



# Review of rail guidelines for the Tarcoola-Darwin Railway

FINAL DECISION

October 2019

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## Glossary of terms

Above-Rail	Rolling stock such as locomotives, carriages and wagons
Above-Rail Operator	Means an operator of <b>Above-Rail</b> infrastructure in accordance with an <b>Access Contract</b>
Act	AustralAsia Railway (Third Party Access) Act 1999
Access Contract	A contractual agreement between an <b>Above-Rail Operator</b> and the <b>Access Provider</b> regarding Access to the <b>Tarcoola-Darwin Railway</b>
Access Price	The price of third party access to <b>Railway Infrastructure</b> , provided by the <b>Access Provider</b>
Access Provider	A party providing, or able to provide, <b>Services</b> for <b>Railway Infrastructure</b> – sometimes referred to as a <b>Below-Rail</b> operator
Access Regime	The regime to allow <b>Third Party Operators</b> access to <b>Railway Infrastructure</b> on the <b>Tarcoola-Darwin Railway</b> , under the <b>Code</b>
Access Seeker	<b>An Above-Rail Operator</b> seeking access to the <b>Services</b> provided by the <b>Railway</b>
Affiliated Operator	The <b>Above-Rail</b> Operator that is a related party to <b>the Access Provider</b>
ARTC	The Australian Rail Track Corporation Ltd
Below-Rail	Refers to operations involving track management, including the track and associated infrastructure required to operate it
Code	The AustralAsia Railway (Third Party Access) Code, which is contained as a Schedule to the AustralAsia Railway (Third Party Access) Act 1999 (SA) and the AustralAsia Railway (Third Party Access) Act 1999 (NT), which specifies the terms and conditions of Access for <b>Third Party Operators</b> to the <b>Tarcoola-Darwin Railway</b>
Commission	Essential Services Commission, established under the Essential Services Commission Act 2002
DORC	Depreciated Optimised Replacement Cost – a methodology for the valuation of assets
ESC Act	Essential Services Commission Act 2002
GWA	Genesee & Wyoming Australia Pty Ltd., the provider of <b>Railway Infrastructure</b> , as well as a provider of <b>Above-Rail</b> services
GWAN	Genesee & Wyoming Australia (North) Pty Ltd, a wholly owned subsidiary of <b>GWA</b>
MCA-NTD	Minerals Council of Australia (Northern Territory Division)
Pacific National	Pacific National Pty Limited

Pricing Schedule	The Schedule to the <b>Code</b> setting out the access pricing principles to be followed by the arbitrator
Railway Infrastructure	Facilities necessary for the operation or use of the railway, including signalling and control systems as well as railway track, but not Rolling Stock
Services	Mean Trains run by an <b>Above-Rail Operator</b> using the <b>Railway</b> , which provides freight or passenger <b>services</b> including work trains
Tarcoola-Darwin Railway	The railway to which the <b>Code</b> applies, being the whole of the railway from (a point near) Tarcoola to its end in Darwin (in the Port of Darwin)
Third Party Operators	<b>Above-Rail</b> operators who are not related to or affiliated with the <b>Access Provider</b>
Vertical Integration	Where the owner of the <b>Railway Infrastructure</b> is also a provider of <b>Above-Rail</b> operations

# 1 Executive summary

The Essential Services Commission (**Commission**) has reviewed the Guidelines for the **Tarcoola-Darwin Railway** pursuant to clause 45A(1) of the AustralAsia Railway ('Third Party Access') Code (**Code**), a Schedule to the AustralAsia Railway (Third Party Access) Act 1999 (**Act**) (SA) and the AustralAsia Railway (Third Party Access) Act 1999 (NT). The review has found the need for amendments to the Guidelines intended to clarify certain requirements and to better align the Guidelines with the requirements of the Code.

The intent of the review was to identify opportunities to improve the Guidelines so that they may better assist commercial negotiation of railway access, are up-to-date and relevant for existing and prospective railway users, and do not impose undue regulatory costs. While neither the Code nor the Act contain listed objectives or an objects clause, the intent of the review was consistent with the overall goals of access regulation under Part IIIA of the Competition and Consumer Act 2010 (Cth); that is, to promote the efficient use of, and investment in, infrastructure and promote competition in activities that rely on the use of infrastructure services.

This Final Decision has been informed by submissions made to the Commission during the course of the review, including submissions to the April 2019 Draft Decision and to the July 2019 Further Draft Decision. The Commission consulted with stakeholders both at the initiation stage of the project in late 2016 and early 2017, on the April 2019 Draft Decision and on the July 2019 Further Draft Decision. Submissions to the review were received from a range of organisations, including rail operators and industry associations representing upstream users of the railway infrastructure.

## 1.1 Findings and recommendations

The findings outlined in the Final Decision are broadly the same as those outlined in the July 2019 Further Draft Decision.

The Commission has:

- ▶ retained the guidance on floor and ceiling pricing principles and incremental cost, which apply in the case of arbitration
- ▶ included the amendments proposed in the Further Draft Decision. Those amendments aim to better meet the Commission's obligations under the Code, and largely relate to the calculation of the rate of return in the case of arbitration, including the treatment of expected inflation, the calculation of the risk premium in the event of any extension of the railway and the clarification of the setting for floor price purposes
- ▶ modified the procedure regarding compliance of regulatory accounts, such that, in the event that the Access Provider does not have an External Director, the statement of compliance may be signed by an External Director of a related entity of the Access Provider
- ▶ retained the guidance on regulatory information requirements including reporting requirements on a financial year basis, and
- ▶ made minor modifications to improve readability and provide clearer language.

The findings noted above are reflected in Guideline No 1 – Access Provider Reference Pricing and Service Policies, Guideline No 2 – Arbitrator Pricing Requirements, and Guideline No 3 – Regulatory Information Requirements, which have been released with this Final Decision.

The Commission notes that in 2020 it will commence a review of the revenues earned for providing access to the Tarcoola-Darwin railway. Alongside the review of revenues, the Commission intends to undertake a compliance audit of the Access Provider's obligations under the Code as they relate, among other things, to ring-fencing and the protection of confidential information.

## 1.2 Background

The Code is established to facilitate commercial negotiation for access by **Third Party Operators** to the Tarcoola-Darwin Railway. The Commission's role as Regulator under the Code is to facilitate access negotiations and conciliate access disputes, monitor performance reporting and compliance with the Code, conduct periodic reviews such as reviews of revenues, and develop and maintain guidelines.

The Guidelines reviewed were:

- ▶ Guideline No 1 – Access Provider Reference Pricing and Service Policies
- ▶ Guideline No 2 – Arbitrator Pricing Requirements, and
- ▶ Guideline No 3 – Regulatory Information Requirements.

The review did not consider Guideline No 4 – Compliance Systems and Reporting, as that Guideline will be reviewed as part of a broader review of compliance and monitoring to be undertaken in 2020.

## 2 The review

### 2.1 Purpose of Guidelines and review

The AustralAsia Railway (Third Party Access) Code (**Code**) is a Schedule to the AustralAsia Railway (Third Party Access) Act 1999 (SA) and the AustralAsia Railway (Third Party Access) Act 1999 (NT) (**Act**).<sup>1</sup> The Code sets out a negotiate-arbitrate framework for access to specified infrastructure services provided by the operator of the **Tarcoola-Darwin Railway**.<sup>2</sup> The Code appoints the Essential Services Commission (**Commission**) as the Regulator of third party access to those services in both South Australia and the Northern Territory. It is noted, however, that the Tarcoola-Darwin Railway does not constitute a regulated industry for the purposes of the Essential Services Commission Act 2002 (**ESC Act**).

The Code includes a Pricing Schedule that provides considerable direction for access pricing in different circumstances.

The Commission has issued four Guidelines for the Tarcoola-Darwin Railway, pursuant to the Code.<sup>3</sup> Those Guidelines are:

- ▶ Guideline 1 – Access Provider Reference Pricing and Service Policies
- ▶ Guideline 2 – Arbitrator Pricing Requirements
- ▶ Guideline 3 – Regulatory Information Requirements, and
- ▶ Guideline 4 – Compliance Systems and Reporting.

