



Rail



Issues paper

South Australian Rail Access Regime Review

February 2020

Request for submissions

The Essential Services Commission (**Commission**) invites written submissions from members of the community on this paper. Written comments should be provided by **Wednesday, 18 March 2020**.

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Responses to this paper should be directed to: **2020 South Australian Rail Access Regime Review**

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

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Summary

Purpose of the access regime

The South Australian Parliament introduced the Railways (Operations and Access) Act 1997 (ROA Act) to facilitate, among other things, competition and efficiency in the provision of rail services.¹ Rail services are typically vertically integrated in South Australia: this means the owner of rail infrastructure (the 'below-rail' service provider) also operates trains ('above-rail' services) on those lines.

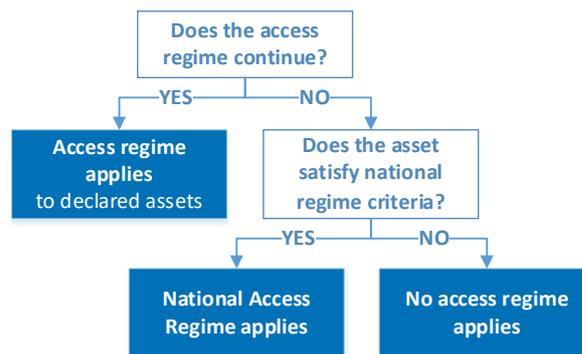
The ROA Act establishes a negotiate-arbitrate framework to facilitate access by accredited rail operators to below-rail services on fair commercial terms. It also establishes the regulator's responsibility for monitoring and compliance, setting requirements for information provision, and conciliation and arbitration of access disputes. In effect, the regime provides a backstop to commercial negotiations that can, ultimately, promote investment and production in upstream markets such as for grain and mineral resources.

Purpose of the review

The Essential Services Commission of South Australia (Commission) is the regulator of the access regime under the ROA Act.² Under section 7A of the Act, the Commission must review the regime and form a view as to whether or not the regime should continue from 31 October 2020 for five years. The Commission must provide a report and conclusions to the Minister for Planning, Transport, Infrastructure and Local Government. Figure 1 illustrates the access arrangements that are available for rail infrastructure services.

The Commission last reviewed the access regime in 2015, recommending that the access regime continue for the five-year period from 31 October 2015 to 30 October 2020. In accordance with that recommendation, the Government extended the access regime until 30 October 2020.³

Figure 1: Access arrangements that could apply



Feedback from stakeholders

This paper outlines the scope of the review and highlights key issues that the Commission intends to consider. The Commission will consult with below-rail and above-rail operators, as well as end-users of rail transport services, such as miners and grain producers, in order to understand the regulatory costs involved with the regime and the potential for market power to be used for improper purposes. The Commission will also consult with stakeholders on feasible alternatives to the current access regime and ways to improve the regime's effectiveness.

The Commission recently reviewed the access regime guidelines, in particular relating to floor and ceiling pricing principles and exchange of information about the terms and conditions of access.⁴ To the extent that issues raised in submissions to the guideline review relate to the access regime in general (rather than the guidelines specifically), these will be considered. Stakeholders may, therefore, wish to limit comments to matters not considered in the guideline review. However, differences in the funding models for road and rail are outside the scope of this review.

¹ The objects of the ROA Act are set out below.

² ROA Act section 9.

³ Commission, *SA Rail Access Regime Review*, 2015, available at: <https://www.escosa.sa.gov.au/projects-and-publications/projects/rail/south-australian-rail-access-regime-review-2015>.

⁴ Commission, *Review of the South Australian Rail Guidelines Access Regime Guidelines*, 2019, available at: <https://www.escosa.sa.gov.au/projects-and-publications/projects/rail/review-of-rail-guidelines-and-access-regimes-2017>.

