

# PACIFIC NATIONAL SUBMISSION TO ACCC



## RE: APPROVAL OF ARTC INTERSTATE ACCESS UNDERTAKING



---

## TABLE OF CONTENTS

1	EXECUTIVE SUMMARY	1
2	INTRODUCTION	2
2.1	This Submission	2
2.2	ARTC Consultation Process	2
3	RESPONSE TO ACCC QUESTIONS	3
3.1	Part 1: Preamble	3
3.2	Part 2: Scope & Administration	4
3.3	Part 3: Negotiation	8
3.4	Part 4: Pricing Principles	17
3.5	Part 5: Capacity Allocation	37
3.6	Part 6: Network Connections & Additions	39
3.7	Part 7: Network Transit Management	41
3.8	Part 8: Performance Indicators	42
3.9	Schedules	42
4	ISSUES NOT COVERED UNDER THE ISSUES PAPER	44
4.1	Relationship Of Undertaking To Proposed Hunter Valley Undertaking	44
4.2	Price Structure Change	47
4.3	Inappropriate Path Model	48
4.4	Insurance	49
4.5	Failure To Take A Whole Of Network Approach	49
4.6	Other Issues Not Covered In The Undertaking	51
4.7	Other Issues Relating To The IAA	53
APPENDIX A	DRAFTING ISSUES	54
APPENDIX B	FORM OF SEPARATE UNDERTAKINGS	60
APPENDIX C	LEGAL ADVICE REGARDING MORE THAN ONE UNDERTAKING APPLYING TO THE SAME INFRASTRUCTURE	65
APPENDIX D	DIFFERENT INFORMATION UNDER NSWRAU & THE UNDERTAKING	66
APPENDIX E	OBJECTIVES	68
APPENDIX F	INVESTMENT PROCESSES & CRITERIA	70
APPENDIX G	TRAIN PATH ALLOCATION PROCESS	74
APPENDIX H	ALTERNATIVE “USE IT OR LOSE IT” PROVISION	79
APPENDIX I	DRAFTING FOR EFFICIENT COSTS	81
APPENDIX J	RECOVERY FROM OPERATIONAL FAILURE	83
APPENDIX K	STORAGE OF ROLLINGSTOCK ON NETWORK	87

---

## TERMINOLOGY

The following abbreviations are used in this submission:

ACCC	Australian Competition & Consumer Commission
ARTC	Australian Rail Track Corporation
COAG	Council Of Australian Governments
DORC	Depreciated, optimised, replacement cost
GRV	Gross replacement value
GTK	gross tonne kilometres
HVU	The undertaking being proposed by ARTC to apply to the Hunter Valley region of NSW.
IAA	Indicative Access Agreement
IAC	Indicative Access Charge
IAP	Indicative Access Proposal
MFN	Metropolitan Freight Network
MUC	Model Undertaking – Coal (a model undertaking dealing specifically with Hunter Valley coal traffic)
MUG	Model Undertaking – General (a model undertaking for all ARTC traffics except for Hunter Valley coal).
NSWRAU	NSW Rail Access Undertaking
QCA	Queensland Competition Authority
SSFL	Southern Sydney Freight Line
U2002	The undertaking approved by the ACCC in 2002 to apply to the ARTC rail network.
Undertaking	The proposed undertaking that is the subject of the approval process by the ACCC to which this submission is addressed.

## 1 EXECUTIVE SUMMARY

The Undertaking will govern the relationship between ARTC and network users for the next 5 years for a substantial part of the ARTC network. It is therefore crucial that it is workable and effective.

ARTC has conducted a consultation process prior to submitting the Undertaking to the ACCC. Ideally this would have led to consensus on the majority of issues. Unfortunately this is not the case. Despite stakeholders having provided ARTC with submissions on two separate drafts, the Undertaking fails to address many issues raised.

This submission details many of these issues in detail, however, in summary the key areas of concern are:

- It is inappropriate for ACCC to approve the Undertaking in the absence of any detail as to how the interfaces with the proposed Hunter Valley undertaking will be managed. Pacific National has pointed out that the Undertaking leaves a number of significant interface issues unresolved.
- The definition of the network covered by the Undertaking is unclear and will result in a number of anomalies whereby the NSW Rail Access Undertaking (NSWRAU) will still apply to parts of the ARTC network (other than that intended to be covered under the proposed Hunter Valley undertaking).
- The Undertaking imposes a single path allocation model on all traffics that is inappropriate. The Undertaking needs to cater for the variety of business needs exhibited by the different traffics operating on the network. The issue has become significantly more important given ARTC's take over of the NSW interstate network and the broader variety of traffics operating on that track.
- The Undertaking does not contain an appropriate investment mechanism and seems directed towards managing an existing network of finite capacity rather than considering the future needs of access seekers.
- The inclusion of only one indicative access charge when this represents only a part of the traffic on the network is inappropriate. Pacific National is of the view that all currently proposed access charges should be included so that the ACCC has the opportunity to consider them.
- The radical restructure of access charges, both the indicative access charge (IAC) and those charges excluded from the Undertaking is unnecessary and will result in severe business consequences for network users.
- The increases in the indicative access charges are not justified and will impact negatively on traffic on rail in Australia.
- The revenue limits proposed in the Undertaking are inappropriate. Pacific National suggests that there is strong precedent for adopting the revenue limits in ARTC's current NSWRAU.
- The escalation proposal is inappropriate – it only covers the IAC, permits a full CPI increment, allows 'banking' for increases in future periods and allows an unlimited number of price rises in any year. Pacific National supports retention of the escalation arrangements in the previous undertaking (U2002) with the exception that this protection should be extended to all prices, not just the IAC.
- The proposed new excess network occupancy charge (ENOC) is conceptually flawed and is not supported by Pacific National.
- The lack of transition arrangements for the Southern Sydney Freight Line leaves network users exposed.
- The Undertaking fails to consider crucial interface issues with adjoining networks.

## 2 INTRODUCTION

### 2.1 THIS SUBMISSION

The Australian Competition & Consumer Commission (ACCC) published an Issues Paper seeking submissions regarding the ACCC's approval of the Australian Rail Track Corporation (ARTC) access undertaking (Undertaking).

This submission responds to the specific questions raised by the Issues Paper in Section 3.

In addition, there are a number of issues that Pacific National wishes to bring to the attention of the ACCC. These are discussed in Section 4.

Several themes underlie many of the comments in this submission that Pacific National wishes to draw to the ACCC's attention:

- As a general proposition, Pacific National believes that the intention of the relevant governments in giving much of the NSW rail network into the stewardship of ARTC did not include making network users worse off. On the basis of this proposition, Pacific National would oppose any charge or term in the Undertaking that would put access seekers in a worse position than they would have been had they remained under the NSWRAU.
- ARTC has been placed in a difficult position. Clearly it is operating as an arm of government policy,<sup>1</sup> yet it is required to operate under a "commercial" model for the provision of rail infrastructure that is intended to apply where normal economic rationales apply. As noted in the recent Productivity Report, rail infrastructure in Australia, generally, has very low returns and could not be considered a commercial proposition. In attempting to give credence to the commercial model, the Undertaking adopts positions (eg the approach pricing and investment) that are unhelpful to the long term interests of the rail freight industry.
- The Undertaking must be workable – Pacific National opposes any provision that does not meet this simple proposition.

### 2.2 ARTC CONSULTATION PROCESS

ARTC has provided industry with two discussion drafts of the Undertaking prior to seeking approval from the ACCC. This process is described in ARTC's Explanatory Guide accompanying the Undertaking.

Prima facie, this would seem to have been an excellent attempt to reach consensus and narrow matters of contention, thus speeding the approval process. Pacific National engaged in the consultation process in good faith, submitting two substantial submissions and also participating in two submissions made by the Freight Rail Operators' Group.

It is thus disappointing that, having set up a process to discuss the Undertaking and various alternatives, ARTC has failed to discuss or address the overwhelming majority of issues raised. While it is understandable that ARTC did not necessarily adopt all of the suggestions made by Pacific National and other stakeholders, it is inappropriate to seek input and then to fail to address issues raised by stakeholders in response.

---

<sup>1</sup> Examples that support this assertion:  
ARTC's only shareholder is the Commonwealth Government,  
ARTC has been massively funded by the Commonwealth Government for virtually all of the investment in the interstate network,  
ARTC was established to manage the granting of access to rail operators to the interstate rail network (Undertaking clause 1.1(a)). If the interstate rail network was a "commercial" proposition, the current government would have sold it to the private sector, as it has done with assets that were profitable such as the Commonwealth Bank and Telstra.

In order to further the debate and to provide a detailed consideration of many of the issues facing ARTC and network users, Pacific National provided to ARTC two complimentary model undertakings (the Model Undertaking – Coal applying to Hunter Valley coal traffic and the Model Undertaking – General for all other traffics on the ARTC network). The documents were crafted show a method of dealing with the significantly different Hunter Valley coal traffic without introducing unnecessary complexity and managing the interfaces appropriately. ARTC failed to even respond to these documents let alone engage in any debate about the merits thereof.

Therefore, Pacific National finds itself in the position that it has made every effort to engage in a constructive process with ARTC to achieve a balanced outcome for the benefit of the rail industry, but has been frustrated in its attempts to effectively contribute prior to consideration of the Undertaking by the ACCC. Clearly the better outcome would have been for ARTC to seek to minimise controversy prior to seeking ACCC approval of the Undertaking, but, having set up a mechanism to pursue this outcome, it has chosen not to engage in dialogue with stakeholders to resolve outstanding issues. Rather, ARTC has chosen to seek approval from the ACCC knowing that very substantial issues have been raised by key stakeholders which it has not addressed.

With this in mind, Pacific National sees the Undertaking as its only protection. Experience shows that once the Undertaking is approved, all parties will attempt to interpret it to their advantage. It is therefore crucial that the ACCC does not approve the Undertaking unless it;

- represents a genuine balance of the interests of the parties and the public interest, and
- is a genuinely workable document.

Pacific National does not believe the Undertaking meets either of these criteria. As will be seen through this submission, the document contains serious flaws that will make it both unbalanced and unworkable.

### **3 RESPONSE TO ACCC QUESTIONS**

#### **3.1 PART 1: PREAMBLE**

- 1) “Does the Undertaking provide sufficient clarity about the broad approach to negotiating access and the proposed terms and conditions of access?”

Yes. While this submission outlines a number of deficiencies (see response to Question 2), the Undertaking provides a clear process for negotiation of an access agreement. Similarly, while there are a number of issues associated with the indicative access agreement (IAA), the Undertaking and negotiation process are materially improved by having such an agreement included compared to no such document being provided.

- 2) “Does the Undertaking provide the basis for outcomes that balance the interests of ARTC, potential access seekers and the public interest?”

No. This submission outlines a number of areas where the balance of interests is inappropriately catered for. As these are dealt with in detail elsewhere, they are not repeated in response to this question. However, the following list demonstrates some of the broad areas of concern:

- Exclusion of a significant part of the network without any indication of how the Undertaking will interact with the excluded network.<sup>2</sup>
- Pricing quantum.
- Pricing structure.
- Prices excluded from the Undertaking.
- Lack of effective stakeholder input to the investment process.
- No recognition of the system wide nature of the product on offer.
- Lack of effective operational processes such as path allocation and possessions planning.
- No recognition that different traffics require different types of train path.

3) “Is there sufficient clarity about the tracks and other infrastructure that the Undertaking applies to now and will apply to during the term of the Undertaking?”

Yes. The Undertaking clearly identifies the tracks and facilities to which it applies. This submission details concerns that the scope of coverage will lead to inefficient outcomes. (See response to Question 4).

### 3.2 PART 2: SCOPE & ADMINISTRATION

4) “Is the scope of the Undertaking sufficient to cover all the facilities necessary for effective access?”

ARTC has been given a difficult task in attempting to achieve efficient regulation for its expanded network. To Pacific National’s knowledge, all parties are in agreement that the NSW Hunter Valley rail network and the coal traffic that is the main activity on that network has substantially different characteristics to the remainder of ARTC’s interstate network; sufficient that separate regulatory arrangements should apply. The difficulty lies in providing separate arrangements for Hunter Valley coal traffic that do not introduce inefficiencies.

Currently the Hunter Valley coal traffic is regulated under the NSW Rail Access Undertaking (NSWRAU) as are all other rail traffics in New South Wales. The high level nature of that document means that there is no real difficulty in accommodating all rail traffics within its scope, regardless of their characteristics. The NSWRAU was originally a State based access regime and, as such, operated within a different framework to that intended for the ARTC network.

The proposed Undertaking is a document of a different nature that is substantially more detailed and specific. Pacific National agrees that this level of detail and specificity is appropriate. However, this means that the flexibility under the current arrangements will not be available under the proposed Undertaking.

Pacific National agrees that it is appropriate that a separate regulatory document is required to cover the Hunter Valley coal traffic (referred to in this submission as the HVU). However, Pacific National disagrees with the formulation used by ARTC in the Undertaking to achieve this outcome. Pacific National has proposed that the most efficient and effective way to address the issue is to have both a geographic and traffic specific separation of the undertaking for the Hunter Valley coal traffic. The form proposed by ARTC based solely on a geographic split is ineffective and will lead to significant administrative inefficiency and difficulty. This issue is discussed in more detail in Section 4.1 of this submission.

<sup>2</sup> Pacific National is aware that ARTC intends to put forward a Northern NSW network undertaking to cover the Hunter Valley coal and other traffics, but despite repeated stakeholder requests, ARTC has given no details of how it intends this undertaking to operate, nor how it will interact with the Undertaking.

As a separate issue, the Undertaking fails to cover a number of facilities, principally sidings, that are required by train operators for the storage of rollingstock and other incidental operations. These facilities are currently covered by the NSWRAU and presumably would continue to be so covered in the event that the Undertaking fails to provide adequate coverage. This would result in requiring a separate access agreement to be entered into by the access seeker under a different regulatory structure. This is clearly contrary to the stated intention of the Council Of Australian Governments (COAG) that rail access regulation should be streamlined and harmonised.<sup>3</sup> The preferred outcome would be that the Undertaking provides appropriate coverage of these facilities and also provides explicitly for the service provided by them, including rollingstock storage. (See further discussion in Section 4.6)

- 5) “Is the Undertaking sufficiently clear about the difference between extensions to the network and expansions to the network’s capacity?”

Yes.

- 6) “Is the proposed term for the Undertaking appropriate, given the nature of the services covered by the Undertaking and of the industry more generally?”

The term is not unreasonable. However, a 10 year term is more appropriate and consistent with other capital intensive infrastructure such as gas pipeline access undertakings.

An issue that appears to have received little consideration is the potential problems that may arise through a mismatch between contracts and undertakings over time. For example a contract that extends beyond the Undertaking might have inconsistencies with any following undertaking when it comes into force. In some circumstances such inconsistencies may not have any significant impact on the workings of the following undertaking, but in others, consistency might be crucial.

An example of the problems that can arise was demonstrated in the difficulties in moving from a price cap to a revenue cap in the current QR Access Undertaking. In order to accommodate existing contracts under the new arrangements, a convoluted series of provisions was required to be put in place. These provisions will inevitably raise administrative difficulties and potentially deter competition as operators attempt to work through the implications of these complexities in what ought to be a relatively straightforward issue.

While it is true that, under the Undertaking, ARTC has indicated a willingness to enter into contracts that extend beyond the Undertaking, the potential exists for such problems to arise and the shorter the term of the Undertaking, the more likely that there will be contracts that extend beyond its term. As it is impossible to know what the difficulties might (or might not) arise concerning incompatibility, it would be prudent for the Undertaking to take the possibility into account. Pacific National’s preferred outcome would be:

- a longer term, more in tune with likely contract lengths (ie 10 years), and
- a provision that requires the parties to any contract originating under a previous undertaking to negotiate in good faith to remove the effect of any inconsistency.

Given the length of any process for approval of an undertaking, a further issue that is likely to occur each time an undertaking expires is that it may elapse prior to a replacement being put in place. This is disruptive to the industry and raises

<sup>3</sup> The February 2006 COAG Communiqué Attachment B, Appendix E at clause 3.1 provides that the signatories agree to “implement a simpler and consistent national system of rail access regulation, using the Australian Rail Track Corporation access undertaking to the Australian Competition and Consumer Commission as a model ...”

considerable uncertainty. It is therefore suggested that the Undertaking should address this issue through the insertion of an obligation on ARTC to seek approval for an extension of the undertaking from the ACCC in circumstances where a replacement will not be approved prior to its expiry.

Clearly this would not be appropriate in the circumstance where there is an intention not to have an undertaking at all, however, where the intention is that a new undertaking will replace an existing one then it is reasonable to extend the existing provisions, provided that this is not seen as giving an incentive to delay the introduction of a new undertaking. As the extension would be subject to the approval of the ACCC, this should not be an issue as the ACCC will have the opportunity to assess the benefits of extension against any negatives that might result. Given the intended "model" status of the ARTC undertaking,<sup>4</sup> PN regards this as an important improvement over the U2002.

- 7) "Is there sufficient clarity about how the Undertaking will extend to the Southern Sydney Freight Line?"
- 8) "Are the arrangements in the Undertaking related to the new Line appropriate?"

Questions 7 and 8 are answered together.

Pacific National understand the reason for the inclusion of the Southern Sydney Freight Line (SSFL) in the Undertaking. However, there is no clarity as to how ARTC intends to extend the Undertaking beyond the bland statement (in clause 2.1(c)) that the Undertaking will include that line when it is constructed. It is assumed, from the wording of the clause, that ARTC does not intend to seek approval separately from the ACCC to cover this extension.

Substantially more is required to make this provision effective, especially if ARTC is seeking approval from the ACCC in advance.

There is no indication from ARTC as to how it intends for the transition of current access arrangements with RailCorp to happen. The SSFL may be a new line, but it will be providing a corridor through southern Sydney as a compulsory alternative for existing movements on existing RailCorp track. It is therefore essential that existing access rights are transferred rather than merely being truncated through the abandonment by one track owner to be taken up (or not) on an indeterminate basis by the new track owner. PN is acutely aware that the current owner of the relevant corridor, RailCorp, is seeking to include provisions in access agreements to excise the SSFL (and the wider metropolitan freight network) and any rights to use relevant train paths once those lines are taken over by ARTC. This leaves access seekers in "no-man's land" without any contractual rights at all as there is no corresponding obligation on ARTC to accept an assignment of the excised provisions.

To remedy this, ARTC should provide in the Undertaking a commitment to accept an assignment of any rights excised from RailCorp agreements due to the transfer and, where it is necessary to modify such rights (eg to accommodate necessary realignment of timetables or pricing), appropriate negotiation provisions that recognise existing rights.

#### **Exclusion Of Other Extensions**

Further, it is Pacific National's understanding that ARTC intends to have transferred not merely the SSFL itself, but also a number of other Sydney freight lines as part of the arrangement. RailCorp refers to these lines as the Metropolitan Freight Network (MFN).

---

<sup>4</sup> See footnote 3.

Clearly the SSFL and the MFN would both fall into the classification of “extensions” to the ARTC network. The exclusion of extensions to the network other than the SSFL in the Undertaking therefore appears to be an odd approach. There seems little logic to include one part of the Sydney package while excluding others. If this is allowed to happen it is likely to place operators in an intolerable situation with parts of the network included in the Undertaking while other parts are excluded, but no longer part of the RailCorp network. Presumably this would require separate access agreements as one would be required to be under the Undertaking while the other would be governed by the NSWRAU – an absurdity. If this just a mismatch in definitions, then ARTC needs to amend the Undertaking to rectify the matter. If it is intentional, then ARTC would need to provide a convincing explanation for it and show a very clear path for operators to gain access to the various parts of the network.

Pacific National is aware that ARTC currently has an application before the NSW Government to acquire the rail line north of Werris Creek to Narrabri. No mention is made of this line nor how ARTC would intend to have it regulated. If ARTC can anticipate one extension to the network, why does it not also anticipate this extension? It is recognised that ARTC might seek to cover that line through the, as yet unseen HVU, but if that is the case then it further dilutes the “coal” specific nature of that document. At the very least ARTC should clarify its intentions in this regard.

- 9) “Are there any aspects of the Undertaking that should be taken into account in considering the objects section 44AA(b), dealing with “a consistent approach to access regulation in each industry?”

Pacific National regards the purpose of section 44AA(b) of the *Trade Practices Act* as aspirational.<sup>5</sup> As such, it is appropriate that the legislature point to the desirability of having consistency in access regulation within an industry. To the extent that the issues needing to be dealt with are the same, it is appropriate that the access arrangements are consistent. However, where the issues diverge, it would be a mistake to attempt to apply a uniform approach as this will inevitably sub-optimize the result to the extent of the divergence. Uniformity, while yielding substantial benefits in some situations, is not universally a good thing.

The matter is more complex in the rail industry given that there are numerous State based regulatory regimes. COAG has required all State based regimes to be submitted to the National Competition Council for determination as “effective”, however there is a limit to which Part IIIA of the *Trade Practices Act* can influence a consistent approach – this is more likely to be effectively managed through the COAG process.

With this in mind, Pacific National does not have a strong view that the Undertaking either supports or detracts from the intent of section 44AA(b), but Pacific National does support the intention of ARTC to have separate access arrangements apply to Hunter Valley coal traffic.

---

<sup>5</sup> The section is clearly setting out the purpose towards which Part IIIA is directed, but does not, by itself, compel any outcome.

**3.3 PART 3: NEGOTIATION****3.3.1 PROVISION OF INFORMATION**

- 10) “Is the information that ARTC commits to provide to an access seeker sufficient/appropriate to enable meaningful access negotiations?”

Generally speaking, the information nominated by ARTC is helpful to an access seeker. It is noted that the information is less comprehensive than the information required to be provided under the NSWRAU.<sup>6</sup>

The NSWRAU provides for substantially more information, of greater detail, than that provided for under the Undertaking. Thus to accept the position in the Undertaking for NSW would result in a substantial reduction in the information available to access seekers. Pacific National does not support such a reduction in the availability of information. Appendix D sets out a comparison of the information required to be made available under the NSWRAU and the Undertaking.

**3.3.2 PARTIES TO NEGOTIATION.**

- 11) “Is the Undertaking sufficiently clear about the processes for the initial phase of negotiations?”

The Undertaking provides a clear process.

While it is not a matter of great practical concern, it is noted that the requirement for an application to be in the form required in Schedule A is overly bureaucratic given that Schedule A adds no real value. Accordingly Pacific National suggests that Schedule A be removed.

- 12) “Do these processes balance the interests of the access provider and access seekers?”

The process is reasonably balanced and Pacific National has found it to be workable under the U2002.

- 13) “Are the prudential and financial criteria that ARTC intends to use to “screen” applicants appropriate?”

**Default History**

The undertaking (clause 3.4(d)(ii)) allows ARTC to refuse to deal with a party that is in material default on any access contract regardless of whether such a contract is with ARTC or not. This extends to parties related to the access seeker.

It is recognised that this is not a new clause, however, PN’s objections to this have been long standing and remain today. Given that this part of the Undertaking relates to ARTC’s obligation to negotiate with the access seeker (ie a bi-lateral negotiation) it seems inappropriate to bring in that party’s dealing with other access providers. A material default under another contract may arise for any number of reasons and could certainly include matters other than those of a prudential nature (eg defaults on operational matters). Further, a material default under an unrelated contract may arise through prudential issues that are not germane to whether the party is able to sustain obligations under a contract with ARTC (eg the default might arise under a dispute between the parties due to the specific provisions of the contract that have nothing to do with the party’s willingness and ability to pay its debts). A blanket discretion to ARTC to avoid negotiation is inappropriate.

<sup>6</sup> See NSW Rail Access Undertaking Schedule 5.

It is also unclear why ARTC should be able to bring related parties into this rubric. There does not appear, prima facie, to be any absolute nexus between related parties such that it should influence the prudential requirements, particularly given the broad scope of the term 'related party'. If ARTC is to retain this right it should provide a comprehensive justification for doing so. Pacific National accepts that ARTC should be able to avoid negotiation with a party that has materially defaulted with ARTC within the previous two year period, but the extension to other parties is inappropriate. As an example of the problems with the way the Undertaking deals with this issue, in the past two years, Pacific National has been related to Toll and Patrick but is now belongs to new and separate entity, Asciano. Under the Asciano umbrella, Pacific National and Patrick Rail are separate entities but also related parties. If Pacific National defaults, should this prevent Patrick Rail from negotiating an agreement? Should Toll, no longer a related party, but having been one within the previous two years, be prevented from rail access? The provision is altogether too broad and unnecessarily discretionary.

As drafted, there is a circularity to clause 3.4(d)(ii) as it refers to a "Material Default" which is defined by reference to the matters in this clause.

#### **Financial Adequacy**

Clause 3.4(d)(iii) is a new clause in the Undertaking. It requires any applicant for access to be able to demonstrate an ability to meet its liabilities under an access agreement. The need for this addition has not been adequately explained by ARTC in its Explanatory Guide. It is unclear why such an obligation should be placed on an access seeker over and above the existing protections available to ARTC through the current solvency requirements.

Even if such a protection is necessary, the Undertaking ought to specify the test which ARTC will apply to determine whether the criteria has been met. Without more, it seems an impossible task to demonstrate that one will be able to meet future liabilities except by placing the funds in escrow – clearly an absurd requirement. If what is meant is some form of current financial adequacy test, then this ought to be explicitly stated. However, Pacific National suggests that such an approach is itself flawed, in that it may well be that the applicant is reliant on obtaining access to the rail network in order to secure rail transport business, which in turn would fund the access charges. Clearly this would be a deterrent to any new entrant to the business. In such a situation ARTC would be denying access to a party contrary to own its stated objectives in clauses 1.2(c)(i)(C), 1.2(c)(ii)(A), 1.2(c)(ii)(C) and 1.2(c)(iii)(B).

- 14) "Is there sufficient clarity about the standards that ARTC intends to use to decide whether an applicant meets the prudential criteria?"

No. Apart from the definition of "Solvent", the undertaking is lacking in any objective standards. In the absence of objective standards ARTC has wide discretion as to how it applies the prudential provisions in the Undertaking. Such discretion is inappropriate where it has the potential to deny access to an access seeker.

- 15) "Does the Undertaking provide ARTC an appropriate level of discretion in applying the prudential criteria?"

See also answer to Question 14 above.

It is noted that clause 3.4(f) provides for arbitration if ARTC refuses to negotiate, and in clause 3.4(g) for ARTC to seek arbitration where it believes an application is frivolous. In Pacific National's view these processes, in both instances are cumbersome and could be streamlined to provide a superior outcome. While in concept the availability of arbitration provides a process whereby negotiation for access can be mandated despite ARTC's contrary decision, in practice this would be

unlikely to provide an access seeker with much comfort. Arbitration is a slow, uncertain and costly process and unsuited to merely gaining a right to negotiate – few business opportunities would be so attractive or so persistent<sup>7</sup> as to warrant taking this path. Similarly it seems excessive to make ARTC seek an arbitration to avoid a frivolous application. Pacific National suggests that this involves unnecessary expense and consumption of ARTC’s scarce management resources which would be better spent managing the network.

Pacific National suggests that a better alternative would be for ARTC to make the following changes:

remove clauses 3.4(f) and (g)

include a new clause as follows:

“3.4([x]) Notwithstanding any rights accorded to ARTC in clauses 3.4(a) – 3.4(d), ARTC undertakes not to unreasonably refuse to commence or continue to negotiate with an Applicant, nor to engage in conduct for the purpose of preventing or hindering an Applicant’s access to the Network for the purpose of operating Services.”

Note that the suggested drafting includes the anti-hindrane provision suggested in section 44ZZA of the *Trade Practices Act*.

As the dispute resolution clause 3.12.1(a) provides for any dispute to be raised, this does not prevent either party seeking to invoke those provisions, thereby safeguarding the ultimate opportunity to seek arbitration, but it removes the specific obligation to do so to resolve the matter.

- 16) “Does the Undertaking provide adequate detail on what is expected of an Accredited Operator?”

