTC was unable to identify specific views expressed by the Review Panel in relation to the regulation of greenfields projects other than the approaches under Part IIIA to obtain exemption from declaration as set out in Table 6 below.

Table 6: Draft Report views – Regulation of greenfields rail projects

Exemption from declaration under Part IIIA	<p><i>There are four regulatory processes by which an infrastructure service may be exempted from declaration under Part IIIA.</i></p> <ul style="list-style-type: none"> <i>Prior to the construction of a new facility, the operator of the proposed facility may apply to the NCC for a recommendation to the relevant Minister that the facility be ineligible for declaration. The facility will become ineligible if the Minister makes that decision. The Minister may only make that decision if the Minister is satisfied that one of the declaration criteria will not be fulfilled.</i> <i>A State or Territory may²¹ apply to the NCC for a recommendation to the relevant Commonwealth Minister that an access regime for a particular infrastructure service in that State or Territory is 'effective'. The infrastructure service will be exempted from declaration if the Commonwealth Minister makes that decision. The criteria to be applied for that decision are set out in the Competition Principles Agreement.²²</i> <i>The Commonwealth or a State or Territory may apply to the ACCC for approval of a competitive tender process for the construction and operation of an infrastructure facility that is to be publicly owned. The facility will be exempted from declaration if the ACCC makes that decision. The ACCC may only approve the tender process if it is satisfied that reasonable terms and conditions of access to the facility will be the result of the tender process.</i> <i>Operators of monopoly infrastructure may offer an undertaking to the ACCC setting out the terms and conditions on which the operator will offer services using the infrastructure. The ACCC is empowered to accept or reject the undertaking. If the undertaking is accepted, the service cannot be declared.</i>
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ARTC provides its views in relation to the regulation of greenfields rail projects and relevant stakeholder views in section 6 of this submission.

3.4 Delivering road/rail competitive neutrality

ARTC has noted the following questions raised in the Issues Paper that may be relevant to delivering road/rail competitive neutrality.

'Are there unwarranted regulatory impediments to competition in any sector in Australia that should be removed or altered?'

'Is there a need for further competition-related reform in infrastructure sectors with a history of heavy government involvement (such as the water, energy and transport sectors)?'

'What are the competition policy reform priorities in sectors such as utilities, transport and telecommunications?'

ARTC has also identified a number of views relevant to the delivery of road/rail competitive neutrality expressed by stakeholders as set out in Table 7 below.

²¹ 'In the 2006 Competition and Infrastructure Reform Agreement, States and Territories agreed to submit their access regimes for certification (page 41).'

²² 'Council of Australian Governments 1995 (as amended to 13 April 2007) Competition Principles Agreement, pages 6-9.'

Table 7: Relevant stakeholder views – Delivering road/rail competitive neutrality

Aurizon (p75)	<i>Aurizon raises the objectives of the National Land Freight Strategy to deliver a streamlined, integrated and multi-modal” land transport and logistics system and improve the efficiency of freight movements across infrastructure networks, minimise the negative impacts associated with such freight movements and influence policy making relevant to the movement of freight” as context for competitive neutrality in the land transport framework. Aurizon goes on to state support of the objective and the outcomes identified by the National Land Freight Strategy and order to maximise the productivity gains available from land freight transport, the outcomes identified above should be delivered in the short to medium term ARTC are in agreement with Aurizon that action must be taken in the short to medium term</i>
Aurizon (p75)	<i>Aurizon argues that inconsistent regulation between road and rail freight in charging, regulation of intermodal terminals, and safety and administrative regulation, is based on the outdated approach of treating each as a separate industry and separate market, and is a key barrier to competitive neutrality and to an integrated freight market across road and rail. ARTC support Aurizon’s argument on this issue.</i>
Aurizon (p78)	<i>The inconsistency between access fees paid by rail freight operators and fuel excise and registration charges paid by road operators has: (a) contributed to the large modal shift from rail to road on long-haul freight routes demonstrated in Figure 21 on page 78; (b) resulted in an inefficient use of infrastructure by heavy vehicles; (c) distorted the demand for competing rail freight operations, and therefore impedes the potential for productivity gains to be made from improvements to the utilisation of and investment in land transport infrastructure. ARTC are in agreement with Aurizon on these statements.</i>
Aurizon (p79 – 83)	<i>Aurizon’s key suggestions: (a) introduction of direct MDL charging to replace the use of fuel excise and registration charges for heavy vehicle access and use of road infrastructure on the major freight corridors; (b) better coordination between governments and industry in identifying locations for centralised larger scale terminals; assessments of whether major infrastructure road or rail projects should link to intermodal terminals; competitive market-based approaches to the development and provision of freight services provided by intermodal terminals; transparent regulatory approach recognising the imperative of private sector infrastructure owners and providers to earn a commercial rate of return. (c) equivalent safety and other social and administrative regulations be applied to both road and rail freight operators, particularly long-haul; where regulations are proposed for only one mode of transport, governments should be required to undertake a cost-benefit analysis to determine whether there is a transparent case for imposing different regulations and industry should be able to comment. ARTC are supportive of Aurizon’s suggestions</i>

ARTC has identified a number of views expressed by the Review Panel in the Draft Report relevant to delivering road/rail competitive neutrality as set out in Table 8 below.

Table 8: Draft Report views – Delivering road/rail competitive neutrality

Pricing Reform and Access	<i>Pricing reform and the move to cost-reflective pricing has been pursued extensively in most infrastructure markets and has been a key driver of efficiency and allowing markets to offer more consumer choice; for example, through facilitating retail price competition. Benefits from pricing reform in infrastructure sectors arise through driving better use of existing infrastructure, which can delay the need for infrastructure investment. Where cost-reflective pricing is present, consumer demand will also provide a more accurate guide to infrastructure investment. This increases the likelihood that such investment is efficient and responds to actual changes in demand and consumer preferences. These factors lower the cost and increase the responsiveness across markets to the benefit of consumers. It also means governments can better target assistance to vulnerable consumers in those markets, reducing the burden on taxpayers. Pricing reform has generally been pursued through deregulating prices where markets are sufficiently competitive, while subjecting the monopoly parts of markets to prices oversight, direct price regulation and access regimes. In contrast, in water and in roads there has been little progress introducing pricing that reflects the actual cost of use on the network, such as time and location charging. Investment in those sectors is either funded directly from budgets or by users across the network, rather than from users according to the costs they impose on the network. Roads in particular have also been subject to investment bottlenecks.(p120)</i>
Road Pricing Reform	<i>The pace of road reform in Australia has been slow compared to other transport and utilities reforms. This is partly due to roads and road transport being traditionally administered through government departments, while airlines, airports, and rail have been operated by public companies. Roads have also been seen as public goods, administered by a large number of authorities at the local, state and territory and Commonwealth level, and it has not been widely accepted that a public utility style organisation could charge for them. As a consequence, Commonwealth, state and territory governments have shown reluctance to explore more cost-reflective pricing arrangements for roads while continuing to raise general revenue from motorists through fuel excise, registration fees and other taxes such as stamp duties.(p134)</i>

	<p><i>While there has been a move towards tolling for new roads over the past two decades, there has not been any attempt to account for the capital costs of the road network as a whole. This has led to the situation where some routes are subject a form of road pricing while others are not, creating distortions and inequities among road users.</i></p> <p><i>Heavy vehicles, being a significant contributor to road damage over time, have been the main focus of road-charging reforms. The current heavy vehicle charging regimes use a combination of registration fees and fuel-based charges to recover cost on average and do not reflect the actual cost to the road network of an individual vehicle. Moreover, taxes and charges on road users in general are not directly linked to the provision of roads.(p134)</i></p> <p><i>Importantly, greater use of cost-reflective pricing linked to road provision holds the prospect of both more efficient use of road infrastructure as well as more efficient investment based on clearly identified demands. Considerable work has been undertaken by the Heavy Vehicle and Investment Reform project to progress both user charging and institutional reform. The challenge is now to agree on a model of implementation. Given the size and importance of the road transport industry for the economy and the importance of efficient road use and provision for urban and regional amenity and consumer wellbeing, much greater progress in this area needs to be made.(p135)</i></p> <p><i>Reform of road pricing and provision should be a priority. Road reform is the least advanced of all transport modes and holds the greatest prospect for efficiency improvements, which are important for Australian productivity and amenity.</i></p> <p><i>Technologies are available that allow for more widespread application of cost-reflective pricing in roads, taking into account location, time and congestion. Revenue raised through road pricing should be channelled into road funds to promote more efficient road use and investment.</i></p> <p><i>Cooperation from all levels of government will be needed to ensure that road pricing does not result in an additional impost on road users.(p136)</i></p>
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ARTC provides its views in relation to delivering road/rail competitive neutrality and relevant stakeholder views in section 6 of this submission.

4 THE SCOPE AND IMPACT OF ECONOMIC REGULATION IN RAIL

4.1 Application of Economic Regulation in Rail

The rail network in Australia is highly segregated and operates with parts operating under a range of different industry structures and ownership arrangements. These also operate in a range of different freight and passenger markets and supply chains and are subject to varying degrees of competition from other transport modes and both national and international supply chains.

Each rail network is subject economic regulation to varying extents and under different instruments. This is not surprising given the diversity of markets and industry structures involved. The range of applications is set out in the table at Appendix A to this submission which has been excerpted from the submission provided by Aurizon²³ to avoid repetition.

A number of different access regimes are applied on these networks under either Commonwealth legislation or legislation developed by each State in Australia, and is administered by either the ACCC or by state based regulators in each state. Access regimes are either incorporated directly within the applicable legislative instrument or capture by way of a voluntary access undertaking made by the owner/manager of the network to the relevant regulator.

4.2 Application of Economic Regulation on the ARTC Network

ARTC is a vertically separated provider of access to the ARTC rail network.

In broad terms, the ARTC network consists of the interstate network between Kalgoorlie in the west and Brisbane in the north, the Hunter Valley coal network, and some regional rail networks in NSW and Victoria. The ARTC owned or leased network is shown at Figure 1 below.

²³ Aurizon Holdings Limited, Submission to the Competition Policy Review, Promoting efficiency, productivity and new investment in the Australian rail freight and export infrastructure sectors, June 2014, p16.

Figure 1: ARTC rail network



Almost the entire ARTC is subject to access regulation under voluntary access undertakings approved by the ACCC. As indicated in section 2 of this submission, separate ARTC access undertakings apply to the interstate rail network and the Hunter Valley coal network. This primarily reflects the significant differences in markets predominantly served by the networks, the extent and nature of competition within these markets and the different commercial and operational arrangements that exist on these networks.

A summary of the different regulatory arrangements on these networks is provided at sections 4.2.1 and 4.2.2 below.

4.2.1 ARTC's Interstate Network Access Undertaking (IAU)

4.2.1.1 History of the IAU

The interstate rail network provides access to rail operators serving a number of key national and regional freight markets including:

- interstate intermodal freight (containerised);
- interstate and intrastate general freight such as steel, manufacturing products, minerals; and
- intrastate agricultural freight such as grain.

Interstate, regional and commuter passenger services are also operated on the interstate rail network.

The predominant market served by the interstate rail network is the intermodal freight market, which faces substantial competition from other transport modes,

mainly road transport. ARTC will further discuss competitive aspects of this market in section 7 of this submission.

In other markets, whilst competition from other transport modes and supply chains is also present, it is likely to be less intense.

ARTC submitted a voluntary access undertaking in accordance with Part IIIA of the Trade Practices Act (1974) (**TPA**) to the ACCC on 15 July 2008, which was accepted on 30 July 2008. This followed expiry of the previous ARTC 2002 Access Undertaking on 31 May 2007. The IAU applies to the interstate network controlled by ARTC, and sets out the framework under which access to that network can be negotiated with ARTC in a fair and balanced way.

ARTC sought, in its development of the IAU, to:

1. - Build upon the provisions of the 2002 ARTC Access Undertaking applicable to ARTC's network at the time, which covered a substantial portion of the East-West rail network.

