

Submission to ESCOSA Issues
Paper relating to the 2015 South
Australian Rail Access Regime
Review

March 2015

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1 INTRODUCTION

Asciano welcomes the opportunity to respond to the Essential Services Commission of South Australia (ESCOSA) Issues Paper relating to the review of the South Australian rail access regime (as required under section 7A of the South Australian Railways (Operations and Access) Act (ROA Act)). This submission is public.

2 SCOPE OF ASCIANO'S SOUTH AUSTRALIAN RAIL ACTIVITIES AND THE RAIL ACCESS REGIME REVIEW

Asciano' undertakes extensive rail activities in Australia via its Pacific National subsidiary, which is one of Australia's largest above rail operators. Consequently Asciano has a strong interest in improving the access regimes which apply to Australian rail infrastructure. In particular Asciano believes that applying strong third party access regimes to natural monopoly rail infrastructure will allow competition in related upstream and downstream markets and will ultimately benefit the broader economy as the potential for increased competition results in more efficient transport costs and the development of market opportunities.

Pacific National currently undertakes the following above rail operations in South Australia:

- interstate intermodal rail operations – these operations primarily use Australian Rail Track Corporation (ARTC) rail infrastructure but do use some rail yards controlled by Genesee and Wyoming (GWA);
- interstate bulk mineral rail operations – these operations primarily use ARTC rail infrastructure but do use some rail yards controlled by GWA;
- intrastate coal rail operations – these operations are not within the scope of this review; and
- “hook and pull” operations on behalf of Great Southern Railways (GSR). Pacific National has no commercial interface with GWA in relation to these operations. The commercial interfaces are between GWA and GSR. Consequently this submission makes no comment on issues relating to these GSR operations.

Asciano understands that this current South Australian access regime review only applies to the Adelaide metropolitan broad gauge rail infrastructure, the GSR terminal

at Keswick and some GWA rail infrastructure such as the GWA rail lines in the Eyre Peninsula, the Murray region and the mid-north region. Asciano does not regularly use these assets.

Asciano regularly uses rail yards in South Australia controlled GWA¹ which adjoin Australian Rail Track Corporation (ARTC) rail infrastructure. These yards include GWA rail yards at Port Augusta, Whyalla, Port Pirie, Tailem Bend, Port Adelaide and Dry Creek. Asciano understands that these yards are not subject to the current South Australian rail access review². Asciano believes that to the extent that these rail yards have natural monopoly infrastructure characteristics then consideration should be given to covering these rail yards with a rail access regime.

Given Asciano does not use the rail infrastructure assets which are the subject of this review this Asciano submission focuses on broader issues related to rail access regulation.

3 RAIL ACCESS REVIEW AND ESCOSA'S ISSUES PAPER

Section 7A of the ROA Act requires ESCOSA to review the South Australian rail access regime. The ROA Act only requires that the ESCOSA review determine whether the access regime should continue to apply or whether the regime should expire. There does not appear to be any explicit power within section 7A of the Act to allow ESCOSA to put forward amendments to the rail access regime which may strengthen the regime, nor is there a requirement for the Minister or Parliament (as appropriate) to consider and adopt any amendments to the rail access regime which are put forward.

Given the current wording of the ROA Act and its requirement that the rail access review is essentially a recommendation as to whether or not the South Australian access regime should continue Asciano strongly recommends that the South Australian rail access regime should continue. However, Asciano believes that, if

¹ Note that Asciano is currently discussing access with GWA in relation to access to a number of rail yards under GWA control. Asciano has no specific concerns relating to GWA with respect to these current discussions.

² Asciano understands there is some uncertainty as to whether these yards are covered by the South Australian access regime and that this uncertainty may be clarified in this review. In the event these yards are covered by the South Australian access regime Asciano may make further submissions addressing this issue in this regulatory process.

possible, the current regime should not just continue but be strengthened as outlined in sections 4 and 5 below.

Asciano believes that the South Australian rail access regime must be considered in the context of the South Australian rail infrastructure industry structure. South Australian rail infrastructure involves a degree of common ownership of above rail and below rail assets by GWA. This common ownership along with the lack of a transparent pricing process raises concerns that the access regime may not be able to fully facilitate competition. Asciano believes that a strong and transparent pricing process and functional separation of below rail and above rail assets is needed to fully facilitate competition.

In making a recommendation to strengthen the access regime Asciano recognises that a balance needs to be struck between the need for strong and credible regulation and the fact that the rail assets being regulated in this case are relatively low use rail assets (from an Australian rail perspective).

4 ASCIANO'S GENERAL CONCERNS RELATING TO SOUTH AUSTRALIAN RAIL ACCESS REGULATION

Asciano has several concerns with the South Australian rail regulation framework, as outlined below.

Ring Fencing

One of Asciano's concerns with the South Australian rail access regime is the lack of strong ring fencing requirements. As the Issues Paper (page 1) notes:

Railway services are generally integrated in South Australia. This means that the owner of the railway is often the also a provider of above rail services on those lines.