It is noted that the Undertaking specifically provides for negotiation with a party that is not an Accredited Operator but it does provide that ARTC will negotiate with a party that is accredited. It is assumed that ARTC believes that it is unnecessary to state the latter, but to a lay reader, it could be interpreted that while there is no prohibition to negotiate with an Accredited Operator, there is no obligation to do so either. It would be helpful for the Undertaking to make the obligation explicit for the benefit of clarity.

Not strictly within the confines of this question is the matter of notice to the access seeker under clause 3.4(e). This allows for two weeks to inform the access seeker of the refusal to negotiate. Given that the time limit only commences from the date when the decision is made, this seems an unreasonable delay to inform a party that ARTC is not going to negotiate. A decision to refuse to negotiate is likely to have serious consequences for the rebuffed access seeker and should be made with the utmost expediency. Pacific National believes that 5 business days provides ample time for such advice to be provided.

### 3.3.3 INDICATIVE ACCESS PROPOSAL

- 17) “Does the Indicative Access Proposal contain sufficient information and details to enable the access seeker to adequately evaluate the proposal?”

Yes, the Indicative Access Proposal (IAP) contains an appropriate level of information.

However, Pacific National is concerned at the length of time provided for ARTC to respond. Clause 3.8(a) provides for the IAP be provided within 30 Business Days. Many proposals ought to be able to finalised quickly and 20 Business Days allows a

<sup>7</sup> Any access seeker that chose to seek arbitration would need to have confidence that the business opportunity that caused it to seek access in the first place will still be available once the arbitration (and subsequent negotiation of an access agreement) is concluded. Given an arbitration will take between 6 and 12 months and potentially longer, the number of opportunities that meet this criteria are likely to be few.

full 4 weeks to achieve this. Where an IAP would take longer can be covered by the qualification in clause 3.8(b), but this should be the exception. As the exception is already provided for, there is no need for the base provision to be padded out to cater for more difficult applications. Note that the QR Access Undertaking and WA Rail Access Code both allow for 30 days (equivalent to 22 Business Days) to provide an IAP.

Similarly other time-frames in the negotiation process should be reduced to 20 Business Days. While there may be complex issues involved, either party ought to be in a position to address these within a month eg, responding as to whether the party wishes to proceed. The current time frames can make an access application process unnecessarily lengthy.

It is also noted that clause 3.8(e) allowing the access seeker to seek arbitration if ARTC is not progressing an application fast enough is effectively redundant:

It is difficult to imagine how the applicant would know whether ARTC is not making reasonable progress in the preparation of the proposal, particularly a new entrant that was not au fait with rail access arrangements (again a block to market entry).

If the applicant formed the view anyway that progress was not being made, (recalling that 30 business days have already elapsed, and probably substantially more than this if clause 3.8(b) has been invoked) it is absurd to imagine that arbitration would provide a useful remedy.

If there is a genuine intent to provide a workable remedy for the applicant, something far more direct would be required, including some method whereby the applicant could reliably form a view as to what progress was being made.

As discussed elsewhere in this submission, given that clause 3.12.1(a) provides that all disputes are to be resolved in accordance with the dispute resolution mechanism it appears unnecessary to have specific clauses such as clause 3.8(e) expressly provide for dispute resolution. Providing such specific clauses merely creates confusion and adds unnecessary verbosity to the Undertaking. For example, does clause 3.8(e) prevent the dispute resolution process being invoked prior to the access seeker forming a view that ARTC has not made reasonable progress? If not why bother with clause 3.8(e)? This is discussed further in Section 3.3.5.

#### **Revision Of Standard Terms & Conditions**

Clause 3.8(c)(iv) suggests that ARTC's standard terms and conditions can be amended "from time to time" which seems to suggest that these might be modified at ARTC's discretion. This appears to be at odds with the concept of including the IAA as Schedule D to the Undertaking which, presumably, would require a formal acceptance by the ACCC of any amendments. This could potentially allow ARTC, at its discretion, to undermine significant parts of the approved IAA thereby undermining the Undertaking process itself.

Notwithstanding the above, clause 3.8(c)(iv) is redundant,<sup>8</sup> given the standard terms and conditions form part of the undertaking which, under clause 2.6(b)(v) is required to be published on ARTC's website already.

- 18) "Does the Indicative Access Proposal provide an adequate basis for meaningful negotiations?"

The concept of an IAP is useful and could provide an appropriate basis for negotiation of an access agreement. Unfortunately, clause 3.8(d) of the Undertaking allows ARTC to avoid any obligation to provide access in accordance with the terms and conditions contained in the IAP. This seems to undermine the whole point of having an IAP. If ARTC is not willing to offer those terms, why would it provide them in the IAP?

<sup>8</sup> accept for the gratuitous amendment wording.

The relationship of clause 3.8(d) and the obligation in clause 3.11(b) is also unclear – does ARTC intend that the proposal might contain terms that are inconsistent with the Indicative Access Agreement (IAA)? If so, presumably this would have only arisen through the request of the applicant and therefore the proposal must reflect something that ARTC is willing to offer (otherwise why offer something ARTC was not willing to provide)?

### 3.3.4 NEGOTIATION

- 19) “Does the Undertaking provide sufficient detail about how ARTC intends to negotiate on access?”

Yes.

#### Party To Agreement

Clause 3.11(a) provides for an accredited operator, a non-accredited operator or both to be parties to the access agreement. Pacific National suggests that it is unnecessary to contemplate tri-partite arrangements. A tri-partite agreement for access would blur accountabilities and would be counter-productive. It is suggested that all that is necessary is that a party to the agreement agrees as a condition that the train services will be operated by an accredited operator. How that is achieved is a matter for the applicant and all that ARTC ought to be concerned with is that the contracting party fulfils its obligations that the operator is accredited.

- 20) “Does the negotiation process achieve an acceptable balance among the interests of ARTC and access seekers?”

The process is appropriate, though Pacific National believes that a number of the provisions within the Undertaking do not provide an appropriate balance. These are discussed throughout this submission.

- 21) “Is there sufficient clarity and transparency about the method that ARTC proposes to use for choosing among competing access applications?”

No. The process proposed is opaque. The process contemplates two (or more) access seekers negotiating in a blind race with each other to offer ARTC the most valuable proposition, presumably without any understanding of the other party’s position. This does not appear to be to the advantage of any access seeker and seems to be directed solely to the benefit of ARTC rather than achieving the best outcome for use of the network.

Pacific National has proposed a series of criteria to ARTC for determining such a conflict in the best interests of rail transport as a whole. These criteria are included in this submission at Appendix G paragraph 1.4.

- 22) “Is there sufficient clarity about the instances in which ARTC can cease negotiations?”

- 23) “Is the level of discretion allowed to ARTC to cease negotiations appropriate?”

Questions 22 and 23 are answered together.

Clause 3.10(b)(iii) provides for negotiations to cease after 3 months unless the parties agree to extend them. Pacific National asked ARTC to explain its expectations as to what would occur in the situation where the access seeker wished to extend the negotiations but ARTC did not – would this, for example, require the access seeker to submit a fresh application for an IAP? Unfortunately, ARTC has not explained its position in this regard.

On its face, it is rather curious that ARTC might seek to terminate negotiations under any circumstances not already covered by the other provisions of clause 3.10. It is far from clear the mischief that is intended to be overcome by this provision.

Clause 3.10(b)(vi) appears incomplete in that it provides for ARTC to give notice to the applicant of an intent to cease negotiations due to evidence of failure to meet the prudential requirements, but does not provide an opportunity for the applicant to provide ARTC with reasonable evidence to the contrary. There is no standard provided by which ARTC will form its judgement and the level of evidence might be very slight, even unsubstantiated rumour. It is inappropriate to leave this to ARTC's discretion without having given the applicant the opportunity to respond. Procedural fairness would require at least that much and it does appear to add greatly to ARTC's costs that such a process would be required – this would be far less onerous than undertaking an arbitration which would be the other recourse open to the applicant.

- 24) “Do operators have sufficient certainty about prospects for the long-term utilisation of the network and their on-going access to train paths when re-negotiating existing train schedules?”

Freight train operators service a number of markets and market segments with differing characteristics. In some markets operators have confidence of long term prospects for viable business (assuming that they are not forced out of the market through input hikes). In other market segments, operators have much less confidence of on-going business. A case in hand is the Sydney – Brisbane freight corridor where, despite substantial government grants for the upgrading of the network, there is by no means any certainty that operators will be able to profitably supply train services into the future. It is therefore fair to suggest that there is no simple response to first part of the question regarding long-term utilisation of the network. In some ways the closeness of the linkages between above and below rail activities make it impossible to answer such a question in isolation – the future of both is dependent on the actions of the other.

The second part of the question must be firmly answered in the negative. The Undertaking and the accompanying IAA provide no certainty at all about the availability of train paths beyond the specific contract entered into.

Under the U2002, access seekers had the opportunity to nominate existing train paths for continuation under a new access contract. This was known as “grandfathering” or “roll-over” of train paths. Some concerns have been expressed regarding the appropriateness of the U2002 provision on the ground that it erected a barrier to entry, but these arguments fail to take into account the effectiveness of the “use it or lose it” provisions. These serve to prevent the hoarding of capacity, and combined with the “take or pay” components of the access charge would make it very difficult for a party to attempt to secure paths for which it did not have a genuine need.

In the new Undertaking, the provision contained in the IAA at clause 2.9 for long-term train paths superficially has the appearance of retaining these arrangements, but the provision has been so completely altered so that it no longer serves any useful purpose.

The obligation on ARTC to roll-over paths from one contract to the next appears to have the intention of requiring the applicant to seek to roll-over all of its train paths, not just a sub-set, although it is arguable that this could be interpreted differently – unfortunately ARTC chose not to provide clarification of its intent when this was raised during the “consultation” process. Under the U2002 IAA, the roll-over provision clearly applied to individual train paths. This new requirement therefore appears to be deliberate and puts the process in a different sphere as it is almost inevitable that a train operator, at the time of renewal of its access contract, would seek to modify at least some of its train path requirements to better suit its business needs even if only through minor modifications. The formulation as proposed by ARTC, would require

the operator to choose between the benefit of the rolling-over all paths or modifying its business to meet its needs and losing the protection supposedly afforded by the roll-over provisions.

Notwithstanding the above appearance at having a roll-over provision, the Explanatory Guide makes it quite clear that ARTC intends for paths not to be rolled over at all under the new Undertaking as the following extract shows:

“The previous indicative agreement enabled an Operator to ‘lock in’ paths indefinitely (known colloquially as ‘grandfathering rights’). As a result of the amendment, paths entitlements will not exceed the term of the access agreement.”<sup>9</sup>

This is given effect through the IAA at clause 2.9(c) that provides that “ARTC may consent to the renewal” of train paths. This is a substantial reduction in obligation from the previous commitment “ARTC will not unreasonably withhold its consent to the renewal” in clause 2.8(c) of the U2002 indicative access agreement. The effect is to remove any certainty to operators through the mechanism of long-term paths as the allocation of the paths is totally at the discretion of ARTC. In fact it is now a fatuous statement – ARTC may consent to any arrangement it pleases, so long as it does not contravene the Undertaking, so in this form the provision might as well be removed altogether. Such an action would at least have the merit of being forthright.

The roll-over of long-term train paths is very important to train operators to provide some certainty that they will have continuity of train paths. The effective removal of such a key provision will have significant consequences for operators when making investment decisions in long lived assets such as rollingstock.

The use of a roll-over arrangement in the U2002 was an attempt to address the underlying problem of a scarcity of desirable train paths to meet demand at the time of recontracting. It is not the only solution to that problem. Train operators would have little concern if they had confidence that sufficient capacity, of an appropriate quality, would be available when it was required. An alternative way to address the problem is for the Undertaking to;

- a) Provide an objective and transparent process for the allocation of train paths. The rail industry in Australia has not collectively attempted to define such a process and the Undertaking provides an ideal opportunity for ARTC to work closely with train operators to address this issue. A suggested train path allocation process is provided at Appendix G.<sup>10</sup>
- b) Include a commitment by ARTC to genuinely seek to provide capacity where and when required by, and in genuine consultation with, the market.<sup>11</sup>

As the Undertaking does not provide such an alternative mechanism, train operators are left with no certainty regarding the long term availability of capacity under the Undertaking.

- 25) “Does ARTC have sufficient flexibility when re-negotiating existing contracts to encourage above rail competition?”

On a conceptual level, Pacific National suggests that ARTC’s role is not to “encourage competition” in the sense that ARTC should deliberately seek to introduce additional train operators into the market. To do this would require ARTC to offer incentives to new operators and this would necessarily mean that ARTC would bias the market in

<sup>9</sup> Explanatory Guide, ARTC p 30

<sup>10</sup> Unfortunately, as with other areas of “consultation”, ARTC has chosen not to engage in any discussion on this issue.

<sup>11</sup> Unfortunately the Undertaking does not address investment on this basis. While it is recognised that the uneconomic nature of rail infrastructure means that the normal market mechanisms do not operate, this should not relieve ARTC of the obligation to seek to provide capacity in its role as steward of a vital part of the country’s infrastructure.

favour of new entrants and undermine efficiency. The Undertaking does not seek to do this. Instead the Undertaking is designed to facilitate competition. If the ACCC's question is directed to encouragement of competition by the Undertaking setting out a level playing field, a framework within which the market can determine the number and scope of train operator activities, then Pacific National would agree that the Undertaking is well constructed to achieve that outcome.

ARTC has extensive flexibility in renegotiating existing contracts within the confines of the Undertaking. The Undertaking effectively sees any "renegotiation" of an access agreement as a new agreement and hence there is no constraint on ARTC offering whatever paths it likes to whatever applicant. See also the response to the related Question 24.

There are two practical issues that do constrain ARTC's flexibility. These are:

- a) the problem of timing – ARTC will receive requests for paths at various intervals in time. If the desired paths are under contract at that time, then they are not available to the applicant at that time. Of course the best solution is to provide sufficient capacity to meet all demand – a capacity allocation solution should only ever be considered as a temporary measure.<sup>12</sup>
- b) The problem of connectivity – in many cases, ARTC provides the network for only part of the journey. While-ever it is the case that ARTC is unable to effectively deliver a "one-stop-shop", this problem will continue to apply. While ARTC is able to apply substantial pathing flexibility in its own territory, the attractiveness of those paths will be dependent to some lesser or greater extent on the paths that the applicant is able to acquire on adjoining networks. The most advantageous path becomes dross if no suitable connection is available at the "border".

### 3.3.5 DISPUTE RESOLUTION.

- 26) "Does the absence of a conflict management phase affect the overall effectiveness of the dispute resolution process?"

Pacific National has not resorted to the use of a conflict manager under the U2002. While the availability of this mechanism appeared to offer some benefits to dispute resolution, it required the consent of both parties to activate it.<sup>13</sup> It is always open to the parties to agree on a process (provided it is not prohibited by the Undertaking) and therefore the removal of the process does not necessarily preclude its use in appropriate circumstances. Pacific National's interpretation of the dispute resolution process in the Undertaking is that it does not prevent the parties adopting this course of action.<sup>14</sup> Therefore Pacific National does not see the removal of resort to a conflict manager as reducing the effectiveness of the dispute resolution process.

- 27) "Do the references to the rights of parties who are in dispute to use the dispute resolution procedures provide an adequate basis for access to these procedures? Conversely, does the absence of a specific reference to dispute resolution in some provisions of the Undertaking

<sup>12</sup> In almost any discussion about capacity on the rail network one eventually winds up back at the problem that while society may value the use of rail for the movement of freight, under current institutional frameworks it will (with the exception of major mineral hauls) never be the case that network capacity increments can be paid for by the parties directly seeking them. This is just a basic fact that prevents any serious consideration of managing the network as a commercial enterprise – it just won't work. While the pretence of commerciality applies, the network owner is forced to manage the network as a finite resource that can never be augmented (note that the only capacity increments to the interstate network have been provided through government funding) and so the focus becomes one of allocating that resource fairly rather than the normal market response of meeting demand with an appropriate level of capacity.

<sup>13</sup> See U2002 clause 3.12.4(a).

<sup>14</sup> While clause 3.12.3(a) of the Undertaking appears to offer only two choices – mediation or arbitration, it does not in fact prohibit any other course of action. Further, clause 3.12.1(a) provides the opportunity for the parties to agree to an alternative dispute resolution process.

affect the way that ARTC may negotiate with access seekers? Does it encourage or discourage use of dispute resolution procedures?”

### **Inclusive Model**

The dispute resolution process is an inclusive model (see clause 3.12.1(a)). That clause clearly says that any dispute arising under the Undertaking is to be resolved under the clause 3.12 dispute resolution process unless the parties otherwise agree.

It therefore seems unnecessary to provide specifically in various places throughout the Undertaking (eg clauses 3.4(f), 3.8(b), 3.8(e), 3.9(d)) for a party to avail itself of the process. Removal of these specific references would help reduce complexity of the document in a number of clauses without detracting from any party's rights in the slightest. In fact the only references to the dispute resolution process that should remain outside of the those in clause 3.12 are those, if any, that remove the right to access the general process.

### **Encouragement Of Disputes**

Pacific National does not see either the form in the Undertaking or that proposed by Pacific National as either encouraging or discouraging dispute resolution. Ultimately any recourse to arbitration is a costly, resource consuming and uncertain adventure and in many cases is unsuited to resolve the types of disputes that might arise under the Undertaking. However, in the current circumstances and institutional settings, a better general dispute resolution framework does not present itself.

### **Arbitration Process**

The arbitration clause in the DDAU is identical to that in the U2002 clause 3.12.4. However, it is of concern that incorporation of the arbitration process set out in Division 3 Sub-division D of Part IIIA of the TPA is heavy handed and not appropriate for the circumstances. That process confers on the ACCC wide reaching powers to conduct any arbitration as it considers appropriate, to compel the provision of certain evidence under oath and to give a wide range of directions. Failure to comply with any directions or determinations by the ACCC as arbitrator may attract a penalty of imprisonment.

These powers are clearly far wider than those typically conferred on a commercial arbitrator. Such powers may be appropriate in circumstances where the access provider is not co-operating or otherwise refuses to give access particularly in circumstances where the infrastructure service was declared under Part IIIA of the TPA against its will. However, given that ARTC is giving a voluntary access undertaking, such a heavy handed arbitration provision seems inappropriate.

### **Appeals**

Clause 3.12.4(xii) provides that the arbitrator's determination shall be binding "subject to any rights of appeal". Clause 3.12.4(xvi) also refers to appeal rights. The appeal, review or challenge rights of any determination or direction by the ACCC under clause 3.12.4 is unclear. This and other inconsistencies in the arbitration clauses are detailed in Appendix A.

### 3.4 PART 4: PRICING PRINCIPLES

#### 3.4.1 ARTC PRICING OBJECTIVES

- 28) “Does the general approach to access pricing achieve the stated objective of striking a balance among the business interests of ARTC, access seekers and the general public?”

Pacific National’s view is that the “commercial” model for rail infrastructure pricing detracts from the public interest in maximising use of the publicly owned rail network and achieving sustainable modal shift from the road network.

The Undertaking itself (clause 4.1) makes it clear that the provision of rail infrastructure services under this Undertaking will not meet any economic criteria that might normally underpin a commercial arrangement.

ARTC has been placed in a difficult position having nominally been required to act “commercially” while at the same time fulfilling a government policy role in providing access to uneconomic infrastructure.<sup>15</sup> Unfortunately, the two propositions are mutually exclusive and cannot co-exist. As a result, ARTC is forced into the position of attempting to construct a “commercial” pricing proposition when this is impossible. Necessarily this leads to a confusion of principles and outcomes that are inconsistent with the stated aims.

If pricing is not on a genuinely commercial basis, then some other logical basis should apply to avoid mere arbitrary price setting. It is Pacific National’s view that prices should be above marginal cost, and that this marginal cost ought to be calculated for each type of use made of the infrastructure. This avoids cross-subsidisation between access seekers. Pacific National also subscribes to the view that prices should not be above the stand-alone cost of providing the service as this would clearly offend economic principles and result in a sub-optimal allocation of resources. But how should pricing between these two limits be determined? A particular difficulty in rail infrastructure is the massive difference between the floor and ceiling costs of providing the service.<sup>16</sup>

Pacific National’s view is that price-setting above marginal cost should be such that it will promote government’s objectives in providing the rail network and does not result in unnecessary transfers to other parts of the supply chain (eg train operators). Clearly this approach requires a level of subjective determination. However, if the objective of pricing is focussed on achieving government objectives rather than a fruitless attempt to achieve some commercial objective, there is a greater likelihood that government objectives will actually be achieved.

#### **Why Would The ACCC Be Concerned Regarding Pricing?**

One argument that has often been raised about the interstate rail network is that it is directly competing against other modes and therefore its pricing is already constrained.<sup>17</sup> The inference from this is that there is little incentive for ARTC to price inappropriately and there is no need for price regulation at all. If this is the case, a legitimate question is, why should the ACCC concern itself with regard to pricing matters within the Undertaking other than ensuring that they are within the floor and ceiling? This submission sets out in response to Questions 33 and 34 some detail regarding concerns as to the quantum of access prices. From a conceptual perspective, the following argument by CRA International in their paper included in the Fright Rail Operators’ Group submission to the Productivity Commission sets out the point:

<sup>15</sup> This discussion is directed to the general interstate network and excludes the Hunter Valley coal network that is economically sustainable.

<sup>16</sup> A reference to floor and ceiling in this discussion is with regard to the normal understanding of these terms, not the specific and rather novel terms used by ARTC in the undertaking.

<sup>17</sup> For example see ARTC 2007 Rail Access Undertaking Explanatory Guide, June 2007, p 4

“The Productivity Commission suggests that continued price regulation of vertically separated below-rail operators supporting intermodal freight may be unnecessary and counterproductive. However, even in an environment where road freight prices constrain rail freight prices to levels that do not permit recovery of full capital costs above and below rail, there is a risk that unregulated infrastructure owners will use what may be short-term market power to capture the quasi-rents associated with above-rail operations. This behaviour would discourage new investment in above-rail operations and may make above rail operators unviable in the longer term. While these outcomes may not be in the long-term interests of the infrastructure owners, the fact is that these infrastructure owners are not viable long-term, either, and may therefore prefer to set access prices in a manner that is expedient in the near term. Moreover, the infrastructure owners are largely publicly owned, and hence their incentives may well be distorted (or at risk of being distorted).

Thus, inter-modal competition and self interest on the part of infrastructure owners cannot be relied upon to safeguard above rail operators against inefficient expropriation. Access price regulation is a more reliable safeguard, despite its noted shortcomings.”<sup>18</sup>

- 29) “Is there sufficient clarity about the way that the various components of access charges are intended to be applied?”

A problem with the Undertaking is that only one set of prices, the Indicative Access Charge (IAC) is provided. Restricting comment to that charge, the application of the components is reasonably clear.

Pacific National disagrees with the application of the fixed component of the IAC. The treatment proposed by ARTC will remove various arrangements that currently apply to train operators under both the existing East-West arrangements and the existing NSW access contracts under the NSWRAU. These include:

**Linkage to provision of train path:** the Undertaking, at clause 4.5(b), contemplates the levy of flagfall, and Excess Network Occupancy Charge (ENOC) on the basis of the path being contracted without any connection to the availability of the path. This would mean that ARTC would apply these charges regardless of whether the path is made available on the day. Pacific National is strongly of the view that it would be inappropriate for ARTC to apply the flagfall or ENOC charge in any circumstance where the path cannot be made available to the operator, regardless of the reason.

Further, in recognition of the integrated nature of the network, the failure by any other track provider to provide a connecting path should also remove the obligation to pay fixed charges.

**Cancellation Charges:** The existing contractual arrangements in NSW under the NSW Rail Access Undertaking do not impose any charge on the operator for the permanent cancellation of a train path. This is in stark contrast to the proposal in the Undertaking (IAA clause 9.9) whereby a substantial cancellation charge is levied, dependent on the term of the contract.

While IAA clause 9.9(a) provides for relief from a certain number of cancellation charges each year, this is referenced to the blank Schedule 2 and therefore there is no base from which access seekers can negotiate. Pacific National believes this is inappropriate. The IAA should provide at least a starting position in Schedule 2 that is reflective of current practice. In both of Pacific National’s access contracts with ARTC, there is an allowance is for 10% of train journeys<sup>19</sup> to be cancelled without payment

<sup>18</sup> CRA International p 1, included in Freight Rail Operator Group Submission to The Productivity Commission Inquiry Into Road & Rail Freight Infrastructure Pricing, November 2006

<sup>19</sup> In Pacific National’s East-West contract, this is rather more complex but in essence results in up to 10% of each train path being cancelled without the flagfall being charged.

of the flagfall charge. Of course, if the ENOC is imposed then this too would need to be cancelled.

As a more general proposition, Pacific National objects to any charge or term in the Undertaking that would put us in a worse position than we would have been had we remained under the NSWRAU.

### 3.4.2 EFFICIENT PRICING IN RELATION TO EFFICIENT USE OF THE NETWORK, AND EFFICIENT INVESTMENT IN THE NETWORK

- 30) “Does the proposed multi-part access pricing structure encourage efficient operation and use of the network by train operating companies, for all types of rail traffics?”

#### Need To Cater For Different Traffics

The multi-part access pricing structure does promote efficiency in certain circumstances. In particular, the form proposed by ARTC encourages the use of longer, regular trains which suits the intermodal business where the nature of the traffic and the pattern of train movements coincides with behaviours promoted by a simple flagfall and variable charge.

Unfortunately, it does not suit some other traffics. A number of bulk train operations in NSW are currently charged on a single rate per unit eg a rate per tonne of product moved or a rate per gross tonne kilometre (GTK). This current charging structure suits these traffics which typically do not have the same characteristics as intermodal trains in terms of regularity nor do they necessarily have a direct length/efficiency relationship. For example some minerals trains run on cycles of 72 hours so that they will not use a path at 8 am on every Monday, but might need that path only every second Monday, or that path might only be needed if a certain peak shipping pattern arises. This does not fit the neat, simple, regular operation that works well for some intermodal and passenger trains.<sup>20</sup> It is inappropriate to adopt a fixed flagfall charge for such traffics. It is also likely that a number of other circumstances will apply that make it unhelpful to encourage a particular rail related outcome in isolation from the wider supply chain requirements. An obvious example of this is the Hunter Valley coal chain where the imposition of a pricing arrangement designed to maximise efficiency on rail would dramatically negatively impact the wider system capacity. While the Undertaking does not apply to the Hunter Valley, the principle is the same and the adoption of a “one size fits all” approach to pricing is likely to have unexpected impacts on other parts of supply chains. As far as Pacific National is aware, ARTC has not taken these issues into account in preferring its two-part pricing structure over existing structures.

This style of charging can even be counter-productive for some regular intermodal traffics, particularly for new entrants without purpose built terminals. It might be argued that ARTC is entitled to not concern itself with the requirements of other parts of supply chains, and seek to impose its view that maximum availability of rail capacity the only criteria. But an access seeker that cannot access a terminal that will allow it to economically amass the maximum size train will pay a cost penalty compared to an operator that can. The fixed and variable charge is likely to favour a large scale participant that;

- a) has sufficient business to be able to regularly field the maximum allowable size train, and
- b) has terminal facilities that allow the marshalling of such a train.

It would be helpful to know if ARTC has discussed the imposition of fixed flagfall charges on grain traffics with the NSW Government, along with the removal of

<sup>20</sup> In fact it doesn't fit some intermodal type trains either. For example, the movement of shipping containers is sometimes worked directly around ship arrivals and therefore does not fit the regular pattern required for a fixed and variable style charge, of the nature proposed by ARTC.

capacity assigned to this traffic. Currently these are only charged when the train runs, thereby removing the cost burden to the industry during poor seasons.<sup>21</sup> The adoption of a fixed path charge regardless of usage would be a dramatic change in charging for these trains and would be expected to have a significant flow-on effect on the utilisation of a branch-line network that is already under-utilised. The effect of increasing access charges can be seen in the current example of Victoria where traffic is moving to road, further marginalising services and exacerbating the problem of trying to maintain a diverse rail network in that State.