#### 2.1.1 Guideline 1

Guideline 1 is published to fulfil the requirements of clauses 9(1)(e) and 9(3) of the Code. In practice, the Guideline sets out matters of procedure relating to the provision of information by an **Access Provider** to an **Access Seeker** on rail track utilisation, time path allocation and service standards. The distinguishing feature of the Guideline is that it addresses the process involved in the request of **Access Prices** for reference purposes.

#### 2.1.2 Guideline 2

In the event of an access dispute, the Code requires an Arbitrator to determine an Access Price payable to the Access Provider by an Access Seeker. The Arbitrator is obliged to apply particular principles and methods in accordance with the Code. Further, the pricing principles outlined in the Code empower the Commission to prepare Guidelines addressing specific matters which arbitrators must consider when determining awards. In practice, Guideline No 2 outlines principles to be considered in calculating rates of return, incremental cost, and floor and ceiling prices for **Railway Infrastructure** services.<sup>4</sup>

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<sup>1</sup> The Code is available at: <http://bit.ly/AustRailway3rdPartyAccessAct>.

<sup>2</sup> See Appendix A for a short summary of the Tarcoola-Darwin Railway.

<sup>3</sup> Amended versions of Guideline 1, 2 and 3 can be found on the Commission's website: <https://www.escosa.sa.gov.au/industry/rail/codes-guidelines>. Guideline 4 is available at: [https://www.escosa.sa.gov.au/ArticleDocuments/231/050428-Tarcoola-DarwinRailGuidelineNo\\_4-ComplianceSystems\\_Reporting.pdf.aspx?Embed=Y](https://www.escosa.sa.gov.au/ArticleDocuments/231/050428-Tarcoola-DarwinRailGuidelineNo_4-ComplianceSystems_Reporting.pdf.aspx?Embed=Y).

<sup>4</sup> See Schedule to the Code: Access Pricing Principles, Division 1, clauses 6(f), (7)(a) and (7)(b)); Schedule to the Code: Access Pricing Principles, Division 2, clauses (2)(d)(iii), (6), (7), (8); and Schedule to the Code: Access Pricing Principles, Division 3, clauses (3), (4), (5).



### 2.1.3 Guideline 3

At various points of the Code, including under clauses 39(1) and 46 of the Code, an Access Provider is obliged to keep and/or report certain information to the Regulator. Guideline 3 outlines the information that the Access Provider is required to keep, prepare and report to the Commission to fulfil requirements under the Code. This includes information on the separation of accounts and records and for periodic reviews of revenue.

### 2.1.4 Guideline 4

Clauses 5 and 46(2) of the Code along with section 8 of the Essential Services Commission Act 2002 (SA) enable the Commission to issue a compliance guideline to fulfil its function to monitor and enforce compliance with the Code. Guideline 4 sets out processes of the reporting of compliance by an Access Provider.

### 2.1.5 The review

Clause 45A of the Code empowers the Commission to vary or revoke guidelines developed and published under the Code, or develop and publish new or substitute guidelines. The purpose of the review was to identify opportunities to improve the Guidelines issued by the Commission so that they may assist commercial negotiation of railway access, are up-to-date and relevant for existing and prospective railway users, and do not impose undue regulatory costs. The Guidelines were last reviewed in 2008.<sup>5</sup>

The Code and the Act do not set out specific objectives or contain an objects clause which might help to guide the conduct of this review. Nonetheless, the scope and purpose of the review is consistent with the general intent of clause 6 of the Competition Principles Agreement including to establish principles that the regulatory framework should embody.<sup>6</sup> It is also consistent with objectives of access regulation under Part IIIA of the Competition and Consumer Act 2010 (Cth): to promote the efficient use of and investment in infrastructure and promote competition in activities that rely on the use of infrastructure services.<sup>7</sup>

## 2.2 Scope of review

The review has focussed on areas where the Guidelines could be amended to better facilitate commercial negotiation of access to **Railway Infrastructure** services, consistent with the general intent of clause 6 of the Competition Principles Agreement and the objectives of access regulation under Part IIIA of the Competition and Consumer Act 2010 (Cth), by seeking to:

- ▶ provide clear, relevant and detailed information about the Access Regime and the Commission's requirements (to assist Access Seekers and Access Providers to understand the framework for gaining access to Railway Infrastructure Services and to provide guidance for the arbitrator)
- ▶ ensure that Access Providers provide Access Seekers with sufficient information to reach commercially agreed outcomes, and
- ▶ ensure that the Commission's requirements represent good regulatory practice and anticipate, as much as practicable, future changes in the rail industry.

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<sup>5</sup> See Commission, 'AustralAsia Railway (Third Party Access) Code: Guideline Review', Final Decision, 2008, pp.1-30, available at: <http://bit.ly/ThirdPartyAccessGuidelineReview-Final>.

<sup>6</sup> See COAG Competition Principles Agreement, 11 April 1995, available at:

<https://www.coag.gov.au/sites/default/files/agreements/competition-principles-agreement-amended-2007.pdf>.

<sup>7</sup> See National Competition Council (2018), 'Declaration of Services: A Guide to Part IIIA of the Competition and Consumer Act 2010 (Cth)', April 2018, p.11, available at: [http://ncc.gov.au/images/uploads/NCC\\_Declaration\\_Guide\\_-\\_Version\\_6\\_-\\_April\\_2018.pdf](http://ncc.gov.au/images/uploads/NCC_Declaration_Guide_-_Version_6_-_April_2018.pdf).

Of the four Guidelines issued by the Commission for the Tarcoola-Darwin Railway, the review has only covered numbers one, two and three; that is, the Guidelines published to set out matters of procedure relating to the provision of information, to set out pricing principles and to outline reporting obligations. Guideline 4 was not considered and will be reviewed as part of the Commission's broader review of its Regulatory and Compliance Framework to be undertaken in 2020; this will allow for greater alignment of compliance requirements across industries regulated by the Commission in South Australia.<sup>8</sup>

Clause 45A(2) of the Code states that, in developing or varying Guidelines, the Regulator should take into account interface issues that may arise under the **Access Regime** (insofar as this may be relevant and insofar as this is consistent with, and not in derogation of the operation of, the other provisions of the Code). Interface issues are those which directly affect the Tarcoola-Darwin railway and at least one other railway (in practice, interface issues are likely to involve the interstate railway).

The Commission has considered interface issues, but has not identified any that would necessitate amendments to the Guidelines. In particular, the Commission has not received any complaints or otherwise become aware of any material interface issues that should be addressed by changes to Guidelines 1, 2 and 3. Further, none of the submissions to the review, including from the Australian Rail and Track Corporation (**ARTC**), which manages Australia's interstate rail network, have so far raised concerns about interface issues.

This review did not examine the Code or the Act; any decision to review the operation of the Code lies jointly with the Northern Territory Minister for Infrastructure, Planning and Logistics and the South Australian Minister for Planning, Transport, Infrastructure and Local Government.<sup>9</sup> Rather, the review focussed on the Guidelines, consistent with clause 45A(1) of the Code, where the Regulator may, from time to time as the Regulator thinks fit, vary or revoke guidelines developed and published under the Code, or develop and publish new or substitute guidelines.

## 2.3 Process of review

In undertaking the review the Commission has been informed by:

- ▶ submissions from stakeholders
- ▶ its analysis of the economic conditions on the Tarcoola-Darwin Railway
- ▶ knowledge gained from its role as the regulator of the Code, and
- ▶ regulatory practice in other parts of Australia.

In December 2016, the Commission sought submissions on the review of the Guidelines. The downstream users of the Tarcoola-Darwin Railway are well placed to comment on the Guidelines. Those users include the Access Provider and rail transport companies (both of which must be accredited by the National Rail Safety Regulator). Upstream users of the Tarcoola-Darwin Railway, such as mining companies, are also likely to have an interest in the Guidelines, as service levels and the cost of transport can influence mining investment decisions and demand for railway services.<sup>10</sup>

Submissions at the initiation of the review were received from:

- ▶ Genesee and Wyoming Australia (**GWA**), a joint-venture of Genesee and Wyoming Inc. and Macquarie Infrastructure and Real Assets. It is a rail freight company with **Above-Rail** assets (rolling

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<sup>8</sup> The same approach for compliance guidelines was taken in the 2019 Review of the South Australian Rail Access Regime Information Kit.