ARTC considered that the 2002 ARTC Access Undertaking was largely a formalised recognition of the approach to access, pricing and operations that had been applied by ARTC for several years prior to 2002, and had been applied since. ARTC saw no compelling reason to substantially adjust the 'formula' for access to the network to that created by the 2002 ARTC Access Undertaking. ARTC sought to extend this approach to the North-South interstate network, in order to achieve greater consistency over the bulk of the national interstate rail network.

2. - Continue to adopt a level of regulatory 'intensity' or 'heavy handedness' that is appropriate in the circumstance of vertically separated network where market power is not substantial.
3. - Recognise specific obligations for ARTC arising from its lease in NSW.
4. - Recognise changes in the commercial, competitive and operating characteristics of the markets serviced by the interstate rail network over the previous six years.

In order to achieve a key objective of increasing utilization of the interstate rail network, ARTC has adopted a strategy of growing the use of rail for the movement of interstate freight in Australia by improving rail's competitiveness within the broader freight transport logistics framework. Rail's competitiveness is also a function of the activity of rail transport operators (ARTC's customers) and the extent to which rail is able to effectively integrate and communicate with other elements of the transport and distribution supply chain within various interstate and international transport markets.

ARTC's strategy of growing freight volume on rail also underpins ARTC's approach to pricing as described in the IAU. ARTC has sought to set access pricing at a level that will assist rail to be competitive with road in markets served by the interstate network. With the current level of utilisation of ARTC's network, however, pricing at this level results in the amount of revenue collected by ARTC not being sufficient for the long-term economic sustainability of its network. It is ARTC's strategy to

grow volumes in the long term, such that rail can be competitive and achieve long-term sustainability of its asset.

The IAU adopts a hybrid rail access model that incorporates certain aspects of both the traditional ex ante and ex post models for determination of access terms and conditions.

The ex-ante model contemplates the up-front determination of generic terms and conditions, whilst the ex post model contemplates determination of access terms and conditions in the context of an access dispute on an ex post basis (a negotiate/arbitrate model). The IAU seeks to provide certainty to users and access seekers by providing for indicative terms and conditions, including pricing and pricing variation, that cover the predominant service on the interstate network, which can also act as a starting point for negotiation for non-standard services, that is underpinned by a dispute resolution process. ARTC committed that the same pricing would be available to any train operator, regardless of ownership, operating under the substantially the same terms and conditions, and in the same end market as another train operator. To provide further certainty, the IAU also provides up-front for publishing of all pricing and other information.

ARTC sees these principles as providing confidence and encouragement to potential access seekers that they will be able to use the network on an even playing field with other access users and seekers.

4.2.1.2 Broad elements of the IAU

Broad elements and treatments in the IAU include:

1. - The IAU codifies underlying principles:

- a. - The majority of ARTC revenue is earned through the transport of interstate freight, in markets which are subject to a substantial degree of competition from other modes of transport.
- b. - ARTC is not vertically integrated. The vast majority of its revenue is derived through providing access to its network for operations by other parties.
- c. - Charges set by ARTC in the marketplace result in revenues that fall significantly below a level that would allow for the business to earn an adequate long-term economic rate of return. To mitigate this, ARTC seeks to grow volumes on the network.
- d. - ARTC has adopted the concepts of equity and transparency as key elements of its pricing policy, in order to stimulate market confidence and growth in the rail industry.

2. - Scope and Administration

- a. - Applies only to those parts of the interstate network owned or leased by ARTC, including the following parts:
 - i. - Kalgoorlie – Adelaide – Melbourne (east-west network)

- ii. - Crystal Brook – Broken Hill – Parkes – Cootamundra (east-west network)
- iii. - Port Augusta – Whyalla (east-west network)
- iv. - Melbourne – Albury – Sefton Park Junction (Sydney) (north-south network) including the SSFL completed and commissioned for operations in early 2013.
- v. - Moss Vale – Port Kembla (north – south network)
- vi. - Newcastle (mains) – Telarah – NSW/Queensland Border (north south network)

ARTC intends to extend coverage of the IAU to its leased network between the NSW Queensland Border and Acacia Ridge (Brisbane) and the metropolitan freight network in Sydney in the near future.

- b. - The IAU has a term of 10 years, and ARTC has completed a review of its operation, in consultation with customers, after 5 years (2013).
- c. - The IAU does not affect existing access contracts.
- d. - ARTC will publish comprehensive information on its website to assist access seekers in the access negotiation process. This includes:
 - i. - Network description
 - ii. - Prices
 - iii. - Terms and Conditions
 - iv. - Network Management Principles
 - v. - Capacity and Usage
 - vi. - Performance Indicators

3. - Negotiation and Dispute Resolution

- a. - Both parties to negotiate in good faith.
- b. - Framework includes preliminary meetings & information exchange, access application, indicative access proposal, negotiation to develop and agreement for execution, and dispute resolution procedures.
- c. - Timeframes apply to all steps in the process.
- d. - Confidentiality provisions apply.
- e. - Either party may seek dispute resolution at any time during negotiation.
- f. - The dispute resolution process:
 - i. - follows a negotiate/mediate/arbitrate model

- ii. - provides for the ACCC to act as arbitrator
- iii. has time constraints on all steps
- iv. - allows for the publishing of arbitration outcomes
- v. - requires the arbitrator to consider matters consistent with Part IIIA and the Competition Principles Agreement.

4. - Pricing Principles

- a. - ARTC pricing must be such that revenue collected on any segment from all users falls between floor and ceiling revenue limits.
- b. - The floor revenue limit is the incremental cost of a segment, being the costs which would have been avoided if the segment were (theoretically) removed.
- c. - Incremental cost includes segment specific costs and an allocation of non-segment specific costs but excludes depreciation and a return on assets.
- d. - The ceiling revenue limit is the economic cost of a segment, which includes all segment specific costs, an allocation of non-segment specific costs, depreciation of relevant assets and a return on relevant assets.
- e. - The rate of return is ARTC Weighted Average Cost of Capital (**WACC**) as approved by the ACCC. In its final decision, the ACCC approved a WACC (vanilla) of 11.76%.
- f. - Assets are valued using the Depreciated Optimised Replacement Cost (DORC) methodology. Valuations are annually adjusted for CPI, capital expenditure and relevant depreciation.
- g. - Charges comprise a variable component (\$/gtkm) and a flagfall component (\$/km).
- h. - Indicative access charges are available for any seeker wishing to operate indicative services (110kph, 21T axle/load, 1500m length east of Adelaide, 1800m west of Adelaide) under the indicative terms and conditions.
- i. - Indicative access charges for the indicative service may be varied annually. Cumulative variations may be less than, and at no time will exceed CPI applied cumulatively from the start of two separate 5 year periods covering the term.
- j. - Pricing for other than indicative services will be based on:
 - i. - indicative access charges;
 - ii. - service characteristics;
 - iii. commercial impacts on ARTC;

iv. - logistical impacts on ARTC; and

v. - cost of any additional capacity required.

k. - Pricing will not be differentiated based on the identity of the applicant, nor where the service characteristics are alike and the services are operating in the same end market.

5. - Capacity Management

a. - ARTC will undertake capacity analysis in preparing an indicative access proposal.

b. - Where two or more applicants seek mutually exclusive capacity, ARTC will seek to satisfy both requirements. If this is not achievable, access will be given to the applicant agreeing to terms and conditions most favourable to ARTC (normally an NPV test).

c. - ARTC has the right to reclaim under-utilised capacity.

d. - Capacity may be assigned by one user to another with ARTC's approval.

6. - Network Connections and Additional Capacity

a. - ARTC will consent to connection to the network provided certain conditions are met (approvals, standards, will not reduce capacity, costs met by proponent).

b. - ARTC will consent to a request for additional capacity from applicant(s) if it is safe, meets standards, is commercially viable to ARTC or the costs are met by the applicant(s).

c. - ARTC's costs could be met by reimbursement as incurred, or through increased charges.

d. - ARTC may apply to the ACCC to approve additional capacity considered worthwhile and beneficial to the industry.

e. - ARTC will provide an opportunity to exchange views on additional capacity with customers.

f. - An investment program covering through to 2011-12, and estimated at around \$2.3bn is incorporated in the IAU.

7. - Network Transit Management

a. - Objective is to exit trains from the network according to their contracted exit time.

b. - Where conflicts arise, trains will be managed according to defined and open Network Management Principles.

c. - Focus is to give priority to the service running on time, where the operator has not caused any delay to the train.

8. - Performance Indicators

- a. - To be published quarterly (or annually where appropriate)
- b. - To relate to service reliability, network availability, transit time, track condition and ARTC unit costs
- c. - To relate to both ARTC and operator performance
- d. - Reporting will be periodically and independently audited.

9. - Indicative Access Agreement

- a. - Forms part of the IAU
- b. - Offered to an applicant seeking to operate services meeting certain prudential criteria and where there is sufficient existing capacity or ARTC has agreed to provide additional capacity. Indicative access charges will apply.
- c. - Otherwise, acts as baseline terms and conditions available to an access seeker and enforceable upon ARTC
- d. - The access seeker and ARTC may agree alternative terms and conditions, but the IAU prescribes those elements which are essential in any access agreement, unless ARTC agrees otherwise.

As a result of the six years of operation under the above principles, ARTC saw no reason to deviate substantially from the model adopted in the 2002 Access Undertaking, nor many of the processes and treatments provided for. ARTC, wherever possible, adopted substantially the same approach in the development of IAU, but recognised that a number of specific requirements (needing alternative or additional treatments in an undertaking) exist to satisfactorily address the market and legislative circumstances on the expanded ARTC network to which the IAU applies.

Due to the strong intermodal competition (primarily road transport) faced by rail in many markets on the interstate network, ARTC does not have substantial market power in these markets, particularly in relation to pricing of its services. ARTC is also vertically separated. As a result, the nature of regulation afforded by the IAU is relatively light handed compared to that which might apply on other networks, particularly those serving bulk commodity markets, and where the access provider is vertically integrated.

4.2.2 ARTC's Hunter Valley Coal Network Access Undertaking (HVAU)

ARTC supports the application of consistent regulatory principles on its network.

ARTC believed that there were many elements of the IAU that could be successfully applied to the Hunter Valley rail network, and sought, where appropriate, to incorporate these in the HVAU. Having said this, ARTC also recognised that there were also elements that were not appropriately applied to coal operations on the Hunter Valley network, and that there were additional elements that may be

needed to address the different commercial and operational characteristics of that network.

It should also be noted that the previous regulatory arrangements applicable to the Hunter Valley coal network were governed by a state based regime, the NSW Rail Access Undertaking (**NSWRAU**), administered by the Independent Pricing and regulatory Tribunal (**IPART**) in NSW.

The NSW Rail Access Undertaking provided for a relatively light handed, less-prescriptive form of regulation (compared to the HVAU) focussing primarily on constraining monopoly pricing where the access provider is vertically separated.

The NSWRAU is not certified as an effective access regime under Part IIIA of the Competition & Consumer Act 2010 (Cth) (**CCA**).

It is generally recognised that whilst the NSWRAU applies to the NSW rail network in its entirety (other than that covered by the IAU), its application in terms of most compliance obligations and constraint on access pricing primarily focuses around the Hunter Valley coal network.

At the time, access revenue related to the carriage of a substantial part of the export coal volume was constrained to the full economic cost of the rail network utilised for that task. Despite being relatively light handed, regulatory application, in practice, with respect to the Hunter Valley coal network is far greater than that applying on the interstate rail network.

It should be noted that the Hunter Valley coal network, whilst predominantly serving the export and domestic coal markets, is also used by a number of other services operating in the general freight, agricultural products and passenger transport markets. These services consume capacity on the Hunter Valley coal network, usually in the form of scheduled train paths. The remaining rail capacity, other than that required for network maintenance purposes is available for the transport of export and domestic coal.

Key features of the NSWRAU are described in Appendix 2 to this submission.

At the time of the development and regulatory assessment of the HVAU (2008-2011) there were also significant and well documented developments occurring with respect to the Hunter Valley coal supply chain. Both the coal industry and the ACCC considered that many of these developments were particularly relevant to the HVAU development. These developments included:

- **Capacity Investment in the Hunter Valley coal network** – ARTC recognised the importance to the Hunter Valley coal industry that sufficient system capacity is in place in a timely manner to enable forecasted demand for Hunter Valley coal to be met. This created further risk to investors in coal infrastructure which must be recognised, and compensated or mitigated in order for investment in infrastructure capacity to be encouraged. Existing arrangements for investment in below rail infrastructure underpinned by the NSWRAU, whilst well intentioned, were not sufficient to encourage appropriate investment.