As a double blow to these traffics, the flagfall component of these charges in NSW has been raised considerably compared to the current price.

### **Business Disruption**

A further issue raised by the radical change in pricing structure is that this will inevitably benefit some traffics while being detrimental to others. Prices for many of the affected traffics have been set using Ramsey pricing principles and ARTC's proposal seeks to reshape these prices to a set of common prices for categories of traffic which do not necessarily align with the previous Ramsey pricing approach. Pacific National and other operators have contracts in place that do not necessarily allow for the passing through of input cost changes and will therefore potentially suffer commercial losses (or windfall gains) until such contracts terminate. At the very least, if there has to be a restructure in access pricing, Pacific National would expect ARTC to put in place transitional arrangements to avoid disruption to existing business.

It is disappointing that ARTC is seeking such a radical restructure in pricing without having engaged with access seekers to understand and mitigate the impacts. When Pacific National asked ARTC to explain why it was seeking to restructure prices, ARTC's only response was that it was administratively easier and consistent with their broader network. This appears to be a very small benefit compared to the commercial disruption and loss of traffic that will occur. It is noted that ARTC currently invoices on a variety of rate structures and therefore the continuation of these will come at no additional cost to ARTC.

See also discussion on this issue in Section 4.2.

### **Lack Of Analysis & Detail**

Pacific National requested ARTC to provide some analysis of its proposal on the effect on access prices. The change in structure involves radical change and while Pacific National has attempted to perform its own analysis, there is insufficient detail made available by ARTC as to how it intends the pricing to operate in detail to allow any confidence to be placed on our analysis. For example, does ARTC really intend to charge grain trains for paths that they do not use? There is no way of telling from the information provided.

However, in the absence of such detail, Pacific National's analysis indicates that some traffics would have access charges nearly doubled while others will be only 20% of the current charges. There would need to be a substantial justification for such variations to be approved, and at the very least some robust analysis by the party seeking to impose the changes so that we can all see what is really intended.

---

<sup>21</sup> A similar question must be asked regarding the ruinously expensive charge being touted by ARTC for storage of grain rollingstock when it is not required – a service that has hitherto been provided as a bundle with normal access and considered part of the standard access charge. It is noted that ARTC has pretended that storage sits outside of the access paradigm and therefore has neglected to deal with it explicitly in the Undertaking.

- 31) “Does the proposed application of the new fixed access price component relating to network occupancy, the Excess Network Occupancy charge, encourage efficient provision and use of capacity in the network by train operators for all types of rail traffics?”

“The consumption of capacity on the network is a complex matter and PN’s view is that it is not amenable to a simplistic application of an additional charge as proposed in the Undertaking. Yet again the chosen model is based on a doctrine that the purpose of ARTC’s network is to serve as a conduit between an entry and exit point. This model suits some traffics and in particular suits many of the traffics using East-West network. However, ARTC has acquired a more complex network with the NSW lease and the traffics on that network do not necessarily conform to the simple model of the network being a pipeline. In some cases, trains need to perform actual work on the network itself. It is apparent from the explanation provided in Explanatory Guide that ARTC wishes to impose an additional charge for such traffics even though they have been using the network in this manner for many years.

The core underlying reason stated by ARTC for the charge is to recognise consumption of capacity beyond the norm. The difficulty arises in that consumption of capacity is a complex matter, eg passenger trains consume far more capacity than their actual running time due to the priority they command. Priority imposes a ‘shadow’ around the train through the need for other trains to be put aside to allow the uninterrupted passage of the priority train. Thus the effective capacity consumed is substantially greater than the apparent capacity consumption. A simple measure based on ‘network occupancy’ if applied consistently should see passenger trains offered a rebate because their actual track occupancy is less the ‘standard’ train, even though they actually consume substantially more capacity. Conversely, slower trains (eg Pacific National’s steel trains) ought to be charged more on this logic because they consume more time on the section than, say, an intermodal train.<sup>22</sup> If the charge was genuinely attempting to maximise network usage, the charge would be based on a single set of train characteristics and any deviation from these would result in a variation of charges. But of course, such variation is contrary to the differentiated pricing structure that ARTC currently has in place (eg passenger trains and express freight trains pay the highest price on the former ARTC East-West network whereas, applying the logic of the excess network occupancy charge would reduce the price compared to the standard train).<sup>23</sup> The QR Access Undertaking has struggled to deal with this very matter and the result is a complex arrangement to attempt to fit a seemingly simple concept (network capacity consumption) into a complex reality. From PN’s perspective, in neither the QR Access Undertaking (which at least attempts a conceptually consistent approach) nor Undertaking has the solution been appropriate.

ARTC suggests that this charge would provide a signal for additional investment. PN would certainly welcome and support a measure that provided for ARTC to invest in the network to provide additional capacity when this is required, however the excess occupancy charge does not appear to drive such behaviour, nor is there any link discernable to investment within the Undertaking. In fact the Undertaking is singularly deficient in any commitment by ARTC to invest in the network on the basis of any customer demand.

There is no explanation of how ARTC has derived the ENOC nor the tolerances in the table provided (Undertaking clause 4.6(c)). Further, the intention of the concept as expressed in the Explanatory Guide is not reflected in the drafting. The only drafting that addresses the application of the charge is in Undertaking clause 4.5(a)(iii), and this drafting is ambiguous. Certainly there is room for more than one interpretation

<sup>22</sup> PN is not advocating this, merely using the example to show that the adoption of a simplistic measure as proposed is conceptually flawed.

<sup>23</sup> While the nominal rates paid by passenger trains is the highest, the actual revenue generated is relatively low on a train basis as passenger trains are very light compared to freight trains – thus a measure based on GTK provides a low yield on the variable component for passenger trains. This does not counter the argument above but points to the fact that ARTC’s pricing is in fact governed by matters other than network capacity consumption.

as to what is, or is not included in the tolerance and what is the nature of the train path to which the charge is applied. For example, this would penalise a party for accepting a path longer than the allowed transit time because no other path was available ie accepting a path 'in excess of a reasonable allowance' for traffic related matters, even though the Explanatory Guide suggests that this is contrary to the intent. This would certainly work against encouraging maximum use of the network and not in anybody's interest. Similarly, there is no link back incentivising ARTC to make appropriate capital investments. It is certainly open to question as to whether the formulation of the charge will improve or detract from network occupancy.

There is no indication as to how ARTC has established the base-line as an appropriate measure to trigger the charge. The arbitrary adoption of a base-line would detract significantly from the rationale for adopting the charge in the first place. As far as Pacific National is able to deduce, the charge is imposed because the train is different from the standard rather than for some underlying consumption of capacity. For example are the sectional run times based on a particular power to weight ratio? If so, how does ARTC justify that this is the appropriate value rather than one which is higher or lower. How does ARTC factor in speed restrictions and their effect on train length into the determination of sectional running times?<sup>24</sup> How have 'reasonable allowances' for above rail activities been determined and how does ARTC justify potentially penalising an operator that performs these activities differently to current practices? For example if an operator chooses to fuel 'on the run' from an on-board tanker, thereby not having to stop to refuel, if the stated principle is applied, such an operator ought to be rewarded with an access charge reduction for occupying less of the network, but the ENOC does not seem to contemplate this; it merely seeks to penalise operations that are different from an arbitrarily determined 'norm'. This is a poorly thought out attempt to increase revenue without merit and should not receive approval from the ACCC. It yet again serves to demonstrate ARTC's approach that "one size fits all" that will be to the detriment of innovation and make it harder for competition to survive on the network.

- 32) "Is there sufficient clarity in the Undertaking about the nature of ARTC's commitments on capital expenditure?"

ARTC has published a capital investment program in Schedule H. Further detail is provided in the Explanatory Guide. As far as it goes, this is a positive step. However, it does not appear to Pacific National that the investment nominated in Schedule H commits ARTC to actually do anything. It reflects an investment program that ARTC has decided to undertake, for a variety of reasons, most of which appear to be driven by Commonwealth Government imperatives. There is no obligation on ARTC within the Undertaking to invest at all.

Pacific National welcomes the investment nominated in Schedule H, but the complete lack of any meaningful investment processes within the Undertaking mean that this area is most unsatisfactorily dealt with by the Undertaking. This is discussed further in Section 3.6, and in response to Question 66.

<sup>24</sup> A speed restriction, even though it is constant, has different effects depending on the characteristics of the train. For example a highly powered, short passenger train will be affected far less by a given speed restriction than a long heavy freight train that takes considerably longer to slow down, pass through the restriction and regain line speed.

### 3.4.3 ENCOURAGEMENT OF INTER-MODAL AND INTRA-MODAL COMPETITION

- 33) “Does the proposed level and structure of indicative access charges promote effective and sustainable competition among operators as well as between rail freight operators and road and sea freight haulage companies?”
- 34) “Are there any pricing considerations that could potentially effect above rail competition and entry into the above rail market by access seekers?”

Questions 33 and 34 are answered together.

The responses to Question 28 in Section 3.4.1 and Question 30 in Section 3.4.2 also pertains to these questions.

#### Incompleteness

In the pre-submission “consultation process”, Pacific National and others made it clear to ARTC that its approach in including only one set of prices, the IAC, in the Undertaking was contrary to customers desires. Unfortunately, ARTC has ignored its customers on this issue. ARTC has not presented any compelling reason as to why it has not included all access charges in the Undertaking. The matter is further confused by the fact that ARTC is willing to publish all of its prices (see Undertaking clause 2.7(b)(iv)), which seems inconsistent with a refusal to include them in the Undertaking.

By only submitting the IAC in the form its has, if the ACCC approves the Undertaking, ARTC will be able to set other prices at will, without regulatory scrutiny. Pacific National regards this as contrary to the spirit and intent of the Undertaking. Clearly ARTC has in mind a set of charges<sup>25</sup> and is denying the regulator the opportunity to consider those charges. It is also material that the escalation process in the Undertaking applies only to the IAC. Pacific National has suffered the consequences of this under the U2002 when ARTC increased prices for traffics other than the IAC by amounts higher than allowed under the Undertaking for the IAC.<sup>26</sup> (This is further discussed in Question 56 in Section 3.4.8)

Pacific National is particularly concerned about this approach given that the charges being proposed by ARTC outside the Undertaking process involve substantial deviations from existing charges. As noted earlier (in response to Question 30) the variations range from nearly double to one fifth of the current access prices. Such large deviations are not in the interests of access seekers who have in place long term contracts set on the basis of previous charges. At a minimum, Pacific National would expect the introduction of a transition from the existing charges to the new proposed rates over a reasonable time period to minimise the level of commercial disruption.

ARTC’s proposal would be similar to Telstra submitting an undertaking for PSTN interconnection for the carriage of a subset of call types in particular geographic areas and reserving the right to set the charges for other calls and geographic areas at substantially different rates without scrutiny. In Pacific National’s view, this incomplete approach to the Undertaking process is inconsistent with the intentions of the legislation, creating substantial uncertainty for access seekers and providing ARTC with a high degree of unwarranted discretion. (The issue of change of pricing structure on many of these traffics is discussed at Question 30 in Section 3.4.2.)

<sup>25</sup> ARTC published a set of access prices under its new preferred structure during the pre-submission “consultation process” but was at pains to point out that these were not intended to form part of the Undertaking. The pricing document is available at [http://www.artc.com.au/docs/news/pdf/news\\_100407\\_Pricing%20Schedule.pdf](http://www.artc.com.au/docs/news/pdf/news_100407_Pricing%20Schedule.pdf).

<sup>26</sup> Prior to the occurrence of this event, it was widely believed that the escalation process in the Undertaking would apply to all access prices, or at least the “posted prices” that ARTC published on its website. Indeed for several years that is how ARTC behaved, applying the escalation formula across all posted prices in the same manner. However, it decided in one year not to do this, apply greater increases on access charges that were not the IAC.

Pacific National strongly urges the ACCC to require that ARTC include all existing prices and/or known proposed prices in the Undertaking so that they can receive appropriate regulatory scrutiny.

### Quantum

ARTC has published a modest amount of information regarding market shares and "door-to-door" transport costs to justify its pricing for the IAC. Unfortunately, the data provided presents a simplistic and distorted view of the situation.

An example of this is the claims being made with regard to Intermodal rail freight to Western Australia. This traffic competes with both road and sea. Rail freight provides various levels of service offerings, and is for a number of traffics is priced above sea freight and below road freight. Pacific National's Express offering is an exception to this, discussed below.

Both road and sea enjoy significant market share of the freight market to WA from the East coast, yet the ARTC analysis ignores the sea component – thus its conclusions regarding market share and the consequences of changes in prices are fundamentally flawed. The true picture is shown in Table 1. It is particularly important to recognise that sea transport volumes are highly volatile, for example in 2000 the NSW – WA volume was 0%, and is highly sensitive to price and service changes compared to modal competitors.

**TABLE 1: MARKET SHARE DATA – 2005/06 FINANCIAL YEAR**

	NSW – WA	Victoria – WA
Rail	53%	59%
Road	28%	15%
Sea	19%	26%
Total	100%	100%

Source: Tables A4 and A5 Australian Rail Freight Performance Indicators 2005–06 Information Paper 59, Bureau of Transport & Regional Economics, Canberra 2007.

The decision by a customer to use rail will be dependent on a number of factors, including the total supply chain cost, reliability of supply, transit time, safety and environmental factors. The total supply chain cost includes the end to end cost of transport, plus inventory holding costs, storage costs, insurance etc. The final modal decision is a balance of these factors and cannot simply be limited to a comparison of direct transport costs. While rail costs may in most situations be below road costs, poor reliability of delivery and inferior transit times mean the total equation is often resolved in favour of road, despite the difference in direct transport cost. Where transit times and service quality is less important, sea becomes a viable alternative to rail as the cheaper price becomes the defining factor.

Specifically in regard to road freight, Pacific National operates an Express service which aims to compete directly with road, by offering a comparable (though not as good) transit time, plus ancillary pick up and delivery services. Current pricing of this service, required to deliver an acceptable return to Pacific National is estimated to be within 2% of the road equivalent service. A 10% increase in access costs, as proposed by ARTC for these services will not be able to be passed on to customers without the risk of a significant transfer of modal share to road and profitability for rail operators is already marginal.

In arguing that rail operators are able to sustain above normal price increases, ARTC is arguing either;

- a) train operators have failed to maximise their current return through charging at the highest price the market will bear, or

- b) that train operators are making too much profit on the East-West corridor and that ARTC is entitled to extract a portion of that profit.

Neither of these propositions appears to withstand scrutiny. It is in the nature of normally functioning competitive markets that suppliers will extract the highest amount from customers that competition will allow. This serves to contradict both (a) and (b) – as normal commercial businesses, train operators will have sought to extract the maximum price but that maximum price will be reduced to the normal supply and demand equilibrium by competition, both between train operators and through substitutability with other modes. It therefore does not seem tenable to suggest that ARTC is able to extract additional prices from the market without affecting the overall market.

ARTC also seeks to justify the East-West increase on the basis of a real reduction in unit access prices over previous years ie the real prices have decreased by 25%. This is true, but this provides no justification for seeking a real price increase at this time. Train operators have also seen real price decreases over the same period and have also suffered significant cost escalations which they have had to absorb though productivity gains, or pass on and suffer the resulting loss of business. For example, over the last several years, the price of fuel, a significant input to rail operations (and to a much lesser extent to track maintenance), has more than doubled. ARTC's claim regarding the ability to use longer and therefore heavier trains improves operator productivity is true, to the extent that operators are able to make use of the opportunity. Without such productivity improvements, train operators would have had to further increase prices and lose further market share to competing modes.

To place some context around ARTC's real rate reduction, Pacific National's most commonly used East-West container rates have fallen in real terms by 34% over the same period. So ARTC is seeking to further transfer additional value to itself from train operators when they are already in a worse position than ARTC.

It is notable that in its justification for a substantial price increase, ARTC has neglected to show the benefits it has received from the growth in volumes over the years. While ARTC's real prices have decreased, the high level of fixed cost in its infrastructure means that its profitability from that infrastructure has soared. It would be appropriate for the ACCC to enquire as to ARTC's actual income, costs and profitability on the East-West axis in recent years, and to show actual expenditure over the same period.

In terms of North-South access pricing ARTC acknowledges that current pricing is above road pricing on Melbourne-Sydney and Sydney-Brisbane. ARTC claims that rail is cheaper than road by 13.7% between Melbourne-Brisbane. Pacific National's experience is that this is not the case. Our market information indicates the direct transport costs to be much closer than this. When combined with the disadvantages of rail (lack of reliability and longer transit time), it is Pacific National's understanding that even Melbourne-Brisbane rail freight is at a significant disadvantage to road today. To address this ARTC is proposing a temporary rebate of 10% on access fees. While this is welcome, we believe this should be a permanent, not temporary, reduction. The efficiency improvements promised as a result of the track improvements may, if ARTC's predictions prove correct, enable rail operators to significantly improve volumes on the corridor. However, rail will be coming off a very low base and will require significant assistance to achieve anything like profitability on this corridor. There is a real question, despite ARTC's proposed rebate, as to whether train operators will be willing to invest in additional rollingstock to take advantage of the potential additional volumes. Unless there is a significant improvement in profitability to train operators, a more likely result is that existing equipment will be used until it is no longer economic to repair and then the corridor will be abandoned.

The ACCC should also exercise great care in accepting ARTC assertions with regard to market data. This data often seems to be presented in its best light without the necessary context, thereby inviting the reader to draw conclusions that may not be

justified. For example, ARTC presents a 2006 growth for the North-South corridor of 4.6% for intermodal traffic.<sup>27</sup> In the 2006/07 financial year, Pacific National has experienced a significant drop in volumes on the Melbourne-Brisbane route, with volumes down by 11% year on year. While Pacific National does not see the volume data for other operators, there is nothing to indicate that there has been a substantial shift in market share between operators. Pacific National does not expect to be able to reclaim any of this volume from road unless prices are significantly reduced. As operators are already losing money on this corridor, there is limited ability for operators to do this.

#### **North-South “Rebate”**

ARTC has suggested that it intends to offer a 10% rebate to traffic on the Melbourne – Brisbane corridor.<sup>28</sup> It is disappointing that ARTC has chosen not to include this in the Undertaking. Pacific National can see no justification for its exclusion. At present all that operators have is an assertion from ARTC that it will provide this discount – there is nothing that obligates ARTC to provide it and we have not been given any details as to how it might be applied, nor what it actually means in terms of prices. The concept of a “rebate” is curious – why would ARTC not merely reduce its prices and remove the administrative burden on both itself and claimants that necessarily accompanies this form of charging?

Pacific National is sceptical of this claim by ARTC until real details are provided. It would be far more preferable for the rebate to be incorporated into access charges and included, along with all other access charges in the Undertaking.

Unstated in the Explanatory Guide, but revealed by ARTC in discussions is the fact that the rebate is only intended to apply to intermodal traffics. Other traffics that are also under severe competitive pressure are not being offered the rebate. ARTC has not provided any sustainable reason for the preferential treatment for intermodal traffic.

### **3.4.4 REVENUE FLOORS AND REVENUE CEILINGS**

35) “Is the Undertaking sufficiently clear about how revenue floors and ceilings are defined?”

Yes.

#### **Cost Allocation**

PN supports ARTC’s proposal to have an intermediate “corridor” allocation for non-segment specific costs and assets as well as a network-wide allocation where these cannot be determined on a corridor basis. It would be helpful if ARTC was to define the corridors by which such allocations are to be made. It is important that the definition of the corridors capture the benefit of this intermediate assignment, ie they should not be defined too narrowly nor too broadly. ARTC is clearly in the best position to determine this as it has the knowledge of how its costs are managed and how the services provided by such cost areas are consumed. This could simply be achieved by nominating the corridor to which each network segment has been assigned in the list in Schedule I of the Undertaking.

It would assist stakeholder confidence for ARTC to provide some detail of the type of costs that it intends to allocate on a corridor basis. In particular, stakeholders will be concerned that the Hunter Valley is not allocated costs inappropriately.

<sup>27</sup> ARTC 2007 Interstate Access Undertaking Explanatory Guide p 56. Note that it is unclear where this is calendar or financial year data.

<sup>28</sup> ARTC Explanatory Guide pp 27, 59, 60

### **Floor Limit**

The Floor Limit is not a floor limit as adopted in most rail access regulation around Australia. It is in fact a "mezzanine" limit reflecting the total receipts to ARTC for a segment of the network and not the minimum price that can be charged to an individual operator. The formulation adopted by ARTC that it can, by agreement, go below this effectively invalidates the concept of a floor. For any party negotiating an access agreement, the mezzanine revenue, in isolation, tells the applicant nothing as the applicant will (in most cases) not be the only party seeking access to a particular line, and anyway ARTC can agree to a price lower than a price that would generate the mezzanine revenue. What is required is a genuine floor limit that is based on the incremental costs (as most people would understand that term to mean) to provide access.

The inclusion in the definition of incremental costs in Undertaking clause 4.4(b) continues the error of principle contained in U2002 in that it nominally includes any non-segment specific costs avoided by the removal of a segment from the network. This must be in error as any cost avoided by removal of a single segment ought to be directly associated with that segment and therefore could not be non-segment specific. In practice this ought not to be an issue if assets have been correctly assigned to either segments or as non-segment specific, in which case the pool of non-segment specific costs that could be allocated to the floor would be a null set. However, it seems inappropriate for the ACCC to affirm an error of principle unless its removal would be inconvenient.

The retention of the phrase "such return being determined by applying Rate of Return to the value of these assets" is otiose given that it refers to assets that are being excluded.

Both of these errors have been brought to ARTC's attention previously but ARTC has not seen fit to respond.

Pacific National prefers the adoption of both a true floor and a mezzanine limit along the lines of ARTC's current NSWRAU. This formulation does away with discretion to go below the floor, but as this is a genuine incremental cost, this is consistent with the underpinning economic principle and prevents cross-subsidisation between access seekers. The adoption of a mezzanine that is an objective rather than a strict limit removes the problem of potential under-recovery on a particular segment leading to an unintended breach of the limit. This formulation has worked well in NSW and Pacific National sees no reason why ARTC would object to adopting this limit. Given that the Undertaking provides room for ARTC to negotiate prices below the floor limit, there does not seem to be any "in principle" objection from ARTC to the adoption of a true floor.

### **Gifted Assets**

The Undertaking is silent on the matter of valuation of gifted assets. Gifted assets should be recognised as such and either excluded from the asset base for the purpose of calculating revenue limits or otherwise included at zero value. Given that ARTC is in receipt of substantial government grants for investment in the network, this is likely to have a significant impact on the calculation of the regulated asset base. It would be inappropriate for the assets purchased with those funds to be valued at replacement cost and included in the RAB such that a rate of return was sought for such assets.

It could further be argued that the initial vesting of the rail network in ARTC was gifted to the extent that the asset was written down on receipt by ARTC. In this regard it is noted that ARTC gifted the Tarcoola to Alice Springs line to FreightLink,<sup>29</sup> so clearly ARTC's owner, the Commonwealth Government was not concerned about

---

<sup>29</sup> Pacific National understands that this was in the form of a lease for a payment of \$1 – somewhat less than even the scrap value of the materials one might suggest.

extracting the economic value out of that line. Pacific National suggests the Commonwealth's gifts to ARTC to enhance the network show a similar lack of intention that ARTC should incorporate that value into its revenue limits and can see little distinction between such gifts and the gift of the network to ARTC in the first instance.

Pacific National notes that its position on this issue is consistent with the ACCC's conclusion in its 2002 Decision on ARTC's Undertaking, in particular, that ongoing Commonwealth grants need to be taken into account in determining floor and ceiling revenue limits. On this basis, Pacific National urges the ACCC to examine the treatment of the substantial grants that ARTC has received from the Commonwealth in its DORC valuation. At a minimum this includes:

- \$80 million for approved projects under the Australian Rail Infrastructure Fund;
- \$260 m under the Auslink funding, of which it has already received \$177m (according to DOTARS information);
- \$450 m and \$100 m, announced in 2003/04 and 2005, respectively.

In Pacific National's view, the DORC valuation of ARTC's network should assign a zero value to assets purchased under Government grants.

36) "Are the objectives of the RAB capitalisation approach clearly set out?"

Yes. ARTC is seeking to retain a high degree of discretion in pricing through the use of this approach. By doing this and combined with a refusal to include other prices in the Undertaking, ARTC introduces uncertainty as to future pricing for any traffic apart from the indicative access charge.'

37) "Is the RAB capitalisation model an appropriate basis for regulating the ARTC network?"

No. The RAB capitalisation model effectively removes the ceiling for all practical purposes.

The ceiling limit proposed by ARTC is a novel approach to economic regulation. Pacific National's understanding is that the proposed ceiling operates such that, so long as ARTC has not recovered the regulated full economic return in any year, prices are unlimited. A cap on revenue only arises once any past under-recovery has been recouped.

The stated reason by ARTC for adopting this approach to limiting prices is to allow it to recover in later years, investments that cannot be supported in earlier years. But the practical reality is that this will never happen for the lines included in the Undertaking.<sup>30</sup> ARTC demonstrates this itself in the graphs in Appendix 1 to Attachment A of the Explanatory Guide wherein all of the line segments show a perpetually increasing RAB. If ARTC believes that the mechanism would actually have some relevance, it should provide a specific real example where it expects the ceiling to come into play to limit pricing at some future point in time. ARTC has not provided any information that suggests such an example is remotely likely. The example that has been provided by ARTC<sup>31</sup> is a conceptual one and does not indicate any practical application.

When this is considered on a segment by segment basis it becomes even more confusing (eg the vexed question of how one should allocate revenues and costs) and will require a substantial level of auditing. It is noted that there are no annual audit

<sup>30</sup> There are no lines contained within the Undertaking as formulated by ARTC where the predominant traffic is a mineral haul. Minerals lines are the only lines where it is at all likely that the ceiling might be reached at some future time.

<sup>31</sup> ARTC Explanatory Guide Attachment A p 36

provisions contained within the Undertaking to ensure compliance with the revenue limits.

The ACCC has rejected this proposed methodology in the past. For example, in the context of pricing Telstra's unconditioned local loop service (ULLS) the ACCC rejected Telstra's proposal to recover past losses associated with ULLS specific costs in prices for the current undertaking period. The ACCC concluded that such an approach was inconsistent with the ex ante access pricing approach and would shift all the risk associated with forecasting errors to access seekers<sup>32</sup>.

Pacific National is not able support the ceiling limit as currently formulated. Instead Pacific National affirms its support for adoption of the two-part ceiling limits contained in the current ARTC NSWRAU. These limits provide both an individual price constraint (the stand-alone cost to provide the service) and a combinatorial revenue limit. These limits have worked well in NSW and have the added advantage that, if adopted, they could be applied uniformly to both the main line and Hunter Valley networks.

It is possible to cater for the type of circumstance ARTC has in mind as the reason for seeking this model.<sup>33</sup> Pacific National suggests that the Undertaking can provide a relatively simple mechanism of negotiation above the limits. A 'catch-all' provision on this basis could easily allow for the sort of temporal shift in access charges proposed by ARTC. Indeed this is already catered for in the Undertaking in clause 6.2, and all that is necessary is for the pricing principles in Part 4 to recognise such an exception as allowable by agreement.

- 38) "Any comments on the factors that ARTC has taken into account in determining whether the RAB model is appropriate?"

This is covered in the response to Question 37.

- 39) "Is the definition of the segment revenue floor appropriate? Should the floor include non-segment specific costs and assets? Is there sufficient clarity about the non-segment specific costs and assets that ARTC intends to allocate to individual segments?"

This is covered in the response to Question 35.

- 40) "Is the Undertaking sufficiently clear about how non-segment specific costs will be allocated to individual segments?"

This is covered in the response to Question 35.

- 41) "Are the proposed cost allocators for non-segment specific costs to segments soundly based? What impacts, if any, do they potentially have on usage patterns of different traffics?"

