



Review of rail guidelines for the Tarcoola-Darwin Railway

FURTHER DRAFT DECISION

July 2019

Request for submissions

The Essential Services Commission (**Commission**) invites written submissions on this paper. Written comments should be provided by **Friday, 30 August 2019**.

It is the Commission's policy to make all submissions publicly available via its website (www.escosa.sa.gov.au), except where a submission either wholly or partly contains confidential or commercially sensitive information provided on a confidential basis and appropriate prior notice has been given.

The Commission may also exercise its discretion not to publish any submission based on length or content (for example containing material that is defamatory, offensive or in breach of any law).

Responses to this paper should be directed to: **2019 Review of rail guidelines for Tarcoola-Darwin Railway**

It is preferred that submissions are sent electronically to: escosa@escosa.sa.gov.au

Alternatively, submissions can be sent to:
Essential Services Commission
GPO Box 2605
ADELAIDE SA 5001

Telephone: (08) 8463 4444
Freecall: 1800 633 592 (SA and mobiles only)
E-mail: escosa@escosa.sa.gov.au
Website: www.escosa.sa.gov.au

Contact Officer: Mark Caputo, Manager Economics

Table of contents

- Glossary of terms iii
- 1 Executive summary..... 1
 - 1.1 Background..... 1
 - 1.2 Draft findings and amendments to the Guidelines..... 1
 - 1.3 Next steps 3
- 2 The review 4
 - 2.1 Purpose of Guidelines and review 4
 - 2.1.1 Guideline 1 4
 - 2.1.2 Guideline 2..... 4
 - 2.1.3 Guideline 3..... 5
 - 2.1.4 Guideline 4..... 5
 - 2.1.5 The review 5
 - 2.2 Scope of review..... 5
 - 2.3 Process of review 6
 - 2.4 Context for review 7
 - 2.4.1 Economic conditions on the Railway..... 8
 - 2.4.2 Access pricing requirements 9
- 3 Draft amendments to the Guidelines 11
 - 3.1 Guideline 1: Access Provider Reference Pricing and Service Policies 11
 - 3.1.1 Price transparency and reference prices 11
 - 3.1.2 Modification to general information to accompany a written request for access 12
 - 3.1.3 Retention of guidance on train-path and train-control policy and service quality 13
 - 3.1.4 Publication of maps and diagrams 13
 - 3.2 Guideline 2: Arbitrator pricing requirements 14
 - 3.2.1 Capital assets 15
 - 3.2.2 Timeframe for avoided costs 16
 - 3.2.3 Calculation of incremental cost 16
 - 3.2.4 Guidance on regulated rate of return 17
 - 3.3 Guideline 3: Regulatory information requirements 19
 - 3.3.1 Ring fencing 19
 - 3.3.2 Minor modifications and clarifications 19
- 4 Appendix A: Tarcoola-Darwin Railway..... 21
- 5 Appendix B: Selected legislation and process for determining arbitrated access prices 22
 - 5.1 Clause 9(1) of the Code 22
 - 5.2 Clause 45A of the Code 22
 - 5.3 Process for determining the arbitrated Access Price 23

6 Next steps 24

Glossary of terms

Above-Rail	Rolling stock such as locomotives, carriages and wagons
Above-Rail Operator	Means an operator of Above-Rail infrastructure in accordance with an Access Contract
Act	AustralAsia Railway (Third Party Access) Act 1999
Access Contract	A contractual agreement between an Above-Rail Operator and the Access Provider regarding Access to the Tarcoola-Darwin Railway
Access Price	The price of third party access to Railway Infrastructure , provided by the Access Provider
Access Provider	A party providing, or able to provide, Services for Railway Infrastructure – sometimes referred to as a Below-Rail operator
Access Regime	The regime to allow Third Party Operators access to Railway Infrastructure on the Tarcoola-Darwin Railway , under the Code
Access Seeker	An Above-Rail Operator seeking access to the Services provided by the Railway
Affiliated Operator	The Above-Rail Operator that is a related party to the Access Provider
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 Third Party Operators to the Tarcoola-Darwin Railway
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 Inc., the provider of Railway Infrastructure , as well as a provider of Above-Rail services
GWAN	Genesee & Wyoming Australia (North) Pty Ltd, a wholly owned subsidiary of GWA
MCA-NTD	Minerals Council of Australia (Northern Territory Division)
Pacific National	Pacific National Pty Limited

Pricing Schedule	The Schedule to the Code 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 Above-Rail Operator using the Railway , which provides freight or passenger Services including work Trains
Tarcoola-Darwin Railway	The railway to which the Code 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	Above-Rail operators who are not related to or affiliated with the Access Provider
Vertical Integration	Where the owner of the Railway Infrastructure is also a provider of Above-Rail operations

1 Executive summary

The Essential Services Commission (**Commission**) is reviewing 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). It released a Draft Decision on the review in April 2019 and has released this further Draft Decision, in which the Commission proposes a number of new amendments for consultation. The Commission has identified the proposed amendments following consultation on the April 2019 Draft Decision and has released this further Draft Decision to provide stakeholders with the opportunity to comment on those proposals. The proposed new amendments clarify aspects of the Guidelines, to more explicitly address certain requirements under the Code.