Context and purpose of the access regime

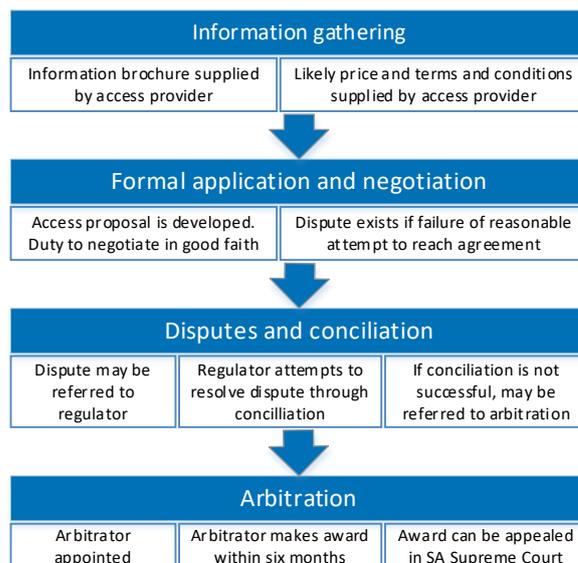
Operation of the ROA Act

The ROA Act sets out the framework for the operation of, and access to, declared intrastate rail infrastructure services. The objects of the ROA Act are:⁵

- ▶ to promote a system of transport in South Australia that is efficient and responsive to the needs of industry and the public
- ▶ to provide for the operation of railways
- ▶ to facilitate competitive markets in the provision of railway services through the promotion of the economically efficient use and operation of, and investment in, those services
- ▶ to promote the efficient allocation of resources in the rail transport segment of the transport industry, and
- ▶ to provide access to railway services on fair commercial terms and on a non-discriminatory basis.

In practice, the regime requires access seekers and access providers to share information (as set out in the access regime guidelines⁶) and negotiate in good faith. Either party may ask the regulator to intervene in the event they cannot reach an agreement. The regulator may then attempt to settle the dispute by conciliation, and/or appoint an arbitrator to determine a price (calculated between the floor and ceiling price according to the pricing principles in the ROA Act and the access regime guidelines). This process is illustrated in Figure 2.⁷ The Commission's previous review highlighted that the absence of access disputes and the limited number of formal access agreements is not an indication of the effectiveness or otherwise of the access regime.^{8,9}

Figure 2: Process for reaching an access arrangement



Background and scope of the access regime

The access regime has been in operation since 1997, and applies to services provided on intrastate rail infrastructure that have been declared by proclamation (Table 1). There are currently three regulated operators of rail infrastructure services under the ROA Act:

- ▶ Genesee & Wyoming Australia (GWA)
- ▶ Journey Beyond Rail Expeditions, and
- ▶ the South Australian Government.

GWA purchased the assets of Australian National's South Australian intrastate freight business in 1997, including trains and infrastructure, for \$57.4 million, and the South Australian Government granted a 50 year lease over the associated freehold property.¹⁰ GWA is a vertically integrated rail operator, with above-rail and below-rail services on their lines; however the accounts for these operations are segregated under the requirements in section 22 of the ROA Act.

⁵ ROA Act section 3.

⁶ Commission, *Review of the South Australian Rail Guidelines Access Regime Guidelines*, p. 9-18.

⁷ See ROA Act or National Competition Council, *South Australian Access Regime: application for certification as an effective access regime*, 2011, pp. 9-12, available at: http://ncc.gov.au/application/application_for_certification_of_the_south_australian_rail_access_regime.

⁸ Commission, *SA Rail Access Regime Review*, p. 29.

⁹ The failure of commercial negotiations to reach agreement does not necessarily indicate a failure in the overall process. For instance, access providers and access seekers can have diverging views of the outlook for rail transport services, and hence different expectations of future costs and prices.

¹⁰ Australian National Audit Office, *Sale of SA Rail, Tasrail and Pax Rail*, 1998, pp. 23-24.