As noted earlier, a concern is that the allocation of costs between the two different undertakings might lead to inappropriate outcomes. This would be particularly the case if GTKs are used as an allocator as the Hunter Valley generates a high proportion of ARTC's GTKs. To some extent, this concern is mitigated by the allocation of costs to corridors as track maintenance costs, the area allocated on GTKs, are mostly identifiable to a corridor if not the actual line segment. There will still be some track maintenance costs allocated at a whole of business level. It would assist stakeholder confidence if ARTC provided costs in each category and indicated the proportions

<sup>32</sup> ACCC 2006, Assessment of Telstra's ULLS Monthly Charge Undertaking, Final Decision, p. 150.

<sup>33</sup> ie the need to invest prior to the traffic which will support the investment being able to sustain a level of access charges to repay the investment.

involved in the allocations to line segments. This is particularly relevant given the splitting of the network under different undertakings.

However, apart from these concerns, the allocators used are reasonable. Provided the split between the undertakings is appropriate, Pacific National does not anticipate that the proposed allocators will result in a substantial bias between line segments.

- 42) What implications does the use of such cost allocators have for encouraging efficient investment in the network by ARTC?"

As the cost allocators are used merely to determine the revenue limits, Pacific National does not expect these to influence investment in the network outside of the Hunter Valley.

### 3.4.5 DORC AND VALUATION OF NETWORK ASSETS

- 43) Given the use of the RAB capitalisation model, what issues should be taken into consideration in establishing the initial RAB?"

The initial RAB is not dependent on the form of the subsequent treatment of the RAB ie whether the capitalisation model is used or a more normal model will not determine the RAB.

The initial RAB should be determined according to the normal considerations in a DORC calculation. Any gifted assets should be excluded from the result.

See also responses to Question 35 and 44 to 48.

- 44) "Is DORC the appropriate valuation methodology for ARTC's assets?"

The use of DORC as a regulatory valuation methodology is well established for rail infrastructure assets in Australia, with notable precedents including the NSW Rail Access Regime and the ARTC 2002 Undertaking.

Pacific National supports the use of the DORC valuation method as being conceptually correct while noting that prices on the interstate network are unlikely to reach the ceiling.<sup>34</sup> However, there is merit in adopting an approach that is consistent in this instance where the result is not detrimental to the any party. The ceiling will become substantially more relevant when the ACCC considers an undertaking for the Hunter Valley export coal traffic and the use of the DORC methodology under the current regulatory structure has the general support of stakeholders.

- 45) "Are there other models that should be used to value ARTC's assets, such as historical cost, reproduction cost or deprival value?"

The use of alternative asset valuation methodologies, such as those listed in the question, would introduce unnecessary uncertainty in the regulatory process for rail infrastructure. Given the weight of precedent and the wide acceptance of DORC, there would be no efficiency benefit in moving to or considering in parallel any of the suggested alternative valuation methodologies. The alternative concept of Gross Replacement Value (GRV) has some standing in Western Australian regulatory practice for rail access. However, GRV and DORC are likely to result in the same access price levels provided the depreciation applied to the DORC valuation is consistent with the depreciation profile that is implicit in the GRV approach.

<sup>34</sup> Pacific National is not in a position to calculate the ceiling that would apply in the case where all of ARTC's assets except those in which it has itself invested were excluded from the network valuation but it is assumed that the ceiling would still exceed current revenues.

- 46) “Is the approach to calculating DORC, used by ARTC in the Undertaking, appropriate?”

ARTC’s consultant estimated the current DORC valuation using the same approach that was used to estimate DORC values for the U2002, and for the NSWRAU, with one exception. The current NSWRAU follows the requirement of the NSW Rail Access Regime that land and formation assets under rail infrastructure prior to the commencement of the Regime be valued at \$0. Newly acquired land, and formation assets constructed or acquired since that date should be included in the regulatory asset base.<sup>35</sup> ARTC’s proposed Undertaking does not observe this valuation convention for pre-existing land and formation assets. Failure to continue to observe this convention—at least for NSW track—would result in an inappropriate valuation of the network.

A second point of concern is the claim by ARTC’s consultants that railway construction costs have increased significantly since 2001. The only evidence provided for this claim is discussed at p.9 of the ARTC Standard Gauge Rail Network DORC report (January 2007). The current cost rates were obtained from detailed cost estimates from ARTC’s Southern Alliance for a proposed passing lane 6.8 km in length. These costs were estimates, rather than actuals. They included some costs that would not apply to a greenfields site, although those that could be identified were stripped out. Most importantly, these estimates for a 6.8 km track section are being extrapolated to obtain a figure for ARTC’s entire interstate network, which has nearly one thousand times as many single track kilometres. A more comprehensive base of evidence would be required before ARTC’s cost escalation claims could be considered properly substantiated.

- 47) “Is there sufficient clarity about the way that ARTC will allocate assets under its control between the “Hunter Valley coal network and the interstate network and among segments in the interstate network?”

As regards trackwork, associated structures, and signals, yes.

The allocation of the costs associated with communication and control assets and functions (which are not readily identifiable with specific sections of track) should be set out in a public document that is updated from time to time, subject to a consultative process with users.

See also response to Question 35.

- 48) Any comments on the treatment of government capital contributions, including infrastructure assets and financial capital, in the RAB?”

To the extent governments contribute or fund capital works on ARTC’s network in their roles of providers of public goods or promoters of policy outcomes, then these government contributions should not be included in the asset base on which ARTC is entitled to earn a regulated rate of return.

See also response to Question 35.

<sup>35</sup> Because the issue did not arise under the NSW Rail Access Regime, it was not necessary at that time to specify a valuation methodology for newly acquired land and formation assets. The DORC methodology is unsuitable for use in valuing land or extremely long-lived assets (such as tunnels) that may never need to be replaced. Land valuation based on nearby property valuations is problematic due to the “bootstrap effect”—the presence of the transport infrastructure alters the value of nearby land. One method of overcoming these difficulties is to use historic land acquisition cost or indexed historic cost. This method was adopted by the ACCC to value the land under Sydney Airport in 2000.

### 3.4.6 WEIGHTED AVERAGE CAPITAL COST DERIVATION AND CAPITAL ASSET PRICING METHODOLOGY

- 49) “Has the Capital Asset Pricing Model been properly used to arrive at the Weighted Average Cost of Capital for ARTC?”

Yes.

- 50) “How appropriate are the parameters and the assumptions that have been used to derive the components of the WACC?”

ARTC’s present proposed WACC parameters market risk premium, asset beta, debt/value, and gamma each differ from the values approved by the ACCC for the 2001 ARTC Undertaking in a direction that tends to increase the permitted return on assets.

Individually, each of the parameter values selected by ARTC lies within what could be considered a plausible range. However, the combined effect of selecting values at the high-WACC end of each parameter’s range is to increase the Vanilla post-tax nominal WACC by 60 basis points relative to the Vanilla WACC that would be obtained under the same formulae with the ACCC’s 2001 parameter settings.

It is not clear what circumstances might have changed between 2001 and 2006 to justify changes to the market risk premium, gamma, or debt/value ratio for ARTC.

Regarding the proposed change to ARTC’s asset beta, the justifications presented in the May 2007 report “ARTC’s Interstate Network Weighted Average Cost of Capital Review” suffer from the weakness that the proxy company analysis does not include any companies that are pure infrastructure operators like ARTC. The railway organisations that are included are either vertically integrated, or above-rail only firms. The inclusion of trucking and shipping firms in the comparator set appears highly questionable as these types of firms would have enormously different risk profiles than ARTC. The proxy analysis would have been more balanced if some networked utility firms had also been included in the set.

Pacific National suggests that the proposed uplift in ARTC’s asset beta does not appear justified.

### 3.4.7 INDICATIVE ACCESS PRICES

- 51) “Does the Indicative Access Charge provide a reasonable basis for setting of access prices for indicative services?”

Comments regarding the IAC are provided in response to earlier Questions, particularly Questions 30 and 33.

- 52) “How appropriate is the definition of indicative service used by ARTC for the purposes of setting indicative charges?”

- 53) “Is the method for setting prices of non-indicative rail services clearly set out?”

- 54) “Is there sufficient guidance about how deviations from the indicative service will be taken into account in setting access prices?”

- 55) “Does the Undertaking provide access seekers with an appropriate level of certainty about how non-reference services will be priced?”

Questions 52 to 55 are answered together.

The indicative service defines a common train used on the interstate network. However, it is very far from being the only train type on the network. ARTC has proposed that there be 6 train types for which it will post prices.

Pacific National does not have the data to know the relative proportions of each train type on each line segment for all operators. However, it is clear that a number of other train types routinely use the network. Pacific National's own train data indicates that of the existing 17 paths in one direction daily to which it has access south of Sydney, only 4 are paths to which the IAC would apply.

It is therefore a pertinent question as to why ARTC has decided not to provide IACs for these other train types. It cannot be that they don't know what these prices are, for they have already published their aspirations on these prices. As noted elsewhere in this submission, Pacific National can only conclude that ARTC is seeking to avoid regulatory scrutiny by not including these prices in the Undertaking.

The Undertaking is effectively silent on pricing for other trains. As these form a significant part of the existing traffic base, this is a peculiar position to adopt. ARTC's secrecy merely raises suspicions as to their intentions with respect to these other prices. Pacific National has raised this issue with ARTC and queried their intentions but received no satisfactory response. Pacific National therefore remains extremely concerned as to ARTC's intentions.

Pacific National's view is that it is inappropriate to have merely one train type for which prices are included in the Undertaking. Rather, all existing train types and their prices should be included in the Undertaking. This would provide access seekers with substantially more confidence in prices and also provide substantially more assistance with regard to any new traffics that are not currently catered for.

#### 3.4.8 PRICE ESCALATION

- 56) "Is there sufficient clarity about how the proposed access prices escalation approach will work in practice?"

In some respects, the process is very clear. ARTC may impose price increases on access holders at any time so long as they have a banked real price decreases in the past. The number of increases in any one year is unlimited and can be imposed without any consideration for the effect on the business of ARTC's customers. This is a most extraordinary degree of discretion, and one that Pacific National believes is totally unjustified.

What is totally unclear, is the escalation mechanism ARTC intends to apply to prices other than the IAC. The IAA shows ARTC's approach in this regard by applying only to Indicative Access Charges.<sup>36</sup> Initially, during the "consultation" process, Pacific National thought that this was merely an error and pointed it out to ARTC as such, expecting the second draft to provide rectify the matter. However, subsequent drafts have indeed continued to adopt this drafting and Pacific National can only conclude that ARTC intends for this approach to be adopted. The drafting in the IAA to U2002 clearly provides for the escalation provisions to apply to all services operating under the agreement and a deliberate change of this nature raises suspicions as to ARTC's true intentions.

In Pacific National's opinion, this change makes no sense at all. A party that signs up to an access agreement will be signing up for particular access rights and will be looking for some certainty as to prices. The prices (some possibly, but not necessarily all) may reflect the IAC, but they will not be the IAC, they will be quite specific. Indeed, if the contract outlives the Undertaking, the prices will not automatically change to those contained in some new undertaking and one wonders what ARTC

<sup>36</sup> IAA clause 4.5(a)

would intend to happen under that circumstance. As it stands, the form proposed by ARTC just does not work even for those prices that are based on the IAC.

It appears that the ENOC, though nominated in the Undertaking, is not subject to the escalation process and that ARTC is thereby free to amend this at will.

The IAA is silent about prices that are not a derivative of the IAC. Unless ARTC is suggesting that these prices are not intended to be escalated, Pacific National suggests that the IAA is flawed in this aspect as well. This is probably related to the issue of the intended coverage of the IAA discussed in response to Question 89.

Pacific National suggests that the IAA escalation provision revert to that contained in the U2002.

See also response to Question 57.

- 57) To the extent that the proposed escalation formula allows ARTC to maintain the real level of access prices and to accumulate increases over time, does this represent an acceptable balance of interests, as required under Part IIIA?"

It is a reasonable balance of ARTC's interests. It doesn't take into account the interests of ARTC's customers or the public interest. It is very difficult to think of a transport business in this country that has managed to maintain anything like real prices – ARTC's proposal will certainly be unique. In essence ARTC will be eroding train operator profitability over time as operator prices to customers continue their real decline while ARTC secures parity with CPI. It should be remembered of course that ARTC has a high fixed cost base (much of which is a sunk cost) and therefore any increment in traffic results in a large proportionate increase in profitability. ARTC will put this at risk if it seeks to insist on its escalation proposal, but as ARTC is two steps removed from the end customer, it cannot be expected to have a close understanding of the effect on end markets until volumes have been lost to rail. ARTC's insistence on placing trust in "expert" reports to determine the ability of operators to bear price increases rather than listening to its customers is most unfortunate, as even the best expert is more distant from the market place than those operating in it.

Pacific National also notes that in the '2002 Decision on ARTC's Undertaking the ACCC placed significant weight on the efficiency aspect of ARTC's escalation mechanism. As access prices were only set approximately on the basis of costs the ACCC was concerned that ARTC would have little incentive to seek efficiencies and reduce costs over time. Therefore, the CPI -  $x$  price-cap mechanism, where the " $x$ " value represents a productivity component, was important for providing incentives to achieve efficiencies over the period of the Undertaking.

In the U2002, ARTC committed to maximum prices increases as the greater of CPI less 2% or two-thirds of CPI. This provided access seekers with real price reductions. However, in the current Undertaking the  $x$  - value has been removed all together and, where a rise of less than CPI occurs, the shortfall is "banked", providing additional scope to increase prices at any time during the term of the Undertaking. This approach removes the already limited incentive that ARTC faces to seek out efficiencies. In Pacific National's view, just because conditions exist that prevent ARTC from achieving full cost recovery does not mean that ARTC should escape the requirement imposed on other regulated access providers to secure operational efficiencies.<sup>37</sup>

<sup>37</sup> The Queensland Competition Authority (QCA), in approving the QR 2005 Rail Access Undertaking, allowed a full CPI escalation, on the basis of QR having achieved efficient costs. Subsequently this was found to be subject to significant accounting error and hence under-reporting of costs. Pacific National suggests that had the true facts been available to the QCA at the time, a decision would have been made with respect to the " $x$ " value.

**3.4.9 EXCESS NETWORK OCCUPANCY CHARGE**

- 58) “What is the conceptual rationale for the Excess Network Occupancy charge?”
- 59) “Is it clear why the Excess Network Occupancy charge has been introduced?”
- 60) “To the extent that the charge is intended to reflect consumption of capacity that is greater than average or “normal” consumption, is the Undertaking sufficiently clear about how capacity is measured?”
- 61) “Does the charge promote sound decisions on the optimal size and timing of additions to capacity?”
- 62) “Is there sufficient clarity about how the Excess Network Occupancy charge will be adjusted over time to reflect changes in actual consumption of capacity relative to changes in “normal” capacity consumption?”
- 63) “Is there sufficient clarity about variances in the Excess Network Occupancy charges across segments?”

See response to Question 31 regarding the ENOC.

**3.4.10 INCENTIVES TO REDUCE COSTS AND ENCOURAGE PRODUCTIVITY GROWTH**

- 64) “Is there sufficient detail in the Undertaking about ARTC’s approach to operating and maintenance expenditures?”

ARTC appears to be equivocal about the inclusion of efficient costs in the Undertaking, in various places referring to its actual costs. For example, in the Undertaking clause 1.2(c)(i)(A), ARTC seeks to recover “all reasonable costs”. Regulatory practice in Australia has looked to service providers recovering “efficient costs”; see IPART p 15<sup>38</sup> and ACCC p 37<sup>39</sup>. While on the surface this looks to be a reasonable approach, it is suggested that the concept of efficient costs does not necessarily include “all reasonable costs” unless the relevant costs are indeed efficient.

ARTC’s costs for the most part only come into play in determining the revenue floor and ceiling and are therefore largely of academic interest only.<sup>40</sup> However, Pacific National sees it as important that the Undertaking should be true to the principles on which it is based. The retention of the principle of efficient cost should therefore be clearly enshrined within the Undertaking.

It could be argued that clause 1.1(e) achieves this purpose. The final part of this clause reads;

“... ARTC has adopted this practice with a view to ensuring that ARTC’s cost structure will reflect efficient infrastructure practice.”

To Pacific National, this clause is insufficient to bind ARTC to using efficient costs in the calculation of its revenue limits.

It is notable that the Ceiling Limit described in clauses 4.4(c) and 4.4(f) do not have any reference to the adoption of efficient costs.

Clause 4.4(d) contains several references to efficiency or prudence;

<sup>38</sup> Independent Pricing And Regulatory Tribunal, “Aspects Of The NSW Rail Access Regime, Final Report, Review Report 99-4”, April 1999

<sup>39</sup> Australian Competition & Consumer Commission, “Decision Australian Rail Track Corporation Access Undertaking”, May 2002.

<sup>40</sup> Given that none of the prices that ARTC is proposing are anywhere near the ceiling, nor for the life of the Undertaking are they likely to be for any line sectors that are not predominantly minerals based lines.

“... Out-turn\_Opext-1 is the total operating expenditure incurred by ARTC in year t-1, on an industry efficient basis.

Net\_Capext-1 is the net additions to the RAB in year t-1 (that is out-turn Capital Expenditure by ARTC less any disposals during period t-1) on a Prudent basis.

For the purpose of this clause, the optimised replacement cost means the cost of replacement by commercially efficient application of best known currently available technology based on existing capacity and performance characteristics of the asset.” (emphasis added)

“Prudent” and “Capital Expenditure” are defined in clause 9.1 as;

“**Prudent**” means in relation to Capital Expenditure, capital and renewals projects identified, and expenditure incurred, having regard to the meaning of Capital Expenditure.

“**Capital Expenditure**” means annual expenditure as incurred by ARTC incorporated in annual revaluation of the Network and Associated Facilities as contemplated in clause 4.4(d) and (e) as estimated in Schedule H. Any variation to Capital Expenditure would be limited to that which may result from:

- (a) the removal or addition of a capital or renewals project by ARTC needed to meet market demand for capacity and performance of the Network, or need to extend the economic life of Network;
- (b) the removal or addition of a capital or renewals project by ARTC resulting from what is considered to represent an efficient means to achieve that demand or extend that economic life;
- (c) whether expenditure is incurred efficiently in implementing the capital or renewals project, in the context of prevailing access and operating requirements, and input costs.
- (d) adjustments in relation to the timing of commencement and/or commissioning of projects.
- (e) the removal or addition of a capital or renewals project by ARTC that is supported by the industry.” (emphasis added)

Thus it could be argued that the RAB contains an obligation for ARTC to include only efficient costs, however the drafting is convoluted and ambiguous. If one was seeking to challenge a particular cost inclusion in the revenue limits before an arbitrator, it is not at all clear as to what ARTC’s obligation is, nor how would many of the terms be construed. This is a particular concern given that once the Undertaking is approved by the ACCC, the arbitrator (also the ACCC) is bound to rule on the basis of it. As the purpose of the Undertaking is to set out such matters clearly, this area needs to be remedied.

Pacific National raised this issue with ARTC during the “consultation process” but ARTC did not respond to Pacific National’s concerns. Pacific National also provided to ARTC drafting to remove the ambiguity and set out the principles explicitly. This drafting is shown in Appendix I.

- 65) “Does the Undertaking contain sufficient incentives to encourage ARTC to undertake efficient operating, maintenance and capital expenditures and to pursue efficiency gains?”

Pacific National is not aware of any incentives within the Undertaking to encourage ARTC to pursue efficiency gains. In particular, the escalation of prices at full CPI removes one of the more obvious incentives to innovation and productivity improvements that might be applied.

- 66) “Are there sufficient incentives to encourage ARTC to provide an efficient level of service quality, including investment in improving service quality?”

No. The Undertaking provides no incentives to achieve these outcomes. Investment is left wholly within the control of ARTC and the Undertaking provides no process for input by stakeholders into the investment process. Pacific National regards this as inappropriate in the circumstances where ARTC is effectively steward for a key economic enabler for Australia. Without the normal profit incentive, the logical rationale for ARTC’s continued provision of the network is to make it available to users, in fulfilment of government policy that ARTC is an enabler of the provision of efficient rail transport solutions for Australia. Both of government and network users have a high degree of interest in the state of the network and any consideration of capacity expansion. Yet the Undertaking is devoid of any obligation on ARTC to even consult, let alone take into consideration the interests of other parties.

During the “consultation process”<sup>41</sup> Pacific National suggested a process for consideration of investments outside of the Hunter Valley and also a series of criteria by which investment could be measured. ARTC did not respond to either of these. Copies of the process and criteria are included in this submission at Appendix F.

- 67) “Are there any other issues of concern arising, from the proposed access pricing, cost allocation and/or asset valuation methodologies?”

No. Pacific National’s concerns regarding these issues are documented elsewhere throughout this submission.

### 3.5 PART 5: CAPACITY ALLOCATION

- 68) “Is there sufficient clarity about the rationale for the reservation fee and how the reservation fee policy would be applied?”

- 69) “Is it appropriate to “reserve” capacity from the date the access agreement is executed?”

- 70) “Is there sufficient detail in the Undertaking about the how ARTC would measure capacity during the reservation period?”

- 71) What signal is the reservation fee intended to give to access seekers? “Is the Undertaking sufficiently clear on how the opportunity cost of reserved capacity would be estimated?”

- 72) What are the likely effects of introducing a reservation fee, particularly for entry by smaller operators?”

- 73) What are the effects of the absence of limits on price differentiation on reserved capacity?”

Questions 68 to 73 are answered together.

The Undertaking introduces the concept of a “reservation fee” where an applicant wishes to negotiate an agreement more than 6 months prior to the commencement of services. This looks to have picked up on the similar proposal by QR in its 2006 Access Undertaking.

<sup>41</sup> Pacific National does not regard the current processes labelled by ARTC as “consultation” as being anything of the sort. Typically ARTC forms a decision, puts that decision to stakeholders as a fait accompli and asks for comments. It then routinely ignores any comments other than those that result in minor amendments to its position. It then trumpets that it has consulted!

The proviso in clause 5(2)(a)(i) of the Undertaking that the capacity is available between when the agreement is negotiated and when it commences is a very strange requirement. Pacific National sought explanation from ARTC on this matter but received no response. Pacific National has not been able to understand why there would be a need for the capacity to be available before it is required. If there is a valid explanation, then ARTC should provide it. The commentary provided in the Explanatory Guide (page 27) does little to shed light on this issue except to show that ARTC's point of view is that of managing a network of fixed capacity. Pacific National rejects this as an inappropriate position to take. ARTC must be responsible for providing capacity to meet demand. Thus, if an access seeker seeks capacity that requires ARTC to build extra capacity to provide, it is surely appropriate for ARTC to build that capacity – this does not give rise to a need for the capacity to be available prior to it being required. In fact ARTC's explanation appears to be the reverse of this situation in that ARTC is concerned it will not be able to sell capacity that is available prior to the reserved capacity being used – so ARTC's argument appears to be that it has difficulty selling capacity that it hasn't actually sold and wishes to penalise a party that is willing to buy that capacity at some future time. Granted, once it has provided a commitment to sell capacity at some time in the future it may have difficulty in selling the residual capacity prior to that time, but that is not the fault of the party buying access in the future, it is a matter of not having sold that capacity in the first place. If ARTC wants to retain the capability of selling that capacity into the future, it is ARTC's role to augment the network so that it is able to provide both the future capacity being contracted and retain the ability to sell the current capacity.

The ability to negotiate access ahead of time is important. The deployment of new rollingstock and terminal space can take at least two years from the time a decision has been taken to invest. It is imperative for an operator to know at the time it places an order for such assets that it can secure the train paths necessary to make use of them. Pacific National sees it as normal prudent commercial behaviour to secure access rights well ahead of the commencement of operations. This does not mean, however that there is a logic in charging a reservation fee for the privilege of being allowed to do so. The normal expectation is that the service provider would so manage its business as to have the capacity available when required rather than immediately quarantining the capacity at the point of contracting.

The limits on differentiation of charging do not apply to arrangements made under this part of the Undertaking. It is possible this was required to allow the application of the reservation fee, but it is not restricted to that and therefore allows all charges to vary. As this appears to be very specific drafting one must question why. Again Pacific National has asked ARTC to explain this but no explanation has been forthcoming.

It is noted that the QCA, while recognising the benefits to forward planning of allowing for paths to be negotiated up to 2 years prior to commencement of operations, rejected the concept of applying a reservation fee.<sup>42</sup> Pacific National is not aware of any substantial differences in the ARTC network such that a different result should arise.

The reservation of "absolute discretion" in Undertaking clause 5.2(a) with respect to these arrangements seems inappropriate. In effect this over-rides the whole provision; ARTC has no obligation to enter into the arrangement even if the access seeker meets the stated criteria. This is inappropriate. If the intention is that ARTC will enter into these arrangements, it should not seek to have any discretion, let alone "absolute discretion" unless the discretion is necessary to make the provision work. Any discretion that is required to make the machinery workable should be adequately justified and qualified to achieving that aim.

---

<sup>42</sup> QCA Decision QR's 2005 Draft Access Undertaking December 2005 p 174

- 74) “Is there sufficient clarity about ARTC’s proposal for awarding access rights in the case of applications for mutually exclusive train paths?”

See response to Question 21 and Appendix G.

- 75) “Are the provisions dealing with cancellation of paths in the event of under utilisation (“use or lose” provisions) appropriate?”

- 76) “Are the current “use or lose” provisions appropriate, for all traffics?”

Questions 75 and 76 are dealt with together.

A key issue that has not been addressed specifically within the ACCC’s Issues Paper is the appropriateness of the capacity allocation model within the Undertaking. This is discussed in Section 4.3.

The “use it or lose it” provisions follow from the capacity allocation model chosen by ARTC. It is therefore necessarily flawed. These provisions are set out in the IAA clause 9.5. They do not appropriately address the needs of a number of existing traffics. A single approach based solely on regular timetabled services does not lend itself to the reality of the diversity of traffics on the network. ARTC is now manager of a complex network with a wide diversity of traffics. The Undertaking must reflect this reality or:

- a) it will have significant negative impacts on the efficiency of access provision; or
- b) ARTC and operators will recognise the dysfunction caused and find ways to ignore the Undertaking.

Neither of these are appropriate outcomes. The Undertaking needs to be amended to ensure it fulfils its intended role ie that it delineates the boundaries of the relationship between access seekers and ARTC in circumstances where ARTC wields excessive bargaining power due to its monopoly status.

To give an example of the problem, an irregular traffic such as grain would be likely to trigger the standard “use it or lose it” provisions almost continually due to the variability of operations demanded by supply chain considerations.

Pacific National has several times brought this to the attention of ARTC, but, ARTC has chosen to ignore the issue. Pacific National has provided drafting to ARTC with the Model Undertaking - General to address the issues with the “use it or lose it” provisions. This drafting is presented in Appendix H.

A further problem not addressed by ARTC is that the current drafting allows for the triggering of the provisions for mere late running of trains. This is assumed to be unintentional, but ARTC has chosen not to address the issue. Again the drafting in Appendix H seeks to obviate this problem.

### 3.6 PART 6: NETWORK CONNECTIONS & ADDITIONS

- 77) “Are the obligations on ARTC to provide additional capacity appropriate, including the processes where an access seeker satisfies the additional capacity criteria in clause 6.2(a)?”

The provision in Undertaking clause 6.2, in practice, covers only the case where an individual access seeker is able to request additional capacity and pay for it. While there may be instances where this might occur, it is likely to be an atypical circumstance.

Network capacity is generally not specifically tied to the operations of a single network user, once it is in place, it is more usual that all network users will make use of the capacity that is generated (eg an additional crossing loop). There are also conceptual

issues that make it difficult to recognise capacity as associated with a particular user.<sup>43</sup>

The more likely circumstance is that there is a general requirement for increased capacity on the network. The Undertaking does not address this possibility at all and it is a substantial flaw in the document. Pacific National has raised this issue with ARTC, including drafting of an appropriate investment process and criteria by which investment proposals should be measured, but received no response. A copy of the Pacific National proposal is provided in Appendix F.