<sup>9</sup> See clause 50(1) and (2) of the Code.

<sup>10</sup> See, for example, Minerals Council of Australia – Northern Territory Division (MCA-NTD), 'Submission on the 2017 ESCOSA Review of Guidelines for the Access regime for the Tarcoola-Darwin Railway', 24 February 2017, p. 3, available at: <http://bit.ly/RailGuidelinesSubmission-MineralCouncil>.

stock such as locomotives, carriages and wagons) and **Below-Rail** assets (track and associated infrastructure required to operate it). Its related entity, GWA (North) Pty Ltd (**GWAN**) is the current concession-holder for the Below-Rail assets of the Tarcoola-Darwin Railway, while GWA operates most trains on that line<sup>11</sup>

- ▶ Pacific National Pty Limited (**Pacific National**), a rail freight company operating Above-Rail Services in parts of Australia,<sup>12</sup> and
- ▶ the Minerals Council of Australia – Northern Territory Division (**MCA-NTD**), an industry association that represents resources companies in the Northern Territory.<sup>13</sup>

Following release of the Draft Decision in April 2019, the Commission received further submissions from GWA<sup>14</sup>, Pacific National,<sup>15</sup> MCA-NTD,<sup>16</sup> as well as submissions from:

- ▶ the ARTC, a Commonwealth Government-owned corporation that manages the majority of Australia's interstate rail network,<sup>17</sup> and
- ▶ the South Australian Chamber of Mines and Energy (**SACOME**), which is the representative body for the minerals and energy industry in South Australia.<sup>18</sup>

The Commission released a Further Draft Decision in July 2019, which proposed new amendments to more explicitly address requirements under the Code.<sup>19</sup> Submissions on the Further Draft Decision were received from GWA<sup>20</sup> and Pacific National.<sup>21</sup>

The issues raised in the submissions to the review were carefully considered by the Commission in making this Final Decision. Where relevant, certain arguments and submissions have been mentioned in this Final Decision, either by direct quotation or by reference to themes or arguments, to assist stakeholders to understand the proposed positions that have been reached. A failure to reference an argument or submission does not mean that it has not been considered by the Commission in arriving at its conclusions.

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<sup>11</sup> See GWA (2017), 'Submission on Review of Regulatory Guidelines', 24 February 2017, available at: <http://bit.ly/RailGuidelinesSubmission-GWA>.

<sup>12</sup> See Pacific National, Submission to the Review of Rail Guidelines, February 2017, p. 3, available at: <http://bit.ly/RailGuidelinesSubmission-PacificNational>.

<sup>13</sup> See MCA-NTD, Submission on the 2017 ESCOSA Review of Guidelines for the Access regime for the Tarcoola-Darwin Railway, p.13.

<sup>14</sup> See GWA (2019), 'Review of Regulatory Guidelines – Submission May 2019', available at: <https://www.escosa.sa.gov.au/ArticleDocuments/1059/20190607-Rail-ReviewOfRailGuidelinesandRegimeDDSubmission-GWA.pdf.aspx?Embed=Y>.

<sup>15</sup> See Pacific National (2019), '2019 Review of rail guidelines for Tarcoola-Darwin Railway and South Australian rail access regime information kit', available at: <https://www.escosa.sa.gov.au/ArticleDocuments/1059/20190607-Rail-ReviewOfRailGuidelinesandRegimeDDSubmission-PacificNational.pdf.aspx?Embed=Y>.

<sup>16</sup> See MCA-NTD (2019), 'Submission on review of rail guidelines for the Tarcoola-Darwin Railway – Draft Decision', available at: <https://www.escosa.sa.gov.au/ArticleDocuments/1059/20190607-Rail-ReviewOfRailGuidelinesandRegimeDDSubmission-NT-MCA.pdf.aspx?Embed=Y>.

<sup>17</sup> See Australian Rail Track Corporation (ARTC) (2019), '2019 Review of rail guidelines for Tarcoola-Darwin Railway', available at: <https://www.escosa.sa.gov.au/ArticleDocuments/1059/20190607-Rail-ReviewOfRailGuidelinesandRegimeDDSubmission-ARTC.pdf.aspx?Embed=Y>.

<sup>18</sup> See South Australian Chamber of Mines and Energy (SACOME) (2019), 'ESCOSA Review of Rail Guidelines for Tarcoola-Darwin Railway', available at: <https://www.escosa.sa.gov.au/ArticleDocuments/1059/20190607-Rail-ReviewOfRailGuidelinesandRegimeDDSubmission-SACOME.pdf.aspx?Embed=Y>.

<sup>19</sup> Consistent with clause 8 of the Code, a notice of the Further Draft Decision under consideration was published in a national newspaper, inviting interested persons to make submissions.

<sup>20</sup> See GWA (2019), 'Re: Further Draft Decision – Review of Guidelines – Tarcoola to Darwin line', 30 August 2019, available at: <https://www.escosa.sa.gov.au/ArticleDocuments/21411/20190910-Rail-ReviewRailGuidelines-Tarcoola-Darwin-FDDSubmission-GWA.pdf.aspx?Embed=Y>.

<sup>21</sup> See Pacific National (2019), 'Further Draft Decision on Review of Rail Guidelines for the Tarcoola-Darwin railway', 27 August 2019, available at: <https://www.escosa.sa.gov.au/ArticleDocuments/21411/20190910-Rail-ReviewRailGuidelines-Tarcoola-Darwin-FDDSubmission-PacificNational.pdf.aspx?Embed=Y>.

## 2.4 Context for review

The Commission has considered two contextual matters as part of this review:

- ▶ the economic conditions that currently prevail and are likely to prevail in the near future and the implications for the use of the Railway, which impact on the Access Regime and requirements of the Guidelines, and
- ▶ the requirements that relate to the Guidelines, as set out in the Pricing Schedule to the Code and clause 9 of the Code.

### 2.4.1 Economic conditions on the Railway

Freight services on the Tarcoola-Darwin Railway are operated solely by GWA<sup>22</sup> and are made up of bulk and non-bulk freight.<sup>23</sup> Previous analysis has found that, while bulk freight does not generally face competitive pressures from road transport,<sup>24</sup> due to the large weight and quantities involved, non-bulk containerised freight does.<sup>25</sup>

Total freight services on the Tarcoola-Darwin Railway have declined over the four years to 2018, with the volume of haulage in calendar year 2018 below the average over that four-year period (Table 1). The four-year decline follows a period of close to a decade in which the volume of freight gradually increased.

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<sup>22</sup> See Department of Infrastructure, Regional Development and Cities, 'Statistical report: Trainline 6', 2018, p. 79, available at: [https://bitre.gov.au/publications/2018/files/train\\_006.pdf](https://bitre.gov.au/publications/2018/files/train_006.pdf).

<sup>23</sup> See GWA, Submission on Review of Regulatory Guidelines, p. 7.

<sup>24</sup> In some instances road transport of bulk commodities can compete with rail transport. SACOME notes that some mine operators proximate to the Tarcoola-Darwin railway use the road network to transport product.

<sup>25</sup> See Commission, 'Tarcoola-Darwin Railway: Ten year revenue review', Final report, 2009, pp.16-20, available at: <http://bit.ly/TenYearRevenue-FinalReview2009>, and GWA, p. 7.