The intent of the review is 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 is 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 further Draft Decision has been informed by submissions made to the Commission during the course of the review, including submissions to the April 2019 Draft Decision. The Commission consulted with stakeholders both at the initiation stage of the project in late 2016 and early 2017 and on the April 2019 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 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 later in 2019.

1.2 Draft findings and amendments to the Guidelines

The draft findings outlined in this Further Draft Decision are, for the most part, the same as those in the April 2019 Draft Decision. This Further Draft Decision discusses the Commission's consideration of submissions received in May and, importantly, puts forward some new proposed amendments to the Guidelines. The new amendments aim to better meet the Commission's obligations under the Code.

The main new proposed amendments are in Guideline 2, as explained below.

- Section 3.6 contains an additional requirement: 'Any return on assets required for the purposes of determining a Floor Price should be calculated as set out in section 6'. This is implied, but not explicit, in the current Guideline.
- Section 4.1.1 contains an additional requirement: 'Where the relevant Above-Rail assets do exist, the arbitrator must take into consideration the Above-Rail Operator's costs for the same or similar Service and any appropriate benchmark efficient Above-Rail costs for the Service in question'. The current Guideline is silent on the calculation of Above-Rail costs where there is a sustainable competitive price and where Above-Rail assets exist.
- A new Section 6.1.2 has been added: '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.' This 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), the arbitrator may also have regard to other relevant factors.
- Section 6.1.2(b) has been changed to 6.1.3(b) and contains an additional requirement: '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'. The current Guideline is silent on the calculation of the risk premium in the event of any extension to the railway.
- Section 6.1.2(b) has been changed to 6.1.3(c) and has a modification: 'other than extensions or expansions to the railway, for Floor Price setting purposes ~~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~~ the Arbitrator could choose to use a premium value as low as 4.7 percent.' This change is to make it clearer that, for the setting of floor price purposes, the same principles as set out in Clause 3 of the Pricing Schedule apply irrespective of whether there is a sustainable competitive price or not.
- Section 6.1.5 has a modification: '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.' This change is to make the language clearer and to be consistent with the changes in Section 6.1.2.

In addition, the Commission proposes no major amendments to the Access Provider's information requirements for reference pricing purposes within Guideline 1.

1.3 Next steps

The Commission invites written submissions on all aspects of this further Draft Decision by 30 August 2019. To facilitate the provision of submissions or address any queries, the Commission would be pleased to meet with stakeholders for a briefing upon request. The Commission intends to release a Final Decision with Final Guidelines in October 2019.

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**).¹ The Code sets out a negotiate-arbitrate framework for access to specified infrastructure services provided by the operator of the **Tarcoola-Darwin Railway**.² 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. Those Guidelines are:

- ▶ Guideline 1 – Access Provider Reference Pricing and Service Policies³
- ▶ Guideline 2 – Arbitrator Pricing Requirements⁴
- ▶ Guideline 3 – Regulatory Information Requirements,⁵ and
- ▶ Guideline 4 – Compliance Systems and Reporting.⁶

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.⁷

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

² See Appendix A for a short summary of the Tarcoola-Darwin Railway.

³ See current version of Guideline 1, available at: https://www.escosa.sa.gov.au/ArticleDocuments/231/040213-Tarcoola-DarwinRailGuidelineNo_1-AccessProviderReferencePricing_ServicePolicies.pdf.aspx?Embed=Y.

⁴ See current version of Guideline 2, available at: https://www.escosa.sa.gov.au/ArticleDocuments/231/080818-Tarcoola-DarwinRailGuidelineNo_2-ArbitratorPricingRequirements.pdf.aspx?Embed=Y.

⁵ See current version of Guideline 3, available at: https://www.escosa.sa.gov.au/ArticleDocuments/231/040607-Tarcoola-DarwinRailGuidelineNo_3-RegulatoryInformationRequirements.pdf.aspx?Embed=Y.