78) “Is it appropriate for ARTC to earn a rate of return on capacity funded by an operator?”

Pacific National does not see the logic in allowing ARTC to earn a return on any gifted asset. The purpose of providing a rate of return is to reward the investor for the risk in the investment. As ARTC is not the investor, it has no right to the reward. Given that a substantial part of ARTC’s network has been (and continues to be) gifted by other parties, Pacific National suggests that this would have a material impact on the portion of the asset base that ought to be considered as appropriate to earn ARTC a return. In support of this view, Pacific National suggests it was always open to the Commonwealth to transfer the value of the network at its replacement value as equity, but chose to do so at a substantially written down book value. Presumably the Commonwealth was happy to do so and forego the returns that it might otherwise have expected to earn had it valued the network on a DORC basis. Similarly, the Commonwealth has more recently gifted ARTC large grants (many times the book value of the network) rather than placing these funds as equity. The gifting of the funds, rather than placement as equity, indicates that the Commonwealth is not expecting a return on these funds.

See also responses to Question 35.

79) “Are the Undertaking provisions on ARTC’s commitments in respect of additions to capacity fully funded by an access seeker appropriate?”

Noting the issue in Question 77, that the likelihood of a single access seeker wanting additional capacity is low compared to the more general requirement, the provision in the Undertaking is reasonable to cover that circumstance.

Pacific National is concerned that the qualification in clause 6.2(b) “In the event ARTC agrees to the creation of Additional Capacity ...”, is couched terms that make the provision of infrastructure discretionary. This appears to be at odds with the commitment in clause 6.2(a) “ARTC will consent to the provision of Additional Capacity if ...” which indicates a positive commitment if certain criteria are met. It would be helpful for clause 6.2(b) to be redrafted to clarify that ARTC will honour the commitment if the criteria are met.

80) “Is there sufficient clarity about how capacity funded by an operator would affect that operator’s access charges?”

An issue that has arisen under the NSWRAU is whether ARTC should require network users to fund the full cost of a project or the agreed cost. The issue is whether ARTC should take construction risk on a project where it has agreed a scope and cost with

<sup>43</sup> For example, if a cross takes place at the new crossing loop, has this advantaged one or both of the trains crossing? If the cross did not take place at that location what would the impact have been on the other traffics using the network – it doesn’t take much to make fruitless any attempt to trace through the consequences and assign “advantage” to one party or another. The answer almost inevitably is that all network users are advantaged in one way or another. Even an example where a crossing loop is extended for the benefit of one user does not resolve to a simple answer as other users might be advantaged by the increased capability of the network even if they themselves do not use longer trains.

network users. Under the drafting in the Undertaking, it is clear that ARTC expects the proponent to pay all of ARTC's costs ie ARTC expects the proponent to take the risk in construction. This position is different with respect to the capital expenditure that is included in determining the economic cost of a line segment where only "prudent" costs are added to the asset base.

Pacific National believes that where ARTC is the project manager and controls all aspects of construction of additions to the network, it is appropriate that ARTC bears the construction risk. The proponent is entirely in the hands of ARTC with regard to the management and delivery of the outcome; ARTC is by far in the best position to estimate the costs of delivery and to manage the project to achieve that outcome. It is therefore inappropriate that ARTC should seek to avoid responsibility for competent management of delivery of the product. Further, without appropriate disciplines, ARTC has no incentive to manage the project within an agreed budget and under the current drafting, the proponent is committed to paying ARTC's costs, whatever they may be.

### **3.7 PART 7: NETWORK TRANSIT MANAGEMENT**

- 81) "Do the traffic decision-making matrices in the Undertaking provide sufficient clarity about the way ARTC would make decisions about network transit movements?"

Generally speaking, Pacific National agrees with the traffic decision matrix proposed in the Undertaking. However, this is a matter requiring detailed consideration by practitioners in the field. Pacific National suggested to ARTC that this was an area where it would be most appropriate for a workshop of practitioners to go through the matrix in detail. Unfortunately ARTC has not responded to this suggestion. Pacific National suggests that it would be appropriate for the ACCC to encourage such a workshop.

As discussed elsewhere in this submission, a disappointing aspect of the Undertaking is the lack of any recognition of the inter-relationship between ARTC's network covered by the Undertaking and adjacent networks. The Undertaking does not even recognise the Hunter Valley network that ARTC intends to deal with under a separate regulatory document, let alone neighbouring networks owned by other parties. Thus the train decision matrix, while internally consistent, stands in isolation from the rest of the interstate network. As there are few journeys on the interstate network that lie wholly within the jurisdiction of the Undertaking, this is a significant flaw. The lack of recognition of other networks and their inter-relatedness, particularly in areas such as train planning and traffic management, is particularly egregious given that ARTC sees itself as a leader in the industry and its Undertaking has been nominated by COAG as the model for all access regulation in Australia.

**3.8 PART 8: PERFORMANCE INDICATORS**

- 82) “Is the system of KPIs proposed by ARTC in the Undertaking appropriate?”
- 83) “Do the KPIs provide information on those aspects of ARTC’s performance that are most important to operators?”
- 84) Any comments on the adequacy of KPIs dealing with ARTC’s capacity to deal with delays due to operators entering the network late?”
- 85) “How does the absence of a KPI relating to the exit from the network of an unhealthy service affect this?”
- 86) What should a system of KPIs include in order to measure the infrastructure owner’s ability to respond to problems in the network caused by operators?”
- 87) “Is the unhealthy/healthy train approach used by ARTC appropriate?”
- 88) “Are the indicators appropriate – for example, should the indicators reflect actual and planned transit times?”

Questions 82 to 88 are answered together.

ARTC has added several indicators measuring transit time, both at a planning and operational level. While these have yet to be seen in operation, Pacific National supports the concept of these new indicators as a significant step forward in reporting.

In the past, Pacific National has been critical of the “healthy train” emphasis in performance reporting as this measure has had a number of practical flaws that reduce the value of the resulting reports. The change in the definition of “healthy” to allow for a train to regain its “healthy” status is a significant improvement and is strongly supported by Pacific National. Previously, a train that became “unhealthy” retained that status regardless of whether it later regained its timetable. Under that arrangement, the train was potentially disadvantaged even though it was ostensibly on time. This has now been remedied.

An issue that is still not, in Pacific National’s opinion, adequately addressed is the reporting of end to end journeys. Clearly this is a difficult matter as it usually involves more than one network owner. However a step forward in this direction that could be addressed in the Undertaking is the recognition that trains entering the network late from an adjoining network should not automatically be seen as “unhealthy”. Late entry into one network may be occasioned by a number of reasons, some above rail and some below rail. It seems unhelpful to report the “health” of a train as “unhealthy” in circumstances where the entry is not the fault of the operator.

**3.9 SCHEDULES**

- 89) “Are the provisions in the Indicative Track Access Agreement consistent with the access Undertaking?”

**Application Of IAA**

It is instructive that the IAA applies only to “Indicative Services”<sup>44</sup>. This is a change from the IAA contained in U2002 and the reason for the change should be explained. As it stands one is left with the impression that ARTC will feel free to negotiate on any

<sup>44</sup> See front cover of IAA (Schedule D to the Undertaking) – which ironically is the second last page as published by ARTC.

basis it sees fit for train services other than indicative services – this surely is not the intention of the Undertaking.

The Undertaking on clause 3.11(b) appears to provide some protection. It reads;

“The Access Agreement must, unless otherwise agreed between ARTC and the Applicant, be consistent with the principles outlined in the Indicative Access Agreement and must address at least the matters set out in Schedule C. The details of Schedule C do not provide an exhaustive list of the issues that may be included in an Access Agreement.”

However, this is a very minimal protection given that ARTC is able to argue that the principles in the IAA are specifically addressed to indicative services only.

Pacific National suggests that it is important that the restriction on the applicability of the IAA be removed, or in the alternative ARTC;

- a) provide a valid explanation of for the changed status of the IAA, and
- b) modify Undertaking clause 3.11(b) so that it provides appropriate protection to access seekers.

### Consistency

Generally, the IAA is consistent with the Undertaking. One issue of inconsistency that Pacific National has noted is contained in Schedule C. Schedule C deals with matters that must be included in any access agreement under the Undertaking. It includes a new term;

“termination of access agreements on termination or cessation of ARTC’s leasehold rights”.

This is not mentioned anywhere else in the Undertaking and does not appear to be reflected in the IAA except possibly by oblique notes in Schedule 1 which qualify the description of the network. An example of these notes is taken from p 46 of the IAA;

“\*\* To the extent that such railway lines are leased by RIC and SRA to ARTC”

Any provision that purports to release ARTC of its obligations under the contract should be clear and explicit. Pacific National would argue that the notes in Schedule 1 are at least ambiguous. Pacific National sees those notes as having the sole purpose of defining what is and is not included in the network at the execution of the document. They are therefore ineffective to exclude parts of the network from the contract where they were considered to be included at its commencement.

ARTC should explain its intentions with regard to this requirement. If ARTC wishes to insist on this carve out of its obligations, an access seeker would necessarily need to be able to examine the lease documentation in order to ascertain the level of risk that attaches to the lease and likelihood that ARTC may lose its leasehold. It is also unclear why this relates only to leases, given that ARTC could lose any part of its network due to any number of reasons and presumably this would be covered by normal force majeure provisions.

See also Appendix A for specific drafting inconsistencies.

- 90) “Are the provisions dealing with indemnities and assignment of responsibilities to ARTC and operators (in the Undertaking and in the Indicative Track Access Agreement) clearly set out and do they achieve an appropriate balance of interests as required under Parl IIIA?”

Generally, Pacific National supports the liability and indemnity provisions within the IAA. These provisions in the IAA to U2002 caused numerous problems for all parties and the revised approach is most helpful. Pacific National expects that the new

drafting will substantially reduce the difficulties of resolving claims. There are several matters of drafting with relation to these provisions that are raised in Appendix A.

91) “Is the Undertaking sufficiently clear on the segments that make-up the ARTC network?”

No.

The text description in the Undertaking does not appear to match the graphical information provided in Schedule E. For example Schedule E excludes sector 915 (Islington Junction to Scholey Street Junction) but in the diagram in Schedule E this appears to be included.

Schedule 1 to the IAA also includes the following lines which are not mentioned in the text or contained in the diagrams:

- Goobang Junction to The Gap
- Merrygoen to Ulan

Clearly ARTC is confused as to which lines it intends to be covered by the Undertaking. Pacific National pointed out to ARTC during the “consultation process” that there were discrepancies in the description of the network but ARTC has not amended the description.

92) “Is there sufficient detail on the nature and extent of capital expenditure that ARTC commits to undertake during the term of the Undertaking?”

It is Pacific National’s understanding that there is no commitment by ARTC in the Undertaking with regard to making any capital expenditure. See response to Question 32.

#### **4 ISSUES NOT COVERED UNDER THE ISSUES PAPER**

This section of the submission covers areas that were not specifically raised in the ACCC Issues Paper. Detailed drafting issues concerning both the Undertaking and the IAA are presented in Appendix A.

##### **4.1 RELATIONSHIP OF UNDERTAKING TO PROPOSED HUNTER VALLEY UNDERTAKING**

Pacific National is very supportive of ARTC’s intention to have a separate undertaking to cater for the Hunter Valley coal traffic. The arrangements for that traffic are substantially different to the requirements of the rest of the network and other traffics. However, Pacific National has significant concerns regarding the adoption of a geographic split rather than adopting a separation that is both geographic and traffic specific.

In considering the effective operation of the Undertaking, a key concern is the interrelationship between the Undertaking and its proposed companion undertaking for the Hunter Valley. During the “consultation process”, Pacific National and others raised with ARTCs the concern that the lack of any detail about the form of the Hunter Valley undertaking and the management of the interfaces created between the two undertakings made it difficult for PN to comment on that form in any specific manner.

Pacific National provided discussion in its submissions to ARTC that highlighted a number of difficulties arising from the geographic split of the network proposed by ARTC and also posed a number of questions. Unfortunately ARTC has chosen to ignore these concerns and has neither explained its rationale for adopting the proposed form of the Undertaking nor has it addressed the consequences of adopting that form. It was clearly open to ARTC to explain in detail how it expects the Undertaking to work, to articulate the concerns raised by Pacific National and other parties and how ARTC expects to overcome those concerns. That ARTC has chosen not to do

this, and instead, to barely mention the fact that there will be two undertakings is a significant concern and speaks to ARTC's own lack of confidence in its proposed solution.

Pacific National suggests that it would be extremely unwise for the ACCC to approve the Undertaking without understanding at least the basic provisions of the proposed Hunter Valley undertaking so that the interaction between the two documents can be understood.

The fundamental problem is that the Undertaking is an undertaking relating to only a portion of ARTC's rail network with a separate undertaking to cover the Hunter Valley region, a region that connects at a number of points with the network covered by the Undertaking. ARTC intends for the split between the two documents to be on the basis of geography, with the Undertaking including all ARTC controlled track except:

- the Hunter Valley coal roads (and, for the purposes of charging, the Sandgate fly-over),
- the Werris Creek line from Muswellbrook, and
- the lines from Muswellbrook to Merrygoen via Gulgong, Werris Creek to Dubbo and Dubbo to Parkes (though is some inconstancy in the documentation with respect to these lines as noted in the response to Question 91).

A region specific undertaking that would apply to all traffics passing through that region has the problem that traffics seeking paths through multiple areas (eg interstate intermodal trains) would need to deal with an additional undertaking and hence the path allocation processes, commercial arrangements and interfaces in the Hunter Valley undertaking would need to mirror those of the Undertaking to avoid unnecessary inefficiency. Taken to its logical conclusion, there would be no benefit in having a separate undertaking for the Hunter Valley as the level of conformity with the rest of the network for the non-coal traffics would need to be substantial. While it would be possible to cater for the differences through a series of schedules to a common undertaking, this would require duplication of much of the document.<sup>45</sup>

It is clear that in the Undertaking ARTC has attempted to isolate those traffics using Newcastle as a destination (eg the coal, grain and minerals traffics). While there is some logic in this approach, unfortunately it is ineffective as there remains a significant volume of traffic that utilises both parts of the network. Examples include:

- container and steel traffics using Morandoo and Bullock Island (which are both parts of the ARTC Newcastle terminal),
- domestic grain movements, minerals traffics and coal traffics continuing on to the RailCorp network,
- through intermodal services using the coal roads for traffic convenience,<sup>46</sup>
- intermodal services being rerouted via the inland route due to track closures,
- export coal from Stratford,
- export coal from south of Newcastle (from the RailCorp network),
- domestic coal movements to destinations south of Newcastle.

By splitting the network in the manner proposed, it will be necessary for all of these traffics to be covered by two separate contracts, one under each of the ARTC undertakings, in addition to the contracts required for other networks. This would cause a significant level of unnecessary

---

<sup>45</sup> This problem does not occur under the NSWRAU due to the high level nature of that document. Most of the arrangements that occur specifically for the Hunter Valley coal traffic are in the nature of custom and practice. While this has worked reasonably well up to the present, it is better that these practices are formalised through an Undertaking to recognise the changed ownership of the network.

<sup>46</sup> As currently defined in Schedule E, all traffic travelling south of Newcastle, including all intermodal trains would travel on the Hunter Valley network, but it is assumed that this is in error and that ARTC does not intend for line sector 915 to be excluded from the Undertaking.

administration and complexity. Pacific National's experience with ARTC in operating under two different contracts for many of its traffics is that ARTC has difficulty in managing such a situation efficiently.

The conclusion that Pacific National draws is that a traffic **and** region specific Undertaking is required to cover the Hunter Region coal and that the Undertaking ought to cover all other traffic for the entire ARTC network (including non-Hunter region coal). Adopting this approach would obviate many of the issues that arise from having non-coal traffic use the Hunter Valley network. If this solution was adopted, there would remain some interface issues between the two Undertakings, but these would be relatively minor and can be easily addressed through:

- ensuring both documents are consistent on key matters such as traffic management, and
- providing a clear order of precedence between the Undertakings where conflict might arise.

If ARTC is determined to follow a geographic only split, then the following questions need to be addressed in the Undertaking:

- The terms and conditions for access to ARTC terminals (at least the existing Newcastle terminal).
- Does ARTC intend that access seekers will be required to hold separate contracts under each undertaking? If so what process does ARTC intend to use to ensure that the terms and conditions are consistent between the contracts for traffics that require to operate under both?
- Will the negotiation of an access agreement for one territory be dependent on negotiations for access to the other and how does ARTC intend to manage this? There is nothing within the Undertaking that contemplates a dual negotiation.
- How will ARTC manage the path allocation process between the two regions and how will inconsistent outcomes be resolved?
- How will ARTC manage trains (ie live run) between the two regions?
- Does ARTC intend to strictly enforce the separate usage of tracks in the Newcastle region (ie not allow Undertaking traffic to use the coal roads when this would be the most efficient manner of controlling the network)? If not, what manner of contract does ARTC envisage covering such ad hoc use of the Hunter Valley network?<sup>47</sup>
- How does ARTC intend to allocate costs between the two jurisdictions for calculation of floors and ceilings (eg non-sector specific costs, corporate overheads)?<sup>48</sup>
- Where incompatible outcomes arise from the undertakings how will these be resolved?

The only effective way to address these uncertainties is for ARTC to concurrently put forward the two undertakings. Pacific National would strongly support this approach. The alternative is for ARTC to make clear how it intends to address these issues. But this is a poor alternative as it requires follow up to ensure that the ultimate result does in fact deal appropriately with those issues.

Subsequent to its initial submission to ARTC, Pacific National provided ARTC with a series of documents including model undertakings for a Hunter Valley coal undertaking and a general

<sup>47</sup> Current practice is that train controllers will make use of the coal roads to most efficiently manage non-coal traffic on occasion. As it is currently formulated, this could not happen without the operator holding a separate access contract with ARTC for use of those coal roads under whatever regulatory document applied to those roads.

<sup>48</sup> The Undertaking covers allocation of costs within the Undertaking network, but is silent on allocation to the Hunter Valley network.

interstate undertaking (the MUC and MUG).<sup>49</sup> Those documents looked specifically at the problem of dealing with Hunter Valley coal in the wider network and worked through the options. The conclusion that Pacific National draws from its consideration of these issues is that the best solution is to have two undertakings:

- a traffic and region specific undertaking to deal with Hunter Valley coal; and
- a general undertaking covering the entire network for all other traffics.

Clearly this solution gives rise to an unusual situation where the same infrastructure is providing services under two separate undertakings. However, Pacific National has been unable to find a solution that is better able manage many of the interface issues that otherwise arise.

It has been suggested that this solution might not be possible under the Trade Practices Act. In researching this alternative Pacific National has received legal advice is that there is no inherent impediment arising from the Trade Practices Act to this arrangement provided that the services to which each undertaking applies are clearly delineated and differentiated (ie that it is not possible to gain access to the same service via both undertakings). The service of provision of access for coal haulage in the Hunter Valley is capable of appropriate differentiation from the service of providing access to general freight on the entire ARTC network. A copy of legal advice from Clayton Utz on this matter is attached as Appendix C. Pacific National's proposed form, as demonstrated in the MUG and the MUC conforms to these requirements.

The issue of the need for separate access undertakings and the form of those undertakings is discussed further in Appendix B.

#### 4.2 PRICE STRUCTURE CHANGE

ARTC is seeking to radically alter the structure of access prices for a number of traffics in two dimensions;

- A wholesale change in the structure of rates from so called 'commodity rates' to the uniform fixed and variable structure, and
- A more subtle adjustment between the flagfall and variable components of the charge.

In the main, these prices sit outside of the Undertaking as they do not fit within the parameters of the IAC. The largest impact of the proposed change in structure relates to bulk traffics in NSW that are currently under the NSWRAU.

As noted in response to Question 30, the new structure doesn't fit many of these traffics well. The change will disturb existing contractual arrangements and does not seem benefit ARTC's customers or the facilitation of competition in any material way.

Pacific National's analysis is that the proposed changes will result in substantial winners and losers. The current commodity rates have been set on a Ramsay price basis and the changes will result in substantial windfall gains to some customers. Given this Ramsey pricing approach, where prices rise, customers are likely to seek an alternative solution. Many of Pacific National's traffics affected by the proposed change are subject to either road or marine competition. Access prices are a substantial input cost to a train operator and increases would almost certainly have to be passed through to end customers. A graphic example of this is currently unfolding in Victoria where substantial increases in access charges for use of the Victorian regional network have had to be passed on to customers. The result is a significant shift of traffic away from the Victorian rail network. Pacific National is aware of a number of bulk traffics in NSW that will similarly be affected by the proposed price changes. Prices for some movements will also fall dramatically, with some reducing to 20% of current prices.

<sup>49</sup> The MUG and MUC have been circulated to a number of industry stakeholders and are available from Pacific National on request.

While Pacific National does not endorse a Ramsey pricing approach, there does seem to be any good reason that prices should reduce where the market has demonstrated a willingness to pay those prices and no rents are being extracted.

Another example is the movement of bulk petroleum. This is a commodity that is moved in relatively small trains around NSW. While the structure of the access charge for this commodity is not changing, the relative proportions of the flagfall and variable charge are. The effect on small trains is disproportionate compared to a large intermodal train. As this is already a marginal traffic for rail, it is a prime candidate for take-over by road. Some petroleum access prices will effectively rise by 99%.

ARTC has not provided its customers with any analysis of the effect it expects the changes to have on its customers and this is a particular problem because train operators do not have access to all of the information required to fully understand the implications of the changes. Discussions with ARTC indicate that it either fails to understand the impacts of its proposal, or has chosen to disbelieve that those impacts will arise.

The effect of removing these charges from consideration by the ACCC is that a key level of scrutiny will be avoided. Any miscalculation or misunderstanding by ARTC will fall on the industry to bear without the benefit of any careful independent consideration. Pacific National's experience is that ARTC has a strong belief in its own understanding of the industry that is not necessarily in accord with reality and is unresponsive to industry concerns about its actions.

#### 4.3 INAPPROPRIATE PATH MODEL

The Undertaking has a "one size fits all" approach to path allocation and therefore fails to address the needs of different traffics for different pathing arrangements. Once again, Pacific National pointed this out to ARTC in two different submissions, but ARTC has chosen not to even respond to the issue, let alone deal with it in an appropriate fashion.

The path allocation model chosen by ARTC is that an access seeker will purchase a path for a specified period<sup>50</sup> and that path is allocated to the access seeker.<sup>51</sup> This generally works well for intermodal traffics that have a regular passage and can therefore be routinely timetabled (eg like a bus, with a known departure point and arrival point and planned departure time). But a number of traffics operating on the network, particularly in NSW, do not fit those criteria. For example, the allocation of fixed paths for traffics such as grain that display a substantial level of irregularity would result in;

- a reduction in flexibility of operations,
- raise the spectre of almost continual failure to meet the "use it or lose it" provisions,
- impose unnecessary rigidity between train operators through the fixed assignment of paths to a particular operator,<sup>52</sup>
- impose additional costs that are not currently incurred by such traffics (eg application of a more rigid flagfall charge).

What is required to address this and other situations is a series of pathing models that provide the appropriate levels of flexibility and capacity required by the different types of traffic. Pacific

<sup>50</sup> The undertaking is equivocal on this point. Nominally one ought to be able to purchase paths for different durations under an access contract. However past experience with ARTC indicates they are unwilling to contract on this basis, requiring the train paths in a particular contract to run for the entire course of the contract. For example, Pacific National would like to contract for additional paths for a period of 3 months each year to cover opportunities for additional intermodal traffic during the peak season, but ARTC has refused to contract paths on this basis, preferring instead to offer paths on an ad hoc basis each year (if available).

<sup>51</sup> While paths are offered on licence basis and are not exclusively assigned to the operator, the effect is an exclusive licence as ARTC contracts not to offer the path to another operator during the life of the contract.

<sup>52</sup> This could have a significant impact on competition for such business as it would more significantly impact a small operator with few trains compared to a large operator with a large fleet that is better able to make use of the assigned paths through greater deployment flexibility of the available fleet.

National suggested an alternative capacity allocation model to ARTC in its first submission that provides this outcome. A copy of the process is contained in Appendix G. That process is more completely demonstrated in the MUG and MUC.

#### 4.4 INSURANCE

ARTC claims that it has increased the insurance coverage under the Undertaking to \$250m in order to have consistent arrangements across the network where it is under an obligation to the NSW Government to apply a minimum of \$250m.

While this might be appropriate for access seekers that operate in NSW as well as on other parts of the network, there seems to be little reason to require this increased coverage from those operators that do not operate in NSW. In fact it is far from clear that ARTC has an obligation imposed on it to provide that level of coverage. Pacific National's understanding is that it is a matter for the relevant party under the NSW rail safety legislation to have an appropriate level of insurance. While it is true that RailCorp requires a minimum \$250m general liability insurance coverage, that has been explained to Pacific National as being due to movements within the Sydney metropolitan area. Pacific National is not aware that the same obligation would necessarily apply to operations outside of Sydney. A far more robust explanation is required from ARTC to justify placing this burden on all operators, some of whom may have no access rights in NSW at all.

Pacific National supports the goal of having "consistent arrangements over the whole network"<sup>53</sup> where this makes sense, however, insurance does not appear to be a matter that lends itself to uniformity. Pacific National's view is that the level of insurance required should be driven by the level of risk arising from a particular operation. While there may be a number of common risk elements in rail operations, Pacific National would argue that there are likely to be differences depending on the circumstances and, rather than adopting ARTC's approach which seeks consistency, it is appropriate to consider whether some level variation is appropriate in the particular circumstances to avoid placing an unnecessary burden on a particular party.

#### 4.5 FAILURE TO TAKE A WHOLE OF NETWORK APPROACH

##### Management Of Horizontal Interfaces

"A key objective of ARTC's lease in NSW has been to deliver improved performance and capacity of the rail network between Melbourne and Brisbane (via Sydney) ("North-South rail network") through strategic investment in that network to enable the performance of the network to meet market requirements in terms of reliability, transit time, availability and yield, as well as through more holistic management of that network, including delivering greater consistency in access regulation to the interstate rail network more broadly. This undertaking forms a key part of ARTC's strategy to deliver on this objective."<sup>54</sup>

Pacific National's view is that the Undertaking, far from assisting to deliver "holistic management" of the interstate network, detracts from that worthy objective. Pacific National has raised with ARTC the need for the Undertaking to explicitly recognize the horizontal interfaces between ARTC and the networks which it adjoins (not the least its own proposed Hunter Valley region!). Pacific National sought ARTC to undertake an obligation to work to minimise these interfaces. It is recognised that this could not impose a requirement on the achievement of any specific outcome, but at the least, it would be indicative that ARTC recognises the inter-relationships of the various parts of the network and the need to manage the network with an eye to achieving the best outcomes overall.

<sup>53</sup> ARTC Explanatory Guide p 25

<sup>54</sup> ARTC 2007 Interstate Access Undertaking Explanatory Guide p 4

It is most disappointing that this issue has neither been acknowledged nor responded to by ARTC. COAG has placed a great deal of faith in the ARTC Undertaking as a model for all rail access undertakings across the nation and it would be a very poor outcome if that model was one which pretended that the interactions between networks were irrelevant. For example, the allocation of train paths (ignoring the problems with the allocation model previously alluded to) solely within the ARTC non-Hunter Valley network without regard to the paths that might be allocated in adjacent networks will (and currently does) lead to inefficient train pathing across the "borders". By refusing to work collaboratively across networks, network owners have created their sets of borders that are every bit as disruptive as the State borders that ARTC was supposed to eliminate.

It is acknowledged that there is informal communication between network owners regarding the allocation of train paths from time to time, but this is ad hoc, dependent on the personalities of the people involved and unstructured. In Pacific National's experience it is far more often the case that the train operator sorts out the pathing in each jurisdiction in order to achieve a sensible outcome.