Table 1: Rail infrastructure services declared under the ROA Act¹¹

Asset covered under access regime	Current use
<u>GWA</u>	
Eyre Peninsula lines (excluding Thevenard)	No users
Mid-North and Barossa lines	No users
Murray-Mallee region lines	No users
Kevin to Thevenard line	One user
Yards and sidings on the interstate mainline track	Multiple users
<u>Journey Beyond Rail Expeditions</u>	
Passenger terminal at Keswick	One user
<u>South Australian Government</u>	
Adelaide metropolitan network	One user
Port Augusta to Leigh Creek line	No users

GWA's intrastate rail lines previously transported predominantly grain to ports or other transport hubs; however, use on the Eyre Peninsula lines (excluding Thevenard) ceased in 2019, and the Mid-North and Barossa lines and Murray-Mallee region lines have been unused for more than five years. GWA operates 66 kilometres of track from Kevin to Thevenard for one user, Gypsum Resources Australia, to transport approximately 2 million tonnes of gypsum per year from the quarry to the port.¹²

GWA yards and sidings are used for storage, shunting and loading on the interstate line.¹³ Demand for these yards and sidings is driven by traffic between Perth and the eastern states, which is mostly transported by rail. As rail carries

the majority of the freight on this east-west corridor, the use of these yards and sidings may be significant.¹⁴

The passenger terminal at Keswick is operated by Journey Beyond Rail Expeditions (previously Great Southern Rail or Pax Rail) under a 50 year lease. The South Australian Government granted the lease in 1997 when Pax Rail purchased trains and other assets to run passenger services between Adelaide and Melbourne, Perth, Sydney and Alice Springs (now Darwin).¹⁵ No access requests have been lodged with the Commission, as there are no other users of the terminal.

The Adelaide metropolitan rail network is state-owned and operated.¹⁶ There are currently no commercial arrangements to access the network, and connectivity between the metropolitan network and other rail networks is limited. All metropolitan passenger rail networks are vertically integrated in Australia.¹⁷

The Leigh Creek line, originally used to transport coal, became part of the access regime in 2018 when the sublease to the previous operator expired and the line returned to state ownership.¹⁸ With the exception of some activity in 2019 on a small section of the line, the line has not been in use since 2018.

The state access regime fits within the broader framework of national access legislation. The National Competition Council assessed the access regime and the Commonwealth Minister certified the regime as effective under section 44N of the Competition and Consumer Act 2010, for a period of ten years from 26 July 2011.¹⁹ The Productivity Commission expressed the purpose of certification as 'to improve the consistency and quality of access regimes, to promote regulatory

¹¹ Proclamation published in the South Australian Government Gazette, 29 September 2016 p. 3912, available at http://governmentgazette.sa.gov.au/sites/default/files/public/documents/gazette/2016/September/2016_057.pdf.

¹² Gypsum Resources Australia, *submission to Viterro wheat port exemption assessment*, 2019, available at: <https://www.accc.gov.au/regulated-infrastructure/wheat-export/wheat-export-projects/viterro-wheat-port-exemption-assessment/exemption-application-issues-paper>.

¹³ GWA, *submission to 2015 Rail Access Regime Review*, p. 1, 2015, available at: <https://www.escosa.sa.gov.au/projects-and-publications/projects/rail/south-australian-rail-access-regime-review-2015>.

¹⁴ Bureau of Infrastructure, Transport and Regional Economics, *Trainline 6*, 2018, p. 4, available at: https://www.bitre.gov.au/publications/2018/train_006.

¹⁵ Australian National Audit Office, pp. 23-24.

¹⁶ However, the Government plans to issue a tender for operating the metropolitan network, see media release, 'Better train services one step closer' 19 December 2019, available at: <https://www.premier.sa.gov.au/news/media-releases/news/better-train-services-one-step-closer>.

¹⁷ Bureau of Infrastructure, Transport and Regional Economics, *Trainline 6*, p. 133.

¹⁸ Proclamation published in the South Australian Government Gazette, p. 3912.

¹⁹ See Ministerial Decision on Effectiveness of Access Regime, available at: <http://ncc.gov.au/images/uploads/CERaSAMD-001.pdf>.

certainty and to reduce the scope for regulatory duplication'.²⁰

If the access regime continues, the South Australian Government will need to consider applying for recertification.

Economic context and market power

The demand for rail infrastructure services is derived from the demand for transport services, which, in turn, flows from the demand for commodities and other goods that require transportation. Given the fixed capacity of rail infrastructure, a fall in demand for rail services leads to excess capacity and higher average costs for rail infrastructure services.

