



AUSTRALIAN RAIL TRACK CORPORATION LTD

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Review of South Australian Rail Access Regime Information Kit: Discussion Paper
Essential Services Commission of SA
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REVIEW OF SA RAIL ACCESS REGIME INFORMATION KIT DISCUSSION PAPER

ARTC SUBMISSION

ARTC welcomes the opportunity to provide comment in relation to your Discussion Paper published in December 2009.

Due the short time from made available at this time of the year and other priorities facing the company, ARTC has not engaged in a detailed review of all the Commission's proposals, but has elected to provide only general comments. Many of the proposals appear to be based on approaches taken in other jurisdictions including the interstate rail network. As such, ARTC has made previous detailed submissions to the relevant regulator (including the Commission) that can be referenced if needed.

ARTC notes that the Commission has recently completed its inquiry into the Access Regime applicable to the intrastate railways in SA, where the need to clarify and improve certain aspects of the Information Kit was identified. Changes proposed to the Information Kit relate primarily to aspects of the Information Kit relating to access pricing principles, and the information brochure.

The Commission would be aware of the scope of ARTC's interstate network and the extent to which its interstate network interfaces with the intrastate lines in South Australia. In its inquiry into the SA Access Regime, the Commission was required to recognise Clause 2.1 of the CIRA which provides an overarching principle, committing all signatories to establish a simpler and consistent national approach to the economic regulation of significant infrastructure. In that inquiry, the Commission stated that it believed that an access regime should be sufficiently



flexible to accommodate differences between railway operations, and reflective of the state of any intermodal competition. As such, an overarching national regulation approach needs to be balanced against the specific context in which regulation is being applied.

ARTC agrees with the Commission's position in this regard, and the draft principles prepared by ARTC and ACCC in 2006 explicitly acknowledged that different regulatory arrangements should apply to all rail networks depending on degree of market power and industry structure.

The intrastate rail lines in SA are vertically integrated. The rail lines serve in various parts a number of different agricultural, mining and general freight supply chains. Without having undertaken a detailed assessment of the markets involved, ARTC would imagine that there are varying degrees of intermodal competition and market power that the access provider may have. ARTC expects that, as is the case for its own network in SA, there will be a number of promising opportunities for growth in rail freight on the intrastate lines sourced from the many mining ventures expected to come on line in the next few years.

It is likely that at least some of this business that will eventuate on the intrastate network in SA will utilize at least some part of the interstate network managed by ARTC. As such, prospective access seekers will be required to negotiate various access aspects, including pricing, with both ARTC and the intrastate access provider. ARTC, its existing customers and prospective customers would prefer consistency with respect to pricing and other facets of access between its own undertaking and neighbouring regimes. Significant volumes could be lost to both the interstate and intrastate rail networks in SA (either diverted to another mode or new projects not getting off the ground) as a result of a lack of coordination and consistency between jurisdictions and regimes covering these networks. Similarly, the conduct of one access provider can impact on rail volumes generally, and affect the viability of the network as a whole.

Presumably to recognise the CIRA obligations, the Commission seems to have sought re-structure elements of the Information Kit with reference to elements of both ARTC's Interstate Access Undertaking and the AustralAsia railway access regime. These regimes are intended to apply to networks with differences in the extent of market power and industry structure where the interstate network is vertically separated and the AustralAsia railway, vertically integrated.

This may have been done so as to reflect the fact that intrastate lines in SA share some characteristics of both the interstate lines and the AustralAsia railway.



Nevertheless, mixing and matching of elements of various regimes needs to be undertaken with some caution.

The Commission's proposals in relation to the Pricing Principles

Presumably with a view to improving consistency of pricing principle across jurisdictions, ARTC notes that the Commission has proposed to incorporate greater prescription in the Pricing Principles similar to the level of prescription incorporated in ARTC's Interstate Access Undertaking. ARTC supports this intention.

The Commission's proposals include increased detail in relation to the approach to determining of costs to be reflected in floor and ceiling prices largely aligned to similar principles incorporated in the AustralAsia regime, but with certain aspects relating to the allocation of costs, asset valuation and roll forward, and rate of return largely aligned to similar elements of the ARTC Interstate Access Undertaking.

ARTC's Interstate Access Undertaking incorporates revenue limits for each part of the interstate network rather than price limits for particular access being sought. This is intended to:

- Recognise the vertically separated nature of ARTC's interstate network;
- Recognise the relatively homogenous nature of usage of the interstate network where pricing for particular types of usage does not vary substantially, and price discrimination for like uses in like markets is prohibited; and
- Prevent cross subsidisation of any part of the network by users of other parts of the network.

The proposed ceiling limits pricing for a third party user to the full economic cost associated with the operation of the required infrastructure needed by that user. The full economic cost is the cost of the required infrastructure less the incremental cost associated with all other usages of that network and a reasonable contribution to the fixed costs of that network by the other usages (but not greater than the contribution to fixed costs generated by the revenues for the other usages).