- **Hunter Valley Coal Chain** – ARTC recognised the benefit to the efficient operation and competitiveness of the Hunter Valley coal network, of coordination between participants in the Hunter Valley coal supply chain. ARTC supported the existing framework for voluntary and cooperative participation in the coordination of logistics and network planning in the Hunter Valley. A broader review of the operation of the Hunter Valley coal chain to address a perceived lack of coordination between investments and operations in various parts of the coal chain which manifested in inefficient outcomes and additional costs to the industry was carried out by the NSW Government (**the Greiner Review**). Key outcomes of the Greiner Review were
 - a commitment by all service providers to develop contractual arrangements with producers that were aligned across the coal chain so that:
 - capacity contracted by individual service providers did not exceed the overall capacity deliverable by the coal chain itself; and,
 - expansion of service provider capacity was aligned and optimised across the coal chain; and
 - the establishment of the Hunter Valley Coal Chain Coordinator (**HVCCC**), and industry body tasked with operational planning and investment of the Hunter Valley coal chain itself, in consultation with service providers.
- **Commercial Arrangements in the Hunter Valley** – ARTC recognised that coal producers were seeking greater certainty of access to sufficient capacity to meet demand for coal, and wished to directly contract for access rights to enable a stronger commitment towards the delivery of that capacity. ARTC also recognised that coal producers needed sufficient flexibility in capacity utilisation to manage fluctuations in demand including such things as shipping arrivals and mine breakdowns. There was however a trade-off between certainty and flexibility. It should be noted that providing a high degree of flexibility and certainty of capacity often translates to a need for higher rail and system capacity and investment. ARTC sought to recognise this in its development of the HVAU.
- **Gunnedah Basin Development** – ARTC recognised at the time that due to strong international demand for Hunter Valley coal, the Gunnedah Basin, a coal producing region north of the Hunter Valley coal network that was recognised under the NSWRAU was commencing a significant expansion phase requiring coal chain and network capacity investment in the early years of the HVAU. As is often the case, such investments are needed ahead of demand with the prospect of volume growing sufficiently to consume the additional capacity over a number of years. In the early years however, the smaller Gunnedah Basin volumes would generate revenue that was insufficient to recover the cost of these investments. That is the revenues on the ARTC network extending to the north of the Hunter Valley coal network prescribed by the NSWRAU would be constrained by the market (and not through regulation) until volumes grew sufficiently.

During development of the HVAU, ARTC consulted regularly with the coal industry both before and during the period of the ACCC regulatory assessment (April 2009 – June 2011).

As features incorporated in the HVAU in addition to that incorporated in the IAU and NSWRAU included:

- **Covered Hunter Valley coal network extended to the Gunnedah Basin coal region** – In order to recognise the expanding Gunnedah Basin coal region and the necessary investment in the network the HVAU covered network includes the network north of the Hunter Valley coal network prescribed under the NSWRAU extended to the Gunnedah Basin coal region.
- **Introduction of Loss Capitalisation** – ARTC recognised that during the early development stage of the Gunnedah Basin coal region, it was likely that recovery of revenue would be insufficient to recover the substantial investment costs needed to facilitate future demand growth. Loss capitalisation was a mechanism introduced in the HVAU that enabled ARTC to capitalise economic losses arising during early life cycle of the network, where volumes were insufficient to recover full economic cost, enabling recovery in the longer term where the market permitted volume grow to sufficient levels to support such recovery. This mechanism was intended to provide incentives for investment in more marginal parts of the Hunter Valley coal network ahead of demand. The HVAU limited application of this mechanism to that part of the Hunter Valley coal network required to only serve the Gunnedah Basin coal region.
- **Alignment with Coal Chain Capacity** - The HVAU provides for alignment and recognition of coal chain capacity through
 - Provision for contracting directly with coal producers;
 - Requirement for an applicant to show that it has matching port capacity for the requested track access;
 - Explicitly recognition of the role of the HVCCC in the assessment of coal chain capacity, the initial granting of track access rights and the ongoing optimisation of coal chain performance; and
 - A role for the HVCCC in aligning coal chain expansions and the endorsement of planned track capacity expansions.
- **Incentive Pricing** – To address long held industry concerns with historical origin-destination per tonne based pricing and to provide a basis for incentives for more efficient utilisation of resources, 2-part pricing (variable/take-or-pay (TOP) components) was incorporated in the HVAU together with pricing objectives linking pricing components to recovery of cost where possible, and a commitment to introduce pricing incentives for more efficient utilisation of resources during the term of the HVAU through the definition of the indicative service and price differentiation of different coal train configurations.
- **Published Pricing** – To improve pricing transparency, the publishing of all coal and non-coal pricing and other information was incorporated in the HVAU.

- **Cost Definition and Allocation** – To support the objectives of the HVAU in relation to the transparency and detail of methodologies, principles and processes for determining Access revenue limits (floor/ceiling), greater prescription around the definition of costs, including the efficiency of costs and the allocation of non-Segment Specific Costs was incorporated in the HVAU.
- **Development and Endorsement of Additional Capacity** – To replace the existing less structured process under the NSWRAU for the development of, and consultation on, capital expenditure proposals a formal, comprehensive mechanism covering the identification, development, consultation, delivery and funding of additional capacity was incorporated in the HVAU. This included the capability for users to fund network expansions if needed.
- **Accountability for performance** - To increase ARTC's accountability for performance against contractual obligations and underpin the direct contracting with coal producers a mechanism to identify shortfalls in performance and application of penalties via a rebate of TOP charges is incorporated in the HVAU.

In incorporating these new features in the HVAU which primarily seek to promote across the Hunter Valley coal chain, ARTC considers that mandating a stronger focus on the efficient development and operation of the broader Hunter Valley into ARTC's operational and investment decision making also increases risk to the company. This is because ARTC is no longer able to contemplate decisions aimed at producing optimal outcomes for its rail network in isolation. What might be an optimal operational or investment decision for the coal chain generally may not be an optimal decision for a service provider operating as part of that coal chain, and therefore may not be the decision that is aligned to the business interests of the service provider alone.

4.3 Consistent Rail Regulation

4.3.1 Interstate Rail Network

ARTC is of the view that it is important that economic regulation is applied consistently across the interstate rail network. This will provide for greater confidence amongst users of the interstate rail network in relation to equity in treatment and certainty of access. Furthermore, investment decisions (above rail and below rail) are made by infrastructure providers and users in the context of the efficiency of service availability and efficiency across the entirety of the interstate rail network requiring the application of a consistent framework for investment.

As stated earlier, ARTC considers that greater consistency of regulation across the interstate rail network has largely been driven through increasing the extent of the network under single management over the last decade and through the engenderment of goodwill and cooperation at operational levels between access providers in the areas of customer service, access negotiation and planning, and capacity and network management.

These drivers have largely arisen from within the industry and through commercial necessity, where the interstate rail network competes against a strong

interstate road network that does not face jurisdictional and regulatory barriers to efficiency to the same extent.

There remains parts of the interstate rail network that are subject to state based regulation. These include:

- Those parts of the interstate rail network in the Sydney metropolitan network being the MFN including Port Botany, and the metropolitan commuter line between Sydney and Newcastle which are covered in the NSWRAU administered by IPART. ARTC is currently working toward extending coverage of the IAU to the MFN and Port Botany.
- The standard gauge interstate rail network between the NSW/Queensland Border and Acacia Ridge (Brisbane) not presently covered under a state based regime. ARTC is currently working toward extending coverage of the IAU to Acacia Ridge.
- The interstate network between Kalgoorlie and Perth, a key part of the east-west rail corridor covered by the WA rail access regime administered by the WA rail access regulator.

That part of the interstate rail network in northern Sydney, currently referred to as the Northern Sydney Freight Corridor (**NSFC**), is the existing metropolitan commuter line between Sydney and Newcastle. The Federal and NSW Governments are funding an upgrade of the NSFC (\$1.1b) to be delivered by ARTC and the NSW Government between 2012 and 2016 that is intended to improve daily freight capacity between Sydney and Newcastle by 50 per cent to support growth on rail and complement ARTC's \$2.5 billion investment in the Melbourne-Sydney-Brisbane corridor.

At this time, ownership of the NSFC will remain the present owner, RailCorp, and this part of the interstate rail network/commuter network will remain covered by NSWRAU administered by IPART.

For those parts of the national rail network upon which interstate rail freight markets operate that are likely to remain under state based access regimes (such as the network connecting Kalgoorlie and Perth in WA and the coastal general freight connecting Brisbane and far north Queensland), and for reasons described earlier, ARTC considers that increased priority should be placed on achieving greater consistency in regulation. ARTC recognises that the certification process under Part IIIA of the CCA, administered by the National Competition Council (**NCC**), contemplates consistency of regulation across jurisdictions to the extent interstate markets are affected (as provided under the Competition Principles Agreement). It is not clear to ARTC that this consideration has delivered effective and consistent outcomes for interstate rail freight users.

4.3.2 Mining Networks

There is a question as to whether it is still desirable to have consistent regulation across the entire rail network, including mining networks.

In its inquiry ‘Progress in Rail Reform’ in the late 1990’s, the Productivity Commission distinguished four different types of rail network in terms of commercial and operational characteristics as follows:

- interstate network;
- high volume regional network (minerals);
- low volume regional network (agricultural); and
- metropolitan commuter network.

ARTC agreed with this differentiation at the time, and considers that the commercial and operational characteristics of these networks remain largely unaltered.

ARTC remains of the view that economic regulation should be applied consistently across the national rail network. This is not to say that uniform regulation in the form of access regimes or undertakings should apply in all circumstances. As indicated at section 3.5, there should be differentiation between access regimes based on the access providers’ market and industry position. The access provider’s market position in relation to the three types of freight networks above can vary. Both the interstate network and many low volume agricultural regional networks do face intermodal competition (primarily from road) and therefore have limited ability to exert monopoly power over rail customers where reduced volume generally manifests in reduced profitability. Access providers on these networks are generally incentivised to promote utilisation of the network.

On the other hand, most high volume mineral networks are not exposed to intermodal competition and are able to act monopolistically in this sense. However, such networks predominantly serve and are part of a broader export supply chain which competes in international markets with other supply chains. As such there are some constraints on monopolistic behaviours on these networks and there is a recent trend in the focus of access regulation towards promoting efficiency not just in the use of and investment in the regulated network but in the wider supply chain (and indicated in the case of the Hunter Valley coal network in section 4.7.4 below).

ARTC considers that the above developments of the IAU and HVAU have been developed on a consistent basis, and can operate effectively with respect to these two parts of ARTC’s network, even from an operational and commercial standpoint at locations where these two parts of the ARTC network interface.

Whilst the two regimes are consistent, they are not uniform, and are aligned to the respective operational and commercial characteristics of each part of the ARTC network.

ARTC also considers that the development of consistent regulation across two different networks was assisted through the involvement of only a single network owner and single regulator. It is not clear that such an outcome would be achievable where multiple network owners were involved.

Nevertheless, given that single ownership of all networks is unlikely to be achievable, the best means to move towards more efficient and consistent regulation across rail networks would be to have a single national rail regulator.

With respect to these and other rail networks, ARTC considers that consistency could apply with respect to the decision (made by a single national body) to cover the network and to the form and intensity of regulation to apply (refer next section) and that consistency should apply with respect to the requirement for the access provider to submit an access undertaking (or similar) to the relevant regulator for approval. Consistency could apply (similar to the form/intensity decision above) in determining where a rejected access undertaking could be withdrawn, or whether a regulator could impose an access undertaking.

Undertakings should be reviewed by a single body (national rail regulator) and should contain certain minimum prescribed requirements for consistency covering negotiation and dispute resolution, regulatory reporting and where vertically integrated, ring fencing. Prescribed guidelines for other mandatory components of an undertaking could provide enough flexibility to deal with the specific commercial and operational requirements of the different types of freight networks listed above whilst maintaining a sufficient degree of consistency.