⁶ See current version of Guideline 4, available at: https://www.escosa.sa.gov.au/ArticleDocuments/231/050428-Tarcoola-DarwinRailGuidelineNo_4-ComplianceSystems_Reporting.pdf.aspx?Embed=Y.

⁷ 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 (Section 5.2 of Appendix B). The purpose of the review was that the Guidelines issued by the Commission 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 2008.⁸

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.⁹ 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.¹⁰

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.

⁸ See Commission, 'AustralAsia Railway (Third Party Access) Code: Guideline Review', Final Decision, 2008, pp.1-30, available at: <http://bit.ly/ThirdPartyAccessGuidelineReview-Final>.

⁹ 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>.

¹⁰ 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.

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 later in 2019; this will allow for greater alignment of compliance requirements across industries regulated by the Commission in South Australia.¹¹

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.¹² 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 (see section 5.2 of Appendix B).

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.¹³

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

¹¹ The same approach for compliance guidelines was taken in the 2019 Review of the South Australian Rail Access Regime Information Kit.

¹² See Clause 50(1) and (2) of the Code.

¹³ 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 line¹⁴

- ▶ Pacific National Pty Limited (**Pacific National**), a rail freight company operating Above-Rail Services in parts of Australia,¹⁵ and
- ▶ the Minerals Council of Australia – Northern Territory Division (**MCA-NTD**), an industry association that represents resources companies in the Northern Territory.¹⁶

Following release of the Draft Decision in April 2019, the Commission received further submissions from GWA¹⁷, Pacific National,¹⁸ MCA-NTD,¹⁹ as well as submissions from:

- ▶ the ARTC, a Commonwealth Government-owned corporation that manages the majority of Australia's interstate rail network,²⁰ and
- ▶ the South Australian Chamber of Mines and Energy (**SACOME**), which is the representative body for the minerals and energy industry in South Australia.²¹

The issues raised in submissions were carefully considered by the Commission in making this further Draft Decision. Where relevant, certain arguments and submissions have been mentioned in the text of this further Draft 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.

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.

¹⁴ See GWA, 'Submission on Review of Regulatory Guidelines', 24 February 2017, available at: <http://bit.ly/RailGuidelinesSubmission-GWA>.

¹⁵ See Pacific National, Submission to the Review of Rail Guidelines, February 2017, p. 3, available at: <http://bit.ly/RailGuidelinesSubmission-PacificNational>.

¹⁶ See MCA-NTD, Submission on the 2017 ESCOSA Review of Guidelines for the Access regime for the Tarcoola-Darwin Railway, p.13.

¹⁷ 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>.

¹⁸ 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>.

¹⁹ 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>.

²⁰ 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>.

²¹ See South Australian Chamber of Mines and Energy (SACOME) (2019), 'ECOSA 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>.

2.4.1 Economic conditions on the Railway

Freight services on the Tarcoola-Darwin Railway are operated solely by GWA²² and are made up of bulk and non-bulk freight.²³ Previous analysis has found that, while bulk freight does not generally face competitive pressures from road transport,²⁴ due to the large weight and quantities involved, non-bulk containerised freight does.²⁵

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.

Table 1: Indicators of demand and utilisation on the Tarcoola-Darwin Railway²⁶

	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.) ²⁷	N/A	6	6	N/A
Average dwell time (%) ²⁸	N/A	15.5	11	N/A

Notwithstanding increases in base metal commodity prices,²⁹ the decline in haulage since 2014 reflects an overall fall in the volume of haulage of goods for which no sustainable competitive price exists,³⁰

²² 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.

²³ See GWA, Submission on Review of Regulatory Guidelines, p. 7.

²⁴ 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.

²⁵ 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.

²⁶ 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.

²⁷ 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; 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; and Department of Infrastructure, Regional Development and Cities, Trainline 6', p. 77. The number of weekly intermodal services was six in calendar year 2017.

²⁸ 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.

²⁹ 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>.

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

likely in part due to some mine closures.³¹ 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.³²

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 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 Appendix B.

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.³³ 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.

³¹ 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.

³² 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.

³³ See Schedule to the Code: Access Pricing Principles, Division 1, Clause 3(f).

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 section 5.3 of Appendix B). 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.³⁴

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 section 5.3 of Appendix B). 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 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.³⁵ That calculation is based on the avoidable costs of Below-Rail Services attributable to the usage of that required infrastructure.³⁶ 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.

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

³⁵ See Schedule to the Code: Access Pricing Principles, Division 1, Clause 3.

³⁶ See Schedule to the Code: Access Pricing Principles, Division 1, Cause 3, and Schedule to the Code: Access Pricing Principles, Division 2, Clause 2.