Table 1: Indicators of demand and utilisation on the Tarcoola-Darwin Railway<sup>26</sup>

	2006	2010	2014	2018
Annual freight (billion gtps)				
<i>Total</i>	2.7	6.1	5.8	4.6
<i>Sustainable</i>	2.6	2.9	3.6	3.2
<i>Non-sustainable</i>	0.1	3.2	2.3	1.4
Weekly intermodal services (no.) <sup>27</sup>	N/A	6	6	N/A
Average dwell time (%) <sup>28</sup>	N/A	15.5	11	N/A

Notwithstanding increases in base metal commodity prices,<sup>29</sup> the decline in haulage since 2014 reflects an overall fall in the volume of haulage of goods for which no sustainable competitive price exists,<sup>30</sup> likely in part due to some mine closures.<sup>31</sup> At the same time, the volume of haulage of goods where a sustainable competitive price exists has been less volatile. Alongside this, some indicators of railway utilisation have remained relatively low. For instance, data on average dwell times in 2017 – a partial indicator of utilisation (for example, higher dwell times can indicate more traffic and time spent in passing loops) – were lower on the Tarcoola-Darwin line compared with other freight routes on the east-west corridor.<sup>32</sup>

The outlook for haulage on the Tarcoola-Darwin Railway will likely depend on commodity prices and economic conditions in South Australia and the Northern Territory. Without stronger economic growth

<sup>26</sup> The years included in Table 1 are selected based on data availability. 2006 and 2010 are based on financial year data, while 2014 and 2018 are based on calendar year data. The annual sustainable and non-sustainable freight in Table 1 may not necessarily add to the total due to rounding.

<sup>27</sup> See Department of Infrastructure, Regional Development and Cities, 'Statistical report: Trainline 1', 2012, pp. 40-51, available at: [https://bitre.gov.au/publications/2012/files/trainL\\_001.pdf](https://bitre.gov.au/publications/2012/files/trainL_001.pdf); Department of Infrastructure, Regional Development and Cities, 'Statistical report: Trainline 2, 2014, p. 76, available at [https://bitre.gov.au/publications/2014/files/trainline\\_002.pdf](https://bitre.gov.au/publications/2014/files/trainline_002.pdf); and Department of Infrastructure, Regional Development and Cities, Trainline 6', p. 77. The number of weekly intermodal services was six in calendar year 2017.

<sup>28</sup> Calculated as a simple average across both directions. Data sourced from Department of Infrastructure, Regional Development and Cities, Trainline 1, p. 51; Department of Infrastructure, Regional Development and Cities, Trainline 2, p. 76; and Department of Infrastructure, Regional Development and Cities, Trainline 6, p. 77. The average dwell time in calendar year 2017 was around 14.5 per cent.

<sup>29</sup> See the Reserve Bank of Australia's Index of Commodity Prices – Base metals index, available at: <https://www.rba.gov.au/chart-pack/commodity-prices.html>.

<sup>30</sup> For reporting purposes, freight services are categorised by GWA into those where a sustainable competitive price exists and those where it does not.

<sup>31</sup> See MCA-NTD, Submission on the 2017 ESCOSA Review of Guidelines for the Access regime for the Tarcoola-Darwin Railway, pp. 14-15, for a list of some apparent mine closures in the Northern Territory between 2012 and 2016.

<sup>32</sup> Due to the distances involved, the most comparable freight route for which data are available is arguably the east-west corridor; see Commission, Ten-year revenue review, p. 20. Nonetheless, there can be limitations in comparing dwell times across rail corridors in Australia. For instance, dwell time can reflect loading and unloading at freight terminals and other operational activities such as refuelling. The measure may also be influenced by the number of passing loops on the line, which are less frequent on the Alice Springs to Darwin section of the Tarcoola-Darwin Railway. See GWA, Review of Regulatory Guidelines – Submission May 2019, pp. 23-24.

or higher commodity prices, the Tarcoola-Darwin Railway will likely continue to face strong competition from road transport and experience low utilisation on parts of the network.

## 2.4.2 Access pricing requirements

Access pricing requirements are set out in clause 9(1)(e) of the Code and in the schedule to the Code (which sets out the access pricing principles to be followed by the Arbitrator; **Pricing Schedule**).

Clause 9(1)(e) of the Code requires that an Access Provider must, on application from an Access Seeker, provide an Access Price for reference purposes in accordance with the guidelines developed and published by the regulator.

The Pricing Schedule sets out pricing principles to be used in arbitration, taking into account whether or not there is a sustainable competitive price. A short summary of those principles are set out below. These include the competitive imputation price methodology to be used when a sustainable competitive price exists and the approach to calculating the floor and ceiling prices when no sustainable competitive price exists. The process for determining prices in arbitration is shown in Attachment A of the Code.

### 2.4.2.1 Competitive imputation price

When there is a sustainable competitive price, an arbitrated Access Price is to be determined by the arbitrator in accordance with the competitive imputation methodology set out in Division 1 clause 1 of the Pricing Schedule, and is to be no less than the floor price and no higher than the ceiling price determined by the arbitrator.<sup>33</sup> The price under the competitive imputation methodology is calculated as the competitive rail-line haul price (maximum competitive price) minus the incremental cost of providing the freight service.

When there is no sustainable competitive price, an arbitrated Access Price is determined by the arbitrator, subject to both floor and ceiling prices calculated in accordance with the Pricing Schedule to the Code and any other matters as set out in clause 21 of the Code (which lists the general principles that the arbitrator must take into account in making an award).

### 2.4.2.2 Ceiling price

An important aspect of the guidance on ceiling price calculations is how the fixed costs of Railway Infrastructure are to be allocated.

When there is not a sustainable competitive price, the ceiling price is to be based on the concept of full economic cost (where total cost is apportioned among multiple access holders; refer Attachment A of the Code). The intent of full economic cost is to ensure that, when multiple access users are involved, the ceiling price recovers not only the directly incurred incremental cost of access but also an appropriate contribution by the Access Seeker towards the fixed costs of the Railway Infrastructure. The full economic cost ceiling pricing principle is also utilised by the Commission in the Access Information and Pricing Principles Guideline for the South Australian intrastate railway access regime, which has been concurrently reviewed by the Commission.<sup>34</sup>

On the other hand, when a sustainable competitive price is determined to exist, the ceiling price is based on the concept of total stand-alone cost (where the total cost attributable to the Railway Infrastructure is imposed on each access holder; refer Attachment A of the Code). The total stand-alone cost may not be a 'fair' ceiling price when multiple access users are involved, as it could lead to over recovery of total costs (as multiple users would pay for the same fixed costs) and may allow excessive profits to accrue to the Access Provider. However, in such a situation the competitive imputation

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<sup>33</sup> See Schedule to the Code: Access Pricing Principles, Division 1, clause 3(f).

<sup>34</sup> See Commission, 2019 Review of the South Australian Rail Access Regime Information Kit, p.10.

pricing rule assumes that competing forms of transport can be established to form the base-line competitive imputation price. Moreover, competing modes of transport may, in practice, prevent the Access Provider from facing the theoretical ceiling price based on total stand-alone cost.

### **2.4.2.3 Floor price**

The floor price for access to freight services on the Tarcoola-Darwin Railway is to be calculated the same way, no matter whether there is a sustainable competitive price or not.<sup>35</sup> That calculation is based on the avoidable costs of Below-Rail Services attributable to the usage of that required infrastructure.<sup>36</sup> The use of avoidable cost reflects the lowest price at which an Access Provider could charge an Access Seeker without incurring an economic loss from providing that particular service.

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<sup>35</sup> See Schedule to the Code: Access Pricing Principles, Division 1, clause 3.

<sup>36</sup> See Schedule to the Code: Access Pricing Principles, Division 1, clause 3, and Schedule to the Code: Access Pricing Principles, Division 2, clause 2.

## 3 Amendments to the Guidelines

The amendments outlined in the Final Decision are largely the same as those in the July 2019 Further Draft Decision. The amendments made as part of the review overall have aimed to improve readability and to more explicitly address certain requirements under the Code. The formatting of Guidelines 1, 2 and 3 has been updated.

### 3.1 Guideline 1: Access Provider Reference Pricing and Service Policies

Guideline 1 sets out the Commission's guidance on information requirements for an Access Provider and an Access Seeker in respect to Access Prices and track and service information (including train-path policy and service quality).

#### 3.1.1 Reference prices

The Commission has made no amendments to the Access Provider's information requirements for reference pricing purposes within Guideline 1. While some stakeholders were supportive of firm- or regulator-driven actions to increase information about Access Prices,<sup>37</sup> with one submission to the Further Draft Decision called for the mandating of reference pricing,<sup>38</sup> the Code does not provide the Commission with the power to require the publication of reference prices under the Guidelines.