Asciano believes that where there is vertical integration in the rail industry (i.e. natural monopoly below rail activities and competitive above rail activities are undertaken by a single entity) then there should be a strong ring fencing regime in place to ensure that the integrated entity does not use its monopoly position in its below rail activities to benefit its activities in the competitive above rail market.

The level of ring fencing which applies under the South Australian rail access regime is less than that which applies to other vertically integrated freight rail operations in Australia. This relatively low level of ring fencing increases the potential for vertically integrated entities to engage in discriminatory treatment of above rail operators.

Asciano believes that the ring fencing requirements in the South Australian rail access regime should be strengthened in order to limit the potential for such discrimination. A ring fencing regime should have the ability to identify discrimination, remedy discrimination and prevent future discrimination³.

Asciano believes that the regulatory regime should have requirements for separation of staff such that staff working on access related network activities should be prevented from undertaking non-network related activities. The South Australian rail access regime as outlined in the ROA Act requires separation of accounts, prohibits unfair discrimination and prohibits hindering access. However the requirements of the ROA Act regarding functional separation are minimal in circumstances where there is common ownership and control of below rail assets and above rail assets. This common ownership creates concerns regarding the equal treatment of above rail operators and the potential for the transfer of sensitive information between operating divisions of GWA. Consequently Asciano believes that the South Australian rail access ring fencing regime could be strengthened by requiring further separation of network access related functions and staff from non-network staff and functions.

Asciano believes that by strengthening the ring fencing regime ESCOSA would be meeting its objectives under section 6 of the Essential Services Commission Act 2002. In particular a strong ring fencing regime will promote competition, prevent misuse of monopoly power and promote economic efficiency.

³ A much more detailed outline of Asciano's position on a strong ring fencing regime can be found in various Asciano submissions to the Queensland Competition Authority relating to the regulation of Aurizon Network. These submissions include:

- Asciano Submission to the QCA in Relation to the 2013 Aurizon Network Draft Access Undertaking October 2013
- Asciano Submission to the QCA in Relation to the 2014 Aurizon Network Draft Access Undertaking October 2014

Links to these submissions are at: <http://www.qca.org.au/Rail/Aurizon/Intro-to-Aurizon>

“Negotiate and Arbitrate” Access Model and Information Provision

One of Asciano’s concerns with the South Australian rail access regime is the reliance on the “negotiate and arbitrate” model for obtaining access. The Issues Paper (page 3) states that:

The ROA Act is intended to be a light-handed regulatory regime, and is based on the principle of promoting negotiated outcomes rather than regulated outcomes.

Asciano queries if light handed regulation of monopoly assets is desirable. Asciano has argued in other regulatory submissions⁴ that the “negotiate and arbitrate” access model is problematic as negotiations with natural monopoly infrastructure providers under this model result in outcomes more favourable to the natural monopolist due to imbalances in bargaining power and information between the parties. Consequently, where rail infrastructure is provided by a natural monopoly infrastructure provider, Asciano supports the development and use of regulator–approved access agreements and, if possible regulated prices.

Asciano recognises that the derivation of regulated prices may be too costly to be considered given the nature of the assets covered by the current review, however the development of regulator–approved rail access agreements should be possible as access agreements have to be developed under the “negotiate and arbitrate” model in any event and there are currently numerous regulator–approved rail access agreements available which could act as a template for such an agreement.

Asciano recognises that to date there have been no disputes referred to ESCOSA arising from an unsuccessful negotiation, but as the Issues Paper (page 3) recognises this could be because access seekers are unwilling to test the dispute resolution process or they are wary of dispute resolution costs or other avenues the access provider may potentially use to impact their business.

⁴ See for example

- Asciano Submission to QCA in Relation to Queensland Rail Draft Access Undertaking July 2012 pp 5-7
- Asciano Submission to the Commonwealth Competition Policy Review Issues Paper June 2014 pp 8-9

Asciano recognises that it is unlikely that the South Australian access regime will move from a “negotiate and arbitrate” access model to a more prescriptive access model with regulated access agreements and prices. Under the “negotiate and arbitrate” model there is a lack of relevant cost information available to access seekers, which in turn places access seekers at a disadvantage in negotiating efficient, cost reflective access prices with the access provider, as only the access provider has detailed knowledge of their costs. Asciano recognises that following the 2009 SA Rail Regime Access Inquiry a requirement for the provision of an information kit was introduced. This information kit includes the provision of cost information which goes some way to addressing this concern.

Given the “negotiate and arbitrate” model continues to be applied then the provision of cost information must be maintained, and if possible strengthened as sufficient cost information is a minimum requirement for even handed price negotiations. An access regime which requires that sufficient cost information be available to both negotiating parties is much more likely to result in an access price which is efficient and cost reflective than a price negotiated in a regime where one party has incomplete information. A negotiation where both parties have information is more likely to result in a price outcome which approximates the outcome that could be expected in a competitive market.