3 Draft amendments to the Guidelines

As highlighted in the Draft Decision in April, the Commission proposes to retain the majority of existing procedures and guidance in Guidelines 1, 2 and 3, with only modest amendments. The Commission also proposes to update the format of the Guidelines to be in line with its publications in other regulated sectors (and some submissions received in May were supportive of this).³⁷

This Further Draft Decision outlines some new proposed amendments in Sections 3.2.3 and 3.2.4 (below). As noted earlier, these new amendments clarify aspects of the Guidelines, to more explicitly address certain requirements under the Code.

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 Price transparency and reference prices

In the April 2019 Draft Decision, the Commission encouraged GWA to publish indicative pricing information to provide price transparency to Access Seekers, noting that the Access Provider already must produce Access Price information for reference purposes upon request within 10 days (albeit not publish them).³⁸ The Commission encouraged the indicative pricing information to be in the form of reference prices, a methodology or principles. Increased transparency of Access Prices can help to facilitate commercial negotiations for access and promote efficient use of and investment in infrastructure.

Submissions to the Draft Decision from the MCA-NTD, SACOME and Pacific National were supportive of (firm- or regulator-driven) actions to increase information about Access Prices.³⁹ In contrast, submissions from GWA and the ARTC supported commercially negotiated access without published reference prices.⁴⁰

Responding to the Commission's suggestion for the publication of reference prices, the Access Provider on the Tarcoola-Darwin railway (that is, GWA) outlined that it uses a demand-based approach to pricing Below-Rail Services. Specifically, that approach takes into account the nature of the access request (ie location, expected duration, physical characteristics of the services etc.) and the Access Seeker's willingness to pay for the service. As stated by GWA:⁴¹

'GWA's task is to set prices which encourages traffics onto the network and contributes to its avoidable costs. In this way, GWA will generate revenue without introducing any economic inefficiency and should achieve recovery of as close to the economic cost of the railway as possible. The regulatory model is based on Ramsey pricing whereby prices are set as closely to economic cost as the price elasticity of traffics allows. This is intended to mimic what would occur in a normal market situation, recognising that the natural monopoly characteristics of a railway network require the adoption of a regulatory framework to achieve a pseudo-market outcome. Users of the network are protected from excessive prices by the imposition of the ceiling.'

³⁷ See GWA, Review of Regulatory Guidelines – Submission May 2019.

³⁸ See Clause 9(1)(e) of the Code.

³⁹ 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.

⁴⁰ See ARTC, p. 1, and GWA, Review of Regulatory Guidelines – Submission May 2019, p. 12.

⁴¹ See GWA, Review of Regulatory Guidelines – Submission May 2019, p. 12.

GWA argued that a demand-based approach to pricing on the Tarcoola-Darwin railway may be hindered by a requirement to publish reference prices. As stated by GWA:⁴²

'The Ramsey pricing principle is expressly inbuilt into the competitive imputation price that applies to intermodal traffics. The competitive transport mode price sets the total revenue available for the above and below rail operators and the Competitive Imputation Price formula applies the residual to below rail after allowing the above rail operator to recover its avoidable costs.'

Pricing for all other traffics follows a similar logic except that in place of a single competitive alternative price setting the maximum, different traffics are likely to have different price elasticities dependent on the specifics of the traffic and the end markets in which they operate. The product transported by each traffic will have different revenues and costs and consequently a different ability to contribute to the recovery of below rail costs above avoidable costs (i.e. the floor).

This environment does not lend itself to the publication of simple reference prices. The majority of situations where reference prices are published in Australia are for the haulage of coal. As discussed in section 3.1.1 above, these are traffics operating largely to the same specification, in the same end market that meet most of the criteria for differentiation noted above. Pricing for those traffics is set at the ceiling and there is no need or opportunity to differentiate access prices.'

The Commission notes that a demand-based approach to pricing is permitted under the Code, insofar as prices comply with floor and ceiling price requirements and to the extent that prices do not generate 'excessive revenues' (as calculated periodically by the regulator). However, in principle, a demand-based approach to pricing could in some particular instances result in monopoly rents and, subject to effective ring-fencing requirements, reduce competition in the above-rail market.⁴³

A key question is, therefore, 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? The Commission will shortly be commencing a review of revenues earned for providing access to the Tarcoola-Darwin railway.

Accordingly, the Commission proposes no amendments to the Access Provider's information requirements for reference pricing purposes within Guideline 1.⁴⁴

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.'

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

⁴² See GWA, Review of Regulatory Guidelines – Submission May 2019, p. 42.