In its submission to the April 2019 Draft Decision, the Access Provider (GWA) noted a demand-based approach to pricing on the Tarcoola-Darwin railway may be hindered by a requirement to publish reference prices, and the Commission acknowledged in the Further Draft Decision that a demand-based approach to pricing is permitted under the Code, insofar as prices do not generate excessive revenues (as calculated periodically by the regulator). A key question, however, is whether or not GWA's pricing approach is leading to monopoly rents and, if so, is greater pricing oversight required, to the extent permitted under the Code? In 2020, the Commission will commence a review of revenues earned for providing access to the Tarcoola-Darwin railway. Should excessive revenues be found as part of the revenue review, the Commission may consider remedial actions, including, but not limited to, the consideration of reference prices.

More generally, the Commission would encourage GWA to make Access Seekers aware of the demand-based approach to pricing used on the Tarcoola-Darwin railway. In its submission to the April 2019 Draft Decision, GWA noted that it would be willing to publish the broad pricing principles followed by the Below-Rail business. The Commission supports that initiative.

#### 3.1.2 Modification to general information to accompany a written request for access

The Commission has made a minor modification to section 2(d) of Guideline 1, which outlines the information an Access Seeker is to provide to an Access Provider as part of a written request for access. Section 2(d) of Guideline 1 previously required an Access Seeker to disclose:

*'the end market for required (freight or passenger) Services in terms of the range of end markets published for this purpose by the Access Provider.'*

<sup>37</sup> See MCA-NTD, Submission on the 2017 ESCOSA Review of Guidelines for the Access regime for the Tarcoola-Darwin Railway, pp. 5-6; SACOME, p. 1; and See Pacific National, 2019 Review of rail guidelines for Tarcoola-Darwin Railway and South Australian rail access regime information kit, p. 1.

<sup>38</sup> In its submission to the July 2019 Further Draft Decision Pacific National stated that: *the Code provides the power to (and accordingly should): Mandate the provision of indicative pricing information in the form of reference prices with methodologies and principles (Section 39, Schedule, Division 1 (2) (5)) [sic].* See Pacific National's submission to the Further Draft Decision, p.2, available at <https://www.escosa.sa.gov.au/ArticleDocuments/21411/20190910-Rail-ReviewRailGuidelines-Tarcoola-Darwin-FDDSubmission-PacificNational.pdf.aspx?Embed=Y>.



The Commission has clarified that the end market is intended to refer to the type of load being transported. It has amended Section 2(d) of Guideline 1 as follows:

*'the type of load (freight type or passenger) intended to be transported and the volume/weight of the load.'*

The amendment aims to improve clarity of the text and address potential confidentiality concerns of an Access Seeker who might interpret 'end market' to mean 'the Access Seeker's customer'.<sup>39</sup>

### 3.1.3 Retention of guidance on train-path and train-control policy and service quality

The Commission has retained and, where possible, clarified its guidance relating to train-path and train-control policy (including competition on the same train paths), and service quality. Much of the guidance is procedural in nature and its scope is more limited than in some other jurisdictions (such as the interstate network<sup>40</sup>).<sup>41</sup> GWA has noted that documents on train-path and train-control policy and service standards are provided to an Access Seeker as part of the information pack provided once an access application request has been received.<sup>42</sup>

A modification has been made to section 4.1.5 of Guideline 1, to prescribe a reasonable time limit in relation to train control procedures:

*'in the event of the Access Provider becoming aware of a railway failure or potential deviation from the Scheduled Train Path, the consultation protocols to apply in notifying all affected parties within a reasonable time.'*

In its submission to the Draft Decision in April, GWA supported the amendment to 4.1.5.<sup>43</sup>

### 3.1.4 Publication of maps and diagrams

In contrast to other jurisdictions, there are no formal requirements on the Access Provider to publish diagrams, maps or plans for the Tarcoola-Darwin Railway (Table 2). Some submissions at the initiation of the review noted a lack of transparency of information about the railway, including rail line diagrams, and suggested this could lower business confidence, reduce access and adversely impact investment in upstream markets (such as in the mining sector).<sup>44</sup>

Table 2: Requirements for publishing diagrams, maps or plans

Jurisdiction	Diagrams, maps or plans	Regulated frequency of publication
South Australia - Intrastate	On request for Information Brochure <sup>45</sup>	Must be kept up to date

<sup>39</sup> Pacific National noted some concern in regard to the confidentiality of access information; see Pacific National, 2019 Review of rail guidelines for Tarcoola-Darwin Railway and South Australian rail access regime information kit, pp. 9-10. However, clause 12A of the Code already sets out requirements for the protection of information.

<sup>40</sup> For more details see ACCC Final Decision, Australian Rail Track Corporation Access Undertaking – Interstate Rail Network, July 2008, available at: <https://www.accc.gov.au/system/files/ACCC%20final%20decision%20on%20the%20ARTC%20Interstate%20Rail%20Access%20undertaking.pdf>.

<sup>41</sup> Specifically, train-path policy includes requirements for a master train plan, reserved paths and competition for the same paths, while train-control policy sets out expectations that a statement of principles, rules and practices should be applied to the Access Provider's services.

<sup>42</sup> See GWA, Submission on Review of Regulatory Guidelines, pp. 8-9.

<sup>43</sup> See GWA, Review of Regulatory Guidelines – Submission May 2019, p. 17.

<sup>44</sup> See MCA-NTD, Submission on the 2017 ESCOSA Review of Guidelines for the Access regime for the Tarcoola-Darwin Railway, pp. 8-9.

<sup>45</sup> See Commission, Review of the South Australian Rail Access Regime Information Kit, April Draft Decision, pp. 6-7.

Jurisdiction	Diagrams, maps or plans	Regulated frequency of publication
South Australia – Tarcoola to Darwin	No requirements	N/A
Western Australia	Must be made available <sup>46</sup>	As often as necessary to be up to date but subject to audit at least every two years <sup>47</sup>
Queensland - 2016 Access Undertaking	Published on website (preliminary information, line diagrams <sup>48</sup> and capacity information)	Must be kept up to date
ARTC	On request and published on website <sup>49</sup>	Must be kept up to date

The Commission agrees that more information about rail line segments could reduce barriers to negotiation,<sup>50</sup> but acknowledges that the Access Seeker and Access Provider have commercial incentives to share this type of information, to the extent incentives are aligned. Indeed, GWA has published rail information and maps on its website.<sup>51</sup> For these reasons, the Commission will not require publication of maps and diagrams. In its submission to the April 2019 Draft Decision, the MCA-NT were encouraged by GWA's plans to publish rail information and maps and considered this may assist upstream users of rail infrastructure.<sup>52</sup>

### 3.2 Guideline 2: Arbitrator pricing requirements

The Commission has retained most existing principles and information for access to freight services in Guideline 2. In addition, the Commission has inserted a number of new amendments.

As noted earlier, the Code requires an arbitrator to determine Access Prices in the event that a dispute is referred by the Commission to arbitration. The Pricing Schedule of the Code outlines the methodology to calculate floor and ceiling prices. It also sets out a role for the Regulator to publish

<sup>46</sup> See Railway (Access) Code 2000 (WA), Schedule 2, clauses 2 and 4, available at: [https://www.legislation.wa.gov.au/legislation/prod/filestore.nsf/FileURL/mrdoc\\_28343.pdf/\\$FILE/Railways%20\(Access\)%20Code%202000%20-%20%5B01-f0-03%5D.pdf?OpenElement](https://www.legislation.wa.gov.au/legislation/prod/filestore.nsf/FileURL/mrdoc_28343.pdf/$FILE/Railways%20(Access)%20Code%202000%20-%20%5B01-f0-03%5D.pdf?OpenElement)

<sup>47</sup> See ERA, Final Determination on Brookfield Rail's Proposed Revised Train Management Guidelines, p. 13, available at: <https://www.erawa.com.au/cproot/10996/2/20121130%20-%20D99106%20-%20Rail%20-%20Brookfield%20Rail%20-%20Final%20Determination%20-%20Brookfield%20Rail%20Proposed%20Revised%20Train%20Management%20Guidelines.pdf>. This indicates that the train management guidelines (which include maps and diagrams) can be audited every two years.