ARTC notes that the Review Panel has suggested that these activities could be carried out by a single access and pricing regulator. ARTC views in relation to the recommended roles of such a body are provided in the next section.

4.4 National Rail Regulator

ARTC notes that the Review Panel has proposed the creation of a separate access and pricing regulator to oversee all industries currently regulated by the Commonwealth. It has proposed that the powers given to the NCC and the ACCC under the National Access Regime be transferred from the ACCC and the NCC and be undertaken within the national access and pricing regulator.

ARTC notes that whilst the Review Panel refers to the regulator as being 'national' it proposes to limit the entity's regulatory function to only those industries regulated by the Commonwealth. This means in the case of rail that the national regulator would only regulate the rail network managed by ARTC.

ARTC is of the view that consistent rail regulation and delivering harmonisation and consistency between national rail networks in differing jurisdictions will not be achievable, if it is administered by several jurisdictional regulators due to the significant discretion provided to the regulator.

ARTC notes that, in its submission, Asciano has cited several benefits resulting from establishing a national rail regulator as follows:

- Reduced duplication of effort.
- Increased specialisation.
- Regulatory capture and independence.
- Improved regulatory certainty.

- Co-ordination benefits.

The Review Panel's proposal does not appear to achieve this outcome, and would seem to perpetuate the existing regulatory circumstances (notwithstanding a change in name) faced by rail. As noted in Table 2, the Review Panel also supports in the Draft Decision a continuing role for state and territory economic regulators, but where a move to national regulation as circumstances permit should be encouraged.

ARTC is cognisant of the support of the states being needed to achieve single regulation of rail networks in Australia. ARTC proposed that the use of a national regulator would best achieve the outcomes of the National Rail Access Regime proposed to the States in 2006 (see section 4.6 below). In this case the proposal was not implemented.

Nevertheless, ARTC would still recommend that all rail networks in Australia be regulated by a single body (the national access and pricing regulator as proposed by the Review Panel) and would welcome further consideration by relevant governments towards achieving this outcome, and would benefit from the resulting administrative efficiencies.

In the case of metropolitan commuter networks which are entirely based in each state and are subject to certain state legislative and policy objectives, the transition to a national framework in relation to access to these networks could be considered on a case by case basis. It is noted that regulation of other aspects of these networks than access (such as price regulation of passenger fares carried in, say, Sydney by IPART) is not included here.

ARTC considers that the following characteristics of the rail industry may make consideration with respect to regulatory decision making, the requirements of regulatory instruments and the administration of those instruments somewhat different to that for other industries such as gas and electricity:

- As described earlier, there are significantly different operating and commercial characteristics applicable to different rail networks in Australia.
- Most rail networks provide services to industries that are integrated into supply chains that compete against other supply chains, both nationally and internationally.
- A number of rail networks face varying degrees of competition from other forms of transport that do not currently operate in way that is competitively neutral with rail.

However, ARTC also recognises that there may also be efficiency advantages in single regulation across industries as pointed out in the Draft Report (see Table 2).

To this end, ARTC supports the establishment of a national access and pricing regulator, as contemplated by the Review Panel, but regulating all rail networks in Australia under a national rail access regime or code (see section 4.6 below). The costs and benefits associated with the establishment of a separate national rail regulator in these circumstances could then be determined.

By and large, the benefits of national regulation for the rail industry can be significant. However, maximising that benefit may depend to some extent on how a national regulator is implemented particularly in relation to the extent and quality of available resources and process that would be employed.

ARTC's experience in dealing with its regulator, the ACCC (noting that this is not a regulator specific to the rail industry) in relation to its interstate and Hunter Valley networks indicates some concerns, in ARTC's view, that are discussed in section 4.7 below. Whilst some improvements for rail have arisen from a reduction in the number of regimes applicable to these networks, and some consistency between these regimes, ARTC has at times noted increased difficulty dealing with a regulator that is further removed from the specific existing and historical operational and commercial arrangements of specific networks than state based regulators, and that also predominantly regulates in other industries.

It is important that the regulator gets the regulatory setting rights and this sometimes requires significant expertise in the operation of a particular rail network. A regulator that is further removed may be less appreciative of specific industry circumstances and risks in making decisions around appropriate investment returns, and around cost efficiency, and less able to objectively identify an appropriate regulatory balance in the face of conflicting stakeholders both between the infrastructure owner and users and between competing users. ARTC believes that this can be overcome under a national regulator.

Further, a regulator more heavily involved in other industries can tend to look to those industries for guidance and precedent in determining what may be most appropriate for the rail network. As stated earlier, there are characteristics of the rail industry that may make consideration with respect to regulatory decision making, the requirements of regulatory instruments and the administration of those instruments somewhat different to that for other industries.

Another area of concern for ARTC has been the additional regulatory risk arising where over time regulatory views change, sometimes due to staff turnover where regulatory information and experience is either not fully transferred or lost altogether. As a result, what may have been considered acceptable at a point to the regulatory staff and decision makers (and therefore becomes a foundation for future long term decision making by the infrastructure owner), may become unacceptable a few years later where different staff and decision makers are in place.

As such, it is ARTC's view that the benefits cited in establishing a national regulator may be diminished unless that body is equipped with sufficient expertise that is also sustainable over a period of time through adequate internal processes.

In relation to the roles proposed for the national access and pricing regulator by the Review Panel as noted in the Draft Report, partly being those afforded to the NCC and the ACCC under the National Access Regime, it is ARTC's view that it is important to separate the coverage/form of regulation decision-making function from the policy implementation and regulatory function, for the following reasons:

- Conflict of interest may exist where a regulator is charged with decision-making at both of these levels, in deciding the scope of its work, which could lead to excessive regulation and creep.

- Access regulation can potentially represent a significant intrusion on the rights of infrastructure owners, and must therefore be subject to safeguards to ensure that its application in any particular case is in the public interest. The importance of public interest considerations in this regard suggest that the coverage and form of regulation decision should be made by a relevant Government Minister (based on the advice of an independent advisory body).
- Separation of these decision-making functions largely reflects the current approach taken in access regulation in Australia, underpinning the current role of the NCC or a successor in relation to its current role in this regard.

Finally, at section 7 of this submission, ARTC proposes that in order to achieve competitive neutrality in the provision of rail and road services in a number of interstate and regional transport markets, it is important for both transport modes to access relevant infrastructure on the same basis, so that resulting pricing and investment decisions can be made efficiently.

This would involve the implementation of similar regulatory frameworks for both modes that applies nationally (particularly for interstate freight) and similar to ARTC's above proposal for a national rail regulator, ARTC sees merit in having a single national road regulator.

A natural advancement to this concept that could be considered is the establishment of a national land transport regulator, regulating both road and rail in relevant markets. This would further enhance consistency in the regulation of infrastructure for the two competing modes.

ARTC recognises that there may be a number of ways of achieving such an outcome, including the regulation of both modes by the proposed national access and pricing regulator. In any event, and as indicated for rail earlier, there would need to be support from the states for the implementation of national regulation of both modes before the costs and benefits associated with implementing an industry specific (land transport) access regime and regulator could be contemplated. The implementation of national regulation of these two modes could be seen as an enabler ahead of determining the most appropriate institutional framework for delivering the best regulatory outcome.

4.5 Differentiation of access regimes should be based on the access providers market and industry position

ARTC considers that there should be differentiation between access regimes based on the access providers' market and industry position. Specifically, the characteristics of an access regime are different when applicable to a service provider related to entities operating in upstream or downstream markets (as opposed to a provider with no such interest), on the basis that the commercial motives of the two providers are different and such motives govern the way the providers operate. Secondly, the characteristics of an access regime differ where the extent to which provision of services utilizing a natural monopoly facility confers market power on the provider of the services.

To exclude entities from coverage of Part IIIA of the CCA on the basis of industry structure (vertical separation) alone may create some undesirable outcomes.

Also, the provision of services utilizing a natural monopoly facility does not necessarily confer market power, assuming an appropriate market definition. ARTC considers the competitive forces in the markets from which it derives a significant portion of its revenue on the interstate rail network do not permit it to conduct its business with market power.

ARTC is supportive of a more inclusive view with regards to the coverage of services under Part IIIA of the CCA, at the risk of some cost and inefficiency to industry. It is ARTC's view that these risks can be mitigated by more formally addressing the market and industry position differences between access providers.

ARTC has proposed two types of regime. A third party access regime applicable in circumstances where the access provider is related to entities with upstream or downstream market significance (vertically integrated) is more prescriptive and covers a range of issues including access application, negotiation and pricing, dispute resolution, service performance, anti-competitive conduct, accounting separation and ring fencing. This is necessary to minimize the anti-competitive behaviour that such an entity has a commercial imperative to engage in. An open access regime would apply in circumstances where the access provider has no upstream or downstream interests, has access revenue as its principle source of income and has a commercial imperative to promote competition in the use of the facility in order to grow the market. The primary regulatory concern here relates to monopoly pricing, where the provider has market power.

Within each of the two types of regimes, the extent of issues covered and the degree of prescription required is largely dependent on the extent of market power that the access provider has. A highly prescriptive third party regime would be applicable with respect to a vertically integrated provider with significant market power. On the other hand a flexible open access regime (or no regulation at all) would be applicable to a separated provider with little or no market power. Figure 1 below illustrates.

Figure 2: Differentiation of Access Regimes

Structure \ Market Power	Significant → None	
	Third Party Access Regime	Third Party Access Regime
Vertically Integrated	Highly Prescriptive Focus on anti-competitive behaviours and monopoly pricing	Highly Prescriptive with respect to anti-competitive behaviours. Less prescriptive with respect to pricing.
Vertically Separated	Open Access Regime Only prescriptive with respect to denial of access and monopoly pricing.	Open Access Regime Little or no prescription

A formal differentiation of regimes in Part IIIA of the CCA may create more efficient outcomes in that regimes could be tailored to specifically address the market and industry position of the provider. Further, unnecessary costs of regulation can be minimized.

Decision making in relation to the type of regime that could apply to particular infrastructure could be made using a similar process and decision maker to a coverage decision for that infrastructure as indicated in the above section.

4.6 National Rail Access Regime

ARTC indicated in section 2 of this submission that, in 2006, governments agreed, through the CIRA, to provide for more simple and consistent national economic regulation of nationally significant infrastructure, including railways. ARTC participated, with the ACCC, in the development of a proposal for a code that would apply to all rail networks that would govern central decision making in relation to the coverage and intensity of regulation applicable to rail networks as well as the application of a consistent set of principles for the development of access undertakings to rail networks. At the time this code became known as the National Rail Access Regime (**NRAR**).

The proposal was considered by governments, but ARTC understands that relevant governments elected to proceed with an alternative path to seek certification of existing state based regimes in order to satisfy CIRA requirements.

Broad principles of the NRAR proposed at that time were:

- For rail infrastructure to be covered by the NRAR, the form of regulation to apply to that infrastructure would be determined by a working party implementing the Council of Australian Governments (**COAG**) infrastructure initiatives or an appointed entity independent of a regulator.
- Covered infrastructure would be subject to a form of regulation taking into account extent of market power, and incentives resulting from structural circumstances as described by the NRAR.
- The outcome of the form of regulation test would determine the relative light handedness or heavy handedness of regulation to apply ('regulatory intensity').
- With respect to the infrastructure initially proposed to be covered by the NRAR, the existing degree of market power and structural characteristics were recommended.
- There would be two forms of regulation. All regulated rail networks would submit an access undertaking to the relevant regulator for assessment. However, in the event that the regulator rejects the proposed undertaking:
 - for some rail networks – the NRAR would require the regulator to impose an undertaking; and
 - for other rail networks – the NRAR would allow the access provider to withdraw the undertaking (although the network would still be subject to the provisions in the code governing negotiation and dispute resolution, regulatory reporting and, if applicable, ring fencing).