⁴³ See ACCC (2006), 'Submission to the Productivity Commission Draft Report into Road and Rail Freight Infrastructure Pricing', October 2006, pp. 3-4, available at: https://www.pc.gov.au/inquiries/completed/freight/submissions/australian_competition_and_consumer_commission2/subd080.pdf.

⁴⁴ The April 2019 Draft Decision included additional requirements, relating to reference prices, assets outside of the Code and price discrimination based on ownership; see GWA, Review of Regulatory Guidelines – Submission May 2019, p. 16-17. Those particular draft proposals have been removed in this Further Draft Decision.

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

The modification 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'.⁴⁵

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

The Commission proposes to retain and, where possible, clarify 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 network⁴⁶).⁴⁷ 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.⁴⁸

A modification is proposed 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 4.1.5.⁴⁹

The Draft Decision in April also proposed an amendment to Guideline 1 to include a requirement for GWA's publication of the Master Train Plan to include a 'clear representation of the accessible assets under the Code'. However, GWA has published rail line maps that display assets under the Code (as discussed in section 3.1.4 below).⁵⁰ In addition, GWA's submission noted that the Master Train Plan may not be the appropriate document for setting out that information.⁵¹ The Commission, therefore, proposes not to include the requirement.

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).⁵²

⁴⁵ In its April 2019 Draft Decision, the words '*nature of goods*' were used instead of '*type of load (freight or passenger)*'. However, the words type of load have been used as they more accurately consider passenger and freight services.

⁴⁶ 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>.

⁴⁷ 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.

⁴⁸ See GWA, Submission on Review of Regulatory Guidelines, pp. 8-9.

⁴⁹ See GWA, Review of Regulatory Guidelines – Submission May 2019, p. 17.

⁵⁰ See GWA's [website](#)

⁵¹ In its submission to the April 2019 Draft Decision, GWA noted that the publication of specific assets is not compatible with the usual format of a Master Train Plan. It argued that a Master Train plan includes a diagram with locations and distances on the Y axis and time (usually a day or a week) along the X axis; see GWA, Review of Regulatory Guidelines – Submission May 2019, pp. 18-19.

⁵² See MCA-NTD, Submission on the 2017 ESCOSA Review of Guidelines for the Access regime for the Tarcoola-Darwin Railway, pp. 8-9.

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 ⁵³	Must be kept up to date
South Australia – Tarcoola to Darwin	No requirements	N/A
Western Australia	Must be made available ⁵⁴	As often as necessary to be up to date but subject to audit at least every two years ⁵⁵
Queensland - 2016 Access Undertaking	Published on website (preliminary information, line diagrams ⁵⁶ and capacity information)	Must be kept up to date
ARTC	On request and published on website ⁵⁷	Must be kept up to date

The Commission agrees that more information about rail line segments could reduce barriers to negotiation,⁵⁸ 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. For these reasons, the Commission proposes that it 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.⁵⁹

3.2 Guideline 2: Arbitrator pricing requirements

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

⁵³ See Commission, Review of the South Australian Rail Access Regime Information Kit, April Draft Decision, pp. 6-7.

⁵⁴ 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)

⁵⁵ See ERA, Final Determination on Brookfield Rail's Proposed Revised Train Management Guidelines, p. 13, available at: <https://www.era.gov.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.

⁵⁶ 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>

⁵⁷ 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>.

⁵⁸ See Commission, Review of the South Australian Rail Access Regime Information Kit, p. 14.

⁵⁹ See MCA-NTD, Submission on review of rail guidelines for the Tarcoola-Darwin Railway – Draft Decision, p. 8.

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 Guidelines about information (such as costs, assets and rates of return) that would serve as an input to the arbitrator's calculations.⁶⁰

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.⁶¹ 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 invested⁶² over time.⁶³

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 Review⁶⁴ 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.⁶⁵ The Commission proposes, therefore, to retain guidance to roll forward the initial DORC valuation, as opposed to requiring periodic revaluations. Also, the Commission proposes to update Guideline 2 to specify the application of a straight-line depreciation method to the relevant assets.⁶⁶

⁶⁰ 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.

⁶¹ See Schedule to the Code: Access Pricing Principles, Division 1, Clause 2(7)(a).

⁶² 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.

⁶³ See Commission (2004), 'AustralAsia Railway (Third Party Access) Code: Guideline Review', p.10, available at <http://bit.ly/ThirdPartyAccessGuidelineReview-Final>.

⁶⁴ 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>.

⁶⁵ See Schedule to the Code: Access Pricing Principles, Division 1, Clause 2(8)(a).