<sup>48</sup> See QR Access Undertaking 1, clauses 1.2.3, 2.1.1 and Schedule A, available at: <https://www.queenslandrail.com.au/business/access/Access%20Undertaking%20and%20related%20documents/Queensland%20Rail%20Access%20Undertaking%201%202016.pdf>

<sup>49</sup> See ACCC, Final Decision, Australian Rail Track Corporation Access Undertaking – Interstate Rail Network, July 2008, p. 43, available at: <https://www.accc.gov.au/system/files/ACCC%20final%20decision%20on%20the%20ARTC%20Interstate%20Rail%20Access%20undertaking.pdf>.

<sup>50</sup> See Commission, Review of the South Australian Rail Access Regime Information Kit, p. 14.

<sup>51</sup> See GWA's [website](#).

<sup>52</sup> See MCA-NTD, Submission on review of rail guidelines for the Tarcoola-Darwin Railway – Draft Decision, p. 8.

Guidelines about information (such as costs, assets and rates of return) that would serve as an input to the arbitrator's calculations.<sup>53</sup>

Alongside general information about the methodologies for floor and ceiling prices, Guideline No 2 outlines guidance on:

- ▶ a procedure for calculating and valuing the capital asset base
- ▶ a timeframe for which costs be considered avoided
- ▶ the calculation of incremental cost when there is a sustainable competitive price, and
- ▶ the financial market data to be considered in the calculation of a return on assets.

### 3.2.1 Capital assets

#### 3.2.1.1 Roll forward method

While there are various known ways of valuing assets, each with disadvantages and advantages, the requirement to use a Depreciated Optimised Replacement Cost (**DORC**) to value the assets on which the Access Provider can earn a return is set out in the Code.<sup>54</sup> A DORC valuation was undertaken around the date of commencement of the railway.

The Code, however, does not set out the procedure for rolling forward the value of the assets. In 2008, the Commission updated Guideline 2 to include both the value of the Railway as at the date of commencement of operations, together with a procedure (in line with industry practice) for updating the value of private capital invested<sup>55</sup> over time.<sup>56</sup>

An alternative to using a roll forward mechanism would be to conduct periodic DORC revaluations of the asset base. A view was put forward in a submission to the 2008 Review<sup>57</sup> supporting periodic DORC revaluations, on the basis that there are risks of inaccuracy in any initial DORC valuation, which would accrue and be magnified in a roll forward mechanism. However, the Commission notes that conducting periodic DORC revaluations is costly and could have practical consequences for future investment decisions, as a DORC valuation may write down (or increase) the value of assets depending on the level of utilisation in the period assessed. Such a variation would risk contravention of the Code, where a reasonable risk-adjusted return on the capital invested in the Tarcoola-Darwin Railway must not be prevented.<sup>58</sup> The Commission has, therefore, retained guidance to roll forward the initial DORC valuation, as opposed to requiring periodic revaluations. Also, the Commission has updated Guideline 2 to specify the application of a straight-line depreciation method to the relevant assets.<sup>59</sup>

#### 3.2.1.2 Government contributions

In addition, submissions to the April 2019 Draft Decision have noted concern regarding the high valuation of the capital assets of the Tarcoola-Darwin railway relative to the value paid for the assets by

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<sup>53</sup> See Schedule to the Code: Access Pricing Principles, Division 1, clause 6(f), (7)(a) and (7)(b)), Schedule to the Code: Access Pricing Principles, Division 2, clause 2(d)(iii), (6), (7), (8) and Schedule to the Code: Access Pricing Principles, Division 3, clauses (3), (4), (5) of the Code.

<sup>54</sup> See Schedule to the Code: Access Pricing Principles, Division 1, clause 2(7)(a).

<sup>55</sup> The value of private capital invested is the component of the DORC valuation that is net of government contributed assets and other government financial assistance.

<sup>56</sup> See Commission (2004), 'AustralAsia Railway (Third Party Access) Code: Guideline Review', p.10, available at <http://bit.ly/ThirdPartyAccessGuidelineReview-Final>.

<sup>57</sup> See ARTC submission to 2008 Guideline Review, p. 3, available at: <https://www.escosa.sa.gov.au/ArticleDocuments/718/071220-AustralasiaRailwayCodeGuidelineRev.pdf.aspx?Embed=Y>.

<sup>58</sup> See Schedule to the Code: Access Pricing Principles, Division 1, clause 2(8)(a).

<sup>59</sup> Those proposals are in Section 2.3.2(b) and 5.1.4 of Guideline 2. In its submission to the April 2019 Draft Decision, GWA accepted this method of depreciation; see GWA, Review of Regulatory Guidelines – Submission May 2019, p. 22.

the Access provider.<sup>60</sup> Pacific National considered that government-contributed assets should be excluded for pricing purposes.<sup>61</sup>

Government-contributed assets and financial assistance can be deducted from the DORC,<sup>62</sup> provided a reasonable risk-adjusted return is not prevented on invested capital.<sup>63</sup> The previous Guidelines removed government-contributed assets and financial assistance for the purposes of providing guidance to an arbitrated price,<sup>64</sup> but did not remove it for ceiling price purposes,<sup>65</sup> as this is a theoretical upper bound – not a guidance on an arbitrated price. The Commission has retained this approach as it is consistent with the Code.<sup>66</sup>

### 3.2.2 Timeframe for avoided costs

The Commission has retained the existing guidance defining the timeframe of avoided costs.<sup>67</sup> The timeframe for which operating and capital costs are to be assessed for floor and ceiling price purposes should be no greater than the proposed term of the Access Contract. Providing any more prescriptive guidance on timeframes is unlikely to be appropriate, as access on the Railway tends to be infrequent and specific to the needs of an Access Seeker.

### 3.2.3 Calculation of incremental cost

The Commission has clarified guidance on the calculation of Above-Rail incremental cost. This is relevant when there is a sustainable competitive price and the Access Price is to be determined by the arbitrator calculated in accordance with the competitive imputation methodology.<sup>68</sup>

The Pricing Schedule of the Code sets out that the incremental cost are costs the service provider would avoid if it did not provide the freight service, including avoided operating costs, administrative costs and an appropriate allowance for capital cost. In the event that Above-Rail assets exist, the Commission's guidance is that the arbitrator must consider actual Above-Rail costs and indicators of benchmark efficient costs in determining the Above-Rail incremental cost. The Commission has amended Section 4.1.1 of Guideline 2: 'Where the relevant Above-Rail assets do exist, the arbitrator should take into consideration the Above-Rail Operator's costs for the same or similar Services and appropriate benchmark efficient Above-Rail costs for the Services in question'. Stakeholders did not raise any concern with the amendment.<sup>69</sup>

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<sup>60</sup> See Pacific National, 2019 Review of rail guidelines for Tarcoola-Darwin Railway and South Australian rail access regime information kit, pp. 5-6, and MCA-NTD, Submission on review of rail guidelines for the Tarcoola-Darwin Railway – Draft Decision, p. 8.

<sup>61</sup> See Pacific National, 2019 Review of rail guidelines for Tarcoola-Darwin Railway and South Australian rail access regime information kit, pp. 5-6.

<sup>62</sup> See Schedule to the Code: Access Pricing Principles, Division 1, clause 2(8).

<sup>63</sup> See Schedule to the Code: Access Pricing Principles, Division 1, clause 2(8)(b).

<sup>64</sup> See Guideline 2, clause 5.

<sup>65</sup> See Guideline 2, clause 2.

<sup>66</sup> In its submission to the 2019 Draft Decision, GWA suggested that the Commission include the following sentence in the Guideline: 'The Guideline removes government-contributed assets and financial assistance for the purposes of providing guidance to an arbitrated price, but does not remove it for ceiling price purposes, as this is a theoretical upper bound – not a guidance on an arbitrated price'; see GWA, Review of Regulatory Guidelines – Submission May 2019, p. 22. However, the Commission has chosen to leave explanations of intent (such as the one proposed by GWA) for inclusion in the Decision Document rather than the Guideline.

<sup>67</sup> According to the Schedule to the Code: Access Pricing Principles, the Regulator's Guidelines must '*...provide guidance on the timeframes within which the Regulator considers costs could be avoided*'. See Division 1, clause (7)(b); Schedule to the Code: Access Pricing Principles, Division 2, clause (7)(b); and, Division 3, clause (4)(b).