5 ASCIANO’S RESPONSE TO SPECIFIC MATTERS RAISED IN THE ISSUES PAPER

The Issues Paper (page 3) explicitly requests comment from stakeholders on eight issues. Asciano’s comment on these issues is outlined below.

Is there any evidence of misuse of market power by rail operators?

Asciano does not have any evidence that there is misuse of market power by rail operators or by monopoly rail infrastructure providers. Misuse of market power by monopoly rail infrastructure providers is likely to occur via monopoly pricing practices. In the absence of detailed information relating to a monopoly rail infrastructure provider’s services it is difficult to obtain evidence that monopoly power is being misused. Asciano believes that the misuse of market power could be tested by ESCOSA by comparing prices negotiated with monopoly rail infrastructure providers with prices which reflect the cost of providing these services.

Has the current Access Regime been successful? How should this success be measured?

Asciano believes that the objectives of the success of a third party access regime could be assessed by using the objectives under section 6 of the Essential Services Commission Act 2002⁵. In particular success could be assessed by considering whether the regime has:

- facilitated third party access to natural monopoly infrastructure;
- promoted competition;
- prevented misuse of monopoly power; and
- promoted economic efficiency.

In relation to these criteria Asciano does not have sufficient information to make an informed assessment as to the success of the regime.

What are the benefits of retaining the current Access Regime? What would be the risks (if any) if it was to expire?

As outlined in section 3 Asciano believes that the South Australian rail access regime should continue. However, Asciano believes that, if possible, the current regime should be strengthened as outlined in section 4. Retaining the current regime will continue to allow for third party access to natural monopoly rail infrastructure, which is the minimum condition required for above rail competition. If the access regime expired it is possible that third party access to natural monopoly rail infrastructure may no longer be facilitated. In this case efficiency benefits arising from potential and actual increased above rail competition would be lost.

What are the current costs of the Access Regime (e.g. costs of compliance and administration)?

In general terms the costs to Asciano of negotiating access are not particularly substantial when compared to the benefits of third party access. As Asciano has not negotiated access to the assets covered by the South Australian rail access regime Asciano cannot make a detailed comment as to the specific costs of negotiating access to these specific assets.

Are there alternative approaches to achieving the intent of the Access Regime that are appropriate at this time? For example, would adoption of the national access

⁵ Other criteria which could be used to assess the success of the regime include those contained in section 44AA of Part IIIA of the Commonwealth Competition and Consumer Act which outlines the objectives of access regulation.

rules (under the Commonwealth Competition and Consumer Act 2010) be suitable?

Asciano recognises that there are alternative approaches to achieving the intent of the South Australian rail access regime. Asciano has argued in other regulatory submissions⁶ that the multiplicity of rail access regimes across Australia adds costs and complexity to rail access for little benefit, particularly as many of the access regulation functions are duplicated across states. Given this Asciano supports moves towards a national access regulator. In particular Asciano notes that the Draft Report of the Commonwealth's Competition Policy Review has proposed the establishment of a national pricing and access regulator separate from the ACCC. Asciano broadly supports this recommendation. If such a national access and pricing regulator is established Asciano believes that it should be considered as a future option for addressing issues related to South Australian rail infrastructure access.

What are the intentions of rail service providers and their customers in the next 5 years? Are there any key industry developments in the foreseeable future that may impact the demand for these services?

As Asciano has not negotiated access to the assets covered by the South Australian rail access regime Asciano cannot make a detailed comment as to the intentions of rail operator's and end use customers in South Australia.

In general terms future demand for bulk mineral rail services is likely to be driven by commodity prices and markets whereas the future demand for bulk agricultural rail services is likely to be driven by driven by commodity prices and markets, weather and the competitive position of road transport. Similarly the future demand for containerised freight is driven by both broader economic factors and the competitive position of road transport. Asciano believes that pricing for heavy vehicle road users needs to be addressed in order to allow a more efficient transport infrastructure pricing regime to develop. Asciano recognises that such transport pricing reforms are beyond the scope of this review.

What other issues are relevant to the decision to continue, or discontinue the current Access Regime?

As outlined in section 3 Asciano believes that the South Australian rail access regime should continue in order for the efficiency benefits from potential and actual above rail competition to be realised.

⁶ See for example the Asciano Submission to the Commonwealth Competition Policy Review Issues Paper June 2014 pp 9-12

Are there any other matters that the Commission should consider as a part of the Review?

Other issues Asciano believes are relevant to the review are outlined in section 4.

6 CONCLUSION

Given Asciano does not use the rail infrastructure assets which are the subject of this review this Asciano submission focuses on broader issues related to rail access regulation.

Asciano strongly believes that the South Australian rail access regime should continue. However, Asciano believes that, if possible, the current regime should not just continue but be strengthened by addressing issues relating to the need for stronger ring fencing provisions and the shortcomings of the “negotiate-arbitrate” access model.

Asciano does not have any evidence that there is misuse of market power by monopoly rail infrastructure providers, but believes that by strengthening the regime by increasing transparency and removing any potential for discrimination then third party access and competition will be further promoted in the South Australian rail industry.