⁶⁶ 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.

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 the Access provider.⁶⁷ Pacific National considered that government-contributed assets should be excluded for pricing purposes.⁶⁸

Government-contributed assets and financial assistance can be deducted from the DORC,⁶⁹ provided a reasonable risk-adjusted return is not prevented on invested capital.⁷⁰ The previous Guidelines removed government-contributed assets and financial assistance for the purposes of providing guidance to an arbitrated price,⁷¹ but did not remove it for ceiling price purposes,⁷² as this is a theoretical upper bound – not a guidance on an arbitrated price. The Commission proposes to retain this approach as it is consistent with the Code.⁷³

3.2.2 Timeframe for avoided costs

The Commission proposes to retain the existing guidance defining the timeframe of avoided costs.⁷⁴ 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 proposes to clarify guidance on the calculation of Above-Rail incremental cost.⁷⁵ 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.⁷⁶

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 proposes that the arbitrator must consider actual Above-Rail costs and indicators of benchmark efficient costs in determining the Above-Rail incremental cost. The Commission proposes a requirement in Section 4.1.1: '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

⁶⁷ 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.

⁶⁸ See Pacific National, 2019 Review of rail guidelines for Tarcoola-Darwin Railway and South Australian rail access regime information kit, pp. 5-6.

⁶⁹ See Schedule to the Code: Access Pricing Principles, Division 1, Clause 2(8).

⁷⁰ See Schedule to the Code: Access Pricing Principles, Division 1, Clause 2(8)(b).

⁷¹ See Guideline 2, Clause 5.

⁷² See Guideline 2, Clause 2.

⁷³ 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 proposes to leave explanations of intent (such as the one proposed by GWA) for inclusion in the Decision Document rather than the Guideline.

⁷⁴ 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).

⁷⁵ The Draft Guideline 2 released in April had omitted section 4.1.1 (c) regarding terminal costs but it has been reinstated in this Further Draft Decision.

⁷⁶ The competitive imputation methodology is set out in Division 1 Clause 6 of the Schedule to the Code: Access Pricing Principles.

benchmark efficient Above-Rail costs for the Services in question'. **This is one of the Commission's proposed new amendments since the release of the Draft Decision in April.**

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. As highlighted in the Draft Decision in April, the Commission proposes to retain 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).⁷⁷

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

The Commission's proposed new amendments are described in Sections 3.2.4.1 (In relation to floor prices), 3.2.4.2 (Retain right to re-determine post-tax real risk premium) and 3.2.4.3 (Parameter choice).

3.2.4.1 In relation to floor prices

The Commission proposes to add 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 proposes to modify Section 6.1.3 in two ways.

First, to introduce 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 current Guideline is silent on that matter. The guidance is consistent with the requirements of Clause 2.7(c)(i)(B) of the Pricing Schedule.

Second, a proposed change to clarify 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.

The proposed changes 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.'

⁷⁷ See Schedule to the Code: Access Pricing Principles, Division 3, Clause 4.

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

The Commission proposes to update 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 proposes to update Section 6.1.4 to reflect the proposed 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’.

3.2.4.3 Parameter choice

In its Draft Decision in April 2019, the Commission did not propose any modifications to parameter choice and submissions to the draft did not raise any concerns.⁷⁸ Nonetheless, the Commission now proposes to add requirements to 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 proposed 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 market⁷⁹), 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 approach⁸⁰), may be a relevant consideration for the arbitrator.

⁷⁸ Pacific National noted the general value in binding rate of return guidelines to reduce discretion in regulatory decisions; see Pacific National, 2019 Review of rail guidelines for Tarcoola-Darwin Railway and South Australian rail access regime information kit, p. 6.

⁷⁹ 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>.

⁸⁰ See Commission, Guidance paper 6 – Treatment of inflation in the regulatory rate of return.

3.3 Guideline 3: Regulatory information requirements

3.3.1 Ring fencing

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

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.⁸¹ 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.⁸² Submissions to the April 2019 Draft Decision raised similar concerns.⁸³

Guideline 3, however, 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. This requirement, coupled with no evidence of misallocation found in KPMG's external 2015 review of GWA's financial allocations,⁸⁴ led the Commission to conclude at that time that the existing requirements provide sufficient ring-fencing.

As noted in the discussion of reference prices, the issue of ring-fencing is linked to price transparency and confidence in the Access Regime. To the extent that ring-fencing were to be ineffective, demand-based pricing could potentially favour the Above-Rail Services of the vertically integrated operator.