### **Need For A Possessions Planning Process**

In a similar vein, the Undertaking is silent on the need for a comprehensive possessions planning process. Track possession is the term for when the network owner closes the track to traffic in order to perform maintenance. It will be readily appreciated that a closure on the Sydney – Brisbane corridor on one day and the Sydney – Melbourne corridor the next will have a far more substantial impact on Brisbane – Melbourne traffic (and most other corridors as well) than if the possessions can be coordinated to occur on the same day. This is not always achievable, but it often is achieved or the effects of possessions ameliorated through close cooperation between the track owner and train operators.

The impacts can be even further reduced if different network owners will cooperate to plan their possessions together. Obviously a Sydney – Brisbane train has little advantage if RailCorp chooses to close the Sydney – Newcastle network one day and ARTC the Newcastle – Queensland border the next, and it is worse again if QR chooses the third day to close its 100km of track to Brisbane, regardless of how well ARTC is coordinated itself.

Again, Pacific National notes that the Undertaking cannot oblige ARTC to have particular outcomes with other network owners, but it can:

- a) oblige ARTC to have an appropriate possessions planning process for its own network; and
- b) recognise the importance of coordination with other network owners and require ARTC to make reasonable efforts to plan network possessions across all relevant network owners.

It is noted that ARTC does interact with some network owners in an attempt to plan possessions on a coordinated basis and, by and large, while far from perfect, these do have a substantial benefit in reducing the effects of network possessions. However, this is a matter that ought to be recognised in the Undertaking and given force by it.

Pacific National provided drafting to ARTC to cover a possessions planning process. This is shown in Appendix G.

### **Third Party Works**

The IAA contains a provision (IAA clause 9.4) regarding third party works on the network. Pacific National recognises that ARTC might be required at times to permit third parties to perform work on the network. However, the drafting in IAA clause 9.4(b) absolves ARTC from all liability to operators with respect to third party works.

Pacific National believes this is an inappropriate absolution of ARTC of any responsibility for the network. Train operators rely on ARTC to provide a network that is safe to operate on, yet this provision removes any responsibility from ARTC totally where a third has caused an incident. If an operator is not able to rely on ARTC to provide a safe network, to whom should the operator look? ARTC's accreditation would not support its walking away from providing a safe network. It is Pacific National's strong view that ARTC cannot resile from its liability to provide a network fit for purpose regardless of who or what other party is involved.

#### **4.6 OTHER ISSUES NOT COVERED IN THE UNDERTAKING**

Experience over the life of the U2002 indicates that a number of other matters ought to be addressed that are not appropriately covered in the Undertaking. These are noted in brief below. Pacific National stands ready to discuss these issues in greater detail with the ACCC. Each of these matters has previously been raised with ARTC but ARTC has chosen not to respond to these issues. For many of these issues, Pacific National has prepared appropriate drafting for inclusion in the Undertaking.

##### **Fundamental & Service Objectives**

The Undertaking is silent on ARTC's purpose in providing the network. It is Pacific National's contention that the purpose of ARTC is to provide the network for the benefit of access seekers, providing an essential service and economic enabler in the same way that the providers of Australia's road networks are the providers of an essential service. It is appropriate that the Undertaking recognise this and set out appropriate objectives. The existing "Undertaking objectives" do not address this area as they are directed towards the purpose of the Undertaking itself.

See Appendix E for a suggested set of objectives.

##### **Occupational Health & Safety**

The Undertaking and the IAA are silent on ARTC's obligations with respect to occupational health and safety matters for train operator employees. Train operators necessarily need to use the ARTC physical corridor and infrastructure in order to perform their duties (eg walking beside the train to perform safeworking functions). A substantial proportion of injuries to Pacific National's staff occur on the ARTC network. As the current contractual and regulatory documents are silent on this matter, this is a matter of some contention between the parties. The IAA to the Undertaking should specifically address this issue in a responsible and balanced manner.

##### **Assistance To Operators To Make Above Rail Investments**

There is a significant gap in the current arrangements whereby above rail investments can be frustrated through lack of action or cooperation by the track owner, or otherwise by refusal to give access to the corridor. The Undertaking places obligations on the access seeker in some instances (eg in Undertaking clause 6.1 relating to network connections), but none on ARTC to assist the access seeker. Appendix F provides a process for ARTC to commit to assisting access seekers in making such investments with appropriate safeguards to protect ARTC's interests.

##### **Arrangements For Recovery From Network Incidents.**

The Undertaking and IAA are silent on the arrangements that should apply when the network is disrupted by an incident. Matters such as the rearranging of train operations and the provision of assistance by one train operator to another (or other trains owned by the same operator) are left at large, as are issues such as liability and payment for providing assistance. At present such matters are left to custom and practice. From the ARTC perspective, IAA clause 8.1 allows for the issue of instructions to train operators (though it is not absolutely clear that such instructions would always be valid) and by virtue of IAA clause 8.2, the operator receiving the

instruction is required to comply. It is appropriate for the Undertaking/IAA to cover such matters in more detail and also include matters relating to the train operators.

To give effect this, Schedule C to the Undertaking should include a requirement to incorporate arrangements associated with recovery from in-service failures and incidents. Drafting for consequential amendments to clause 8 of the IAA and a new Schedule to the IAA is suggested at Appendix H.

### Storage Of Rollingstock

The Undertaking is silent on the storage of rollingstock on the network and any associated charges. This has been a vexed issue between operators and ARTC and is even more pertinent now that ARTC controls the NSW leased network where storage on the network, free of charge, has been the normal practice in certain situations. ARTC has expressed a position on this; it is of the view that this is not a matter for coverage under the Undertaking.

Pacific National is of the view that this is a matter that is necessary and incidental to the operation of a railway and therefore should properly be addressed in an access undertaking. This is a matter that has had some airing between the parties but there has never been any clear articulation by ARTC how it intends to manage complex issues that arise.

Pacific National believes that this issue ought to be addressed in the Undertaking and suggested drafting is provided at Appendix K.

In a related issue, it is Pacific National's interpretation of the NSWRAU that it covers all railway infrastructure, including sidings owned by ARTC. This view is formed from the following definitions:

From Schedule 7 of the NSWRAU:

**"NSW Rail Network** has the same meaning as "NSW rail network" in the Transport Administration Act."

The definition in the Transport Administration Act is:

**"NSW rail network** means the railway lines vested in or owned by or managed or controlled by a rail infrastructure owner (including passing loops and turnouts from those lines and loops and associated rail infrastructure facilities that are so vested or owned or managed or controlled)."<sup>55</sup>

If this is the case, the exclusion by ARTC of sidings from the Undertaking would lead to the situation that access seekers would have the right to seek access to this infrastructure under the NSWRAU. Instead of "more holistic management of [the] network"<sup>56</sup> ARTC appears to be breaking the network into a myriad of pieces and jurisdictions. It would be preferable to have these sidings included in the Undertaking and dealt with as part of the network.

<sup>55</sup> It will be seen that the definition of "rail infrastructure facilities" below (also from the Transport Administration Act) refers in (b) to track not vested in the rail infrastructure owner and therefore does not remove sidings from the operation of the NSWRAU.

"rail infrastructure facilities:

- (a) includes railway track, associated track structures, over track structures, cuttings, drainage works, track support earthworks and fences, tunnels, bridges, level crossings, service roads, signalling systems, train control systems, communication systems, overhead power supply systems, power and communication cables, and associated works, buildings, plant, machinery and equipment, but
- (b) does not include any stations, platforms, rolling stock, rolling stock maintenance facilities, office buildings or housing, freight centres or depots, private sidings or spur lines connected to premises not vested in or owned by or managed or controlled by a rail infrastructure owner." (emphasis added)

<sup>56</sup> ARTC 2007 Interstate Access Undertaking Explanatory Guide p 4

#### 4.7 OTHER ISSUES RELATING TO THE IAA

Drafting issues with regard to the IAA are presented in Appendix A. The following issues other than drafting are noted with regard to the IAA:

Clause	Issue
2.8	Light engines – the proposed requirement ignores current practice with regard to traffics that are charged on an 'output' basis such as coal (charged as a rate per tonne). These charges are intended to be inclusive of ancillary movements such as light engines and repositioning movements and need to be accounted for in the agreement. Obviously ARTC would not see this as an issue given its proposed pricing structure, however, if that pricing structure is not approved, this would need to be addressed.
2.9	See response to Question 25 in Section 3.3.4 with regard long-term pathing. As this provision now stands it might as well be removed as it is useless in securing any certainty of long-term availability of train paths to a party contracting for access with ARTC.
4.1	This is inconsistent with current cancellation arrangements under the NSW arrangements. ARTC seems to have ignored any benefit that previously accrued to operators under the current ARTC NSW contract terms and conditions.
5.5(j)	With regard to communications equipment changes, ARTC ought to reimburse the operator the net cost to the operator of replacing or upgrading the communications equipment, taking into account any reductions in charges or other benefits that will tangibly accrue to the operator as a result of the system change. Without this, ARTC is able to effect reductions in its costs at the expense of train operators by unilateral imposition of a change in communications systems.
8	The operator should not be liable for damage caused as a result of compliance with an Instruction and should be indemnified by ARTC for any claims. A liability carve out is needed in clause 8.2(e).  Clause 8.2(f) does not cover the risk of claims by third parties and should include an indemnity for this.
8.1(e)	The ARTC Instruction should be made available to the Operator in writing if also requested by the Operator.
New 8.1(f)	In line with the need to cover network disruption, the following is suggested for inclusion:  "Where there is a disruption to the network a modification to the Daily Train Plan (other than the mere early or late running of Trains), Schedule [X] will apply."
8.2(c)	The obligation of the train operator to comply with an Instruction needs to be qualified in addition to the qualification in paragraph (c). The operator should only be required to comply with an Instruction where the instruction is one that: <ul style="list-style-type: none"> <li>a) the Operator is qualified to perform;</li> <li>b) is within the terms of the Operator's safety accreditation; and</li> <li>c) can be safely performed.</li> </ul>
9.9	Schedule 2 is blank and therefore it is assumed that no standard approach to allowances for cancellations is contemplated. Both the current NSW and non NSW agreements give an allowance for cancellations and PN would be looking for ARTC to continue this. (See also discussion in Question 29, Section 3.4.1.)

## APPENDIX A DRAFTING ISSUES

This appendix contains three tables dealing with drafting:

Table A1 Drafting issues with the Undertaking main body

Table A2 Drafting issues with Schedule D, the Indicative Access Agreement

Table A3 Typographical errors

**TABLE A1: ARTC DRAFT ACCESS UNDERTAKING DRAFTING COMMENTS**

Clause No.	Comment
1.1(c)	The first sentence of this clause is an expression of ARTC's view only and should be expressed to be as such.
1.2	The objectives clause does not actually list as an objective the provision of access to the network. Rather, paragraph (a) simply refers to establishing an effective "process for lodging and processing Access Applications". See also Appendix E to this submission.
2.1(b)	As noted in the substantive submission, it is not clear why the undertaking should carve out any extension to the Network. To do so, gives rise to costs and inefficiencies with no real benefit.
2.2(b)	Should note that withdrawal of the undertaking requires ACCC consent (s. 44ZZA(7), TPA) as per clause 2.4(b).
2.5(a)	The clause may mean that an operator is subject to different access agreements for access rights to the network as a different access agreement may apply to additional or new access rights, to those applicable to current access rights. This would be administratively difficult and costly with little benefit.
2.5(b)	This clause has not been imported into the draft IAA and should be as there is benefit in having the arrangements continue post termination.
3.3(a)(x)	The Applicant should only be required to pay the costs of provision of this "other information" where the information is not ordinarily and freely available as provided for in clause 3.3(b)(ii). As such, the words in paragraph (x) "and the Applicant agrees to pay such costs" should be qualified with "where such information is not ordinarily and freely available to ARTC".
3.4(d)(ii)	There is a circularity to this clause as it refers to a "Material Default" which is defined by reference to the matters in this clause. In addition, the clause should be limited to material default under ARTC contracts and not extended to other third party rail access agreements. The inclusion of third party contracts is broad and may pick up a range of rail infrastructure including assets, and is from a practical perspective, difficult to administer.
3.8(a)	ARTC should be required to use its "best endeavours" rather than "reasonable efforts".
3.8(b)	A requirement of "acting reasonably" should be imposed on ARTC in considering whether to extend time. Pacific National's reading of the advice regarding the need for an extended time is that this occurs within 5 Business Days after the acknowledgement of the application. However the clause is very unclear and should be redrafted to aid clarity.
3.8(c)(iv)	The ARTC standard terms and conditions can only be revised from time to time if in accordance with the approved undertaking and agreement, or with the consent of the Commission.
3.8(d)	<p>This clause seems to undermine the point of having an indicative access proposal. ARTC to advise its intent in providing the proposal if there is no obligation on ARTC to provide access in accordance with those specific terms and conditions?</p> <p>The relationship of this clause and the obligation in clause 3.11(b) is also unclear - does ARTC intend that the proposal might contain terms that are consistent with the IAA? If so, presumably this would have only arisen through the request of the applicant and therefore the proposal must reflect something that ARTC is willing to offer (otherwise why offer something ARTC was not willing to provide)?</p>

Clause No.	Comment
3.8(e)	<p>How will the Applicant know whether ARTC is not making reasonable progress in the preparation of the proposal?</p> <p>Clause 3.12.1(a) provides that disputes are to be resolved in accordance with the dispute resolution mechanism set out in clause 3.12.1(a). A “Dispute” is defined as that arising under the undertaking or in relation to the negotiation of access between an Applicant and ARTC. Given this “cover all” application of the dispute resolution mechanism, why is it necessary to have specific clauses such as clause 3.8(e) expressly provide for dispute resolution?</p> <p>The clause reference here is to clause 3.12 whereas it should be clause 3.12.4 which is the clause dealing with arbitration if that is the real intention.</p>
3.8(g)	<p>See comment in relation to clause 3.8(e). The dispute resolution clause in 3.12.1(a) should cover the field for all disputes including that referred to in clause 3.8(e).</p>
3.10(b)(iii)	<p>The 3 month time period is likely to be too short and it is unclear what benefit accrues to either party through having a strict deadline. A cessation of negotiations by the applicant can occur at any time so having a strict deadline is only ever going to be of assistance to ARTC, but ARTC does not require such protection. Pacific National would prefer that no specific end time be stated and if either party believes the negotiations are not proceeding satisfactorily the party can seek dispute resolution under the general provision clause 3.12.4.</p>
3.10(b)(iv)	<p>This amounts to a unilateral termination of negotiations by ARTC. The applicant should have a right to have the matter dealt with under the dispute resolution mechanism. ARTC should advise if it has a different view.</p>
3.10(b)(v)	<p>Pacific National would expect this to be covered by the general provision for raising disputes. If this clause is to be retained either party should be able to refer the matter to the arbitrator if it considers the other party has not been negotiating in good faith within a reasonable time period, and not just ARTC.</p>
3.10(b)(vi)	<p>The ARTC evidence that the applicant no longer satisfies the prudential requirements should be made available to the Applicant, and the Applicant should be given a right to respond and rectify the position if the case of non-compliance is made out.</p>
3.10(e)	<p>This clause is not required as clause 3.12.1(a) is inclusive and applies to all disputes under the IAA unless otherwise specified.</p>
3.11(a)(ii)	<p>Access agreements should only be between the Applicant and ARTC. This clause provides that there may be a tripartite agreement such that both the Applicant and an accredited operator are both a party to an agreement with ARTC. This has the potential to confuse the responsibilities of the various parties and is unnecessary.</p>
3.11(b)	<p>The Access Agreement should be consistent with the terms outlined in the indicative access agreement rather than the “principles”. Note also discussion in response to Question 89 (Section 3.9 of this submission) regarding the qualified application of the IAA.</p>
3.12.4(b)(iii)	<p>The carve out to TPA Part IIIA Division 3, Subdivision D is confusing. In particular:</p> <p style="padding-left: 40px;">it suggests that the rules of natural justice do not otherwise apply. This is unlikely to be the case.</p> <p style="padding-left: 40px;">there is a doubling up of matters already covered by the Subdivision. For example, TPA s 44ZF(1)(a) provides that the Commission is not bound by the rules of evidence. Similarly, TPA s 44ZE already provides that a party may appear in person or be represented by someone else. The restatement of these matters, expressed in slightly different language, in the access undertaking given that the TPA provisions have been imported, creates confusion.</p>
3.12.4(b)(iv), (v), (vi)	<p>All of these clauses pick up matters already provided for in Division 3 of the TPA although they use slightly different wording which may create confusion.</p>
3.12.4(b)(vii)	<p>Paragraph (A) says that the ACCC “may” deal with the matters set out in s 44V, TPA. This includes not having to give a written decision and appears inconsistent with the obligation under paragraph (b)(iii)(C).</p>
3.12.4(b)(xv), (xvi)	<p>The language referring to “appeal rights” should be changed to “appeal, review or challenge” as the nature of any rights to challenge the ACCC’s decision as arbitrator is not clear. It may or may not be in the nature of judicial review which in any case, gives only a right of review rather than an appeal of the decision.</p>
4.5(b)	<p>The term “vests in” is not appropriate. Rather the reference should be to the granting of access to the Train Path.</p>
5.2(a)(ii)	<p>This introduces the concept of an “Access Seeker” although this term is not defined. Should the clause refer to a “Customer” or “Applicant”?</p>

Clause No.	Comment
5.3(a)	There is an inconsistency in this clause as it requires that access rights will be allocated to the first Customer but then applies a decision criterion that they be allocated to the Customer with the access agreement that in the opinion of ARTC is most favourable to it. Thus the circumstance might arise that mean that someone other than the first customer may be allocated capacity, which would seem to contradict the first part of the clause.
5.4(a)	The criterion for under utilisation is provided in Schedule D at clause 9.5(a) in the IAA. It is noted that this is included in Schedule C, but Pacific National believes that this ought to be specified in the body of the Undertaking. Note that in either case the clause needs to be modified to take into account the different traffics that will operate under the Undertaking.
Definition of "Capital Expenditure"	This is an operative clause and should be contained in the body of the Undertaking and not in the definitions section.
Definition of "Solvent"	This should be limited to events that have occurred in the last 3 years. Query also the tense used in this definition as it refers to events that have happened but, for example, paragraph (b) refers to a meeting that has been convened referring to a future event.
Definition of "Prudent"	The phrase "having regard to the meaning of Capital Expenditure" should be replaced with "in accordance with paragraphs (a) to (e) in the definition of "Capital Expenditure".
Schedule B (3)	What does a "vehicle" refer to that is not already covered by the definition of rollingstock?

**TABLE A2: ARTC DRAFT ACCESS AGREEMENT DRAFTING COMMENTS**

Clause No.	Comment
Definition of "Access Undertaking"	Need to insert the words "and accepted and improved by" after the words "given or submitted by ARTC to".
Definition of "Network"	The definition of the network in Schedule 1 is inconsistent with the definition in the DDAU Schedule E
Definition of "Third Party Works"	This definition needs to make clear and for the avoidance of doubt that the work does not include work done by ARTC contractors or third parties doing work for or on behalf of ARTC.
2.2	A train path is ultimately defined as having a particular departure and arrival time and location. Accordingly, once that path is allocated, exclusivity to that path is given to that operator. The first sentence of this clause should refer to there being no grant of exclusivity to the Network rather than to a specific Train Path.
2.5(a)	The word " <i>Despite</i> " is unclear and we would recommend changing it to " <i>Notwithstanding</i> ".
2.9(b)	Why has the notice period been increased from the current 60 days to 120 days? Query whether this clause is required at all unless the long-term path rights are retained. (See discussion in response to Question 24 in Section 3.3.4 of this submission).
2.10(a)	Words appear to be missing from this clause.
3	The Undertaking (clause 2.5(b)) provides for a carry over of the terms and conditions of the agreement following expiry of the access agreement with the consent of the parties. This provision is absent from the access agreement and should be inserted.
4.1	The operator should not be required to pay a flagfall charge if the operator was not able to use the train path due to ARTC's inability to provide the path whether through breach of the agreement or any other circumstance.
4.3	The term " <i>excess network occupancy Charges</i> " is not defined and needs to be specified in Schedule 3 if not otherwise defined.

4.4(a)	<p>There is no obligation on ARTC to provide accurate invoices. If the obligation in (b) is to apply then ARTC should have such an obligation.</p> <p>The timing for payment is inconsistent with obligations in the current Indicative Access Agreement and ARTC to justify the shortening of this period.</p>
4.4(b)	<p>There should be no obligation to pay outstanding amounts if they are the subject of a genuine dispute between the parties.</p>
4.5(a), (b), (c)	<p>There is no limitation in the clause as to the number and period of “<i>Review Dates</i>”. The clause provides that ARTC may at any time after the Commencement Date vary the indicative charges. Paragraph (b) also states that ARTC may vary the charges more than once in between determination dates during the term. Paragraph (c) also states that ARTC may at any time give a notice to increase charges. This could expose operators to continual review of charges.</p> <p>The agreement needs to include actual prices and charges and not just indicative prices and charges. See also discussion in Section 3.4.8 of this submission.</p>
4.7(a)	<p>There is a lack of clarity in paragraph (a). Does this clause contemplate a variation to the definition of the Network for the purposes of the Access Agreement?</p> <p>Disputes as to track extensions should be covered by the clause 17 dispute resolution mechanism.</p> <p>This provision seems to be inconsistent with clause 2.1(b) of the Undertaking which excludes extensions to the network.</p>
4.9(b)	<p>This clause should carve out monies the subject of a genuine dispute between the parties.</p>
4.9(c)	<p>There is no reason to have a carve out from the clause 17 dispute resolution mechanism here.</p>
4.9(e)	<p>This clause effectively entitles ARTC to determine a new amount of the Security every 12 months with no recourse to the clause 17 dispute resolution mechanism. ARTC should explain the need for this.</p>
4.9(f)	<p>This obligation should be made subject to paragraph (d) in which the Security can be withdrawn following a period of compliance.</p>
4.9(g)	<p>ARTC should be required to release the Security on expiry of the Agreement less any amount outstanding or payable under the Agreement. Accordingly, words to the following effect should be added to the end of the clause: “<i>in which case, the Security must be returned to the Operator less any undisputed Charges owing by the Operator to ARTC pursuant to this Agreement</i>”.</p>
4.10(a)	<p>This should be limited to any charges that are owed rather than any “<i>loss</i>” suffered by ARTC.</p>
4.11(a), (b)	<p>The definition of “<i>Input Tax Credit</i>” should be amended by deleting “<i>Section 9-5 of</i>”. Replace the heading in clause 4.12(b) with the words “<i>GST payable</i>”.</p>
4.12	<p>This clause needs to make it clear that ARTC’s legal costs are not included such that the Operator is not liable to pay such costs.</p>
5.5(h)	<p>The words “<i>wilfully or negligently</i>” should be inserted before the word “<i>materially</i>”.</p>
5.7(c)	<p>It is unreasonable to expect that the Operator will indemnify ARTC for any injury and loss or damage arising from the removal of the train pursuant to the clause “<i>including without limitation ... where such injury, loss and damage is caused by the negligence of ARTC ...</i>”. ARTC should be expected to act in a manner that is not negligent or intentionally damaging and there needs to be such a carve out from this indemnity.</p>
6.1	<p>The standard service requirement of “<i>fit for use</i>” is an undefined term. This should be related back to the Operator being able to operate trains according to their specification.</p>
6.2	<p>This clause effectively allows ARTC to walk away from its standard quality obligation in clause 6.1 by issuing a notice to restrict speed and weight. Such restrictions undermine the service quality obligation in clause 6.1.</p>
8	<p>The operator should not be liable for damage caused as a result of compliance with an Instruction and should be indemnified by ARTC for any claims. A liability carve out is needed in clause 8.2(e). Clause 8.2(f) does not cover the risk of claims by third parties and should include an indemnity for this.</p>
8.1(e)	<p>The ARTC Instruction should be made available to the Operator in writing if also requested by the Operator.</p>

New 8.1 (f)	See discussion in Section 4.6 and Appendix J of this submission. In line with the need to cover network disruption, the following is suggested for inclusion: “Where there is a disruption to the network a modification to the Daily Train Plan (other than the mere early or late running of Trains), Schedule [X] will apply.”
8.2(c)	The obligation of the train operator to comply with an Instruction needs to be qualified in addition to the qualification in paragraph (c). The operator should only be required to comply with an Instruction where the instruction is one that: a) the Operator is qualified to perform; b) is within the terms of the Operator’s safety accreditation; and c) can be safely performed.
8.2(e)	What is a “ <i>proper Instruction</i> ”? This should be defined.
8.3	This clause needs to make clear that the Operator is only obliged to comply with laws and other obligations that pertain to its use of the Network as the Operator.
9.4(b)	ARTC should be responsible for ensuring that the network is fit for use and should not be relieved of this obligation in respect of third parties. Regardless of any statutory rights held by third parties to perform work on ARTC’s property, ARTC is the accredited party on whom operators rely to ensure the track is safe. See also Section 4.5 of this submission.
9.5(b)	There needs to be a carve out for acts and omissions of ARTC not otherwise caused by the operator. Wording such as the following should be inserted at the end of the clause: “ <i>where such circumstances have arisen other than due to the actions or omissions of ARTC or another track owner, path disruptions on the Network not caused or contributed to by the Operator or force majeure events as defined in clause 20.</i> ”
14.1(c)	The clause should clearly state that it is the non-defaulting party that has the right to terminate.
15.2(b)	The definition of “loss or damage” is unclear. The reference to “reasonable legal expenses on a solicitor/client basis” is unclear. Is this meant to cover costs on a full indemnity basis or party/party costs basis and how would this sit with any costs order by the court? It would be more appropriate to simply refer to legal expenses incurred in relation to any claim made by a third party and the costs of recovery of any property damaged or affected by the Incident.
15.4	The prohibition on claiming Consequential Loss only applies to restrict claims for consequential loss in respect of an Incident and not other breaches of the agreement. What is the rationale for limiting the prohibition in this way?  The last sentence appears to be incorrect. Consequential Loss generally does include liability to third parties. It is this loss that is being excluded for the purposes of claims under clause 15.4.
15.8	This clause needs to be clarified to provide that the indemnity payment by the Responsible Party to the Indemnified Party is not required to be made on demand by the Indemnified Party if the Responsible Party objects to the claim.
17.3(e)	If legal proceedings have been initiated, it is for the Court to grant an order adjourning or staying proceedings pending completion of the dispute resolution procedure. The second sentence in this clause does not add anything as the party to the dispute would in any event be entitled to apply for an adjournment. Is the intent of the clause that both parties agree that an application for a stay would be made and would not be challenged by any other party? If so, this should be specified.
19.2(c)(i)(E)	This paragraph needs to be deleted as there is no justification in requiring that the operator appoints ARTC as its attorney to enforce the Trade Agreement.
19.2(c)(i)(H)	This paragraph refers to “ <i>vetting</i> ” and “ <i>permitting</i> ” by ARTC yet the procedure set out in clause 19.2 does not require such ARTC approval.
19.2(c)(i)(I)	This discretion is too broad and should be limited at the very least to any other matter which ARTC reasonably requires.
19.2(c)(v)	This indemnity is extremely broad and is rejected. An indemnity for loss or damage arising from the Operator’s acts or omissions is appropriate and is given in clause 15.3. It may be appropriate to require the Proposed Operator to indemnify ARTC for its use. To impose an indemnity on the Operator is not appropriate.
19.2(c)(vi)	Operators should not be required to indemnify ARTC for third party claims.

**Typographical Errors**

The following typographical error has been noted in the Undertaking:

Clause	Error/Correction
Undertaking 9.1	Definition of Network requires a new paragraph (currently joined with Material Default)

## **APPENDIX B FORM OF SEPARATE UNDERTAKINGS**

---

The following is adapted from the Explanatory Document to the MUG Version 2\_02 which is available from Pacific National on request. It:

- a) discusses the reasons for having two separate undertakings for the ARTC network; and
- b) examines the ways in which this might best be achieved.