- The decision on the form of regulation (ie whether an undertaking can or cannot be imposed) should depend on whether the rail network has substantial:
 - market power - in effect, the ability of the rail network to provide access on terms and conditions that would not occur if there was effective competition; and/or
 - incentives, in the absence of regulation, to prevent or hinder access to non-affiliated access seekers – in effect, whether the rail network is vertically integrated or separated.
- Elements to be addressed in an access undertaking:
 - Services
 - Extensions & expansions
 - Pricing principles
 - Quality of service
 - Network management
 - Indicative access agreement
 - Duration
- Other elements of the access code (vertically separated networks)
 - Negotiation & dispute resolution
 - Regulatory reporting
 - Ring fencing

It should be noted that given the historical nature of this development, these principles should not be taken as representative of any current ACCC view in this regard, and may warrant some reconsideration in light of more recent experience.

4.7 ARTC's Experience to Date

ARTC has been heavily involved in the development and application of economic regulatory principles on its network and in other rail jurisdictions since the late 1990's. This involvement has resulted in the development of undertakings on its network and the need to regularly consult with the ACCC, other state based regulators and its customers in such developments. The breadth of ARTC's network covers the interstate network, the Hunter Valley coal network and some regional networks. Each of these networks has different commercial and operational characteristics requiring different regulatory intervention and regulatory principles as described in the above sections.

To this end, ARTC considers that is uniquely placed to offer its views in relation to regulation in rail and broader supply chains as a result of this experience.

ARTC will provide its specific comments and views in relation to a range of different aspects of the existing approach to access regulation in rail, and particularly on the ARTC network, and of its dealings with economic regulators in developing arrangements on rail networks, in the remainder of this section.

4.7.1 Regulatory Focus

The fear of competition and the sometimes constrained return that the infrastructure owner is able to achieve inhibits asset renewal to an extent that could produce market failure. Regulatory practice to date has focused more-so on delivering efficient service (and lower end user cost) rather than on investment for sustainability and future growth capacity. Significant gains have been achieved for the industry in this regard and now the focus needs to be re-balanced towards the need and incentives for infrastructure owners to renew assets and invest for capacity enhancement. This needs to be recognised in the regulatory framework.

ARTC has sought to improve this balance in the regulation of its network by introducing some relatively new and innovative provisions in its access undertakings which have received regulatory support. These include a focus on ex-ante, industry based approval of capital expenditure for inclusion in the cost base, and the introduction of capitalisation of early year losses into the cost base in order to encourage riskier investments (sought and supported by industry) in capacity ahead of demand so as to ensure that the rail network does not become the constraining element in the relevant supply chain as demand increases. Further detail in relation to these innovations can be found in the HVAU and supporting documents.

Part IIIA of the CCA provides for an infrastructure provider to permit extension of a facility where sought by a user (subject to certain economic criteria being met) but does not necessarily require the access provider to fund an extension. This provides for the possibility of a user or users to directly fund an extension through some form of initial up-front capital payment (as opposed to initial funding being provided by the access provider recovered through access charges or some other re-payment stream over time).

However, the provision of initial capital payments by users for extensions to a facility may introduce a range of uncertainties for both parties in relation to ownership of extended facilities, the taxation treatment of the initial capital payments, and taxation treatment of ongoing depreciation of the assets. Such uncertainties may result in the legal and financial framework surrounding such arrangements becoming far more complex than otherwise might be necessary in order to mitigate the risks arising from these uncertainties, posing a constraint to the completion of such arrangements and investments in the network.

To this end, and in order to mitigate such barriers to investment, a review of the alignment of this element of Part IIIA of the CCA and the relevant aspect of taxation legislation may be appropriate, with a view to promoting clear and simpler taxation treatment of these infrastructure funding arrangements.

ARTC notes that the submission to the Issues Paper provided by Aurizon goes into this aspect in more detail.

4.7.2 Complexity in the application of regulation/consultation

ARTC's original submission of the IAU took place around 13 months ahead of final approval. This undertaking was essentially a replacement for its original access undertaking accepted in 2002.

ARTC originally submitted its HVAU around 26 months ahead of final approval. The original submission followed a period of 12 months of separate consultation with industry.

ARTC accepts that the regulator should have a reasonable period of time in order to give due consideration to regulatory instruments, and acknowledges the introduction of legislative provisions around time frames for regulatory decision making. ARTC also recognises the difficulty associated with balancing the interests of stakeholders that are often opposed even within a particular group of stakeholders (eg network users).

Regulators often seek to expedite the approval process by encouraging separate consultation and negotiation between the access provider and network users. In the case of the HVAU separate negotiation was complicated by the existence of 14 competing coal users with different interests and an industry body purporting to represent the interests of all coal users.

The approval process with respect to the HVAU for many reasons ended up being a protracted and very detailed process that resulted in a far more complex and wide reaching access framework than any party may have originally anticipated. This was further complicated by the changing interests and requirements of stakeholders and the regulator during the regulatory process, sometimes as a result of changing personnel being involved.

Even then, the HVAU provided for a number of near term reviews intended to finalise a number of processes that could not otherwise be finalised during the regulatory approval process. The conduct of these near term reviews commenced in the second half of 2011 (upon commencement of the HVAU itself) and is still continuing today (second half of 2014). Each of the reviews themselves has had a 6-12 month regulatory approval process. The initial HVAU was an access arrangement that in the view of users and the regulator contained sufficient uncertainty at the time to warrant reducing the original term of the HVAU by half (from 10 years to 5 years) with an expiry date of 30 June 2016. Given the time taken for industry and regulatory consultation in relation to the initial HVAU, and having regard to the settlement of a number of the reviews since then, the development and regulatory approval process for the next undertaking would need to commence around now, only 3 years after initial commencement and whilst some reviews as part of the initial HVAU are still being conducted.

The extended time needed to develop and approve an access undertaking, as well as the early reviews of unresolved processes, more general mid-term reviews of undertakings, and conservative approach to the term of undertakings all impose significant additional cost and resourcing on the access provider, as well as operating in an uncertain environment. An access undertaking is intended to provide certainty for all participants over its term.

The costs are only immediately recoverable, if at all, by the access provider where the network is constrained. This is not the case on any part of the interstate network, and only on some parts of the Hunter Valley network.

There is also a cost associated with the risk of uncertainty.

Whilst ARTC accepts that there is need for due consideration of such regulatory instruments, ARTC considers that there needs to be further consideration of mechanisms that will aid the timeliness and efficiency with which regulatory decisions can be made, so as to provide a sufficient level of certainty in order to encourage investment.

ARTC notes similar concerns raised by Aurizon in its submission, specifically in relation to where regulatory pursuit that might be considered an optimal solution may have distracted from the regulatory determination as to whether an access proposal is reasonable. ARTC agrees that this pursuit has increased complexity of an assessment, resulted in delay and created greater uncertainty around the regulatory outcome or treatment.

ARTC is unable to locate any direct reference in relation to the increasing complexity and development time for regulatory instruments and the impact that this may be having on regulated businesses in the Draft Report.

4.7.3 Regulatory Uncertainty & Risk

Following on from the previous section, the final 6 months of the regulatory approval process was largely consumed by a separate negotiation between ARTC and the coal industry in order to deliver a reasonable balance of interests for both key network users and ARTC. In this case, the coal industry sought further development of the HVAU in order to increase transparency, and ARTC accountability for performance whilst ARTC, in order to address the additional risks that resulted sought a rate of return that was higher than the regulator was prepared to contemplate at the time, but was needed to facilitate the investment needed in the Hunter Valley coal network. This is discussed further in a later section.

This separate negotiation was sought and encouraged by the regulator and delivered a negotiated outcome that the regulator considered to represent a reasonable balance of interests as well as efficient outcomes going forward.

At the time, it was ARTC's view that the negotiated outcome would deliver to both the industry and itself at least 5 years of certainty in order to encourage the investment needed.

In relation to investment in the network, a substantial part of the investment in the network to deliver the existing level of throughput as well as that required in the medium term was incurred by ARTC since the commencement of the HVAU. This investment has amounted to around \$1bn and has increased annual coal throughput by around 70-80mT, and international coal revenue by around \$6-7bn per year. Clearly this is a very positive outcome for the coal industry.

Nevertheless, since that time and through annual compliance reviews and the near term reviews alluded to earlier, it is ARTC's view that both the industry and the

regulator have sought adjust the balance of interests negotiated in 2011. At that time, the HVAU contained a range of provisions governing the level of information to be made available by ARTC to the industry, regulator and the public both in the normal course of its business and during specific regulatory processes prescribed under the HVAU.

Whilst ARTC does not seek to withhold information from the industry or regulator, it is of the view that a balance between the information needs of users and its own need for flexibility in how it runs its business is reasonable and indeed desirable.

At the time the level of disclosure was considered to represent a reasonable balance of interests by the regulator, and whilst perhaps not optimal from the industry's perspective, the level of disclosure was negotiated as part of a package that was the HVAU.

ARTC understands that users will always seek more information about an infrastructure owner's costs and business processes in order to optimise its negotiating position in ongoing pricing and other negotiations. ARTC considers that, in a regulated environment, it is the regulator who should ensure that a balance is maintained at a level in accordance with a regulatory instrument during the period of that regulatory instrument.

Since commencement of the HVAU, the level of disclosure required in ARTC's dealing with industry has increased in response to the continued submissions of industry that more information is required. This has primarily occurred during the near term reviews by way of setting precedent.

It concerns ARTC that having committed substantial time and resources into developing and gaining approval for a regulatory instrument that is intended to provide certainty for business and investment decisions can be gradually undermined during its term.

It is ARTC's view that the purpose of a regulatory approval process is to ensure that the regulator and industry have sufficient information about the infrastructure owners business and proposals submitted to the regulator to be able to reasonably assess the regulatory instrument in terms of the relevant legislative requirements.

During the development and approval process, ARTC provided substantial information to the regulator and in the public domain in relation to the various elements of the HVAU, including detailed financial modelling. Subject to confidentiality requirements, ARTC would have provided further information, had it been sought by the regulator, as is required under the CCA.

ARTC understands that personnel changes for regulators and industry participants are inevitable, and that sound processes for ensuring knowledge retention within such organisations are important, particularly over an extended regulatory period. ARTC does not believe that it is its responsibility to maintain a high level of understanding of what are fairly complex regulatory processes. It is in the interests of, and is best managed by, relevant entities to ensure that such knowledge is maintained over time.

ARTC considers that it is inappropriate to point to the infrastructure owner, where the existing knowledge of such processes may have diminished over time, for a lack of transparency.

Where a change in regulatory position results from a perceived lack of understanding during the term of a regulatory instrument that is perceived to have resulted from a lack of transparency at the time, or simply from a change of view due to regulatory staff turnover²⁴, this can create substantial uncertainty for the infrastructure owner. This could not have been anticipated, and could impact significantly on the risk associated with investment occurring during the term on the basis of the certainty provided by the regulatory instrument.

4.7.4 Regulatory Coverage

During the early development of the HVAU in 2008 and 2009, a related regulatory development was occurring at the port of Newcastle arising from a government review of existing commercial and operational practices in the Hunter Valley that were seen to manifest in undesirable outcomes where contracted shipping volumes consistently outstripped the capacity of the coal chain resulting in excessive queues of ships awaiting loading off Newcastle with a high demurrage cost to industry.

The long term solution sought by Government required the port operators to seek authorisation for certain conduct needed to address these capacity constraints. A detailed framework for managing capacity at the ports was developed by the ports (directed by coal producers) which largely due to pressure to expedite the process and implement the solution did not, in ARTC's view, sufficiently address the need to consider other elements of the coal supply chain, including the rail network. A fundamental premise of the port arrangements reflected the fact that a tonne of coal arrived at the port was a tonne of coal irrespective of its origin. On the rail network, however, a tonne of coal originating from one mine can have significantly different capacity impacts to a tonne of coal originating at another mine.

The port capacity framework was considered and authorised in late 2009 by the ACCC in an expeditious manner, again under pressure to implement the solution. During this time, the development of the HVAU was still in its early stages, and any alignment with capacity management protocols considered for the rail network at the time did not appear to be a major objective. At the time, ARTC recommended that the development of the two capacity frameworks should occur concurrently rather than sequentially in order to fully contemplate alignment issues.

In the end, following authorisation of the port capacity framework for a period of 15 years in late 2009, the only means then seen by the industry by which any sort of alignment between arrangements could be achieved was through altering or introducing related mechanisms in the HVAU and requiring ARTC to demonstrate that its proposed framework was aligned to the authorised port arrangements.