This formulation is identical with one leg of the full economic cost calculation used in the AustralAsia regime (where there is no sustainable competitive price). The



other leg in that regime is a stand alone cost of the infrastructure required for that third party user. The ceiling price is the lesser of the two formulations in the AustralAsia regime.

ARTC would expect, given the present nature, usage and cost recovery of the intrastate network in SA that the first leg above would be the leg that constrains pricing in most cases, but that there would still be a significant gap between floor and ceiling. As such, an argument not to incorporate both legs of the test could be made.

Whilst ARTC's Interstate Access Undertaking incorporates a revenue test only, a ceiling price reflecting the shortfall in recovery of full economic cost (similar to the first leg above) is implied by that revenue test. As such, it could be argued that there is some consistency in ceiling price limits. However the likely gap between ceiling and floor price (due to the relatively low level of cost recovery on these networks) is of some concern in the absence of reference or indicative pricing, and where the network is vertically integrated.

ARTC believes that where the network is vertically integrated, controls should be put in place so that charges cannot be structured in such a way as to yield a competitive disadvantage to a third party user, and that the access provider should charge a third party user no more than it charges itself for a given service.

The presence of reference or indicative charges that are published would also assist in this regard.

ARTC proposes that the Commission should seek to satisfy itself that these controls are in place and are effective.

Finally, in relation to the Commission's proposal in relation to asset base roll forward, which are largely the same as the principles incorporated in ARTC's Interstate Access Undertaking; ARTC seeks the Commission's consideration of the roll forward principles incorporated in ARTC's Hunter Valley Access Undertaking, currently being reviewed by the ACCC. These principles enable economic losses incurred to be included in the asset base roll forward for later recovery, where market conditions are suited, so as to enable recovery of the full cost of an investment over the longer term. ARTC believes that such an approach will provide incentive for an infrastructure provider to invest ahead of demand (as is often required by users) as economic losses incurred during volume ramp up as the market grows to take up the capacity provided by the investment can be recovered when the market grows to a point where it can afford it. Without being able to capitalise losses, constraining cost recovery to a simple building blocks



ceiling may prevent achievement of a regulated return on the investment over the life of the investment. Further detail in relation to this approach can be found at Attachment D to ARTC's Explanatory Guide¹ accompanying ARTC Hunter Valley Access Undertaking application to the ACCC.

The Commissions proposals in relation to the Information Brochure.

ARTC notes that the amendments to the Information proposed by the Commission are made with a view to:

- Making explicit the requirement for separation of above and below rail components of the indicative prices;
- Requiring the access provider to provide more detail regarding the factors to be used to determine where access prices are likely to fall within the floor-ceiling range;
- Include greater detail regarding the quantitative basis of the indicative floor and ceiling prices provided; and
- Listing the types on non-price terms and conditions of access to be provided by the access provider.

ARTC supports these objectives. ARTC believes that this level of disclosure will increase consistency with the level of disclosure of pricing information required to be published or incorporated in an indicative access proposal under ARTC's Interstate Access Undertaking, so long as the information provided is sufficient for the third party user to have confidence in the level of pricing to be charged and that the level of pricing will not competitively disadvantage the third party user.

ARTC has no issue with the proposed amendments at section 4 of the Information Kit.

In section 4A of the Information Kit, the Commission has proposed amendments designed to facilitate the second of the objectives above, by requiring the access provider to make available 'likely price' information. The proposals provide for the provision of factors to be used to determine where access prices are likely to fall within the floor-ceiling range. Proposals also include the factors that the access

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<http://www.accc.gov.au/content/item.phtml?itemId=870155&nodeId=ff9452fd1948a80806fec3ec2f48bdce&fn=ARTC%20Hunter%20Valley%20Access%20Undertaking%20Explanatory%20Guide.pdf>



provider may consider in differentiating and limits on differentiation largely similar to those incorporated in ARTC Access Undertaking. Among other things, the proposal seems to provide for an indicative price for the service to be provided, any requirement for additional capacity and resulting price impacts. This is consistent with the equivalent requirement in ARTC's Interstate Access Undertaking and is therefore supported by ARTC.

Section 4A also provides scope for non-pricing information to be provided as part of the Information Brochure. The Commission's proposals are not inconsistent with the type and extent of information that ARTC is required to make available during negotiation under its Interstate Access Undertaking. The differences are not substantial and in some cases disclosure under the Information Kit is even more comprehensive. A greater level of disclosure may, however, be appropriate to address incentives inherent in the vertically integrated nature of the network.

The submission contains no information that ARTC would consider commercial-in-confidence.

For further information regarding the preparation of this submission, could you please contact myself on (08) 8217 4314, sormsby@artc.com.au, or Mr. Glenn Edwards, (08)82174292, gedwards@artc.com.au.

A handwritten signature in black ink, appearing to be 'S Ormsby'.

per

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