The issues discussed here are directly relevant to the ACCC's consideration of the Undertaking.

### **Why Separate Undertakings?**

It would normally be expected that ARTC would have one Undertaking to cover access to any part of its network. After all, there was one NSWRAU and one U2002 why would you need more than one?

In considering this matter, Pacific National looked at the requirements for the Undertaking. It is immediately apparent, on anything other than a cursory inspection, that there are substantially different requirements for Hunter Valley coal trains in a variety of matters, both commercial and operational, that need to be detailed in the undertaking separately from other traffics. For example, the Hunter Valley coal traffics (but not other traffics using that part of the network) are expected to cover the ceiling revenue, but nowhere else on the network is this ever likely to happen. This has implications for a number of areas in the undertaking covering the two different areas such as pricing provisions and investment. The path allocation process for Hunter Valley coal is substantially different to the allocation mechanism for other traffics (though some traffics require a process that is a hybrid of the Hunter Valley coal mechanism).

In formulating the MUG, four alternatives were considered:

- a) a single undertaking for all traffics across the whole network;
- b) region specific undertakings (one for the Hunter Valley and one for the rest of the network – this is the option chosen by ARTC for the Undertaking);
- c) traffic specific undertakings (one for coal and one for all other traffics); and
- d) a traffic specific undertaking that was also region specific (one for Hunter Valley coal and one for all other traffics across the entire network).

Each of these options is discussed in the following sections.

From these considerations it was determined that the 'least worst' solution is option (d). Thus the MUG has been designed to cover:

- a) a geographic region – covering the entire ARTC controlled network (including both owned and leased infrastructure). This is defined in MUG Schedule E; and
- b) exclusion of a specific traffic on a particular portion of the network – coal (both export and domestic) in the Hunter Valley region.

While no solution is perfect, this was seen as the solution that best achieves:

- requiring only one access arrangement for a particular train within ARTC territory,
- catering for the special requirements of the Hunter Valley coal trains,
- minimising consistency problems between the two undertakings (ie the MUG and the MUC).

### **One Undertaking For All Traffics & Regions**

A key issue that underlies the regulation of the ARTC network is that the service that is for sale in the Hunter Valley network for coal trains is of a different nature to that which is for sale on

the rest of the network (though some traffics, typically bulk traffics, do in fact exhibit a hybrid of the two service descriptions – eg grain, minerals and non Hunter Valley coal).

The most common product packaging, as exhibited by ARTC in the Undertaking, is that ARTC sells train paths to network users. These are delineated by specific entry and exit points to the network at specific times (as well as intermediate times). Once an agreement is executed, the network user has a license (effectively, though not in contract, an exclusive entitlement within certain constraints) to use that 'path'.

The system nature of the Hunter Valley coal chain requires a very different approach. To sell fixed train paths would substantially reduce the capacity available to network users because of the interaction between network users and other parts of the coal chain.<sup>57</sup> In brief, the service required for sale to Hunter Valley coal trains is that of an aggregate capacity, with actual allocation of train paths carried out daily by the centralised planning group.<sup>58 59</sup> In effect ARTC is selling (through processes described in the MUC) a right to participate in a capacity allocation process that meets the dynamic nature of the coal chain. As such this is a fundamentally different product to selling fixed train paths over an extended period.

It would be possible bundle the separate requirements for the Hunter Valley coal traffic and the rest of the network into a series of schedules to a common undertaking. However, the level of difference between the two documents to accommodate these different models is substantial and would in effect be two separate documents combined into one. Table B1 sets out the areas of major difference between the two documents.

Were these differences to be accounted for in one undertaking, the only sections that would not require significant 'bifurcation' (ie provisions that apply to one group of traffics but not the other) to account for these differences would be:

Part 1	Preamble
Part 2	Scope & Administration
Part 7	Network Transit Management (both documents, by necessity need to have complete and consistent coverage of all activity on the network where they interact).
Part 9	Definitions (although there would be a significant number of additional definitions to cater for the Hunter Valley coal arrangements).

For example, while Part 3 (dealing with the negotiating process) retains significant portions the same between the two documents (eg the dispute resolution process), the different path allocation processes requires substantial variation between them. Such differences are non-trivial and would result in a complex document. Similarly many of the schedules require substantial variation between the two documents.

For these reasons, a single document would be cumbersome at best.

The QR Access Undertaking is an example of a single document covering an entire network, dealing with a similar variety of traffics that arise on the ARTC network. It is notable that a considerable portion of that document is specifically devoted to dealing with the specific requirements of the Queensland coal traffic. In Pacific National's opinion, this is a good example of the problems that arise from attempting, with all the best intentions, to deal with very diverse matters within a single regulatory document. It will also be noted that the Standard Access Agreement that forms part of that undertaking is directed towards the

<sup>57</sup> This is discussed in more detail in MUC Explanatory Document which is available from Pacific National on request.

<sup>58</sup> This effectively describes the current path allocation arrangements under the NSWRAU. Much of this is driven by custom and practice which is facilitated by the high level nature of the NSWRAU. However, any new regulatory arrangement needs to conform with these existing processes.

<sup>59</sup> This planning group is called the Logistics Team and is discussed in detail in the MUC Explanatory Document. ARTC, PN, QR, RIC, RailCorp, PWCS and Newcastle Port Corporation are all members of the Logistics Team.

operation of cyclic export coal trains and is poorly suited to more general traffics such as intermodal operations.

**TABLE B1: DIFFERENCES BETWEEN MUG & MUC**

	Model Undertaking - General	Model Undertaking - Coal
Investment	Generally low ability of traffics to meet economic investment returns – leading to different investment drivers and government policy relationship. Higher level of integration with other network providers.	Requirements impacted by decisions of other coal chain participants. Need coordination with coal system. Investments able to be funded through access charges. More clearly 'part of the system'.
Path allocation	Generally long term specific paths allocated to a particular operator, though some bulk traffics have hybrid requirements and long term allocation is not always the solution.	Pathing allocated on a daily basis in coordination across the coal chain. Not possible to define the rights of an operator in terms of train paths as contrary to system requirements.
Pricing	Prices ideally on 'posted' basis. Suited to simple annual adjustment. Certainty of pricing over long term critical. Significant competitive alternatives constrain prices below Ceiling.	Must cater for prices at the Ceiling explicitly. Escalation of prices needs to take into account total network costs and revenues for annual adjustment. Certainty of pricing in absolute terms less critical than for Intermodal traffics provided it is reasonably predictable.
Network traffic management	Transit time is the critical key performance criteria. Arrival 'on time' at destination important (not network boundary).	Sequence of trains arriving at port is more important than 'on time' arrival. Individual transit time less important on the day. <sup>60</sup>
Maintenance practices	Horizontal interfaces between different networks are typically more important.	Critical to align maintenance with other parts of the coal chain to minimise system 'down time'.
Measurement of service quality	Suite of measures based around transit time performance and time of arrival (though the AAU focuses on the Healthy Train concept).	Usual 'on time' related measures are not relevant. Integrated nature of the coal chain makes it very difficult to assign performance measures in a contractual sense.

So having argued that there is very good reason to have separate undertakings, the sections below examine the alternatives.

**Region Specific**

A region specific undertaking would provide specific arrangements to apply in each of the two regions ie a Hunter Valley region and the rest of the ARTC network. This is the model adopted by ARTC in the Undertaking.

A region specific Undertaking that would apply to all traffics passing through that region has the problems that:

- Traffics seeking paths through multiple areas (eg interstate intermodal trains) would need to deal with an additional undertaking and hence the path allocation processes in the MUC would need to mirror those of the MUG. To cater for these through traffics, the level of conformity with the rest of the network would need to be substantial, to the point of questioning whether it would be better to have a single undertaking.

<sup>60</sup> Transit time is an important factor for the coal system at the aggregate level, but less so at the individual train level. Thus efforts to "speed up the system" may well yield benefits in terms of capacity, but these need to be matched across the entire coal chain to be effective and changing operations solely with regard to rail transit times may be insufficient (eg if the port receival capabilities are unable to match the new train arrival rates) and even counter-productive (eg if all that is achieved is a queue at the port).

- Two access agreements would be required for travel through ARTC's network. This is undesirable and results in additional costs and effort to all parties.<sup>61</sup>
- Putting aside the 'through traffic' problem, a Hunter Valley region undertaking will inevitably have to provide for a number of other traffics. It is difficult to see how this would therefore differ from a single undertaking and the problems already discussed with that approach. This problem would only be avoided if the Hunter Valley region could be so tightly defined as to exclude all other traffics. In formulating the MUG, a definition that would achieve this without also excluding at least some of the coal traffic that needs to be included was not able to be discovered. It is clear that ARTC has not been able to define such a network in the Undertaking.

The conclusion is that this solution does not appear to provide any real advantage over having a single document for the whole network.

### Traffic Specific

A coal traffic specific Undertaking offers little advantage outside the Hunter Valley network as the nature, volume and location of coal traffic in other areas is very different.<sup>62</sup> This is because the principle other coal traffic, that originating from the Blue Mountains and Southern Highlands regions of NSW uses, to a large extent, the RailCorp metropolitan network and must therefore conform to the constraints of what is essentially an urban passenger network. This factor, combined with the fact that the export terminal at Pt Kembla operates as a 'stock-pile' terminal rather than a 'turn-of-arrival' terminal means that the southern coal trains operate much more in the fashion of fixed paths like intermodal traffics.<sup>63</sup> While there is a need for close cooperation between the various parties involved in the southern coal chain, there are not the same imperatives for the centralised planning of activities as in the Hunter Valley nor is there the same level of variation in train pathing.

In addition, these coal traffics are of far lower volume and not able to sustain pricing at the ceiling. It is therefore not necessary to incorporate the specific mechanisms for dealing with the ceiling that apply to the Hunter Valley coal traffic. Indeed the requirements to deal with the non Hunter Valley coal conform much more closely with those of the other non-coal bulk traffics.

Thus the conclusion is drawn that separating undertakings on the basis of traffic description alone is not universally necessary.

### Region & Traffic Specific

The remaining option to consider is that of separating the Undertakings by traffic **and** region.

This does yield the benefits of dealing separately with the substantial differences exhibited by the Hunter Valley coal traffic. However, it introduces a unique feature to the regulation of infrastructure in that two regulatory instruments would apply, in part, to the same physical network. In order to accommodate this, care needs to be taken to ensure consistency between

<sup>61</sup> This is the current situation for PN. PN has always assumed that this arrangement is a transitional one and that the intention is to have a single ARTC agreement for trains traversing ARTC's network. It will remain the case that many PN trains will traverse ARTC, RIC and RailCorp territories just in NSW and will require a separate access agreement with each. This seems unavoidable under current ownership arrangements and it is clear the original vision of ARTC providing a "one stop shop" for access to the interstate network will never eventuate with substantial structural change within the Australian rail industry.

<sup>62</sup> Over the life of the MUG, coal traffic on the ARTC network outside of the Hunter Valley is unlikely to increase dramatically given the known coal deposits and planned new mines within the next 10 years with the exception that will arise if ARTC acquires additional parts of the RIC network to cater for Gunnedah Basin coal.

<sup>63</sup> While these trains run to fixed paths, the operation requires a greater degree of flexibility than is required for intermodal traffic and this is provided by allocating additional paths than would be needed for a strictly fixed path operation. Under the current access agreement these are termed flexible paths and are really a hybrid between the allocation of fixed paths and the capacity allocation in the Hunter Valley. These, in practice, provide the basis for what Pacific National terms "traffic specific capacity". There are similar requirements for grain and minerals trains.

the two documents; they need to cater for those areas of interface that inevitably arise. These are principally in the areas of:

- Path allocation
- 'Live run' traffic management on the network
- Allocation of costs (and consequently, though peripherally, pricing) – noting that this is an issue for the other options except a single undertaking covering all traffics across the whole network.
- Resolving any unforeseen conflict between the two undertakings.

Appendix C provides discussion of the legal position with regard to having two undertakings covering different services provided by the same physical infrastructure.

As in all the other separation options, this results in a requirement for separate access agreements, in this case for Hunter Valley coal trains and all other trains. This presents a less objectionable outcome for the following reasons:

- The complexity involved in dealing with the Hunter Valley coal traffic in the same document as all other traffic is removed – there is a substantial degree of separation of the coal arrangements in the current ARTC NSW contract (prior to separation this was the RIC contract).
- Hunter Valley coal trains are typically managed separately from other trains and this option covers the entire journey for the train (for those operating wholly within the ARTC network) so dealing with them under a separate access contract presents little administrative burden (compared to dealing with different access agreements for the one train).<sup>64</sup>

The MUC has been crafted to resolve the potential for conflicting path allocation outcomes with the MUG. Note that this is dealt with in practice through effective separation of the coal and non-coal traffics and so does not present a practical problem, the problem is one of reflecting good practice in the regulatory and commercial documentation – a problem that appears to be less administratively difficult to manage compared to the alternatives.

The other issues can similarly be managed, for example the MUC and MUG both provide for ARTC to identify Hunter Valley regional costs associated with the coal traffic and a mechanism for the allocation of non-specific costs to avoid unnecessary biasing due to the large traffic volumes in that region.<sup>65</sup> Resolution of unforeseen inconsistency can be dealt with through the simple mechanism of both documents identifying one of them as taking precedence where such a situation arises – though, in the formulation of the MUG and the MUC, no issues have been identified as likely to arise apart from those that are already provided for. Both the MUC and the MUG recognise the MUC as taking precedence in the case of an inconsistent outcome on the basis that the 'special' should take precedence over the 'general' in such a situation.

The conclusion is that a region and traffic specific separation provides the best alternative. The MUG and MUC have been fashioned accordingly.

---

<sup>64</sup> Note, however, that some Hunter Valley coal trains traverse the RIC or RailCorp networks during part of their journey and by necessity will be covered by different contractual arrangements. This is unavoidable while control of the rail network is fractured.

<sup>65</sup> For example, the Hunter Valley generates a substantial proportion of the total GTKm on the ARTC network over a very small portion of the infrastructure. Allocating non-specific costs that do not have a mass  $\times$  distance causal factor on the basis of GTKm (as is the method used in the U2002 and proposed in the Undertaking) is likely to lead to an excessive burden being placed on the Hunter Valley.

**APPENDIX C      LEGAL ADVICE REGARDING MORE THAN ONE UNDERTAKING  
APPLYING TO THE SAME INFRASTRUCTURE**

---

## APPENDIX D DIFFERENT INFORMATION UNDER NSWRAU & THE UNDERTAKING

The NSWRAU contains in Schedule 5 a list of information that the network owner is required to provide to access seekers on request. In Table D1, this is compared to the information required to be made available under the Undertaking.

**TABLE D1**

Issue	NSWRAU (From Schedule 5 unless otherwise indicated)	ARTC Undertaking
Network details	<ul style="list-style-type: none"> <li>▪ Diagrammatic map of the network, showing track configuration</li> <li>▪ Diagrammatic map showing Sector codes, as used for asset management and costing purposes</li> <li>▪ Route kilometres and track kilometres by Sector</li> <li>▪ Curve and gradient diagrams, and ruling grades by Sector</li> <li>▪ Line class and track design characteristics, by Sector</li> <li>▪ Indicative sectional running times for various types of standard train</li> <li>▪ Indicative maximum trailing tonnages for locomotives of various characteristics, by Sector</li> <li>▪ Maximum axle loads and speed restrictions, by Sector</li> <li>▪ Indicative maximum train lengths, by Sector</li> <li>▪ Transit space standards (defining dimensional requirements for rollingstock)</li> </ul>	<ul style="list-style-type: none"> <li>▪ A map containing a geographical description of the network <sup>#1</sup></li> <li>▪ A narrative description of the network <sup>#1</sup></li> <li>▪ Route standards by corridor <sup>#1</sup> (note these contain many, but not necessarily all of the specific details enumerated separately under the NSWRAU)</li> <li>▪ Axle load limitations <sup>#2</sup></li> <li>▪ Maximum allowable speeds <sup>#2</sup></li> <li>▪ Infrastructure characteristics <sup>#2</sup></li> <li>▪ Applicable safeworking requirements <sup>#2</sup></li> <li>▪ Indicative section running times for indicative services by corridor <sup>#1</sup></li> <li>▪ Segment run times <sup>#2</sup></li> </ul>
Capacity Information	<p>System Usage - Gross tonnes per annum by Sector, aggregated into the following tonnage bands; Gross tonnes per annum:</p> <ul style="list-style-type: none"> <li>▪ 0 - 200,000</li> <li>▪ 200,001 - 500,000</li> <li>▪ 500,001 - 1 million</li> <li>▪ 1 - 2.5 million</li> <li>▪ 2.5 - 5 million</li> <li>▪ 5 - 7.5 million</li> <li>▪ 7.5 - 10 million</li> <li>▪ 10 - 15 million</li> <li>▪ 15 - 20 million,</li> <li>▪ thereafter in increments of 10 million gross tonnes</li> </ul> <p>Unutilised capacity - Indicative figures for the number of unutilised train paths for representative trains of various configurations and characteristics as follows:</p> <ul style="list-style-type: none"> <li>▪ by sector;</li> <li>▪ by time period; and</li> <li>▪ by day of week.</li> </ul> <p>That part of the master timetable (excluding rail operator identity) that is directly relevant to the access seeker</p>	<p>A graphical representation of committed Capacity on the network (excluding track possessions for network maintenance) <sup>#1</sup> Available capacity <sup>#2</sup> Path length availability <sup>#2</sup></p>

Issue	NSWRAU (From Schedule 5 unless otherwise indicated)	ARTC Undertaking
Capital related information	<ul style="list-style-type: none"> <li>▪ Asset values by asset class, allocated by sector.</li> <li>▪ Treatment of depreciation</li> <li>▪ Committed capital works and capital investment</li> <li>▪ Cost of debt</li> <li>▪ Capital structure</li> </ul>	<ul style="list-style-type: none"> <li>▪ DORC values in relation to the Segment to which Access is being sought <sup>#2</sup></li> </ul>
Revenue limits & prices	<ul style="list-style-type: none"> <li>▪ Attributed costs by Sector (ie ceiling)</li> <li>▪ Indicative variable cost rates by region (ie the floor)</li> </ul>	<ul style="list-style-type: none"> <li>▪ Incremental cost and the economic cost for the segment to which access is being sought (ie floor and ceiling)<sup>#2</sup></li> <li>▪ Indicative access charges for indicative services <sup>#1</sup></li> <li>▪ Prices for which access has been granted together with general description of the services to which such prices relate <sup>#1</sup></li> </ul>
Recurrent cost information	<p>Recurrent costs disaggregated into:</p> <ul style="list-style-type: none"> <li>▪ Infrastructure maintenance, further disaggregated into:                             <ul style="list-style-type: none"> <li>○ Routine maintenance</li> <li>○ Major Periodic Maintenance</li> </ul> </li> <li>▪ Network control costs</li> <li>▪ Terminal management costs</li> <li>▪ Depreciation, where applicable</li> <li>▪ Technical services costs</li> <li>▪ Interest</li> <li>▪ Overhead costs, further disaggregated into:                             <ul style="list-style-type: none"> <li>○ Corporate overheads</li> <li>○ Marketing overheads</li> <li>○ Asset management overheads</li> <li>○ Train operations and network control overheads</li> </ul> </li> <li>▪ Cost attribution methodology used to allocate costs to sectors</li> <li>▪</li> </ul>	<p>Recurrent costs in the form of unit rates <sup>#3</sup></p> <ul style="list-style-type: none"> <li>▪ Total annual expenditure associated with outsourced infrastructure maintenance and associated ARTC maintenance contract management function.</li> <li>▪ Total annual expenditure associated with ARTC train control and transit management function.</li> <li>▪ Total annual expenditure associated with 2 above, and ARTC operations planning and management function.</li> </ul>
Contractual terms and conditions	<p>The Rail Infrastructure Owner's standard access agreement                      The Rail Infrastructure Owner's credit policy, when available                      Arbitration Information                      A copy of any determinations published by the arbitrator in relation to this access undertaking.</p>	<p>the Indicative Access Agreement <sup>#1</sup>                      the Network Management Principles <sup>#1</sup> (note these are contained within the Undertaking and IAA)                      the Performance Indicators <sup>#1</sup></p>
Other information	<p>Operational and other information.                      An Access Seeker may request the track owner to provide further information directly relating to the Access Seeker's request for specific train path(s), such further request may not be unreasonably refused. (NSWRAU paragraph 8.8)                      The track owner may require the payment of a reasonable fee for copying the Information Package (NSWRAU paragraph 8.6)</p>	<p>Any other information relating to capacity or train operations reasonably required by the applicant in relation to the access application, provided ARTC is given an opportunity to provide to the applicant an estimate of the reasonable cost of preparing such other information, and the applicant agrees to pay such costs <sup>#2</sup>                      A copy of ARTC's annual report <sup>#1</sup></p>

#1 From Undertaking clause 2.7(b)

#2 From Undertaking clause 3.3(a)

#3 From Undertaking clause Schedule G

## APPENDIX E OBJECTIVES

---

Below are set out suggested fundamental and service objectives for the Undertaking. These are in addition to the objectives already contained in the Undertaking.

### Fundamental Objectives

ARTC's purpose for being in business is to:

- (a) Manage the parts of the Australian interstate rail network that it controls on behalf and in the interests of the Australian public;
- (b) Develop the rail network that it controls to meet future rail transport needs, and
- (c) Provide access to that network to any party seeking to use that network.

### Service Objectives

In seeking to fulfil its fundamental objectives, ARTC will structure its activities with aim of achieving the following service objectives:

- (a) provide sufficient Capacity<sup>66</sup> in the Network, with Train Paths of a sufficient quality, to meet demand from Access Seekers;
- (b) enter into commercial arrangements with Access Seekers that provide sufficient certainty to encourage the parties to invest in the provision of rail capacity to meet the demands of end markets;
- (c) plan the availability of Train Paths on a cooperative basis with Customers in accordance with agreed processes, with the objective of maximising Train Path availability consistent with the requirements for network maintenance;
- (d) manage any ARTC Terminal to facilitate the achievement of planned Train movements;
- (e) maintain the Network to a standard such that:
  - (i) Trains are able to achieve target transit times; and
  - (ii) the quality of the track meets Customer needs as identified from time to time;
- (f) adopt standards, rules and procedures consistent with the requirements of;
  - (i) safety;
  - (ii) efficiency;
  - (iii) maximising system capacity;
- (g) work closely with other infrastructure access providers to the Interstate Rail Network to ensure that, to the extent reasonably practicable:
  - (i) standards, rules and procedures are consistent between infrastructure access providers;

---

<sup>66</sup> Capitalised terms in this list of objectives are defined terms in the document "Model Undertaking – General" prepared by Pacific National, a copy of which can be made available on request. For the purpose of this submission it is sufficient for these terms to retain their normal meaning.

- (ii) Train Paths are made available seamlessly to the extent possible given the commercial relationships between the other infrastructure access providers and users of the Interstate Rail Network; and
- (iii) where investment or changes to systems and/or procedures are required to provide Capacity that impact more than one infrastructure access provider, these are managed to ensure that the planned increase in Capacity or change to systems and/or procedures is achieved.

## **Investment Processes**

### **1 Additional Capacity and Network Investment**

- (a) ARTC will manage investments of its own initiative, any requests by Access Seekers for Additional Capacity and any request from a Customer for investment in the Network in accordance with this clause 1.
- (b) The Network Investment Plan will describe all planned investments showing the location, schedule, estimated cost and the train operating and maintenance benefits of all Network investments planned for the immediately following financial year plus as much detail as can reasonably be provided for investments in the remaining years of the plan.
- (c) ARTC will consult in good faith with Access Seekers regarding the Network Investment Plan in each year, prior to its publication. ARTC is not bound by any results of such consultation, but will give reasonable consideration to the expressed preferences of Access Seekers in formulating the Network Investment Plan.
- (d) On or before 1 March of each year, ARTC will publish a Network Investment Plan for the next five (5) financial years.
- (e) ARTC will evaluate investment proposals using the criteria in Schedule [x].
- (f) An Access Seeker may request ARTC to make an investment in the Network. ARTC will conduct an evaluation in accordance with the investment evaluation criteria in Schedule [x]. In the event that ARTC declines to make the investment ARTC will publish its evaluation of the investment showing the reasons for declining to make the investment.
- (g) Where ARTC has evaluated an investment proposal requested by an Access Seeker and the proposed investment meets the criteria in Schedule [x] except for the financial criteria, then ARTC will undertake the investment where;
  - (i) it is able to negotiate a sufficient financial contribution by the requesting party to enable the investment to meet the financial criteria,
  - (ii) ARTC obtains grant funding in order to carry out the investment,
  - (iii) a combination of paragraphs (i) and (ii) above, or
  - (iv) it is otherwise satisfied that the investment should proceed despite failing to meet the financial criteria.
- (h) Nothing in this Undertaking prevents ARTC investing in the Network at its own discretion and cost provided the investment meets, as a minimum, criteria 3.1, 3.5 and 3.6 of Schedule [x].
- (i) Any Disputes arising in relation to this clause [x].1 will be dealt with in accordance with clause 3.12 of the Undertaking. [Note – not required if the dispute resolution process is generally inclusive.]

## 2 Access Seeker Related Investments

### Clause 2

This clause is designed to cover the situation where an Access Seeker needs to make an investment that requires some form of assistance from ARTC. The types of investments and forms of assistance cover a broad range from inputs into safety approvals through to physical location of assets. Examples:

The installation of a monitoring device for use by the Access Seeker that was required to be affixed to ARTC's infrastructure.

An Access Seeker requires ARTC to provide input into an environmental impact assessment to achieve regulatory approval regarding an above rail investment.

The intent is that ARTC will provide such assistance as is necessary to accommodate or facilitate the investment. Where ARTC incurs costs to do so, it is entitled to recover these and liability issues are covered off.

- (a) From time to time, an Access Seeker may require assistance, accommodation or facilitation by ARTC in order to make an investment associated with the running of Trains.
- (b) Where ARTC receives a request from an Access Seeker to facilitate an investment of the type in clause 2(a), ARTC will provide the appropriate assistance, accommodation or facilitation provided that:
  - (i) the resulting asset;
    - (A) does not compromise the safe and reliable operation of the Network;
    - (B) does not compromise ARTC's rail safety accreditation;
    - (C) meets any relevant ARTC engineering and operational standards; and
    - (D) does not interfere with ARTC's assets in a manner unacceptable to ARTC, acting reasonably.
  - (ii) ARTC is not required to engage disproportionate resources, time or expenditure;
  - (iii) the requesting party agrees to pay ARTC's reasonable costs associated with providing the assistance, accommodation or facilitation;
  - (iv) the requesting party agrees to indemnify ARTC against all liability with respect to any assistance, accommodation or facilitation provided for the purposes of Access Seeker's investment except to the extent that ARTC is negligent or engages in wilful misconduct, and
  - (v) where relevant, the requesting party agrees to pay ARTC's reasonable on-going costs associated with the physical accommodation of the asset on the ARTC's property.
- (c) Where ARTC agrees, it will provide the relevant assistance, accommodation or facilitation on the basis of this clause 2, notwithstanding that it may be required to amend its rail safety accreditation or modify existing engineering or operational standards. In such case, ARTC will seek the relevant amendments and/or make the relevant modifications.
- (d) Where ARTC is required to create an engineering or operational standard to provide the relevant assistance, accommodation or facilitation, it will create the standard.

- (e) In providing the required assistance, accommodation or facilitation, ARTC will act in a timely manner.
- (f) Where the resulting asset requires physical accommodation on ARTC's property,
  - (i) ARTC will not seek any lease or licence fee for such accommodation beyond any actual costs incurred by ARTC,
  - (ii) ARTC will provide, without cost, any permission, licence or authority required by the Access Seeker in order to gain access to the asset provided that such access is exercised by the Access Seeker in accordance with any reasonable safety requirements imposed by ARTC.
- (g) The Access Seeker retains ownership of and responsibility for the asset at all times.
- (h) The Access Seeker is responsible for removal of the asset once it is no longer required for operational purposes. In circumstances where the Access Seeker fails to become a Customer within a reasonable period after the installation of the asset, ARTC may require the Access Seeker to remove the asset.
- (i) In considering any matter with regard to this clause 2 requiring ARTC's permission, approval, agreement, cooperation or assistance, ARTC will give the matter bona fide consideration and will not unreasonably refuse to give any permission, approval, agreement, cooperation or assistance as required.