²⁴ The ACCC has recently carried out a review of fundamental aspects of the application of floor and ceiling tests proposed by ARTC (and approved by the ACCC) for incorporation in the HVAU in 2011. The review is being carried out 3 years into the 5 year term of the HVAU and any resulting adjustments could be applied retrospectively. The proposed application of these tests was aligned to that applied in the Hunter Valley for many years and was advised to, and consulted on by, ACCC staff at the time of consultation on the HVAU in 2009-11 and ahead of its approval.

To assist, ARTC sought to make amendments to the HVAU to bring about alignment in a practical sense in a number of areas, but this substantially complicated and increased uncertainty in relation to many of ARTC's proposals, particularly where the port arrangements are premised on a different capacity paradigm as described above. This was further complicated by the inconsistent application of the port capacity framework to the two terminals at Newcastle, where one had yet to be constructed.

In the end, and in order to achieve practical alignment, a number of relatively straightforward mechanisms in the HVAU became increasingly convoluted and with uncertain outcomes going forward.

Nevertheless, ARTC considers that unless it adequately addressed alignment with arrangements for other elements of the coal supply chain in the HVAU as sought by the ACCC and industry, the ACCC would not have accepted the HVAU.

Since the HVAU has been approved, and whilst many capacity management mechanisms are working due to cooperation of participants, there have been some failures identified that have now required further ongoing industry development and regulatory intervention to resolve. Again, a source of failure arises from the inconsistent application of, and commitment to, the port capacity framework in relation to the two terminals at Newcastle.

A broader concern here, and one that may be particularly applicable to transport networks, is that such networks often are dedicated (to varying extents) to broader supply chains.

ARTC recognises the benefit to the efficient operation and competitiveness of the Hunter Valley coal network of coordination between participants in the Hunter Valley coal supply chain. To this end ARTC incorporated a number of elements in the HVAU aimed at delivering effective consultation between itself and other industry participants, particularly the HVCCC, in a number of operational and investment decision making processes. These are detailed at section 4.2.2 of this submission.

ARTC also described in that section how ARTC is no longer able to contemplate decisions aimed at producing optimal outcomes for its rail network in isolation. What might be an optimal operational investment decision for the coal chain generally may not be an optimal decision for a service provider operating as part of that coal chain, and therefore may not be the decision that is aligned to the business interests of the service provider alone. This increases risk and cost for the service provider.

Whilst ARTC accepts that the ACCC (and other regulators) have a fairly broad ambit and responsibility for the delivery of efficient outcomes in industries, it is important to ensure that pursuits in this regard are measured and balanced in the way they are implemented.

Nevertheless, ARTC believes that using a regulatory instrument applicable to one element of a broader supply chain is not necessarily the best means to pursue wider supply chain efficiency and coordination objectives, and may increase regulatory complexity and risk (without adequate compensation) as described above.

ARTC notes that Aurizon has expressed similar concerns that regulation ‘has gone beyond that necessary to promote competition in dependent markets, and has begun to include elements of a broader industry policy’.

ARTC agrees that if this is seen as the way forward in developing regulatory frameworks for certain industries, competition policy should better prescribe:

- the extent to which this is may be appropriate;
- limitations on the role of regulators where intervention in these broader elements of industries may be inappropriate or outweigh the costs; and
- recognition of the increased risks faced by relevant infrastructure facilities taking on responsibilities for broader industry efficiencies.

If regulatory pursuit is to widen from the regulated infrastructure assets to a broader transport supply chains, then ARTC considers that it is also reasonable for regulators to give greater focus to the market and competitive circumstances experience by such supply chains. ARTC notes that the Review Panel has indicated *‘While the objective of the CCA is to protect and promote competition in Australian markets, frequently the sources of competition in Australian markets are global.’*²⁵

Mining supply chains compete with supply chains both within Australia and in other countries. Competing in international markets creates a range of different risks for participants in a supply chain including political and economic circumstances in both competing countries and customer countries. Factors around international competition and the inherent risks are relevant in the assessment of the extent to which the supply chain and participants have market power and are exposed to risk.

On the interstate rail network, where ARTC is a monopoly infrastructure provider in rail, the presence of strong intermodal competition in interstate freight markets is generally considered to constrain ARTC’s ability to exert market power. It could be argued that the presence of competing international supply chains may have a similar impact on the use of market power in mining networks in Australia.

4.7.5 Regulatory impact on innovation in Rail

ARTC notes that, in its submission, Aurizon indicated that regulation, whilst effective at promoting productive and allocative efficiency in a number of downstream markets, has been less effective at ‘achieving dynamic competition – namely, encouraging dynamic service offerings in downstream markets, prompting the development of new facilities, promoting innovation, or contributing to major advancements in research or technology’. Aurizon suggested that regulation severely limits the ability of both regulated businesses and the users of regulated services to capture a return from innovation, linked to the reluctance of regulators to endorse efficient price discrimination, and the tendency of regulatory regimes to socialise the benefits of innovation by regulated businesses.

²⁵ Draft Decision, p 39.

ARTC sees some merit in these observations. In particular, ARTC is of the view that the application of economic regulation to infrastructure, at least as it is currently formulated in many areas, does not reward performance where an infrastructure owner achieves desirable outcomes (e.g. increased capacity) through means other than investing in hard (and more expensive) infrastructure assets. In particular, the use of a building blocks rate of return mechanism to constrain pricing generally allows an infrastructure owner to earn a return on a regulated asset base which normally consists of a group of hard assets. The cost of such assets is normally included in the regulated asset base where such cost is considered prudent.

A desirable outcome in the Hunter Valley of increased capacity is normally achieved through investment in hard infrastructure assets, but can sometimes be achieved in other ways, such as improved network management and/or coal chain coordination. Efforts by the industry over the past 5 years to better align the performance of individual service providers with the objectives of the broader coal chain has resulted in significant capacity improvement without the need to make commensurate hard investments. However, alignment with broader coal chain objectives can also increase risk for individual service providers who are no longer able to optimise the utilisation of their assets in isolation. ARTC is not aware of this risk being adequately recognised in regulated returns.

It should be noted that ARTC is not suggesting that an infrastructure owner be rewarded for activity or innovation resulting in improvements in capacity and utilisation of existing assets, where such improvements only deliver the capacity intended to be achieved from that infrastructure in the first place.

However, where such activity or innovation results in improved capacity beyond that intended from the assets, such that further investment in hard (and more expensive) infrastructure assets is partially or completely avoided or deferred, there is may be some scope to reward the infrastructure owner.

Without this, there is little incentive for the infrastructure owner to do anything other than seek a hard asset solution. This may not necessarily be the most cost effective solution. Economic regulation currently seeks to bring about innovation more so by using a stick rather than a carrot, where a prudency assessment in relation to the cost of an investment in infrastructure could exclude any expenditure in excess of what might have been the case without innovation. This provides little incentive (reward) for the infrastructure owner to act innovatively.

Whilst industry involvement in the development and endorsement of additional capacity proposed in the 2011 HVAU acts to ensure investment is prudently incurred, ARTC is likely to be in the best position to identify and develop opportunities to innovate to increase capacity and therefore, unless appropriate incentives are in place, may promote hard asset options over possible innovative solutions.

The industry is able to capture the benefit of any innovative development of additional capacity through endorsement of a lower capital cost than might otherwise have been needed. There would seem to be little positive incentive to encourage ARTC to seek out innovative solutions to increasing capacity, where the actual cost of delivering the additional capacity that is endorsed into the regulated

asset base incorporates any innovation in development. Further, the delivery of additional capacity through innovation alone (i.e. without any capital investment) may not be recognised in the regulated cost base at all.

It is not unrealistic for the industry to expect some innovation on infrastructure owners part (innovation should be a normal competitive market outcome), nor is it unrealistic for the industry to expect to obtain some benefit from advances made through innovation. However, the approach adopted in normal regulatory practice, does little to incentivise the infrastructure owner to engage in innovation, as the infrastructure owner will obtain no net benefit from the additional capacity created.

4.7.6 Regulatory impact on pricing setting and flexibility in Rail

On ARTC's interstate network, and even to some extent in Hunter Valley coal markets, there can be substantial differences in the markets served by users of the network, which results in differences in user requirements for access to the network. Such differences do not manifest substantively in relation to the non-price aspects of the terms and conditions of access to the network. However, it is ARTC's experience that substantial differences have and will continue to arise in different markets in relation to users requirements in relation to both the level and structure of access pricing, where users seek pricing arrangements that promote specific efficiency and competitive outcomes in their markets further down the supply chain.

As is the case in many regulated industries, it is difficult for the infrastructure provider to gain a detailed and robust understanding of the commerciality and competitiveness in a diverse range of downstream markets that the network may serve. As such, it is difficult for the access provider to foresee a particular access pricing arrangement that may best support efficiency and competitiveness in downstream markets.

As such, ARTC considers it important that the regulatory framework provide for sufficient access pricing flexibility to address user needs, particular where a network services a diverse range of different markets, which is often the case on transport networks, and particularly in interstate rail freight markets. To promote inflexible or highly prescriptive access pricing on a network can potentially impact on network competitiveness and utilisation of the network, and on network investment.

ARTC recognises that the pricing principles set out in Part IIIA of the CCA provide for an access pricing structure that allows multi-part pricing and price discrimination where it aids efficiency. In principle, ARTC supports this objective as a flexible approach to pricing would appear to be supported.

It is ARTC's experience on both the interstate and Hunter Valley rail networks that regulators place significant importance on transparency in terms and conditions, including pricing, as a means of promoting utilisation of the network. ARTC supports transparency (publishing) of negotiated terms and conditions, and access pricing, as an important element in promoting user confidence and network utilisation.

As described earlier in this submission, the trend in this aspect experienced by ARTC is that greater transparency is sought in relation to how the level and structure of access pricing will be determined, resulting in the potential for greater prescription and rigidity in the regulatory framework as to how access pricing will be determined. This can result in adverse outcomes for network utilisation and efficiency.

Increased prescription as to how pricing will be determined is likely to promote increased use of fully distributed cost based pricing and less utilisation of negotiated pricing outcomes set within a framework of floor-ceiling cost based limits. In negotiating pricing within reasonable bounds, other relevant considerations such as market affordability and downstream efficiencies can be made (i.e. Ramsay pricing). Flexible pricing and discriminating on this basis can lead to efficient outcomes on many rail networks.

Whilst increased transparency and prescription may provide greater certainty for potential users of the network, the ability to negotiate flexible pricing to suit particular user needs becomes constrained. ARTC believes that providing for transparency by publishing indicative pricing (where it helps) and other negotiated access pricing can also provide sufficient certainty for users without constraining pricing flexibility and promoting efficient outcomes.

As such, ARTC would support provisions under Part IIIA of the CCA that clarify the emphasis on promoting pricing flexibility to meet efficient outcomes in order to discourage the apparent regulatory trend towards prescriptive access pricing determination, particularly in relation to networks serving diverse downstream markets, such as a number of transport networks in Australia.

5 RAIL INDUSTRY STRUCTURE

5.1 Structure of the Australian Rail Industry

The current Competition Policy Review has opened up discussion on whether the rail reforms of the 1990's are still relevant in today's commercial and economic environments. Submissions to the Review Panel have questioned the effectiveness of the vertical separation model in promoting competition, stimulating investment and enhancing productivity in the Australian rail industry.

In response to submissions on the structure of the rail industry, the Review Panel have offered a measured response in the Draft Report:

*'Rail reform has been relatively successful and proceeded at a reasonable pace. Many rail freight tasks face significant competition from road freight, which has made efficiency-enhancing reforms relatively palatable. Regulators and policymakers should be pragmatic about structural separation of railways, recognising that on some low-volume rail routes vertical integration may be preferable.'*²⁶

Of further relevance to the competitive structure of the Australian rail industry, Draft Recommendation 1 states that:

'The Panel endorses competition policy that focuses on making markets work in the long-term interests of consumers. The following principles should guide Commonwealth, state and territory and local governments in implementing competition policy:

- *governments should separate remaining public monopolies from competitive service elements, and also separate contestable elements into smaller independent business activities;*²⁷

ARTC welcome the Review Panel's view that rail reform has been successful. ARTC further welcomes the finding that public monopolies should be separated from competitive service elements; and submits that vertical separation remains the best model to promote competition and drive efficiency gains in the freight logistics sector.