As well as excess capacity, intrastate rail is currently characterised by a small number of users sharing fixed infrastructure costs.²¹ Some infrastructure has limited salvage value (for example, earthworks and bridges). Many lines are in need of refurbishment and, as noted earlier, are not currently in use. A minimum level of maintenance is required to replace and repair track and equipment, and expenditure is likely to be incurred even on unused lines.

Competition from road transport is one of the drivers of excess rail infrastructure capacity, highlighting the challenging outlook for intrastate rail in South Australia. Road transport tends to have advantages over rail transport on non-bulk freight, urban freight and intercity freight routes due to factors such as shorter delivery times, greater flexibility and less double-handling (delivering freight to and from rail terminals); however, relative prices, and therefore competition, between road and rail are sensitive to technology changes and movements in commodity prices.^{22,23}

The Commission is interested in information and views about the outlook for rail transport services in South Australia. This includes views on the

outlook for end-user demand as well as the level of rail infrastructure investment and service standards.

Questions for stakeholders:

What factors have led to the movement away from rail transport in favour of road? Are these factors likely to be permanent, or could market or regulatory changes lead to an increase in demand for rail?

Access regimes are generally implemented to counter the improper exercise of market power by owners of certain infrastructure, for example where anticompetitive advantages may be available to unregulated vertically integrated firms that operate above-rail and below-rail services. That is, a vertically integrated firm with market power in below-rail services can have incentives to prevent access or discriminate against competitors in the supply of above-rail services.²⁴ The extent of market power, or conversely, the degree of competitive pressure in the market (for example, due to competition from road and other modes of transport, and/or any countervailing bargaining power of above-rail operators), is therefore central to the question of whether the access regime is necessary to achieve the objects of the ROA Act.

The extent of market power is unlikely to be uniform across proclaimed infrastructure. For some rail lines, road transport will be a competitive substitute capable of exerting competitive pressure on price and service quality. There may, however, be other rail lines for which there is no close substitute and the cost of duplicating the infrastructure is high.

²⁰ Productivity Commission, *National Access Regime*, 2013, p. 59, available at: <https://www.pc.gov.au/inquiries/completed/access-regime>.

²¹ For example, between 2010 and mid-2015 just four access agreements were reported (noting that agreements below a certain contract value or duration do not need to be reported): Commission, *Review of the South Australian Rail Guidelines Access Regime Guidelines*, p. 8.

²² Bureau of Infrastructure, Transport and Regional Economics, *Road and Rail Freight: Competitors or Complements?*, 2009,

available at: https://www.bitre.gov.au/publications/2009/is_034.

²³ Rail is significantly safer than road, with 0.02 deaths per thousand, compared with 4.91 deaths per thousand for road: Department of Infrastructure, Transport, Cities and Regional Development, *Transport and Australia's Development to 2040 and Beyond*, 2016, p. 23, available at: <https://www.infrastructure.gov.au/infrastructure/publications/>.

²⁴ Petersen, Bull & Dermody, *Access Regulation in Australia*, 2016, p. 25, 27.

Question for stakeholders:

For which declared rail infrastructure services is competition sufficient that parties would reach competitive access arrangements in the absence of the regime?

Proposed assessment framework

The access regime should continue in operation if the benefits it delivers outweigh the costs of maintaining it, taking into account the costs and benefits of feasible alternatives. Table 2 presents examples of costs and benefits that will be evaluated. Alternatives to the current access regime include the national regime or no formal access regulation (as shown earlier in Figure 1).

Table 2: Examples of benefits and costs under different access arrangements

Status quo: access regime continues to apply
- benefit of protecting against market power and promoting activity in related markets under current access arrangements
- compliance costs under current access arrangements
- risk of regulatory failure (such as any impact on investment)
- cost of recertification under national legislation
Counterfactual 1: if the national regime applies
- benefit of protecting against market power and promoting activity in related markets under the national regime
- compliance costs under the national regime
- risk of regulatory failure
- uncertainty and transition costs
Counterfactual 2: no access regime
- cost of any misuse of market power, including impacts on related markets

Benefits

The Commission will consider whether or not there is evidence that market power has been, or could be, used for improper purposes, and consider whether or not the protections provided by the access regime are effective. The Commission is especially interested in hearing from parties that have sought or considered access to declared rail infrastructure services, including infrastructure not currently in use.