## **Investment Criteria**

### **3.1 Safety And Technical Requirements**

In the opinion of ARTC (acting reasonably) the provision of the Additional Capacity:

- (a) is technically feasible;
- (b) is consistent with the safe and reliable operation of the Network; and
- (c) meets ARTC's relevant engineering and operational standards.

### **3.2 Demand**

There is an identified level of Additional Capacity required to provide for a level of traffic task that:

- (a) is forecast on a reasonable basis by ARTC in consultation with relevant Access Seekers; and
- (b) it can reasonably be expected that demand for the Additional Capacity is likely to be sustained for at least 5 years after the completion of the investment; or
- (c) where the predicted demand is not expected to be sustained for at least 5 years after the completion of the investment, then the demand is expected to be maintained for the period over which ARTC intends reasonably to depreciate the investment where this is less than 5 years.

### **3.3 Capacity Created**

The investment will provide sufficient Additional Capacity to meet the additional demand for which it is designed.

### **3.4 Efficiency**

The investment is the most efficient method of providing the Additional Capacity, taking into account:

- (a) timeliness of providing the Additional Capacity to meet demand;
- (b) cost of providing the Additional Capacity;
- (c) appropriateness of the investment for facilitating future expansions of Capacity; and
- (d) impact on Customers using the Network both during and after construction,

or, if the investment is not the most efficient, it is otherwise the most desirable method taking into account the criteria in paragraphs (a) to (d) above.

### **3.5 Standards**

As a minimum, the investment meets the existing standard for rail infrastructure on the relevant part of the Network and does not inhibit the utilisation of the Network for existing or planned train configurations.

### **3.6 Maintenance Of Existing Capacity**

The investment does not materially reduce the Capacity of the Network.

### **3.7 Return On Investment**

ARTC can reasonably expect to earn an appropriate return on the investment over the life of the asset created, taking into account;

- (a) the efficient incremental costs and revenues forecast to be generated by the investment; and
- (b) any capital contributions made by other parties to the investment, or

regardless of the expected investment return, the investment otherwise meets the requirements of ARTC's Board of Directors.

### Train Path Allocation Process

The following is an extract from Network Management Principles (MUG Schedule F) dealing with the allocation of train paths.

#### F.1 Management Of Timetabling & Capacity Allocation Process

##### F.1.1 Periodic Review Of Capacity & Train Path Allocation

ARTC will engage in a process of reviewing Capacity and Train Path allocation as often as required, but at least every 12 months in accordance with Undertaking clause [x]<sup>67</sup>, for the purpose of:

- (c) efficient allocation of Train Paths and Capacity given Network constraints with the objective of minimising overall transit times on each corridor, subject to Customer requirements;
- (d) minimise loss of Capacity; and
- (e) allow for adjustment of Train Paths and allocations of Capacity to meet Customer requirements.

##### F.1.2 Adjustment Of Capacity Entitlement

In respect of any existing Train Path which is part of a Capacity Entitlement, if ARTC determines that the Train Path may be structured in a more efficient way to achieve the purposes set out in clause F.1.1 or would otherwise allow for ARTC to fulfil a request for a Train Path from an Applicant:

- (a) ARTC may request the relevant Customer to agree to amend its Capacity Entitlement with respect to that Train Path, including, but not restricted to, undertaking the following activities:
  - (i) convene meetings with the Customer and other Access Seekers either separately or jointly;
  - (ii) make formal or informal proposals regarding amendments to Train Paths, alternative Train Paths or operational changes to one or more Access Seekers;
  - (iii) formally request a Customer to consent to amending its Capacity Entitlement to accommodate an Access Application.

If the relevant Customer agrees, the parties will amend the relevant Access Agreement to reflect the agreed alterations.

ARTC will amend the Train Path as required to reflect the agreement referred to in clause F.1.2(b).

---

<sup>67</sup> These principles have been taken from Pacific National's "Model Undertaking – General and contain references back to the main body of that document. As the purpose of inclusion in this appendix is to provide an example of the concepts, it is not necessary for the detailed references also to be included. However, a copy of the Model Undertaking – General" can be provided on request.

### **F.1.3 Allocation of Train Paths**

Train Paths will be allocated on a “first come first served” basis provided that:

- (a) Passenger Trains will be allocated in accordance with the requirements of legislation.
- (b) Train Paths forming part of an existing Capacity Entitlement will not be available for allocation to any Applicant except;
  - (i) where the Customer has agreed to a modification to one or more Train Paths in accordance with the process outlined in clause F.1.2;
  - (ii) the allocation is for purposes of transferring the Train Paths to the same Customer’s Capacity Entitlement under a new Access Agreement in accordance with Undertaking clause [x]; or
  - (iii) the Train Paths have been withdrawn by ARTC or otherwise relinquished by the Customer in accordance with Undertaking clause [x].
- (c) Train Paths forming part of Traffic Specific Capacity will not be available for allocation to any Applicant as general Train Paths except where;
  - (i) the Customers who have an interest in accessing the relevant sub-category of Traffic Specific Capacity and ARTC can agree that such Train Paths are no longer required to be designated as Traffic Specific Capacity, or
  - (ii) Undertaking clause [x] applies.
- (d) Where relevant, Capacity reserved for Hunter Valley Coal Trains under any other access undertaking will not be allocated as Train Paths.

### **F.1.4 Resolution Of Incompatible Access Applications**

If two or more Access Applicants seek the same or incompatible Train Paths the following process will apply:

- (a) Each Applicant will be advised of the fact that there is more than one Access Applicant seeking the same or incompatible Train Paths. The Applicants will be advised of the extent of the incompatibility but no further details will be provided. The Applicants will be offered the opportunity to revise their Access Applications, but will retain their original receipt date for the purposes of determining priority with other Access Applications.
- (b) On request by either Applicant, ARTC will offer the Applicants the opportunity to meet together to consider options to resolve the incompatibility. Where the Applicants agree, ARTC will convene the meeting and provide sufficient information to allow the parties to resolve the incompatibility. In providing such information, ARTC not be taken to breach any confidentiality obligation. At the conclusion of the meeting, the Applicants will be offered the opportunity to revise their Access Applications.
- (c) In the circumstance that the Applicants choose not to revise their Access Applications or the revisions do not resolve the capacity conflict ARTC will determine the most suitable solution. In determining the most suitable solution ARTC will undertake the following steps and consider the following factors in relation to the Access Applications treating each Access Application in its entirety.
  - (i) Step 1: Apply the factors in the following order of priority;
    - (A) Network utilisation; the Access Application offering the greatest utilisation of the network will be given preference. Network utilisation includes

considerations such as train performance, frequency of use, distance of journey and term for which Access is sought.

- (B) Magnitude of amendments required to satisfy all Access Applications; the Application requiring the least modification to satisfy all or some other Applications will be the Application that is modified. Modifications will only be applied where they are of a minor nature in relation to the Access requested. Where this factor is inconsistent with factor (A), factor (A) will prevail.
- (C) Date of receipt; the Access Application received first will be given preference. Factors (A) and (B) will prevail over this factor.
- (D) Severable portion; where a severable portion of an Access Application can be satisfied the Applicant will be offered that portion of the Access requested.

(ii) Step 2: Consider Options

ARTC will, where appropriate, generate a number of additional possible solutions by allocating capacity to severable portions of the Access Applications. ARTC will make an assessment of the most suitable option by applying the factors in clause 1.4(b)(i) to all options. Options including severable portions of Access Applications will only be considered if the network utilisation is greater than offered by any single Access Application and the entire Access Application offering the greatest network utilisation can be satisfied without modification or with only minor modifications.

(iii) Step3: Advise Applicants

ARTC will advise each Applicant of the outcome of the above process in relation to its Access Application and provide the opportunity for the Applicant to revise its Access Application. A revised Access Application will retain the same receipt date (for the purposes of priority) as the original application.

### **F.1.5 Allocation Process For Traffic Specific Capacity**

In accordance with Undertaking clause [x], ARTC will develop Train Path allocation processes for each sub-category of Traffic Specific Capacity by agreement with Customers from time to time as necessary.

### **F.1.6 Shortfall Of Capacity**

Any shortfall of Capacity will be identified and dealt with in accordance with Undertaking clause [x].

## **Possession Planning Process**

The following drafting is taken from the MUG, Clause 5.

### **5.8 Possession Planning Process**

#### **Clause 5.8**

This clause provides for a process to manage maintenance of the Network where it is required to close the track (known in the industry as “taking possession”). Closing the track necessarily disrupts train movements and therefore careful planning is required to minimise the negative effects. The clause mandates a process that is currently carried out. The emphasis is on

cooperation with the aim of minimising disruption while allowing ARTC to carry out its maintenance task efficiently. Further, ARTC is obliged to work with adjacent track providers to coordinate track possessions between them, again with the aim of minimising disruption to the wider network operations.

- (j) ARTC recognises that:
  - (i) from time to time, it is necessary to close or restrict Access to a portion of the Network in order to perform essential maintenance, and
  - (ii) such closures of the Network are disruptive to Customers' operation of Trains and their businesses.
- (k) With the objective of minimising disruption to Customers and achieving efficient maintenance of the Network, ARTC will agree a Possession Planning Process with Customers as described in clause [x].
- (l) In formulating its plans for maintenance of the Network, ARTC will use its reasonable endeavours to coordinate maintenance closures with adjoining rail infrastructure providers to minimise overall disruption to Customers.

The following drafting is taken from the MUG Schedule F.

## **F.2 Possession Planning Process**

### **F.2.1 Requirement To Adjust Train Paths Temporarily**

From time to time as required, it will be necessary for ARTC to adjust any or all Train Paths and, where relevant, Capacity reserved for Hunter Valley Coal Trains on a temporary basis to efficiently maintain the Network.

### **F.2.2 Possession Planning Process**

In order to plan maintenance of the Network effectively and minimise the disruption to Customers, ARTC will agree with Customers a Possession Planning Process that will determine, at least on a quarterly basis, for the following year;

- (m) the scope of work requiring possession of the Network,
- (n) the impact of the work on each Customer's Capacity Entitlement, Traffic Specific Capacity, and, where relevant, Capacity reserved for Hunter Valley Coal Trains,
- (o) the priority for allocation of Train Paths and, where relevant, Capacity reserved for Hunter Valley Coal Trains under any alternative temporary arrangements,
- (p) the opportunities for aligning possessions with maintenance closures of other Track Owners and any other parties that will impact on the ability of Customers to operate Trains, and
- (q) the opportunities for mitigation of any disruptive effects on Customers,

### **F.2.3 Determination Of Priority**

In determining the priority for allocation of Train Paths and Capacity reserved for Hunter Valley Coal Trains in the Possession Planning Process:

- (a) ARTC will attempt, in good faith, to minimise the disruption to each Customer's business, recognising that it may not be able to satisfy all Customer demands.
- (b) ARTC will, to the extent it is practical to do so, implement any preferences for priority determined by each Customer for its own Trains.
- (c) A Train will not be given low priority merely because it is a Train that would use a Non-Coal Train Path allocated from Traffic Specific Capacity or, if relevant, is Capacity reserved for Hunter Valley Coal Train Services.

### **F.2.4 Requirement For Consultation & Cooperation**

The Possession Planning Process will involve extensive consultation with Customers and will provide opportunity for close cooperation between ARTC and Customers to minimise disruption to Customers while allowing ARTC to maintain the Network with reasonable efficiency.

## APPENDIX H ALTERNATIVE "USE IT OR LOSE IT" PROVISION

The following is drafted from the Indicative Access Agreement which forms Schedule D to Pacific National's "Model Undertaking – General". This has previously been provided to ARTC and other stakeholders.<sup>68</sup> The drafting deals with the "use it or lose it" provisions in a more comprehensive manner than provided for by ARTC in the Undertaking. The comments in the [blue boxes](#) describe differences from U2002 and are for clarification only.

### 9. VARIATION OR CANCELLATION OF TRAIN PATHS

...

#### 9.4 Removal Of Train Path For Under-Utilisation

- (a) ARTC may, by notice in writing to the Customer, delete any Scheduled Train Path from Schedule 2 (upon which deletion Schedule 2 is deemed to be amended accordingly) if the that Scheduled Train Path is not used 7 or more times (whether consecutively or not) out of any 12 such Trains which are consecutively scheduled. Such notice may only be given within 10 Business Days after the seventh occasion of not operating.
- (b) Other than if the parties agree to substitute an alternative Train Path, a Train Path has not been used within the meaning of clause 9.4(a) if the Customer has failed:
  - (i) to present a Train at the scheduled entry point onto the Network; or
  - (ii) to operate the relevant Train so that it completes its full journey,in conformance with the locations, days and times set out in the Scheduled Train Paths.
- (c) The following events do not constitute a failure under clause 9.4(a);
  - (i) the presentation of a Train at the scheduled entry point onto the Network at a time earlier or later than its scheduled departure time; and
  - (ii) the failure of a Train to exit the Network at the scheduled exit time, provided that it completes its full journey.

#### Clause 9.4(c)

Required to avoid late running trains counting towards the trigger.

- (d) ARTC may only give a notice under clauses 9.4(a);
  - (i) where, at least 5 Business Days prior to the scheduled departure time of the Train Path that would allow the issue of the notice, it has advised the Customer of its intention to issue such a notice if the criteria in clause 9.4(a) are met, and
  - (ii) where it is able, or reasonably expects to be able on the basis of current enquiries at the time, to sell the Scheduled Train Path to another Customer or prospective Customer at the time it intends to issue the notice.

#### Clause 9.4(d)

This prevents ARTC removing a Scheduled Train Path except where it has a valid alternative use for the path.

<sup>68</sup> The Model Undertaking General was created by Pacific National to address a number of issues that are not otherwise dealt with in the Undertaking. In particular it seeks to address the problem of having different undertakings for different parts of the network owned by the same entity. It is a public document and electronic copies can be obtained from Pacific National on request.

- (e) ARTC may, by notice in writing to the Customer, delete any Semi-Scheduled Train Path from Schedule 2 (upon which deletion Schedule 2 is deemed to be amended accordingly) if the following conditions are met:
- (i) the Semi-Scheduled Train Path is required by the Customer for the purpose of fulfilling a contractual obligation to a third party;
  - (ii) the contractual obligation to that third party ceases to exist;
  - (iii) the Customer ceases to use the Semi-Scheduled Train Path;
  - (iv) the Semi-Scheduled Train Path is requested by an Other Customer or potential Other Customer;
  - (v) ARTC has required the Customer to show cause why the Semi-Scheduled Train Path should not be deleted from Schedule 2; and
  - (vi) the Customer has not, within 10 Business Days of being required to show cause, provided, in ARTC's opinion, a reasonable justification why the Semi-Scheduled Train Path should not be deleted from Schedule 2.

**Clause 9.4(e)**

New clause. Semi-Scheduled Train Paths by their nature require a different 'use it or lose' arrangement.

**9.5 Review Of Scheduled Train Paths & Semi-Scheduled Train Paths**

- (a) Scheduled Train Paths and Semi-Scheduled Train Paths will be subject to a review in accordance with this clause 9.5.
- (b) ARTC may at its discretion by written notice given to the Customer cause a Scheduled Train Path or Semi-Scheduled Train Path ("**Review Path**") to be reviewed in a bona fide manner by the parties by comparing the stated departure and arrival times for the Review Path with the performance during the preceding continuous 3 month period of the actual Trains using or purporting to use that reviewable entitlement ("**3-Month History**").
- (c) If on such comparison of the Review Path with the 3-Month History the departure or arrival times for a Train using or purporting to use the Review Path differ in material respects, the parties will negotiate in good faith to amend the Review Path so that the Review Path reflects, as closely as is reasonably practicable, the 3-Month History.
- (d) Nothing in this clause 9.5 compels ARTC to offer a Train path to the Customer under clause 9.5(c) if:
  - (vii) such Train Path is unavailable by reason of contractual obligations owed by ARTC to any person (including the Customer); or
  - (viii) to do so would materially adversely impact on ARTC's ability or opportunity to efficiently and safely manage the Network.
- (e) Nothing in this clause 9.5 compels the Customer to accept a Train Path offered by ARTC under clause 9.5(c) if contractual obligations owed by the Customer to any person (including ARTC) would prevent it from doing so.

**Clause 9.5**

Modified to include Semi-Scheduled Train Paths.

The following drafting deals with efficient costs and attempts to remove ambiguity on this matter. The drafting is taken from Pacific National's "Model Undertaking – General". The comments in the blue boxes are for clarification only.

**4. PRICING PRINCIPLES**

...

**4.10 Efficient Costs**

**Clause 4.10**

The MUG adopts the principle that all costs should reflect the efficient cost of providing access rather than the actual cost. In order for this to be effective and not just a point for contention, a number of specific issues are addressed including guidance to an arbitrator should a matter involving efficient costs come to formal dispute resolution.

A mechanism is also provided for ARTC to seek endorsement of a specific cost arrangement to avoid the potential for later dispute.

- (a) Any reference in this Undertaking to costs or to a term dealing with costs, whether as a defined term or otherwise, is to be interpreted as a reference to efficient forward looking costs.
- (b) In determining whether a cost is efficient in the resolution of any dispute under clause 3.12, the arbitrator will take into account at least the following factors:
  - (i) whether the activity is reasonably necessary or incidental to providing Access to the Network to the standard required by this Undertaking;
  - (ii) the cost to achieve the same outcome by reference to any contestable market;
  - (iii) whether the scope and timing of the activity is consistent with any methodology generally accepted within the rail industry as appropriate for that activity;
  - (iv) the cost of compliance with any relevant legislation, regulation or standard;
  - (v) the requirements and expectations of Customers and other stakeholders with regard to the quality and quantum of Access to the Network.
- (c) Where ARTC undertakes an activity in a way that incurs a higher cost than might otherwise have been incurred in order to meet the requirements of Customers, and the additional cost is not disproportionate to the benefit to Customers, ARTC is entitled to treat the cost of performing the activity in that way as efficient. By way of example, if ARTC maintains the Network using a method that minimises disruption to Trains but is more expensive than a method that caused significant disruption to Trains, then provided the additional expense is not disproportionately greater than the benefit obtained, ARTC is entitled to treat such a cost as efficient.
- (d) With regard to any specific matter, where all of the Relevant Access Seekers have specifically endorsed the cost and associated scope, in the resolution of any subsequent dispute under clause 3.12 regarding that matter, the arbitrator is required to treat that cost as an efficient cost to achieve that objectives of that matter.

**Clause 4.10(d)**

The intention is to provide ARTC with a definitive process that would protect it against any subsequent disputes.

- (e) For the purposes of clause 4.10(d), where a Relevant Access Seeker has accepted ARTC's invitation to participate in a consultation process but fails to actively participate in that consultation process, if after ARTC has taken reasonable steps to obtain that person's active participation, ARTC is of the view that that person is unlikely to actively participate in the consultation process, ARTC is entitled to exclude that person from its considerations and that person is deemed to give its endorsement to the ARTC recommendations with regard to the relevant matter.

**Clause 4.10(e)**

Where a party has indicated it will participate, it is necessary that it does so. Otherwise the process would be ineffective. By deeming acceptance from a participating party, a 'non-decision' does not negative the proposition. This is acceptable as any of the participating parties is free to actively refuse endorsement of the matter.

The drafting below deals with recovery from an operational failure that causes a disruption to normal network operations. The drafting is taken from Pacific National's "Model Undertaking – General". The comments in the blue boxes are for clarification only.

## **Restated Undertaking IAA Clause 8**

### **8. COMPLIANCE WITH INSTRUCTIONS**

#### **8.1 Issue Of Instructions By ARTC**

- (a) ARTC may issue Instructions to the Customer.
- (b) Instructions may include, but are not limited to, Instructions:
  - (i) to cease use of a Train Path by the Train and for the Train to proceed over such path on the Network as ARTC nominates;
  - (ii) to continue use by the Train of the Network subject to such variation of the applicable Train Path or the Train or the composition or quality of the Train as ARTC nominates;
  - (iii) to cause the Train to proceed to a point on the Network and stand there until ARTC issues a further Instruction in relation to the Train; or
  - (iv) without limiting the generality of clauses 8.1(b)(i) to(iii), if the Train operates outside of its Train Path, to delay or redirect the Train in accordance with the Network Management Principles to allow access to the Network by a Train operated by another party that would, but for the delay or redirection of the Customer's Train, be delayed or further delayed.

**Clause 8.1(b)**

References to 'directions' removed as these are included in the definition of 'Instruction'.

'Scheduled Train Path' changed to 'Train Path' to recognise all Train Path types.

Clause 8.1(b)(iv) modified to better reflect the intent.

- (c) ARTC must:
  - (i) in giving any Instruction have due regard to minimising the disruption to the Customer's Trains; and
  - (ii) other than in an emergency, consult with the Customer in giving an Instruction concerning the use of an Customer's locomotive and its crew for the purpose of assisting in the clearing of a Network blockage.
- (d) If an Instruction which varies the Customer's Train Paths is intended by ARTC to be permanent, such permanent effect of the Instruction will not take effect until the procedure in clause 9.2 for permanent variation of a Train Path has been satisfied. Until the clause 9.2 procedure has been satisfied such Instruction will nevertheless have a temporary effect.

- (e) As soon as is reasonably practicable and in any event before an Instruction becomes effective, ARTC must give to the Customer a written copy of the Instruction if such Instruction is ordinarily advised in writing by ARTC to Accredited Operators.

## 8.2 Compliance By The Customer With Instructions And Train Control Directions

### Clauses 8.2

Substantial modification. All train operators have an obligation not to comply with any Instruction that is not lawful or contravenes the safeworking or operating rules [see Glenbrook Enquiry]. The MUC identifies those criteria that would qualify an Instruction as lawful. These are directed towards the issuer of the Instruction not knowingly requiring the operator to do something which would be unsafe.

- (a) Subject to clause 8.2(d), the Customer will comply with all lawful Instructions and will promptly advise all relevant Train crew of any changes to, or the making or giving of, Instructions.
- (b) If a lawful Instruction is a Train Control Direction, it must be complied with immediately.
- (c) To be a lawful Instruction, an Instruction must at least meet the following criteria:
- (i) the Instruction is not contrary to the requirements of any Operational Document;
  - (ii) the Customer is qualified to perform the activities explicitly or implicitly required to comply with, and in the manner anticipated by, the Instruction;
  - (iii) the Instruction would not require either party to breach its Accreditation;
  - (iv) to the best of ARTC's knowledge the Instruction can be safely performed in the known prevailing circumstances; and
  - (v) the Instruction does not contravene, nor would cause the Customer to contravene, any law if complied with in the manner anticipated by the issuer of the Instruction.
- (d) Unless the Train Control Centre gives an Instruction that is a Train Control Direction, the Customer need only comply with an Instruction if it was given a reasonable time before the required time for compliance.
- (e) The Customer must comply with all lawful Instructions in such a way as to reasonably minimise disruption to any other person's use of the Network.
- (f) Subject to clause 8.3 and clause 16, ARTC is not responsible for any delay suffered or cost incurred by the Customer in complying with a lawful Instruction of ARTC, and the Customer releases ARTC from any Claim arising from such compliance.
- (g) Subject to clause 8.3 and clause 16, the Customer is not responsible for any delay suffered or cost incurred by ARTC in the Customer complying with an Instruction of ARTC, and ARTC releases the Customer from any such Claim arising from such compliance.

### 8.3 Provision Of Assistance To A Distressed Train

#### Clause 8.3

New clause.

- (a) Where ARTC issues an Instruction requiring the Customer, to aid a distressed Train of an Other Customer;
  - (i) ARTC will pay to the Customer the Prescribed Fee set out in Schedule 3 or, the Customer's actual reasonable Direct Costs, whichever is the greater;
  - (ii) ARTC will indemnify the assisting Customer against any liability for damage or negligence that arises in complying with the Instruction except to the extent that the assisting Customer engages in wilful, dishonest or unlawful conduct.
- (b) Where ARTC issues an Instruction requiring an Other Customer to aid a distressed Train being operated under this Access Agreement, the Customer will indemnify ARTC against;
  - (i) the costs incurred in providing the assistance; and
  - (ii) any liability for damage or negligence that arises from ARTC arranging assistance and the Other Customer complying with the Instruction except to the extent that either ARTC or the Other Customer engages in wilful, dishonest or unlawful conduct.

### New Schedule To Undertaking & IAA

#### Recovery From Failure Of Normal Operations

- (a) In the event there is a significant disruption to the normal operation of the Network necessitating a modification to the Daily Train Plan (other than the mere early or late running of Trains), ARTC will modify its management of those elements of the Daily Train Plan under its control so as to attempt to minimise disruption to Services and restore the Network to normal operation.
- (b) The elements of the Daily Train Plan under ARTC's control or partial control include:
  - (i) safeworking of Trains and infrastructure maintenance personnel and their equipment;
  - (ii) resequencing, repositioning and prioritisation of Trains; and
  - (iii) allocation, cancellation and reprogramming of Train Paths.
- (c) In undertaking remedial action in accordance with clause [x].(a), ARTC will, using its discretion, determine the optimum recovery strategy to restore the Network to its normal operation and, except where required otherwise for reasons of safety or contractual requirements, will seek to implement that course of action.
- (d) In determining the optimum recovery strategy identified in clause [x].(a), ARTC will take into account the preferences of Customers and seek to minimise any negative consequences that arise to Customers from the implementation of the optimum recovery strategy.

- (e) ARTC may issue Instructions to an Operator for the purpose of assisting with the recovery from disruption to normal operations and the Operator will be required to comply with the Instruction, or if the Operator is not a Customer, that the Customer will obligate its Operator to comply with an Instruction.
- (f) Where an Instruction is issued in accordance with clause [x].(e) requiring an Operator to use its Rollingstock to aid a distressed Train belonging to another Operator;
  - (i) ARTC will pay to the assisting Operator the prescribed fee set out in Schedule [x] or, the Operator's direct costs, whichever is the greater;
  - (ii) ARTC will indemnify the assisting Operator against any liability for damage or negligence that arises in complying with the Instruction; and
  - (iii) the Customer whose Train is assisted will be required to indemnify ARTC against;
    - (A) the costs incurred in providing the assistance; and
    - (B) any liability for damage or negligence that arises from the assisting Operator complying with the Instruction.

## **APPENDIX K STORAGE OF ROLLINGSTOCK ON NETWORK**

---

The drafting below deals with the storage of rollingstock on the network. The drafting is taken from Pacific National's "Model Undertaking – General". The comments in the blue boxes are for clarification only.

### **STORAGE OF ROLLINGSTOCK**

- (a) ARTC will allow the Operator to store Rollingstock on the Network, free of charge, provided that;
  - (i) the Operator conforms to any reasonable requirement by ARTC with regard to location, safety or environment.
  - (ii) the storage does not reduce the availability of the Network otherwise required for the operation of Trains, including Trains that had not been planned at the time that the storage was permitted; and
  - (iii) the Operator warrants that it will remove the relevant Rollingstock when requested by ARTC.
- (b) The Operator is required to give ARTC at least 20 Business Days notice that it wishes to store Rollingstock on the Network and identify the preferred location, quantity and type of Rollingstock and any other relevant details, including, if known, the expected duration of the storage.
- (c) ARTC will use its reasonable endeavours to provide the storage as requested, but may, at its discretion, provide one or more alternative locations if the preferred location is not suitable or available.
- (d) ARTC may require the Operator to remove the stored Rollingstock by giving the Operator at least 20 Business Days notice, in circumstances where the stored Rollingstock prevents or reduces the use of the Network for the operation of any Train (including prospective Trains).