Looking to the future, the rail industry is expected to pick up a growing share of Australia's ever increasing freight task. It is a stated government objective of Australia's eastern states to increase rail's modal share. A competitive rail industry, driven by open access, will promote the best outcomes for the economy and the Australian community. Competition drives price efficiency, innovation, service reliability and; above all, increased consumer welfare. From an ARTC perspective, open access allows us to retail rail through a number of market segments, tailoring the service to the customer need.

²⁶ Draft Report, p 134.

²⁷ Ibid, p24.

Broadly speaking, the Australian rail industry can be divided into three market segments; the interstate standard gauge network, mining networks, and grain branch lines (or agricultural rail). The interstate network could be segmented further, but the broad definition is suitable for the purposes of this submission. This section discusses the competition framework as it applies to three broad market segments.

5.2 Interstate (Standard Gauge) Network

ARTC notes that submissions to the Review Panel have questioned the current structural separation of the Australian interstate network, through competition law and government-ownership of the network. The two main arguments put forward are that:

- Structural separation of the long-haul freight market has been less effective at promoting competition as volumes on general freight networks are typically well below those needed to reach efficient scale; and
- much of the freight rail industry is neither commercially sustainable nor effectively competitive with road freight: general freight markets typically rely on on-going tax-payer support for the network infrastructure, calling into question the long-term sustainability of the interstate rail network in its current form.

In regard to the first point, ARTC contests that the evidence within the marketplace contradicts the position that open access has not promoted sustainable above-rail competition.

While the freight rail market is regulated, market forces will prevail such that uncompetitive operators will exit the market where there is not sufficient scale of competition to sustain inefficient operations. Within the rail freight market there are clearly defined market segments. Above-rail competition is more intense in some market segments, i.e. general intermodal, than others i.e. bulk, however; the level of contestable volumes both within and across market segments is sufficient to sustain multiple operators.

There are currently ten above rail operators on the interstate network. It is true that since privatisation that number has declined from around 30; however, only three operators have exited the market. Contrary to claims of unsustainable contestable volumes, the main reason for the decline in operators has been the consolidation of smaller operators [15 in total] into Qube, Asciano (Pacific National), Aurizon (formerly QR), and Genesee & Wyoming (GWA). ARTC contests that this is evidence of efficient competition, i.e. firms maximising their scope to enhance their competitive position.

In regard to the second point, ARTC's publicly available annual reports show that ARTC has a positive cash flow sufficient to cover depreciation, interest and tax - indicating that the business is sustainable. Statements regarding ARTC requiring ongoing tax-payer support are false and show an inherent failure to recognise equity injections from a shareholder to increase the value of its commercial entity and tax-payer support of a public good.

ARTC acknowledges that intense competition from the road sector has diminished contestable volumes in the intermodal rail market, particularly on the East Coast. However; ARTC contests the assertion that the strong growth of road market share is due to the competitive structure of rail. On the North-South corridor it is widely recognised that the trend away from rail is attributable to the duplication of the highway network coupled with the introduction of higher productivity vehicles (6 axle articulated trucks and B-doubles).

ARTC further submits that the strong performance of road is partly attributable to the failure of regulators to establish a full cost recovery pricing mechanism in the road sector; allowing operators to pass on inefficiently low prices to the market. This is discussed in greater detail in section 7 of this submission.

In relation to the general performance of structural separation, ARTC asserts that examining market share in isolation provides an incomplete picture. Prior to the reforms the rail industry was characterised by chronically unprofitable above and below rail operations. Upon commencement of the reforms, National Rail and ARTC took ownership of unprofitable and dilapidated assets and have turned them into sustainable businesses with positive operating cash flows. Infrastructure investments since reform have, for instance, allowed train operators to benefit from the economics of heavier and longer trains. The reforms have undoubtedly delivered an improved rail asset. It is disappointing that rail industry participants have chosen to portray the reforms in a negative manner.

5.3 Coal Network

ARTC manages the Hunter Valley coal network, connecting coal mines in the Hunter Valley and Gunnedah coal basins to the port of Newcastle, under an open access vertically separated model.

ARTC is aware of industry submissions calling for the vertical integration of the NSW [Hunter Valley] coal supply chain. Proponents of a shift to structural integration point to the vertically integrated iron ore supply chains of the Pilbara and the coal networks of Central Queensland as models of greater efficiency. The rationale is that integrated networks provide greater investment incentives and allow for economy of scope.

ARTC submits that, given its scope of operation, the Hunter Valley coal chain is not comparable to the Pilbara or Central Queensland supply chains. The Hunter Valley coal chain generates more than \$15 billion in export revenue annually. It's the largest coal supply chain in the world and requires over 14,000 train trips each year to transport coal from approximately 35 mines owned by 11 different operators to the port of Newcastle²⁸. There are four rail haulage providers delivering to three coal terminals. It would not be in the best interests of competition for one owner operator to determine the interests of the entire supply chain.

The HVCCC is an independent body responsible for ensuring the efficient movement of coal volume from mine to port and, over the longer term, assessing

²⁸ www.hvccc.com.au

the adequacy of the coal chain infrastructure to fulfil future export demand. By identifying capacity constraints, the HVCCC is able to develop and integrated capital investment plan to meet future coal export growth. The HVCCC includes all current Hunter Valley coal chain producers and service providers. This arrangement ensures that coal chain producers are able to harness the benefits of efficient price competition to compete in an aggressive global coal market. It is unlikely that such coordinated investment and price efficiency would exist under an integrated model, where one provider enjoys significant market power and competition is severely diminished.

As noted by Glencore in their submission to the Review:

'In every instance of monopoly coal infrastructure being sold into private ownership in the last 15 years there has been an associated significant increase in the cost of access to use that infrastructure arising from both the imposition of higher access charges and/or the reallocation of risk back to the users of that infrastructure.'

*These problems have arisen as a result of the failures of the regulatory regimes which have been imposed to fully deal with the problems which arise from natural monopoly infrastructure. The problems have arisen much more in Queensland than in New South Wales, since the rail track and port infrastructure in New South Wales currently remains user or Government owned.'*²⁹

Considering the scope of operation and importance of the Hunter Valley coal chain to the Australian economy, ARTC submits that vertical separation should be maintained in the Hunter Valley.

ARTC would also be concerned if a single operator attempted to use the Competition Policy Review as a vehicle to position itself to reduce regulatory impact on their business to obtain a commercial advantage over their competitors.

5.4 Grain Branch Lines

ARTC notes the Review Panel's finding that vertical integration may be preferable on low-volume rail lines and are aware of industry submissions to the Review calling for such action on grain branch lines.

The rationale behind a widespread shift to vertical integration of grain branch lines appears to be that structural integration creates efficiency of scope which allows for greater levels of investment.

ARTC notes this argument; however, we are not seeing evidence in the marketplace to support it.

It is important to understand that regional grain lines across Australia operate under a broad spectrum of competitive structures. Over the past 20 years, there have been major reforms to regional branch lines, which have resulted in:

- Vertical integration and privatisation of rail operations and regional grain infrastructure in South Australia, Victoria, and Western Australia and the

²⁹ Refer Table 3.

introduction of third party access regimes to enable above rail competition for grain haulage. Subsequent separation of rail operations from regional grain infrastructure in WA and Victoria, and the return of grain infrastructure to government control in Victoria.

- Vertical separation of the rail operations from the regional grain infrastructure in NSW, with privatisation of the contestable above rail operations, corporatisation of the monopoly infrastructure element, and the introduction of an open access regime to encourage competition.

In terms of investment, the reality is that across all grain lines and all jurisdictions, both vertically separated and vertically integrated, public and private, there is a chronic maintenance deficit. If private vertically integrated grain lines produce materially more efficient investment outcomes one would expect to see higher levels of investment in those jurisdictions that operate integrated rail lines. The reality is this has not occurred.

Revenue seeking operators under both market structures should respond to commercial opportunities in a similar way, in that operators in both structures seek to earn a commercial return on investment. The lack of investment under both market structures indicates that minimal investment is in fact the efficient scenario for operators, that is to say there is little possibility of commercial returns on grain branch lines in all jurisdictions.

ARTC acknowledge that under-investment on grain branch lines is an issue. The quality and capability of the infrastructure is a major impediment to the efficiency of rail operations across all jurisdictions. However, ARTC does not consider that structural arrangements per se (integration/separation) are a major driver of investment and service performance. Rather, the current under-investment and poor standard of branch line infrastructure results from a number of historic and economic realities such as:

1. - A history of under-investment - the present maintenance deficit is responsible for a situation where the cost to restore the lines to a reasonable service level is well over that which could achieve a viable economic return.
2. - Low and seasonal volume on many lines is insufficient to sustain economic return for the owner.
3. - A lack of road and rail infrastructure pricing transparency and equity - a failure to price road transport on a full cost-recovery basis.

In the end, market forces will dictate the most appropriate transport mechanism for the industry. It is the role of competition policy to provide a regulatory and investment framework that supports this. To this end, ARTC would support improved transparency and equity of modal infrastructure pricing and regulation in a manner that produces fair and efficient outcomes for the transport industry as a whole – discussed in greater detail in section 7 of this submission.

6 REGULATION OF GREENFIELDS RAIL PROJECTS

ARTC notes, in its submission, that Aurizon expressed a number of strong views in relation to how greenfields projects should be treated under competition legislation. Specifically, rather than exposing sunk capital to an ex-poste risk of declaration (and potential truncation of returns), governments should be able to determine access arrangements for greenfields projects before capital is invested.

Existing mechanisms such as investors and governments seeking to obtain ineligibility rulings (“access holidays”) or submitting voluntary access undertakings ahead of the investment are not particularly well suited to the task of promoting infrastructure development.

ARTC notes that Aurizon has been involved in a number of recent and future greenfields proposals and are likely to have substantial practical experience underpinning its views.

Nevertheless, ARTC is not convinced that the existing legislative framework (perhaps with some modification) cannot be applied in such a way as to address Aurizon’s concerns.

For example, under the NRAR suggested by ARTC in section 4.6 above, for greenfields rail projects to be covered by the NRAR, an independent national government appointed entity would determine the form of regulation to apply to that rail project, which would determine the relative light or heavy handedness of the applicable regulation (regulatory intensity).

The form of regulation determined would take into account the likely extent of market power, and incentives resulting from structural circumstances as prescribed by the NRAR.

For the greenfields rail infrastructure, the likely extent of market power and structural impacts could be informed by the circumstances surrounding existing rail infrastructure, which operates in a range of different markets and industry structures.

Following the form of regulation decision, investors in the greenfields rail project would have greater certainty in the knowledge of the regulatory intensity that would apply, and the extent to which a regulatory arrangement could be imposed by the regulator.

In the Draft Report, the Review Panel has proposed (if translated to the NRAR context) that a national access and pricing regulator should be responsible for both the decision on the form of regulation to apply and also act as the rail regulator. As indicated in section 4.6 above, it is ARTC’s view that it is important to separate the coverage/form of regulation decision-making function from the policy implementation and regulatory function.

7 DELIVERING ROAD/RAIL COMPETITIVE NEUTRALITY

7.1 Findings of the Competition Policy Review

The Draft Report is definitive in its finding on road pricing and investment reform:

*'Draft Recommendation 3 — Road transport Governments should introduce cost-reflective road pricing with the aid of new technologies, with pricing subject to independent oversight and linked to road construction, maintenance and safety.'*³⁰

In reaching *Draft Recommendation 3* it is clear that the Review Panel has recognised the strength of industry position on road pricing reform. The Draft Report references submissions and associated material from a variety of industry bodies:

- The Business Council of Australia (BCA) – advocate broad-based user charging as part of broader tax and funding reform.
- Aurizon – argue that a lack of competitive neutrality distorts modal choice to the detriment of supply chain efficiency.
- IPART – assert that lack of proper road pricing exacerbates congestion, which imposes greater costs on society and the economy than would an effective pricing mechanism.
- The Productivity Commission – a corporatised public road agency model is vital in delivering net benefits from funding and provision of roads.
- Infrastructure Partnerships Australia – rural and regional drivers will benefit most from cost-reflective direct road user charges.