<sup>68</sup> The competitive imputation methodology is set out in Division 1 clause 6 of the Schedule to the Code: Access Pricing Principles.

<sup>69</sup> See GWA, Re: Further Draft Decision – Review of Guidelines – Tarcoola to Darwin line.

Where Above-Rail assets do not exist, Guideline 2 currently sets out that the acquisition costs of the relevant assets are to be based on the leasing market or similar agreement for assets of a similar quality. The Commission has retained this guidance.

### 3.2.4 Guidance on regulated rate of return

The Pricing Schedule of the Code provides that the Guidelines must have regard to the calculation of the nominal rate of return, risk premiums measured at the time of construction, development and operation of the Tarcoola-Darwin Railway and financial market indicators (including measures of expected inflation and risk-free rates).<sup>70</sup>

The Commission has retained guidance on the rate of return information outlined in Guideline 2, but clarified aspects of the Guideline by using clearer language and adding new requirements to more explicitly address certain requirements under the Code.

#### 3.2.4.1 In relation to floor prices

The Commission has included guidance in Section 3 of Guideline 2 stating that: *'Any return on assets required for the purposes of determining a Floor Price should be calculated as set out in Section 6'*. While section 6 of Guideline 2 may be interpreted as relating to Floor Price calculations, the additional guidance in section 3 of that Guideline is intended to avoid any doubt.

In addition, the Commission has modified Section 6.1.3 in two ways.

First, it has introduced guidance for the arbitrator on the appropriate risk premium to be applied for Floor Price calculations relating to any extension or expansion of the railway. The previous Guideline was silent on that matter. The guidance is consistent with the requirements of Clause 2.7(c)(i)(B) of the Pricing Schedule.

Second, it has clarified that, for the setting of Floor Prices, the principles set out in Clause 3 of the Pricing Schedule apply, whether or not there is a sustainable competitive price.

Those amendments are set out below.

*'in the event of any expansions or extensions to the railway, the (post-tax) real-terms risk premium to be applied for Floor Price setting purposes should be the prevailing rate at the date of commencement of construction of that expansion or extension.'*

*'other than extensions or expansions to the railway, for Floor Price setting purposes ~~for the purposes of setting a price between the floor and ceiling limits where there is no sustainable competitive price,~~ the (post-tax) real-terms risk premium ('m') applied to project funds should ~~not fall below~~ be 7.0 percent ~~unless~~. However, if the Arbitrator considers that the returns being achieved under non-arbitrated outcomes or under arbitrations applying competitive imputation reflect the full range of returns implied by the pre-regulation probability distribution of expected returns, ~~in which case~~ the Arbitrator could choose to use a premium value as low as 4.7 percent.'*

Stakeholders did not raise any concern with the amendments.<sup>71</sup>

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<sup>70</sup> See Schedule to the Code: Access Pricing Principles, Division 3, clause 4.

<sup>71</sup> See GWA, Re: Further Draft Decision – Review of Guidelines – Tarcoola to Darwin line, and Pacific National, Further Draft Decision on Review of Rail Guidelines for the Tarcoola-Darwin railway.

### 3.2.4.2 Retain right to re-determine post-tax real risk premium

The Commission has updated Section 6.1.5 to reflect the proposed changes to 6.1.3 and to make the language clearer (by removing the ambiguity of the term ‘significant developments occurring’). The changes are presented below.

*‘The Commission also reserves the right to re-determine the values of the ~~two~~ forms of the real-terms risk premium (‘m’) if ~~significant developments occurring~~, after operations commence on the New Railway, the corporate tax rate and/or the market risk premium vary significantly from the following values observed at the time of financial closure, ~~namely~~: (a) corporate tax rate = 30 percent; and (b) the market risk premium = 6.0 percent.’*

Also, the Commission has updated Section 6.1.4 to reflect changes to 6.1.3 and to make the language clearer.

*‘The Commission reserves the right to re-determine the values ~~of the two forms~~ of the real-terms risk premium (m) if the DORC value of the Railway Infrastructure Assets varies significantly from values underlying the values stated above, in accordance with all relevant requirements of the Guideline and the Code’.*

Stakeholders did not raise any concern with these amendments.<sup>72</sup>

### 3.2.4.3 Parameter choice

The Commission has amended Guideline 2 in relation to expected inflation. The changes are presented below.

*‘p = the expected inflation rate (calculated as a fraction) during the course of the period in question.*

*When the Arbitrator is considering values for ‘p’, the Arbitrator:*

- (a) consistent with the Code, must have regard to financial market-based measures (including but not limited to the average differential between yields expected on indexed and nominal bonds of a similar maturity over the 40 days immediately prior to the start of the period; calculated using the Fisher equation); and*
- (b) may also have regard to other factors such as the geometric average of the estimates of inflation over a ten-year horizon, calculated using the Reserve Bank of Australia’s forecast for inflation one-year ahead and assuming inflation expectations of 2.5 per cent thereafter.’*

The change is to make it clearer that, while the Code requires the Commission to prepare a Guideline which requires the arbitrator to have regard to financial market-based measures of expected inflation (including but not limited to measures derived from the bond market<sup>73</sup>), the arbitrator may also have regard to other relevant factors. Those other factors, such as the credibility of the Reserve Bank of Australia’s inflation targeting framework, which currently underpin some regulators’ approaches to estimating long-term inflation expectations (including the Commission’s current approach<sup>74</sup>), may be a

<sup>72</sup> See GWA, Re: Further Draft Decision – Review of Guidelines – Tarcoola to Darwin line, and Pacific National, Further Draft Decision on Review of Rail Guidelines for the Tarcoola-Darwin railway.

<sup>73</sup> In addition to the bond break-even approach, some alternative market-based measures of inflation expectations are available, such as in financial products known as inflation swaps; see Commission (2019), ‘Guidance paper 6 – Treatment of inflation in the regulatory rate of return’, available at: <https://www.escosa.sa.gov.au/ArticleDocuments/11293/20190606-SAWRD20-GuidancePaper6-InflationForecastingMethodology.pdf.aspx?Embed=Y>.

<sup>74</sup> See Commission, Guidance paper 6 – Treatment of inflation in the regulatory rate of return.

relevant consideration for the arbitrator. Stakeholders did not raise any concern with these amendments.<sup>75</sup>

### 3.3 Guideline 3: Regulatory information requirements

#### 3.3.1 Ring fencing

The Commission has retained the existing guidance on reporting and account separation applying to the Tarcoola-Darwin Railway.

In its submission to the July 2019 Further Draft Decision, Pacific National<sup>76</sup> stated that:

*“the Code provides the Commission with the power to (and accordingly should):*

- *Mandate the provision of indicative pricing information in the form of reference prices with methodologies and principles (Section 39, Schedule, Division 1 (2) (5)).*
- *Include a ‘most favoured nation’ clause to ensure non-discrimination between GWA’s related party above-rail provider and its below-rail network compared to the prices offered to other above-rail providers (Section 39).*
- *Request information on whether GWA received access proposals and offered access pricing on a non-discriminatory basis (Section 10(4), Section 46 (2)(c), Schedule, Division 1 (2) (5)).*
- *Require separate regulatory accounts for its above and below rail businesses and to publish this information (Section 46).*
- *Conduct a compliance review of the ring fencing and confidentiality provisions and non-discrimination requirements; to our knowledge there has been no Commission compliance review undertaken on ring-fencing compliance.”*

The actions suggested by Pacific National are activities aimed in various ways to protect against the Access Provider discriminating in favour of its Above-Rail business. The Commission has an ongoing role in monitoring and verifying conformance to the requirements of the Code including as it relates to ring-fencing and the protection of confidential information. The Code provides the Commission with powers to obtain and verify information and the Commission intends to conduct a compliance audit in parallel with its upcoming review of revenues. Should breaches of the Code be identified, the Commission will consider appropriate remedial actions, including, but not limited to, future adjustments to the Guidelines and consideration of reference prices.