The Commission notes that more prescriptive Guidelines relating to ring-fencing⁸⁵ and confidential information about access⁸⁶ may not necessarily imply more protection against cost shifting than is already in the Code. 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 (including Above-Rail Services). Clause 12A sets out requirements for the protection of information. If there were any evidence to suggest that price discrimination against third-party Access Seekers had occurred, the Commission would obtain and review access contract information from the Access Provider and audit ring-fencing procedures and documentation.⁸⁷ The Commission is not aware of any such evidence. If such evidence comes to light, the Commission would assess the evidence and make an assessment of the required course of action (which could include strengthening ring-fencing provisions).

3.3.2 Minor modifications and clarifications

The Commission proposes to update Guideline 3 with minor updates and clarifications to improve readability. It has also considered updating reporting dates.

In its submission to the April 2019 Draft Decision, GWA proposed changing reporting dates to be in calendar years.⁸⁸ However, calendar year reporting cannot extend to the cost information provided in relation to revenue reviews of the Tarcoola-Darwin Railway. The reporting period for these reviews is

⁸¹ See Pacific National, Submission to the Review of Rail Guidelines, February 2017, pp. 4-6.

⁸² See Pacific National, Submission to the Review of Rail Guidelines, February 2017, pp. 4-6.

⁸³ 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.

⁸⁴ See KPMG, Review of GWA financial allocations.

⁸⁵ The MCA-NTD argues that that the Guidelines could assure that no cost shifting would occur; see MCA-NTD, Submission on review of rail guidelines for the Tarcoola-Darwin Railway – Draft Decision, p. 9.

⁸⁶ 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.

⁸⁷ See Code, Part 4, Clause 39.

⁸⁸ See GWA, Submission on Review of Regulatory Guidelines, p. 9 and GWA, Review of Regulatory Guidelines – Submission May 2019, p. 23.

set out in Clause 50(10) of the Code. In light of the change in ownership of GWA expected to be announced soon, the Commission will consider reporting dates as further information about ownership, and hence company reporting periods, becomes clearer.⁸⁹

There is also a modification proposed to the procedure regarding compliance of regulatory accounts, such that, in the event that the Access Provider does not have an External Director⁹⁰, the statement of compliance may be signed by an External Director of a related entity of the Access Provider.⁹¹

Other minor amendments include, clarifying terminology and definitions (such as relating to train procedures and service quality standards in Guideline 1^{92,93}), adding greater specificity (such as relating to calculating CPI inflation in Guideline 2⁹⁴) and removing information that may now be redundant.⁹⁵

⁸⁹ See GWA media announcement, available at: <https://ir.gwrr.com/press-release/acquisitions-investments/genesee-wyoming-inc-be-acquired-brookfield-infrastructure>.

⁹⁰ 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.

⁹¹ The change may add flexibility; see GWA, Submission on Review of Regulatory Guidelines, p. 9.

⁹² 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.

⁹³ 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.

⁹⁴ 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.

⁹⁵ Such as references in current Guideline 3 to cost information and information procedures that have already passed.

4 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.⁹⁶

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 has been Regulator of the Code since its inception 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 2030.⁹⁷

⁹⁶ See Commission, Ten-year review of revenues, p. 7.

⁹⁷ See National Competition Council, AustralAsia Railway Access Regime; Final Recommendation, February 2000, available at <http://ncc.gov.au/images/uploads/CERaNtRe-001.pdf>.

5 Appendix B: Selected legislation and process for determining arbitrated access prices

5.1 Clause 9(1) of the Code

9—Obligation of Access Provider to provide information about access

(1) The Access Provider must, on application of any person, provide the person with information reasonably requested by the person about—

- (a) the extent to which the access provider's railway infrastructure facilities are currently being used;
- (b) technical details and requirements of the Access Provider, such as axle load data, clearance and running speeds;
- (c) time-path allocation and reallocation policies for the railway;
- (d) service quality and train management standards; and
- (e) relevant prices and costs associated with Railway Infrastructure Services provided by the Access Provider, prepared by the Access Provider for reference purposes in accordance with Guidelines developed and published by the Regulator.