Questions for stakeholders:

To what extent do parties rely on the access regime in negotiations for access to declared rail infrastructure services? Please specify the rail lines for which access was sought, and any difficulties in gaining access.

What other benefits does the access regime deliver?

Costs

The Commission is interested in information on direct costs (regulatory compliance costs) and any indirect costs imposed by the access regime, in particular, any evidence that the regime has altered investment behaviour.

Question for stakeholders:

What are the direct and indirect costs of the access regime? Please provide qualitative or quantitative evidence.

Alternatives

If the state access regime expired, the national regime may provide some level of regulatory protection for access seekers;²⁵ however, it may not apply to all rail infrastructure services currently covered by the state regime if they do not meet relevant criteria such as the 'national significance' test.²⁶ Some have suggested that the time taken to resolve applications under the national access regime adds uncertainty and cost.²⁷ Were the national regime to apply, the relative costs and

²⁵ Access under this pathway may occur through declaration of services by the relevant Commonwealth Minister or an access undertaking submitted by the service provider and approved by the Australian Competition and Consumer Commission under Part IIIA of the Competition and Consumer Act 2010.

²⁶ Criteria for declaration or access undertakings can be found in Part IIIA of the Competition and Consumer Act 2010.

²⁷ Productivity Commission, p. 238; Petersen, Bull & Dermody, p. 138.

benefits of the state and national regimes, rather than the absolute costs and benefits of each one, would be central to the assessment.

Questions for stakeholders:

To what extent would the national access regime apply to intrastate rail infrastructure services in the absence of a state regime?

What would be the costs and benefits of regulating access arrangements through the national regime?

If the access regime were to expire, market developments could later require its reintroduction. However, this would impose transitional costs, including the cost of collecting evidence to identify and assess the need for re-introduction of the regime, and the cost of legislative change.

Question for stakeholders:

What is the value in continuing the access regime as insurance in the event that demand for rail transport services increases?

Other issues

If the Government decides to continue the current regime, there may be changes that could increase benefits or reduce costs. The Commission does not have the power to make changes to the current regime, but may suggest that the Government consider changes that may be worthy of investigation. For example, there is currently no formal mechanism for stakeholders to seek to have rail infrastructure declared under, or removed from, the access regime.²⁸ Given changes to market conditions and uncertainty about future demand, introducing such a mechanism may improve the efficiency and responsiveness of the regime.²⁹

Questions for stakeholders:

What would be the costs and benefits of introducing a mechanism for stakeholders to seek to have rail infrastructure services declared or excluded from the access regime, and what form should it take (for example, should coverage be included in the periodic review of the access regime)?

What other changes could improve the efficiency or effectiveness of the current regime? Please explain with reference to the costs and benefits that would accrue to each relevant party.

Next steps

The Commission will consider information provided by stakeholders in preparing a draft report. Submissions to the draft report are due by Wednesday, 18 March 2020, and can be submitted electronically to escosa@escosa.sa.gov.au or following instructions above. The draft report will contain a further call for submissions prior to the final report, which the Commission plans to publish by October 2020.

Please direct any queries relating to this review to:

- ▶ Vashti Maher, Senior Economist

If you would like to keep up to date with the Commission's rail industry activities and the release of papers for consultation, subscribe at <http://www.escosa.sa.gov.au/subscribe.aspx>.

²⁸ National Competition Council, pp. 18-19.

²⁹ Criteria for determining which assets should be included in an access regime are set out in the COAG *Intergovernmental Agreement on Competition and Productivity-Enhancing Reforms*,

2016, available at: <https://www.coag.gov.au/about-coag/agreements/intergovernmental-agreement-competition-and-productivity-enhancing-reforms>.