In response to the points raised by Pacific National, the Commission notes the following:

#### *Provision of indicative pricing information in the form of reference prices*

As noted in section 2.1.1, the Code does not provide the Commission with the power to require the publication of reference prices under the Guidelines. However, the Commission has the power to collect pricing information under Clause 39 of the Code and, as noted above, intends to undertake a compliance audit. As part of the audit, information regarding access pricing will be considered.

#### *Requiring a “most favoured nation” provision*

Pacific National does not provide the exact detail for a proposed most favoured nation clause. The Commission interprets the recommendation to mean that an offer made to an Access Seeker will be as good as the best offer made to any Access Seeker under the same circumstances. However, this

<sup>75</sup> See GWA, Re: Further Draft Decision – Review of Guidelines – Tarcoola to Darwin line, and Pacific National, Further Draft Decision on Review of Rail Guidelines for the Tarcoola-Darwin railway.

<sup>76</sup> See Pacific National, Further Draft Decision on Review of Rail Guidelines for the Tarcoola-Darwin railway, p 2.

would, in effect, lead to prices being set and therefore inconsistent with the flexibility provided in the Code for parties to negotiate prices.

#### *Regulatory accounts*

In relation to Pacific National's comments on the keeping and publishing of separate accounts, clause 46 of the Code provides for the keeping of separate accounts between above and below rail businesses. However, that clause does not require GWA to publish the accounts nor does it provide the Commission with the power to require their publication. Nonetheless, as part of the audit noted above, GWA's account separation practices will be audited.

#### *Ring-fencing and compliance audits*

Submissions to the initiation of the project raised concerns that section 2 of Guideline 3 was not sufficiently prescriptive in relation to the derivation of the Access Provider's regulatory accounts for Above-Rail Services, as distinct from those for Below-Rail Services.<sup>77</sup> At the centre of this concern was the potential for cost shifting between Above- and Below-Rail Services by a vertically-integrated Access Provider, such that internal cost allocations may not necessarily reflect an accurate account of costs.<sup>78</sup> Submissions to the April 2019 Draft Decision<sup>79</sup> and July 2019 Further Draft Decision raised similar concerns.

The Commission has the power to audit the separation of accounts. Clause 46 of the Code requires the Access Provider to give a true and fair view of the Below-Rail business as distinct from other business components (including Above-Rail Services). Guideline 3 currently requires that, if costs cannot be directly attributable to a specifically prescribed business, they are to be attributable on a causal basis. If that is not possible, they may be allocated on a non-causal basis, accompanied by supporting documentation. Although this requirement, coupled with no evidence of misallocation found in KPMG's review of GWA's financial allocations in 2015,<sup>80</sup> led the Commission to conclude the existing requirements were effective, the Commission considers it prudent to reassess this matter as part of the compliance audit noted earlier.

### **3.3.2 Minor modifications and clarifications**

The Commission has amended Guideline 3 with minor updates and clarifications to improve readability.

In its submission to the April 2019 Draft Decision, GWA proposed changing reporting dates to be in calendar years to match the calendar year financial reporting cycle of its US-based parent company.<sup>81</sup> Consequently, the Draft Guideline Review had recommended a change so that reporting periods were in respect of calendar years rather than financial years (other than for the purposes of the revenue review, where financial year reporting is mandated by Clause 50(10) of the Code). However, it has since been announced that Genesee and Wyoming Inc has been sold to Brookfield Rail and that, due to a conflict of interest with Brookfield's existing Australian assets, the Australian assets of GWA would be sold to a third party. Since the publication of the Further Draft Decision, it has been announced that GWA's Australian assets will be acquired by Macquarie Infrastructure and Real Assets (MIRA) and PGGM, a

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<sup>77</sup> See Pacific National, Submission to the Review of Rail Guidelines, February 2017, pp. 4-6.

<sup>78</sup> See Pacific National, Submission to the Review of Rail Guidelines, February 2017, pp. 4-6.

<sup>79</sup> See Pacific National, 2019 Review of rail guidelines for Tarcoola-Darwin Railway and South Australian rail access regime information kit, pp. 9-10, and MCA-NTD, Submission on review of rail guidelines for the Tarcoola-Darwin Railway – Draft Decision, p. 9.

<sup>80</sup> See KPMG, Review of GWA financial allocations.

<sup>81</sup> See GWA, Submission on Review of Regulatory Guidelines, p. 9 and GWA, Review of Regulatory Guidelines – Submission May 2019, p. 23.



Dutch pension fund manager.<sup>82</sup> These companies acquired a minority shareholding (49 percent) in GWA's Australian assets in 2016.

Based on GWA's new ownership, it is unlikely that a change to calendar year reporting will be required. The Commission has, therefore, maintained the position held in the previously published Guideline 3; that is, for reporting in respect of financial years rather than to adopt the change to calendar years. If required, an exemption to the relevant provision in the Guideline could be negotiated on a case-by-case basis along the lines of the exemption that applied to GWA under US ownership.

There has also been a change to the procedure regarding compliance of regulatory accounts, such that, in the event that the Access Provider does not have an External Director<sup>83</sup>, the statement of compliance may be signed by an External Director of a related entity of the Access Provider.<sup>84</sup>

Other minor amendments include, clarifying terminology and definitions (relating to train procedures and service quality standards in Guideline 1<sup>85,86</sup>), adding greater specificity (relating to calculating CPI inflation in Guideline 2<sup>87</sup>) and removing information that is redundant.<sup>88</sup>

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<sup>82</sup> See GWA's public notice on ownership at [https://www.gwrr.com/railroads/australia/genesee\\_wyoming\\_australia/gwa-mira-announcement](https://www.gwrr.com/railroads/australia/genesee_wyoming_australia/gwa-mira-announcement)

<sup>83</sup> Since the 2019 April Draft Decision, the term 'Non-Executive Director' has been replaced with 'External Director', as the latter is defined in the Corporations Act 2001.

<sup>84</sup> The change may add flexibility; see GWA, Submission on Review of Regulatory Guidelines, p. 9.

<sup>85</sup> In its submission to the April 2019 Draft Decision, GWA proposed minor amendments to make the language in Guideline 1 clearer; see GWA, Review of Regulatory Guidelines – Submission May 2019, pp. 16-20. The proposed suggestions for several sections (3.1.2, 3.2.2, 3.2.3, 3.3.7, 3.3.8, 3.3.9, 3.3.11, 4.1.2, 5.1.2, 5.1.4 and 5.1.5) have been included by the Commission.

<sup>86</sup> There were some minor amendments proposed by the Commission in its April 2019 Draft Decision that were intended to clarify that the Access Provider has an obligation to develop and maintain train control procedures and service quality standards (including in Section 4.1.1 and 5.1.1 of Guideline 1). In its submission to the April 2019 Draft Decision, GWA did not object to those proposals.

<sup>87</sup> The addition of CPI is proposed for Sections 5.1.5 and 2.3.2(d). In its submission to the 2019 Draft Decision, GWA supported the inclusion.

<sup>88</sup> Such as references in current Guideline 3 to cost information and information procedures that have already passed.

## Appendix A: Tarcoola-Darwin Railway

The Tarcoola-Darwin Railway operates from (a point near) Tarcoola to its end in Darwin at the Port of Darwin. It is operated by Genesee and Wyoming Australia (North) Pty Ltd, under a 50-year concession right granted under the AustralAsia Railway Project Concession Deed. The Concession Deed is due to expire in 2054, when the right to operate the Railway reverts to the AustralAsia Railway Corporation, which consists of representatives from both the Northern Territory and South Australian Governments.<sup>89</sup>

The Tarcoola-Darwin Railway comprises both an older section of line between Tarcoola and Alice Springs and the more recently constructed section of line between Alice Springs and Darwin – all standard gauge.

The Commission was appointed as the Regulator under the Code upon its commencement in 2004. The AustralAsia Railway Access Regime was certified by the Commonwealth Treasurer in 2000 as an effective state-based access regime until 31 December 2030.<sup>90</sup>

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<sup>89</sup> See Commission, Ten-year review of revenues, p. 7.

<sup>90</sup> See National Competition Council, AustralAsia Railway Access Regime; Final Recommendation, February 2000, available at <http://ncc.gov.au/images/uploads/CERaNtRe-001.pdf>.



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