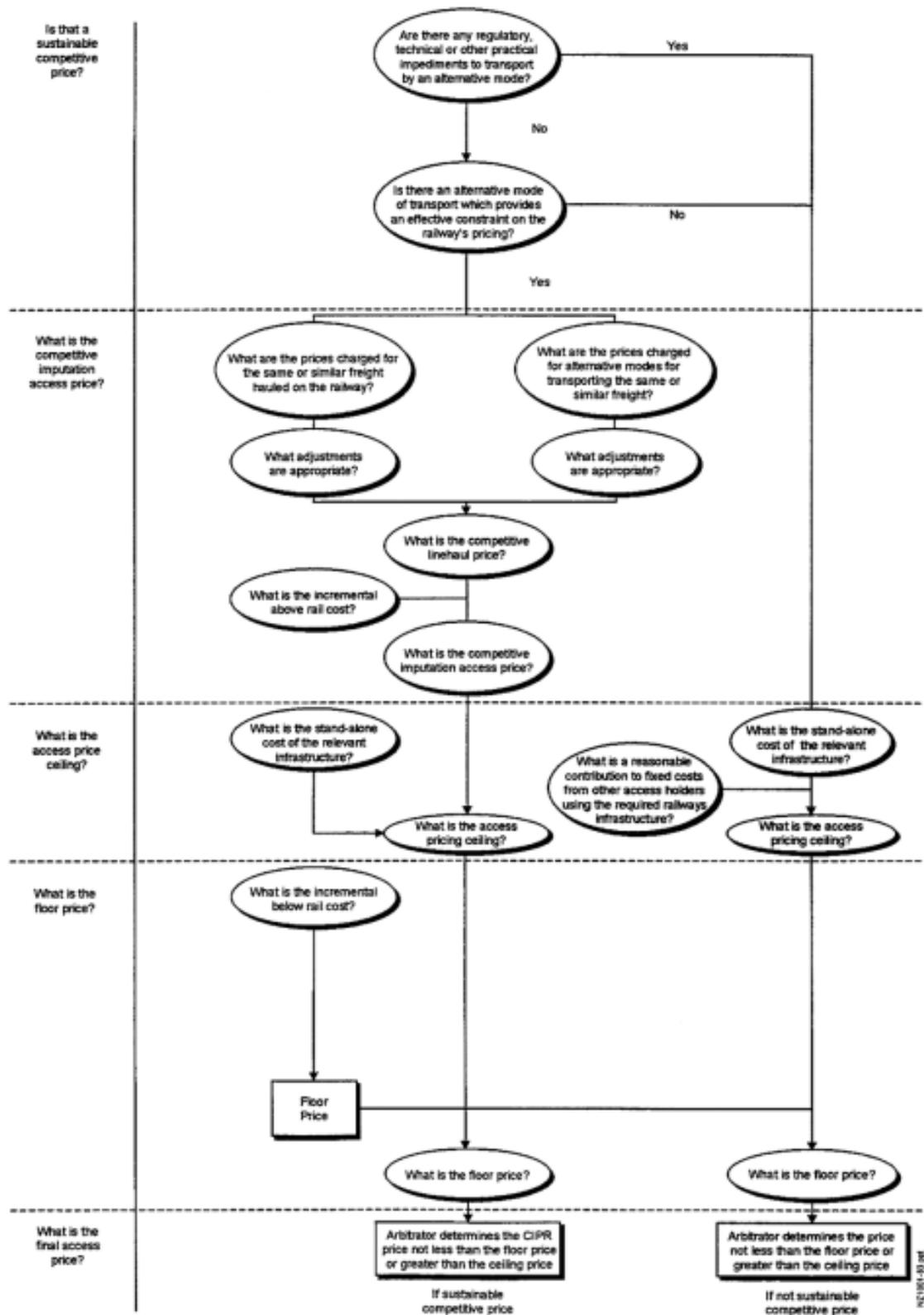
5.2 Clause 45A of the Code

45A—Power to vary Guidelines

(1) The Regulator may, from time to time as the Regulator thinks fit, vary or revoke guidelines developed and published by the Regulator under this Code, or develop and publish new or substitute guidelines.

(2) The Regulator should, in developing (or varying) guidelines under this Code, take into account interface issues that may arise under a corresponding 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 this Code).

5.3 Process for determining the arbitrated Access Price⁹⁸



⁹⁸ Source: Code, Attachment A.

6 Next steps

This further Draft Decision extends the period of consultation on the review of rail guidelines of the Tarcoola-Darwin railway. The Commission invites submissions on this further Draft Decision by 30 August 2019. The inside cover of this report explains how to make a submission.

The Commission would also be pleased to meet informally with stakeholders, either individually or with representative organisations, to discuss the draft decision. If you or your organisation wish to meet with Commission staff, please use the contact details on the inside cover of this further Draft Decision.

The Commission intends to release a Final Decision with final guidelines in October 2019.



The Essential Services Commission
Level 1, 151 Pirie Street Adelaide SA 5000
GPO Box 2605 Adelaide SA 5001
T 08 8463 4444

E escosa@escosa.sa.gov.au | W www.escosa.sa.gov.au