It is encouraging that the Review Panel has considered the breadth of views and articulated the core issue of the road pricing reform debate:

*'More effective institutional arrangements are needed to promote efficient investment and usage of roads, and to put road transport on a similar footing to other infrastructure sectors. Lack of proper road pricing leads to inefficient road investment and distorts choices between transport modes, particularly between road and rail freight.'*³¹

ARTC welcomes the findings of the Draft Report and urges the Review Panel to strengthen *Draft Recommendation 3* in the final report by including a recommendation on the accelerated introduction of road pricing reform as a matter of priority for Government.

³⁰ Draft Report, p 28.

³¹ Ibid, p 24.

Recognising that *Draft Recommendation 3* explicitly relates to road pricing as a whole, the greatest productivity benefits will be achieved through improving the efficiency of the freight logistic supply chain. ARTC therefore asserts that any road pricing reform must commence with heavy vehicle charging and investment reform.

7.2 Competitive neutrality and capital investment

In its submission to the Issues Paper, Aurizon asserts that the current road pricing system is a key barrier to competitive neutrality in the land transport sector (page 75) and that this distorts investment signals (page 78).

ARTC is strongly supportive of Aurizon's position and note that Aurizon's submission on road pricing and investment reform is largely adopted from the rail freight industry submission to the Productivity Commission's Public Infrastructure Audit. Titled *Improving the Efficient Provision, Funding and Financing of National Road Infrastructure*, the submission was lodged in December 2013 by the Australasian Railway Association (**ARA**) on behalf of ARA, Asciano, Aurizon, and Australian Rail Track Corporation³².

The Review Panel accepts there is a lack of competitive neutrality in the land freight transport market and this is inhibiting an efficient mix of road and rail mode share, as well as leading to inefficient road investment³³. Beyond distorting efficient pricing and investment signals to the marketplace and government respectively, there are real consequences for commercial investment in freight rail infrastructure.

There are three factors that affect the capacity of rail to compete evenly with road; service availability, service reliability, and price. In markets where availability and reliability are fairly even, typically long haul, any artificial price advantage enjoyed by road will erode rail's capacity to compete in the short term and fund infrastructure improvements in the long term.

Rail operates on a commercial basis, where investment decisions are based on capacity to earn a commercial return on investment [Note: this is a key difference from the road sector]. Therefore, the short term inefficiency of the pricing framework has a compounding long-term effect as the capacity to earn a commercial return is diminished over time, and rail's ability to compete on service and reliability is restricted by the condition of capital.

This is clearly a perverse outcome that arising from a lack of competitive neutrality in the land transport market.

7.3 Accelerated Implementation

The Review Panel acknowledges that road pricing reform is a priority in the Draft Report:

³² http://www.pc.gov.au/__data/assets/pdf_file/0019/131635/sub056-infrastructure.pdf

³³ Draft Report, p24.

*'Reform of road pricing and provision should be a priority. Road reform is the least advanced of all transport modes and holds the greatest prospect for efficiency improvements, which are important for Australian productivity and amenity.'*³⁴

The finding of the Review Panel supports the position of the Productivity Commission taken in the draft report on Public Infrastructure that

*'The Commission supports the HVCI project and urges governments to draw on its advice as soon as possible to implement a reformed system of heavy vehicle charging.'*³⁵

ARTC asserts that the finding of the Review Panel should be strengthened and included as a recommendation or finding in the final report of the Competition Policy Review.

Ideally, the Review Panel would recommend that reform must commence with heavy vehicle charging and investment reform. As an interim measure, and to accelerate introduction, pricing reform should apply to articulated vehicles on the National Highway and State Arterial road network.

It is important that the Review Panel formally make this recommendation because:

- The conversation around heavy vehicle charging reform has progressed beyond the question of whether or not it is capable of delivering productivity benefits. The need for heavy charging reform is widely recognised³⁶. The conversation must now progress to how best to implement reform - a point that is recognised by the Review Panel in the Draft Report³⁷.
- A mass-distance-location charging model has been formulated by the Heavy Vehicle Charging and Investment Secretariat (**HVCI Secretariat**) that could be applied to articulated trucks travelling on the national highway network.
- Progress with heavy vehicle charging and investment reform has stalled with the closing of the HVCI Secretariat in June 2014, and there is a risk that the valuable work undertaken by HVCI Secretariat will be forgotten.

³⁴ Draft Report, p 135.

³⁵ Productivity Commission, Inquiry into Public Infrastructure, Draft Report, p131.]

³⁶ See:

- 1) Infrastructure Partnerships Australia (IPA) *Road Pricing and Transport Infrastructure Funding: Reform Pathways for Australia*, March 2014
- 2) Productivity Commission *Draft Report into Public Infrastructure* March 2014
- 3) Henry Tax Review *Section E3 Road transport taxes, Recommendations 62 and 64*, 2010
- 4) Australian Logistics Council *Submission to Productivity Commission Inquiry into Public Infrastructure* Submission 48, December 2013
- 5) Rod Sims, Chairman ACCC, Speech to 2014 ACCC/AER Regulatory Conference *Regulating for efficient infrastructure outcomes*, August 2014
- 6) National Commission of Audit *Towards Responsible Government, Recommendation 3, page 24*, March 2014

³⁷ Draft Report, p 35.

- A specific recommendation by the Review Panel would ensure that the productivity benefits of heavy vehicle charging reform are given the appropriate sense of urgency.
- A stated objective of the Competition Policy Review is to increase Australian GDP by at least 2.5 per cent a year. If this objective is to be achieved, government will be required to make real structural reform to competition policy and regulatory frameworks in the short term.
- Governments have a constrained capacity to fund infrastructure improvements from general budget revenue. Fiscal constraint, coupled with projections showing a doubling in the amount of freight to be carried on major road freight networks, indicate the need for investment reform is pressing.

ARTC asserts that heavy vehicle charging and investment reform is a critical initiative to drive productivity in the transport and logistics sector. This reform has been in development for 7 years and we believe that now is the right time for concrete actions to be taken toward its implementation, and that there should be an appropriate sense of urgency toward achieving the benefits it offers.

ACCESS REGULATION ON AUSTRALIAN RAIL NETWORKS

(Excerpt from the Aurizon submission)

Overview of rail economic regulation in Australia				
	Economic Regulator	Regulatory Instruments	Rail Access Provider	Primary use
Cth	Australian Competition and Consumer Commission (ACCC)	Competition and Consumer Act 2011 (Cth) Part IIIA and ARTC Interstate Access Undertaking	ARTC (Interstate)	Intermodal, grain, ores, steel
		Competition and Consumer Act 2011 (Cth) Part IIIA and ARTC Hunter Valley Access Undertaking	ARTC (Hunter Valley)	Coal
		Competition and Consumer Act 2011 (Cth) Part IIIA	BHP (Goldsworthy Railway)	Iron ore
		Competition and Consumer Act 2011 (Cth) Part IIIA, and Rail Company Act 2009	TasRail (Tasmanian Rail Network)	Intermodal, coal, ores
QLD	Queensland Competition Authority (QCA)	Queensland Competition Authority Act 1997 (Qld) and Aurizon Network Access Undertaking	Aurizon Network (Central Queensland Coal Network)	Coal
		Queensland Competition Authority Act 1997 (Qld) and Queensland Rail Access Undertaking and	Queensland Rail (Non-QCCN rail infrastructure in Queensland)	Passenger, coal, ores, intermodal, grain and cattle
NSW	Independent Pricing and Regulatory Tribunal (IPART)	Transport Administration Act 1998 (NSW) and NSW Rail Access Undertaking	John Holland (Country Regional Network)	Grain, ores, cotton
			Sydney Trains (Metropolitan Rail Network)	Passenger and intermodal
VIC	Essential Services Commission (ESC)	Rail Corporations Act 1996 (Vic)	V-line (regional Victoria) Vic Track (some yards and terminals in metropolitan Melbourne)	Passenger and intermodal
		Rail Management Act 1996 (Vic)	Metro Trains Melbourne (Metro Rail Network)	Passenger and intermodal
		Rail Corporations Act 1996 (Vic); South Dynon Access Arrangements	Asciano (South Dynon)	Intermodal
SA	Essential Services Commission of South Australia (ESCOSA)	Railways (Operations and Access) Act 1997 (SA)	Trans Adelaide, Genessee & Wyoming, Asciano, NRG Flinders, One Steel Ltd	Grain, gypsum, ores
		Australasia Railway (Third Party Access) Act 1999 (SA)	Genessee & Wyoming (Tarcoola to Darwin)	Intermodal, ores
NT	ESCOSA	Australasia Railway (Third Party Access) Act 1999 (NT)	Genessee & Wyoming (Tarcoola to Darwin)	Intermodal, ores
WA	Economic Regulation Authority (ERA)	Railways (Access) Act 1998 (WA) and Railways (Access) Code 2000 (WA)	Brookfield Rail (Brookfield Rail Network)	Grain, ores and intermodal
		Railways (Access) Act 1998 (WA) and Railways (Access) Code 2000 (WA)	The Pilbara Infrastructure (TPI) (Cloudbreak to Port Hedland)	Iron ore

KEY FEATURES OF THE NSWRAU³⁸

Pricing Principles

1. - Floor and Ceiling Test - Pricing must be negotiated such that:
 - a. - Access revenue from any access seeker must at least meet the direct cost imposed by that access seeker. In addition, for any sector or group of sectors, revenue from access seekers should, as an objective meet full incremental cost.
 - b. - For any access seeker, or group of access seekers, access revenue must not exceed the full economic cost of the sectors required on a stand-alone basis for the access seeker or group of access seekers.
2. - Regulatory Asset Base – The regulatory asset based commenced with an opening value approved by the NSW Minister for Transport in 2001, and is rolled forward to current valuation by the annual application of CPI, additions to the network, capital expenditure and depreciation. Assets are initially valued on the basis of Depreciated Optimised Replacement Cost.
3. - Capital Expenditure – Only capital expenditure that is prudently incurred and relates to coal traffic on a stand-alone basis is to be included. Prudency must have regard to minimum demand requirements over a five year period, and must be based on a prescribed consultation process where:
 - a. - The infrastructure owner must • work with access seekers to identify and prioritise network investments, and refine works programs, and formally evaluate significant future investments in consultation with access seekers;
 - b. - identify capital expenditure forecasts over a five year period;
 - c. - explain input to and outputs from evaluations;
 - d. - provide an assessment of the impact of the capital expenditure on the regulatory asset base; and
 - e. - establish a process for access seeker input.
4. - Depreciation – Depreciation is calculated on a straight line basis and based on the remaining mine life of coal mines using a sector. Remaining mine life was approved at 30 years in 2009 and is reviewed every five years.
5. - Rate of Return – Rate of Return is approved by the regulator every five years. Approved at 8% real, pre-tax in 2004.
6. - Compliance – The infrastructure owner is required to annually demonstrate compliance with the ceiling test and regulatory asset base roll-forward. The

³⁸ Definition of terms used can be found in the NSW Rail Access Undertaking pursuant to Schedule 6AA of the Transport Administration Act 1988 (NSW).

regulator is to publish findings. Any deviation around the maximum rate of return is to be managed through an unders and overs account established for each applicable access seeker.

Access Agreements

Any agreement must cover certain specified matters and conform to the pricing principles.

Arbitration

1. - The Independent Pricing and Regulatory Tribunal of NSW (IPART) is the arbitrator.
2. - IPART will also determine Rate of Return, estimated remaining mine life, and undertake compliance assessment.

Infrastructure Owner Obligations

1. - Provide access consistent with the undertaking.
2. - Use reasonable endeavours to accommodate access and new investment.
3. - Maintain passenger priority.
4. - Structure its accounts to facilitate effective dispute resolution, transparency and effective access.
5. - Separate accounts to below rail activities and other activities.
6. - Provide an information pack containing prescribed information to an access seeker.

Application

The infrastructure owner is not required to demonstrate compliance with the ceiling test or asset roll forward where it can be demonstrated to the regulators reasonable satisfaction that access revenue does not exceed more than 80% of full economic cost of the relevant network.